

STATE OF NEW YORK  
STATE TAX COMMISSION  
ALBANY, NEW YORK 12227

May 13, 1983

12 Chatham Square Restaurant, Inc.  
11-12 Chatham Square  
New York, NY 10038

Gentlemen:

Please take notice of the Decision of the State Tax Commission enclosed herewith.

You have now exhausted your right of review at the administrative level. Pursuant to section(s) 1138 of the Tax Law, any proceeding in court to review an adverse decision by the State Tax Commission can only be instituted under Article 78 of the Civil Practice Law and Rules, and must be commenced in the Supreme Court of the State of New York, Albany County, within 4 months from the date of this notice.

Inquiries concerning the computation of tax due or refund allowed in accordance with this decision may be addressed to:

NYS Dept. Taxation and Finance  
Law Bureau - Litigation Unit  
Building #9 State Campus  
Albany, New York 12227  
Phone # (518) 457-2070

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative  
Maxwell Slote  
56 Tain Drive  
Great Neck, NY 11021  
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

\_\_\_\_\_  
In the Matter of the Petition :  
of :  
12 Chatham Square Restaurant, Inc. :  
for Redetermination of a Deficiency or a Revision :  
of a Determination or a Refund of Sales & Use Tax :  
under Article 28 & 29 of the Tax Law for the :  
Period 6/1/76-5/31/79. :  
\_\_\_\_\_ :

AFFIDAVIT OF MAILING

State of New York  
County of Albany

David Parchuck, being duly sworn, deposes and says that he is an employee of the Department of Taxation and Finance, over 18 years of age, and that on the 13th day of May, 1983, he served the within notice of Decision by certified mail upon 12 Chatham Square Restaurant, Inc., the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

12 Chatham Square Restaurant, Inc.  
11-12 Chatham Square  
New York, NY 10038

and by depositing same enclosed in a postpaid properly addressed wrapper in a (post office or official depository) under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the petitioner herein and that the address set forth on said wrapper is the last known address of the petitioner.

Sworn to before me this  
13th day of May, 1983.

David Parchuck

James A. Haglund

AUTHORIZED TO ADMINISTER  
OATHS PURSUANT TO TAX LAW  
SECTION 174

STATE OF NEW YORK

STATE TAX COMMISSION

\_\_\_\_\_  
In the Matter of the Petition :  
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12 Chatham Square Restaurant, Inc. :  
for Redetermination of a Deficiency or a Revision :  
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Period 6/1/76-5/31/79. :  
\_\_\_\_\_ :

AFFIDAVIT OF MAILING

State of New York  
County of Albany

David Parchuck, being duly sworn, deposes and says that he is an employee of the Department of Taxation and Finance, over 18 years of age, and that on the 13th day of May, 1983, he served the within notice of Decision by certified mail upon Maxwell Slote the representative of the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

Maxwell Slote  
56 Tain Drive  
Great Neck, NY 11021

and by depositing same enclosed in a postpaid properly addressed wrapper in a (post office or official depository) under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the representative of the petitioner herein and that the address set forth on said wrapper is the last known address of the representative of the petitioner.

Sworn to before me this  
13th day of May, 1983.

David Parchuck

Annunzio A. DiGirolamo

AUTHORIZED TO ADMINISTER  
OATHS PURSUANT TO TAX LAW  
SECTION 174

STATE OF NEW YORK

STATE TAX COMMISSION

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In the Matter of the Petition	:	
of	:	
12 CHATHAM SQUARE RESTAURANT, INC.	:	DECISION
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 June 1, 1976	:	
through May 31, 1979.	:	

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Petitioner, 12 Chatham Square Restaurant, Inc., 11-12 Chatham Square, New York, New York 10038, 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 June 1, 1976 through May 31, 1979 (File No. 31474).

A small claims hearing was held before Arthur Johnson, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on June 16, 1982 at 2:45 P.M. and continued on July 20, 1982 at 10:30 A.M. Petitioner appeared by Maxwell Slote, Esq. The Audit Division appeared by Paul B. Coburn, Esq. (Irwin Levy, Esq., of counsel).

ISSUES

I. Whether the Audit Division's use of the markup method of audit as a basis for determining petitioner's sales of liquor, beer and wine was proper and, if so,

II. Whether the additional taxable sales resulting from the use of such procedure was correct.

III. Whether the Audit Division's use of a "test period" to determine sales tax overcollections for a three year period was proper.

