

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
FORESTVIEW RESTAURANT, LLC	:	
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, 2004	:	
through May 31, 2007.	:	
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In the Matter of the Petition	:	DETERMINATION
of	:	DTA NOS. 823465
GEORGE A. PEPPE	:	AND 823466
OFFICER OF FORESTVIEW RESTAURANT, LLC	:	
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, 2006	:	
through May 31, 2007.	:	

Petitioner Forestview Restaurant, LLC, 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, 2004 through May 31, 2007.

Petitioner George A. Peppes, officer of Forestview Restaurant, LLC, 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, 2006 through May 31, 2007.

A consolidated hearing was held before Arthur S. Bray, Administrative Law Judge, at the offices of the Division of Tax Appeals, 183 East Main Street, Rochester, New York 14604, on

September 13, 2011, at 9:30 A.M., with all briefs to be submitted by February 27, 2012, which date commenced the six-month period for the issuance of this determination. Petitioners appeared by Harris Beach, PLLC (Pietra B. Lettieri, Esq., of counsel). The Division of Taxation appeared by Mark F. Volk, Esq. (Michael B. Infantino, Esq., of counsel).

ISSUES

I. Whether the Division of Taxation correctly determined that additional sales and use taxes were due using an indirect audit methodology.

II. Whether, assuming the use of an indirect audit methodology was proper, petitioners have shown error in the audit method or result.

III. Whether petitioners have established any facts or circumstances warranting the reduction or abatement of penalties.

FINDINGS OF FACT

1. Petitioner Forestview Restaurant, LLC, (Forestview) is a restaurant located in DePew, New York. Petitioner George Peppes and his brother, Vasilios, purchased the building that became Forestview in 2001. Each brother acquired a 50-percent ownership interest in the outstanding stock.¹

2. At the time the building was acquired, it was a vacant Perkins restaurant. Upon acquisition, Mr. Peppes and his brother made cosmetic changes such as changing the wallpaper and replacing booths and carpeting.

3. When it opened, Forestview was a traditional Greek diner, which operated 24 hours a day, 7 days a week. Mr. Peppes would go to the restaurant at seven o'clock in the morning. His

¹ Unless otherwise indicated, references to "Mr. Peppes" are to the individual petitioner in this proceeding.

activities included making soups, determining the daily specials, reviewing inventory, greeting customers and guiding them to their seats, accepting payment for meals and performing paperwork. His working day normally ended at 9:00 P.M.

4. On September 6, 2007, the Division of Taxation (Division) mailed a letter to Forestview and Mr. Peppes scheduling a field audit on October 2, 2007 for the period December 1, 2004 through May 31, 2007. The letter stated that “[a]ll books and records pertaining to the sales and use tax liability, for the audit period, must be available on the appointment date.” A schedule of books and records to be produced was attached to the letter. The foregoing appointment was changed to October 18, 2007.

5. When Mr. Peppes received the letter from the auditor, he directed the auditor to contact his accountant, Mr. Nicholas Buccieri. Thereafter, Mr. Peppes received a telephone call from Mr. Buccieri and his assistant, Linda Ward, and they advised Mr. Peppes what actions he should take. On October 18, 2007, Mr. Peppes brought 10 to 15 boxes of materials to a room in the basement of the building where the accountant’s office was located. This location for the audit was chosen because renovations were taking place at the restaurant. The boxes had materials from the months of January through May of 2007. Mr. Peppes had additional boxes that contained documents for the balance of the audit period, but the production of documents for the last five months of the audit period was viewed as a starting point.

6. During the initial audit appointment, the auditor met with petitioner George Peppes and his accountant, Nicholas Buccieri and his assistant Linda Ward. At this time, the auditor explained what items he wished to review. The Division learned that in April 2006, Mr. Peppes

installed a point of sale cash register system.² The auditor also ascertained that Mr. Peppes did not “z out” the register. When a z-tape was produced, the cash register printed the total sales and then reset to zero. It then began registering sales again. The z-tapes can be created at the end of a shift or end of a day. They were sequentially numbered, which enabled the examiner to follow them from day to day in order to verify that all of the sales are recorded. However, in this instance, since Mr. Peppes or his brother made a practice of cashing out the register several times a day, it meant that Mr. Peppes did not z-out the register and the cash register did not reset to zero. The cash-out slips are for the servers and did not have sequential numbering on them.

