JURISDICTION: **OKLAHOMA TAX COMMISSION - DECISION**
CITE: **98-05-14-003 / NOT PRECEDENTIAL**
ID: **P8800223 / P8899225**
DATE: **05-14-98**
DISPOSITION: **SUSTAINED IN PART / DENIED IN PART**
TAX TYPE: **SALES / MIXED BEVERAGE**
APPEAL: **NO APPEAL TAKEN**

FINDINGS OF FACT AND CONCLUSIONS OF LAW

1. At all times relevant herein, the Corporation owned and operated a mixed beverage establishment known as THE CORPORATION.

2. In 1986, the Division conducted an initial inspection of the club. During this inspection the auditor received information concerning admission charges, prices, pour sizes, days and hours of operation, bartenders' names and officers' names.

3. The club utilized a gun system and jiggers for dispensing liquors. Both the bartender and the manager stated that the pour size was one (1) ounce. The inspection additionally confirmed that the gun system was calibrated at one (1) ounce. Further, the bottles were marked at one (1) ounce intervals.

4. In November of 1987, the audit which is at issue in this cause was conducted. At the time of the audit, the club was out of business.

5. The auditor met with THE PRINCIPLE OWNER/PRESIDENT and the accountant for the business, MR. ACCOUNTANT. The information received for performing the audit was the same as that provided during the initial inspection. Although detail records of price changes, pour tests on bartenders and register tapes were requested, none were provided. The gun system was rechecked and it was found to be calibrated at one (1) ounce.

6. Based on the information provided and the wholesalers' reports of purchases of liquor, wine and strong beer, it was determined that Protestants understated their gross receipts for the period of July 1, 1985 through May 31, 1987 by a total amount of $384,615.77. As a result, the Division caused to be issued proposed mixed beverage gross receipts tax and sales tax assessments against the Corporation in the following amounts:

MIXED BEVERAGE GROSS RECEIPTS TAX

Tax:	$38,461.58
Interest:[1]	4,665.52
Penalty:[2]	3,886.16
TOTAL:	$47,013.26

SALES TAX[3]

Tax:	$20,197.33
Interest:	2,423.04
Penalty:	2,019.23
TOTAL:	$24,634.60

7. The initial assessment did not include admission charges in the calculation of gross receipts despite the auditor's knowledge that admissions were charged by the club.

8. In December of 1988, the audit was revised to reflect a change in the prices charged for "well drinks". The revision was precipitated by the receipt of a price list.

9. The revision also included in the computation of gross receipts admission charges in the total estimated amount of $164,909.50. The admission charges were calculated by dividing the total number of drinks sold by the number of days the club was open to find the drinks sold per day. This figure was divided by ten to find the average number of people per day. This average was then multiplied by a cover charge of $3.50.

10. As a result of the change in "well drink" prices and the inclusion of admission charges, the proposed assessments were reduced to the following amounts:

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[1] Represents interest accrued through February 10, 1988 at the rate of one and one-half percent (1½%) per month.

[2] Added pursuant to 68 O.S. Supp. 1983, § 217(c) and represents ten percent (10) of the total amount of tax determined to be due and delinquent.

[3] The proposed sales tax assessment was also issued against THE PRINCIPAL OWNER/PRESIDENT, THE VICE-PRESIDENT AND THE SECRETARY/TREASURER, as officers of the Corporation and as individuals. Protestants do not challenge their individual liability as principal officers of the Corporation.

MIXED BEVERAGE GROSS RECEIPTS TAX

Tax:	$24,834.49
Interest:[4]	7,063.69
Penalty:[5]	2,523.45
TOTAL:	$34,421.63

SALES TAX [6]

Tax:	$13,038.11
Interest:[7]	3,676.73
Penalty:	1,303.81
TOTAL	$18,018.65

11. On cross-examination, the auditor was question extensively concerning any wholesaler purchase invoices dated subsequent to the close of PROTESTANT CORPORATION. The business was closed on April 24, 1987. A review of the master list of invoices indicates that none are dated subsequent to April 24, 1987.

12. The entries on the master list reflecting a date of May 28, 1987, represents the ending inventory which was excluded from the audit. Protestants prepared the ending inventory. It was taken on June 9, 1987 and reflects a date of May 31, 1987.

13. On October 19, 1989, the audit was revised to conform with Oklahoma Tax Commission Order No. 89-10-12-005. As a result, the assessments were reduced to the following amounts:

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[4] Represents interest accrued through February 10, 1989 at the rate of one and one-half percent (1½%) per month.

[5] See, Footnote 2.

[6] See, Footnote 3.

