STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
GREYSTOKE INDUSTRIES LLC D/B/A PARADISE FOUND	:	DETERMINATION
	:	DTA NO. 822532
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, 2003 through May 31, 2006.	:	
	:	

Petitioner, Greystoke Industries LLC d/b/a Paradise Found, 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, 2003 through May 31, 2006.

A hearing was held before Brian L. Friedman, Administrative Law Judge, at 183 East Main Street, Suite 1500, Rochester, New York, on July 21, 2009 at 10:30 A.M., with all briefs to be submitted by December 30, 2009, which date began the six-month period for the issuance of this determination. Petitioner appeared by Bond, Schoeneck & King, PLLC (Jonathan B. Fellows, Esq., and Courtney Alan Wellar, Esq., of counsel). The Division of Taxation appeared by Daniel Smirlock, Esq. (Osborne Jack, Esq., of counsel). Administrative Law Judge Friedman retired from State service during the pendency of this matter and the same was transferred to Dennis M. Galliher, Administrative Law Judge. After review of the evidence and arguments, Judge Galliher renders the following determination.

ISSUES

I. Whether the Division of Taxation has established that the door admissions and fees for private dances collected by petitioner from its customers are subject to sales tax pursuant to Tax Law § 1105(f)(1) as admission charges to a place of amusement, or whether petitioner has established entitlement to the exemption provided under the same section for admission charges to a dramatic or musical arts performance.

II. Whether the Division of Taxation has established that the door admissions and fees for private dances collected by petitioner from its customers are subject to sales tax pursuant to Tax Law § 1105(f)(3) as amounts paid as charges of a roof garden, cabaret or other similar place.

III. Whether the Division of Taxation has established that the door admissions and fees for private dances collected by petitioner from its customers are subject to sales tax pursuant to Tax Law § 1105(d)(1), as cover, minimum, entertainment or other charges made to patrons in an establishment which provides taxable food or beverages.

IV. Whether the audit methodology utilized by the Division of Taxation, to wit, a full-day observation and recording of petitioner's receipts conducted shortly after the end of the audit period, should be either adjusted or rejected as unreasonable for failing to account for growth in petitioner's business over the course of the audit period and for failing to reflect that petitioner's business is a "seasonal" business.

V. Whether, assuming the charges and fees in issue are subject to sales tax, the liability therefor properly rests not with petitioner but rather with the entertainers, who perform at petitioner's premises but are not employees of the petitioner.

FINDINGS OF FACT

1. Petitioner, Greystoke Industries LLC doing business as Paradise Found, operated an adult entertainment establishment, referred to as an adult juice club, located in Syracuse, New York, offering entertainment in the form of nude and semi-nude exotic dancing by females during the audit period at issue, June 1, 2003 through May 31, 2006. The entertainment provided at petitioner's premises consists of dancers performing routines in costume for a portion of the time, and in the nude for the balance of the time, in both the public stage and surrounding areas of the premises as well as in the private rooms located in the premises. Since petitioner offered nude entertainment, it was not allowed to sell alcoholic beverages and hence served only bottled water, juices, soda and other nonalcoholic beverages. Petitioner's business was open from approximately 5:00 P.M. to 4:00 A.M., seven days per week.

2. To gain entry into petitioner's club customers paid a general admission door charge, the amount of which varied among $5.00, $8.00 and $10.00 depending upon the time of entry. Customers could also purchase, at the time of entry, special packages, which included chips entitling them to a private or "lap" dance performed on a "one-on-one" basis in a small private or VIP room.[1] As described more fully hereinafter, customers could, and were encouraged to, purchase such private dances at any time they were in the premises.

3. By an appointment letter dated May 5, 2006, the Division of Taxation (Division) scheduled a June 21, 2006 sales and use tax field audit of petitioner's business for the period spanning June 1, 2003 through February 28, 2006. Subsequent identical appointment letters dated May 18, 2006 and June 19, 2006 were issued changing the appointment date to June 20,

[1] The record also notes the existence of an "Oasis" room. There is scant detail in the record on this, but it appears that the same was a larger or more luxurious version of the VIP rooms utilized for private lap dances.

2006 and thereafter to July 11, 2006, respectively. Each of these appointment letters was accompanied by a Records Required List, detailing the documents petitioner was expected to have available for review.

4. At the July 11, 2006 audit appointment, petitioner provided incomplete purchase records, incomplete bank statements, and Excel spread sheets in support of its sales receipts. Petitioner did not provide sales invoices or other original source documents of sales, and advised that cash register tapes of its receipts were not available because they had been destroyed in a flood in the manager's office at the premises.

