STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
JOHN SCARFI	:	
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, 2008 through February 28, 2014.	:	DECISION DTA NOS. 828745 AND 828746
In the Matter of the Petition	:	
of	:	
METRO ENTERPRISES CORP.	:	
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, 2008 through February 28, 2014.	:	

Petitioners, John Scarfi and Metro Enterprises Corp., filed an exception to the determination of the Administrative Law Judge issued on August 5, 2021. Petitioners subsequently filed a motion to remand this matter to the Administrative Law Judge based on new evidence. Petitioners appeared by Barton LLP (Alvan L. Bobrow, Esq., of counsel) on brief and on the motion and by Meister Seelig & Fein LLP (Amit Shertzer, Esq., of counsel) 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 the exception. The Division of Taxation filed a brief in opposition. Petitioners filed a reply brief. The Division of Taxation filed a response to petitioners' motion. Oral argument was heard in Albany, New York, on August 25, 2022, 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 petitioners have met their burden of proving that the sales of scrip at certain adult entertainment establishments were not subject to tax.

II. Whether petitioner Metro Enterprises Corp. was a responsible person within the meaning and intent of Tax Law §§ 1131 (1) and 1133 (a) for the collection and payment of sales tax for scrip sales, general admission charges, bar sales, coat check fees and room rentals of 44th Enterprises Corporation, MLB Enterprises Corporation, Lace Entertainment, Inc., and Stiletto Entertainment LLC for the period March 1, 2010 through February 28, 2014.

III. Whether petitioners are entitled to estoppel against the Division of Taxation.

IV. Whether petitioners have shown that the assessments violate the federal and state constitutions.

V. Whether petitioners have shown that alleged irregularities in proceedings constitute grounds to invalidate the Division of Taxation's assessments.

VI. Whether petitioners' motion to remand the present matter to the Administrative Law Judge should be granted.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except that we have modified findings of fact 35 and 36 to reflect the record more accurately. We have also added additional findings of fact numbered 53, 54 and 55. The Administrative Law Judge's findings of fact, the modified findings of fact and the additional findings of fact appear below.

1. By letter dated April 21, 2014, the Division of Taxation (Division) scheduled a field

audit with petitioner, Metro Enterprises Corp. (Metro), for the period March 1, 2008 through February 28, 2014 (the period at issue or audit period). The letter advised Metro that during an audit appointment on May 15, 2014, it must provide "any and all documentation in auditable form" and included an information document request (IDR) describing the books and records to be produced.

2. Petitioner, John Scarfi was an officer, director, and shareholder of Metro during the period at issue.

3. In Mr. Scarfi's affidavit, dated January 30, 2018, attached to petitioner's exhibit 1, he states that he is the sole officer of Metro. Mr. Scarfi's sworn statement is contradicted by Metro's bank signature card that lists Debra Zarucka as Metro's vice president.

4. Metro's audit was commenced as a result of audits the Division was conducting of two other entities, 44th Enterprises Corporation (44th) and MLB Enterprises Corporation (MLB). The audits of Metro, 44th and MLB were conducted by the Division's auditor, Jennifer Genovese, under the supervision of auditor Christine Scala.

5. The Division also audited Lace Entertainment, Inc. (Lace), and Stiletto Entertainment, LLC (Stiletto) during the same time frame. The Division's auditor, Crystal Ricks, conducted those audits under the supervision of Ms. Scala.

6. 44th, MLB, Lace and Stiletto (collectively referred to as the Clubs) operated adult entertainment clubs in New York, New York, during the period at issue.

7. During the audits, the auditors determined that Metro's role with the Clubs was integral, and they were structured in a way that one could not exist without the other. The auditors found that transactions were commingled between Metro and the Clubs and could not be distinguished. The auditors also determined that the same employees were working for and

receiving payments from both Metro and the Clubs.

8. The auditors also noted that books and records of Metro and the Clubs were commingled. During the audit of MLB, its owner provided the auditors with envelopes containing a day's receipts for both MLB and Metro stapled together.

9. The Clubs offered live exotic dance performances to patrons and collected general admission charges, admission charges for dances in private rooms, private dance fees, charges for alcoholic and nonalcoholic beverages and coat check fees from customers. The Clubs also collected performance fees from the dancers in the amount of $150.00 per performance date (***see*** finding of fact 25).

10. Metro provided the Clubs with dancer referrals and scheduling, and dispensed scrip in the Clubs by providing credit card terminals for the exchange of patrons' credit card payments into scrip. Scrip (also known as funny money or Lace dollars) is a fictitious currency patrons could purchase at the Clubs with a credit card. Scrip could be used to purchase exotic dances at the Clubs. In Mr. Scarfi's affidavit, dated January 30, 2018, attached to petitioners' exhibit 1, he affirms that "[p]atrons often used scrip for 'tips' in addition to 'dancer fees.'"

11. An example of the scrip dispensed by Metro was introduced into the hearing record by the Division. The scrip is in a denomination of "20," prominently displays that club's name, "Lace," and lists the club's address, and further states "visit our sister club, Lace 2" and lists the address. There is fine print at the bottom that is mostly illegible, the legible portion of which states "property of Metro Enterprises" and contains an expiration date in December 2013.

12. Customers could pay for exotic dances at the Clubs with cash or scrip. The use of scrip allowed customers to pay for dances with a credit card rather than using cash. A customer would purchase scrip through the Clubs' employees, who would run the charge through a credit

card terminal maintained by Metro. Metro charged patrons a 20% surcharge on every purchase of scrip (e.g., a customer is charged $120.00 in order to receive $100.00 of scrip). Metro charged the dancers a 10% or 20% redemption fee when they redeemed the scrip for cash.[1]

13. Metro had credit card terminals at each of the Clubs for processing customers' credit cards for the purchase of scrip. The credit card terminals were maintained by Metro inside the Clubs and were operated by the Clubs' employees. Mr. Scarfi testified that for a period of time either Metro's credit card terminal or the club's credit card terminal went down and they "swapped out terminals." He did not specify which club and it is unclear from his testimony whether it was Metro's or the club's terminal that went down or what charges were placed on the other's terminal.

14. MLB's and 44th's credit card terminals were also used to process scrip transactions on occasion.

15. Entertainment Services Agreements (agreements) between Metro and the Clubs provided that Metro would refer exotic dancers to perform at the Clubs. The agreements provided that Metro agreed to schedule dancers for performance dates at the Clubs, Metro would provide the Clubs with adequate supplies of "funny money," Metro agreed to place on the Clubs' premises its credit card machines for all patron purchases of "funny money," and Metro agreed to be solely responsible for all credit card transactions conducted on its credit card machines. The agreements further provided that all customer credit card purchases of "funny money" shall be made exclusively on Metro's credit card machines, "the income from which shall be exclusively owned by Metro," and that the Clubs agreed to make no claim of any right, title or interest in the proceeds from Metro's credit card machines.

[1] Although Mr. Scarfi testified that the redemption fee is 10%, a contract between Metro and a dancer presented into the record provides that Metro retains 20% of the face value of the scrip.

16. Metro did not report the credit card payments from the sales of scrip as income on its federal income tax return. Mr. Scarfi testified that Metro reported only the 20% surcharge from the scrip sales and 10% redemption fee as income on its federal returns.

17. In order for dancers to redeem scrip received from a customer into cash, they were charged a 10% (or 20%, ***see*** footnote 1) redemption fee by Metro. To redeem the scrip for cash, the dancers would go to the Clubs' managers at the end of the night, and the managers would exchange the scrip for cash, less Metro's redemption fee. The cash used to redeem the scrip came from Metro's bank accounts and was kept in safes located in the Clubs. The managers who sold the scrip to the patrons and exchanged the scrip into cash for the dancers were employees of the Clubs.

18. During the audit, Mr. Scarfi told the auditors that either he, Metro's employee Keith Warech, or one of the Clubs' employees would bring cash from Metro's bank to the Clubs to cash out the dancers' scrip.