IV. Whether the Audit Division correctly determined the value of tangible personal property transferred in a bulk sale transaction.

FINDINGS OF FACT

1. Petitioner, 12 Chatham Square Restaurant, Inc., operated the Chi Mer Restaurant located at 11-12 Chatham Square, New York, New York.

2. On July 21, 1980, as the result of an audit, the Audit Division issued a Notice of Determination and Demand for Payment of Sales and Use Taxes Due against petitioner covering the period June 1, 1976 through May 31, 1979 for taxes due of \$18,462.14, plus penalty and interest of \$10,630.43, for a total of \$29,092.57.

3. Petitioner executed a consent extending the period of limitation for assessment of sales and use taxes for the period at issue to September 20, 1980.

4. Petitioner maintained and provided the Audit Division with the following books and records for audit: cash receipts and disbursements journals, cash register tapes, guest checks, purchase invoices, bank deposits, sales tax returns and corporation income tax returns.

The Audit Division accepted the accuracy of food sales recorded in petitioner's books and records based on a reported markup of 152 percent. However, the auditor felt that the reported liquor and beer markup of 112 percent was low. Therefore, a markup test was performed for liquor and beer using purchases for the month of May, 1979. The test revealed a liquor markup of 257 percent and a beer markup of 172.9 percent. The liquor markup was computed using a 1½ ounce serving of liquor (2 ounces for gin and vodka drinks), selling prices in effect in May, 1979 and a 15 percent allowance for spillage. The foregoing markups were applied to applicable purchases for the audit period

to determine liquor and beer sales of \$359,237.00. Food sales of \$1,096,627.00 were added to this amount to arrive at total taxable sales of \$1,455,864.00. Petitioner reported sales of \$1,294,364.00, leaving additional taxable sales of \$161,500.00 and taxes due thereon of \$12,920.00.

Additionally, the Audit Division analyzed guest checks for a sample period which disclosed an overcollection error factor of .003356 percent. This test was used to project additional taxes due of \$342.14 for the audit period.

The Audit Division also determined that petitioner failed to pay the bulk sales tax on the tangible personal property it acquired when the business was purchased. The personal property was valued at \$65,000.00 by the Audit Division on the basis that the depreciation schedule filed with petitioner's corporation tax returns listed that amount for furniture and fixtures. Petitioner admitted that tax is due on personal property transferred; however, it takes exception to the value assigned to such property by the Audit Division.

5. Petitioner and the Audit Division stipulated to the following facts:

(a) The sales tax computation for the quarter ended August 31, 1976 includes \$65,000.00 as the total selling price paid by the petitioner for the subject restaurant business it acquired.

(b) The sales tax auditors herein initially requested of, and received from, the petitioner all of its purchase invoices for the months of March, April and May, 1979, but used only the May bills in its markup tests.

(c) The petitioner made available to said auditors, at their request, all its monthly summaries for liquor, wine and beer purchases for the entire 36 month period.

(d) No purchase invoices of the petitioner were at any time requested by the auditors respecting (sic) months other than those for March, April and May, 1979.

(e) In the analysis by the auditors of petitioner's invoices purchased in May, 1979, for purposes of the mark-up test, the quantities of liquor, wine and/or beer indicated thereon were recorded correctly, as shown in said analysis, but without regard as to whether any part of the quantities so purchased were unused as of the end of said month.

(f) The mark-up test and analysis of petitioner's purchase invoices for May, 1979 reflect an estimated, not an actual, dollars and cents taxable sales figure. The test and analysis use actual figures from the purchase invoices, all based on departmental tables.

(g) The dollars and cents taxable sales figure to which reference is made in the last preceding paragraph was computed by the Department of Taxation and Finance by applying its own calculation of mark-up on purchases, also known as the gross profit ratio over cost.

(h) The auditors accepted the petitioner's figures for purchases and sales of food during the entire 36 months under review, except for a 1.6% "error rate" which they set forth in a work sheet dated on or about July 10, 1981.

On the basis set forth in the last preceding paragraph, the auditors calculated and accepted a gross profit ratio of 152.0848% over cost, for food, that being the mathematical result of petitioner's own figures.

