

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petitions	:	
of	:	
<b>CORAM DINER CORP.</b>	:	DETERMINATION
<b>AND</b>	:	DTA NOS. 824918
<b>KOSTAS HIONAS</b>	:	AND 824919
for Revision of Determinations or for Refund	:	
of Sales and Use Taxes under Articles 28 and 29	:	
of the Tax Law for the Period December 1, 2005	:	
through August 31, 2008.	:	

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Petitioners, Coram Diner Corp. and Kostas Hionas, filed petitions for revision of determinations or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period December 1, 2005 through August 31, 2008.

A hearing was held before Dennis M. Galliher, Administrative Law Judge, at the offices of the Division of Tax Appeals, Agency Building One, Empire State Plaza, Albany, New York, on December 3, 2012, at 10:30 A.M., with all briefs to be submitted by April 30, 2013, which date commenced the six-month period for the issuance of this determination. Petitioners appeared by Buxbaum Sales Tax Consulting, LLC (Michael Buxbaum, CPA). The Division of Taxation appeared by Amanda Hiller, Esq. (Michael B. Infantino, Esq.).

***ISSUES***

I. Whether the Division of Taxation clearly requested and, in turn, received from the corporate petitioner books and records that were sufficient for the conduct of a direct audit.

II. Whether, if not, petitioners have established that the indirect audit methodology utilized by the Division of Taxation was not reasonably calculated to reflect the correct amount of tax due, or that there were errors made in the application of such audit methodology.

III. Whether petitioner Kostas Hionas was properly subjected to liability as a person under the obligation to collect and remit sales and use taxes on behalf of the corporate petitioner Coram Diner Corp.

IV. Whether petitioners have established any bases justifying reduction or cancellation of the penalties assessed.

#### ***FINDINGS OF FACT***

1. Petitioner Coram Diner Corp. (Coram Diner) operates a diner style restaurant located in Coram, New York. Coram Diner's premises consist of a one-story establishment and include a main dining room with 9 booths and 6 stools, a second dining room with 10 booths and 58 seats and a third dining room with 6 booths, 5 tables and 20 seats. Its total capacity is 161 persons. Coram Diner is open five days per week from 6:00 A.M. until 2:00 A.M., and is open 24 hours on Fridays and Saturdays.

2. Petitioner Kostas Hionas is the owner of the Coram Diner. He immigrated to the United States from Greece in 1979 and worked at various positions at the Coram Diner until he purchased the business in 1999. At the hearing, Mr. Hionas conceded and does not dispute that during the period at issue he was the person responsible to collect, account for and pay over sales and use taxes on behalf of the Coram Diner pursuant to Tax Law § 1131(1) and § 1133(a).

3. Since the assessment at issue results from the application of an indirect audit methodology by the Division of Taxation (Division), and since petitioners challenge the adequacy of the Division's request for and review of Coram Diner's records prior to proceeding

via such methodology, it is necessary to review in close detail the events that occurred during the course of the conduct of the subject audit.

4. On November 20, 2008, the Division mailed a letter to the corporate petitioner scheduling a field audit pertaining to Coram Diner's sales and use tax liability for the period December 1, 2005 through August 31, 2008. This audit was a follow-up audit to two previous audits of Coram Diner, including an audit covering the immediately preceding period spanning March 1, 2003 through November 30, 2005. This earlier audit resulted in an adjustment increasing Coram Diner's reported gross sales and a finding of additional tax due in the amount of \$257,911.72.

5. The audit for the period in issue (December 1, 2005 through August 31, 2008) was to commence with a field visit by the Division's auditor on December 3, 2008. The November 20, 2008 audit appointment letter issued to petitioners by the Division stated that "[a]ll books and records pertaining to the sales and use tax liability, for the audit period, must be available on the appointment date." Accompanying this audit appointment letter was a Records Requested List, further specifying the records required to be made available for review as including, among other items, sales tax returns, worksheets, canceled checks, federal income tax returns, New York State corporation tax returns, general ledger, general journal and closing entries, sales invoices, exemption documents, chart of accounts, fixed asset purchase and sale invoices, expense purchase invoices, bank statements, depreciation schedules, lease contracts, utility bills, guest checks and cash register tapes. A note at the foot of the Records Requested List states, in bold-faced type, that any of the above-requested items "may be submitted in electronic format, if available, and this may facilitate the audit process."

6. On December 2, 2008, the Division received a power of attorney appointing Steven Kohilakis, who was Coram Diner's accountant, as its representative for the audit. The initial audit appointment date of December 3, 2008 was subsequently rescheduled, at Mr. Kohilakis's request, to take place at Mr. Kohilakis's offices on December 22, 2008. At this appointment, the Division's auditor was provided with bank statements pertaining to one of Coram Diner's bank accounts (Bank of NY) and some "daily sheets." In turn, the auditor commenced her review of these items.

7. The auditor returned to Mr. Kohilakis's offices on January 15, 2009 and resumed her review of the foregoing bank statements and daily sheets. The auditor was advised that Coram Diner had installed a Versitouch point-of-sale (POS) computerized record-keeping system in September 2005, i.e., very shortly before the beginning of the audit period. During the January 15, 2009 appointment, the auditor "discussed POS system with [Mr. Kohilakis] and he indicated we may be able to obtain the records electronically and stated he would discuss this request with Mr. Hionas . . . ."