19. Mr. Scarfi testified that Metro only had one employee and the Clubs' employees processed the credit card transactions for the sale and redemption of scrip. Mr. Scarfi further testified that Metro does not compensate the Clubs' employees for running Metro's scrip transactions and delivering Metro's cash. However, Metro's business records show repeat payroll expenses to Catherine Navarro, Viktoryia Arbolay, Olga Deulina, Leticia Johnson, Brianna, Zurec, Jennifer Padilla, Jessica Stankowski, Krystle Rivera, Evtenlya Fletcher, and Ulrike Wrage. In addition to Metro's records showing payroll expenses, the Division introduced into the record numerous checks from Metro made out to these individuals and others, including but not limited to Alyshia Holland, Mario Barnes,[2] Jacqueline Martino, Jennifer Saffi, Sandra

[2] Mr. Barnes was a manager at MLB (***see Matter of 44th Enterprises Corp. and MLB Enterprises Corp.***, Tax Appeals Tribunal, May 26, 2022, finding of fact 2). Official notice of the record of proceedings in ***Matter of***

Harting, Keema Jamison, Yvonne Fentelli, Daniella Visocky, Barbara Gallo, Greg Alfredo, Joseph Labetti, Phil Compargio, and Richard Kennedy. When questioned regarding the checks from Metro to these individuals, Mr. Scarfi testified that checks were made out to "Richard and Jessica and [Ulrike], those are employees of the club," and were for reimbursements of tips left by patrons when credit card transactions were processed by Metro. According to Mr. Scarfi, "[s]o what happened was, when the credit card terminals spits out a receipt customers wanted to leave the waitress money. So they would write, I want to leave this girl, I don't know five dollars, ten dollars whatever the amount was . . ." and added that it "only happened in one club." Mr. Scarfi did not identify which club or provide an explanation for the other checks in the record made out to the other individuals and checks that exceeded $5.00 or $10.00. During the audit of Metro, Mr. Scarfi told the auditor that the checks were written to the Clubs' employees.

20. Alyshia Holland, an employee of 44th, had signatory authority on Metro's bank account and withdrew money from Metro's account and delivered it to the Clubs when needed. Mr. Scarfi testified that he never paid Ms. Holland. Metro's bank records show checks paid from Metro to Ms. Holland as follows:

- 12/28/07, check #1298, $645.00
- 1/24/08, check #1490, $520.00
- 1/18/08, check # 1480, $1,025.00
- 3/13/08, check #1586, $590.00
- 4/3/08, check #1618, $705.00
- 5/23/08, check #1715, $955.00
- 8/1/08, check #1838, $580.00
- 8/15/08, check #1865, $1,135.00
- 8/28/08, check #1888, $845.00
- 9/18/08, check #1928, $760.00
- 11/21/08, check #2034, $685.00

44th Enterprises Corp. and MLB Enterprises Corp. 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]).

- 12/11/08, check #2082, $880.00

21. Mr. Scarfi testified that Metro did not make any payments to the Clubs and the Clubs made no payments to Metro. Contrary to Mr. Scarfi's testimony, the affidavit of Anthony Capeci, attached to petitioners' exhibit 1, states that the Clubs paid registration fees to Metro by cash.

When questioned further as to whether payments or loans were made by Metro to the Clubs, Mr. Scarfi testified that at one club, for about six months, either Metro's credit card terminal or the club's terminal went down and they "swapped out terminals." He did not identify the one club where he claimed this occurred or specify the alleged six-month period. Metro's bank statements show the following payments to the Clubs:

Date	Club	Amount
11/25/08	MLB	$20,000.00
1/12/09	MLB	$26,775.00
1/4/10	MLB	$22,175.00
1/25/10	MLB	$21,525.00
2/1/10	MLB	$16,050.00
2/13/10	MLB	$21,975.00
12/31/10	Stiletto	$3,728.00
12/31/10	Lace	$13,263.00
1/31/11	Lace	$45,347.00
4/11/11	Lace	$55,347.00
12/31/11	Lace	$67,056.00
3/13/12	Lace	$59,256.00
6/5/12	Lace	$48,836.00
1/20/14	44th	$15,000.00
1/23/14	44th	$2,173.00
1/24/14	44th	$10,000.00
1/31/14	44th	$10,000.00
2/24/14	44th	$10,000.00

There was no explanation in the record for the discrepancy between Mr. Scarfi's testimony and the documentary evidence.

22. During the audits, the auditors were informed by the Clubs' managers that if a

customer wanted a dance in a private room, they were charged separately on two credit card receipts – one for the room charge and one for the dance fee. The charges varied depending on the size of the room and the amount of time spent with the dancer.

23. The Clubs had a minimum fee of $20.00 for dances. Petitioners' witness, Anthony Capeci, testified that the dancers could negotiate a higher or lower price for a personal dance with the customer.[3]

24. The Division introduced into the record copies of Professional Exotic Dancer Registration and Referral Service Contracts (referral contracts) between Metro and the dancers, obtained by the auditors during the audit of Metro. The referral contracts provide that dance customers may use Metro's credit card machine to "purchase private dances" and Metro is entitled to retain 10% or 20% "of the face value of all 'Funny Money' purchased by patrons at any Registered Adult Nightclubs and used to pay DANCER for her services of rendering private dances."

25. The auditors also obtained copies of contracts between the Clubs and the dancers entitled Non-Exclusive Lease of Entertainment Facilities (contracts). The contracts provide that the dancers will pay the club $150.00 per performance date, and that all scheduling of dancers' performances shall be arranged through Metro.[4] The contracts also provide that the "Club agrees

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[3] It is noted that in ***Dennis v 44th Enterprises Corp. and Capeci***, (Sup Ct, NY County, Freed, J, Index No. 153420/2016), plaintiff Louisa Dennis, a dancer at 44th's club, stated in an affidavit that "I did not set the price for dances – Lace II did." Official notice of the record of the proceedings in ***Dennis v 44th Enterprises Corp. and Capeci***, is taken pursuant to SAPA § 306 (4), by which official notice can be taken of all facts of which judicial notice could be taken. The Division of Tax Appeals may take official notice of official court records and filings from other state and federal actions and proceedings (***see e.g. RGH Liquidating Trust v Deloitte & Touche LLP***, 71 AD3d 198, 207-208 [1st Dept 2009] ***revd on other grnds*** 17 NY3d 397 [2011]). Petitioners' witnesses testified regarding the ***Dennis*** matter and entered a portion of the pleadings into the record, but did not enter the entire record of proceedings. As such, official notice of the full record of proceedings in the ***Dennis*** matter is taken.

[4] The affidavits of both Mr. Scarfi and Mr. Capeci included with petitioners' exhibit 1 state that the agreements between the dancers and the Clubs specify that the dancers' scheduling will be negotiated between the dancers and the Clubs. Petitioners provided no explanation for the discrepancy between the contracts and the affidavits.

that Entertainer is 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.'" The contracts further provide as follows:

> "No Employment Relationship
>
> The parties agree that Entertainer is not an 'employee' of the Club. Entertainer agrees Club will not pay her wages, overtime, expenses, benefits, or any other employee-related benefits, in exchange for permitting her to retain all dance fees paid to her by customers while on Club's premises.
>
> Entertainer further understands that she is entitled to retain all dance fee and gratuities paid to her by patrons on Club's premises only during such periods as she is considered a non-employee."

26. Mr. Scarfi testified that dancers, waitresses and bartenders were all employees of the Clubs. Mr. Capeci testified that during the audit period, the Clubs were not treating the dancers as employees and were not reporting tips, withholding payroll taxes or paying worker's compensation insurance for the dancers. During the audit of Metro and the Clubs, the auditors were told that the dancers were tenants of the Clubs. In the ***Dennis*** matter answer (***see*** footnote 3), 44th and Mr. Capeci affirmatively stated that the dancers were independent contractors, not employees. In the ***Dennis*** matter admissions, 44th and Mr. Capeci admitted that the dancers did not receive compensation (i.e., hourly, salaried or otherwise) from them.

27. Mr. Scarfi offered contradictory testimony as to whether records were maintained for the scrip transactions. He initially testified that Metro kept books and records of money paid to dancers from the redemption of scrip and payments the customers made with scrip. However, he later testified that the money from the credit card transactions for scrip purchases were not recorded in Metro's books and records.

28. Petitioners did not introduce into the record any documents with regard to patrons'

credit card transactions for scrip or dancers' redemption of scrip for cash. The Division introduced into the record copies of handwritten ledger pages dated March 13, 2010, March 23, 2010, April 5, 2010, April 23, 2010, April 29, 2010, May 5, 2010, May 25, 2010, March 23, 2012, June 2, 2012, June 14, 2012, July 10, 2012, July 23, 2012, and August 2, 2012 obtained during the audit. Mr. Scarfi identified the documents as business records of Metro. Attached to the ledger pages are settlement reports for the corresponding dates showing a summary of charges for Visa, Mastercard and American Express, described by Mr. Scarfi as "batch reports." Metro's name and address appears at the top of the batch reports. The batch reports do not contain a tip line showing amounts paid for tips, and do not identify individual transactions. The amounts in the ledgers are inconsistent with the batch reports and petitioners offered no testimony to explain the records. When questioned whether he had any documents that would show a receipt for tips, Mr. Scarfi testified that he did not.

