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.	:	
	:	ORDER DTA NOS. 823465
In the Matter of the Petition	:	AND 823466
of	:	
GEORGE A. PEPPES 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.

On June 28, 2012, the Administrative Law Judge issued a determination that granted the petitions and cancelled the notices of determination dated August 18, 2008 and August 25, 2008.

By a motion dated September 27, 2012, petitioners, appearing by Harris Beach, PLLC (Pietra B. Lettieri, Esq., of counsel) brought an application for costs under Tax Law § 3030. The Division of Taxation, appearing by Amanda Hiller, Esq., (Michael Infantino, Esq., of counsel), filed an affirmation in opposition to the application. Pursuant to an extension of time, the Division of Taxation had until January 14, 2013 to file its papers in opposition to the motion, which date began the 90-day period for issuance of this order.

Based upon petitioners' application for costs, the Division's affirmation in opposition, the determination issued June 28, 2012, and all pleadings and proceedings had herein, Arthur S. Bray, Administrative Law Judge, renders the following order.

ISSUE

Whether petitioners are entitled to an award of costs pursuant to Tax Law § 3030.

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] During the audit period, Forestview was a traditional Greek diner. Immediately following the audit period, it adopted a motif that resembled a Cheesecake Factory or a TGI Friday's.

2. On September 6, 2007, the Division of Taxation (Division) commenced an audit of Forestview for the period December 1, 2004 through May 31, 2007. From the outset, the Division encountered numerous difficulties in completing the audit. In response to a request for

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

books and records for the entire audit period, petitioners offered records for the last five months of the audit period. A second request for records was not honored. The records that were made available presented numerous problems. Among other things, they were placed in unmarked boxes without any apparent order. The record of sales consisted of a single figure, which could not be traced to other documents. Similarly, the record of purchases lacked any detail of what was purchased. A review of guest checks for April 2007 showed that the sales on the tapes exceeded the sales reported on the sales tax returns. There were also large discrepancies between the amount of sales found on the server reports and the sales tax returns. Under the circumstances, it was evident that the records were not sufficient to verify taxable receipts and conduct a complete audit. After ascertaining the forgoing deficiencies in the restaurant's records, the Division attempted to conduct the audit using the restaurant's utility bills. However, this approach was abandoned because of concerns raised by petitioners' representative. Thereafter, at the request of petitioners' representative, the Division decided to conduct an observation test. Following the observation test, the results were adjusted in an attempt to reflect the differences between the original and remodeled restaurant.

3. On the basis of the observation test, the Division issued a Notice of Determination to Forestview, dated August 18, 2008, that 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, that 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.

4. Petitioners filed petitions challenging the notices that led to a hearing and a determination. The determination examined the question of whether the audit methodology was reasonably calculated to reflect the amount of taxes due and concluded that, despite a request from a prior representative to perform an observation test, in view of the significant differences between the original restaurant, a Greek diner, and the remolded restaurant, which was based upon a Cheesecake Factory or TGI Friday's restaurant motif, it was unreasonable to utilize an observation of the latter restaurant to estimate the sales of the original restaurant. As a result, the assessment was cancelled.

5. The determination of the Division of Tax Appeals was dated June 28, 2012. On this date, the determination was mailed to the parties with a cover letter, stating, in pertinent part:

> If no party to the proceeding files an exception, an application for reasonable administrative costs pursuant to Tax Law § 3030 may be filed with the Division of Tax Appeals by any petitioner who has substantially prevailed with respect to the amount in controversy or with respect to the most significant issue or set of issues presented. However, if the time to file an exception was extended for any party by the Tax Appeals Tribunal, then an application for reasonable administrative costs must be filed within 30 days from such extended filing date.

6. Pursuant to their request of August 27, 2012, petitioners were given until September 27, 2012 to file an application for costs. Thereafter, petitioners filed an application for costs on September 27, 2012. Upon review of the application, it came to the administrative law judge's attention that the application for costs may not have been served upon opposing counsel. Accordingly, in a letter dated November 8, 2012, the administrative law judge requested that petitioners' representative provide proof of service or documentation showing that the Division's representative was provided with a copy of the application. Petitioners provided the proof of service and the Division has acknowledged receipt of the application on November 14, 2012.