8. By a March 5, 2009 letter addressed to Mr. Kohilakis, the auditor requested the computerized files from Coram Diner's POS system, as follows:

Please send me a copy of the RCS and Win32 directories for the audit period . . . from Coram Diner Corporation's computerized register. If you require assistance with this process our IT department can assist you either by phone or in person. We will then extract the data necessary thereby expediting the audit process.<sup>1</sup>

Petitioner Kostas Hionas responded to this letter by a telephone call on March 24, 2009, advising the auditor that the requested files would be provided via flash drive by March 25, 2009.

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<sup>1</sup> The RCS and Win32 directories were described as the files necessary to read and extract the information that resides on Coram Diner's Versitouch POS system hard drive and, presumably, on any copy thereof such as a flash drive or portable hard drive.

9. A power of attorney authorizing petitioners' current representative, Buxbaum Sales Tax Consulting, LLC, to appear on petitioners' behalf was filed with the Division on April 20, 2009. In turn, a June 2, 2009 letter from the auditor to petitioners' newly appointed representative confirmed that an audit appointment was scheduled for June 19, 2009 "at your client's office."<sup>2</sup> A Records Requested List identical to that appended to the initial (November 20, 2008) audit appointment letter was attached, as was a copy of the March 5, 2009 letter specifically requesting the RCS and Win32 directories. Testimony at hearing by petitioner Kostas Hionas also noted that a new accountant, Nick Mastrogiannis, CPA, had been hired for Coram Diner in replacement of Mr. Kohilakis.

10. By a letter from petitioners' representative dated June 10, 2009, the foregoing June 19, 2009 audit appointment was canceled, with a request that the same be rescheduled for July 1 or July 8, 2009 to take place at petitioners' representative's office. In turn, the auditor issued a letter to petitioners' representative, dated July 13, 2009, confirming that the audit appointment had been rescheduled for July 24, 2009 and would, as requested, take place at petitioners' representative's office. Again, a copy of the Records Requested List was attached to the auditor's letter. In addition, the auditor's log of "Contacts and Comments of All Audit Actions" (Audit Log) maintained as part of the auditor's Field Audit Record notes that a July 17, 2009 telephone call was received from petitioners' representative advising that "[he] will be sending federal returns, daily sheets, and other records. Per phone conversation computerized records requested will not be forthcoming."

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<sup>2</sup> In context, the phrase "at your client's office" would appear to mean at Coram Diner's premises.

11. By a letter dated July 23, 2009, petitioners' representative submitted Coram Diner's federal income tax returns for the years 2006 and 2007 and daily sales sheets for the month of January 2008. This letter notes that the July 24, 2009 audit appointment has been postponed and requests that the auditor contact petitioners' representative after reviewing the submitted returns and daily sheets (daily shift sales reports for January 2008). As requested, the auditor reviewed Coram Diner's federal income tax returns versus its sales tax returns for the years 2006 and 2007, finding that its sales tax returns for the period covering 2006 reported some \$225,144.00 more in gross sales than did its federal returns for 2006 (\$1,107,903.00 versus \$882,759.00), while such returns were in near agreement for the year 2007.<sup>3</sup>

12. By a letter dated September 3, 2009, the auditor summarized the foregoing audit activities and attempts to schedule appointments and obtain records. This letter also provides, with respect to a telephone call between the auditor and petitioners' representative, as follows:

You [petitioners' representative] indicated that the books and records would be sent to this office for my review. I indicated to you that we expect all of the items listed on the Records Requested List be furnished at this time including the 2 directories for the Versitouch Point of Sales system. You indicated that we would not be receiving the electronic data. We are in receipt of the information you sent on July 23, 2009: the Federal Income Tax Returns for 2006 & 2007 and Daily Shift Sales Reports for January 2008. This information is insufficient to complete the sales tax audit of this company.

Please clarify if the data from the Versitouch Point of Sales system exists as well as the other items listed on the enclosed records requested list. If the data does exist, please provide the basis for not providing it. Also, explain why the records requested have not been provided to this office to date.

This letter requested a response by September 19, 2009.

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<sup>3</sup> For 2007, the comparison revealed a difference of \$864.00 (sales tax returns [\$1,368,192.00] versus federal income tax returns [\$1,369,056.00]). No reason other than "accounting error" was provided in explanation of the difference for the year 2006.

13. Petitioners' representative responded to the foregoing correspondence via a letter dated September 15, 2009, citing therein (and quoting from) Tax Law § 1138(a)(1) and *Matter of Basileo* (Tax Appeals Tribunal, May 9, 1991), and requesting that the auditor provide any workpapers created with regard to the subject audit. The purpose for citing and quoting the noted materials, pertaining to the Division's statutory authority to determine tax due via indirect audit methods (including the use of external indices) and its obligation to provide information with respect to the method of audit utilized, was not specified in this letter.

14. By a letter dated November 12, 2009, the auditor responded to the foregoing correspondence, noting that the Division was still attempting to obtain Coram Diner's records in order to review the same. This letter further provided:

While we are not opposed to meeting with you at your office, we first must insist that you answer the following questions, prior to our scheduling any such meeting.

