

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petition	:	
of	:	
<b>INDIAN CURRY MAHAL, INC.</b>	:	SMALL CLAIMS DETERMINATION DTA NO. 821566
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 September 1, 2002 to May 31, 2005.	:	

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Petitioner, Indian Curry Mahal, 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 September 1, 2002 to May 31, 2005.

A small claims hearing was held before James Hoefler, Presiding Officer, at the offices of the Division of Tax Appeals, 90 South Ridge Street, Rye Brook, New York, on November 13, 2007 at 1:30 P.M. Petitioner appeared by George J. Silverman, CPA. The Division of Taxation appeared by Daniel Smirlock, Esq. (Leon Drucker and Chae Kuo).

Since neither party elected to reserve time to file a post hearing brief, the three-month period for the issuance of this determination commenced as of the date the hearing was held.

***ISSUE***

Whether the Division of Taxation properly determined that petitioner underreported its sales, and corresponding sales tax liability, through the use of indirect audit methods, specifically, a rent factor audit methodology.

***FINDINGS OF FACT***

1. Petitioner, Indian Curry Mahal, Inc., was formed in 1998 pursuant to the Business Corporation Laws of the State of New York. Since its inception, petitioner has continuously operated a small restaurant located at 78 Second Avenue, New York, New York, which, as its name suggests, specializes in Indian cuisine.

2. On June 13, 2002, an investigator from the Division of Taxation (Division) visited petitioner's premises and his report, based on a conversation with the owner, noted that the restaurant was approximately 15 feet wide by 50 feet long, had 4 employees, was open 7 days a week from noon to midnight and had 8 tables each seating up to 4 customers. The investigator noted in the comments section of the report that petitioner reported gross sales of \$10,966.00 for the quarter ending February 28, 2002, an average of \$121.00 per day, and that "sales reported are too low for the location. Sales tax audit recommended." On February 1, 2005, a second investigator conducted a visual observation of petitioner's lunch and dinner business. The investigator noted that from 12:17 P.M., the time petitioner opened for business, until 3:00 P.M., it had 8 walk-in customers and 12 deliveries. The dinner observation, from 6:00 P.M. until 8:00 P.M., revealed that petitioner had eight walk-in customers and nine deliveries. The visual observation did not record or otherwise note the amount of each sale.

3. On August 22, 2005, the Division initiated a field audit of petitioner's books and records to determine if it had collected and remitted the proper sales and use taxes due for the 33-month period September 1, 2002 through May 31, 2005. Initially, the auditor noted that petitioner had filed sales and use tax returns for the audit period reporting total gross and taxable sales of \$161,106.00, an average of \$160.46 per day. It was also determined on audit that a detailed review of sales could not be performed since petitioner's books and records were

incomplete and inadequate. Specifically, the auditor found that petitioner did not have or produce for audit daily cash register tapes, sales invoices, guest checks or purchase invoices.

4. After reviewing petitioner's operations, the Division decided to use a rent factor of 6.8% to compute petitioner's sales for the audit period. Using the "Retail Trade - Other Food Stores - Table 1" section of the 28<sup>th</sup> Edition (1997) Almanac of Business and Industrial Financial Ratios, the Division found that the annual rent expense for 21,198 other food stores with money amounts and size of assets under \$100,000.00 was 6.8% of operating income. This data was taken from the accounting period July 1993 to June 1994. The Division determined on audit that petitioner's rent was \$1,600.00 per month, or \$52,800.00 for the audit period (\$1,600.00 x 33 months). The \$52,800.00 in rent charges for the audit period was divided by the rent factor of 6.8% to compute audited gross sales of \$776,470.00. Reported sales of \$161,106.00 were subtracted from audited sales to produce additional taxable sales of \$615,364.00. Applying the 8.625% sales tax rate to additional taxable sales produced a tax due of \$52,620.64.

5. On March 2, 2006, the Division issued a Notice of Determination to petitioner asserting that it owed \$52,620.64 in sales tax due, plus penalty of \$14,287.92 and interest of \$15,945.85. The Notice of Determination advised petitioner that "since you have not submitted adequate records for audit . . . we determined that you owe tax, interest, and any applicable penalties . . . based upon available records and information."

6. It is undisputed in this matter that petitioner did not maintain adequate records of its sales for the period in question. In an effort to reconstruct credit card sales, petitioner submitted in evidence copies of monthly bank statements for one checking account for the entire audit period. Deposits made into this checking account total \$156,369.00. Cash sales of \$54,906.00, a figure which was provided by petitioner to its representative, were added to the deposits into the

checking account to arrive at total revenue, including sales tax and tips, of \$211,275.00. When tax and tips are backed out of the total revenue figure, petitioner arrives at a gross sales figure of \$160,569.00, an amount almost identical to the \$161,106.00 in gross and taxable sales reported on its sales and use tax returns for the period at issue.