29. Metro did not file any sales tax returns or pay any sales tax to New York for the period at issue.

30. During the audit of Metro, the Division requested that Metro provide its books and records for the period at issue. Similarly, during the audits of the MLB, 44th, Lace and Stiletto, the Division requested that each provide their books and records for the audit period.

31. The Division reviewed the books and records provided by Metro and the Clubs and determined that they were incomplete and insufficient to determine the proper amount of sales tax.

32. Metro maintained separate bank accounts for the credit card receipts from scrip sales from each of the Clubs. The Division issued subpoenas for Metro's bank statements. The auditors transcribed the deposits from credit card receipts in Metro's bank accounts for the

period at issue to compute its tax liability from scrip receipts.

33. Based on a review of Metro's bank deposits, the Division determined taxable sales from the sale of scrip in the amount of $38,281,746.00.

34. The auditors also determined that Metro was responsible for taxes due on additional audited taxable sales made in each of the Clubs. During the audits of the Clubs, the Division determined tax due from the sales of beverages, room rentals, general admission charges and coat check charges.

35. For sales at MLB's club, the auditors added the club's receipts from bar sales, door admissions, coat check and room rentals for the quarter ending November 2013 and determined audited gross receipts from those areas of $1,051,743.82 for that quarter. The club did not separately state sales tax on its invoices. Therefore, to determine audited sales, the auditor subtracted tax remitted for that quarter ($59,575.92) from audited gross receipts and determined audited gross sales of $992,167.90 for the quarter. The auditor divided audited gross sales by gross sales reported by MLB for that quarter ($671,278.00) to determine an error rate of 1.478.[5] The auditor then multiplied gross sales reported in the amount of $8,790,452.00 by the error rate to determine audited gross sales of $12,992,537.09 and additional taxable sales of $4,202,085.09 for the period March 1, 2010 through February 28, 2014 from MLB's door admissions, coat check, bar sales and room rentals.

36. The Division used the same method detailed in finding of fact 35 to determine the additional gross sales from bar sales, door admissions, coat check and room rentals at 44th's club for the period March 1, 2010 through February 28, 2014. For the quarter ending November 2013, 44th's audited gross receipts from bar sales, door admissions, coat check and room rentals

[5] The determination of the Administrative Law Judge erroneously states that the error rate was 1.47%. The audit report and the computations therein show the correct error rate as 1.478.

were $662,326.08. To determine audited sales, the auditor subtracted tax remitted for that quarter ($40,622.65) from audited gross receipts and determined audited gross sales of $621,703.43 for the quarter. The club had reported gross sales of $457,720.00 for that quarter. The auditor divided audited gross sales by gross sales reported to determine an error rate of 1.3583.[6] The auditor then multiplied gross sales reported ($4,698,853.00) by the error rate to determine audited gross sales of $6,382,270.89 and additional taxable sales of $1,683,417.89 for the period March 1, 2010 through February 28, 2014 for door admissions, coat check, bar sales and room rentals at 44th's club.

37. The Division used a similar audit method to determine the taxable sales at Lace's and Stiletto's clubs from bar sales, door admissions, coat check and room rentals. Although Lace and Stiletto did not provide complete and adequate books and records as requested for the entire audit period, they provided some computerized point of sales records for the quarter ending November 2013. The auditors compared the point of sales records to the sales reported by Lace and Stiletto for that quarter.

38. For Lace, the auditor compared its point-of-sale records to its reported sales for the quarter ending November 2013 and calculated an error rate of .16. The auditor then multiplied gross sales reported by the error rate to determine audited gross sales of $1,303,460.40 and additional taxable sales of $228,049.74 for the period September 1, 2013 through February 28, 2014 from door admissions, coat check, bar sales and room rentals at Lace's club.

39. For Stiletto, the auditor compared its point-of-sale records to its reported sales for the quarters ending November 2013 and February 2014 (no point-of-sale system was in place for the months of September and October 2013, so the auditor determined an average for these months)

[6] The determination of the Administrative Law Judge erroneously states that the error rate was 1.35%. The audit report and the computations therein show the correct error rate as 1.3583.

and determined additional taxable sales of $43,267.34 for the period September 1, 2013 through February 28, 2014 from door admissions, coat check, bar sales and room rentals at Stiletto's club.

40. The Division determined that Metro had taxable sales and tax due for the period March 1, 2008 through February 28, 2014 as follows:

Sales of scrip at MLB club	$23,912,554.61
General admission, bar sales, coat check, room rental at MLB	$4,202,085.08
Sales of scrip at 44th club	$6,308,899.73
General admission, bar sales, coat check, room rental at 44th	$1,683,417.89
Sales of scrip at Stiletto club	$1,293,723.33
General admission, bar sales, coat check, room rental at Stiletto	$43,267.34
Sales of scrip at Lace club	$6,866,568.33
General admission, bar sales, coat check, room rental at Lace	$228,049.74
Total Taxable Sales	**$44,438,566.05**
Total Tax Due	**$3,863,002.13**

41. The Division issued notice of determination L-045794061, dated December 1, 2016, to Metro asserting tax due of $3,863,002.13 plus penalties and interest for the period March 1, 2008 through February 28, 2014.

42. The Division issued four notices of determination, each dated December 1, 2016, to petitioner Scarfi. Notice of determination L-045796581 asserted tax due of $3,863,002.13 plus penalties and interest for the period March 1, 2008 through February 28, 2014 from Mr. Scarfi as a responsible person of Metro. Notice of determination L-045794591 asserted tax due of $94,622.50 plus penalties and interest for the period ended February 28, 2014 from Mr. Scarfi as

a responsible person of MLB. Notice of determination L-045794596 asserted tax due of $25,339.55 plus penalties and interest for the period ended February 28, 2014 from Mr. Scarfi as a responsible person of 44th. Notice of determination L-045794597 asserted penalties of $10,000.00 from Mr. Scarfi as a responsible person of 44th, for 44th's failure to provide books and records for the period ended February 28, 2014.

43. Mr. Capeci had check signing authority for Metro and signed checks on occasion. Mr. Capeci testified that he signed checks from Metro's account for employees when Mr. Scarfi was not available, but he did not specify whose employees he signed checks for. Mr. Scarfi testified that Metro only had one employee, Keith Warech, and Mr. Capeci signed checks on Metro's account for other individuals, at least some of whom were employees of the Clubs. The Division presented into the record copies of at least 28 checks from Metro's account signed by Mr. Capeci during the audit period. In contrast to the testimony and documentary evidence, Mr. Scarfi affirmed under oath in his affidavit introduced with petitioners' exhibit 1 that Mr. Capeci never exercised his check signing authority for Metro.

44. Mr. Scarfi had signatory authority on MLB's and 44th's bank accounts.

45. Mr. Capeci was the owner and officer of MLB and 44th.

46. In addition to the testimony of Mr. Scarfi and Mr. Capeci, petitioners offered the testimony of Jennifer Kinsley. When the nature of the witness's testimony was questioned by the Division's counsel, petitioners' representative stated that Ms. Kinsley was an expert in state and local sales tax. The Division objected to her qualifications as a sales tax expert and Ms. Kinsley admitted that she is not an expert in state and local taxation. Rather, she stated that she is "an expert in other legal matters that will not be relevant today" but could "factually . . . offer information . . . ." The Administrative Law Judge instructed the parties that the witness would

not be recognized as an expert witness for purposes of testimony, that opinion testimony would not be allowed, and the testimony was limited to factual issues for which Ms. Kinsley had first-hand knowledge. Ms. Kinsley testified that she is an attorney and has represented Mr. Capeci, MLB and 44th in various employment-related lawsuits, and discussed the posture of the ***Dennis*** matter and a declaratory judgment action by MLB. She testified that Metro has a contractual relationship with 44th and MLB. Ms. Kinsley further testified regarding MLB's and 44ths club setups. She described that the Clubs sell beverages and have a public stage area where customers can view exotic dancers, as well as private party rooms where dancers perform for customers. She further testified that Metro provides machines in the Clubs that exchange customers' credit card payments for scrip, which, according to Ms. Kinsley, enables the customer to offer a credit card gratuity to the entertainers. During cross examination, Ms. Kinsley claimed that patrons were never charged dance fees, that there were no dance fees that the club sets, and that patrons paid gratuities to entertainers of their own choice. Ms. Kinsley further testified that she did not look at ledgers or "in and out list of transactions" that showed Metro paying scrip value over to the entertainers, but later testified that she did see books and records showing that a transfer of scrip payments from Metro to the dancers took place. However, she did not identify or describe what books or records she was referring to, and petitioners did not offer any into evidence.

