

HEARING
OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Franchise/

Income Tax Appeals Hearing of:

PARTNERSHIP OF BAWANI,

OTA Case No. 18053151

MAREDIA, AND SWARTZ,

DBA VALLEY WIDE DISTRIBUTION,

Appellant.

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REPORTER'S TRANSCRIPT OF PROCEEDINGS

THURSDAY, FEBRUARY 28, 2019

9:00 A.M.

OFFICE OF TAX APPEALS
955 M. STREET, STE. 960
FRESNO, CALIFORNIA

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APPEARANCES

Panel Lead:

WAYNE DANG, ADMINISTRATIVE LAW JUDGE

STATE OF CALIFORNIA
OFFICE OF TAX APPEALS
955 M. STREET, SUITE 960
FRESNO, CALIFORNIA

Panel Members:

JEFFREY ANGEJA, ADMINISTRATIVE LAW JUDGE

LINDA CHENG, ADMINISTRATIVE LAW JUDGE

For Appellant:

Pro Se

For Franchise Tax Board:

JOSH ALDRICH, TAX COUNSEL
STATE OF CALIFORNIA

STEPHEN SMITH, TAX COUNSEL
STATE OF CALIFORNIA

Also Present:

SHELLY ANESLMI

EXHIBITS

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Combined PDF	6

(Exhibits premarked, described
and retained by Administrative
Law Judge.)

1 THURSDAY, FEBRUARY 28, 2019 - 9:00 A.M.

2 ALJ DANG: Welcome to Fresno and the Office of Tax
3 Appeals.

4 We are opening the record in the appeal Partnership
5 of Bawani, Maredia, and Swartz, dba Valley Wide Distribution
6 before the Office of Tax Appeals. The case number is
7 18053151.

8 The hearing is being convened in Fresno on
9 February 28th, 2019 and the time is 1 p.m. Today's case is
10 being heard by a panel of three judges. My name is Wayne
11 Dang and I'll be the lead judge for purposes of conducting
12 this hearing.

13 Also on the panel with me today is Judge Jeffery
14 Angeja and Judge Linda Cheng.

15 At this time will the parties please introduce
16 themselves for the record beginning with Appellant.

17 THE APPELLANT: My name is Harry Swartz.

18 ALJ DANG: Thank you, Mr. Swartz.

19 And CDTFA.

20 MR. ALDRICH: Good afternoon, I'm Josh Aldrich with
21 the CDTFA.

22 MR. SMITH: I'm Stephen Smith with CDTFA.

23 MS. ANESLMI: I'm Shelly Aneslmi with CDTFA.

24 ALJ DANG: Thank you.

25 The issues I have before me today are whether the

1 adjustments -- whether adjustments, sorry, are warranted to
2 the measure for underreported distributions of untaxed
3 tobacco products in California. And also whether CDTFA has
4 shown that the 25 percent fraud penalty is supported by clear
5 and convincing evidence.

6 Mr. Swartz, does that sound correct to you --

7 THE APPELLANT: Yeah.

8 ALJ DANG: -- as far as the issues? Thank you.

9 CDFTA --

10 MR. ALDRICH: Yes.

11 ALJ DANG: -- as far as the issues? Okay. Great.

12 Thank you.

13 Prior to the hearing the parties have communicated to
14 me that they intend to submit as evidence the exhibits that
15 were previously attached to their briefs. CDTFA also had
16 additional submission following the prehearing conference.
17 We took all those exhibits and combined them into an
18 electronic PDF file which were -- which was sent to the
19 parties.

