



# This Week in State Tax (TWIST)

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## New York: Party Supply Store Selling Exempt Clothing

Recently, an Administrative Law Judge for the New York Division of Tax Appeals issued a lengthy decision addressing whether a party supply retailer properly collected and remitted sales tax on certain sales. The taxpayer sold party supplies, accessories, and costumes both at retail stores and online. Under New York law, items of clothing under \$110 per article are exempt from sales and use tax, but they are subject to local sales tax in jurisdictions that do not conform to the state exemption. By statute, “clothing” does not include costumes. The party supply retailer did not collect the full amount (state and local) of sales tax on sales of certain items. On audit, the Division asserted that numerous items should have been taxed at the full state and local amount because they were intended to be part of a costume based on how the taxpayer marketed and presented the items in its retail stores and online. Using the SKUs assigned to the items, the auditor also determined that the items were listed on the taxpayer’s website as a costume or a costume accessory. For certain other items, the auditor could not verify what the intended use was from the taxpayer’s website and argued the full sales tax rate applied to these items as well.

The ALJ determined that the auditor’s reliance on how the taxpayer marketed its items to determine their taxability was unreasonable. Whether an item qualifies for the clothing exemption is determined at the time of the sale. The sales receipt provided to the customer at the time an item is purchased is what should be used to determine the taxability of the item. The taxpayer’s sales receipts provided to customers at the time of sale included the item’s SKU number and a description of the item purchased. Many of the SKU descriptions listed on the taxpayer’s receipts included identifiers of items that were considered exempt under the Division’s guidance in TB-ST-350, such as hats, shirts, dresses, jackets, and robes. Some of the SKU descriptions, such as tutu, petticoat, skirt, tunic, jumpsuit, capelet and vest, were not specifically enumerated in TB-ST-350 as exempt. However, in the ALJ’s view, these items constituted articles of clothing worn by human beings. In sum, the ALJ concluded that the auditor erroneously relied on the taxpayer’s sales reports and should not have tried to verify the characterization of items from the taxpayer’s website. The taxpayer’s sales receipts included the SKU numbers, and those numbers and descriptions were adequate for determining the taxable status of each item. The ALJ concluded that almost all the disputed items were exempt as clothing. Having found in the taxpayer’s favor on this issue, the ALJ next rejected as “meritless” the taxpayer’s claim that the Division unevenly applied the exemption to similarly situated retailers selling both clothing and costumes in violation of the Equal Protection Clause of the United States Constitution. Please contact Judy Cheng with questions on *Matter of Party City Corporation*.

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