5. The Division reviewed the books and records provided and informed petitioner that the same were insufficient for the conduct of a detailed audit. By a letter dated July 17, 2006, the Division advised petitioner that due to such insufficiency, an observation of petitioner's sales activity would be conducted for an entire day at petitioner's place of business.

6. On August 11, 2006, the Division utilized five auditors and conducted an observation of petitioner's business, recording petitioner's receipts for door admissions, including special packages purchased at the door, beverage sales receipts, and fees for private dances, between the hours of 5:00 P.M. (opening) and 4:00 A.M. (closing).[2] This observation resulted in total sales receipts of $4,492.00, consisting of door admission receipts of $978.00, beverage receipts of $314.00, and private dance receipts of $3,200.00. All such sales receipts were considered by the Division's auditors to be subject to sales tax. One of the auditors observed that by 12:45 A.M. on the observation date, there were no entertainers on the floor of the club, as opposed to an average of four to six dancers observed on the floor during the hours prior to that time, and in

[2] Petitioner's hours of operation in fact caused the observation audit to span two dates (i.e., August 11 and 12, 2006). However, since the audit encompassed a full "day" cycle of operation, it is referred to herein simply as the "observation date."

contrast to advertisements that 20 girls were present on Friday and Saturday nights. At 2:30 A.M., the auditor noted that the "door woman" was informing customers that there were only four dancers working that night. At 3:15 A.M., he observed that customers returned to the door area to complain that there were only two dancers working. Shortly thereafter, he noted that there was only one dancer available to perform private dances and that there were five customers waiting for private dances.

7. The Division utilized petitioner's summary spread sheets, listing petitioner's claimed sales (money collected) for the audit period, and determined therefrom that sales on Fridays were, on average, 22.5% of petitioner's weekly sales. Utilizing this information, the Division determined weekly sales to be $19,920.18, and multiplied this amount by 13 (weeks per sales tax quarterly period) to arrive at audited quarterly sales of $258,962.00. After making allowance reductions for legal holidays and other days when the business was closed, the Division calculated audited taxable sales of $3,079,460.00 for the audit period. This amount was reduced by reported taxable sales ($402,111.00), resulting in additional taxable sales of $2,677,349.00 and additional tax due in the amount of $207,321.27.

8. On May 7, 2007, the Division issued to petitioner a Notice of Determination, based on the results of the foregoing audit, assessing additional tax due for the period June 1, 2003 through May 31, 2006 in the amount of $207,321.27, plus penalty and interest. The initial audit appointment and records request letters had specified the period of audit as spanning June 1, 2003 through February 28, 2006 (***see*** Finding of Fact 3). However, by a letter dated April 24, 2008, i.e., subsequent to the issuance of the notice, the Division advised petitioner that the audit period was being extended to include the sales tax quarterly period spanning March 1, 2006 through May 31, 2006. At hearing, the Division admitted that this extension did not include a

proper preceding request for petitioner's records and thus conceded that the tax assessed for such quarterly period ($17,450,27), plus penalty and interest thereon, should be eliminated from the amount at issue herein. Accordingly, the amount of tax at issue has been reduced from $207,321.27 to $189,871.00, plus penalty and interest.

9. Petitioner purchased the club, formerly known as Moulin Rouge, shortly before the beginning of the audit period. Petitioner changed the name of the club to Paradise Found. Subsequent to purchasing the club, petitioner made certain renovations, including changing the club interior to a tropical theme and replacing the exterior siding. Petitioner installed an automated teller machine (ATM) inside the premises, added a large exterior neon sign to advertise the club's presence, and also established radio, television and billboard advertising.

10. Petitioner's club is decorated in a Polynesian/tropical theme. Upon entering the club, customers are able to see entertainers dancing on a main stage, either singly or, on occasion, with another entertainer. The main stage is a "T" shaped raised area consisting of approximately 500 square feet with a large rectangle forming the top of the T and an approximately 36-square foot (3 feet by 12 feet) runway that extends outward from the rectangle at the top of the T. There is a floor to ceiling brass pole in the main rectangle area of the stage, and many of the entertainers incorporate the pole into routines they perform while on stage. The back wall of the main stage is covered with mirrors. The main stage is accessed by the entertainers either directly from the dressing rooms or from a small set of stairs that lead to the main floor of the club. The main stage has a multitude of lights (e.g., spot lights, strobe lights, etc.) in a variety of different colors. There is a professional sound system that is operated by a DJ (disc jockey) from a booth overlooking the main stage. The main stage is surrounded by chairs, and there are booths from which customers are able to watch the dancers. The chairs surrounding the main stage are

separated from the stage by a brass "tipping rail," at which customers may offer tips to the dancers. There is a large bar adjacent to the main stage with stools around it. As noted, petitioner sells bottled water, soda, juices and other nonalcoholic beverages to its customers. There is no charge, other than the door admission charge, to a customer to view the entertainers on or in the areas adjacent to the main stage.