20 Mr. Swartz, did you receive that file and did you
21 have a chance to review that file?

22 THE APPELLANT: Yes, I did.

23 ALJ DANG: Okay. And does that file look accurate to
24 you? As far as your submissions and --

25 THE APPELLANT: Oh, yes.

1 ALJ DANG: It contains everything that you intend to
2 submit?

3 THE APPELLANT: Yes.

4 ALJ DANG: Okay. Thank you.

5 Now are there any objections to admitting that file
6 today to the record?

7 THE APPELLANT: No.

8 ALJ DANG: Thank you. And CDTFA, the same questions,
9 did you receive that file?

10 MR. ALDRICH: We did.

11 ALJ DANG: Okay. And you had a chance to review it?

12 MR. ALDRICH: We did.

13 ALJ DANG: And --

14 MR. ALDRICH: No objections.

15 ALJ DANG: -- no errors? Okay. And are there any
16 objections?

17 MR. ALDRICH: No.

18 ALJ DANG: No objections. Thank you.

19 With that being said, this file, this PDF file, it
20 will now be admitted into the record as evidence.

21 (Exhibits admitted into evidence.)

22 ALJ DANG: As we stated prior to this hearing, there
23 was a little SNAFU and I'd like to change the order of
24 presentation because CDTFA has the burden of proof to
25 establish fraud that would allow them to go first.

1 So CDTFA, if you're prepared, you can begin. And you
2 have 15 minutes for your presentation.

3 MR. ALDRICH: Thank you. The adjusted FBO should be
4 upheld because it was calculated using purchase records
5 obtained directly from out-of-state vendors as well as
6 invoices and bank statements that were received -- or were
7 seized during the execution of a search warrant. These were
8 compared to the actual filings of Appellant and the
9 partnership. Adjustments were given for nontobacco items and
10 credits were applied for seized tobacco items.

11 The audit clearly indicates that \$202,422 in credits
12 were granted for seized tobacco products for the -- this
13 liability period. There were three liability periods. This
14 liability period is from February 1st, 2006 through May 31st,
15 2007.

16 Appellant contended that the measure is not accurate
17 based on theft of tobacco products, however, Appellant has
18 not identified which transactions or products were stolen and
19 they haven't provided any documentary proof that a theft
20 occurred. Typical proof may include an insurance claim or a
21 police report but neither of those were provided. The audit
22 was used -- the audit was performed using the best available
23 records and calculated reasonably, therefore we respectfully
24 request that you uphold the adjusted FBO.

25 There's clear and convincing evidence that Appellant

1 and his partners committed fraud or intended to invade excise
2 tax. Therefore, 25 percent penalty must be added to the
3 adjusted FBO pursuant to Revenue and Taxation Code Section
4 30205. Each partner had extensive knowledge in cigarette and
5 tobacco products.

6 At the time of the search warrant, there were several
7 documents found that would have provided the requisite
8 knowledge to accurately report cigarette and tobacco
9 products. Those included publication for California
10 Cigarette and Tobacco Products Tax Law Guide, Publication 15,
11 California Cigarette and Tobacco Products Tax Registration
12 Guide, as well as California Revenue and Taxation Code
13 Sections 30101 through 30111.

14 In addition, the partners received separate
15 billings -- sorry, separate letters and bulletins from the
16 CDTFA -- well the BOE, formerly the CDTFA. Actually, the
17 reverse of that. Excuse me. Which included information on
18 why tax fraud and the cigarette industry hurts competitors.
19 One of the partners pled guilty to a felony tax evasion prior
20 to joining the partnership. And this was specifically
21 regarding cigarette and tobacco products. Therefore, the
22 partners had the requisite knowledge to correctly report the
23 measure should they have chosen to.

24 During the 16-month liability period, Appellant and
25 his partners underreported the taxable measure by \$821,739.

1 This resulted in a nonpayment of \$384,000 -- two hundred --
2 \$384,240 in excise tax. Of the 16-month period, 14 months
3 were underreported. The monthly average for the
4 underreported months was \$59,409.29. The sum of the
5 underreporting and the monthly average of the underreporting
6 cannot be reasonably attributed to a miscalculation or error
7 which is evidence of fraud or attempt to evade.

