STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petitions of **WEST 20TH STREET ENTERPRISES CORPORATION, PACIFIC CLUB HOLDINGS, INC., SUSHI FUN DINING & CATERING, INC., AND DOMINICA O'NEILL** for Revision of Determinations or for Refunds of Sales and Use Taxes Under Articles 28 and 29 of the Tax Law for the period December 1, 2007 through November 30, 2013.	:	DECISION DTA NOS. 828472, 828473, 828474 AND 828475

Petitioners, West 20th Street Enterprises Corporation, Pacific Club Holdings, Inc., Sushi Fun Dining & Catering, Inc., and Dominica O'Neill, filed an exception to the determination of the Administrative Law Judge issued on May 6, 2021. All petitioners appeared by Bartons, LLP (Alvan L. Bobrow, Esq., of counsel) on the brief in support; petitioners Pacific Club Holdings, Inc. and Dominica O'Neill appeared by Bartons, LLP (Alvan Bobrow, Esq. of counsel) at oral argument while petitioners West 20th Street Enterprises Corporation and Sushi Fun Dining & Catering, Inc. appeared by Selim Zherka at oral argument. The Division of Taxation appeared by Amanda Hiller, Esq. (Osborne K Jack, Esq., of counsel).

Petitioners filed a brief in support of their exception. The Division of Taxation filed a brief in opposition. Petitioners did not file a reply brief. Oral argument was heard in New York, New York on July 28, 2022. The Division was granted until August 29, 2022, to respond to petitioner West 20th Street Enterprises Corporation's motion at oral argument, which date began the six-month period for the issuance of this decision.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the

following decision.

ISSUES

I. Whether the sale of scrip at an adult entertainment establishment is a taxable admission charge to a place of amusement for sales tax purposes.

II. Whether West 20th Street Enterprises Corporation, Sushi Fun Dining and Catering, Inc., Pacific Club Holdings, Inc. and Dominica O'Neill are liable for sales tax due on the sale of scrip as recipients of amusement charges for purposes of the Tax Law.

III. Whether the Division should be estopped from asserting sales tax on the sale of scrip at the VIP Club.

IV. Whether the assertion of tax on the sale of scrip at the VIP Club violates the United States and New York State constitutions.

V. Whether penalties should be abated.

VI. Whether the Tribunal should consider new evidence offered by petitioners after closing of the record below.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge, except finding of fact 16, which we have modified to more clearly reflect the record. The facts as determined by the Administrative Law Judge, together with the modified finding of fact, are set forth below.

1. On August 5, 2013, the Division of Taxation (Division) commenced an audit of petitioner West 20th Street Enterprises Corporation (West 20th). West 20th operates an adult entertainment establishment called the VIP Club, at 20 West 20th Street, New York, New York, (the Club). Selim Zherka and Maurice Kavanagh owned West 20th.

2. On October 24, 2013, the Division's auditor and section head met with West 20th's representatives, accountants Robert Sands and Nicolas Puglisi, at its business location. At this meeting, West 20th's representatives explained that two other entities operated the Club with petitioner; to wit: petitioners Sushi Fun Dining & Catering, Inc. (Sushi Fun) and Pacific Club Holdings, Inc. (Pacific Club). It was explained that West 20th's primary function and source of revenue was from admission charges and coat check charges; Sushi Fun operated the restaurant (food and liquor sales) and Pacific Club's function was dispensing "funny money" (scrip or VIP currency) at the Club.

3. Based on the ongoing audit of West 20th, the Division started field audits of Sushi Fun and Pacific Club. These entities were also represented by Messrs. Sands and Puglisi.

4. Although Sushi Fun operated the restaurant operations in the Club, the liquor license for the Club is held by West 20th. Sushi Fun is also owned by Messrs. Zherka and Kavanagh.

5. Pacific Club is owned by petitioner Dominica O'Neill. Prior to 2006, Pacific Club was owned by Messrs. Zherka and Kavanagh. The record does not reveal how or exactly when Ms. O'Neill came to own Pacific Club or how and why Messrs. Zherka and Kavanagh transferred ownership of Pacific Club to her.[1]

6. Beginning in 2012, the Club maintained a point of sale system (POS) upon which sales from all three entities were recorded. Petitioners' representatives stated that the POS system was not reliable and, therefore, was not used to prepare West 20th's or Sushi Fun's sales tax returns. Pacific Club was not a registered sales tax vendor, nor did it file sales tax returns. According to Pacific Club's representatives, Pacific Club did not engage in any taxable transactions for sales tax purposes.

[1] New York S Corporation Shareholders' Information Schedules filed by Pacific Club for 2005 and 2006 list Selim Zherka and Maurice Kavanagh as the owners of Pacific Club. A separate schedule for 2006 indicates that Ms. O'Neill was the sole shareholder.

7. As noted, Pacific Club's function was to dispense scrip in the Club. A concession agreement between Pacific Club and West 20th, dated October 13, 2005, provided that in exchange for $25,000.00 a month, Pacific Club had the exclusive right to operate a scrip desk at the Club, the purpose of which was to "facilitate transactions for patrons desiring to hire entertainers for First Amendment of the United States Constitution of expressive activities…." The terms of the agreement provide that Pacific Club could not impose a surcharge in excess of 20% to patrons to facilitate scrip transactions. The concession agreement is signed by Ms. O'Neill, but it does not indicate what her title with Pacific Club was at that time.

8. An example of the scrip used at the Club was introduced into the hearing record by petitioners. The scrip is in a denomination of "20" and is entitled "The New VIP Club New York" and lists the Club's address. It states that "[t]his Bill is Legal Tender for Table Dances and Tipping Only." There is an expiration date on bottom of the scrip. On the right side of the scrip in fine print it states as follows:

> "WE ARE ACCOMODATING YOU IN PAYING OUR TENANTS WHO ARE PERFORMERS PROVIDING A SERVICE TO YOU, UNRELATED TO US. OUR SERVICE IS PROVIDING YOU WITH A CURRENCY SO YOU CAN PAY THE PERFORMERS. THIS CURRENCY IS NOT VALID FOR ADMISSION, FOOD OR BEVERAGES OR PRIVATE LOUNGE RENTALS. THIS CURRENCY IS USED FOR TIPPING SELF EMPLOYED ENTERTAINERS WHO ARE ENGAGING IN A FIRST AMENDMENT EXPRESSIVE ACTIVITY."