[7] Represents interest accrued through February 15, 1989 at the rate of one and one-half percent (1½%) per month.

MIXED BEVERAGE GROSS RECEIPTS TAX

Tax:	$18,663.37
Interest:[8]	7,412.16
Penalty:[9]	1,866.34
TOTAL:	$27,941.87

SALES TAX[10]

Tax:	$9,798.26
Interest:	3,867.20
Penalty:	979.83
TOTAL	$14,645.29

14. ABLE COMMISSION AGENT "A" of the Alcoholic Beverage Law Enforcement Commission conducted an investigation of THE CORPORATION on December 11, 1986. ABLE COMMISSION AGENT "A" paid $5.00 to enter the club. He was given an empty plastic cup and advised that he could receive an unlimited number of beverages without additional compensation during happy hour. Upon conclusion of happy hour, mixed drinks and wine were sold for 75 cents and $1.00, respectively.

15. ABLE COMMISSION AGENT "B" of the Alcoholic Beverage Law Enforcement Commission conducted an investigation of THE CORPORATION on October 3, 1986. He did not recall paying an admission charge and stated that if there had been he would have reported it. ABLE COMMISSION AGENT "B" paid $9.00 for three (3) shots of Jose Cuervo Gold Tequila which were served in shot glasses.

16. A Certified Public Accountant, testified that as the accountant for the business he prepared monthly bookkeeping records, sales and mixed beverage tax reports, federal and state income tax returns and franchise tax returns. Bank statements, check stubs and other information were utilized to prepare the reports. According to MR. ACCOUNTANT, the auditor reviewed the financial statements and other information contained in his file for

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[8] Represents interest accrued through November 15, 1989 at the rate of one and one-half percent (1½%) per month.

[9] See, Footnote 2.

[10] See, Footnote 3.

purposes of performing the audit.

17. The income tax returns and sales and mixed beverage tax reports were prepared from the same information. MR. ACCOUNTANT is of the opinion that the Corporation did not make additional sales of $248,344.91 during the audit period.

18. MR. ACCOUNTANT also testified that the drinks were grossly underpriced in an effort to lure customers into the club. According to MR. ACCOUNTANT, the prices were fairly consistent.

19. On cross-examination, MR. ACCOUNTANT testified that he did not compare the deposits of the business with any source documentation such as register tapes. He stated that he was never engaged to implement any inventory control measures nor did he conduct any on sight inventories. He further stated that he was never involved in a discussion of the pour sizes utilized by the club. MR. ACCOUNTANT also testified that admission charges were not separately stated, but were lumped in with the gross receipts subject to tax on the mixed beverage tax reports.

20. THE PRINCIPLE OWNER/PRESIDENT testified that THE SECRETARY/TREASURER was the manager of the club, THE ASSISTANT MANAGER and THE HEAD BARTENDER. He stated that during the audit period the club was open either four (4) nights a week or five (5) nights a week. He also stated that an admissions fee was not charged every night, that not everyone entering the club was charged an admissions fee and that the amount of the fee would vary from a high of $5.00 to a low of $1.00. He further testified that the club never dispensed plastic cups and the promotions regarding an admission fee for free drinks never applied to male customers.

21. THE PRINCIPLE OWNER/PRESIDENT testified that the pour size was 1.25 ounces to 1.5 ounces and that at times the pour size exceed 1.5 ounces. He stated that the metal jigger utilized by the bartenders measured 1.25 ounces and that the gun system was calibrated to 1.25 ounces. He also stated that the club served shots in five ounce gibraltor glasses, straight liquor on the rocks in seven ounce gibraltor glasses and mixed drinks in ten ounce gibraltor glasses.

22. THE PRINCIPLE OWNER/PRESIDENT also testified that not all of the price changes which resulted in the first revision to the audit were taken into account. As an example, THE PRINCIPLE OWNER/PRESIDENT identified wine by the glass which was priced from 49 cents to 99 cents during the audit period instead of the $1.50 utilized in the audit. THE PRINCIPLE OWNER/PRESIDENT also identified Jose Cuervo Gold Tequila which was priced at $1.75 rather than $2.50, Kahlua which was priced from $1.25 to $1.50 rather than $2.50 and Amaretto which was priced at $1.75 rather than $2.50.

23. THE PRINCIPLE OWNER/PRESIDENT further testified that he reported all complimentary drinks and paid tax on the retail value of those drinks. He stated that in his opinion not all of the inventory was sold and cited as examples pilferage, waste, spillage and breakage. He also stated that all receipts from the business were deposited in the bank. He further testified that the business did not generate the additional gross receipts determined by the audit.