8 Furthermore, at the time of the search warrant, there
9 were three -- there were two licensed locations and four
10 locations being used by Valley Wide. So they knew how to
11 obtain a license since they had done so for Suites 202 and
12 203, but we're using Suites 114 and 201 without the proper
13 license. This shows also an intent because the common
14 practice in tobacco products evasion and fraud is to have
15 tobacco products stored at a separate site.

16 Based on the forgoing, Appellant Swartz is jointly
17 and severally liable for the unpaid liabilities of the
18 Bawani, Maredia, Swartz partnership doing business as Valley
19 Wide Distributors. And we concur with the Appeals Division's
20 recommendation. We're available for questions.

21 ALJ DANG: Thank you. Does that conclude your
22 opening statement?

23 MR. ALDRICH: Yes.

24 ALJ DANG: Okay. Mr. Swartz, you have 40 minutes for
25 your presentation. But before you begin, I will need to

1 swear you in because we can only accept testimony under oath.

2 Do you have any objection to being sworn in at this time?

3 THE APPELLANT: (Shakes head no.)

4 ALJ DANG: Okay. If you want to stand and raise your
5 right hand.

6 Do you swear or affirm that the testimony you shall
7 give today will be the truth, the whole truth, and nothing
8 but the truth?

9 THE APPELLANT: Yes, I do.

10 (Appellant sworn in.)

11 ALJ DANG: Okay. You may be seated.

12 And if you're ready, you have 40 minutes to begin.

13 THE APPELLANT: Yeah. It'll be a little lengthy,
14 sorry about that.

15 Good afternoon, ladies and gentlemen. Your Honors of
16 the Court. I'm thankful to have this opportunity to voice my
17 concerns to the Court on issues enforced this day. I would
18 like to ask the Court to please be patient with me
19 considering I'm not as familiar with the procedures as all of
20 you are.

21 What I want to argue is about how the calculations
22 were formed from the beginning. So I have to go back into
23 the search warrant to show that calculations that they
24 actually determined were actually calculated wrong. So what
25 I want to do is go over a little bit of five different codes,

1 laws, and rules that apply to tobacco tax that's upheld here
2 in California.

3 The first one that I wanted to read from is -- I have
4 it in my opening brief that I sent to you. It's on the
5 fourth page. And it's going to be Revenue and Tax Code
6 3123(b). It states that there shall imposed upon every
7 distributor a tax upon distribution of tobacco products based
8 on the wholesale cost of each product at a tax rate that's
9 determined annually by the state BOE which is equivalent to a
10 combine rate of tax imposed on cigarettes by subdivision A
11 and the other provisions of this part.

12 The next Revenue and Tax Code is 3109 and it reads,
13 "Unless the contrary is established, it is presumed that all
14 cigarettes or tobacco products acquired by a distributor are
15 untaxed cigarettes or products and that cigarettes or tobacco
16 products manufactured in state or transported to the state
17 and no longer in the possession of the distributor have been
18 distributed." Pretty simple their statement of how tobacco
19 is brought in and when it's paid upon distribution.

20 The next part I want to read from is my Exhibit
21 Number 2 which is "Tobacco Products Distributor's Tax
22 Return." And on that first page underneath imposition of tax
23 it states, "Every distributor must pay tax upon the
24 distribution of untaxed tobacco products in this state."

25 And if you drop down to the tenth paragraph just

1 under "Filing Requirements," I want to read the first two
2 sentences in there. "Every person who distributes tobacco
3 products in the state must file this tax return on or before
4 the 25th day of the month, following the month for which the
5 tax is due. A tax return must be filed even if there was no
6 distributions during the period covered by the return."

7 I'm going to go on to the second page. And just
8 underneath "Preparation of Return," that second paragraph, I
9 want to read two sentences there also. It says, "Wholesale
10 cost of all tobacco products distributed enter the wholesale
11 cost as defined of untaxed tobacco products as -- that you
12 distributed."