7. The Division received guest checks, checking account statements, credit card merchant reports, sales tax returns, federal returns for 2004, 2005, and 2006, some server reports for May of 2007 and expense purchases from Georgios Enterprises. Gerorgios Enterprises was another business owed by Mr. Peppes that provided food and supplies to Forestview and another restaurant in which Mr. Peppes was a part owner. The Division also reviewed a calendar book that resembled a typical date book. It had a number written on each page that purported to be the total sales for that day. There was no indication in the book whether the amount entered for each day included sales tax.

8. After Ms. Ward placed certain documents on the table, the auditor decided to focus on May 2007 since he could find the documents pertaining to this month quickly. By the end of the day, the auditor had transcribed about 1,900 checks from May 2007 and concluded that there were many gaps in the sequence of guest check numbers. On the other hand, the credit card sales appeared to be properly reported based on an initial calculation.

² “Point of sale” refers to the location where the sale takes place. There are a number of different point of sale systems. At the entry level, there is the basic cash register. With a sophisticated system, a restaurant can simultaneously manage its sales, kitchen and inventory.

9. The auditor compared the monthly returns with the guest checks and found a small discrepancy. However, the auditor was particularly concerned that the Division did not have all of the invoices and he was not sure what made up the missing guest checks.³

10. The auditor also attempted, without success, to match the amount shown on the server reports to the amounts reported on the sales tax return for May of 2007. After letting Ms. Ward know what he had found, Ms. Ward attempted to reconcile the server reports to the sales tax returns over a period of several months. When she did the reconciliation, some months showed a small discrepancy and in other instances there were large discrepancies.⁴ The records reviewed by Ms. Ward were not in order and the boxes were not marked in any particular way. A single box might have documents from two successive months. The auditor advised Ms. Ward that he could not use the server reports by themselves without the corresponding guest checks because he did not know if all of the sales were included.

11. Mr. Buccieri's office provided the auditor with some reports, journals and ledgers in the Quicken accounting software program. These materials were not used because neither the auditor nor the Division's computer department was able to convert this program into a format that they could read.

12. After the initial audit appointment, the Division sent a letter to petitioners, dated October 23, 2007, explaining that certain records were missing. Specifically, the Division stated that the following records were not available for review: sales journal tapes for the entire audit

³ One cause of the missing checks arose from a feature of the system used to print checks. In those instances where a group decided to divide a check into individual checks, the check printing system would delete the original check number and print individual checks bearing the following numbers. The result would be a "missing" check number.

⁴ Ms. Ward examined the restaurant's records for the months of February through May 2007.

period, guest checks for the entire audit period, end-of-day cash out tapes showing time, date and cash out sequence number or guest check range, sales journal, a fixed asset invoice for one entry and details of expense purchases from Georgios Enterprises.

13. No additional records were provided in response to the second request for records, and an audit based on the actual documentation never proceeded beyond this point.

14. The Division concluded that it could not verify the purchase information because the purchase invoices only showed a dollar amount. It omitted any details showing what was purchased and there were no documents providing backup for the invoices. Moreover, the fact that Mr. Peppes also owned the business that was supplying Forestview made it difficult to verify that the purchase records were accurate because the transactions were not at arm's length.

15. The Division considered the sales records inadequate because it could not verify the accuracy of the sales tax returns through the backup that Mr. Peppes had provided.

16. On January 23, 2008, the auditor and an investigator went to the restaurant with the intention of performing an observation test. However, the plan was abandoned because the restaurant had changed its method of receiving cash from a single cash register to a point of sale system with multiple terminals. The auditor and investigator concluded that two individuals were not adequate to conduct an observation test with the restaurant's new method of conducting business.⁵

17. The Division attempted to conduct an audit using the restaurant's utility bills and a report from Deloitte & Touche. According to this analysis, the amount of tax due was \$258,786.63.

⁵ Under the new point of sale system, each server used his or her own server report, cashed out at the end of the shift, and left the server report and cash under Mr. Peppes' office door.

18. On March 10, 2008, the auditor presented the results of the utility audit to a prior representative, Mr. Steve Schop. Mr. Schop had concerns about the accuracy of the utility markup because the restaurant was open 24-hours a day, and there was no indication in the utility markup study that the markups were based on similar establishments. Mr. Schop told the auditor that, despite his concerns about the propriety of doing an observation test in view of the renovations to the restaurant, he wanted the Division to perform an observation test.