- 1) Does the flash drive containing the point of sales files which Mr. Hionas promised us in his March 24 phone call still exist?
- 2) If it does still exist, will either you or Mr. Hionas be providing this information?
- 3) If so, then *when* will you be providing this information?
- 4) If it does not still exist, then what happened to it?

This November 12, 2009 letter goes on to note that in addition to the foregoing (electronic) point of sales files questions, the Records Requested List had been sent on six separate dates, but that the requested records and information had not been provided.<sup>4</sup> The letter again included the Records Requested List, in a columnar "check off" format such that the existence and availability

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<sup>4</sup> The dates specified are 11/20/08, 03/05/09, 06/02/09, 06/26/09, 07/13/09 and 09/03/09. The 09/03/09 letter is a request for records with an attached Records Requested List, captioned Second Request, and is to be distinguished from the letter, also dated September 3, 2009, referenced and described in Finding of Fact 12.

of each of the records requested (listed in column one) could be in turn confirmed (by check mark in the two adjoining columns). A response to this letter was requested by December 1, 2009.

15. Petitioner's representative responded by a letter dated November 20, 2009, stating that there would be no "'inventory' of records that may be available for inspection and no further communication absent a contact to schedule a field appointment or a teleconference."

16. The auditor's Field Audit Record and audit log includes an entry for December 1, 2009, as follows:

received a call from Nick Mastrogiannis, he indicated that he would be representing Coram Diner and that the computerized records would be made available. He stated we were welcome to go the place of business and extract what was needed. I told him Win32 and RCS directories are needed. N. Mastrogiannis stated that a poa was forthcoming and I requested he complete the questions we had regarding the availability of records.

In response to this telephone contact, the auditor sent a letter dated January 5, 2010 to petitioners' representative advising of the foregoing telephone call and its content, and offering an opportunity to petitioners' representative to accompany the auditor to Coram Diner's premises when the data extract would take place.

17. A letter from petitioners' representative dated January 5, 2010, as well as entries in the audit log, clarify that Mr. Mastrogiannis was not serving as petitioners' representative or acting on behalf of petitioners' representative. The January 5, 2010 letter also asks that petitioners' representative be advised when the auditor would be at Coram Diner's premises for the data extract, confirms that such representative would not be attending any such meeting, and requests any "current work papers."

18. On January 25, 2010, Mr. Mastrogiannis arrived at the auditor's office and delivered a flash drive allegedly containing the information from Coram Diner's Versitouch point of sale

system. Entries in the audit log confirm that the flash drive was scanned for viruses, the data therein was copied (in read only format), and that Mr. Mastrogiannis advised the auditor as follows:

- a) that he did not know the date on which the data had been extracted from the Versitouch hard drive at Coram Diner's premises;
- b) that the Versitouch system has been in place for the entire audit period and that all data "should be" on the flash drive;
- c) that he did not know the size of the hard drive, whether the "audit trail" was on or off, if the guest checks were in sequential order and if there were any controls on the guest checks;
- d) that he was unsure of the number of terminals (registers) tied to the system and if there were any offline terminals;
- e) that he did not know the contents of the flash drive or if the same was password protected; and
- f) that he was Coram Diner's new accountant but that he would not be assisting on the audit.

The flash drive was returned to Mr. Mastrogiannis after being copied.

19. The auditor reviewed in detail the data contained on the flash drive. By this review, the auditor found multiple gaps in internal sequence numbers, as well as gaps in time segments where complete meal times (i.e., times when the Coram Diner was open) had no information as to any sales having been made. Further, a comparison of sales information found on the flash drive for the date October 6, 2006 was made to the information recorded during a daylong observation and recording of sales conducted by the Division on the same October 6, 2006 date as part of its prior audit of Coram Diner (*see* Finding of Fact 4). While some 295 guest checks were generated on October 6, 2006 (as recorded per the Division's observation on that date), the flash drive only reflected 14 guest checks for that date. Gross sales (as observed) totaled

\$5,072.34 (including tax and tips) while gross sales per the flash drive totaled only \$260.96. Further, for the current audit period, while the directory of credit card sales per the flash drive showed \$2,367,606.67 in customer sales paid by credit card, the flash drive summary of guest checks paid by credit card totaled only \$782,685.82. The auditor also noted that in contrast to the 27.09 percent credit card to cash sales ratio observed on October 6, 2006 (*see* Finding of Fact 22), the flash drive directory information reflected that credit card sales (\$2,367,606.67) represented approximately 65 percent of total reported taxable sales (\$3,623,061.00), and that net credit card sales (\$1,969,717.97) represented approximately 54 percent of total reported taxable sales (\$3,623,061.00). In view of these discrepancies, the auditor concluded that the information on the flash drive was incomplete, inadequate and unreliable.

20. By a letter dated June 14, 2010 (denominated a “Third Attempt”), the auditor requested that Coram Diner supply its records for review, again specifying therein via an attached list the records required to be provided.

21. In turn, and having received virtually none of the records requested, the auditor proceeded to determine Coram Diner’s sales tax liability by resort to indirect auditing. Specifically, subpoenas for Coram Diner’s bank statements were issued on October 6, 2010 by the auditor to the banks with whom Coram maintained accounts (Capital One North American Bank [f/k/a North Fork Bank] and JP Morgan Chase Bank of North America). In response, the two banks provided the subpoenaed statements on November 29, 2010.

