STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition :

of :

NICK TSIGOS :

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 December 1, 1996 through November 30, 1998. :

In the Matter of the Petition :

of :

RODOS FOODS, INC. :

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 December 1, 1995 through November 30, 1998. :

DETERMINATION
DTA NOS. 818515 & 818813

Petitioner Nick Tsigos, 8 Niagara Street, Miller Place, New York 11764-2614, 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 December 1, 1996 through November 30, 1998.

Petitioner Rodos Foods, Inc., 1015 Rt. 25A, Stony Brook, New York 11790, 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 December 1, 1995 through November 30, 1998.

A consolidated hearing was held before Frank W. Barrie, Administrative Law Judge, at the offices of the Division of Tax Appeals, New York State Office Building, Hauppauge, New York, on January 12, 2002 at 10:30 A.M., with all briefs to be submitted by August 23, 2002, which date began the six-month period for the issuance of this determination. Petitioner appeared by Mark Levitch, CPA. The Division of Taxation appeared by Barbara G. Billet, Esq. (Michael P. McKinley, Esq., of counsel).

ISSUE

Whether the one-day observation test, conducted by the Division of Taxation, of a Long Island pizzeria and restaurant, was a sales tax field audit method reasonably calculated to reflect taxes due.

FINDINGS OF FACT

1. Petitioner Nick Tsigos, by his corporation, Rodos Foods, Inc. ("Rodos Foods"), operated a popular pizzeria and restaurant known as Cosmos Café in Stony Brook, Long Island, near the state university and across from a Long Island Railroad station. More than a pizzeria, Cosmos Café also offered Greek and Italian specialties, such as its most expensive dishes of shrimp tourkolimano, shrimp parmigiana, and veal francese, each priced at $11.95 on its menu, as well as beer and wine.

2. During the period at issue,[1] Rodos Foods reported the following taxable sales:

Sales tax quarter ended	Taxable sales reported
Feb. 29, 1996	$ 37,150.00
May 31, 1996	47,150.00
Aug. 31, 1996	47,878.00
Nov. 30. 1996	48,182.00

[1] The corporate taxpayer, Rodos Foods, Inc. executed consents to extend the period of limitations for assessing tax determined due for the period December 1, 1995 to November 30, 1996 while the individual taxpayer, Nick Tsigos, did not, and consequently the period of limitations for assessing additional tax tolled vis-a-vis Mr. Tsigos for the first four sales tax quarters included in the table in this finding of fact. Nonetheless, this distinction appears to be merely academic since Rodos Foods, Inc. remains in existence and continues to operate Cosmos Cafe.

Feb. 28, 1997	36,870.00
May 31, 1997	40,485.00
Aug. 31, 1997	40,227.00
Nov. 30, 1997	48,803.00
Feb. 28, 1998	39,992.00
May 31, 1998	38,897.00
Aug. 31, 1998	38,448.00
Nov. 30, 1998	46,206.00
Total taxable sales reported	$510,288.00

3. Suffolk County, which has its own investigators who survey different types of businesses to ensure compliance with sales tax obligations, made a referral in late November of 1998 to the Division of Taxation ("Division") of petitioners' restaurant operation as one "worthy of audit" after the county's own survey of the premises and review of taxable sales reported by petitioners. Apparently, given the size and nature of petitioners' restaurant business, annual taxable sales reported of approximately $170,000.00 seemed questionable.

4. By a letter dated December 7, 1998 and a subsequent letter to the former representative of Rodos Foods dated December 23, 1998, the Division's auditor advised the corporate petitioner that its tax records for sales tax for the three-year period December 1, 1995 to November 30, 1998 were going to be audited. The following request for records was made:

> All books and records pertaining to your sales and use tax liability . . . must be available . . . . This includes financial statements, journals, ledgers, sales invoices, purchase invoices, cash register tapes, sales and use tax returns, federal income tax returns, and exemption certificates.
>
> During the course of the audit, you may be required to furnish additional records and/or information.

5. The records provided to the auditor were extremely minimal. Petitioners did not provide any records to substantiate sales such as cash register tapes, guest checks, cash receipts, sales journal, or day book. There was no record listing the restaurant's sales that corresponded to the amount of cash being deposited in its checkbook. Nor was there a record of the restaurant's purchases. Further, the auditor was not able to reconcile bank statements to sales tax returns and also could not reconcile information she had obtained from third-party suppliers to the purchase invoices provided by petitioners. In fact, the information from the third-party suppliers showed greater purchases than what was shown in the invoices[2] provided by petitioners.