24. On cross-examination, THE PRINCIPLE OWNER/PRESIDENT testified that although he was responsible for making the purchases for the business, he did not check the invoices against the inventory received. He also stated that he did not cross check the purchases against the sales of the business. THE PRINCIPLE OWNER/PRESIDENT also identified the monthly mixed beverage gross receipts tax reports of THE CORPORATION and agreed that neither the retail value of complimentary drinks nor admission charges were separately reported. He also identified the price list prepared by THE CORPORATION and agreed that the pour size reported thereon for well drinks and premium drinks was one (1) ounce.

25. Protestants timely protested the results of the audit.

ISSUES AND CONTENTIONS

Four issues are identified in the record of these proceedings. These issues are:

1. Whether the method utilized by the Division in auditing the gross receipts from the sale of mixed beverages is statutorily authorized.

2. Whether Protestants sustained their burden of proving that the use of a one (1) ounce pour size in performing the audit is erroneous.

3. Whether Protestants sustained their burden of proving that incorrect prices were used in performing the audit.

4. Whether Protestants sustained their burden of proving that the inclusion of admission charges in calculating the additional gross receipts subject to tax is erroneous.

Protestants contend that the assessments are erroneous. In support of this contention, Protestants argue that the depletion method is not statutorily authorized and is invalid. In the alternative, Protestants argue that the assessments are flawed. In support of this argument, Protestants assert that the Division in performing the audit utilized an incorrect pour size and incorrect prices. Protestants further assert that there is no basis in the record for assessing additional admission charges. Protestants also argue that the use of a formula for determining admission charges is not supported by statute or regulation.

The Division contends that the assessments should be sustained. In support of this contention, the Division argues that the depletion method of auditing the gross receipts from the sale of mixed beverages is statutorily authorized and is a valid exercise of Commission authority. The Division further argues that Protestants have not sustained their burden of proving that the incorrect pour size or prices were utilized in performing the audit. The Division also argues that Protestants have not sustained their burden of proving that the inclusion of additional admission charges in the calculation of the gross receipts subject to tax is erroneous.

APPLICABLE LAW

Mixed beverage gross receipts tax is levied and imposed on total gross receipts from: (1) the sale, preparation or service of mixed beverages; (2) the total retail value of complimentary or discounted mixed beverages; (3) ice or nonalcoholic beverages that are sold, prepared or served for the purpose of being mixed with alcoholic beverages and consumed on the premises where the sale, preparation or service occurs; and (4) any charges for the privilege of admission to a mixed beverage establishment. 37 O.S. Supp. 1985, § 576(A). Total gross receipts is defined to mean the total amount of consideration received as charges for admission to a mixed beverage establishment and the total retail sales price received for the sale, preparation or service of mixed beverages, ice, and nonalcoholic beverages to be mixed with alcoholic beverages. 37 O.S. Supp. 1987, § 576(B)(2).

In addition to the mixed beverage gross receipts tax levied and imposed under the provisions of Section 576(A), sales tax is levied and imposed on the gross receipts from the sale of drinks sold or dispensed by hotels, restaurants, or other dispensers, and sold for immediate consumption upon the premises or delivered or carried away from the premises for consumption elsewhere. 68 O.S. Supp. 1985, § 1354(1)(I). The gross receipts for purposes of calculating sales tax is the total of the retail sale price received for the sale, preparation or service of mixed beverages, ice, and nonalcoholic beverages to be mixed with alcoholic beverages. 37 O.S. Supp. 1985, § 576(E).

The Tax Commission, pursuant to 37 O.S. Supp. 1985, § 586, adopted Regulation XXX-20.[11] This regulation adopts the depletion method for auditing the total gross receipts of a holder of a mixed beverage license or other person transacting business subject to Section 576 of the Oklahoma Alcoholic Beverage Control Act. The depletion method accounts for the number of drinks available for sale, preparation, or service from the total alcoholic beverages received.

[11] Oklahoma Tax Commission Order No. 85-05-16-02. Subsequently codified as Rule 37.018.00 of the Oklahoma Tax Commission Permanent Rules (Eff. March 10, 1989). Currently codified as Rule 710:20-5-8 of the Oklahoma Administrative Code.

The rules and regulations of an administrative agency which implement the provisions of a statute are valid unless the rules and regulations are beyond the scope of the statute, are in conflict with the statute or are unreasonable. See, ***Boydston v. State***, 277 P.2d 138 (Okl. 1954); ***Arkansas Louisiana Gas Co. v. Travis***, 682 P.2d 225 (Okl. 1984); ***Rutherford v. United States***, 438 F. Supp. 1287 (D.C. Okl. 1977). As a general rule, it is presumed that administrative rules and regulations are fair and reasonable and that the complaining party has the burden of proving the contrary by competent and convincing evidence. ***Stiner v. Califano***, 438 F. Supp. 796 (D.C. Okl. 1977); ***State ex rel. Hart v. Parham***, 412 P.2d 142 (Okl. 1966).