47. In the ***Dennis*** matter answer, 44th and Mr. Capeci denied plaintiff Dennis's allegation that the club's customers reasonably believed that 100% of the tips would be given to employees and affirmatively stated that "some or all of the payments received by Plaintiff for performances were administrative charges, which a reasonable customer should understand were not gratuities . . ." (***see*** footnote 3).

48. Petitioners served first requests for admissions, dated June 20, 2019, and second requests for admissions, dated June 25, 2019, on the Division. The Division timely responded to petitioners' first and second requests for admissions on July 10, 2019 and July 15, 2019, respectively.

49. On July 5, 2019, petitioners filed a motion for summary determination. Included with the motion was a memorandum of law, an affirmation from Mr. Bobrow dated July 3, 2019, affidavits from ***Metro Enterprises Corp. & Scarfi v New York State Dept. of Taxation and Finance*** (Sup Ct, Albany County, Index No. 901347-17) of John Scarfi, dated January 30, 2018, Glenn Orecchio, dated January 30, 2018, and Anthony Capeci, dated January 29, 2018,[7] copies of the following pleadings from ***Dennis v 44th Enterprises Corp., et al.***, (Sup Ct, NY County, Index No. 153420/2016): class action complaint, defendants-stakeholders' interpleader complaint against plaintiffs-claimants and third party defendants-claimants and cross-complaint for declaratory and injunctive relief against cross-defendants-claimants, answer and claim in interpleader of defendant-claimant Metro Enterprises Corp., and defendants-stakeholders 44th Enterprises and Anthony Capeci's response to plaintiffs' first request for admissions. Petitioners also included a copy of a complaint for declaratory and injunctive relief from ***MLB Enterprises Corp. v New York State Dept. of Taxation and Finance*** (US District Court, Southern District of NY), copies and petitioners' first and second requests for admissions, and a copy of a document entitled tax field audit record for MLB Enterprises Corp.

By letter dated July 8, 2019, the Administrative Law Judge informed petitioners that pursuant to 20 NYCRR 3000.5 (e), the filing of a motion does not constitute cause for postponement of a hearing from the set date and the hearing would not be adjourned. Petitioners

[7] The affidavits of Scarfi, Orecchio and Capeci each reference attached exhibits; however, no exhibits were attached to the affidavits.

were told that issues raised in their motion may be raised during the scheduled hearing and would be ruled on in the determination in this matter. Petitioners presented a partial copy of their motion for summary determination into the record during the hearing, consisting of the notice of motion, memorandum of law and affirmation of Mr. Bobrow, and the above-mentioned affidavits from ***Metro Enterprises Corp. & Scarfi v New York State Dept. of Taxation and Finance*** of Mr. Scarfi and Mr. Capeci, without the referenced exhibits attached, and an unsigned affidavit of Mr. Orecchio, without the referenced exhibits attached. At the time the motion was offered into the record, the Administrative Law Judge asked Mr. Bobrow whether it was the complete document that was previously filed, to which he responded yes. However, a comparison reveals that motion introduced into the record consisted of only a portion of the papers originally filed.

50. 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."

51. 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.

52. Petitioners also introduced a redacted, unsigned letter, dated July 30, 2004, allegedly from Frank Susi, Tax Technician II of the Division's Sales Tax Instructions & Interpretations unit. The name and address of the party to whom the letter was sent is redacted. The letter states, in pertinent part:

> "I am writing in response to your letter dated July 16, 2004, [redacted] operates a gentlemen's club and cabaret in [redacted] New York. The club offers a full service bar and live entertainment, but does not serve food. You ask if the performance of private dances for patrons are subject to sales tax.
>
> Section 527.10 of the Sales Tax Regulations provides, in part:
> (a) Imposition. (1) A tax is imposed upon any admission charge in excess of ten cents to or for the use of any place of amusement in this State.
> * * *
> (b)(4)(i) Amusement charge. Any admission charge, dues or charge of a roof garden, cabaret or other similar place.
>
> Accordingly, if a gentlemen's club charges admission to enter the premises, the charges are subject to tax. Private dances, in and of themselves, which are performed for individual patrons, are not subject to tax. However, if private dances are performed in a separate room, then the charges for the private dances are considered to be admission charges subject to tax."

Petitioners did not offer any testimony authenticating the letter.

53. On August 14, 2019, following the hearing in this matter, petitioners filed a motion to reopen the record or for reargument pursuant to 20 NYCRR 3000.16 and to recuse Osborne Jack from representing the Division in this matter. By an order dated January 2, 2020, the Administrative Law Judge denied the motion.

54. On January 28, 2020, petitioners filed a motion for reconsideration of their previous motion to reopen the record or for reargument and to recuse Mr. Jack. Also on January 28, 2020, petitioners filed a motion by petitioner John Scarfi to intervene and for summary determination. On February 11, 2020, petitioner filed a motion to consolidate the present matter with ***Matter of 44th Enterprises Corp. and MLB Enterprises Corp.*** (***Matter of 44th and MLB***) (Division of Tax Appeals, February 18, 2021, ***affirmed*** Tax Appeals Tribunal, May 26, 2022 [DTA Nos. 828639 and 828640]) and ***Matter of Anthony Capeci*** (Division of Tax Appeals, December 23, 2021 [DTA Nos. 828636, 828637 and 828638]). The Administrative Law Judge denied these motions by an order dated September 24, 2020.

55. Petitioners filed a motion with the Tax Appeals Tribunal on May 17, 2022 (four months after they filed their reply brief on exception), seeking to remand this matter to the Administrative Law Judge to consider "newly discovered" evidence consisting of certain documents. Petitioners' motion states that the documents in question, which were attached thereto, did not exist at the time of the hearing. The Division opposed the motion.

THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE

Regarding the taxability of scrip sales, the Administrative Law Judge determined that scrip was used to purchase exotic dances at the Clubs and not merely to tip the dancers. The Administrative Law Judge further determined that scrip sales for the purchase of such dances were subject to tax under Tax Law § 1105 (f) (1) as admission charges to a place of amusement. The Administrative Law Judge rejected petitioners' contention that the structure of the scrip transactions, i.e., separate ownership of the scrip seller and the Clubs, enabled the transactions to avoid sales tax. The Administrative Law Judge also found that petitioner failed to show how much of the scrip, if any, was used for tips, noting evidence indicating a $20.00 minimum charge

for a dance and requirements that customers pay a dancer's fee in the private rooms. Accordingly, given the statutory presumption of taxability and the presumption of correctness attaching to a notice of determination, the Administrative Law Judge found that all scrip sales were taxable. The Administrative Law Judge also found that petitioner Metro was a recipient of amusement charges and a vendor of scrip and was therefore under a duty to collect and remit sales tax on such sales.

The Administrative Law Judge rejected petitioners' argument that the New York Labor Law (Labor Law) and the Federal Labor Standards Act (FLSA) support its contention that the scrip was solely used for gratuities and that petitioners did not retain any portion of the scrip proceeds. The Administrative Law Judge noted evidence showing that scrip was used to pay for dances and that petitioners did retain a portion of the scrip proceeds, i.e., the surcharge and redemption fees, thereby undermining petitioners' argument.

The Administrative Law Judge next determined that petitioner Metro was liable for sales tax due on non-scrip sales at the four Clubs; that is, general admission charges, bar sales, room rentals and coat check fees. She observed various facts in the record that she deemed indicative of a commingling and overlapping of the business operations of Metro and the Clubs, including conducting business at the same locations, effectively sharing employees, and unexplained transfers of funds in large amounts from Metro to the Clubs. Most significantly, according to the Administrative Law Judge, Metro and the Clubs used each other's credit card terminals.

The Administrative Law Judge found that petitioners failed to meet their burden to show error in the non-scrip sales portion of the assessment and concluded, therefore, that petitioner Metro was a person required to collect tax with respect to such receipts and thus liable for the sales tax due on such receipts.

The Administrative Law Judge sustained the notices of determination issued to petitioner Scarfi as a responsible officer of Metro. She noted that there was no dispute that Scarfi was such a person.