13 So. So now we kind of understand that the tobacco
14 tax is paid upon the distribution and not when you bring it
15 into the state or warehouse within the state. That last
16 example on page 2 there will give you an idea of -- the
17 latter tax example would be I buy \$75,000 worth of tobacco
18 product from a manufacturer or other distributor. And then I
19 sell \$42,000 worth of tobacco. Depending on the month, I
20 would pay the tobacco tax on the \$42,000 worth of tobacco
21 product only on the 25th of said month. The remaining \$33,000
22 worth of tobacco product tax would be paid when and if it
23 sells on the month that it is sold.

24 So now I want to go into my Exhibit Number 3 and I'm
25 going to be reading from page 3 under "The Probable Cause."

1 This is the warrant part, staking a probable cause. And I'm
2 going to read that first paragraph. It's two sentences,
3 actually, under "Results of Investigation."

4 "On April 20th, 2006, your Affiant prepared an
5 investigative complaint alleging that a business known as
6 Valley Wide Distributors in Bakersfield had received untaxed
7 tobacco products in excess of amounts reported to the BOE.
8 This was discovered during your Affiant's, who is Mike Maddox
9 at this time, review of tobacco products shipment of records
10 provided three out-of-state suppliers known as U.S. Smokeless
11 Tobacco, Altadis U.S.A., and Swisher International."

12 These are powerful statements of an allegation by the
13 Affiant. But that statement is actually a flagrant
14 misleading statement. These two sentences as I go forward
15 and show this Court there are -- they are the downfall of the
16 warrant.

17 I want to go into staying in this warrant, I need to
18 turn to page 6. And I'm going to read that first few lines,
19 13 through 20 there. "Your Affiant" -- which is Mike Maddox
20 and Malina (phonetic), and I don't remember his first name
21 was Fred or Frank or something like that -- "performed
22 dumpster dives each evening of the surveillance and found
23 documents evidencing sales and deliveries of tobacco products
24 from Valley Wide Distributors to customers located throughout
25 California, including sales invoices and delivery manifests

1 from DHL. Also several documents were found evidencing
2 multiple purchases and deliveries of untaxed tobacco products
3 from outside suppliers including U.S.T. Altadis, Swisher,
4 Lil' Brown Smoke Shack, Conwood Sales Company, Rick's
5 Tobacco, Renegade Tobacco, and Intercontinental Cigar
6 Company."

7 I'm going to drop down to 25 to 28 and goes over to
8 two more sentences on the following page. "The invoices
9 found during the dumpster dives include those from U.S.T. and
10 Altadis. Each invoice from U.S.T. included a statement at
11 the bottom that read, 'Customer responsible for applicable
12 state tobacco taxes.' Each invoice from Altadis included a
13 statement at the bottom that read, 'Tobacco products
14 described here within are sold without payment of state or
15 local taxes unless such taxes are separately stated upon
16 invoice.' Your Affiant knows from experience that such
17 statements are commonly found on invoices from out-of-state
18 tobacco products suppliers in order to advise the customer of
19 respective state tax obligations."

20 I would like to point out that these dumpster
21 dives -- oh, I want to backtrack just one thing. I only need
22 to show preponderance in this stuff but I also want my Fourth
23 Amendment rights kept in thought as I proceed through this
24 because there is violations there once I get this all laid
25 out.

1 ALJ DANG: Mr. Swartz, if I can just interrupt you
2 for a moment.

3 THE APPELLANT: Yes.

4 ALJ DANG: Today we only -- this panel only has the
5 authority to address the tax at issue and not any --

6 THE APPELLANT: Yeah, I'm not asking you --

7 ALJ DANG: -- violation of your rights.

8 THE APPELLANT: Okay.

9 ALJ DANG: If you could stay focused on that, I'd
10 appreciate it.

11 THE APPELLANT: Okay.

12 ALJ DANG: Thank you.

13 THE APPELLANT: Okay. Sure. Anyways, I'd like to
14 point out that these dumpster dives were on a closed lid
15 dumpster on private property. Also you will notice that Mr.
16 Maddox uses bold print on the liability of tobacco tax as if
17 there's something completely wrong. And please remember that
18 this is all going on before the search warrant is issued.