6. By a letter dated March 17, 1999, the auditor advised petitioners' former accountant that "the vendor's books and records are insufficient to determine if the proper amount of sales tax has been reported for the audit period." The auditor added that "an observation at your client's place of business" was necessary and would be performed "within the next six weeks." She noted that:

> Sales activity will be recorded for an entire day, from opening to closing. The observation will be performed discreetly, with minimal interruption of business activity.

7. In March of 1998, an investigator with the Division performed what she described as a "mini observation" of petitioners' restaurant without disclosing that she was a representative or employee of the Division. At such time, she obtained a menu which noted the restaurant's hours as 10:00 A.M. until 3:00 A.M.

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[2] Petitioners did not even have an accounting or bookkeeping record of purchases and merely provided stacks of invoices to the auditor.

8. The investigator followed-up her mini observation with an observation test of petitioners' restaurant on Thursday, April 22, 1999. She arrived at 9:30 A.M. based on information she obtained the day before that the restaurant opened at 10:00 A.M., which confirmed the opening time on the menu. However, when she attempted to enter the restaurant at 10:00 A.M., the restaurant remained closed. Waiting outside in her car, the restaurant eventually opened at 11:00 A.M. When she entered the restaurant, she noticed a sign "that you could write on with a marker listing the days of the weeks and the hours," not attached to a window or door but rather leaning against a window, which noted the restaurant's hours as 11:00 A.M. to 7:00 P.M. Mr. Tsigos identified himself as "in charge," and he responded to the investigator's explanation of why she was at the restaurant with a request that she leave the premises. The investigator left the premises and after consulting her superior, she returned to the restaurant and commenced her observation test.

9. The investigator observed restaurant sales of $605.90 in a six and one-half hour period running from 11:00 A.M. to 5:30 P.M. at which time her colleague, who had arrived at 5:00 P.M., took over from her and continued the observation test of the restaurant's sales. From 5:30 P.M. until the restaurant's closing that day at 8:30 P.M., the colleague observed restaurant sales of $469.30. Consequently, the two investigators personally observed sales of $1,075.20, with a head count of 185 customers.

10. Prior to commencing her observation of sales at 11:00 A.M., the investigator requested that the restaurant's cash register be zeroed out. At the end of the day's business, the cash register tape, which showed total taxable sales of $1,096.18, was provided to the investigator. The register tape showed sales which were $20.98 more than the sales listed by the investigators on their work schedules of $1,075.20, as detailed in Finding of Fact "9". In

calculating tax due based upon this one-day observation of sales, the Division's auditor used the *lesser* amount listed on the investigator's schedules, in fairness to petitioners. It was suggested by the Division's auditor that when one of the investigators was on the phone speaking with her, she might have failed to observe the sales consisting of the difference of $20.98.

11. Petitioner Nick Tsigos actively undermined the performance of the observation test. Initially, he delayed the opening of the restaurant and sent home two of his employees, including a waitress, leaving himself and five employees to conduct the restaurant's business. He also impeded the restaurant's sales by doing the following:

(i) Offering buy one, get one free on all of the daily specials when the board listing specials noted that only soup sales were buy one, get one free;

(ii) Mr. Tsigos was on the restaurant's telephone for most of the time between 5:30 P.M. and 6:00 P.M. so that phone orders could not be made during a crucial period of the day, and at other times, the phone was found to be either not in working order or the ringer set very low so that incoming calls could not be identified;

(iii) The restaurant was closed several hours before its usual closing time.

12. Petitioner Nick Tsigos also attempted to mislead the investigators by stating that no deliveries were made by the restaurant. When the investigator showed Mr. Tsigos that on the board listing the restaurant's specials was written a phone number to call for delivery of food, he, at first, "claimed he did not understand how that was written there." Eventually, he stated that "he made deliveries on and off when he felt like it but was not making deliveries this day." Nonetheless, he started making deliveries at 4:00 P.M., which he attempted to use to his advantage, since the phone to call in orders was made inoperable when he was away from the restaurant making deliveries.

13. Utilizing the observed total sales, which included sales tax, of $1,075.20, the auditor backed out the tax to determine actual sales for the observed period on April 22, 1999 of $993.26. She then divided this amount by 9 hours to calculate hourly sales of $110.36. She then calculated daily sales of $1,545.04 by multiplying the hourly sales of $110.36 by 14 based upon restaurant hours of 10:00 A.M. to 12:00 A.M. The auditor then calculated quarterly sales of $140,595.00 as follows:

Daily sales	$ 1,545.04
Multiplied by days per week	7
Weekly sales	$ 10,815.00
Multiplied by weeks per quarter	13
Quarterly sales	$140,595.00

14. Based upon her estimate of quarterly sales of $140,595.00, the auditor computed additional tax due for the three-year audit period of $97,176.50 as follows:

Quarter Ended	Audited Taxable Sales	Taxable Sales Reported	Additional Taxable Sales	Tax Rate	Additional Tax Due
2/29/96	$ 140,595.00	$ 37,150.00	$103,445.00	.085/.0825	$8,620.42
5/31/96	140,595.00	47,150.00	93,445.00	.0825	7,709.21
8/31/96	140,595.00	47,878.00	92,717.00	.0825	7,649.15
11/30/96	140,595.00	48,182.00	92,413.00	.0825	7,624.07
2/28/97	140,595.00	36,870.00	103,725.00	0.0825	8,557.31
5/31/97	140,595.00	40,485.00	100,110.00	.0825	8,259.08
8/31/97	140,595.00	40,227.00	100,368.00	.0825	8,280.36
11/30/97	140,595.00	48,803.00	91,792.00	.0825	7,572.84
2/28/98	140,595.00	39,992.00	100,603.00	.0825	8,299.75
5/31/98	140,595.00	38,897.00	101,698.00	.0825	8,390.09
8/31/98	140,595.00	38,448.00	102,147.00	.0825	8,427.13

11/30/98	140,595.00	46,206.00	94,389.00	.0825	7,787.09
Totals	$1,687,140.00	$510,288.00	$1,176,852.00		$97,176.50

15. The Division issued a Notice of Determination dated February 3, 2000 against petitioner Rodos Foods, Inc., asserting additional sales and use tax due of $97,176.50 for the three-year period, December 1, 1995 through November 30, 1998, as detailed above, plus interest and penalties. Penalties were imposed for underpayment of tax, including the omnibus penalty since additional tax due was more than 25 percent of the audited tax due. A couple of weeks later, the Division issued a Notice of Determination dated February 25, 2000 against petitioner Nick Tsigos, as an officer or responsible person liable for taxes determined to be due from the corporate petitioner,[3] asserting additional sales and use tax due of $65,573.65 for the two-year period, December 1, 1996 through November 30, 1998, as detailed above, plus interest and penalties. Penalties were again imposed for underpayment of tax, including the omnibus penalty since additional tax due was more than 25 percent of the audited tax due.

16. Customers of the Cosmos Café include students attending the State University of New York at Stony Brook which is nearby. On April 22, 1999, the day of the observation test, the university was in session. In the course of a calendar year, the university is closed for several weeks.

SUMMARY OF THE PARTIES' POSITIONS

17. The Division maintains that "the method of estimation used by the Division was reasonable and petitioners have not proven that the method used by the Division was erroneous or that the tax due is less than that assessed" (Division's brief, p. 13). The Division emphasizes

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[3] Petitioner Nick Tsigos has not contested his status as an officer or responsible person for the corporate taxpayer.

that petitioners' minimal introduction of evidence was "hardly clear and convincing evidence" (Division's brief, pp. 16-17). It points out that little, if any, weight should be given to petitioners' sole witness, Mr. Levitch, who "admitted that he had no personal knowledge about the business, other than its location near SUNY Stony Brook" (Division's brief, p. 17). The schedule alleged by petitioners to represent its sales during 1998 was not credible evidence according to the Division: "Petitioners' self-serving records of sales, which were not produced on audit, do not constitute clear and convincing evidence" (Division's brief, p. 17). The Division further contends that penalties should be sustained especially in light of the admission at hearing that the restaurant's sales were "substantially and consistently under reported" (Division's brief, p. 20). An analysis by the auditor of petitioners' schedule of its 1998 sales, as introduced at the hearing, noted that:

> During the [three year] audit period (12/1/95-11/30/98), the company reported taxable sales of $471,840. Petitioner now claims . . . that its taxable sales for Calendar Year 1998 were $265,118. If the $265,118 annual amount is extrapolated over the three-year audit period, the taxable sales for three years would be $795,354 ($265,118 X 3). $795,354 is 69% higher than the $471,840 that the company reported.

18. In its response to the Division's brief, petitioners point to "a second physical observation on Tuesday, February 26, 2002, for the period December 1, 1998 to November 30, 2001" (Petitioners' response, p. 1). According to petitioners, the second observation resulted in taxable sales of $844.00 per day, and they attached an exhibit to their response detailing a computation of additional tax due for this later audit period. Further, petitioners contend that the auditor incorrectly applied the same hourly sales to the period from 9:00 P.M. to 12 A.M. since "[t]he restaurant serves mainly snacks after 9 pm" (Petitioners' response, p. 2). They also contend that the auditor incorrectly used the daily sales determined on the observation test day for every day of the calendar year without making adjustments for the period when the

university is closed or in summer session and for weekend days when the university's many commuter students are not present.