9. On April 29, 2016, the Division's auditors went to the Club to observe its operations. To gain admission to the Club, a patron was required to pay an admission charge of $20.00 after 9:00 p.m. The admission charge was waived if the patron had a coupon or a "VIP Platinum card." Admission to the Club allowed a patron to view live performances on the Club's stage. It was observed that admission charges and coat check charges were collected and were being recorded in a POS system near the door.

10. The Club consists of two floors, with the restaurant operated by Sushi Fun occupying the second floor. There are five private rooms on the second floor and eleven semi-private rooms on the first floor for private dances. A patron seeking a private dance would arrange the dance with the Club's host and was charged $500.00 per hour for a private room plus $600.00 an hour for the dancer; a semi-private room incurred a charge of $400.00 for the room plus $500.00 per hour for the dancer. The room charges were collected by the Club and reported by Sushi Fun as lounge charges. A sign on the wall stated that sales tax was included in the room charges. The patron would pay the dancer for her charge using either cash or scrip. The Club's manager told the auditors that a dancer was entitled to keep all dance fees and tips paid in cash but would be charged a fee upon redemption of scrip. Patrons paid a 20% surcharge on the purchase of the scrip and, when the dancers redeemed the scrip, they paid an additional 10% processing fee. According to the audit log, the Club's manager also told the auditors that scrip could only be used to pay the dancers and could not be used to purchase food, drinks or be used for tipping.

11. Included in the hearing record are copies of the contracts for fourteen of the dancers and West 20th doing business as the Club. The contracts are denominated as a non-exclusive lease of entertainment facilities. Under the terms of the contracts, the dancer and Club disavowed an employment relationship. Pursuant to these lease agreements, West 20th leased its stage areas to the dancers "to market [their] entertainment." In return, the dancer would pay a fee to the Club. The Division's auditors were told by the Club's manager that the dancers paid $80.00 to $120.00 per night to entertain at the Club. This fee was recorded as rent revenue on the Club's POS system and reported by Sushi Fun. Under the terms of each contract, the dancer was required to perform eight stage shows per performance date and was required to schedule her performance dates through Pacific Club. Pursuant to the contract, the dancer was "entitled to

keep all dance fees paid to her and all 'tips' (gratuities) given to her by patrons during her performance date, during any period during which she is considered a 'tenant' and not an 'employee.'" Of the fourteen contracts introduced into evidence, two provided that the "[dancer] agreed to charge the fair market rate as determined by the New York City Adult Entertainment Industry wide standards for dancing in private Champagne Rooms." In addition, five of the contracts contained a provision stating that the "[dancer] agreed to charge the fair market rate as determined by the New York City Adult Entertainment Industry wide standards for table dancing and in private champagne lounges . . ."

12. Included in the record are confidentiality agreements signed by various dancers wherein dancers agreed to keep certain information of the "the Company" confidential. "The Company" is defined in the confidentiality agreements as "[Pacific Club, Sushi Fun, West 20th], its members, managers, shareholders, beneficiaries, partners, agents, affiliated companies, principals, officers, directors, tenants, their successors and assigns doing business at 20 West 20th Street, New York, N.Y."

13. In addition to acting as the scrip dispenser, Pacific Club acted as the Club's booking agent. Contracts in the record between dancers and Pacific Club indicate that in return for being booked at the Club to dance, the dancer was required to pay a referral fee of 20% ". . . of the face value of all [scrip] obtained by patrons . . . and used to pay DANCER for her service of rendering private dances."

14. During the audits, petitioners provided POS records for 2012 and 2013. During the course of the audits, the Division obtained third party credit card information, which was used to compare sales reported by each of the corporate petitioners to sales reported.

15. The audit of Sushi Fun resulted in no change, while the Division determined that West 20th owed additional sales tax of $16,000.00, which amount was agreed to and is not at issue herein.

16. The audit of Pacific Club led to the determination to assert sales tax on amounts paid for scrip. Using third-party credit card data for Pacific Club for 2011, 2012 and 2013, the Division calculated sales tax due for those years by multiplying the third-party credit card receipts for that period of $12,877,649.32 by the tax rate to determine sales tax due of $1,142,891.38.

To determine sales tax due for 2007 through 2010, the Division first determined how much of total credit card sales were reported on Pacific Club's income tax filings. During the audit period, Pacific Club reported credit card commissions on its income tax returns, which represented processing fees charged to the Club's patrons and its dancers. For 2011 through 2013, the Division determined that reported commissions amounted to 24.69% of actual credit card receipts. Since Pacific Club did not provide any records for 2007 through 2010, the Division divided the reported commissions for each of those years on its income tax filings by 24.69% to determine receipts from sales of scrip of $13,747,078.77 and computed tax due of $1,176,049.07 for those years. Total tax asserted due for the period December 1, 2007 thru November 30, 2013 amounted to $2,318,940.40.

17. Michael Russell, a sales tax section head with the Division, testified at the hearing and explained the rationale for the assertion of tax in this matter. Mr. Russell supervised the auditor who had initiated the audit but is no longer employed by the Division. Mr. Russell accompanied the auditor on his field appointments and was involved in every aspect of the audits. Mr. Russell explained that the Division determined that in addition to Pacific Club, West

20th and Sushi Fun were responsible for the taxes due on sales of scrip because the three entities operated as one business. Mr. Russell explained that the Division began with an audit of West 20th and during that audit, the Division learned that West 20th and Sushi Fun were involved in the operation of the Club. Mr. Russell stated that the Division audited all of the entities to understand the operation of the Club. Mr. Russell noted that during the audits, all three entities were represented by the same representatives and that the Club's records were provided in one POS report. He explained that the Division had to review the one POS system to determine what sales were attributable to which entity. Mr. Russell stated that "… when a customer walks in and a person takes their coat, they think the VIP Club is taking their coat, and when they go get a drink at the bar, they think the VIP Club is selling them a drink. When they go get funny money, they think that VIP is giving them funny money, so we felt that it's one club, one establishment, separated into three entities for reporting purposes."