19 Now what I'd like to do is go to Exhibit Number 1.
20 And that's the "California Department of Tax and Fee
21 Administration Appeals Bureau Decision Statement." And I'm
22 going to go to page 14 and I'm going to read that last
23 paragraph at the bottom down there, and I believe it goes
24 over to a sentence or two on the next page.

25 ALJ DANG: Thank you.

1 THE APPELLANT: "ISOB next found that Petitioner
2 intentionally evaded the cigarette and tobacco products tax
3 law by substantially underreporting its tax liability. When
4 examining the records obtained from the out-of-state vendors,
5 ISOB noted that there were significant differences for each
6 order in which the purchase records were obtained. After
7 executing the search warrant and seized additional purchase
8 records, ISOB determined that the Petitioner substantially
9 underreported its taxable distributions of tobacco products
10 in almost every single quarter of the liability period.

11 "For example, in February 2006, Petitioner made total
12 purchases of untaxed tobacco products of \$56,311 but only
13 reported \$22,116 of taxable distributions of untaxed tobacco
14 products in California which resulted in deficiency of
15 \$32,830 and an error ratio of 58 percent. In March 2006,
16 Petitioner made total purchase of untaxed tobacco products of
17 \$71,858 but only reported \$48,142 of taxable distributions of
18 tobacco products which results in a difference of \$23,000 at
19 a ratio of 33 percent."

20 Staying in the same page here -- oh, one thing I want
21 to do is I want to read that one sentence so you can keep
22 this in the back of your mind. It's right at the beginning.
23 I says, "When examining the records obtained from the out-of-
24 state vendors, ISOB noted that there were significant
25 differences from each quarter in which the purchase records

1 were obtained." Again this is before the warrant is issued.

2 Now staying in the same exhibit, I'm going to go up
3 to page 3 and I'm going to read that first top paragraph up
4 there. "In 2006, CDTFA received an anonymous -- anonymous
5 complaint that Valley Wide was receiving untaxed tobacco
6 products and not properly reporting those taxable
7 distributions of tobacco products. Based on this complaint,
8 an ISOB investigator obtained tobacco products shipment
9 records from three out-of-state vendors, U.S. Smokeless
10 Tobacco brands, Altadis, and Swisher International to Valley
11 Wide. Based on review of the shipment records and Valley
12 Wide's reported tobacco distributions, the investigator
13 determined that Valley Wide was significantly underreporting
14 its distribution of tobacco products in California."

15 First of all, there wasn't an anonymous complaint, it
16 was actually the owner of the business that called in which
17 was Zulfiqar Bawani. I want to reread that last sentence
18 because that goes with that other sentence that I read, that
19 other one, it really ties in together.

20 "Based on the review of the shipment records and
21 Valley Wide's reported tobacco distributions, the
22 investigator determined that the Valley Wide was
23 significantly underreporting its distributions of tobacco
24 products in California." This is all before the warrant is
25 issued.

1 These are powerful allegations from the investigator
2 at the ISOB but nevertheless, he determined this. And this
3 also shows that the CDTFA agrees with the way that ISOB has
4 done their calculations. But I just accused ISOB of an
5 erroneous miscalculation to come into this play. Okay. You
6 just heard a moment ago how tax is paid on tobacco by
7 distribution allowed by law. Then tell me how the ISOB and
8 CDTFA can take monthly purchase receipts and then compare
9 them to monthly tobacco tax returns to get a tax error ratio.
10 You can't. But this is just what you heard in Exhibit
11 Number 1 on page 14 in that last paragraph in their
12 admissions of calculating tax error ratios.