However, the auditors rejected the petitioner's sales and purchase figures in calculating the gross profit ratios for liquor, wine and beer.

(i) Following is a schedule showing the tax deficiency variously calculated by the Department by schedules dated as shown:

<u>Date of Schedule</u>	<u>Deficiency claimed</u>	<u>Based on additional taxable sales of</u>
January 23, 1980	\$12,920.60	\$161,500.00
February 4, 1980	10,030.89	figure not available
March 11, 1980	12,920.60	161,500.00
April 30, 1980	10,889.95	136,124.40
May 1, 1980	16,432.09	figure not available
June 16, 1980	10,573.92	132,174.00
July 21, 1980	18,462.14 ("Final")	226,000.00

(j) Petitioner should be credited with beer consumed by its 16 employees at the rate of 2½ bottles daily, seven days a week for the 36 month period, the value thereof to be determined.

(k) The Department has given no credit to the petitioner in its calculations of the final tax deficiency by reason of the consumption of beer by petitioner's employees, although it has given a credit for the consumption of food by them.

6. In December, 1975, petitioner entered into an agreement with Chin Mer Restaurant, Inc. to purchase a restaurant business located at 11-12 Chatham Square, New York, New York for \$60,000.00. Said agreement provided that the sale included all of the chattels, fixtures and equipment, together with all other chattels commonly used in and about the premises and used in connection with the operation of said business, as well as the trade name and telephone number of the seller and the good will.

7. Bowery Auction Outlet, which is engaged in buying and selling restaurant equipment, examined the fixtures and equipment located on the restaurant premises and appraised the value of each item as of July, 1976, the total of which was \$11,585.00.



8. At the hearing, the Audit Division conceded that the taxes due should be adjusted to \$16,116.06 on the basis that it understated the taxable sales reported by petitioner by \$29,328.00.

9. During the test month of May, 1979, petitioner made extraordinary purchases of gin and vodka. Petitioner purchased  $9\frac{1}{4}$  cases of gin and 5 cases of vodka, whereas for the audit period purchases of said items averaged 2.6 cases and 3.3 cases per month, respectively. The markup on gin was 348 percent and vodka was 549 percent; thus, the markup computation gave excessive weight to high markup items.

10. Petitioner has excellent internal control of guest checks. Each waiter is assigned a number and is issued a numerical series of checks. When the waiter leaves for the day, he must account for the checks by returning the unused checks. The used checks are segregated as to cash or charge and are used to verify receipts. The following day the waiter is issued the unused checks from the previous day, plus new checks in numerical sequence if needed.

All bar charges for beer, liquor and wine are recorded on the back of the guest check and the total for beverages is entered on the front of the check and added to the charges for food. Sales tax is collected on the total. The charges on the guest check are rung separately on the cash register. The cash register tapes are used to record entries in the cash receipts journal.

Petitioner is primarily an eating establishment. The bar area is small with limited seating. Approximately 70 percent of liquor, wine and beer is sold in the dining room.

11. Petitioner's liquor drinks contained between  $1\frac{1}{2}$  ounce and  $2\frac{1}{2}$  ounces of liquor, depending on the type of drink.

12. The beer consumed by employees (Finding of Fact "5(j)") had a cost of \$12,230.40.

13. Petitioner argued that the Audit Division overstated beer sales by including beer purchased on May 31, 1979 in its markup test.

The markup test for beer using all purchases made in May, 1979 revealed a markup of 172.9 percent which resulted in estimated beer sales of \$69,855.90 for the audit period. If the beer purchases made on May 31, 1979 were deleted from the test, the beer markup would be 193 percent.

14. Petitioner also argued that the markups were overstated because the test used 1979 selling prices when such prices were less during earlier periods of the audit. Petitioner, however, did not establish that markup percentages were lower in 1976 than in 1979.

#### CONCLUSIONS OF LAW

A. That the audit procedures described in Finding of Fact "4" are generally accepted procedures established by the Audit Division and are used to determine the accuracy of books and records; that the auditor is allowed to resort to external indices to verify the accuracy of petitioner's records (Holland v. United States, 348 U.S. 121).

That based on such audit procedures, the Audit Division concluded that petitioner's books and records adequately reflected food sales; however, its markup test for liquor, beer and wine disclosed a significant variance with the markup obtained from the purchase and sales figures recorded on petitioner's books and records to conclude that not all liquor, beer and wine sales were recorded on the books and thus established the insufficiency of petitioner's books and records (Matter of George Korba v. State Tax Commission, 84 A.D.2d 655).