SUMMARY OF THE PARTIES' POSITIONS

7. In their brief, petitioners maintain that the Division's position was not substantially justified, that petitioners substantially prevailed with respect to the amount in controversy and the most significant issue presented and that petitioners are entitled to reasonable administrative costs consisting of attorney's fees, accountant's fees and expert fees. In accompanying affidavits, petitioners presented evidence that the restaurant is an unincorporated business whose net worth did not exceed five million dollars and did not have more than 500 employees, and that the individual petitioner did not have a net worth exceeding two million dollars when the proceeding was commenced. Petitioners also submitted itemized statements from their legal, accounting and expert personnel in order to support the actual time expended and the rate at which the fees were computed.

8. In response to the forgoing, the Division submitted a brief that maintained that the application for costs was untimely and should be dismissed. In the alternative, the Division maintains that petitioners are not a "prevailing party" within the meaning of Tax Law § 3030. The Division further contends that petitioners failed to provide adequate evidence of the fees and expenses they incurred .

CONCLUSIONS OF LAW

A. Tax Law § 3030(a) provides, generally, as follows:

> In any administrative or court proceeding which is brought by or against the commissioner in connection with the determination, collection, or refund of any tax, the prevailing party may be awarded a judgment or settlement for:
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> (1) reasonable administrative costs incurred in connection with such administrative proceeding within the department, and
>
> (2) reasonable litigation costs incurred in connection with such court proceeding.

Reasonable administrative costs include reasonable fees paid in connection with the administrative proceeding, but incurred after the issuance of the notice or other document giving rise to the taxpayer's right to a hearing. (Tax Law § 3030[c][2][B].)

B. Initially, the Division maintains that the application in this matter is untimely. The Tax Law requires that an application for costs must be initiated within 30 days of the "final judgment" in the matter (Tax Law § 3030[c][5][ii][I]). Unfortunately, the Tax Law does not provide a definition of "final judgment" and regulations have not been promulgated pursuant to this section of the Tax Law. However, this issue was addressed by the Tax Appeals Tribunal in ***Matter of Lawson*** (Tax Appeals Tribunal, October 4, 2001), which concluded that a judgment became "final" within the meaning of Tax Law § 3030(c)(5)(i)(I) when the time for taking an exception, including any extensions which may have been granted by the Secretary to the Tribunal, expired. In ***Lawson,*** the Secretary had granted an extension to file an extension to November 1, 2000. Therefore, the Tribunal concluded that the determination of the administrative law judge became final on that date. It followed that petitioner had 30 days from November 1, 2000, when the judgment became final, or December 1, 2000, to file an application for costs.

Applying the same reasoning as that presented in ***Lawson***, leads to the conclusion that the application for costs was timely. The determination in this matter was issued on June 28, 2012. Therefore, in the absence of an extension of time to file an exception, the determination became final in 30 days, which was July 28, 2012. Thus, petitioners had 30 days from July 28, 2012, or August 27, 2012, to either make their application for costs or request an extension of time. Here, petitioners made a timely request for an extension of time on August 27, 2012, and in response, petitioners were given until September 27, 2012 to submit an application for costs.

C. The Division next argues that the application for costs was untimely because it was not served by September 27, 2012. An issue has not been raised regarding whether it was timely filed.

D. Section 3000.5(b) of the Rules of Practice and Procedure provides, in pertinent part, that "[a] copy of each written motion shall be served on the adverse party." Thus, the issue presented is whether a motion which has been timely filed but not served within the prescribed time requires that the application be denied.

An analogous situation arises when a party files a timely exception with the Tribunal but fails to serve the opposing party. When this occurs, the Tribunal has been guided by the curative provisions of Civil Practice Law and Rules (CPLR) 5520(a), which permits a court to excuse a party's failure to perform one of two procedural steps provided that the remaining step has been timely performed (***Matter of American Express Company***, Tax Appeals Tribunal, July 3, 1991, ***confirmed on other grounds***, 190 AD2d 104 [3d Dept 1993], ***lv denied*** 82 NY2d 663 [1993]).

In this matter, I am similarly guided by the curative provisions of CPLR 2004, which permit a court to "extend the time fixed by any statute, rule or order for doing any act, upon such terms as may be just . . . . ." Here, jurisdiction was established by the timely filing of the application (***see Matter of American Express Company***) and, in accordance with the spirit and language of CPLR 2004 and Rule 3000.23, when the lack of service came to my attention, petitioners were given a reasonable period of time to cure the omission. Since this was accomplished, the application for costs is properly before the Division of Tax Appeals.