18. Consequently, on August 30, 2016, the Division issued notice of determination L-045423066 to Pacific Club assessing sales tax due of $2,318,940.40, plus penalties and interest.

19. On August 31, 2016, the Division issued notices of determination L-045427441, L-045427440 and L-045427439 to Ms. O'Neill, Sushi Fun and West 20th, respectively. Each of the notices asserts tax due of $2,318,940.40, plus penalties and interest, as persons responsible for the taxes due from Pacific Club. At the hearing in this matter, Ms. O'Neill conceded she is a responsible person of Pacific Club but did not concede that Pacific Club owes tax.

20. Mr. Zherka and petitioners' representative, Alvan Bobrow, testified for petitioners in this matter. Although Ms. O'Neill was present at the March 5, 2020 hearing in this matter, she was not called as a witness.

21. Mr. Zherka was steadfast in his testimony that scrip could only be used for tipping and that the Club did not charge patrons for private dances. Mr. Zherka explained that the use of scrip was for patrons' convenience. Mr. Zherka alleged the Club was different from its competitors in that it did not charge for dances; the patron was free to tip or to not tip the Club's dancers and that the dancers could dance for free if they chose. Mr. Zherka testified that the Club did not realize any benefit from the sale of scrip by Pacific Club or the use thereof by Club patrons. While Mr. Zherka acknowledged that the Club was run by West 20th and Sushi Fun, he was adamant that other than dispensing scrip, Pacific Club's activities were separate and distinct and Pacific Club had no part in operating the Club.

22. Petitioners presented a letter, dated December 24, 2008, from Carla Adsit-Vassari, director of the Division's sales tax audit bureau, addressed to petitioners' representative, Mr. Bobrow. The letter provides in pertinent part, as follows:

> "New York State Department of Taxation and Finance Director of Tax Audits, Nonie Manion, asked me to respond to your letter dated October 14, 2008, regarding West 20th Enterprises Corp. and Notices and Demand, L-027740782 and L-027759052, issued against the corporation and responsible person Anthony Capeci, respectively. Also at issue is refund claim #2007-05-0477 for the period June 1, 2002 through August 31, 2002.
>
> In your letter you refer to conversations you had with Joseph Carzo. According to Mr. Carzo, he spoke to you on August 16, 2007 and informed you that if appropriate books and records were provided to corroborate the 'unique' business model of West 20th and the records reflect the business scenario as discussed in theory, then refund #2007-05-0477 representing the tax paid on Notice and Demand L-027740782, for the quarter ended August 31, 2002, would be approved and submitted for payment, subject to the approval of the State Comptroller. Applicable books and records for the refund claim period, June 1, 2002, through August 31, 2002, are needed to support any adjustment. As of this date, you have not provided records to support your position that the dance revenue is not subject to sales tax. Accordingly, until complete books and records are supplied to substantiate the business model of West 20th Enterprises, the refund will not be approved."

23. Petitioners also introduced a letter, dated January 7, 2011, addressed to Mr. Bobrow that notified him that after performing a sales tax audit of Pacific Club Services, Inc., for the period December 1, 1999 through November 30, 2004, the Division determined that no additional tax was due.

24. Petitioners submitted a Satisfaction of Judgment, dated January 20, 2012, for a warrant in the amount of $4,297,664.23, dated March 13, 2007, filed by the Division against West 20th. In addition, petitioners submitted a stipulation for discontinuance of proceeding wherein Mr. Zherka and the Division settled a sales tax matter before the Division of Tax Appeals for no tax due for the quarter ended November 30, 2005. Petitioners, through the testimony of Mr. Zherka, explained that based upon the letters referred to above and the resulting audit action, the Division indicated that it subsequently accepted that the sale or exchange of scrip by Pacific Club was not a taxable transaction.

25. Mr. Bobrow was sworn in and testified concerning the background and the meaning of the December 24, 2008 letter from Ms. Adsit-Vassari referred to in finding of fact 22. Mr. Bobrow explained that he represented West 20th for a prior audit period. Although Mr. Bobrow's testimony was vague, it is evident that West 20th had undergone a sales tax audit that involved the same issues present herein and did not file a formal appeal. Instead, Mr. Bobrow approached upper-level management within the Division and explained the Club's business model. Specifically, Mr. Bobrow explained that different legal entities were responsible for different functions within the Club and that the sale of scrip was handled by a separate entity not involved with the restaurant operations or other operations of the Club. According to Mr. Bobrow, auditors from the Division confirmed that the Club operated in the way detailed to the Division's management team and refunds were eventually granted. Mr. Bobrow opined that

since the letter did not state it was for settlement purposes only, it was tantamount to an informal ruling that the sale of scrip by a separate entity is not subject to sales tax. Mr. Bobrow was cross-examined by the Division's representative at length about a declaration he swore to in a Fair Labor Standards Act (FLSA) action brought by a former disc jockey of the Club against petitioners herein and others involved with the Club (the Romero Action).[2] In the declaration, Mr. Bobrow stated that petitioners herein had requested an informal ruling from the Division with respect to the sales tax consequences of certain transactions. Mr. Bobrow averred that the Division made certain written findings that the transactions were not subject to sales tax and, as part of its findings, stated that the Division concluded that the dancers were neither independent contractors nor employees. In the declaration, Mr. Bobrow stated that the Division's ruling provided the Club a competitive advantage over competing gentlemen's clubs and further claimed that disclosing any of the information concerning the informal ruling to the FLSA plaintiffs would harm the Club. Mr. Bobrow confirmed that the December 24, 2008 letter was the "informal ruling" referred to in this declaration. Mr. Bobrow acknowledged that the letter did not mention employees or independent contractors. When asked to explain his basis for making the statement in his declaration, Mr. Bobrow stated that "[m]aybe I should have said did not care whether they were. I said concluded, concluded because I made the inference that it was not an issue." Mr. Bobrow also claimed to not know the purpose for the declaration.

