JURISDICTION: **OKLAHOMA TAX COMMISSION - DECISION**
CITE: **2002-04-17-003 / NOT PRECEDENTIAL**
ID: **P0100122**
DATE: **04-17-02**
DISPOSITION: **DENIED**
TAX TYPE: **MIXED BEVERAGE / SALES / TOURISM**
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 COMPANY in ANONYMOUS, Oklahoma and had secured in its name sales and mixed beverage tax permits for purposes of its operations. OFFICER A held the office of President of the Corporation during the audit period. OFFICERS B and C held the offices of Secretary/Treasurer and Vice President of the Corporation, respectively during the audit period. OFFICERS D, E, AND F held the offices of Officers of the Corporation during the audit period.

2. Protestants' operations were the subject of a depletion audit conducted by AN AUDITOR for the Division. The tax period subject to audit was January 1, 1997 through November 30, 1999.

3. According to the Auditor, her first contacts with Protestants were by a telephone conversation and mail whereby she scheduled a face to face meeting with Protestants and provided Protestants with an instruction sheet listing the information required for the audit and papers for purposes of recording Protestants' prices, pour sizes and glass sizes. The Auditor testified that during their initial meeting, Protestants provided her with some of their Z-tapes, some of their other records and a written response to her questions regarding prices, pour sizes, specials and inventories.

4. The original audit and assessment in this cause utilized the prices for liquor, wine and strong beer provided by Protestants and the inventory of liquor purchased during the audit period as shown on the invoices acquired from the liquor wholesalers. Protestants did not provide a beginning inventory of alcoholic beverages, consequently Protestants' ending inventory was not considered in performing the audit.

5. Protestants originally reported a pour rate of one ounce (1 oz.) for liquor and ten ounces (10 ozs.) for wine. According to the auditor, she defaulted to the regulation pour size for wine of six ounces (6 ozs.) for purposes of depleting the wine inventory because "Protestants originally reported a ten ounce (10 oz.) wine glass size, then reported a twelve ounce (12 oz.) glass and pour size." She stated that the discrepancy in the glass and pour sizes reported by Protestants and her opinion that "you can't get ten ounces (10 ozs.) of wine in a ten ounce glass" caused her to default to the regulation pour size for wine. The auditor admitted on cross-examination that she did not measure the wine glasses, but instead relied on the size originally stated by Protestants.

6. Protestants testified that they only served cheap wine, that the actual wine glass size was twelve ounces (12 ozs.) and that wine was poured at a rate of twelve ounces (12 ozs.) during the audit period.

7. After further investigation, a review of Protestants' records and Z-tapes, and a pour test performed on three (3) bartenders on November 13, 2000, the pour sizes and prices for liquor utilized in the original audit were adjusted. The pour size for well drinks was adjusted to the default regulation pour size of one and one-half ounces (1.5 ozs.). According to the auditor, the regulation pour size was used because the actual pour size could not be determined and agreed to based on the discrepancy between the pour size originally reported by Protestants and the pour sizes (1.6 oz., 1.7 oz. and 1.6 oz.) determined by the pour test which was questioned by the auditor because the test was performed approximately one (1) year subsequent to the initiation of the audit. The auditor stated that a 1.62 ounce pour size was allowed for other than well drinks due to the allowance of a two ounce (2 oz.) pour for exotic or multi-liquor drinks.

8. The original audit was also adjusted to take into account exotic drinks. The auditor testified that based on Protestants' Z-tapes exotic drinks represented twenty-four percent (24%) of Protestants' total mixed beverage sales. She further stated that the average rate of pour per liquor was one ounce (1 oz.) which Protestants agreed to and that an average of two ounces (2 ozs.) were allowed for exotic drinks. The average price for exotic drinks was determined from Protestants' Z-tapes. On cross-examination, the auditor testified that she compromised on the use of exotic drinks in the audit since all the information indicated that exotic drinks had low pour sizes and high prices.

