

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
AMISANA BAGELS, INC.	:	DETERMINATION DTA NO. 826719
for Revision of a Determination or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the Period June 1, 2010 through February 28, 2013.	:	

Petitioner, Amisana Bagels, Inc., filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period June 1, 2010 through February 28, 2013.

A hearing was held before Dennis M. Galliher, Administrative Law Judge, in New York, New York, on January 20, 2016 at 10:30 a.m., with all briefs to be submitted by June 10, 2016, which date began the six-month period for the issuance of this determination. Petitioner appeared by Buxbaum Sales Tax Consulting, LLC (Michael Buxbaum, CPA). The Division of Taxation appeared by Amanda Hiller, Esq. (M. Greg Jones, Esq., of counsel).

ISSUES

I. Whether the audit methodology utilized by the Division of Taxation in its audit of Amisana Bagels, Inc., had a rational basis and was reasonably calculated to reflect the tax due.

II. Whether petitioner has shown reasonable cause for the abatement of penalties.

FINDINGS OF FACT

1. During the period at issue petitioner, Amisana Bagels, Inc., operated a bagel shop and delicatessen located in a small shopping center in Baldwin, New York. There is customer

parking available in front of the shop. The shop is open seven days per week from 5:30 a.m. through 3:30 p.m., and offers breakfast all day and free delivery.

2. The Division of Taxation (Division) commenced a sales and use tax audit of petitioner's business in early May of 2013. On May 2, 2013, the auditor assigned to the case made an unannounced visit to petitioner's premises. At that time, he noted two cash registers in use at the premises and three employees serving customers. He observed a coffee station, coolers for soda, water and juices, a bagel rack with a variety of bagels, and an open dine-in seating area, including seven tables with seats for two patrons at each table. The auditor's observations at the time of his visit, as well as his review of petitioner's printed and posted menu, revealed that petitioner sells items including breakfast sandwiches, bagels with a wide variety of spreads, lunch specials, club sandwiches, hot and cold sandwiches and salads, as well as prepackaged bakery items, cookies, cereals, and iced tea. The auditor purchased a cinnamon bagel with cream cheese. The cash register receipt for this purchase, paid for in cash, did not identify or describe the item purchased, but rather simply listed a "non-taxable" sale for \$2.95, with no sales tax charged thereon.

3. By an appointment letter dated May 10, 2013, the Division confirmed that petitioner was scheduled for an audit of its New York State sales and use tax records for the period June 1, 2010 through February 28, 2013. The letter noted an initial audit appointment date of June 12, 2013, and further explained that all books and records pertaining to petitioner's sales and use tax liability for the audit period must be available for the appointment. An attached Information Document Request (IDR) provided a detailed list of the documents and information to be made available for audit, including: sales tax returns; worksheets and canceled checks; federal income tax returns; New York State corporation tax returns; general ledger; general journal and closing

entries; sales invoices; all exemption documents supporting nontaxable sales; chart of accounts; fixed asset purchase and sales invoices; expense purchase invoices; merchandise purchase invoices; bank statements, canceled checks and deposit slips; cash receipts journal; cash disbursements journal; the corporate book, including minutes, board of directors, and articles of incorporation; depreciation schedules; lease rental agreements; guest checks and cash register tapes for the entire audit period.

4. The initial appointment date was postponed at petitioner's request. In turn, a second audit appointment letter, dated August 1, 2013, was issued rescheduling the audit appointment date to August 12, 2013. This letter was accompanied by an attached IDR, identical to the IDR described above.

5. In response to the Division's letters and IDRs, petitioner supplied only bank statements and sales tax returns, plus cash register tapes for the months of July and August of 2012. By a letter dated August 5, 2013, petitioner's representative advised the auditor that "the taxpayer [did] not have complete and adequate records under Tax Law [§] 1135-Records to be kept."

6. The auditor's review of the cash register tapes submitted by petitioner revealed that none of the cash register tapes included any description or other means of identifying the particular items being sold, that sales were simply rung up either as taxable or nontaxable, and that the vast majority of sales were recorded as nontaxable sales paid in cash. The auditor concluded, in light of the foregoing, that petitioner's records were not adequate for the conduct of a detailed audit, and that petitioner's sales tax liability would therefore be determined upon the basis of indirect auditing, i.e., estimation.

7. The auditor reviewed petitioner's cash register tapes, in conjunction with petitioner's menu, for the period spanning August 2 through August 8, 2012. For this period, petitioner's

register tapes listed gross sales of \$5,093.30, taxable sales of \$746.97 and sales tax charged thereon in the amount of \$64.43, thus reflecting that 85.33% ($\$4,346.33 \div \$5,093.30$) of petitioner's sales were recorded as nontaxable sales and 14.67% ($\$746.97 \div \$5,093.30$) of such sales were recorded as taxable sales.¹ The auditor concluded that this recording rate was entirely inconsistent with the taxable nature of the vast majority of items listed for sale on petitioner's menu, and was further inconsistent with his observations and experience during his May 2, 2013 visit to the premises (*see* Finding of Fact 2).