11. An entertainer's work schedule at petitioner's club is generally broken out into two "sets" (or shifts), typically from the 5:00 P.M. opening time until approximately 10:00 P.M. and then from 10:00 P.M. through the 4:00 A.M. closing time. Dancers sign up in advance and may choose to work either of such shifts or to work both shifts. A dancer typically performs on the main stage for approximately 12 to 15 minutes. This period is also known as a "set," and on a busy night, a dancer will typically do one or two, or occasionally three, such sets. The dancer chooses the music to which she will dance, which is played by the DJ while she is on the main stage, and also selects the attire or "costume" she will wear.

12. In addition to the main stage, entertainers also may perform dances in the area of tables and booths adjacent to the main stage, as well as in the private or VIP rooms. Customers may secure private dances in these rooms by purchasing chips from the dancers or from the bartenders. Dancers will typically mingle and engage in conversation or flirting with customers seated in the chairs surrounding the main stage, in the booths, or at the bar after, or between, the times when a dancer is performing a set on the main stage. The dancers seek, by this activity, to entice the patrons to purchase private dances. Testimony at hearing established that the dancers view the main stage performance as an "advertisement" for themselves from which customers will want to purchase private dances, which constitute, along with the receipt of tips, the two means by which a dancer may earn money. In this regard, testimony from one of the entertainers

who performed at petitioner's club described this customer/entertainer interaction as a "sales pitch," whereas petitioner's expert witness described the same in testimony as "kind of like an 'intermission' from the staged, choreographed dance or the choreographed private dance."

13. Customers are able to select a particular entertainer to perform a private dance. The charge for an initial private dance with a particular dancer was $21.00, of which $1.00 went to the bartender, with the balance ($20.00) split equally between petitioner and the dancer. Customers may remain in a private room by purchasing additional private dances from the same dancer at $20.00 per dance, with the split for such additional dances being $5.00 to petitioner and $15.00 to the dancer. A customer leaving a private room and then reentering a private room with a different dancer would apparently return to the initial charge of $20.00 plus $1.00, with the same split between the dancer and petitioner as described herein for the initial and any subsequent dances. The auditors noted a sign in the club advising of the $20.00 price for a private dance. Money given by customers to the dancers is thereafter turned over to the bartenders by the dancers. The bartenders track the number of private dances and, at the end of a dancer's set, pay over the dancer's share to the dancer.

14. Petitioner's club has ten private rooms. The private rooms average approximately 50 square feet in size and have a chair or couch for the customer to sit on and an area in front of the chair or couch for the entertainer. There is a curtain across the entrance to each private room allowing for privacy. There is white and colored lighting (including black lighting) which can be controlled by the entertainer. Each private dance lasts approximately three minutes, the music is prerecorded and prearranged, repeats periodically and is familiar to, though not controlled by, the dancer. When a new song starts, the entertainer begins her dance for the customer such that the customer is then receiving the full length of the song (and any additional songs or dances

purchased) as their private dance. Contact between the customer and the entertainer may include the entertainer sitting on the customer's lap (hence the term "lap dance") or putting her arms around the customer. Activities in the private rooms are monitored for security purposes by petitioner's personnel via video cameras and display screens. To protect the privacy of its customers, petitioner does not record or maintain recordings of such video monitored activities.

15. Entertainers typically perform dances on the main stage and in the private rooms, although dances are also sometimes performed on the main floor of the club, near the bar, or around the booths. Petitioner's bartenders utilize a computer system to keep track of the monies paid for private dances, but do not track the monies paid by the customers as tips to the dancers. According to testimony provided by one of petitioner's entertainers, there is a computer terminal located at the end of the bar area that the dancers can access to determine the amount of money they have earned during the course of a given set. The record is not entirely clear as to whether this computer system is tied to the cash registers and thus would have generated the cash register tape receipts which were described as destroyed in a flood at the premises. Petitioner's owner noted that he transferred the sales information from the cash register receipts to Excel spread sheets each day or every few days as time permitted.

16. The entertainers who perform at petitioner's club enter into an Entertainment Lease with petitioner, pursuant to which the entertainer schedules herself to perform on certain days and agrees to be at petitioner's club on those days and available to perform for a minimum of six consecutive hours (i.e., a set). The relationship between petitioner and each entertainer is described as that of landlord and tenant involving the "joint and non-exclusive" leasing of portions of the club to each of the various entertainers to perform in the manner described herein. The Entertainment Lease provides that the entertainers are not employees of petitioner, as

differentiated from the door host, bartenders, security personnel, DJ and manager, who are employees. Each entertainer determines what days and hours (sets) she wishes to perform at the club, when during such time she will actually dance, where she will dance, the music that is to be played while she is dancing (on the main stage), who she will provide private dances for, what she will wear while dancing, and the duration and type of dance she will perform. The entertainers are not prohibited from dancing at other clubs. The Entertainment Lease does not specify the amount to be charged for a private dance. However, as noted previously, the $20.00 amount for such dances is set by petitioner (***see*** Finding of Fact 13).