7. Petitioner also submitted into evidence various documents to establish that in the restaurant industry credit card sales are approximately 70% to 80% of total sales. Petitioner introduced into evidence its sales records for the months of September and October 2007 to support that credit card sales were 62.90% for September 2007 and 64.50% for October 2007. The Division does not dispute that in the restaurant industry that 70% to 80% of total sales are made by credit card.

#### ***SUMMARY OF PETITIONER'S POSITION***

8. Petitioner maintains that all deposits into its checking account have been verified by bank statements and that these statements should be accepted as a complete and accurate record of all credit card sales. Since it is undisputed that credit card sales represent 70% to 80% of all sales, petitioner argues that its cash sales can be easily calculated to be between \$39,092.00 (using 80%) and \$67,015.00 (using 70%). Petitioner posits that since its claimed cash sales of \$54,906.00 clearly fall within the undisputed 70% to 80% range, its sales, as reported on its sales and use tax returns, should be accepted as filed and that the Division's assessment, based on the use of a rent factor, is in error and should be canceled.

#### ***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 request 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 gross and taxable sales for the audit period including, most tellingly, any records of sales. Having established the unavailability of required books and records, the Division was clearly entitled to resort to the use of indirect methods, including the use of a rent factor, to determine petitioner's sales and sales tax liability. In fact, the Division's authority to do so has been consistently sustained (*see Matter of Del's Mini Deli, Inc. v. Commissioner of Taxation and Finance*, 205 AD2d 989, 613 NYS2d 967 [1994]; *Matter of Vebole Edibles v. Tax Appeals Tribunal*, 162 AD2d 765, 557 NYS2d 678

[1990]; *Matter of Sarantopoulos v. Tax Appeals Tribunal*, 186 AD2d 878, 589 NYS2d 102 [1992]) and the use of a rent factor has been specifically addressed and approved (*see Matter of Constantini*, Tax Appeals Tribunal, January 10, 2008; *Matter of Your Own Choice, Inc.*, Tax Appeals Tribunal, February 20, 2003; *Matter of Bitable on Broadway, Inc.*, Tax Appeals Tribunal, January 23, 1992). In view of the foregoing, the only questions presented in this case are whether petitioner has established that the audit method employed was unreasonable and whether the amount of tax assessed as the result of the application of the method used in this case was erroneous (*Matter of Surface Line Operators Fraternal Organization v. Tully, supra.*).

C. Petitioner has not established that the audit method was unreasonable or that the amount of tax determined by application of such method was erroneous. For the period in question, petitioner admittedly did not maintain any record of sales as required by the Tax Law. Petitioner's attempt to reconstruct sales through the use of deposits into a checking account and then backing into cash sales by use of percentages is simply insufficient to meet its burden of showing that the audit method utilized by the Division was unreasonable and the amount of tax assessed was erroneous. The indirect method used by petitioner to reconstruct its sales assumes that all credit card sales were deposited into the one checking account introduced into evidence and that its percentage of cash sales fell within the industry standard. Having established the inadequacies of a taxpayer's records, the Division is under no obligation to utilize one indirect method of audit as opposed to another, but rather must only select a method of audit reasonably calculated to determine the amount of tax due (*Matter of Grant Co. v. Joseph, supra.*) Without any record of sales, it is not possible to determine which indirect method is more accurate. Under these circumstances, the Division's resort to a rent factor to determine sales was entirely reasonable. Furthermore, as a general proposition, any imprecision in the results of an audit

arising by reason of a taxpayer's own failure to keep and maintain records of all of its sales as required by Tax Law § 1135(a)(1) must be borne by that taxpayer (*Matter of Markowitz v. State Tax Commission, supra., Matter of Meyer, supra.*).

D. I also note that the investigator who performed the lunch and dinner observation on February 1, 2005, noted a total of 16 walk-in customers and 21 deliveries during her 5-hour observation. Initially, it must be noted that petitioner was open 12 hours a day, and therefore the 5-hour observation period cannot be reflective of all of petitioner's sales on this day. A review of petitioner's menu reveals that the 68 entrees included thereon have an average price of \$7.74. Assuming that each of the 37 transactions observed on February 1, 2005 resulted in a minimum sale of \$10.00, total sales for this 5-hour observation period would be \$370.00, an amount more than double the \$160.46 daily sales reported by petitioner during the audit period. Accordingly, there is ample evidence to suggest that petitioner's reported sales are indeed understated.

E. The petition of Indian Curry Mahal, Inc. is denied and the Division's Notice of Determination dated March 2, 2006 is sustained.

DATED: Troy, New York  
February 7, 2008

/s/ James Hoefler  
PRESIDING OFFICER