22. Review of the bank statements, directly and in comparison to the flash drive information, revealed that direct bank deposits from Coram Diner’s credit card sales (\$2,367,606.67) was, as above, \$1,584,920.85 greater than the guest check summary amount of credit card sales per the flash drive (\$782,685.82). Further, the amount of credit card sales per

the bank statements (\$2,367,606.67) represented approximately 77.25 percent of Coram Diner's total bank deposits of \$3,064,804.92 (i.e., credit card deposits [\$2,367,606.67] plus cash deposits [\$697,198.25]). In contrast, such 77.25 percent ratio of credit card sales to cash sales was significantly higher than the 27.09 percent ratio calculated based on the Division's October 6, 2006 observation (*see* Finding of Fact 19), and was significantly higher than the ratio (approximately 30% credit card sales versus 70% cash sales) the auditor testified that she would expect to find based on her experiences in auditing approximately 50 diners located on Long Island over some 31 years of conducting such audits. Further, cash deposits per bank statements (\$697,198.25) represented 29.45 percent of Coram Diner's total bank deposits of \$3,064,804.92. By comparison, cash sales (\$408,469.93) plus guest check credit sales (\$782,685.82) per the flash drive, totaling \$1,291,155.75, represented only 42.13 percent of total bank deposits per bank statements (\$3,064,804.92). Finally, and in comparison, cash sales per the flash drive information (\$408,469.93) represented only 58.59 percent of cash deposits per bank statements (\$697,198.25), and guest check credit sales per the flash drive information (\$782,685.82) represented only 33.06 percent of credit card deposits per bank statements (\$2,367,606.67).

23. To arrive at a calculation of additional tax liability, the auditor first reduced total credit card sales per bank statements (\$2,367,606.67) by tips included therein (based on a 9.63 tip percentage computed per the October 6, 2006 audit observation results), and reduced the resulting amount further by sales tax included therein (8.624%) to arrive at net credit card sales in the amount of \$1,969,717.97. The auditor then applied the 27.09 percent October 6, 2006 observed ratio of credit card sales versus cash sales to such net credit card sales amount

(\$1,969,717,97) to arrive at audited taxable sales of \$7,271,015.03.<sup>5</sup> Audited taxable sales were reduced by reported taxable sales (\$3,623,061.00 per sales tax returns), resulting in additional taxable sales of \$3,647,954.03 with additional tax due thereon in the amount of \$314,636.04.

24. By a letter dated January 19, 2011, the foregoing computations and supporting workpapers were sent to petitioners' representative. The same information was again sent to petitioners' representative on February 1, 2011. Thereafter, in a letter to petitioner's representative dated March 7, 2011, the auditor specified, by list, those records requested but not supplied, and also detailed that the only records that had been provided by petitioners were:

- Versitouch Shift Sales Reports for October 6, 2006 and for the period January 1, 2008 through January 31, 2008;
- Versitouch Tickets with pay information for October 6, 2008;
- federal income tax returns for 2006 and 2007;
- flash drive containing electronic Versitouch data. (*see* Finding of Fact 19)<sup>6</sup>

This letter also notes that despite repeated requests for records, including specifically guest checks in either paper or electronic format, the same had never been provided. The letter describes the method by which the auditor computed additional tax due (*see* Finding of Fact 23), and closes with another request that the guest check detail for the audit period be provided together with an explanation as to why such data would differ from that supplied on the flash drive previously submitted.

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<sup>5</sup> By the auditor's calculation, cash sales (72.01% of all sales) totaled \$5,301,297.06.

<sup>6</sup> The letter notes that the flash drive reflected total sales of \$1,191,155.75 (cash sales of \$408,469.93 plus guest check credit card sales of \$782,685.82), while taxable sales reported by Coram Diner totaled \$3,623,061.00, and further noted that there was no guest check detail available for the \$2,431,905.25 difference between total sales per the Versitouch flash drive information and reported sales per tax returns.

25. No guest check detail or other additional records were provided by petitioners or their representative and on May 2, 2011, the Division issued a Statement of Proposed Audit Change for Sales and Use Taxes reflecting tax due as calculated above in the amount of \$314,636.03.

26. On May 26, 2011, the Division issued to petitioner Coram Diner Corp. a Notice of Determination (L-036033786-7) assessing additional sales tax due for the period December 1, 2005 through August 31, 2008 in the amount of \$314,636.03, plus interest and penalties. The auditor noted that penalties were imposed based upon the failure to provide adequate records for audit and because of underreporting of tax by more than 25%. On May 27, 2011, the Division issued to petitioner Kostas Hionas a Notice of Determination (L036067859-4) assessing the same amounts of tax, interest and penalties upon the premise that Mr. Hionas was a person responsible to collect, account for and remit taxes on behalf of Coram Diner Corp.<sup>7</sup>

27. At hearing, petitioner Kostas Hionas described how a customer's order at Coram Diner is entered into the POS system via a computer terminal, noting that there are three such terminals at the premises. The order is then transmitted to the kitchen for preparation, and paper copies of the bill for the order are generated for the customer and for Coram Diner, with the information for each such order stored on the POS hard drive. Petitioner Kostas Hionas claimed in testimony that Coram Diner's paper copies of the bills (i.e., guest checks) are retained at Coram Diner's premises. He also testified concerning customers' orders that are paid for by credit card versus orders paid for by cash, noting that sometimes the ratio was half and half, sometimes credit card sales were double cash sales, and that over the past five years payments have been mostly made by credit card.