17. Pursuant to Addendum A of the Entertainment Lease, the entertainers pay a weekly fee of $60.00 to petitioner, plus $10.00 for each set performed. If an entertainer performs five or more sets in a given week, the weekly fee is reduced to $10.00, with the $10.00 per set fee remaining the same. In each instance the fee paid by the entertainer to petitioner is described in the Entertainment Lease as a rental fee or an additional rental fee.[3]

18. The entertainers generate revenue for themselves via tips from customers while dancing on or in the areas adjacent to the main stage, and from fees and tips for dancing off the main stage, including private dances. Petitioner, by contrast, generates receipts from three sources consisting of door admission charges, beverage sales, and from the fees for private dances. As determined from the results of the observation audit, approximately 71 percent of petitioner's receipts were derived from the fees for private dances ($3,200.00 out of total observed receipts of $4,492.00). In addition, approximately 21 percent of petitioner's receipts were derived from the door admission charges ($978.00 out of total observed receipts of

[3] The addendum also provides that the entertainers will pay a fee ($65.00 per 15 minutes or $110.00 per 30 minutes) for the Oasis Suite.

$4,492.00). The door admission charges are collected by petitioner at the main entrance to the club, and payment of this charge permits customers to access the public areas of the club, but does not entitle the customer to access the private rooms. Rather, such access follows the purchase of a private dance, with continued access to and presence in the private rooms premised upon the purchase of additional private dances. When petitioner purchased the club, it continued the practices of the prior owner with respect to sales tax and paid sales tax, allegedly erroneously, on the reported door admission charges it collected. Petitioner also sells nonalcoholic beverages, as described. The results of the observation audit determined that approximately seven percent of petitioner's revenue was derived from the sale of beverages ($314.00 out of total observed receipts of $4,492.00). Petitioner paid sales tax on its reported beverage sales.

19. Petitioner introduced into evidence a DVD containing five video clips to illustrate the types of dance techniques typically employed by the entertainers. Four of the video clips depict routines being performed on petitioner's main stage and one of the video clips depicts a private dance. Three of the four main stage video clips depict individual entertainers performing movements as described utilizing or centering on the brass pole, while one of the four main stage video clips depicts two dancers who appear to be practicing movements utilizing the brass pole. Petitioner's premises appear to be empty or nearly empty of customers in these video clips, and there is no interaction between the entertainers and any customers. The other video clip depicts a dance performed in one of petitioner's private rooms for an individual customer. This video clip depicts a customer seated in a chair, observing an entertainer located directly in front of the customer and moving to the music being played while removing a portion of her costume. As with the other video clips, there is no contact or interaction between the entertainer and the

customer such as was described as occurring either when an entertainer is on the main stage, or in the areas surrounding the main stage, the booths or at the bar, or as was described to occur during a lap dance (***see*** Findings of Fact 12 and 14).

20. One of petitioner's owners, who also serves as its general manager, provided many of the details of petitioner's business. He is responsible for the day-to-day business management and handles the bookkeeping for petitioner. He explained that petitioner's business had increased over the period of time covered by the audit, noting that petitioner hired additional security personnel and added an additional bartender in order to service people who lined up around the bar. He noted that the club was busiest between the hours of 10:30 P.M. and 2:30 A.M. and, with regard to the auditor's observations concerning the number of dancers working in the latter part of the second set on the observation date, stated that the "downside" of petitioner's relationship with the entertainers is that "I can't control them within the club and tell them they have to get out of the dressing room and go to the floor." He also maintained that petitioner's business is "seasonal," with summer being its busiest period.

21. Judith Lynne Hanna, PhD, a cultural anthropologist, was retained by petitioner to express an opinion in this matter based upon her expertise as an anthropologist, dance scholar and dance critic. Dr. Hanna earned a master's degree in anthropology from Columbia University in 1975 and a doctoral degree in anthropology from Columbia University in 1976, specializing in nonverbal communication and the arts and society. Her doctoral dissertation was on a group's choreography and its meaning and style. She is a senior research scholar in the Department of Dance and an affiliate in the Department of Anthropology at the University of Maryland, College Park, Maryland. Dr. Hanna has training in a multitude of dance genres, has taught dance as well as courses on dance theory at the college level, and has continually conducted teacher and youth

dance workshops. She has served as a dance consultant and critic, has written 6 books on dance, published more than 150 articles in dance periodicals, and written many reviews and commentaries on dance. Since 1995, Dr. Hanna has been conducting on-site research on exotic dance and adult entertainment. Along with the research approach she has taken with other forms of dance, she has examined the characteristics and choreography of exotic dance. Dr. Hanna has been retained on 45 occasions as an expert in court matters relating specifically to exotic dance and was accepted as an expert in this field for this matter.