8. In addition to the foregoing, the auditor noted that he had conducted a prior (first) audit of petitioner's business for the period spanning September 1, 2007 through May 31, 2010 (i.e., the period immediately preceding the audit period herein). In that prior audit, petitioner asserted that 55% of its sales were taxable sales. This represented an increase over its reported taxable sales percentage, and resulted in the calculation of an additional sales tax liability of \$48,309.67. The auditor testified that he accepted petitioner's assertion as to its taxable sales percentage, coupled with petitioner's agreement to maintain proper records of the taxable status of each of its sales going forward, as the basis for closing the audit.

9. By a letter dated September 24, 2013, the auditor advised petitioner that the Division would conduct an in-person observation of petitioner's sales and business activities at petitioner's premises. Petitioner's representative responded to this letter on September 30, 2013, and declined the opportunity for an on-premises observation of petitioner's sales and business activities.

¹ As a confirmatory calculation, the auditor's review of petitioner's cash register tapes for the period August 5, 2012 through August 11, 2012 listed gross sales as \$3,390.63, taxable sales as \$261.75 and sales tax charged thereon in the amount of \$22.50, thus reflecting 92.28% ($\$3,128.88 \div \$3,390.63$) of petitioner's sales recorded as nontaxable sales and 7.72% ($\$261.75 \div \$3,390.63$) recorded as taxable sales.

10. In computing petitioner's audited taxable sales, the auditor's review of petitioner's menu revealed that the only nontaxable item listed thereon was a single plain bagel with a selling price of 70 cents. The auditor concluded that any sales amounts listed on the register tapes that were evenly divisible by .70 would be allowed as nontaxable sales (i.e., as representing nontaxable sales of unheated, unsliced bagels without any spread purchased for off-premises consumption).² Applying this method of calculation to the cash register tape amounts for the period August 2, 2012 through August 8, 2012, the auditor determined petitioner's nontaxable sales to be \$428.40, thus leading to his conclusion that 8.41% ($\$428.40 \div \$5,093.30$) of petitioner's sales were nontaxable sales while 91.59% ($\$4,664.90 \div \$5,093.30$) of petitioner's sales were taxable sales.

11. The auditor accepted petitioner's gross sales as reported (\$1,063,629.00), and applied the foregoing nontaxable sales percentage (8.41%) thereto to arrive at audited nontaxable sales (\$89,462.38). The balance of petitioner's reported sales (\$974,166.62) were treated as audited taxable sales, and after reduction for reported taxable sales (\$202,438.00) resulted in additional taxable sales (\$771,728.62), with additional sales tax due thereon in the amount of \$66,561.59.

12. The Division issued a Notice of Determination to petitioner dated August 8, 2014 and asserting additional sales tax due of \$66,561.59 for the period June 1, 2010 through February 28, 2013, plus interest and penalty (based on petitioner's underreporting of tax by an amount in excess of 25% of the amount of tax due) under Tax Law § 1145(a)(1)(vi).

² For example, a register tape amount of \$2.80, when divided by .70, results in the even number 4. Thus, the auditor allowed the same as an instance where the sale represented a customer's nontaxable purchase of four "unadorned" bagels for off-premises consumption.

CONCLUSIONS OF LAW

A. The standard for reviewing a sales tax audit where an indirect audit methodology has been employed in the determination of sales tax liability is well established, and was set forth in *Matter of AGDN, Inc.* (Tax Appeals Tribunal, February 6, 1997) as follows:

“a vendor . . . is required to maintain complete, adequate and accurate books and records regarding its sales tax liability and, upon request, to make the same available for audit by the Division (*see*, Tax Law §§ 1138[a]; 1135; 1142[5]; *see, e.g., Matter of Mera Delicatessen*, Tax Appeals Tribunal, November 2, 1989). Specifically, such records required to be maintained ‘shall include a true copy of each sales slip, invoice, receipt, statement or memorandum’ (Tax Law § 1135). It is equally well established that where insufficient records are kept and it is not possible to conduct a complete audit, ‘the amount of tax due shall be determined by the commissioner of taxation and finance from such information as may be available. If necessary, the tax may be estimated on the basis of external indices . . . ’ (Tax Law § 1138[a]; *see, Matter of Chartair, Inc. v. State Tax Commn.*, 65 AD2d 44, 411 NYS2d 41, 43). When estimating sales tax due, the Division need only adopt an audit method reasonably calculated to determine the amount of tax due (*Matter of Grant Co. v. Joseph*, 2 NY2d 196, 159 NYS2d 150, *cert denied* 355 US 869); exactness is not required (*Matter of Meyer v. State Tax Commn.*, 61 AD2d 223, 402 NYS2d 74, *lv denied* 44 NY2d 645, 406 NYS2d 1025; *Matter of Markowitz v. State Tax Commn.*, 54 AD2d 1023, 388 NYS2d 176, *affd* 44 NY2d 684, 405 NYS2d 454). The burden is then on the taxpayer to demonstrate, by clear and convincing evidence, that the audit method employed or the tax assessed was unreasonable (*Matter of Meskouris Bros. v. Chu*, 139 AD2d 813, 526 NYS2d 679; *Matter of Surface Line Operators Fraternal Org. v. Tully*, 85 AD2d 858, 446 NYS2d 451).”