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<sup>7</sup> A series of consents were executed by petitioners pursuant to which the period of limitations on assessment for the audit period was extended for both petitioners. Petitioners have raised no challenge concerning the timeliness of the assessments issued by the Division.

28. Petitioners also provided, at hearing, “Shift Sales Reports” and “Tickets w/Pay Info” (tickets with pay information) from the POS system for the quarterly periods spanning June 1, 2008 through August 31, 2008 and March 1, 2007 through May 31, 2007 (Exhibits 1 and 2). A shift sales report, upon which Coram Diner’s sales and use tax returns are prepared, provides a summary of total sales, net sales after discounts, taxable sales, cash sales, credit card (charge) sales and credit card tips for a given time period (a shift). In this instance petitioner provided a summary shift sales report for each of the two noted quarterly periods, and a shift sales report for each day (referred to as “daily sheets”) within such quarterly periods (Exhibit 3). The “tickets with pay information” sheets reflect seven columns carrying the headings a) Check #, b) Table, c) Server, d) Total, e) Cust. Entree, f) Open and g) Close referring, respectively, to a) guest check number<sup>8</sup>, b) table number, c) server’s name, d) total dollar amount of the check and the method of payment<sup>9</sup>, e) number of customers and number of entrees (if entrees were ordered), and the date and time the check was f) opened and g) closed. Petitioners also provided printouts from the POS system of each guest check for two dates (August 5, 2008 and May 17, 2007), together with a “shift sales report” printout and a “tickets with pay information” printout for such dates. These guest checks for the two noted dates are the only actual guest checks presented with respect to the audit period. They show the check number, table number, number of customers, server’s name, seating area and all of the items ordered and prices of such items.

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<sup>8</sup> Guest checks are not listed in sequential number, allegedly as a safeguard against theft by employees and to prevent competitors from having too much information about petitioners’ business. The POS system allegedly assigns a sequential (though internal) number to each guest check in the system.

<sup>9</sup> The “Total” portion of the document indicates, in addition to the total amount of the check, the method of payment (cash versus credit card), the amount of cash tendered (either as “exact change” or “change due” depending on the amount of cash tendered) and, in the case of payment by credit card, the amount of the tip if any (no specific information is reflected with regard to cash tips).

29. The shift sales reports for the sales tax quarterly periods spanning March 1, 2007 through May 31, 2007, and June 1, 2008 through August 31, 2008, respectively, reflect the following information:

Period	03/01/07 -05/31/07	06/01/08 - 08/31/08
Total Accountable	\$371,004.96	\$466,985.01
less: walkout (no pay)	(\$21.02)	(\$14.07)
Net Accountable	\$370,983.94	\$466,970.94
Cash Sales	\$165,783.36	\$195,961.32
Credit Card Sales	\$205,200.58	\$271,009.62
Cash Sales Percentage	44.69%	41.96%
Credit Card Sales Percentage	55.31%	58.04%

30. In contrast to the foregoing, Coram Diner's bank statements for the same two quarterly periods reveals the following amounts of cash and credit card deposits:

– For the quarterly period March 1, 2007 through May 31, 2007–

Month	Cash Deposits	Credit Card Deposits	Total
March 2007	\$17,922.00	\$64,480.60	\$82,402.60
April 2007	\$29,063.00	\$63,152.26	\$92,215.26
May 2007	\$25,983.00	\$76,863.32	\$102,846.32
Total	\$72,968.00	\$204,496.18	\$277,464.18

–For the quarterly period June 1, 2008 through August 31, 2008–

Month	Cash Deposits	Credit Card Deposits	Total
June 2008	\$30,800.00	\$94,744.76	\$125,544.76
July 2008	\$29,700.00	\$88,617.37	\$118,317.37

August 2008	\$32,123.70	\$83,887.11	\$116,010.81
Total	\$92,623.70	\$267,249.24	\$359,872.94

The credit card deposit amounts result from direct-to-bank electronic deposit of customers' purchases paid for by credit card.<sup>10</sup> The manner and frequency of Coram Diner's bank deposits of cash sales was not specified in the record.

31. As noted, petitioners also submitted shift sales reports, but not guest checks, for the month of January 2008 (*see* Finding of Fact 24). A comparison of these shift sales reports to Coram Diner's bank statements for the same period reveals approximately 53 percent of sales were credit card sales, and that cash sales per shift sales reports were approximately \$24,000.00 greater than cash bank deposits. Petitioners did note that sales per the Division's audit observation conducted on October 6, 2006 matched with sales per the POS system, as reflected on a July 29, 2010 printout of the shift sales report and tickets with pay information for the date October 6, 2006 (Exhibit 6). It is specifically noted that the ratio of credit card sales to total sales

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<sup>10</sup> The shift sales reports for the foregoing two sales tax quarterly periods also show information for what is denominated "IRS Sales," as follows:

Period	03/01/07 - 05/31/07	06/01/08 - 08/31/08
IRS Total	\$318,581.43	\$408,812.36
IRS Cash	\$242,028.46	\$300,444.52
IRS Credit Card	\$76,552.97	\$108,367.84
IRS Credit Card Tips	\$16,172.16	\$21,553.14
Cash Sales Percentage	75.97%	73.49%
Credit Card Sales Percentage	24.03%	26.51%

This information, appearing on the quarterly shift sales summary sheets, was not discussed or explained in any manner, but presumably presents Coram Diner's accounting summaries with regard to IRS wage and withholding tax reporting requirements as the same apply to wait staff in dining establishments.

per the POS system for October 6, 2006 (27.44%) was nearly identical to the 27.07 percent ratio of such sales found by the Division on the observation date.