19. Mr. Schop also asked the auditor to compare the available guest checks for May 2007 with the server reports and the time cards. The time cards were used to determine if all of the server reports were present. The Division found that the sales per the server reports were less than what was reported on the return. It also found that there were quantities of missing server reports. In addition, the bank deposits were more than the credit card deposits or the information gleaned from the server reports. On April 18, 2008, the Division received cash register tapes for April 2007. The Division added the amounts reported on the tapes and found that they were more than were reported as gross sales.

20. On April 28, 2008, the auditor called the taxpayer's representative and asked if he could view the restaurant so he would know the layout and how many people were needed to perform the observation. On May 7, 2008, the auditor called Mr. Schop and told him that the Division would conduct the observation on May 15, 2008.

21. Usually, the Division does not tell a taxpayer in advance of the date of an observation test in order to avoid the possibility that the results would become skewed. In this case, the taxpayer was told because the Division was trying to make everything as fair as possible and give petitioners every opportunity to present the information that was needed.

22. The day of the observation, May 15, 2008, was a pleasant spring day, mostly sunny, with a high temperature of 60 degrees. The Division positioned observers, in morning and evening shifts, at each terminal from 7:00 A.M. until 11:00 P.M. When a guest check was printed, it would be shown to the observer who would log the check number, server and the dollar amount to ascertain what the sales were for the day.

23. There were difficulties in completing the observation of the restaurant. Some of the waiters were uncooperative and not turning over their guest checks. One server thought that the observers were from another department that was interested in examining the amount of tips. A couple of waiters cashed out past 11:00 P.M. and the Division did not receive those slips. One or two waiters cashed out and slipped their information under the office door so the Division was not able to get that information on the day of the observation.

24. The day after the observation, one of the investigators went back to the restaurant and obtained the information that they were unable to procure on the day of the observation.

25. As the basis for its projection, the Division transcribed the z-tapes by server. The z-tapes were then compared to the Thursday sales per the date books that petitioners had presented. The Division did not use the guest checks to determine the amount of tax due because, when they were added up, they were less than the z-tapes from the servers. The Division did not feel that it had all the guest checks because if it did, the amounts on the guest checks would have corresponded with the z-tapes. The Thursday sales were added and divided by the number of Thursdays in the audit period to obtain an average number of Thursday sales per the taxpayer's books during the audit period. One of the Thursdays in petitioners' date book was left blank. The Division included it in the average as a zero because it could not determine if the restaurant was closed or petitioners had just failed to include the sales for that day. The comparison of the

z-tapes for the day of the observation and the average Thursday resulted in an error rate of 36 percent. The error rate was then multiplied by the reported sales in order to calculate the additional sales. The additional sales, in turn, were multiplied by the tax rate in order to compute the amount of additional tax due.

26. The Division made certain allowances to the findings of the observation. The Division was able to isolate the amount of the credit card sales from the cash sales. With respect to the credit card sales, it removed 20 percent as an allowance for tips. For cash sales, the Division did not believe that the tips would be included as part of the guest check so the same adjustment would not be warranted. The sales tax was not backed out of this computation because there was nothing in the date book to indicate that sales tax was included in those sales.

27. On the basis of the forgoing audit, the Division issued a Notice of Determination to Forestview (assessment number L-030579634-4), dated August 18, 2008, which assessed sales and use taxes for the tax period December 1, 2004 through May 31, 2007, in the amount of \$94,110.82, plus penalty and interest, for a balance due of \$166,214.98. The Division also issued a Notice of Determination to George A. Peppes, as a responsible officer or responsible person of Forestview, dated August 25, 2008, which assessed sales and use taxes for the period June 1, 2006 through May 31, 2007 in the amount of \$39,089.02, plus penalty and interest, for a balance due of \$63,387.89. Both statutory and omnibus penalties were imposed because of the inadequacy of the records and the amount of tax due was more than 25 percent of what was reported.

28. After the notices of determination were issued, the Division ascertained that when the calculations were performed, the auditor reversed the numerator and denominator and that the

error rate should have been 56 percent. If the computation was performed correctly, the amount of tax that the Division would have asserted to be due would have been \$146,507.37.