B. In this case, the record establishes the Division’s clear and unequivocal written requests for books and records of petitioner’s sales, as well as petitioner’s failure to produce such books and records. The Division reasonably concluded that petitioner did not maintain or have available books and records that were sufficient to verify taxable sales for the audit period, including specifically any cash register tapes, guest checks or invoices on which the items sold by petitioner were or could be identified such that the taxable or nontaxable status of such items and

sales could be discerned. Having established the unavailability of required books and records, the Division was clearly entitled to resort to the use of indirect methods to determine petitioner's sales and sales tax liability (*see Matter of W. T. Grant Co. v. Joseph*, 2 NY2d 196 [1957], *cert denied* 355 US 869 [1957]; *Matter of Del's Mini Deli, Inc. v. Commissioner of Taxation and Finance*, 205 AD2d 989 [1994]; *Matter of Vebol Edibles v. Tax Appeals Tribunal*, 162 AD2d 765 [1990]). In turn, the auditor determined petitioner's taxable sales and resulting tax liability by resort to an analysis based upon the only records provided by petitioner, consisting of a review of the limited number of cash register tapes provided coupled with petitioner's menu of items sold (*see* Finding of Fact 10). Under the circumstances, this method of audit was entirely reasonable.³

C. Since it is concluded that the audit method was reasonable, petitioner had the burden of proof to show, by clear and convincing evidence, that the result of the audit was unreasonably inaccurate or that the amount of tax assessed was erroneous (*Matter of Sarantopoulos v. Tax Appeals Tribunal*, 186 AD2d 878 [1992]). Petitioner failed to meet this fairly substantial burden (*see Matter of Center Moriches Monument Co. v. Commr. of Taxation & Fin.*, 211 AD2d 947 [1995]). Petitioner did not produce any documentary evidence to dispute the results of the Division's analysis and calculations, or to substantiate its argument that the Division's estimate of petitioner's taxable sales was unreasonable. In this regard, petitioner's argument seems to be that the percentage of taxable sales as computed herein on audit (91.59%), as compared to the percentage of taxable sales accepted in the course of the previous audit (55%), represents such an increase that it is per se arbitrary and capricious. This simple argument overlooks the fact that

³ It is noted that the Division's offer to conduct an on-premises observation of sales was rejected out of hand by petitioner (*see* Finding of Fact 9).

the taxable percentage determined herein was based upon the auditor's review of petitioner's own very limited submission of records, that petitioner declined the Division's offer of an alternative method of audit and calculation, and that the prior taxable sales percentage was based simply upon petitioner's assertion that 55% of its sales were taxable (an assertion that appears to have been accepted, coupled with an agreement on petitioner's part to maintain the required records going forward, essentially for purposes of resolution of that first audit of petitioner's business; *see* Finding of Fact 8). On balance, the audit method employed herein, and the resulting amount of additional tax determined to be due, is sustained.

D. Addressing the issue of penalties, in establishing reasonable cause for penalty abatement, the taxpayer faces an onerous task (*Matter of Philip Morris, Inc.*, Tax Appeals Tribunal, April 29, 1993). The Tribunal explained that “[b]y first requiring the imposition of penalties (rather than merely allowing them at the Commissioner’s discretion), the Legislature evidenced its intent that filing returns and paying tax according to a particular timetable be treated as a largely unavoidable obligation [citations omitted]” (*Matter of MCI Telecommunications Corp.*, Tax Appeals Tribunal, January 16, 1992, *confirmed* 193 AD2d 978 [1993]). Petitioner’s failure to maintain records of the business’s sales supports the imposition of penalties. Petitioner has failed to demonstrate reasonable cause for the failure to pay the taxes due, and the imposition of penalties by the Division was justified (*Matter of Miller v. State Tax Commission*, 94 AD2d 841, 843 [1983]).

E. The petition of Amisana Bagels, Inc., is denied and the Notice of Determination, dated August 8, 2014, is sustained.

DATED: Albany, New York
December 01, 2016

/s/ Dennis M. Galliher
ADMINISTRATIVE LAW JUDGE