13 And also in Exhibit Number 3, the warrant, page 3,
14 the Affiant admits the same calculating before the warrant is
15 issued. You cannot just take three out-of-state suppliers'
16 purchase receipts. And it would not matter even if you had
17 all tobacco suppliers' purchase receipts and then compared
18 them to monthly tobacco tax returns. Even if you match the
19 same month purchase receipts at the same month tobacco tax
20 returns or of any other month, you will always have a
21 deficiency. This is because you only pay tax on what you
22 sold in that month. There will be times when you have some
23 tobacco products sitting on the shelf for 2 to 12 months or
24 longer before it gets distributed and then you pay said tax.

25 I will like the Court to ask the -- our tax

1 specialists here to explain how you can take only three out-
2 of-state suppliers' purchase receipts then compare them to
3 monthly tobacco tax returns that you only pay tax on what you
4 sold in any particular month and come up with a tax error.
5 You can't.

6 So now I ask the Court how could ISOB's calculations
7 be correct, then? They can't be. This clearly shows that
8 what the ISOB and CDTFA has said is no way possible. And
9 this is the downfall without doing an audit. You cannot --
10 and I say cannot determine a tax error ratio by comparing
11 only three out-of-state suppliers' purchase receipts to
12 monthly tobacco tax returns. You must do a full audit.

13 And again, this all before the warrant is issued.
14 This is simple accounting 101 that any junior college student
15 would understand. These document statements by the ISOB and
16 CDTFA completely contradict what is allowed by law through
17 Revenue and Tax Codes 3123(b), 3109, and the filing of the
18 tobacco products distributor's tax return.

19 This shows a blatant mishandling of calculations and
20 misuse of Revenue and Tax Codes 3123(b) and 3109 on the part
21 of the ISOB and shows perjury to obtain a search warrant.
22 This also shows a complete disregard to the rules of the
23 tobacco products distributor's tax return. You now
24 understand their calculations were wrong from the get-go. Or
25 worse, they were doctored.

1 Is there any questions at this point before I go
2 further?

3 ALJ DANG: No. Yeah, go ahead and please proceed.

4 THE APPELLANT: Okay. I've shown beyond a reasonable
5 doubt right there that these are factual documentations and
6 they're irrefutable, they cannot be denied. I believe that
7 unfortunately, this search warrant was rubber stamped.
8 Because no judge that understands tobacco laws would have
9 agreed in the way that the calculations were done from the
10 beginning.

11 I still do not understand why the CDTFA and ISOB went
12 out of their way to obtain a search warrant on an alleged
13 tobacco tax evasion. In Exhibit Number 9, under AB71,
14 22978.1 and 22978.5, it clearly states that all distributors
15 and wholesalers must keep on hand on site a year's worth of
16 records of purchases and sales and shall be made available
17 for inspection from the CDTFA or law enforcement agency of
18 said records. Not compliant with this law is a crime.
19 Any -- the CDTFA, ISOB, or any law enforcement agency could
20 have just walked in, looked at the records with no search
21 warrant needed.

22 I believe the true intent of the search warrant was a
23 witch hunt for ownership. If the ISOB had so much probable
24 cause and after serving of said search warrant, the Court
25 must ask why was there not any criminal convictions or

1 arrests? In fact, the only reason we are here is
2 vindictiveness on the part of the state. The attorney
3 general will use any opportunity to press any allege charges
4 suggested the CDTFA to go after Valley Wide Distributors on a
5 civil case. This could be seen in Exhibit Number 7 under the
6 conclusion paragraph.

7 So now I ask the Court to dismiss this case due to my
8 Fourth Amendment rights. And I know that you can't do
9 anything on there. But there was never any criminal intent
10 proven and nothing -- and I say nothing that was seized from
11 five different locations that would suggest or show that
12 there was any crime being committed.

13 This case should be dismissed because of a deceitful
14 filing of a probable cause search warrant with an erroneous
15 miscalculation that led to the destruction of Valley Wide
16 Distributors. Also any fraud charges should also be
17 dismissed since their calculations are all based upon
18 purchase receipts and not actual sales that is allowed by Tax
19 and Revenue Codes 3123(b), 3109, and the Rules of the Tobacco
20 Products Distributor's Tax return. They compared purchase
21 receipts to monthly tobacco taxes paid by Valley Wide
22 Distributors to get their tax error ratios without doing an
23 audit on inventory. This again cannot be denied, it is
24 irrefutable.