29. At the time the restaurant first opened, it had a cash register in the front of the establishment. When a customer walked up to the host station and submitted a check, the check would be punched into the computer, cashed out and the customer would receive change. The checks were then placed in a basket. When the register was cashed out, Mr. Peppes would take a reading. After leaving a sum of money in the drawer, the remaining amount would be taken back to the office and counted and compared to the tape. The tapes would be added together and the sum recorded in the daily log book. This process was performed until late 2007 when the remodeling occurred.

30. In 2005, Mr. Peppes started to see a decline in the business and the renovations that were installed in 2001 were starting to show wear and tear. Mr. Peppes and his brother realized that they had to make changes or the restaurant would fail. As a result, they hired an interior designer from California to give the restaurant a new feeling. He recommended that they install a bar and change the motif to resemble a Cheesecake Factory or a TGI Friday's. It was believed that the new motif would prompt customers to spend more money.

31. The renovations started at the end of July 2007. As the remodeling took place, the restaurant stayed open because Mr. Peppes and his brother needed the money to pay bills. By mid-October 2007 the construction had reached a point where the restaurant had to be closed in order to complete the renovations. The restaurant was closed for about three or four weeks and reopened on or about November 15, 2007.

32. There were a number of significant differences between the original restaurant and the remodeled restaurant. During the audit period, the restaurant served beer and wine. It started

selling liquor after the restaurant was remodeled in late 2007. The new menu, which was introduced in the middle of November 2007, was noticeably different. The grilled cheese sandwich was eliminated and items such as gourmet hamburgers, gourmet sandwiches, filet mignon, Wasabi salmon, crab cake salad and barbecue rack of ribs were added. The original menu had breakfast selections while the new menu did not offer breakfast. In those instances where the same item was offered, the price of the item differed. For example, the chicken Parmesan was \$9.99 on the original menu and \$12.99 on the revised menu. There were other comparable increases in prices.

33. The appearance of the restaurant was also considerably different. A patron would enter the restaurant through a new vestibule with a fireplace in the center. To the left, a bakery area was added in order to display new desserts and bakery items. In addition, three tables with seating were added to the bakery area. On the right, a full-course bar was added with a 12-draft system and a wine cooler to feature wines. Thirty-six seats were positioned next to the bar, which also served food. Seating was added to the interior of the dining room to accommodate larger parties and booths for six were added in a couple of areas.

34. The renovated restaurant featured a new entrance, which included a pie case on the left that was about 10 feet long. Mr. Peppes hired a baker who made unique cakes, pies and desserts that were placed on display. An entire cake or pastry could be ordered in advance for functions.

35. During the audit period, the restaurant employed about 40 people. After the renovation, the restaurant employed 65 to 70 people.

36. The renovation added a patio, which had heaters, an office of 750 square feet and about 1,000 square feet in the bar area.

37. In late May of 2007, after the restaurant was remodeled, the restaurant started the practice of “server banking.” In this process, the customers paid the server and the server created change for them. Mr. Peppes was not a participant in this process. Using their individual number, food orders were entered into the system by the server and received by the kitchen. The placing of an order resulted in the creation of a corresponding guest check. When they were done with their shift and the tables were closed, each server created a z-report. After the server cashed out at the end of the shift, Mr. Peppes received the z-report and all of their checks. Mr. Peppes took each of the server reports, calculated them with the sales tax, and stored all of the tapes and checks.

SUMMARY OF THE PARTIES’ POSITIONS

38. Petitioners maintain that their books and records were adequate and that the Division was precluded from employing an observation test. They also submit that the use of the observation test was unreasonable and resulted in an erroneous assessment because the auditor failed to account for the change in the business operations. Lastly, petitioners contend that there were numerous errors in the Division’s calculation of the error rate.

39. In response, the Division submits that petitioners have not proved by clear and convincing evidence that the audit methodology or the notices of determination are erroneous. It also submits that there is no basis for making any adjustments to the assessments.

CONCLUSIONS OF LAW

A. It is well established that any person making taxable sales is a “vendor” under Tax Law § 1101(b)(8). As such, petitioners were “required to maintain complete, adequate and accurate books and records regarding [their] sales tax liability and, upon request, to make the same available for audit by the Division” (*Matter of AGDN, Inc.*, Tax Appeals Tribunal, February 6,

1997). The records required to be maintained “include a true copy of each sales slip, invoice, receipt, statement or memorandum” (Tax Law § 1135[a]; 20 NYCRR 533.2[b][1]).