22. Dr. Hanna prepared for her testimony in this matter by reviewing six videos, provided to her by petitioner, which depicted four main stage performances and two private dances. She also observed nine dances (eight main stage dances and one private dance) performed at petitioner's premises. She also spent time interviewing the dancers about their backgrounds and training.

23. Dr. Hanna stated that exotic dance contains many of the attributes of ballet and other forms of dancing, including movement, balance, dissonance, symbolism and emotion. She described this as a choreography, or arrangement, of about 61 different moves with theme and variation patterns with repetition. She identified the use of locomotion, gesture, pole, mirror and floor work at variable levels in response to the music being played. Dr. Hanna stated that exotic dance is theater in the sense that there is an admission charge, a raised stage, special lighting, dressing rooms, a professional sound system and a disc jockey. She explained that the entertainers' dance routines include dance moves from a variety of well recognized disciplines, including ballroom dance, gymnastics, cheerleading, belly dancing, tap, jazz, ballet and burlesque, and include arm extensions, overhead movements, undulations, hip movements, struts, shimmies, and hair tosses. The entertainers have a variety of backgrounds, training and

levels of dance experience. Some have training in gymnastics, ballet, jazz, or exotic dance and refine their routines within the parameters set forth by the club, advancing their own ability and creativity over time. New steps and routines are often learned from videos, from YouTube, and from other dancers.

24. Dr. Hanna's report discussed dance in general, and exotic dance in great detail. She noted that adult or exotic dance has a less formalized repertoire of moves than other forms of dance (e.g., ballet), that there is a range in the quality of the dances performed by different entertainers, and that a large number of entertainers have no formal training in dance. Her report focused on the sequential parts of the performance, the messages of the performer, the skill it takes to perform dance routines, and the psychology of dance and its effect on the viewers. She set forth a description in detail of the choreographed sequence for each dancer and the dance that she reviewed and discussed the various characteristics of the dancers' choreography. Dr. Hanna concluded that the presentations at petitioner's premises are live dramatic choreographic performances in a theater which has shows that consist entirely of dance routines.

25. In contrast and response to the Division's audit, petitioner presented its own analysis and calculations in support of the claim that the Division's audit unreasonably overstates the amount of tax due by failing to account for growth in revenue over the audit period. Petitioner's premise is that receipts and, consequently, any sales tax due thereon were less at the beginning of the audit period when petitioner first operated the club and thereafter increased, based on improvements made by petitioner to the club, over time to a level closer to that observed upon audit. In support of this argument, petitioner calculated $87,025.30 as audited taxable sales for the month of August 2006 (based on the Division's August 11, 2006 observation). In turn, petitioner calculated the percentage relationship between such audited taxable sales and its

$27,259.83 payroll for August 2006 ($87,025.30 ÷ $27,259.83 = 319.24%), and also calculated the percentage relationship between such audited taxable sales and the $49,380.00 of ATM cash withdrawals for August 2006 ($87,025.30 ÷ 49,380.00 = 176.24%). Petitioner then applied these resulting percentage amounts, 319.24% and 176.24%, to its quarterly payroll and to its quarterly ATM withdrawals, respectively, over the course of the audit period, to calculate "taxable sales adjusted to reflect growth." Such "adjusted" taxable sales totals were reduced in each instance by reported taxable sales, to arrive at additional taxable sales and additional tax due in the respective amounts of $39,877.00 (based upon payroll growth adjustment), and $67,836.00 (based upon increased ATM withdrawals). Petitioner also determined the average of the two foregoing percentage amounts (319.24% + 176.24% ÷ 2 = 247.74%) and, using the foregoing methodology, applied such percentage to its quarterly payroll plus its quarterly ATM withdrawals to arrive at additional taxable sales and additional tax due in the amount of $53,856.00.

CONCLUSIONS OF LAW

A. The primary issue in this matter is whether the door admission fees collected at the main entrance to petitioner's premises and the fees collected for private dances are subject to sales tax. Petitioner has also raised the issue of whether the indirect audit method employed by the Division was unreasonable in its result for lack of any adjustment to reflect growth in petitioner's business over the period of the audit and for the alleged "seasonal" nature of petitioner's business. Finally, petitioner has argued that if the charges in question are subject to tax, the liability rests with the dancers who sell the entertainment and not with petitioner.