26. Prior to Mr. Bobrow's testimony, Joseph Carzo, the Division's director of tax audits, testified at the hearing. Mr. Carzo stated that the December 24, 2008 letter represented settlement discussions held between the Division and the specific taxpayers mentioned in the

[2] On May 21, 2014, Sheldon Romero, a disc jockey who worked at the Club, filed a lawsuit against petitioners Sushi Fun, Pacific Club, West 20th, Selim Zherka as well as ABCZ Corp., ABCZ Mgmt Corp., and John Does #1-10 in the Southern District of New York: Romero v ABCZ Corp., et al., No. 14-cv3653 (AT).

letter. Mr. Carzo testified that he had never communicated to petitioners' representative that charges to view adult entertainment are not subject to sales tax.

27. Consistent with the testimony of Mr. Zherka, petitioners submitted the affidavit of Ninive Galan sworn to February 20, 2020. Ms. Galan professed to be an entertainer at the Club on and off since 2010. Ms. Galan averred that scrip would only be used for voluntary tipping purposes, stating specifically that "the tip amount by a customer has been totally voluntary and or negotiable by and between the dancer and the customer."

28. During the course of petitioners' opening statement at the hearing in this matter, petitioners' representative stated that a subpoena had been prepared and was on its way to the Division of Taxation's Office of Counsel in an attempt to discern why notices of determination issued to Times Square Restaurant Group, Ltd., Times Square Restaurant #1, Inc., Three Amigos SJL, Restaurant, Inc., and Maurice Kavanagh, were cancelled by the Office of Counsel subsequent to a hearing in the Division of Tax Appeals in those matters (the Times Square matters), and prior to a determination being issued. A hearing in the Times Square matters occurred on June 26, 2019. The issue in those matters is identical to that in the present matter, i.e., whether the sale of scrip constitutes an admission charge to a place of amusement subject to sales tax. The notices of determination issued to the petitioners in the Times Square matters were settled via stipulations for discontinuance of proceeding for $0.00. and were filed with the Division of Tax Appeals on October 28, 2019. Copies of those stipulations for discontinuance of proceeding were entered into the hearing record at the hearing in this matter. The corporate entities therein have the same owners as the corporate petitioners herein. Notably, the corporation that sold scrip in that matter, Times Square Restaurant Group, was owned by Mr. Kavanagh; while Ms. O'Neill owned Times Square Restaurant No 1., the function of which was

rental of private rooms and booking events such as bachelor parties at the Cheetah Club. Mr. Zherka owned Three Amigos SJL, Restaurant Inc., which ran the Cheetah Club including the food and drink operations in that club.[3]

29. Following Mr. Zherka's testimony at the March 5, 2020 hearing in this matter, petitioners opted not to present the testimony of petitioner Dominica O'Neill or Maurice Kavanagh, although both were present. The Administrative Law Judge asked Mr. Bobrow if he was sure he did not want to call either Ms. O'Neill or Mr. Kavanagh, because petitioners would be given as much time as needed for petitioners to present their case. Mr. Bobrow responded that he was satisfied with Mr. Zherka's testimony and would not need to call either individual as a witness.

30. Following the conclusion of testimony, petitioners requested that the hearing record be left open for petitioners to submit: (i) three affidavits of current or former entertainers or employees of "the Club;" and (ii) two deposition transcripts from a Fair Labor Standards Act suit brought against Cheetah Club, a related club that Mr. Selim Zherka and Dominica O'Neill owned or were associated with. On April 1, 2020, petitioners submitted: (i) the affidavit of Diana O'Neill; (ii) the affidavit of Doreen Elliott; (iii) the affidavit of Dominica O'Neill; (iv) receipts from the purchase of scrip; (v) a September 29, 2017 deposition transcript of Diana O'Neill; and (vi) tax returns of Pacific Club Holdings, Inc. By letter dated May 5, 2020, the Administrative Law Judge notified the parties that the affidavits of Diana O'Neill, Dominica O'Neill and Doreen Elliott and the deposition transcript of Diana O'Neill were marked and taken into evidence. Since petitioners did not request that the hearing record be left open for the

[3] Official notice of the hearing transcript in the Times Square matters is taken pursuant to State Administrative Procedure Act (SAPA) § 306 (4). Pursuant to SAPA § 306 (4) official notice can be taken of all facts of which judicial notice could be taken. Since a court may take judicial notice of its own records (***Matter of Ordway***, 196 NY 95 [1909]), the Division of Tax Appeals may take official notice of its record of proceedings (***see Bracken v Axelrod***, 93 AD2d 913 [3d Dept 1983], ***lv denied*** 59 NY2d 606 [1983]).

admission of Pacific Club's tax returns or receipts for the purchase of scrip, these items were not made part of the record.

31. According to the affidavit of Diana O'Neill (Mrs. O'Neill), she worked as a "house mom" at the Club and at the Cheetah Club from 2010 to 2013. In her affidavit, Mrs. O'Neill avers that scrip was only used for tipping and that dancers could dance for free if they chose.