25 Another one of my main concerns is the way the ISOB

1 and CDTFA has mishandled documentation. The failure of the
2 ISOB handling the return of said search warrant shows a
3 complete lack of competency to return all documentation. As
4 we can see in Exhibit Number 5, the fourth page, the seventh
5 page through the eighteenth and the nineteenth through the
6 twenty-ninth page was not submitted with Exhibit Number 3,
7 the original search warrant that I received from the Kern
8 County Superior Court. I can understand one or two documents
9 not being filed but it should still be none. But in this
10 case, it was 24 pages that were not returned with the
11 original search warrant. It makes us wonder whether it was
12 incompetency or were they trying to hide something? Either
13 way, it was one of these things.

14 The CDTFA shows negligence on my request for
15 disclosure of documentation. If we look at Exhibit Number 6,
16 we can see that I requested all vendor's purchase receipts
17 and the CDTFA sent me a package about that big [indicates]
18 and that's not what a multimillion dollar business of
19 documents would have.

20 And again, they seized two large filing cabinets that
21 were five foot in height, two foot in depth of all
22 documentation. All computers, it was like four or five
23 computers, and several boxes of more documentation as seen in
24 Exhibit Number 3, the first four pages, the twelfth page and
25 the fourteenth page with some of these pages having up to 22

1 lines each of seized property. So I should have received a
2 package a lot bigger than that. And I was only asking for
3 receipts from the vendors so I could do some calculating.
4 But I'm going to get to that in a minute.

5 Now I'd like to ask the CDTFA to tell us how much
6 product they seized illegally that was never returned. Now
7 adding arrogance to ignorance or injury to insult, they
8 seized more than \$2,115,686 worth of tobacco products as seen
9 in Exhibit Number 5, and want Valley Wide Distributors to pay
10 tax on the \$821,731 in a miscalculated tax. These were the
11 24 pages that were not returned with the original search
12 warrant. I've taken the liberty of calculating these
13 documents with actual purchase receipts from vendors dealing
14 with Valley Wide Distributors.

15 As seen in Exhibit Number 5, the first two pages are
16 cost of product purchased by Valley Wide Distributors. The
17 third page is a total of these purchases that were seized by
18 the CDTFA and ISOB. I did guesstimate on some of the
19 cigarette vendors because CDTFA did not send these documents
20 from my request. But I can assure you the price I listed was
21 no less than or more than I listed. This is why you see two
22 totals, a low total and a high total. I used a low total for
23 the illegally seized products. This total also does not
24 include the last 11 pages in Exhibit Number 5 of tobacco
25 products also seized by the CDTFA and ISOB. Again, this

1 cannot be denied, it is irrefutable.

2 Now before I conclude, I would ask the Court to
3 please remember the key words in this issue of an alleged
4 tobacco tax evasion are calculations and audit. These two
5 words are completely intertwined and are the only true way to
6 determine a tax error. In conclusion, we now know without a
7 doubt that the ISOB investigator, Mike Maddox, admits on
8 page 3, Exhibit Number 3 of probable cause that he took only
9 three out-of-state suppliers' purchase receipts and then
10 compared them to monthly tobacco tax returns which
11 contradicts what is allowed by law to determine his tax
12 errors without doing any kind of audit.

13 As I've shown through the ISOB's probable cause
14 search warrant in Exhibit 3 and the CDTFA Appeal Bureau's
15 Decision in Exhibit Number 1, that there is actually no
16 possible way that the ISOB or CDTFA could have known any tax
17 error ratio before the search warrant was served without an
18 audit or after it was served for they seized illegally only
19 80 to 85 percent of the inventory leaving them no possible
20 way for having done any accurate audit on inventory.