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

C. The standard for reviewing a sales tax audit where external indices are employed was set forth in *Matter of Your Own Choice, Inc.*, as follows:

To determine the adequacy of a taxpayer’s records, the Division must first request (*Matter of Christ Cella, Inc. v. State Tax Commn.*, [102 AD2d 352, 477 NYS2d 858] *supra*) and thoroughly examine (*Matter of King Crab Rest. v. Chu*, 134 AD2d 51, 522 NYS2d 978) the taxpayer’s books and records for the entire period of the proposed assessment (*Matter of Adamides v. Chu*, 134 AD2d 776, 521 NYS2d 826, *lv denied* 71 NY2d 806, 530 NYS2d 109). The purpose of the examination is to determine, through verification drawn independently from within these records (*Matter of Giordano v. State Tax Commn.*, 145 AD2d 726, 535 NYS2d 255; *Matter of Urban Liqs. v. State Tax Commn.*, 90 AD2d 576, 456 NYS2d 138; *Matter of Meyer v. State Tax Commn.*, 61 AD2d 223, 402 NYS2d 74, *lv denied* 44 NY2d 645, 406 NYS2d 1025; *see also, Matter of Hennekens v. State Tax Commn.*, 114 AD2d 599, 494 NYS2d 208), that they are, in fact, so insufficient that it is “virtually impossible [for the Division of Taxation] to verify taxable sales receipts and conduct a complete audit” (*Matter of Chartair, Inc. v. State Tax Commn.*, 65 AD2d 44, 411 NYS2d 41, 43; *Matter of Christ Cella, Inc. v. State Tax Commn.*, *supra*), “from which the exact amount of tax due can be determined” (*Matter of Mohawk Airlines v. Tully*, 75 AD2d 249, 429 NYS2d 759, 760).

D. Here, the record is clear that, upon the commencement of the audit, the Division made an unequivocal request for the restaurant's books and records for the entire audit period. In response, petitioners produced 15 boxes of records, which pertained to the last 5 months of the audit period. Petitioners offered this abridged version of their records on the premise that it was a good place to begin. The Division responded with a second request for records, which was not honored. There is no indication that petitioners actually produced all of the records that were requested in the first or second written requests for records.

E. It is equally clear that the records that were produced presented numerous difficulties. While petitioners made an effort to maintain records, it is also apparent that the records were kept in a haphazard fashion. The records were simply placed in unmarked boxes without any apparent order. The record of monthly sales was simply a bare figure recorded in a calendar book and not traceable to any particular source documents. Similarly, the record of purchases was equally lacking in any detail regarding what was purchased. In addition, following a review of guest checks for May 2007, the Division found that numerous guest checks were missing. When the Division was presented with cash register tapes for April 2007, it determined that the amounts reported on the tapes were more than were reported as gross sales on the returns. Although they are not substitutes for cash register tapes, it is noteworthy that when Ms. Ward attempted to reconcile the server reports to the sales tax returns over a period of several months, there were instances of large discrepancies. Under these circumstances, it is readily apparent that the records maintained by petitioners were so insufficient that it was virtually impossible to verify taxable receipts and conduct a complete audit (*see Matter of Jin Fong Restaurant, Inc.*, Tax Appeals Tribunal, February 23, 2012).

F. Petitioners argue that there is no requirement that guest checks be numbered and used in sequence. This argument is rejected because it overlooks the purpose of the audit, i.e., to determine through independent verification of the records the amount of taxable receipts and conduct a complete audit (*Matter of Giordano v. State Tax Commn.*, 145 AD2d 726 [1988]). When there are unexplained missing guest checks, the Division's ability to perform this function with the taxpayer's records is severely hampered. Thus, it has been recognized for a long time that an incomplete record of guest checks is an important factor in determining whether it is appropriate to resort to the use of external indices (*Matter of Hanratty's 1732 Amsterdam Tavern v. State Tax Commn.*, 88 AD2d 1028 [1982], *lv denied* 57 NY2d 608 [1982]). Recently, the Tax Appeals Tribunal noted that a restaurant's practice of discarding voided checks or permitting customers to leave with their checks completely destroyed the reliability of the guest records (*Matter of 2720 Henrietta-Brighton, Inc.*, Tax Appeals Tribunal, May 12, 2011).