That when books and records are insufficient, "test period" and percentage markup audits are permissible (Matter of Chartair, Inc. v. State Tax Commission, 65 A.D.2d 44; Matter of Sakran v. State Tax Commission, 73 A.D.2d 989).

B. That the audit conducted by the Audit Division was proper, with the exception noted below in Conclusion of Law "C", based on the books and records examined and information obtained at the time the audit was performed. However, based on the evidence presented at the hearing, the Audit Division overstated petitioner's markup on liquor in that it did not give full consideration to the quantity of liquor served in drinks and the extraordinary purchases of gin and vodka (Findings of Fact "9" and "11"). Moreover, the audit did not allow for beer consumed by employees as stipulated.

That taking into account a substantially reduced markup based on the above factors; the fact that food sales which comprised 80 percent of petitioner's sales were accepted as correct; that 70 percent of liquor, wine and beer is sold in the dining room, recorded on guest checks and reported on sales tax returns; the degree of internal control; and the completeness of the books and records, petitioner's sales as recorded in its books and records are correct in their entirety. Accordingly, the additional taxes of \$12,920.00 determined as a result of the markup test are cancelled. Petitioner, however, is liable for use tax on the beer consumed by employees (Finding of Fact "12").

C. That petitioner had guest checks available for the entire audit period and, therefore, the Audit Division's use of a test period to estimate sales tax overcollections is unauthorized (Matter of Chartair v. State Tax Commission, *supra*; Matter of McCluskey's Steak House, Inc. v. State Tax Commission, 80 A.D.2d 713). Accordingly, the overcollections of sales tax are reduced to \$.86, the actual amount found due for the test period.

D. That the entire purchase price of the restaurant was not attributable to tangible personal property; that the agreement to purchase did not specify the sales price of the personal property; however, petitioner established through substantial documentary evidence that such property had a market value of \$11,585.00 at the time it was acquired. Therefore, the bulk sales tax is reduced to \$926.80.

E. That the penalty is cancelled and interest is reduced to the minimum statutory rate.

F. That the petition of 12 Chatham Square Restaurant, Inc. is granted to the extent indicated in Conclusions of Law "B", "C", "D" and "E"; that the Audit Division is hereby directed to modify the Notice of Determination and Demand for Payment of Sales and Use Taxes Due issued July 21, 1980; and that, except as so granted, the petition is in all other respects denied.

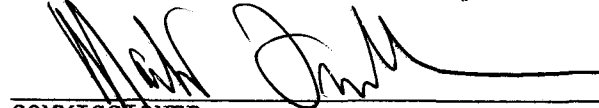
DATED: Albany, New York

STATE TAX COMMISSION

MAY 13 1983

  
PRESIDENT

  
COMMISSIONER

  
COMMISSIONER

P 389 758 958  
RECEIPT FOR CERTIFIED MAIL

NO INSURANCE COVERAGE PROVIDED—  
NOT FOR INTERNATIONAL MAIL

(See Reverse)

Sent to	
12 Chatham Square Apt 2C	
Street and No.	
11-12 Chatham Sq.	
P.O., State and ZIP Code	
New York, NY 10038	
Postage	\$
Certified Fee	
Special Delivery Fee	
Restricted Delivery Fee	
Return Receipt Showing to whom and Date Delivered	
Return Receipt Showing to whom, Date, and Address of Delivery	
TOTAL Postage and Fees	\$
Postmark or Date	

PS Form 3800, Feb. 1982

P 389 758 959  
RECEIPT FOR CERTIFIED MAIL

NO INSURANCE COVERAGE PROVIDED—  
NOT FOR INTERNATIONAL MAIL

(See Reverse)

Sent to	
Newell Slato	
Street and No.	
36 Tain Dr.	
P.O., State and ZIP Code	
Great Neck NY 11021	
Postage	\$
Certified Fee	
Special Delivery Fee	
Restricted Delivery Fee	
Return Receipt Showing to whom and Date Delivered	
Return Receipt Showing to whom, Date, and Address of Delivery	
TOTAL Postage and Fees	\$
Postmark or Date	

PS Form 3800, Feb. 1982