B. The Division has advanced three statutory bases upon which the door admission charges and the fees for private dances are properly subject to sales tax. That is, Tax Law § 1105 provides that sales tax shall be imposed upon certain receipts and charges, as follows:

> (d)(i) The receipts from every sale of beer, wine or other alcoholic beverages or any other drink of any nature, or from every sale of food and drink of any nature or of food alone, when sold in or by restaurants, taverns or other establishments in this state, or by caterers, *including in the amount of such receipts any cover, minimum, entertainment or other charge made to patrons or customers (except those receipts taxed pursuant to subdivision (f) of this section)* (emphasis supplied):
>
> (1) in all instances where the sale is for consumption on the premises where sold . . . .
>
> * * *
>
> (f)(1) Any *admission charge* where such admission charge is in excess of ten cents *to or for the use of any place of amusement* in the state, *except charges for* admission to race tracks, boxing, sparring or wrestling matches or exhibitions which charges are taxed under any other law of this state, or *dramatic or musical arts performances*, or live circus performances, or motion picture theaters, and except charges to a patron for admission to, or use of, facilities for sporting activities in which such patron is to be a participant, such as bowling alleys and swimming pools (emphasis supplied).
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> * * *
>
> (3) The amount paid as charges of a roof garden, cabaret or other similar place in the state.

C. The identical primary issue presented in this matter was very recently addressed by the Tax Appeals Tribunal. In ***Matter of 677 New Loudon Corporation*** (Tax Appeals Tribunal, April 14, 2010), the Tribunal held that the door admission charges and the additional charges (couch sales) for private dances were properly subject to sales tax under each of the three foregoing provisions. This holding in ***677 New Loudon*** proves dispositive in this matter since there are no significant differences in the manner of operation of the venue in that case versus the manner in which petitioner operated its business.

D. In ***677 New Loudon***, the Tribunal first rejected the argument that the admission charges collected at that venue were excepted from taxation as admission charges to a place of amusement, per Tax Law § 1105(f)(1), because they constituted admission charges for dramatic

or choreographed musical arts performances. The Tribunal, relying upon ***Matter of 1605 Book Center v. Tax Appeals Tribunal*** (83 NY2d 240 [1994], ***cert denied*** 513 US 811 [1994]), concluded that the petitioner in ***677 New Loudon*** was an adult juice club providing adult entertainment, accessible to a customer by the payment of a door admission charge, which entitled the customer to view the entertainment on and around the main stage area of the club, with further entertainment available to the customer by the payment of additional admission charges upon which access to and continued presence in the private rooms was predicated. The Tribunal held that the charges in question were "admission charges," per Tax Law § 1101(d)(2), to a "place of amusement," per Tax Law § 1101(d)(10) and 20 NYCRR 527.10(b)(3)(i). The Tribunal concluded that the fees for private dances, which in each case generated the most income, constituted admission charges to the private rooms, which were, from a tax standpoint, indistinguishable from the admission charges to the public areas of the club. The entertainers in ***677 New Loudon***, like the entertainers performing at petitioner's club, were independent contractors and not employees, who received a portion of the fee for each private dance. The door admission charges, as well as the charges for securing additional entertainment in the private rooms were, in both cases, set by the club. The entertainers in each instance provided performances on both the main stage and in the private rooms and, apart from providing dance performances, spent considerable time engaged in interaction and contact, including mingling, conversing and flirting with customers. The same expert witness, Dr. Judith Hanna, testified in each case, and the testimony she gave, the expert report she furnished, and the opinion she expressed in each matter are essentially identical in content and conclusion. The Tribunal accorded little weight to this testimony, the report and the expert opinion as furnished by Dr. Hanna in ***677 New Loudon***, noting that this testimony appeared at times "designed to neatly fit

the statutory exemption language, e.g., that the performances . . . constitute 'live, dramatic, musical, choreographic performances'." The Tribunal concluded that the petitioner in ***677 New Loudon*** was an adult juice club for adult entertainment and not a theater or theater-in-the-round as contemplated by the statute and regulations (Tax Law § 1105[f][1]; 20 NYCRR 527.10[b][3][i]; [d][2]). Given the nearly identical manner of operation of the two clubs, the same holding applies herein leaving petitioner's receipts subject to tax in the same manner pursuant to Tax Law § 1105(f)(1).