G. Petitioners rely upon *Matter of King Crab Restaurant, Inc. v. New York State Tax Commn.* (134 AD2d 51 [1987]) and *Matter of Christ Cella, Inc. v. State Tax Commn.* (102 AD2d 352 [1984]) to support their position that the Division has not shown that the restaurant's records were inadequate. This argument is also without merit. It was sufficient for the Division to show that the restaurant was unable to produce a complete set of cash register tapes to justify the use of external indices (*Matter of Licata v. Chu*, 64 NY2d 873 [1985]).

H. The issue that remains is whether the audit methodology employed by the Division to estimate the amount of sales tax due was reasonable. The principles employed to resolve this issue are well established. The methodology selected by the Division must be reasonably calculated to reflect the taxes due (*Matter of Ristorante Puglia v. Chu*, 102 AD2d 348 [1984]). However, exactness is not required (*Matter of Meyer v. State Tax Commn.*, 61 AD2d 223

[1978], *lv denied* 44 NY2d 645 [1978]; *Matter of Markowitz v. State Tax Commn.*, 54 AD2d 1023 [1976], *affd* 44 NY2d 684 [1978]) because “[c]onsiderable latitude is given an auditor’s method of estimating sales” (*Matter of Grecian Square, Inc. v. State Tax Commn.*, 119 AD2d 948 [1986]). The burden of proof is upon the taxpayer to show by clear and convincing evidence that the methodology was unreasonable or that the amount of tax assessed was erroneous (*Matter of Meskoruis Bros. v. Chu*, 139 AD2d 813 [1988]; *Matter of Surface Line Operators Fraternal Org. v. Tully*, 85 AD2d 858 [1981]).

I. The Division submits that the reasonableness of using the remodeled restaurant as a basis for determining the amount of sales tax due is established by the fact that petitioner’s representative asked for the use of an observation test. According to the Division, rejection of this methodology would penalize the Division for its reasonableness in accommodating this request and would render the statutory burden of proof a nullity.

J. Petitioners have established by clear and convincing evidence that the audit methodology was not reasonably calculated to determine the amount of sales and use taxes due. Regardless of the fact that petitioners’ representative requested the use of an observation test, the Division is not relieved of its obligation to select an audit methodology that is reasonably calculated to reflect the taxes due (*Matter of Ristorante Puglia v. Chu*; *Matter of Surface Line Operators Fraternal Org. v. Tully*). The differences between the original restaurant and the remodeled restaurant make the use of the former to estimate the sales of the latter problematic. It is readily evident that the menus of the two restaurants were very different. For the same number of customers, one would expect that the remodeled restaurant would have substantially more sales because of the higher price of the menu items. The fact that the remodeled restaurant sold alcoholic drinks while the original restaurant sold only beer and wine also raises serious

questions. It is recognized that the Division eliminated the sales of alcoholic drinks from the bar. However, this adjustment only accounts for a portion of the difference. No adjustment was made for the sale of alcoholic drinks at the tables. Perhaps more significantly, the Division's adjustment does not take into account the increased number of customers who may have patronized the remodeled establishment because of the more modern appearance, more diverse menu and the availability of alcoholic drinks in addition to beer and wine. It is reasonable to surmise that there was a significant increase in the number of patrons of the remodeled restaurant because there was a very substantial increase in the number of employees. In sum, the audit methodology chosen by the Division is not supported by a rational basis in the record. As a result, the notices of determination and demands for payment of sales and use taxes due are cancelled (*see e.g. Matter of Abbasi*, Tax Appeals Tribunal, June 12, 2008; *Matter of Fokos Lounge, Inc.*, Tax Appeals Tribunal, March 7, 1991).

K. In view of the forgoing, consideration of the arguments regarding adjustments to the audit are academic and will not be addressed. It is noted that petitioners' reliance upon what took place at the conciliation conference is misplaced. Correspondence taking place during the conciliation conference process is in the nature of settlement negotiations and has no bearing on the audit or the amount of tax assessed. Therefore, these matters are irrelevant. Lastly, the imposition of penalties will also not be addressed because it is also moot.

L. The petitions of Forestview Restaurant, LLC, and George A. Peppes, officer of Forestview Restaurant, LLC, are granted and the notices of determination and demands for payment of sales and use taxes due, dated August 18, 2008 and August 25, 2008, respectively, are cancelled.

DATED: Albany, New York
June 28, 2012

/s/ Arthur S. Bray
ADMINISTRATIVE LAW JUDGE