***SUMMARY OF THE PARTIES' POSITIONS***

32. The Division maintains that petitioners did not provide Coram Diner's complete books and records for the audit period, including guest checks or register tapes, either in paper form or in electronic form via Coram Diner's POS system. The Division points out that multiple requests for records were made, but that only minimal records were provided in response and that such limited records were simply insufficient to meet the required records standard or to enable the conduct of a direct audit. In this respect, the Division specifically points out that the flash drive provided for review, allegedly containing full books and records from Coram Diner's POS system hard drive, was thoroughly reviewed and found to be patently unreliable. The Division notes that petitioners were made aware of the problems with the contents of the flash drive, yet took no measures to correct the same by submitting records as requested.

33. Petitioners, in contrast, assert that the information allegedly entered into, maintained on and obtainable from the POS system hard drive was complete, accurate and reliable. Petitioners maintain that the Division did not make a reasonable effort to obtain and review Coram Diner's records, either in electronic or paper format. Petitioners assert that the POS system printouts for the two sales tax quarterly periods as provided at hearing (*see* Findings of Fact 28 and 29) establish that Coram Diner maintained complete and accurate records for the entire audit period and that the same were adequate for the conduct of a direct audit, thus negating the Division's authority to resort to an indirect audit method as was done in this case.

***CONCLUSIONS OF LAW***

A. Tax Law § 1105(a) imposes a sales tax on the receipts from every "retail sale" of tangible personal property except as otherwise provided in Article 28 of the Tax Law. A "retail

sale” is “[a] sale of tangible personal property to any person for any purpose, other than . . . for resale as such . . .” (Tax Law § 1101[b][4][i][A]). Under Tax Law § 1135(a)(1), “[e]very person required to collect tax shall keep records of every sale . . . in such form as the commissioner of taxation and finance may by regulation require.” These records must be kept in a manner suitable to determine the correct amount of tax due and must be available for the Division's inspection upon request for a period of three years (Tax Law § 1135[g]; 20 NYCRR 533.2[a][2]). The regulations provide that among the sales records required to be maintained are a “sales slip, invoice, receipt, contract, statement or other memorandum of sale; . . . guest check, . . . cash register tape and any other original sales document” (20 NYCRR 533.2[b][1]).

B. Tax Law § 1138(a)(1) provides, in relevant part, that if a sales tax return was not filed, “or if a return when filed is incorrect or insufficient, the amount of tax due shall be determined [by the Division] from such information as may be available. If necessary, the tax may be estimated on the basis of external indices . . . .” When acting pursuant to section 1138(a)(1), the Division is required to select a method of audit reasonably calculated to reflect the tax due. The burden then rests upon the taxpayer to demonstrate that the method of audit or the amount of the assessment was erroneous (*see Matter of Your Own Choice, Inc.*, Tax Appeals Tribunal, February 20, 2003). The standard for reviewing a sales tax audit where estimated or indirect auditing methods, including external indices, were employed was set forth in *Matter of Your Own Choice, Inc.*, as follows:

To determine the adequacy of a taxpayer's records, the Division must first request (*Matter of Christ Cella, Inc. v. State Tax Commn.*, [102 AD2d 352, 477 NYS2d 858]) and thoroughly examine (*Matter of King Crab Rest. v. Chu*, 134 AD2d 51, 522 NYS2d 978) the taxpayer's books and records for the entire period of the proposed assessment (*Matter of Adamides v. Chu*, 134 AD2d 776, 521 NYS2d 826, *lv denied* 71 NY2d 806, 530 NYS2d 109). The purpose of the examination is to determine, through verification drawn independently from within these records (*Matter of Giordano v. State Tax Commn.*, 145 AD2d 726, 535 NYS2d 255; *Matter of Urban Liqs. v. State Tax Commn.*, 90 AD2d 576, 456

NYS2d 138; *Matter of Meyer v. State Tax Commn.*, 61 AD2d 223, 402 NYS2d 74, *lv denied* 44 NY2d 645, 406 NYS2d 1025; *see also, Matter of Hennekens v. State Tax Commn.*, 114 AD2d 599, 494 NYS2d 208), that they are, in fact, so insufficient that it is “virtually impossible [for the Division of Taxation] to verify taxable sales receipts and conduct a complete audit” (*Matter of Chartair, Inc. v. State Tax Commn.*, 65 AD2d 44, 411 NYS2d 41, 43; *Matter of Christ Cella, Inc. v. State Tax Commn.*, *supra*), “from which the exact amount of tax due can be determined” (*Matter of Mohawk Airlines v. Tully*, 75 AD2d 249, 429 NYS2d 759, 760).