32. The deposition transcript taken from Mrs. O'Neill dated September 29, 2017, in a Fair Labor Standards Act lawsuit entitled ***Guzman et al. v Three Amigos SJL Inc., et al.***, 14 Civ 10120 (Guzman FLSA action), which involved alleged FLSA violations involving the Cheetah Club, was also submitted as support for her affidavit. Her testimony during the deposition was consistent with her affidavit herein wherein she avers that the Club's entertainers worked for tips that were totally voluntary. As a house mom, she collected rents from the tenants (entertainers) and provided them goods and services such as deodorant, sewing services, etc. She testified that she was not hired by anyone at the Cheetah Club, nor was she an employee of the Cheetah Club and claimed she started working there after she visited that club. She testified that on the date of the deposition, September 29, 2017, she no longer worked at the Cheetah Club. When questioned about whether she worked as a house mom at the Club, she stated that she only filled in as a house mom there one night. It was also revealed that she is petitioner Dominica O'Neill's mother.

33. Consistent with Mrs. O'Neill's affidavit, the affidavit of Doreen Elliott, submitted by petitioners, states that scrip could only be used for tipping. Like Mrs. O'Neill, Ms. Elliott identified herself as a house mom at the Club.

34. In Dominica O'Neill's affidavit, she avers that she has been the sole shareholder and president of petitioner Pacific Club. Ms. O'Neill states that Pacific Club replaced the previous

company, Pacific Club Services Corp., as the currency exchange company at the Club. She further averred that Pacific Club was contracted by the owners of the Club to provide currency exchange services (scrip) within the Club and that Pacific Club had its own employees, payroll, and credit card machines. According to Ms. O'Neill, Pacific Club and the Club had no common employees, shareholders, or managers. Finally, Ms. O'Neill stated that scrip could only be used for tipping.

35. At the hearing, the Division introduced a copy of a complaint filed by former dancers of the Club against each of the petitioners herein, as well as Maurice Kavanagh, Selim Zherka ABCZ Corp. and ABCZ II Management Co., in the United States District Court for the Southern District of New York (Acevedo complaint). The Acevedo complaint alleges that while plaintiffs worked as dancers at the Club between May 2009 and September 2013, the defendants, inter alia, failed to pay plaintiffs minimum wages, illegally withheld plaintiffs' tips, forced plaintiffs to share tips with others in the club and imposed illegal fines on plaintiffs. In response to the Acevedo complaint, the defendants therein filed an amended answer and affirmative defenses on April 6, 2017. In the amended answer and affirmative defenses, the defendants alleged that scrip was not used for gratuities, that the amounts paid for dances were mandatory performance fees, that through the complaint, the plaintiffs were seeking to reclassify mandatory performance fees as tips, and that the dancers retained any tips given to them by patrons.

36. On March 19, 2020, petitioners served a subpoena duces tecum on the Division seeking "any and all documents and communications concerning or related to the decision to cancel the notices of determination issued to [the Times Square matters' petitioners]." The subpoena was issued by petitioners' representative, Mr. Bobrow.

37. On March 30, 2020, the Division brought a motion, seeking an order modifying or quashing the subpoena. By order dated September 3, 2020, the Division's motion was denied. Although the motion was denied, it was noted that the hearing record was not left open for documents that petitioners had yet to subpoena. The findings of fact and conclusions of law of that order are incorporated herein by reference as if set forth herein in their entirety.

THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE

The Administrative Law Judge began his determination in this matter by setting forth the provisions of the Tax Law that impose sales tax on admission charges to places of amusement, together with the statutory definitions of those terms. The Administrative Law Judge reasoned that because the Club was clearly a place of amusement, the question that remained was whether scrip was used to purchase dances in the Club or was used purely for voluntary gratuities.

The Administrative Law Judge next described the presumption of correctness of the notice of determination as well as the burden of proof that petitioners must meet in order to prevail on their claim. According to the Administrative Law Judge, so long as a rational basis exists for the Division's determination, the burden of proving by clear and convincing evidence that the tax assessed is unreasonable lies with the taxpayer. The Administrative Law Judge found that petitioners failed to bear their burden of proving that the scrip sold in the Club could only be used to tip to the dancers, noting that petitioners' contention was belied by the documentary evidence in the record. For the Administrative Law Judge, while scrip may have been used to tip dancers, it was clear that the scrip sold in the Club was used to purchase dances as well.

Ultimately, according to the Administrative Law Judge, petitioners failed to overcome the presumption under the Tax Law that all of a taxpayer's sales receipts are subject to sales tax

until the taxpayer proves otherwise. According to the Administrative Law Judge, petitioners failed to prove that scrip was used exclusively for voluntary gratuities and not to pay mandatory performance fees, or even how much of the scrip was used for gratuities. Based on the foregoing, the Administrative Law Judge concluded that the Division properly asserted tax on the scrip sales and that Pacific Club, as a vendor of scrip, was under a duty to collect and remit sales tax on such sales.

The Administrative Law Judge rejected West 20th's and Sushi Fun's arguments that Pacific Club's scrip conversion service was separate from Club operations, and thus nontaxable. The Administrative Law Judge observed that sales of scrip used for private dances are properly subject to sales tax even in instances where such charges are collected by a separate entity. The Administrative Law Judge noted the services provided by the Club and Pacific Club's integration into its operations. The Administrative Law Judge found petitioners' claim that West 20th and Sushi Fun did not benefit from the purchase of private dances to simply defy credibility in light of the evidence presented.

The Administrative Law Judge considered and rejected petitioners' claim that the Division should be estopped from asserting sales tax based on the outcome of previous audits. The Administrative Law Judge found that petitioners failed to establish the elements of estoppel, specifically that the Division made no representations that advised petitioners that their sales of scrip used to pay mandatory performance fees are not subject to tax.

The Administrative Law Judge also rejected petitioners' claim that their rights to due process under the United States and New York State constitutions were violated. Petitioners claimed that the Tax Law made compliance with federal and state labor laws impossible, since the dancers are treated as employees under the labor laws and, therefore, the scrip must be

deemed to be gratuities and not dance fees. The Administrative Law Judge found such claims unavailing, because whether the dancers are employees, independent contractors, or lessors of Club space did not matter for purposes of determining whether scrip was used to tip dancers or was used to pay mandatory performance fees. According to the Administrative Law Judge, petitioners' argument is based on the proposition that the scrip was used solely for tipping, which he found to not be supported by the record.