9. Protestants testified that they agree to the one ounce (1 oz.) rate of pour per liquor in exotic drinks, but based on the number of liquors in some of their exotic drinks, the average price per ounce should be less. Protestants stated that some of their exotic drinks have up to five (5) different liquors. Protestants did not provide evidence of the prices for exotic drinks containing more than two (2) liquors or the percentage of these drinks sold to total exotic drinks sold. Protestants also stated that exotic drinks represented 30 to 33 percent of Protestants' total mixed beverage sales. Protestants' percentage is based on experience and the fact that the bar is in a college town and college age patrons drink more exotic drinks.

10. The auditor testified that the Z-tapes indicated numerous shots served at Protestants' establishment, but that this was taken into account in the pour size.

11. Admission charges in the amount of $85,643.59 were included in the depletion audit. Protestants testified that they charged and collected the twelve percent (12%) tax and sales tax on some of their admission charges during the audit period. According to the auditor, admission charges were included in the audit because Protestants' gross profit from mixed beverage sales were less than 350 percent of their cost of mixed beverage inventory. In performing the calculation, she added the total of each invoice from the liquor wholesalers, multiplied this by 350 percent and compared this amount with Protestants' gross mixed beverage sales. The auditor further testified that non-intoxicating beer (3.2) was not included in Protestants' costs.

12. Protestants testified that they did charge admission during the audit period, but that the admission charge did not entitle the patron to a complimentary or discounted drink. Protestants also stated that 3.2 beer was included in the calculation of their costs.

13. The only beers listed on the wholesaler invoices are strong beers, in excess of 3.2. Schedule D to the mixed beverage audit workpapers indicates the receipts from strong beer sales during the audit period should have been $27,446.88. The sales tax audit workpapers show the depletion of 3.2 beer either in bottles/cans or in kegs (at costs). The total amount underreported during the audit period was $119,191.24. The sales tax depletion audit of 3.2 beer was performed by obtaining the purchase invoices, which were separate from the liquor invoices, from the distributors. The auditor used Protestants' reported prices of $2.25 and $2.00 and information from the Z-tapes to allow for a coin beer which according to the auditor, coin beer was sold at a lot of different prices, but the parties agreed to an average price of ten cents. Keg beer was allowed at cost because it was given away. The auditor testified that no other specials for coin beer appeared on the Z-tapes. The average price of the 3.2 beer was determined by using a ratio of 54 percent coin beer to 46 percent regular price beer.

14. Protestants testified that they also sold coin beer during the audit period at a price of $1.25 and produced Z-tapes to corroborate the testimony.

15. The mixed beverage depletion audit found that Protestants had underreported their mixed beverage sales during the audit period by the amount of $114,757.56, inclusive of the five percent (5%) variance for undetermined losses. As a result, a proposed mixed beverage gross receipt tax assessment was issued against the Corporation in the aggregate amount of $17,983.30, consisting of tax in the amount of $13,770.91, penalty in the amount of $1,377.09 and interest accrued through April 30, 2001, in the amount of $2,835.30.

16. The sales and tourism tax audits not only included the underreported mixed beverage sales in the amount of $114,757.56, but the underreported 3.2 beer sales in the amount of $119,191.87, inclusive of the five percent (5%) variance for undetermined losses, as found by the sales tax depletion audit for a total underreported amount of $233,948.80. As a result, proposed sales and tourism tax assessments were issued against the Corporation and proposed sales tax assessments were issued against the Officers of the Corporation in the following amounts[1]:

[1] The assessments reflect that interest was accrued through April 30, 2001.

SALES TAX

Tax:	$ 11,697.42
Interest:	3,351.92
Penalty:	1,169.74
Total:	$ 16,219.08

TOURISM TAX

Tax:	$ 233.96
Interest:	61.78
Penalty:	23.43
Total:	$ 319.17

ISSUES AND CONTENTIONS

Five issues are presented for decision. The issues are:

1. Whether it was erroneous to include admission charges in the calculation of the mixed beverage depletion audit.

2. Whether the average price for exotic drinks should be adjusted further to take into account exotic drinks which contain more than two (2) liquors.

3. Whether the percentage of exotic drinks to total mixed beverage sales allowed by the mixed beverage depletion audit is erroneous.

4. Whether the depletion of 3.2 beer should be adjusted to take into account the sale of 3.2 beer at the price of $1.25 during the audit period.