The Administrative Law Judge cancelled the notices of determination issued to petitioner Scarfi as a responsible person of 44th and MLB.

The Administrative Law Judge rejected petitioners' argument that the Division should be estopped from asserting the tax at issue against them. She found that petitioners did not establish any false representation by the Division or any representation wherein the Division advised petitioners that their sales of scrip were nontaxable. The Administrative Law Judge found that contrary audit determinations from earlier periods involving non-party taxpayers did not give rise to an estoppel.

The Administrative Law Judge also rejected petitioners' contention that the Division violated SAPA by adopting a policy that scrip sales are always subject to sales tax. The Administrative Law Judge determined that the Division did not have such a policy.

The Administrative Law Judge dismissed petitioners' contention that the assessments violate their due process rights under the federal and state constitutions by making it impossible for petitioners to comply with both tax laws and labor laws. The Administrative Law Judge found that this assertion was premised on petitioners' unfounded claim that the scrip was paid to the dancers solely as voluntary gratuities. The Administrative Law Judge also found that petitioners failed to show that they were treated by the Division differently than any similarly situated taxpayer.

The Administrative Law Judge rejected as baseless the following procedural claims: that the Division refused to conference with petitioners' representative for purpose of stipulation and

that petitioners were thus prejudiced by their inability to proffer stipulated facts; that the Division improperly denied requested admissions; that the Division misrepresented Mr. Capeci's status at the hearing as a non-party witness; that the Division improperly questioned witnesses about documents that were not in its hearing memorandum; that the Division's closing argument was improper; and that consents extending the period of limitations were invalid.

Finally, the Administrative Law Judge sustained the Division's assertion of penalties. She found that petitioners did not provide all records that were requested and those that were provided were incomplete. She also found that petitioners presented no evidence to show that their failure to properly report and pay over sales tax was due to reasonable cause and not due to willful neglect. She noted, however, that the penalty assessment against petitioner Scarfi as a responsible officer of MLB was cancelled.

Also in her determination, the Administrative Law Judge denied petitioners' motion for summary determination.

ORDERS OF THE ADMINISTRATIVE LAW JUDGE

On January 2, 2020, the Administrative Law Judge issued an order denying petitioners' motion to reopen the record or for reargument pursuant to 20 NYCRR 3000.16 and to recuse Osborne Jack from representing the Division in this matter (***see*** finding of fact 53). The motion to reopen or for reargument was denied as premature (***see*** 20 NYCRR 3000.16 [b]). As to their motion to recuse Mr. Jack as the Division's representative in this matter, petitioners argued that Mr. Jack became an essential fact witness in the instant case when he submitted a declaration dated July 26, 2019 in support of a motion to dismiss in a federal case involving MLB and the Division (***MLB Enterprises Corp. v New York State Dept. of Taxation and Fin.*** [USDC SDNY] [19-CV-04679]). Petitioners contended that Mr. Jack was disqualified as a representative under

the Rules of Professional Conduct under these circumstances. The Administrative Law Judge disagreed, finding that: 1) the Division of Tax Appeals lacks jurisdiction to enforce the rules of professional conduct; 2) since MLB is not a party in the present case, the fact that Mr. Jack submitted an affidavit in that case does not make him an essential fact witness in the present matter; 3) the hearing was completed at the time petitioner brought the motion and Mr. Jack had not been called as a witness; 4) the submission of an affidavit by an attorney in support of a motion does not necessarily make that attorney a witness in a case, as it is common practice for an attorney to submit such an affidavit; and 5) the declaration itself shows that the statements therein are based on Mr. Jack's review of the audit file.

The Administrative Law Judge also issued an order dated September 24, 2020 (***see*** finding of fact 54). As relevant here, that order denied petitioners' motion to consolidate the present matter with ***Matter of 44th and MLB*** and ***Matter of Anthony Capeci***. In support of their motion, petitioners asserted that these matters involve virtually identical factual records and substantially similar issues of law. The Administrative Law Judge's denial was premised on petitioners' failure to show that these other petitioners were given notice of the motion, much less supported or joined the request for consolidation. The September 24, 2020 order also denied petitioners' motion for reconsideration of their previous motion to reopen the record or for reargument and to recuse Mr. Jack, as well as a motion by petitioner John Scarfi to intervene, none of which were contested on exception.

ARGUMENTS ON EXCEPTION

Petitioners continue to assert that the scrip at issue was used solely for voluntary gratuities. That is, petitioners contend that customer scrip payments to dancers were voluntary and entirely at the customer's discretion. Petitioners assert that voluntary gratuities are not

subject to sales tax, even where the establishment keeps part of the gratuities, as such gratuities are not admission charges as defined in the Tax Law. Petitioners also continue to assert that relevant FLSA and Labor Law provisions and caselaw require a finding that the scrip payments to the dancers were gratuities. Specifically, petitioners assert that the cash provided to the dancers in exchange for scrip was not recorded in Metro's gross receipts and thus the scrip must be presumed to be gratuities under the FLSA and Labor Law. Petitioners contend that the Division wrongly failed to consider the relevant FLSA and Labor Law provisions on audit. Additionally, petitioners seek to distinguish the present matter from prior cases on the facts by their claim that Metro does not sell dances for profit and that scrip could not be used to purchase dances. Petitioners also contend that the Division's audit wrongly failed to consider the relationship between Metro, the dancers and the Clubs.

Petitioners also argue that the Division should be estopped from moving forward with the subject assessments. Petitioners refer to an earlier audit of an adult entertainment club and a scrip-issuing entity that operated similarly to Metro. Following that audit, the Division ultimately canceled a sales tax assessment based on scrip sales. Petitioners contend that they relied on such prior audit and reasonably believed that they would receive similar treatment. Petitioners further contend that the Division has not explained the difference in treatment between the previous case and the present one.

Petitioners continue to argue that the Division adopted a policy that scrip sales in adult entertainment clubs are always taxable; that this policy is a rule adopted in contravention of the requirements of SAPA; that as such, the rule is invalid and the assessment must be cancelled. Petitioners also contend that the asserted policy is contrary to caselaw requiring an analysis of the relationship between the dancers, the Clubs and the scrip issuer.

Petitioners continue to maintain that the assessments violate their due process rights by imposing conflicting legal obligations upon them, thereby making it impossible to simultaneously comply with both the Tax Law and the relevant labor laws. This is because, according to petitioners, the same amounts determined to be gratuities belonging to the dancers under the labor laws have been determined to be receipts subject to sales tax and payable by petitioners.

Petitioners make many of the same the same claims regarding asserted procedural irregularities as they made to the Administrative Law Judge. Specifically, petitioners continue to assert that the Division refused to conference with petitioners' representative for purpose of stipulation and that petitioners were thus prejudiced by their inability to proffer stipulated facts; that the Division improperly denied requested admissions; that the Division misrepresented Mr. Capeci's status as a non-party witness; that the Division improperly questioned a witness about documents that were not in its hearing memorandum; and that the Division's closing argument was improper.

Petitioners also take exception to the Administrative Law Judge's January 2, 2020 order by which she denied petitioners' motion to recuse the Division's representative in the present matter. As in their motion, petitioners contend that Mr. Jack's representation of the Division in this matter violated the New York Rules of Professional Conduct because he became an essential fact witness when he submitted an affidavit in connection with federal litigation involving MLB and the Division.

Petitioners also take exception to the Administrative Law Judge's September 24, 2020 order denying their motion to consolidate the present matter with ***Matter of 44th and MLB*** and ***Matter of Anthony Capeci***. As they did below, petitioners note the similarity of the facts and

legal issues in these matters. Petitioners also correctly observe that the Administrative Law Judge took official notice of the record in ***Matter of 44th and MLB.***

Although petitioners assert in their notice of exception that the Division erred in attributing the Clubs' non-scrip sales to Metro, thereby subjecting petitioners to sales tax liability for those sales, they offer no legal argument in support of this assertion.

Petitioners do not contest the imposition of penalties in their exception.

The Division contends that the Administrative Law Judge properly found that the sales of scrip were taxable under Tax Law §§ 1105 (f) (1), (f) (3) and (d). The Division agrees with the Administrative Law Judge's finding that the record shows that scrip was not used solely for voluntary gratuities and that petitioners have failed to show what portion of the scrip was used for such gratuities. The Division also contends that petitioners have failed to distinguish prior case law that found similar scrip sales to be taxable.

The Division further agrees with the Administrative Law Judge's rejection of petitioners' arguments regarding labor laws, estoppel, SAPA, constitutionality, and the various procedural issued raised by petitioners in the determination and orders.