Lastly, the Administrative Law Judge considered petitioners' argument that the penalties imposed should be abated. The Administrative Law Judge noted that penalties may be abated if any failure to timely file a return or pay a tax was due to reasonable cause and not willful neglect. According to the Administrative Law Judge, the Division's failure to assess tax on sales of dances in prior audits did not amount to its acceptance of petitioners' position that their business model effectively avoided sales tax, and thus it was unreasonable for petitioners to rely on such an interpretation in subsequent audit periods. The Administrative Law Judge rejected petitioners' argument that penalties should be abated, denied the petitions and sustained the notices of determination here at issue.

ARGUMENTS ON EXCEPTION

Petitioners state that Pacific Club did not sell scrip, but rather merely acted as an exchange for converting cash into scrip and vice versa. According to petitioners, such transactions are not subject to sales tax because Pacific Club had no venue of its own to which it could admit customers or patrons. Accordingly, they claim no transaction it engaged in could be considered a charge for admittance to a "place of amusement" as that term is contemplated within the Tax Law.

Petitioners maintain that the Administrative Law Judge erred in concluding that the Division was not estopped from asserting sales tax on sales of scrip in light of the December 24, 2008 letter from the director of the Division's sales tax audit bureau. Petitioners argue that the letter comprises acceptance of their position that their joint business model avoids sales tax on sales of scrip used to purchase dances in the Club, on which they relied to their detriment, and thus the doctrine of estoppel should be applied against the Division.

Petitioners also argue that the Administrative Law Judge erred in concluding that imposing sales tax on sales of scrip used to purchase dances did not violate their due process rights under the United States and New York constitutions. In essence, petitioners argue it is impossible to comply with the Tax Law and federal and state labor laws as applied to them.

Petitioners claim that the Administrative Law Judge erred in concluding that they failed to show reasonable cause for the failure to timely pay taxes due and in denying their request for abatement of penalties.

The Division states that the Administrative Law Judge correctly determined all of the issues presented at the hearing below. First, the Division argues that petitioners' receipts from sales of scrip are subject to sales tax. According to the Division, the record demonstrates that the Club charged mandatory dance fees, payable with scrip, that were not voluntary gratuities. Second, the Division argues that petitioners' insistence that the entity selling scrip must have a place of amusement in order for its sales to be taxable is misplaced. Rather, petitioner Pacific Club is the recipient of amusement charges under the Tax Law and is therefore also a person required to collect tax on the sales it makes to the Club's patrons.

The Division also argues that petitioners West 20th and Sushi Fun are likewise liable for the tax on sales of scrip as amounts paid as charges of a roof garden, cabaret or other similar

place. According to the Division, charge of a roof garden, cabaret or similar place includes any charge for entertainment. The Division also argues that petitioners' receipts are taxable as additional cover, minimum or entertainment charges includable in taxable food and beverage receipts.

Lastly, the Division states that petitioners' estoppel claims are baseless. It points out that the document upon which petitioners base their estoppel claims, the December 24, 2008 letter from the Division's director of sales tax audits, does not indicate that the Division advised petitioners that their receipts from sales of scrip would not be subject to sales tax. The Division states that the issues petitioners raise on exception were fully addressed by the Administrative Law Judge in his determination and asks this Tribunal to deny petitioners' exception.

OPINION

Tax Law § 1105 (f) (1) imposes sales tax on, generally, "any admission charge . . . to or for the use of any place of amusement in the state." An admission charge includes "any service charge and any charge for entertainment or amusement or the use of facilities therefor" (Tax Law § 1101 [d] [2]). A place of amusement is defined as "any place where any facilities for entertainment, amusement or sports are provided" (Tax Law § 1101 [d] [10]).

Tax Law § 1105 (f) (3) imposes sales tax on "the amount paid as charges of a roof garden, cabaret or other similar place in the state." A charge of a roof garden, cabaret or other similar place includes "[a]ny charge made for admission . . . or entertainment . . . at [such a place]" (20 NYCRR 527.12 [b] [1]). A roof garden, cabaret or other similar place is, generally, any such place "which furnishes a public performance for profit" (Tax Law § 1101 [d] [12]).

Receipts from "every sale . . . of beer, wine or other alcoholic beverages or . . . of food and drink of any nature . . . when sold in or by restaurants, taverns or other establishments in this

state" are subject to sales tax under Tax Law § 1105 (d). Liability under Tax Law § 1105 (d) also includes receipts from any "cover, minimum, entertainment or other charge made to patrons or customers."

A charge for a lap dance or a private dance at an adult entertainment establishment is a charge for the entertainment or amusement in a place of amusement and is, therefore, subject to sales tax under Tax Law § 1105 (f) (1). The same charge is also taxable under Tax Law § 1105 (f) (3) as a charge for entertainment at a roof garden, cabaret or other similar place (***see e.g. Matter of Gans v New York State Tax Appeals Trib.***, 194 AD3d 1209, 1211 [3d Dept 2021]; ***Matter of HDV Manhattan, LLC v Tax Appeals Trib. of the State of N.Y.***, 156 AD3d 963, 965-966 [3d Dept 2017]; ***Matter of 677 New Loudon Corp. v State of N.Y. Tax Appeals Trib.***, 85 AD3d 1341 [3d Dept 2011], ***affd*** 19 NY3d 1058 [2012], ***rearg denied*** 20 NY3d 1024 [2013], ***cert denied*** 571 US 952 [2013]; ***Matter of 44th Enterprises Corp. and MLB Enterprises Corp.***, Tax Appeals Tribunal, May 26, 2022; ***Matter of Marchello***, Tax Appeals Tribunal, April 14, 2011).

A separate charge for access to a private room in an adult entertainment club is also considered a charge for entertainment subject to sales tax pursuant to Tax Law § 1105 (f) (1) and (3) where the private room is to be used for a private dance (***Matter of HDV Manhattan, LLC***; ***Matter of The Executive Club LLC***, Tax Appeals Tribunal, April 19, 2017).