5. Whether the use of the regulation pour size for depleting the wine inventory for purposes of the mixed beverage depletion audit is erroneous.

Protestants contend that the depletion audits and resulting assessments of mixed beverage gross receipts, sales and tourism taxes are erroneous in several respects.

First Protestants contend that they should be allowed a credit for the twelve percent (12%) tax they charged and collected on admission charges during the audit period because they do not give out complimentary or discounted drinks. In the alternative, Protestants contend that their purchases of 3.2 beer were included in their costs for purposes of the formula used by the Division to include admission charges in the mixed beverage depletion audit.

Second, Protestants contend that the average price for exotic drinks was less than that used in the audit since some of their exotic drinks contained more than two (2) liquors. Protestants further contend that exotic drinks represented up to 33 percent of their total mixed beverage sales rather than the 24 percent used by the Division.

Third, Protestants contend that the average price for 3.2 beer should be adjusted to take into account the price of $1.25.

Lastly, Protestants contend that the use of the regulation pour size for wine is erroneous.

The Division contends that the audits and assessments should be sustained. In support of this contention, the Division argues that Protestants failed to present any records or other evidence to support their allegations. The Division further argues that the audit is based on Protestants records and the other information supplied by Protestants.

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 which entitle a person to complimentary mixed beverages or discounted prices for mixed beverages. 37 O.S. 1991, § 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. 1991, § 576(B)(2).

In addition to the mixed beverage gross receipts tax levied and imposed under the provisions of Section 576(A), sales tax and tourism tax are levied and imposed on the gross receipts from the sale of drinks sold or dispensed by hotels, restaurants or bars, 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. 1991, §§ 1354(1)(I) and 50012(A)(2). 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. 1991, § 576(E).

The disposition of mixed beverages shall be taxed in a manner other than by simply computing sales from cash register receipts. See, Kifer v. Oklahoma Tax Commission, 1998 OK CIV APP 34, 956 P.2d 162 (1997). In Kifer, the Court found:

> `Total gross receipts' includes `total retail value' of drinks. `Total retail value' is defined as the `total amount of consideration that would be required for the sale, preparation or service of mixed beverages.' Section 506(33) of the [Oklahoma Alcoholic Beverage Control Act, 37 O.S. 1991, §§ 502 et seq.] defines `sale' as `any transfer, exchange or barter in any manner or by any means whatsoever, and includes and means all sales made by any person, whether as principal, proprietor or as an agent, servant or employee.'

The Tax Commission, pursuant to Section 586 of the Oklahoma Alcoholic Beverage Control Act[2], promulgated Regulation XXX-20.[3] 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. It has been determined to be a reasonable method for determining the total gross receipts subject to tax under Section 576(A). Kifer, supra.

Rule 710:20-5-8 of the Oklahoma Administrative Code provides:

> (a) Liability in general. Every mixed beverage tax permit holder or any other person transacting business subject to the gross receipts tax shall be liable for the tax upon the gross receipts from such beverages (on the basis of the number of drinks available for sale, preparation, or service from the total alcoholic beverages received). Each permit holder or other person shall be liable for the gross receipts tax upon any and all disposition by his agents or employees or any other persons on the premises of the mixed beverage tax permit holders or other person, except upon seizure or other disposition of the alcoholic beverage by employees of the ABLE Commission, Tax Commission, or other law enforcement agencies in the execution of their official duties. [See: 37 O.S. § 576]

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[2] 37 O.S. Supp. 1985, § 502 et seq.

[3] 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.

(b) Audit procedures.

(1) Upon audit of the books and records of a mixed beverage establishment for Gross Receipts Tax, it shall be assumed that spirits have been dispensed at the average rate of one and one-half fluid ounce (1 and oz.), except for drinks with recipes calling for more than one type of spirit or for double portions of spirits, or upon reasonable evidence of a different rate of use.

(2) Wines will be presumed to have been dispensed at the average rate of six ounces (6 oz.) per serving. The Tax Commission may use an average rate greater or less than those set out in this Rule upon reasonable evidence of a different rate of use.