E. The Tribunal further concluded in ***677 New Loudon*** that the foregoing charges were subject to tax pursuant to Tax Law § 1105(f)(3) as "charges of a roof garden, cabaret or other similar place," that the selling of beverages was an integral part of the business (the adult juice club experience) and rejected the argument that petitioner's sales of refreshments (i.e., soda, water, juices, and other nonalcoholic beverages) in that case were merely incidental to the entertainment provided (Tax Law § 1101[d][12]; 20 NYCRR 527.12[b][2][ii]). On this latter point, while acknowledging in ***677 New Loudon*** that customers likely did not frequent the premises for its nonalcoholic drinks, and that such drinks may be incidental from the customer's perspective, the Tribunal focused on the extent to which the sale of beverages is a profit center for the club. The extent of beverage sales in this matter was less, as a percentage of overall revenue, than in ***677 New Loudon*** (7% as opposed to 15%). Nonetheless, the same clearly constituted an integral part of the entire adult juice club experience, as well as a revenue source to petitioner's business, and was not merely a paltry, incidental or inconsequential part thereof. Thus, the charges in question are properly subject to tax pursuant to Tax Law § 1105(f)(3).

F. Finally, and in the same manner, the Tribunal held that the charges at issue could be subject to tax pursuant to Tax Law § 1105(d)(i)(1) as a cover or entertainment charge of an

establishment which provides taxable food or beverages for consumption on the premises where sold. The Tribunal based its holding upon the "broadly inclusive language" of Tax Law § 1105(d). Given that there is little if any apparent factual difference between the operation of the bar in ***677 New Loudon*** and of petitioner herein, the Tribunal's holding in ***677 New Loudon*** applies equally and the charges in issue could be taxed under Tax Law § 1105(d)(i)(1).

G. The petitioner has raised two additional issues not presented or specifically addressed in ***677 New Loudon***. First, petitioner maintains that liability for the tax in issue properly falls upon the entertainers, who are not employees of petitioner but rather are independent contractors or tenants who merely rent space and access to the premises owned by petitioner, at which the entertainers then provide the activities from which the taxable receipts in question are derived.

Second, and as to the audit, petitioner does not challenge the sufficiency of the Division's request for and review of records, or its ensuing conclusion that due to the absence of cash register tapes or other source receipts for each individual sale, petitioner's records were not sufficient to conduct a detailed audit. Further, petitioner does not dispute that the Division was entitled to proceed on audit by resort to indirect audit methodology, or contest the Division's use of an observation audit methodology, as described. However, petitioner maintains that the audit methodology was unreasonable as applied, and overstated petitioner's receipts by failing to account for the seasonal nature of the business and by failing to account for growth in receipts over the audit period. Petitioner thus argues that the audit results should be adjusted or discarded.

H. Addressing the argument that the liability for tax properly falls upon the entertainers and not upon petitioner, Tax Law § 1101(b)(8)(i) includes within its definition of a "vendor":

> (A) a person making sales of tangible personal property or services the receipts from which are taxed under this article;
>
> (B) a person maintaining a place of business in the state and making sales, whether at such place of business or elsewhere, to persons within the state of tangible personal property or services, the use of which is taxed;
>
> (C) a person who solicits business either:
>
> (I) by employees, independent contractors, agents or other representatives.

A "person" liable to collect and remit sales and use taxes, per Tax Law §§ 1131 and 1133, includes an "individual, partnership, limited liability company, society, association, joint stock company, corporation, estate, receiver, trustee, assignee, referee, and any other person acting in a fiduciary or representative capacity, whether appointed by a court or otherwise, and any combination of the foregoing" (Tax Law § 1101[a]). Clearly petitioner falls within this framework and was therefore required to collect and remit sales taxes on its receipts from admission charges, as above, and on its beverage sales.

I. Although petitioner's argument in favor of holding the entertainers liable for the tax at issue was not specifically raised or directly addressed in ***677 New Loudon***, the entertainers in that case were, as here, not employees of the petitioner but rather independent contractors who received a portion of the charge paid by a customer for each private dance purchased. As determined by the Tribunal in ***677 New Loudon,*** the door charges and private dance fees at issue were admission charges allowing access to petitioner's premises, i.e., the place of amusement where the entertainment was provided. The amounts of such charges were, as noted, determined by the petitioner in each case. In addition to the door admission charge, payment for private dances could be made to petitioner's employee at the door, in which case the customer would receive a chip to present in order to redeem the private dance. Apparently, this method of

securing private dances could be followed by customers in the club via purchasing chips from the bartenders. Furthermore, though in some instances the entertainers may have collected cash from customers for dances (or additional dances in the private rooms), the cash appears to have been turned over to and accounted for by petitioner through its bartenders. The Tribunal described the admission charges to the private areas of the premises as indistinguishable, from a tax standpoint, from the door admission charges. In ***677 New Loudon*** the entertainers paid a "house fee," which was described as a "space rental fee for the rental of the facility in which to perform," a payment which is essentially identical to the "rental fee" or "additional rental fee" paid to petitioner by the entertainers in this case for the "joint and non-exclusive leasing" of portions of the club in which to perform (***see*** Findings of Fact 16 and 17). Accordingly, notwithstanding that the petitioner in ***677 New Loudon*** did not specifically raise the argument that the dancers and not the petitioner were responsible for any sales tax due, given the provisions of Tax Law § 1101(b)(8)(i) and the like manner in which both venues were in fact operated, petitioner's argument that the liability for the tax should be borne by the entertainers and not by it is rejected.