Scrip sales in an adult entertainment club are subject to sales tax where such scrip is used by customers to pay charges for admission, amusement or entertainment taxable pursuant to Tax Law § 1105 (f) (1) and (3) (***Matter of Gans***, 194 AD3d at 1211; ***Matter of HDV Manhattan, LLC***, 156 AD3d at 965; ***Matter of Marchello***; ***see also Metro Enters. Corp. v New York State Dept. of Taxation & Fin.***, 171 AD3d 1377, 1380 [3d Dept 2019]). Sales tax is collectable on

such scrip sales at the time the customer purchases the scrip (***Matter of Executive Club, LLC***, Tax Appeals Tribunal, July 24, 2019, ***confirmed sub nom Gans v New York State Tax Appeals Trib.***)

We agree with the Administrative Law Judge that the Club qualifies as a place of amusement under the statutory definition, leaving only the question of whether the transactions here at issue qualify as sales of scrip to pay charges for admission, amusement or entertainment, thus qualifying as taxable admission charges. In accordance with our prior holdings, we conclude that they do.

As noted by the Administrative Law Judge, a presumption of correctness attaches to a notice of determination upon its issuance (***Matter of Hammerman***, Tax Appeals Tribunal, August 17, 1995). So long as it appears that a rational basis existed for the Division's determination, the burden of proof lies with petitioners to show, by clear and convincing evidence, that the audit method employed or the tax assessed was unreasonable (***Matter of Meskouris Bros. v Chu***, 139 AD2d 813 [3d Dept 1988], citing ***Matter of Surface Line Operators Fraternal Org. v Tully***, 85 AD2d 858 [3d Dept 1981]). We note that here petitioners take no issue with the accuracy of the calculations regarding receipts from sales of scrip. Rather, petitioners steadfastly maintain that scrip could be and was only used for voluntary gratuities to the dancers, and thus was not subject to sales tax. However, this contention is belied by the record. We have reviewed the contracts in the record between West 20th and the dancers and have considered the Club's requirement that the dancers charge locally prevailing rates for dances. We note the Division's observations made during the field audit that admissions to private and semi-private rooms carried specific charges, revenue from which was reported by Sushi Fun, in addition to the fees paid to the dancers. We have also considered the fact that the

Club's dance customers were allowed to access Pacific Club's credit card terminals "to purchase private dances" pursuant to Pacific Club's written agreements with the dancers. Moreover, petitioners' responsive pleadings in the ***Acevedo*** matter, wherein petitioners asserted that the Club charged mandatory performance fees, only further confirms that the scrip was not exclusively used for discretionary gratuities.

While it is possible that some scrip purchased from Pacific Club was used to tip dancers, it was incumbent upon petitioners to prove the amount of scrip so used (***see Matter of HDV Manhattan, LLC***, 156 AD3d at 966). Petitioners have failed to show what amount of scrip purchased was used exclusively for tipping and, accordingly, have failed to meet their burden of proof. We agree with the Administrative Law Judge that the record demonstrates that scrip sold in the Club was used to purchase exotic dances, and thus constitutes charges for admission to a place of amusement or to a roof garden, cabaret or similar place, or as an entertainment charge to be included in taxable receipts for sales of food and beverages, and thus subject to sales tax pursuant to Tax Law § 1105 (f) (1) and (3) and Tax Law § 1105 (d).

Tax Law § 1132 (c) (1) creates a presumption that all receipts for amusement charges described under Tax Law § 1105 (f) and services described under Tax Law § 1105 (d) are subject to tax until the contrary is established, and the burden of proving that any receipt or amusement charge is not taxable is allocated to the person required to collect tax or the customer. Persons required to collect tax include, among others, every vendor of tangible personal property or services and every recipient of amusement charges (Tax Law § 1131 [1]). As discussed, petitioner Pacific Club was a recipient of amusement charges through its agreements with the dancers to allow customers of the Club to use its credit card terminals "to purchase private dances" in exchange for 20% of the face value of scrip. Similarly, Sushi Fun was a recipient of

amusement charges due to the fact that it was the recipient of room charges for private and semi-private dances. Finally, West 20th qualified as a recipient of amusement charges through its concession agreement with Pacific Club, wherein Pacific Club paid West 20th for the exclusive right to operate a scrip desk at the Club, the explicit purpose of which was to "facilitate payment of entertainers in the nightclub by patrons." We conclude that petitioners were persons required to collect tax by reason of their qualification as recipients of the amusement charges at issue herein.

Petitioners also assert, as they did below, that the Division should be estopped from asserting sales tax on sales of scrip based on the outcome of a prior audit of the Club. We note that absent unusual facts, the doctrine of estoppel may not be invoked against a governmental agency engaged in the exercise of its governmental functions (***Matter of Ryan v Tax Appeals Trib. of the State of N.Y.***, 133 AD3d 929, 930 [3d Dept 2015]; ***see also Matter of Rashbaum v Tax Appeals Trib. of State of N.Y.***, 229 AD2d 723, 725 [3d Dept 1996]; ***Matter of Walsh v Tax Appeals Trib. of State of N.Y.***, 196 AD2d 367, 370 [3d Dept 1994]) and does not typically apply in tax cases unless "unusual circumstances support a finding of manifest injustice" (***Matter of Ryan***, at 930, citing ***Matter of Salh v Tax Appeals Trib. of State of N.Y.***, 99 AD3d 1124, 1126 [3d Dept 2012] ***lv denied*** 20 NY3d 863 [2013]; ***see also Matter of Winners Garage, Inc. v Tax Appeals Trib. of the State of N.Y.***, 89 AD3d 1166, 1168-1169 [3d Dept 2011], ***lv denied*** 18 NY3d 807 [2012]). In order to invoke estoppel against a party, the proponent must establish three elements: 1) conduct which amounts to a false representation or concealment of material facts; 2) intention that such conduct will be acted upon by the other party; and 3) knowledge of the real facts (***Matter of Rashbaum*** 229 Ad2d at 725).