E. Petitioners argue that they are the prevailing party because the notices of determination were cancelled. A prevailing party is defined by the statute as follows:

> [A]ny party in any proceeding to which [Tax Law § 3030(a)] applies (other than the commissioner or any creditor of the taxpayer involved):
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> (i) who (I) has substantially prevailed with respect to the amount in controversy, or (II) has substantially prevailed with respect to the most significant issue or set of issues presented, and
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> (ii) who (I) within thirty days of final judgment in the action, submits to the court an application for fees and other expenses which shows that the party is a prevailing party and is eligible to receive an award under this section, and the amount sought, including an itemized statement from an attorney or expert witness representing or appearing in behalf of the party stating the actual time expended and the rate at which fees and other expenses were computed . . . and (II) is an individual whose net worth did not exceed two million dollars at the time the civil action was filed . . . .
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> (B) Exception if the commissioner establishes that the commissioner's position was substantially justified.
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> (i) General rule. *A party shall not be treated as the prevailing party in a proceeding to which subdivision (a) of this section applies if the commissioner establishes that the position of the commissioner in the proceeding was substantially justified.* (Emphasis added.)
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> (ii) Burden of proof. The commissioner shall have the burden of proof of establishing that the commissioner's position in a proceeding referred to in subdivision (a) of this section was substantially justified, in which event, a party shall not be treated as a prevailing party.
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> (iii) Presumption. For purposes of clause (i) of this subparagraph, the position of the commissioner shall be presumed not to be substantially justified if the department, inter alia, did not follow its applicable published guidance in the administrative proceeding. Such presumption may be rebutted.
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> * * *
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> (C) Determination as to prevailing party. Any determination under this paragraph as to whether a party is a prevailing party shall be made by agreement of the parties or (i) in the case where the final determination with respect to tax is made at the administrative level, by the division of tax appeals, or (ii) in the case where such final determination is made by a court, the court. (Tax Law § 3030[c][5]; emphasis added).

If the Division satisfies its burden of showing by a preponderance of the evidence that its position was substantially justified, a prevailing party is not entitled to the recovery of costs (***City of New York v. State of New York***, 94 NY2d 577, 598 [1977]). Therefore, the question on this

application is whether the Division's position was substantially justified within the meaning of Tax Law § 3030(c)(5)(B). Recently, in ***Matter of Grillo*** (Tax Appeals Tribunal, August 23, 2012), the Tribunal set forth the following principles in determining whether the Division had substantial justification for its position:

> In order to prove substantial justification, the Division must show that its position "had a reasonable basis both in fact and law" (***see Powers v Commissioner***, 100 TC 457, 470 [1993]; ***see also Pierce v Underwood***, 487 US 552 [1988]). While the cancellation of a notice may be considered (***Heasley v Commissioner***, 967 F2d 116 [1992]), this determination must also consider "all the facts and circumstances" surrounding the case, not solely the final outcome (***Phillips v Commissioner***, 851 F2d 1492, 1499 [1988]). The Division has met its burden when it has shown that the issuance of the Notice was "justified to a degree that could satisfy a reasonable person" (***Pierce*** at 565).

F. In this matter, petitioners succeeded, based upon their production of extensive testimony and documentary evidence at the hearing, in meeting their burden of showing that the audit methodology was not reasonably calculated to determine the amount of sales and use taxes due and, consequently, the notices of determination were cancelled. Notwithstanding this result, however, petitioners were not the prevailing party within the meaning and intent of Tax Law § 3030 because the Division was substantially justified in issuing the notices of determination based upon the information in its possession at the time the notices were issued. As detailed above, and, as set forth in greater detail in the determination, despite repeated requests, petitioners never presented a complete set of books and records for the audit period. Those records that were presented for examination were unorganized, incomplete and inconsistent with the restaurant's other records. Under the circumstances, the Division had no alternative but to utilize an external index to determine the amount of sales and use taxes due. The Division then tried several methods to estimate the amount of sales tax due and, in each instance, encountered substantial difficulty. It was at this juncture that the Division acceded to a request by petitioners' representative to conduct

an observation test. Following the observation test, the Division made a series of adjustments in an attempt to reflect the difference in the business models between the Greek restaurant and the remodeled restaurant. Under the circumstances, the Division has clearly shown that its position had a reasonable basis in law and fact and that the issuance of the notice was justified to a degree that would be satisfactory to a reasonable person (***Matter of Grillo***). It follows that petitioners were not prevailing parties within the meaning of Tax Law § 3030(c)(5)(A).

G. Since a determination has been made that the Division was substantially justified in its position, and therefore petitioners are not entitled to an award of costs, it is unnecessary to determine whether the costs claimed are reasonable or appropriate.

H. The application for costs of Forestview Restaurant, LLC and George A. Peppes is denied.

DATED: Albany, New York
March 21, 2013

/s/ Arthur S. Bray
ADMINISTRATIVE LAW JUDGE