Where the Division follows this procedure, thereby demonstrating that the records are incomplete or inaccurate, the Division may resort to external indices to estimate tax (*Matter of Urban Liqs. v. State Tax Commn.*, *supra*). The estimate methodology utilized must be reasonably calculated to reflect taxes due (*Matter of W.T. Grant Co. v. Joseph*, 2 NY2d 196, 159 NYS2d 150, *cert denied* 355 US 869, 2 L Ed 2d 75), but exactness in the outcome of the audit method is not required (*Matter of Markowitz v. State Tax Commn.*, 54 AD2d 1023, 388 NYS2d 176, *affd* 44 NY2d 684, 405 NYS2d 454; *Matter of Cinelli*, Tax Appeals Tribunal, September 14, 1989). The taxpayer bears the burden of proving with clear and convincing evidence that the assessment is erroneous (*Matter of Scarpulla v. State Tax Commn.*, 120 AD2d 842, 502 NYS2d 113) or that the audit methodology is unreasonable (*Matter of Surface Line Operators Fraternal Organization v. Tully*, 85 AD2d 858, 446 NYS2d 451; *Matter of Cousins Serv. Station*, Tax Appeals Tribunal, August 11, 1988). In addition, “[c]onsiderable latitude is given an auditor's method of estimating sales under such circumstances as exist in [each] case” (*Matter of Grecian Sq. v. Tax Commn.*, 119 AD2d 948, 501 NYS2d 219, 221).

C. The long-standing statutory and regulatory authority of Tax Law § 1135(a) and 20 NYCRR 533.2(b), together with case law, clearly mandates that records concerning a taxpayer’s sales transactions are to be maintained and made available to the Division for review upon request. While the maintenance of taxpayer records has in the past typically involved hard copy (paper) records, technological advances have been recognized and expanded authority has been provided by the enactment of regulations that give taxpayers the option to retain and maintain records in electronic format. In this regard, the Division has adopted regulations in order to comply with the record retention and electronic recordkeeping provisions of the New York Electronic Signatures and Records Act (L 1999, ch 4 § 3) and the federal Electronic Signatures in Global and National Commerce Act (5 USC § 552; 47 USC § 231, as added by Pub L 106-299,

114 Stat 464, et. seq.). Pursuant to those regulations and as applicable to the retention of taxpayer records, beginning June 1, 2001, taxpayers are generally given the option of retaining required records in either hard-copy (paper) or electronic format. The Division does not prescribe technologies or technical specifications for maintaining electronic records and does not require the use of particular types of hardware or software. The provisions apply only to the format in which taxpayer records are to be maintained (*see* 20 NYCRR 2402.1; 20 NYCRR 2402.1). 20 NYCRR 2402.2(c)(1) describes in detail the components of the electronic record retention rules, in pertinent part, as follows:

A taxpayer must retain electronic records that accurately reflect the information that is required to be set forth in the records. The electronic records, either alone or in conjunction with the taxpayer's other records, must contain sufficient information in order to support and verify all of the entries that are made on the taxpayer's tax returns or informational reports, and to determine the proper taxes or other amounts that may be due. These records, either alone or together, must be reconcilable to the taxpayer's reporting periods and must create an audit trail designed so that the details underlying each of the entries made on the taxpayer's returns or reports can be identified and made available to the department upon its request.

D. In view of the foregoing, there is no question that petitioners were entitled to keep Coram Diner's records in electronic format, and petitioners allege that such was done. However, retaining records but not providing the same for review upon request is not sufficient for audit standards. Even accepting, for the sake of argument, that Coram Diner's records (however kept) were in fact complete, it remains clear that such records were never directly provided to the Division, either in electronic form or in paper form for the audit period, nor was the Division afforded a meaningful opportunity to access and review such records, as required. This failure occurred notwithstanding that the Division clearly requested the records on numerous occasions, both verbally and in writing, and also provided petitioners with lists appended to the written requests that set forth the specific records being sought for review. Petitioners do not claim that

such records were in fact provided to the Division. Rather, petitioners argue that the same were maintained and were available but were not accessed by the Division. Petitioners appear to argue that the POS system printouts for two quarterly periods, as submitted at hearing, establish that all sales for the audit period were recorded by and retained within the POS system and that the same were able to be audited, thereby eliminating any need for the Division to resort to indirect auditing methods. While not clearly articulated, petitioners seem to attribute the Division's lack of review and reliance on the POS system, or on the paper records (guest checks) allegedly maintained by Coram Diner, to some unspecified failure in the process of accessing such records.

E. The difficulty with petitioners' argument is that the record simply does not support the same. As detailed, taxpayers have the choice to maintain required records in electronic or hard copy (paper) format, or both (*see* Conclusion of Law C). At the same time it remains axiomatic that regardless of the chosen format, a taxpayer is obligated to both retain and maintain its records, *and* to make such records available for review by the Division upon request. In this case, petitioners failed to fulfill the second requisite obligation to make Coram Diner's records available to the Division for examination as requested. The record in this case clearly bears out that the Division made repeated requests for Coram Diner's records, including several requests for the provision of those records in electronic format. In fact, the Division first received some bank statements and some daily sheets, together with an offer from petitioners' initial representative that Coram Diner's records might be made available in electronic format. This offer was followed by a promise from petitioner Kostas Hionas to provide Coram Diner's records in electronic format on a flash drive (*see* Finding of Fact 8). However, nothing was provided for several months thereafter. In turn, petitioners' representative then specifically advised the Division that records in electronic format would not be forthcoming (*see* Findings of Fact 10 and 12). Notwithstanding this advice, however, Coram Diner's accountant thereafter delivered to the

Division a flash drive allegedly containing such promised records (*see* Finding of Fact 18). Upon examination, the content on the flash drive was found to be incomplete and unreliable (*see* Finding of Fact 19). Petitioners were advised of the problems with the information on the flash drive, and there followed several additional detailed requests by the auditor for Coram Diner's records. However, the requested records were never in fact produced, in any format, for the Division's review. While petitioners would, as noted, somehow try to pin this failure on the Division, the record amply supports the conclusion that the Division was never afforded a reasonable or meaningful opportunity to either access or review Coram Diner's records. Rather, only a very limited number of items was furnished and, in the end, complete records were simply never made available for review.