CONCLUSIONS OF LAW

A. Every person required to collect sales tax must maintain records sufficient to verify all transactions, in a manner suitable to determine the correct amount of tax due (Tax Law § 1135[a][1]). As noted in Findings of Fact "4" and "5", petitioners failed to provide to the auditor any records to substantiate sales such as cash register tapes, guest checks, cash receipts, sales journal, or day book. The records that were provided were not even reconcilable with bank statements. At the hearing, petitioners brought forward for the first time cash register tapes for which no testimony was offered to establish their relevancy. Notably, petitioner Nick Tsigos, who operated the restaurant, chose not to appear at the hearing to testify concerning these tapes, and given such failure to explain why, when, how and where they were created, along with their late production, they were properly accorded no weight (***see, Meixsell v. Commissioner of Taxation***, 240 AD2d 860, 659 NYS2d 325, ***lv denied*** 91 NY2d 811, 671 NYS2d 714; ***Matter of Greenwald***, Tax Appeals Tribunal, November 24, 1993). Consequently, the Division of Taxation's right to resort to an estimate of the restaurant's sales, as long as it selected an audit method reasonably calculated to reflect the sales and use taxes due, remains unassailable (**see, *Matter of Grant v. Joseph***, 2 NY2d 196, 204, 159 NYS2d 150, 157, ***cert denied*** 355 US 869).

B. The one-day observation test described in detail in Findings of Fact "8" through "10" was carefully performed by the Division, despite the active steps taken by Mr. Tsigos to impede its proper performance, and the test provided a reasonable basis for estimating the restaurant's taxable sales (***see, Matter of Agnone***, Tax Appeals Tribunal, January 23, 1992 [wherein the Tribunal upheld the results of a one-day observation test and noted that precision in determining taxable sales was not required when lack of adequate records required the estimation of taxable sales]; ***Matter of Sarantopoulos***, Tax Appeals Tribunal, February 28, 1991 [one-day observation test upheld]). Further, it was entirely reasonable for the auditor to apply the same hourly sales rate to the period from 9:00 P.M. to 12:00 A.M. as a consequence of the premature closing of the restaurant by Mr. Tsigos, which made it impossible for the investigator to observe the sales during such three-hour period.

C. Since it is concluded that the audit method was reasonable, petitioners 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, supra***). Petitioners' failure to produce any evidence, other than the academic calendar for the nearby university and the minimal testimony of their representative, who lacked personal knowledge concerning the restaurant's operation, fell far short of meeting this fairly substantial burden (***see, Center Moriches Monument Co. v. Commr. of Taxation & Fin.***, 211 AD2d 947, 621 NYS2d 720). Although it would seem that the restaurant's sales on days that the university was not in session would be less than on days when it was in session, there is no evidence in the record to support a specific percentage reduction in the restaurant's sales for days that the university was not in session (***see, Matter of Spartan Coffee Shop***, Tax Appeals Tribunal, September 14, 1989 [wherein the administrative judge was reversed for reducing an assessment by various percentages where there was no *evidence* to support such reduction]). As noted in Conclusion of Law "A", the register tapes brought forward by petitioners at the hearing may be given no weight. Furthermore, the evidence concerning a second observation test in early 2002, which was attached by petitioners to their brief, may be given no weight because the record was closed to any additional evidence at the hearing other than the auditor's analysis of petitioners' schedule analyzing the register tapes, which they did not produce during the audit process but rather presented at the hearing for the first time (***see, Matter of Ronon***, Tax Appeals Tribunal, October 24, 2002). In contrast, the Division specifically requested permission at the hearing to submit an analysis by the auditor in the form of an affidavit of a schedule and tapes produced by petitioners for the first time at the hearing, and it was reasonable to grant such request. As the Tax Appeals Tribunal emphasized in its recent decision in ***Matter of Ronon (supra)***:

> We have held that a fair and efficient hearing process must be defined and final, and the acceptance of evidence after the record is closed is not helpful towards that end and does not provide an opportunity for the adversary to question the evidence on the record [citations omitted].

In sum, since petitioners' representative was advised at the hearing that no further evidence would be accepted into the record, and he indicated his understanding of such limitation and made no request for permission to submit any additional evidence, the evidence concerning a second observation test attached to petitioners' brief may be given no weight.

D. Finally, petitioners' substantial underreporting of taxable sales, well in excess of 25%, justified the imposition of penalties under Tax Law § 1145, including the omnibus penalties.

E. The petitions of Nick Tsigos and Rodos Foods, Inc. are denied, and the respective notices of determination dated February 25, 2000 and February 3, 2000 are sustained.

DATED: Troy, New York
November 27, 2002

/s/ Frank W. Barrie
ADMINISTRATIVE LAW JUDGE