

STATE OF NEW YORK

STATE TAX COMMISSION

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In the Matter of the Petition

of

PHOENIX GARDEN RESTAURANT, INC. (SELLER)

for Revision of a Determination or for Refund  
of Sales and Use Taxes under Articles 28 and 29 :  
of the Tax Law for the Period March 1, 1980  
through November 30, 1983.

DECISION

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In the Matter of the Petition

of

PHOENIX GARDEN RESTAURANT, INC. (PURCHASER)

for Revision of a Determination or for Refund  
of Sales and Use Taxes under Articles 28 and 29 :  
of the Tax Law for the Period March 1, 1980  
through November 30, 1983.

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Petitioner Phoenix Garden Restaurant, Inc. (Seller), 16-18 Elizabeth Street, New York, New York 10013, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period March 1, 1980 through November 30, 1983 (File No. 55562).

Petitioner Phoenix Garden Restaurant, Inc. (Purchaser), 46 Bowery (Arcade 15/16), New York, New York 10013, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period March 1, 1980 through November 30, 1983 (File No. 62146).

A consolidated hearing was commenced before James Hoefer, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on March 6, 1986 at 1:45 P.M. and continued to conclusion on April 30, 1986 at 9:15 A.M., with all briefs to be filed by September 15, 1986. Petitioners

appeared by Leonard Brenner, Esq. The Audit Division appeared by John P. Dugan, Esq. (Irwin A. Levy, **Esq.**, of counsel).

### ISSUES

I. Whether the Audit Division was justified in using a test period audit method to determine the sales and use tax liability of petitioner Phoenix Garden Restaurant, Inc. (Seller), and, if so, whether such determination properly reflected said petitioner's sales and use tax liability.

11. Whether the failure of the Audit Division to respond to petitioner Phoenix Garden Restaurant, Inc. (Seller)'s protest of a Statement of Proposed Audit Adjustment, more commonly known as a 30-day letter, constituted a denial of due process of law.

111. Whether the Notice of Determination and Demand for Payment of Sales and Use Taxes Due was timely issued to petitioner Phoenix Garden Restaurant, Inc. (Purchaser).

### FINDINGS OF FACT

1. During the period at issue, petitioner Phoenix Garden Restaurant, Inc. (Seller)' operated a small Chinese restaurant in an arcade between the Bowery and Elizabeth Street in the Chinatown section of New York City. In the latter part of 1980, the business was completely destroyed by a fire. Renovation work required as a result of said fire was completed in March 1981. Additional renovation work was performed in January 1982 when Phoenix Garden acquired the store adjacent to it and combined the two premises. Subsequent to the combining Phoenix Garden had 10 tables available for customers and employed an average

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1 Petitioner Phoenix Garden Restaurant, Inc. (Seller) shall be referred to hereinafter as Phoenix Garden.

of 13 individuals. In October, 1984, Phoenix Garden executed an agreement to sell its business to Kam-Cheong Chu, or a corporation to be formed by him. Mr. Chu then formed Phoenix Garden Restaurant, Inc. (Purchaser). On November 1, 1984, Phoenix Garden sold the business to Phoenix Garden Restaurant, Inc. (Purchaser) for \$70,000.00.

2. On June 20, 1984, the Audit Division, as the result of a field audit, issued to Phoenix Garden a Notice of Determination and Demand for Payment of Sales and Use Taxes Due assessing additional sales and use taxes due of \$21,902.04, plus interest of \$4,707.35, for a total amount due of \$26,609.39 for the period March 1, 1980 through November 30, 1983, excluding September 1, 1980 through February 28, 1981 when Phoenix Garden was closed due to the fire. Phoenix Garden, by signature of its representative, executed two consents extending the statute of limitations for issuing an assessment for sales and use taxes, the second of which extended the period March 1, 1980 through February 28, 1981 to June 20, 1984.

3. On March 27, 1985, the Audit Division issued to petitioner Phoenix Garden Restaurant, Inc. (Purchaser) a Notice of Determination and Demand for Payment of Sales and Use Taxes Due assessing taxes due of \$21,902.04, plus interest of \$6,828.63, for a total amount due of \$28,730.67. The notice contained the following explanation:

"The following taxes are determined to be due from Phoenix Garden Rest. [sic], Inc. and represents [sic] your liability, as purchaser, in accordance with Section 1141(c) of the Sales Tax Law."