The long-continued construction of a statute by a department of government charged with its execution is entitled to great weight and should not be overturned without cogent reasons. ***Peterson v. Oklahoma Tax Commission***, 395 P.2d 388, 391 (Okl. 1964). Where the legislature has convened many times during the period of administrative construction without expressing its disapproval, such silence may be regarded as acquiescence in or approval of the administrative construction. See, ***Atlantic Refining Company v. Oklahoma Tax Commission***, 360 P.2d 826 (Okl. 1961).

The utilization of the depletion method in auditing the gross receipts from the sale of mixed beverages has been upheld by the Tax Commission in numerous decisions. See, Oklahoma Tax Commission Order Nos. 89-08-22-038 and 93-04-22-008. See also, ***McDaved's Bar & Grill, Inc. et al. v. State***, No. CJ-93-8603 (Dist. Ct. Okla. County, August 30, 1995).

Moreover, rules promulgated pursuant to the Administrative Procedures Act[12] are presumed to be valid until declared otherwise by a district court of this state or the Supreme Court. 75 O.S. Supp. 1987, § 306(C). They shall be valid and binding on the persons they affect and shall have the force of law. 75 O.S. Supp. 1987, § 308.2(B). They shall also be prima facie evidence of the proper interpretation of the matter to which they refer. Id.

The burden of proof in all proceedings, unless otherwise provided by law, is on the taxpayer to show in what respect the action or proposed action of the Tax Commission is incorrect. Rule 710:1-5-47 of the Oklahoma Administrative Code. See, ***Enterprise Management Consultants, Inc. v. State ex rel. Oklahoma Tax Commission***, 768 P.2d 359 (Okl. 1988) and ***Big Country Club, Inc. v. Humphreys***, 511 S.W. 2d 315 (Tex.Civ.App. 1974). In ***Big Country Club***, the issue before the court was whether the taxpayer or the taxing officials had the burden of proving the amount of tax due under a depletion audit. The court held that where records do not account for vast quantities of liquor purchased, and the state computes a tax on a reasonable formula, the burden is on the taxpayer to prove that the tax determination was unreasonable, or that it was achieved capriciously or arbitrarily. ***Id***., at 317.

[12] 75 O.S. Supp. 1987, § 250 et seq., § 301 et seq.

In civil cases, a category of proceedings to which administrative proceedings are ascribed, the standard burden of proof is "preponderance of evidence." Black's Law Dictionary, 1064 (5th ed. 1979). See, Oklahoma Tax Commission Order No. 91-10-17-061. "Preponderance of evidence" means "[E]vidence which is of greater weight or more convincing than the evidence which is offered in opposition to it; that is, evidence which as a whole shows that the fact sought to be proved is more probable than not." Id. It is also defined to mean "evidence which is more credible and convincing to the mind ... [T]hat which best accords with reason and probability." Id. In Oklahoma the standard does not require the exclusion of every other reasonable conclusion. ***Chickasha Cotton Oil Co. v. Hancock***, 306 P.2d 330 (Okl. 1957).

CONCLUSIONS OF LAW

1. Jurisdiction over the parties and subject matter of this proceeding is vested in the Tax Commission. 68 O.S. 1991, § 207.

2. Rule 37.018.00 was properly promulgated pursuant to the Administrative Procedures Act and as such, is applicable in these proceedings. 75 O.S. Supp. 1987, §§ 306(C) and 308.2(B).

3. Protestants failed to sustain their burden of proving that the one (1) ounce pour size is incorrect. Evidence of a one (1) ounce pour size consisted of the contemporaneous statements of the bartender, the manager and THE PRINCIPLE OWNER/PRESIDENT. In addition, the auditor testified that the gun system was calibrated to one (1) ounce and that the bottles at the bar were marked at one (1) ounce intervals. The only evidence presented in opposition to the one (1) ounce pour size was the testimony of THE PRINCIPAL OWNER/PRESIDENT which was directly contradictory to his previous statement. Evidence in support of THE PRINCIPAL OWNER/PRESIDENT testimony was not presented. Based on the evidence, the undersigned finds that the Division's utilization of a one (1) ounce pour size in performing the depletion audit is supported by the record and should be sustained.