OPINION

Taxability of scrip sales

After the determination in the present matter was issued, this Tribunal issued ***Matter of 44th Enterprises Corp. and MLB Enterprises Corp.*** (Tax Appeals Tribunal, May 26, 2022 [***Matter of 44th and MLB***]). In that decision, we held that receipts from scrip sales at 44th and MLB during the period March 1, 2010 through February 28, 2014 were subject to sales tax pursuant to Tax Law § 1105 (f) (1) and (3). The period at issue in ***Matter of 44th and MLB*** falls within the March 1, 2008 through February 28, 2014 period at issue in the present matter

and thus necessarily involves the same business model and, indeed, many of the same scrip transactions as are at issue in the present matter. The record also shows that 44th and MLB were operated in the same manner during the earlier March 1, 2008 through February 28, 2010 period and further show that Lace and Stiletto were operated in the same manner as 44th and MLB at all times relevant. Accordingly, given the substantial similarity in the facts in these two cases, we find that the holding in ***Matter of 44th and MLB*** controls the outcome of the present case with respect to the taxability of the scrip transactions as described herein. The authority for our holding in ***Matter of 44th and MLB*** appears below.

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 is "the amount paid for admission, including 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 "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]). An amusement charge is "[a]ny admission charge, dues or charge of a roof garden, cabaret or other similar place" (Tax Law § 1101 [d] [3]). 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 sales of drinks in a bar 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 subject to sales tax both as an admission charge for the use of a place of amusement pursuant to Tax Law § 1105 (f) (1) and as a charge of a roof garden, cabaret or other similar place pursuant to Tax Law § 1105 (f) (3) (***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 Greystoke Indus.***, Tax Appeals Tribunal, May 19, 2011; ***Matter of Marchello***, Tax Appeals Tribunal, April 14, 2011).

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 v New York State Tax Appeals Trib.***, 194 AD3d at 1211; ***Matter of HDV Manhattan, LLC v Tax Appeals Trib. of the State of N.Y.***, 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.***).

Private dance charges at an adult entertainment club are alternatively taxable under Tax Law § 1105 (d) (***Matter of 677 New Loudon Corp. d/b/a Nite Moves***, Tax Appeals Tribunal, April 14, 2010, ***affd on other grounds Matter of 677 New Loudon Corp. v State of N.Y. Tax Appeals Trib.***).

All charges of any type mentioned in Tax Law § 1105 (f) and receipts under Tax Law § 1105 (d) are presumptively subject to tax until the contrary is established and the burden of

proving that any such charge or receipt is not taxable is upon the person required to collect or the customer (Tax Law § 1132 [c] [1]). Persons required to collect tax include every recipient of amusement charges and every vendor of tangible personal property or services (Tax Law § 1131 [1]). Furthermore, it is well established that a presumption of correctness attaches to a notice of determination issued by the Division, and that the taxpayer must overcome this presumption by clear and convincing evidence (***see e.g. Matter of Wilmarth***, Tax Appeals Tribunal, June 4, 2015).

As in ***Matter of 44th and MLB***, petitioners do not contest the foregoing principles, but rather contend that their customers' scrip payments to the dancers were voluntary gratuities and therefore not subject to sales tax.

Voluntary gratuities are generally not subject to sales tax because such payments are not properly includible in the receipt for property or services taxable under Tax Law § 1105 (a), (c) or (d) or the charge taxable under Tax Law § 1105 (f) (***see*** Tax Law § 1101 [b] [3], [d] [2-4]; ***see also*** TSB-M-09[13]S ["Sales Tax on Gratuities and Service Charges"] [August 4, 2009]).

As the Administrative Law Judge determined, however, the record shows that the amounts paid by customers to the dancers were not voluntary. Specifically, the Clubs had a minimum fee of $20.00 for dances (***see*** finding of fact 23). Additionally, customers were required to pay a fee to procure a dance in a private room, a charge that varied based on the amount of time spent with the dancer (***see*** finding of fact 22). These facts are consistent with the record in ***Matter of 44th and MLB***, of which the Administrative Law Judge took notice (***see*** footnote 2). Indeed, our decision in that case expressly finds that dances cost $20.00 minimum and that private dances cost much more (***Matter of 44th and MLB*** [finding of fact 13 therein]). These findings are further corroborated by the affidavit of Ms. Dennis, a dancer at 44th's club, in

the ***Dennis*** matter (***see*** footnote 3). Additionally, as the Administrative Law Judge observed, the contracts between the Clubs and dancers refer to, and appear to distinguish between, dance fees and tips (***see*** findings of fact 10 and 24). Additionally, the contracts between petitioner Metro and the dancers refer to the purchase of private dances (***see*** finding of fact 24). Further, the affidavit of petitioner Scarfi, dated January 30, 2018, similarly distinguishes between "tips" and "dancer fees" (***see*** finding of fact 10). Finally, we note that the Administrative Law Judge rejected the testimony of petitioners' witnesses that no amount of scrip was used to purchase dances as lacking in credibility. Although we are not bound by an administrative law judge's credibility assessment, we find nothing in this record to alter it (***Matter of Strachan***, Tax Appeals Tribunal, June 28, 2018). Accordingly, as we found in ***Matter of 44th and MLB***, some customers may well have paid dancers an amount greater than the set price for a dance and such excess amount could be deemed a voluntary gratuity not subject to tax. As in ***Matter of 44th and MLB***, however, there is no evidence in the record of the amount of such payments (***see*** finding of fact 28). Hence, given the presumption of taxability under Tax Law § 1132 (c) (1), we must consider all scrip payments by customers to the dancers as charges subject to tax under Tax Law §1105 (f) (***see also Matter of HDV Manhattan, LLC v Tax Appeals Trib. of the State of N.Y.***, 156 AD3d at 966).

Petitioners also argue that certain FLSA and Labor Law provisions require a finding that the scrip payments to the dancers, even if mandatory, must be treated as gratuities. Specifically, petitioners assert that, where, as here, the dancers are employees who retain the payments made by customers; the customers reasonably believe such payments will be retained by the dancers; and such payments are not included in the employer's gross receipts, then the scrip payments must be presumed to be gratuities under the FLSA and Labor Law. In support of this argument,

petitioners cite, among other cases, ***Hart v Rick's Cabaret Intl. Inc.*** (60 F Supp 3d 447 [SDNY 2014]), a case involving alleged violations of New York Labor Law and the FLSA, where the court found that scrip payments made by customers to dancers in an adult entertainment club should be seen as "gratuities belonging to the dancer, not as service charges belonging to the Club" (60 F Supp 3d at 457). Petitioners note that the scrip payments to the dancers here did not become part of their gross receipts and assert, accordingly, that such payments, even if mandatory, must be treated as nontaxable gratuities. Petitioners also note that Labor Law § 196-d prohibits employers from demanding, accepting or retaining, directly or indirectly, any part of an employee's gratuity or any charge purported to be a gratuity. Petitioners further contend that amounts paid directly to an employee are properly presumed to be gratuities under Labor Law regulations (***see*** 12 NYCRR 146-2.18).

Petitioners' argument is similar to that advanced by petitioners in ***Matter of 44th and MLB*** and rejected in our decision in that matter. We similarly reject petitioners' argument here. As we observed in ***Matter of 44th and MLB***, the Tax Law, and not the Labor Law or the FLSA, determines whether payments for dances are subject to sales tax. The taxability of such transactions is thus not contingent on whether the dancers are employees or independent contractors (***e.g. Matter of HDV Manhattan, LLC*** [dancers were independent contractors], ***Matter of 677 New Loudon Corp., d/b/a Nite Moves***, Tax Appeals Tribunal, August 25, 2016 [dancers were employees]). Moreover, petitioners' argument wrongly focuses on the treatment of the customer's payment after the transaction. As the sales tax is a transaction tax, liability occurs at the time of the transaction (20 NYCRR 525.2 [a] [2]). Persons required to collect sales tax must do so at the time of purchase (Tax Law § 1132 [a] [1]). Furthermore, the tax is payable, in the first instance, by the customer, and is in addition to the charge to which it applies (20

NYCRR 525.2 [a] [4]; Tax Law § 1132 [a] [1]). As noted, we have held that sales tax is collectable on similar scrip sales at the time the customer purchases the scrip (***Matter of Executive Club, LLC confirmed sub nom Gans v New York State Tax Appeals Trib.***). Petitioners here, like the petitioners in ***Matter of 44th and MLB***, simply failed to charge and collect sales tax from their customers at the time of the transactions. Accordingly, whether customer payments to the dancers are deemed gratuities for labor law purposes does not determine whether those transactions are subject to sales tax.