J. As to the arguments concerning the Division's method of carrying out the audit, there is scant evidence to conclude that petitioner's business is a "seasonal" business. This argument seems to be premised upon the claim that cold, wintry or inclement weather negatively impacts petitioner's sales, as opposed to a claim that petitioner's business should be viewed in the context of the more traditional types of seasonal businesses such as landscaping, lawn care or exterior painting. Inclement weather would logically be viewed as impacting not only petitioner's business but, in all likelihood, almost any business. More to the point, review of petitioner's reported sales does not show such a significant variance between the colder winter months and the warmer summer months as to justify a conclusion that the audit and its results were

unreasonable and should be rejected for failure to adjust in this respect for any such seasonal variance.

K. Petitioner has also raised an argument concerning the Division's failure to account for alleged business growth over the audit period. As a starting point, the absence of source documents verifying petitioner's receipts clearly allowed the Division to proceed via indirect auditing including, as here, an observation of sales audit (***see Matter of Del's Mini Deli, Inc. v. Commissioner of Taxation and Finance***, 205 AD2d 989 [1994]). In turn, and under such circumstances, it is well established that exactness in result is not required (***Matter of Meyer v. State Tax Commn.***, 61 AD2d 233 [1978], ***lv denied*** 44 NY2d 645 [1978], that petitioner must come forward with clear and convincing evidence that the Division's assessment is erroneous (***Matter of Meskouris Bros., Inc. v. Chu***, 139 AD2d 813 [1988]; ***Matter of Scarpulla v. State Tax Commn.***, 120 AD2d 842 [1986], and that a taxpayer cannot invalidate the Division's audit by offering its own "estimate" of tax liability as a substitute for the Division's (***see Matter of Albanese Rapid Mix***, Tax Appeals Tribunal, June 15, 1989; ***see also Matter of Wahba v. New York State Tax Commn.***, 127 AD2d 843 [1987]).

L. In response to the Division's audit, petitioner has provided essentially a proposed "refinement". It is telling that petitioner's proposed refinement is itself an estimation method, and arrives at the conclusion that petitioner owes a significant tax liability, albeit less than the amount determined by the Division. In fact, petitioner's estimate of liability varies broadly in amount depending upon which of the three possible indicators one uses as a base for adjustment, a reminder of the imprecision inherent in indirect auditing methodologies (***see*** Finding of Fact

25).[4] Petitioner argues it has presented "proof verified through independent sources" that its business grew over the period of audit. In fact, petitioner provided evidence that its payroll increased over such period (petitioner hired additional security personnel and added an additional bartender), and that the dollar volume of ATM cash withdrawals also increased. It is possible, and perhaps even likely, that petitioner's business grew over the time period covered by the audit. While it might be a reasonable inference that such increases in payroll and ATM activity indicate business growth, the absence of source records to establish the amount of petitioner's receipts from what is apparently a nearly all cash business leaves this inference to remain in the realm of speculation. To the extent petitioner's method relies on ATM withdrawals, there is no assurance that all of the cash withdrawn was in fact spent at petitioner's premises. The result of petitioner's refinement of the Division's observation audit, while perhaps useful or persuasive in the context of settlement negotiations, simply does not suffice to meet petitioner's burden of establishing that the audit was unreasonable and should be invalidated. The Division, for its part, did acknowledge that the chosen day of observation was a higher sales day in comparison to other business days, and adjusted its audit method to reflect the proportion that observation day sales bore to sales on other days of the week (***see*** Finding of Fact 7). Given that petitioner's further proposed adjustments leave a significant tax understatement, it does not follow that the Division's choice of audit method or its manner of application thereof was unreasonably inaccurate or erroneous.

M. The petition of Greystoke Industries LLC d/b/a Paradise Found is hereby granted to the extent of the modification resulting from eliminating the tax, penalty and interest assessed for

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[4] The three possible indicators are payroll, ATM cash withdrawals, or combined payroll plus ATM cash withdrawals.

the quarterly period spanning March 1, 2006 through May 31, 2006 (***see*** Finding of Fact 8), but is otherwise denied and the Notice of Determination dated May 7, 2007, except as so modified, and including penalty and interest thereon, is in all other respects sustained.

DATED: Troy, New York
June 24, 2010

/s/ Dennis M. Galliher
ADMINISTRATIVE LAW JUDGE