4. Protestants sustained their burden of proving that the prices for wine, Kahlua and Amaretto should be adjusted. The evidence shows that the price list was relied on in initiating the first revision to the audit. Furthermore, the price charged for wine by the glass was corroborated by the contemporaneous report of ABLE COMMISSION AGENT "A". Accordingly, the undersigned finds that the audit should be revised based on a reduction in the prices for wine, Kahlua and Amaretto.

5. The price for Jose Cuervo Gold Tequila should not be adjusted. Although the price list reflects a price of $1.75 for Jose Cuervo Gold Tequila, the contemporaneous report of ABLE COMMISSION AGENT "B" reflects a price of $3.00. This inconsistency went unexplained. Accordingly, the undersigned finds that Protestants failed to sustain their burden of proving that the price utilized in the audit for Jose Cuervo Gold Tequila was incorrect.

6. The most troublesome aspect of this case is the inclusion of an estimated amount of admission charges in the audit. Although it is undisputed that admissions were charged by the club, the facts do not support the formula utilized in estimating the admission charges. The formula assumes that admissions were charged each day the club was open, that the club was open five (5) day per week and that the average charge for admission was $3.50 per person. The evidence indicates that admissions were not charged each day the club was open, that the club was open sometimes four (4) days and sometimes five (5) days per week during the audit period and that the admission charges varied. Additionally, the undersigned is unaware of any rule or regulation adopting a formula for estimating admission charges. See, ***Fort Howard Paper Company v. Oklahoma Tax Commission***, 792 P.2d 87, 90 (Okl. App. 1989), citing *Oklahoma Tax Commission v. First National Bank & Trust Co.*, 178 Okla. 260, 62 p.2d 1220 (1936). Accordingly, the undersigned finds that the Division erred in including in the audit the estimated amount of admission charges based on a formula unsupported by the facts.

7. Protestants' protest to the proposed assessments should be sustained in part and denied in part.

DISPOSITION

Based on the above and foregoing findings of fact and conclusions of law, it is DETERMINED that the protests of Protestants, CORPORATION AND OFFICERS, be sustained in part and denied in part. It is further DETERMINED that the assessments be adjusted in accordance herewith and that the resultant amounts of tax, penalty and interest, plus any additional interest accrued and accruing, be fixed as the deficiencies due and owing.

ADDENDUM TO FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

NOW on this 17th day of March, 1998, the Findings, Conclusions and Recommendations issued on July 11, 1997, in the above styled and numbered cause CAME on for consideration of additional findings of fact and a recommendation as to the amount of the deficiency TO BE confirmed by an order of the Tax Commission.

The Division, as directed by the Findings, Conclusions and Recommendations, revised the proposed mixed beverage gross receipts tax and sales tax assessments and provided notice of the revisions to Protestants. Protestants have not challenged the revision proposed by the Division.

Upon consideration of the Findings, Conclusions and Recommendations, and the revisions to the assessments, the ADMINISTRATIVE LAW JUDGE FOUND that the following Findings of Fact should be added to and incorporated in the Findings, Conclusions and Recommendations:

1. That notice of the revisions to the assessments was filed of record in this cause on February 12, 1998.

2. That the Division revised the mixed beverage gross receipts tax assessment to an amount of $22,533.42, consisting of tax in the amount of $8,358.35, penalty in the amount of $835.83, and interest accrued through November 15, 1997, in the amount of $13,339.23.

3. That the Division revised the sales tax assessment to an amount of $11,827.88, consisting of tax in the amount of $4,388.13, penalty in the amount of $438.82, and interest accrued through November 15, 1997, in the amount of $7,000.93

4. That the revisions comply with the recommendations set forth in the Findings, Conclusions and Recommendations.

5. That Protestants were provided notice of the revisions.

6. That Protestants did not file a response to the revisions.

The ADMINISTRATIVE LAW JUDGE further FOUND that the following Recommendation should be added to and incorporated in the Findings, Conclusions and Recommendations:

It is further recommended that the amounts in controversy, inclusive of any additional accrued and accruing interest be respectively fixed as the deficiency due and owing.

THEREFORE, the Findings, Conclusions and Recommendations issued on July 11, 1997, WERE amended to include and incorporate the above and foregoing findings of fact and WERE INCORPORATED AND ADOPTED BY THE COMMISSION.

OKLAHOMA TAX COMMISSION

CAVEAT: This decision was **NOT** deemed precedential by the Commission. This means that the legal conclusions are not generally applicable or are limited in time and/or effect. Non-precedential decisions are not considered binding upon the Commission. Thus, similar issues may be determined on a case-by-case basis.