Petitioners' argument on this point also fails on the facts, as the record shows that the dancers did not retain the full amount spent by the customers to purchase dances. Metro's share was a 20% surcharge on the customer's purchase and a 10% (or 20% [***see*** finding of fact 12]) charge on the dancer's redemption. Metro thus received about 25% of amounts spent by customers to purchase dances via scrip.

Petitioners also echo arguments raised in ***Matter of 44th and MLB*** by their contention that sales of scrip are taxable only in a club that offers exotic dancing for profit or when the scrip is used to pay for a private dance at such a club. As discussed in that previous case, the taxability of the scrip transactions turns on whether such receipts are properly deemed amusement charges under Tax Law § 1105 (f) (1) and (3). Taxability does not turn on whether the recipient of the charge turns a profit on the sale of exotic dances. Even if petitioners' argument had merit, it is undermined by the facts. As noted, Metro retained about 25% of all scrip revenue and thus plainly sold scrip for profit (***see Matter of 44th and MLB*** [the Clubs derived significant economic benefit from scrip sales]).

Metro's liability

Having determined that the scrip sales were subject to sales tax, we now consider

whether Metro was a person required to collect such tax. As relevant here, Tax Law § 1131 (1) defines such persons as including "every recipient of amusement charges." As noted, scrip sales are taxable as amusement charges pursuant to Tax Law § 1105 (f). A recipient for purposes of Tax Law § 1105 (f) is "[a]ny person who collects or receives or is under a duty to collect an amusement charge" (Tax Law § 1101 [d] [11]). Pursuant to its agreements with the Clubs, Metro was responsible for all aspects of the scrip transactions in the Clubs throughout the period at issue. Metro provided and maintained credit card machines dedicated to scrip purchases on the premises of each Club. All scrip purchases were processed on Metro's machines. Metro received about 25% of customer expenditures on scrip. All such revenue was deposited in accounts controlled by Metro. Metro was also responsible to supply the Clubs with an adequate supply of scrip and sufficient cash for the redemption of scrip by dancers. Metro thus clearly collected or received customer payments by credit card in exchange for scrip. Accordingly, Metro was a recipient of amusement charges and a person required to collect tax under Tax Law § 1131 (1) and is therefore liable for the tax on scrip sales under Tax Law § 1133 (a).

The facts noted above showing that Metro was a recipient of amusement charges are substantially similar to the facts as set forth in the complaint brought by petitioners in their declaratory judgment action against the Division (***see Metro Enters. Corp. v New York State Dept. of Taxation & Fin.*** (171 AD3d 1377 [3d Dept 2019] affirming Sup Ct, Albany County, August 29, 2017, Weinstein, J., Index No. 901347-17). After noting their acceptance of the facts as true for purposes of the declaratory judgment action, the Appellate Division found that Metro "may be deemed a 'recipient of amusement charges' required to collect sales tax" (171 AD3d at 1380).

As petitioners observe, the Appellate Division also found "myriad questions of fact

regarding the relationship between plaintiffs [i.e., petitioners], the dancers and the registered clubs (***id.***). Accordingly, the court was "unable to conclude whether or to what extent plaintiffs' [i.e., petitioners'] receipts are taxable" and determined, therefore, that plaintiffs had failed to exhaust their administrative remedies and thus affirmed the Supreme Court's dismissal of the declaratory judgment action on that basis (***id.***). To the extent that the Appellate Division's decision in ***Metro Enters. Corp. v New York State Dept. of Taxation & Fin.*** requires an examination of the relationships among Metro, the Clubs and the dancers, we observe that those relationships were the focal point of the hearing and indeed the entire record in this matter. As discussed above, we find that the record shows that Metro was a recipient of amusement charges and therefore a person required to collect and pay over sales tax on the scrip transactions.[8]

As to Metro's liability for the non-scrip sales, there is evidence in the record indicating that Metro and the Clubs jointly operated those businesses. Metro was primarily responsible for the scrip transactions, as discussed. Those transactions appear to have generated more revenue than any other part of the Clubs' operations (***see*** finding of fact 40). Metro used Club employees to carry out that responsibility and appears to have paid them (***see*** findings of fact 17 through 20). Metro was responsible for the referral of dancers to the Clubs and was involved in the scheduling of those dancers (***see*** findings of fact 10 and 15). The dancers were plainly integral to the Clubs' operation. Metro also made several significant payments to the Clubs (***see*** finding of fact 21). Mr. Capeci, the owner of 44th and MLB, had check-signing authority for some Metro bank accounts and exercised that authority (***see*** finding of fact 43). Mr. Scarfi had check signing

[8] In ***Matter of 44th and MLB***, we determined that 44th and MLB were liable on some of the same scrip sales as are at issue in the present matter. Such liability does not impact Metro's liability in the present matter, however, because liability for sales tax is joint and several (***see Matter of Marchello***; Tax Law §§ 1131 [1] and 1133 [a]).

authority for 44th and MLB. The Clubs and Metro used each other's credit card terminals (***see*** finding of fact 13). On this point, we note that the Administrative Law Judge rejected the testimony of Mr. Scarfi and Mr. Capeci regarding the "swapping out" of credit card terminals as having occurred at one club for a brief period as vague, evasive and unconvincing. We defer to this characterization. Additionally, we note that the Clubs' managers maintained records of scrip transaction on Metro's behalf (***see Matter of 44th and MLB*** [finding of fact 15 therein]).

Such evidence provides a rational basis to conclude that Metro and the Clubs operated the adult entertainment establishments jointly and thus provides a rational basis to conclude that Metro was a vendor with respect to the Clubs' non-scrip sales (***Matter of Khan***, Tax Appeals Tribunal, September 4, 2008 ["a determination of tax must have a rational basis in order to be sustained upon review"] citing ***Matter of Grecian Sq. v New York State Tax Commn.***, 119 Ad2d 948, 950 [3d Dept 1986]).

Petitioners offer little evidence and no legal argument against a finding of liability against Metro for non-scrip sales. Petitioners have thus failed to overcome the presumption of correctness attaching to the statutory notices at issue (***Matter of Hammerman***, Tax Appeals Tribunal, August 17, 1995).

We note that petitioners have not contested the reasonableness of the Division's audit methodology or the accuracy of the resulting audit calculations. Accordingly, we must sustain such calculations (***see e.g. Matter of West Grenville Liqs., Inc.***, Tax Appeals Tribunal, May 9, 1996). We note, too, that the scrip sales assessment is premised on a detailed audit of Metro's bank records. As to the estimated audit method for non-scrip sales, the record shows that the records made available were incomplete, thereby justifying the use of an indirect audit method (***see e.g. Matter of Aum Sidhdhy Vinayak, LLC***, Tax Appeals Tribunal, December 8, 2011; ***see***

also Tax Law § 1138 [a] [1]).

Petitioners do not contest Mr. Scarfi's status as a person responsible to collect sales tax on behalf of Metro pursuant to Tax Law § 1131 (1). Accordingly, the notice of determination asserting liability against him personally for such tax in accordance with Tax Law § 1133 (a) is sustained.

Estoppel and SAPA

Petitioners' estoppel argument is similar to that advanced by the petitioners in ***Matter of 44th and MLB*** and is similarly rejected. "[T]he doctrine of estoppel does not apply in tax cases unless 'unusual circumstances support a finding of manifest injustice'" (***Matter of Ryan v Tax Appeals Trib. of the State of N.Y.***, 133 AD3d 929, 930 [3d Dept 2015] [internal quotation marks and citations omitted]). It is well-established that "previous assessments and audits are non-binding upon future years" (***Matter of Winners Garage, Inc.***, Tax Appeals Tribunal, April 16, 2014, ***confirmed sub nom Matter of Wolkowicki v New York State Tax Appeals Trib.***, 136 AD3d 1223 [3d Dept 2016]). This follows from the general proposition that an administrative agency may correct its erroneous interpretations of the law (***Matter of Liberty Coaches v State Tax Commn.***, 79 AD2d 775, 776 [3d Dept 1980]). Accordingly, a taxpayer's reliance on the result of a prior audit does not rise to the level of manifest injustice (***Matter of Washington Sq. Hotel LLC v Tax Appeals Trib. of the State of N.Y.***, 155 AD3d 1477, 1479 [3d Dept 2017], ***lv denied*** 31 NY3d 909 [2018]). It is also well-established that "'erroneous advice given by an employee of a governmental agency is not considered to rise to the level of an unusual circumstance' warranting invocation of the doctrine of estoppel" (***Matter of Winners Garage Inc. v Tax Appeals Trib. of the State of N.Y.***, 89 AD3d 1166, 1169 [3d Dept 2011], ***lv denied*** 18 NY3d 807 [2012] [internal quotation marks and citation omitted]). It follows, therefore, that the

outcome of previous audits of other adult entertainment businesses (***see*** finding of fact 51) or statements made by Division auditors during the course of dealings with other adult entertainment businesses (***see*** findings of fact 50 and 52) are insufficient to estop the Division in the present matter.