F. In this case, petitioners' conduct clearly was a hindrance to the Division in pursuing the aim of carrying out an audit. Further, it is clear that the impact of petitioners' conduct resulted essentially in moving the audit process into the hearing process. A hearing is not the optimal setting in which to conduct an audit. Rather, an audit should occur at earlier stages allowing for and encouraging a frank and open give and take between the parties, ordinarily leading to the resolution of some issues or transactions or, at the least, identifying and crystalizing the issues and items in dispute which may then be presented for resolution by formal hearing. On this score, the Tribunal has observed as follows:

Petitioner's failure to produce documentation concerning the transactions at issue during the audit is unfortunate since that was the appropriate time for adequate consideration by both parties of the documents and the nature of the transactions they represent. The formal nature of the hearing before the Administrative Law Judge operates against such discussion and analysis. While such documents can be reviewed post-hearing by the Administrative Law Judge, again the bilateral review and consideration that can occur during audit is absent. (*Matter of Jenkins-Covington*, Tax Appeals Tribunal, August 25, 1988, *confirmed on other grounds* 195 AD2d 625, 600 NYS2d 281, *lv denied* 82 NY2d 664, 610 NYS2d 151.)

G. In end result, the conduct of an audit in this case was circumscribed by the varying actions and unfulfilled promises made but not kept by petitioners. Petitioners had a period of nearly two years within which to provide records, yet, as detailed, this did not occur. Even up to the point of the instant hearing, and notwithstanding multiple requests for records, petitioners only provided a sampling of Coram Diner's allegedly complete records for a portion (two quarterly periods) of the audit period. Under these circumstances, the Division was fully justified and within its authority to resort to estimated auditing methodologies, including methods that did not rely upon the limited and partial information provided by petitioners, to determine whether Coram Diner had properly remitted sales and use taxes for the audit period. Any other conclusion essentially places the Division in the position of relying upon a taxpayer's chosen sample of its records as proof that its records were complete and accurate for the entire audit period, without affording the Division the opportunity to conduct an audit to verify the same. This would represent a reversal of the audit process and allow a taxpayer to confirm the correctness of its returns as filed merely by providing its own chosen sample of its records.

H. Having determined that the Division was entitled to resort to indirect auditing leaves only the questions of whether the method of audit chosen was unreasonable or whether the results obtained by application of such method were erroneous (*Matter of Surface Line Operators Fraternal Org. v. Tully*, 85 AD2d 858 [1981]). In this case, the auditor obtained Coram Diner's bank statements by subpoena and utilized the same in conjunction with the results of the Division's full day observation of sales at the diner premises, undertaken as part of its audit for the period immediately preceding the subject audit period, to calculate liability (*see* Finding of Fact 23). In turn, petitioner has not established, by clear and convincing evidence, that either the method of audit chosen was unreasonable or that the results of its application were erroneous. Using Coram Diner's bank statements in conjunction with the results of the

Division's observation of sales at the premises, as described, is clearly an acceptable audit methodology under the circumstances (*see e.g. Matter of Burbacki*, Tax Appeals Tribunal, February 9, 1995). Case law is clear that the results of a one-day observation test may reasonably be extrapolated over a multiple-year audit period (*Matter of Marte*, Tax Appeals Tribunal, August 5, 2004). In fact, although the results of the observation of sales utilized in this matter are taken from an earlier audit of petitioner conducted by the Division, it remains that the observation day itself (October 6, 2006) fell within the subject audit period. In fact, the accuracy of the data recorded by the Division on the observation date, including specifically its cash to credit card sales ratio, is supported by Coram Diner's own records for the same day (*see* Finding of Fact 31), and is not challenged. At least for that day, one would expect a taxpayer's recordkeeping to comport with its sales as observed by an audit team. This fact does not, in any manner however, overcome petitioners' failure to provide its records for review for the entire audit period, or establish the completeness or accuracy of Coram Diner's records for the entire audit period. In sum, petitioners have not established that the selected method of audit or the results of its application were unreasonable or erroneous and such results are therefor sustained.

I. Finally, petitioners have not advanced any bases upon which abatement of penalties would be justified and the same are, therefore, sustained.

J. The petitions of Coram Diner Corp. and Kostas Hionas are hereby denied and the notices of determination dated May 26, 2011 (regarding Coram Diner Corp.) and May 27, 2011 (regarding Kostas Hionas), together with penalties and interest, are sustained.

DATED: Albany, New York  
October 24, 2013

/s/ Dennis M. Galliher  
ADMINISTRATIVE LAW JUDGE