4.(a) On January 12, 1983, the Audit Division initiated an audit of Phoenix Garden's **books** and records. On April 5, 1983, an auditor visited the office of Phoenix Garden's representative and performed some preliminary work. On July 21, 1983, the auditor sent a letter to the representative indicating

specific books and records which were required as well as audit procedures which must be conducted to complete the audit. Between August 1 and November 1, 1983, the auditor went on maternity leave.

(b) On August 25, 1983, a second auditor visited Phoenix Garden's premises for one hour. The auditor did not conduct an audit, but merely observed the premises. On August 31, 1983, the auditor sent Phoenix Garden a Statement of Proposed Audit Adjustment (30-day letter) for sales taxes of \$24,053.07 for the period March 1, 1980 through May 31, 1983. (It should be noted that the Audit Division could not explain how these taxes were computed.) On September 6, 1983, the representative submitted a protest of the 30-day letter.

(c) On October 18, 1983, the second auditor went to the representative's office and prepared a schedule of fixed asset purchases from the cash disbursements journal and bills. Many of the bills were written in Chinese and, without requesting further explanation, were considered taxable by the auditor. In a letter dated November 18, 1983, the original auditor, in response to the representative's protest to the 30-day letter, advised the representative that the Audit Division would not process the assessment if it were allowed to continue the audit.

(d) On January 5, 1984, the original auditor sent the representative a letter stating as follows:

"In accordance with our recent telephone conversation it is the department's policy to conduct at least one full day observation of the taxpayer's business activity at taxpayer's premises. Please contact us as soon as possible to schedule an appointment for the observation."

Notwithstanding the intervening telephone calls between the auditor and the representative to arrange an observation test, on April 4, 1984, the auditor

sent Phoenix Garden a second 30-day letter for sales and use taxes of \$21,902.04 for the period March 1, 1980 through November 30, 1983. The basis for this amount is explained infra. On April 30, 1984, the representative protested this 30-day letter. No further action was taken by the Audit Division until June 20, 1984 when the notice of determination was issued to Phoenix Garden.

5. The additional sales taxes at issue herein, \$14,889.31, were computed in the following manner: the original auditor first determined purchases for the period March 1, 1980 through February 28, 1983 from Phoenix Garden's cash disbursements journal of \$412,275.17. These purchases were marked up 150 percent (pursuant to the Audit Division's experience in conducting audits of similar businesses) to compute audited taxable sales for this test period of \$1,030,687.50. Audited taxable sales were reduced by taxable sales reported of \$895,542.00 to compute additional taxable sales for the test period of \$135,145.50 which represented a margin of error of 15.091 percent. The margin of error was applied to taxable sales reported for the entire audit period of \$1,205,127.00 to determine additional taxable sales of \$181,865.00 and additional sales tax due of \$14,889.31. The additional use taxes at issue, \$7,012.73, were computed as follows: the original auditor multiplied by the use tax rate the total of the schedule of fixed assets of \$85,357.84 (the amount determined by the second auditor as a result of his review of Phoenix Garden's cash disbursements journal on October 18, 1983). The additional sales and use taxes total \$21,902.04.

6. At no time during the audit did Phoenix Garden or its representative fail to make books or records, which were requested, available to the auditors. Additionally, complete and adequate books and records were maintained from which the exact sales and use tax liability could have been determined. Phoenix Garden's books and records reflected a markup of 117 percent.

7. The taxable fixed assets as determined by the Audit Division, \$85,357.84, included a \$47,500.00 distribution to the principals of Phoenix Garden, a \$10,000.00 payment to Tommy S. Ho for the assignment of the lease for the premises adjacent to Phoenix Garden, and \$18,200.00 in payments for capital improvements. Phoenix Garden admits that it is liable for use tax on the remaining balance, \$9,657.84.