We also reject petitioners' contention that the Division improperly adopted a policy that all scrip transactions in adult entertainment clubs are taxable in violation of the State Administrative Procedure Act. As in ***Matter of 44th and MLB***, we agree with the Administrative Law Judge's finding that the Division did not have such a policy and made its determinations with respect to scrip transactions on a case-by-case basis.

Constitutional Arguments

Petitioners' argument that the assessments violate their due process rights by imposing conflicting legal obligations upon Metro and their business associates (i.e., the Clubs), thereby making it impossible for them to simultaneously comply with both the Tax Law and the relevant labor laws is similar to the argument advanced by the petitioners in ***Matter of 44th and MLB***. As in that case, this is a question of whether a statute as applied to a specific set of facts is constitutional and is within our jurisdiction (***Matter of Frog Design, Inc.***, Tax Appeals Tribunal, April 15, 2015; ***cf. Matter of A & A Serv. Sta., Inc.***, Tax Appeals Tribunal, October 15, 2009 [the constitutionality of a statute by its terms is presumed at the administrative level]). Petitioners bear the burden to prove their as-applied constitutional challenge (***Matter of Brussel***, Tax Appeals Tribunal, June 25, 1992). According to petitioners, compliance with both the Tax Law and the relevant labor laws is impossible because the same monies that are considered gratuities belonging to the dancers for labor law purposes are also taxable charges under the Tax Law. We rejected this argument in ***Matter of 44th and MLB*** and we reject it here. As we found

in ***44th and MLB***, even if we assume that amounts paid to the dancers were gratuities for labor law purposes, the Club operators' compliance with the Tax Law with respect to scrip sales was plainly not impossible. As we observed in ***44th and MLB***, this is because sales tax is collectible, in the first instance, from the customer at the time of the transaction and is in addition to the amusement charge to which it applies (20 NYCRR 525.2 [a] [4]; Tax Law § 1132 [a] [1]). We found in ***44th and MLB*** that the Club operators could have complied by simply charging and collecting sales tax from their customers at the time of the transactions. The same reasoning applies to petitioners here.

We note, too, that petitioners' constitutional argument here is further undermined by the fact that, in contrast to the club operators in ***44th and MLB***, petitioner Metro does not employ the dancers. Hence, Metro has no labor law obligations to the dancers and thus no simultaneous compliance problem.

Penalties

The notices of determination remaining at issue impose penalties against petitioners pursuant to Tax Law § 1145 (a) (1) (i) and (vi). Abatement of such penalties requires a showing of reasonable cause and an absence of willful neglect. Petitioners have not articulated an argument in support of abatement. Accordingly, we sustain the imposition of penalties.

Procedural claims

We agree with the Administrative Law Judge's rejection of the various claimed "irregularities in the proceedings [that] undermine the validity of the assessments."

Petitioners' complaint that the Division refused to conference with petitioners' representative for purpose of stipulation and that petitioners were thus prejudiced by their inability to proffer stipulated facts is meritless. Our Rules of Practice and Procedure provide for

a motion to compel stipulation if, as petitioners claim here, "a party has refused or failed to confer with his or her adversary with respect to entering into a stipulation" (20 NYCRR 3000.11 [f] [1]). Such a motion requires the movant to include a proposed stipulation of facts with its motion papers. (***id.***). Petitioners did not avail themselves of this procedure. Indeed, petitioners apparently did not, at any point in this proceeding, submit a proposed stipulation to the Division. Any negative consequence to petitioners resulting from the lack of stipulated facts in the record is thus self-inflicted.

The Administrative Law Judge correctly determined that the Division properly objected to and denied requested admissions in accordance with our Rules of Practice and Procedure as such requested admissions were in substantial dispute or not within the Division's knowledge (***see*** 20 NYCRR 3000.6 [b]).

Petitioners' complaint that the Division misrepresented Mr. Capeci's status as a non-party witness at the hearing is baseless. This is, in fact, an accurate statement of Mr. Capeci's status in the present matter.

Petitioners' complaint that the Division improperly questioned witnesses about documents that were not in its hearing memorandum is also baseless. As the Administrative Law Judge noted, the transcript shows that two items that were not offered in evidence were shown to a witness to refresh her recollection. "A witness may refresh his or her recollection by the use of anything whatsoever, 'provided it actually serves that purpose'" (***People v Neff***, 287 AD2d 809, 810 [3d Dept 2001] quoting ***People v Betts***, 272 App Div 737, 741 [1st Dept 1947], ***affd*** 297 NY 1000 [1948]).

The Administrative Law Judge correctly rejected as unsupported by the record petitioners' complaint that the Division's representative offered improper closing argument at the hearing regarding facts that were either not in evidence or disproved by the evidence.

The Administrative Law Judge's January 2, 2020 order properly denied petitioners' motion to recuse the Division's representative in the present matter. As in their motion, petitioners continue to argue on exception that Mr. Jack should be disqualified because he became an essential fact witness in this case because when he submitted a declaration dated July 26, 2019, in connection with federal litigation involving MLB and the Division. The hearing in this matter was held and the record was closed on July 15, 2019. Mr. Jack was not called as a witness and did not testify at the hearing. Mr. Jack cannot be an essential fact witness in a proceeding in which he did not testify and in which the record has been closed.

We agree with the Administrative Law Judge's September 24, 2020 order denying petitioners' motion to consolidate the present matter with ***Matter of 44th and MLB*** and ***Matter of Capeci***. Petitioners' motion was received by the Division of Tax Appeals on February 20, 2020. At that point, separate hearings had been held and completed and thus separate records had been made in the present matter and in ***Matter of 44th and MLB***. Hence, any benefit of economizing legal and administrative efforts that might have been achieved by consolidation was largely lost at that point. In any event, as the Administrative Law Judge noted, petitioners' motion papers provide no evidence to show that the other parties supported or joined in the request. Indeed, the motion papers do not indicate that the other parties were even given notice of the motion. Finally, at this point in time, with separate hearings having been held and completed in all three of these matters, petitioners' motion is moot (***see*** CPLR 602 [*pending* actions subject to consolidation]).

Post-exception motion

Petitioners' post-exception motion to this Tribunal is improper under our Rules of Practice and Procedure. As noted, petitioners filed this motion on May 17, 2022, some four months after they filed their reply brief on exception. The post-exception motion requests that we remand this matter to the Administrative Law Judge to consider "newly discovered" evidence consisting of certain documents. Petitioners thus seek to reopen the evidentiary record. While our Rules do provide for a motion to reopen the record upon the grounds of newly discovered evidence, such a motion must be made to the Administrative Law Judge within 30 days of the issuance of the determination and may not be granted after the filing of an exception with the Tribunal (20 NYCRR 3000.16). Petitioners' motion fails on both such conditions. Additionally, newly discovered evidence for purposes of such a motion means evidence that was in existence but undiscoverable with due diligence at the time of the hearing (***Matter of Frenette***, Tax Appeals Tribunal, February 1, 2001, citing ***Matter of Commercial Structures v City of Syracuse***, 97 AD2d 965, 966 [4th Dept 1983]). Petitioners' motion papers state that the evidence in question did not exist at the time of the hearing.

Accordingly, it is ORDERED ADJUDGED and DECREED that:

1. The exception of John Scarfi and Metro Enterprises, Corp. is denied;

2. The motion of John Scarfi and Metro Enterprises, Corp. is denied;

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

4. The orders of the Administrative Law Judge, dated January 20, 2020 and September 24, 2020, are affirmed;

5. The petition of John Scarfi is granted to the extent indicated in the determination of the Administrative Law Judge, but is otherwise denied;

6. The petition of Metro Enterprises, Corp. is denied; and

7. Notices of determination L-045794061 and L-045796581 (***see*** findings of fact 41 and 42) 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