(3) A deduction may be allowed from the gross receipts tax liability determined by an audit for losses due to undetermined causes, not to exceed five percent (5%) of the total gross receipts.

(4) In addition, a deduction may be allowed from the gross receipts tax liability determined by an audit or other investigation of the books and records of a mixed beverage tax permit holder, for alcoholic beverages that are:

(A) consumed in food as verified by the audit;

(B) destroyed due to breakage for which the permit holder has retained the container or that portion thereof that has the unbroken seal and the identification stamp affixed thereto for full unopened bottles or for partial bottles destroyed by breakage for which the permit holder has completed a breakage affidavit listing the date of the occurrence, the brand and type of liquor, the size bottle, the identification stamp number, the approximate amount left in the bottle by 1/10ths, and the cause of the breakage. The affidavit shall be signed by the permit holder and two witnesses;

(C) stolen or destroyed by a disaster such as a fire or flood, provided that reasonable evidence is provided to support a claim. Reasonable evidence might include a copy of a police or sheriff's crime report , or an insurance claim detailing the inventory destroyed by brand, size, and type of liquor;

(D) not consumed, and exist or existed, at the close of a taxable period in question, provided that the amount and nature of the unconsumed inventory has been verified by agents of the Tax Commission, ABLE Commission, or verified by invoice to a mixed beverage permittee or wholesaler approved to purchase the inventory by the ABLE Commission. Partially filled bottles which are not included in a transferred inventory should be verified by a Tax Commission or ABLE Commission agent or agents.

(5) If an establishment was selling alcoholic beverages prior to the starting date of the audit period being used by the Commission in its audit, the establishment shall be required to furnish the Commission with a beginning inventory of all liquor, wine, and strong beer on hand if an ending inventory is offered for audit purposes. When the permittee is unable or unwilling to furnish such an inventory, then no beginning or ending inventories shall be considered for the audit period used and the audit will be conducted solely on the taxpayer's purchases made during the audit period.

With respect to the liability of a mixed beverage tax permit holder for gross receipts tax upon admission charges the Tax Commission promulgated OAC, Rule 710:20-5-5, which provides:

(a) On and after June 29, 1987, the Gross Receipts Tax shall apply to any charges for admission to a Mixed Beverage establishment which entitle a person to complimentary or discounted Mixed Beverages. Such admission charges shall be subject to the Gross Receipts Tax whether:

(1) Expressly stated or advertised by the Mixed Beverage Permit holder that such charges are an entitlement to complimentary or discounted drinks;

(2) Lower prices than can reasonably be expected without an admission charge are established for a limited or indefinite period, and the permit holder is enabled to maintain lower prices due to an admission charge;

(3) A permit holder maintains that lower prices, made possible by an admission charge, are actually normal prices;

(4) An admission charge enables the permit holder to set lower prices at any date before or after the admission charge was established; or

(5) A permit holder represents that an admission charge is for some other purpose than to offset mixed beverage prices if the admission charge in fact enables him to maintain lower prices or allow complimentary drinks to the individual paying such admission charge or to another individual or class of individuals.

(6) It shall be deemed by the Tax Commission that for the purposes of this rule that a gross profit ratio of less than 350% (3 1/2 times cost) shall be considered a lower price than can reasonably be expected without an admission charge. Exceptions to this requirement are "Specials" which are reduced in price for a minimum of seven calendar days as provided for by statute.

(b) Admission charges which are responsible for complimentary and discounted mixed beverages, as well as some other purpose not commonly considered incidental to the operation of a Mixed Beverage establishment, shall be subject to the Gross Receipts Tax upon that portion covering mixed beverages.

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).

Moreover, rules promulgated pursuant to the Administrative Procedures Act[4] 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.

A proposed assessment is presumed correct and the taxpayer bears the burden of showing that it is incorrect, and in what respect. 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 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.

The standard of review in administrative proceedings is preponderance of the evidence. Oklahoma Tax Commission Order No. 99-04-08-003 (citing Oklahoma Tax Commission Order No. 91-10-17-061). That means "evidence which is of greater weight or more convincing than the evidence which is offered in opposition to it; that is, evidence which shows that the fact sought to be proved is more probable than not or best accords with reason and probability." BLACK'S LAW DICTIONARY, 1064 (5th ed. 1977).