8. At the hearing, the petitioner Phoenix Garden Restaurant, Inc. (Purchaser) presented a copy of the Notification of Sale, Transfer or Assignment in Bulk which it supposedly served on the Audit Division and which bore a date of November 1, 1984. No evidence was presented by petitioner Phoenix Garden Restaurant, Inc. (Purchaser) as to the method or date of service of said notice on the Audit Division.

#### CONCLUSIONS OF LAW

A. That although there is statutory authority for use of a test period to determine the amount of tax due, resort to such method of computing tax liability must be founded upon an insufficiency of record keeping which makes it virtually impossible to verify such liability and conduct a complete audit (Chartair, Inc. v. State Tax Commission, 65 AD2d 44, 46).

B. That petitioner Phoenix Garden Restaurant, Inc. (Seller) maintained adequate books and records from which the actual tax could have been determined. Therefore, the Audit Division's resort to the use of a test period to determine its sales tax liability was incorrect and that portion of the assessment with respect to the tax on additional taxable sales is cancelled.

C. That petitioner Phoenix Garden Restaurant, Inc. (Seller) has sustained the burden of proof required to show that it is liable for use tax on purchases

totalling \$9,657.84 and not \$85,357.84 as determined by the Audit Division (see Finding of Fact "7").

D. That section 1141(c) of the Tax Law provides, in pertinent part, the following:

"(c) Whenever a person required to collect tax shall make a sale, transfer, or assignment in bulk of any part or the whole of his business assets, otherwise than in the ordinary course of business, the purchaser, transferee or assignee shall at least ten days before taking possession of the subject of said sale, transfer or assignment, or paying therefor, notify the tax commission by registered mail of the proposed sale and of the price, terms and conditions thereof..." (emphasis added).

E. That 20 NYCRR 537.2(b) provides, in pertinent part, the following:

"(b) Service. (1) Such notice of a sale, transfer or assignment in bulk shall be given by the purchaser, transferee or assignee by: (i) personal service (hand delivery), upon persons authorized by the Department of Taxation and Finance to accept such service, at the Bulk Sales Unit, Central Office Audit Bureau, Audit Division, Department of Taxation and Finance, State Campus, Albany, **N.Y.**; or (ii) United States registered mail to the Bulk Sales Unit, Central Office Audit Bureau, Audit Division, Department of Taxation and Finance, State Campus, Albany, **N.Y.** 12227; or (iii) United States certified mail -- return receipt requested, to the Bulk Sales Unit, Central Office Audit Bureau, Audit Division, Department of Taxation and Finance, State Campus, Albany, **N.Y.** 12227; provided that the envelope or other wrapper containing the notice is delivered to an employee of the United States Postal Service who postmarks the sender's receipt for such envelope or wrapper." [emphasis in original.]

F. That the Notice of Determination and Demand for Payment ~~of~~ Sales and Use Taxes Due was timely issued to petitioner Phoenix Garden Restaurant, Inc. (Purchaser). Said petitioner failed to show that it met the notification and/or service requirements of section 1141(c) of the Tax Law and 20 NYCRR 537.2(b).

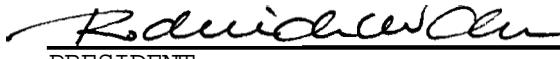
G. That there is no provision in the Tax Law or regulations requiring the Audit Division to entertain a protest to a 30-day letter prior to issuing a notice of determination. Therefore, the actions of the Audit Division (see Finding of Fact "4[d]") do not constitute a denial of due process of law.

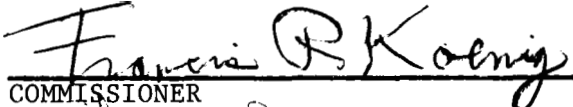
H. That the petitions of Phoenix Garden Restaurant, Inc. (Seller) and Phoenix Garden Restaurant, Inc. (Purchaser) are granted to the extent indicated in Conclusions of Law "B" and "C"; the Audit Division is hereby directed to modify the notices of determination and demands for payment of sales and use taxes due issued June 20, 1984 and March 27, 1985; and that, except as so granted, the petitions are otherwise denied.

DATED: Albany, New York

STATE TAX COMMISSION

JAN 16 1987

  
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PRESIDENT

  
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COMMISSIONER

  
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COMMISSIONER