We agree with the Administrative Law Judge that petitioners have not established the requisite elements to impose an estoppel on the Division nor have they shown that unusual circumstances are present that support a finding of manifest injustice. The letter from the Division's director of sales tax audits that petitioners argue forms the basis for their estoppel claim does not rise to the level of false representation or concealment that would be necessary to establish that the Division intentionally misled petitioners. The language of the letter is prospective and contingent upon petitioners demonstrating their business model, which, in turn, is premised on the fact that the Club does not charge for private dances, which petitioners have failed to prove. Furthermore, petitioners were not entitled to rely on the letter, as results from prior audits are not binding on subsequent audit periods (***People ex rel. Watchtower Bible & Tract Socy. v Haring***, 286 AD 676, 680 [3d Dept 1955], ***lv granted*** 11 AD2d 605 [3d Dept 1960]; ***Matter of 677 New Loudon Corp D/B/A Nite Moves***, Tax Appeals Tribunal, August 25, 2016; ***Matter of Winners Garage, Inc.***, Tax Appeals Tribunal, April 16, 2014, ***confirmed sub nom Wolkowiki v New York State Tax Appeals Trib.***, 136 AD3d 1223 [3d Dept 2016]).

Petitioners assert that assessments issued to them for sales tax on sales of scrip in the Club violated the United States and New York constitutions, in essence arguing impossibility of simultaneous compliance with New York tax law and state and federal labor laws. Petitioners' constitutional arguments are as-applied claims, which we may consider (***Matter of Frog Design, Inc.,*** Tax Appeals Tribunal, April 15, 2015, citing ***Matter of Eisenstein***, Tax Appeals Tribunal, March 27, 2003). Petitioners argue that state and federal labor laws require them to treat the dancers as employees, and thus scrip must be deemed to be a gratuity and not a fee. Even assuming that amounts paid to the dancers are gratuities for labor law purposes, petitioners have not explained how it was impossible to comply with the Tax Law under the circumstances. Sales

tax is collectible from the customer at the time of the transaction and such tax is in addition to the amusement charge to which it applies (20 NYCRR 525.2 [a] [4]; Tax Law § 1132 [a] [1]). Here, as was the case in ***Matter of 44th Enterprises Corp. and MLB Enterprises Corp.***, petitioners simply failed to charge and collect sales tax from their customers at the time of the transactions. We also observe that such a constitutional argument, even if petitioners had set forth how the Tax Law as applied to them violated the United States and New York constitutions, would only apply to the entity deemed to have been the employer of the dancers and not petitioners as a whole. The Administrative Law Judge correctly determined that the employment status of the dancers has no bearing on the threshold question presented – that is, whether scrip was used to tip dancers or whether it was used to pay mandatory dance fees. Since petitioners' argument necessarily depends on the proposition that scrip was only used to tip dancers, an assertion that has been proven false, petitioners' constitutional arguments must also fail.

Petitioners have requested an abatement of the penalty assessed for the failure to timely file a return or pay any tax imposed by articles 28 and 29 of the Tax Law (***see*** Tax Law § 1145 [a] [1] [i]). Penalties may be abated if such failure to file or delay was due to reasonable cause and not due to willful neglect (***id.***, at [a] [1] [iii]). As petitioners' failure to timely pay the tax imposed was due to their reliance on their own misrepresentations regarding allowable uses of scrip in the Club, we find that petitioners' position is unreasonable. Accordingly, we deny petitioners' request for abatement of penalties.

Petitioners have requested that this Tribunal take official notice of and consider certain records from a case filed in federal district court for the Southern District of New York in rendering our decision. As we have held in our prior cases, the hearing process must be both

final and defined in order to maintain a fair and efficient hearing system and that the submission of evidence after the record is closed deprives an adversary of its right to question the evidence on the record (***Matter of Jenkins Covington, N.Y.***, Tax Appeals Tribunal, November 21, 1991, ***confirmed***, 195 AD2d 625, ***lv denied*** 82 NY2d 664; ***Matter of Schoonover***, Tax Appeals Tribunal, August 15, 1991).

Petitioners are correct that a court may take judicial notice of particular facts if the items are of common knowledge or are determinable by referring to a source of indisputable accuracy (***Matter of Crater Club v Adirondack Park Agency***, 86 AD2d 714 [3d Dept 1982], ***affd*** 57 NY2d 990 [1982]). A court may take judicial notice of its own record of proceedings, not only in the case before it, but also in other actions involving one or more of the same parties (***Berger v Dynamic Imports, Inc.***, 51 Misc2d 988 [Civ Ct City of NY, 1966), but need not take judicial notice of records of proceedings in other actions in other courts (***Currier v Woodlawn Cemetery***, 300 NY 162 [1949]). Proof of the facts is required and, accordingly, the records from the other court must be introduced as evidence and accepted as part of the record. For these reasons, we decline to take judicial notice of the facts petitioners ask us to consider in rendering our decision.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of West 20th Street Enterprises Corporation, Pacific Club Holdings, Inc., Sushi Fun Dining & Catering, Inc., and Dominica O'Neill is denied;

2. The determination of the Administrative Law Judge is affirmed;

3. The petitions of West 20th Street Enterprises Corporation, Pacific Club Holdings, Inc., Sushi Fun Dining & Catering, Inc., and Dominica O'Neill are denied; and

4. The notices of determination (L-045423066, L-045427439, L-045427440, and L-045427441), dated August 30 and 31, 2016, are sustained.

Dated: Albany, New York
February 23, 2023

/s/ Anthony Giardina
Anthony Giardina
President

/s/ Dierdre K. Scozzafava
Dierdre K. Scozzafava
Commissioner

/s Cynthia M. Monaco
Cynthia M. Monaco
Commissioner