[4] 75 O.S. Supp. 1987, ¸ 250 et seq., ¸ 301 et seq.

With respect to the use of specialty drinks for purposes of a depletion audit, a taxpayer's must present evidence of four factors. Oklahoma Tax Commission Order No. 92-08-04-027. Evidence of the pour sizes, prices, recipes and percentage of specialty drinks sold to total drinks sold must be presented. Id.

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. Mixed beverage gross receipts tax is levied and imposed on 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, the total retail value of complimentary or discounted mixed beverages and the total amount of consideration received as charges for admission to a mixed beverage establishment which entitle the person to complimentary or discounted mixed beverages. 37 O.S. 1991, § 576(A) and (B).

3. Sales and Tourism taxes are also levied and imposed on the sale, preparation or service of mixed beverages, ice, and nonalcoholic beverages to be mixed with alcoholic beverages. 68 O.S. 1991, § 1354(1)(I) and 50012(A)(2). The retail sales price received for the sale, preparation or service of mixed beverages, ice, and nonalcoholic beverages to be mixed with alcoholic beverages is used in calculating gross receipts for sales tax purposes. 37 O.S. 1991, § 576(E).

4. The authorized method of auditing a mixed beverage establishment is the depletion method. Regulation XXX-20. This method accounts for the number of drinks available for sale, preparation, or service from the total alcoholic beverages received. Id. It is a reasonable method for determining the total gross receipts subject to tax under Section 576(A). Kifer v. Oklahoma Tax Commission, 1998 OK CIV APP 34, 956 P.2d 162 (1997).

5. The inclusion of the additional admission charges in the calculation of the mixed beverage depletion audit was not erroneous. The evidence establishes that Protestants' gross profit ratio was less than 350% and that the cost of 3.2 beer was not included in the calculation of Protestants' cost. Protestants' admission charges allowed them to maintain lower mixed beverage prices than could reasonably be expected for an indefinite period of time and thus entitled the individuals paying the admission charges discounted mixed beverages when compared to the prices Protestants would have had to charge for mixed beverages without the admission charges.

6. Protestants' evidence is insufficient to show that the average price for exotic drinks is anything other than the price used in the audit. Protestants failed to present any evidence of the prices for exotic drinks containing more than two (2) liquors or the percentage of these drinks sold to total exotic drinks. In addition, Protestants failed to consider the lower pour sizes and higher prices which would be reasonably expected for such exotic drinks.

7. Protestants' evidence is also insufficient to show that the percentage of exotic drinks to total mixed beverage sales allowed in the audit is erroneous. The best and most convincing evidence of the percentage is Protestants' Z-tapes.

8. Protestants' request to adjust the average price of 3.2 beer to take into account a price of $1.25 for such beer is not well considered. In the event a price of a $1.25 is allowed, not only is the percentage of the beer sold at a normal price reduced, but the percentage of coin beer would be reduced by a like amount. Consequently, the average price of 3.2 beer would increase.

9. Protestants' evidence is also insufficient to show that the use of the regulation pour size to deplete the wine inventory is erroneous. Assuming Protestants' wine glasses are twelve ounces (12 ozs.), it is neither reasonable nor probable that in a bar setting a bartender could pour twelve ounces (12 ozs.) in a twelve ounce (12 oz.) wine glass. Further, the undersigned finds that based on Protestants' inconsistent statements of the rate of pour for wine, it is more probable than not that Protestants did not know what the pour rate for wine was during the audit period. Reasonable evidence of a rate of use different than the regulation rate of six ounces (6 ozs.) per serving has not been presented, therefore, the use of the regulation pour size was appropriate.

10. Protestants' protest to the proposed assessments should be denied.

DISPOSITION

Based on the above and foregoing findings of fact and conclusions of law, it is DETERMINED that the protests of THE COMPANY AND THE OFFICERS be denied. It is further DETERMINED that the amounts in controversy, inclusive of any additional interest accrued and accruing, be respectively fixed as the deficiencies due and owing.

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.