21 If we look at the time frame of the ISOB's
22 calculations before the warrant was served, they would have
23 had to have done a complete audit on Valley Wide
24 Distributor's complete records and complete inventory to have
25 calculated any form of tax error. This is how you calculate

1 tax error ratios. You cannot just wing it as did the ISOB
2 and CDTFA. This is the root to the whole problem before us.

3 The sad situation here is so simple that a complete
4 audit of records and inventory could have solved this
5 problem. But now we can never know because of the debacle
6 that these two state agencies have created.

7 I rest my argument at this point.

8 ALJ DANG: Thank you, Mr. Swartz.

9 Mr. Aldrich, at this time do you have any questions
10 or a comment? If you'd like, you can take a minute.

11 MR. ALDRICH: No.

12 ALJ DANG: No questions?

13 MR. ALDRICH: Not for him.

14 ALJ DANG: Okay. Panel members, Judge Cheng, do you
15 have any questions for Mr. Swartz?

16 ALJ CHENG: No questions.

17 ALJ DANG: Judge Angeja?

18 ALJ ANGEJA: They're going to have a rebuttal, both
19 parties? Can I hold my questions till the end?

20 ALJ DANG: Sure. Nothing? So we're going to move to
21 closing arguments since there's no questions for you,
22 Mr. Swartz.

23 CDTFA, if you're ready, you have ten minutes for your
24 closing presentation.

25 MR. ALDRICH: So. Appellant has mentioned the

1 warrants multiple times. As we're aware, we're not here to
2 discuss the validity of the warrants or not. But just to --
3 for clarification of the Court or the Panel, the Superior
4 Court upheld the search warrants, there were multiple search
5 warrants, not just one. There was at least three. And they
6 were upheld after Bawani's attorney filed a motion to quash.
7 Also there seems to be a conflation in between probable cause
8 and what that standard is versus what that standard is for an
9 audit.

10 Regarding the statement that Appellant made that
11 product could sit on the shelf for two months to years, on
12 page 36 of the exhibit package -- let me --there's a
13 memorandum of interview contact, the sentence begins, "Swartz
14 was asked about cigarette and tobacco purchasing." There's
15 a, "Swartz explained that even though some tobacco has a
16 shelf life of a year or so, all cigarettes and tobacco turns
17 over each month, some as often as weekly. Swartz purchases
18 200 to \$300 of cigarettes and tobacco each month."

19 So the idea that tobacco is sitting on shelves for
20 two months or three -- or two years is unlikely since it's
21 his own statement.

22 And then also the audit used the actual records from
23 the business from the -- the purchase invoices from the
24 vendors, the bank statements, so it's quite accurate,
25 actually. There also seems to be some sort of a confusion

1 between the requirements to retain records. Distributors for
2 inspection purposes are required to retain records for a
3 year. And then four -- a year at the location and then four
4 years off premises. However, for audit purposes, Mr. Swartz
5 was put on notice as of the date of the first search warrant
6 that this was a criminal investigation. So he should have
7 been made aware to keep records.

8 Also a fill billing order was sent, I provided that
9 in our submission is the first one I think it was the
10 November 25th, '08. That would be a further reminder or
11 notice, hey, you should be keeping records.

12 Excuse me?

13 MS. ANESLMI: November 5th.

14 MR. ALDRICH: Sorry, it's November 5th. I can
15 provide a page number for you if you'd like. So that would
16 be page 4.

17 Furthermore, regarding his request for records, the
18 two other partners requested all the records be returned to
19 them and there's e-mail documentation of that, should the
20 panel request that. But they contacted us April 28th of 2014
21 and we arranged for the return of all of those documents,
22 computers. They were returned by a shipping company to Texas
23 pursuant to their instruction.

24 Prior to the return, Mr. Swartz could have made
25 arrangements with the ID department to review any of the

1 records he wanted. The -- they were in west Sacramento so he
2 could have come in and made copies of them at his leisure but
3 he didn't do that.

4 MR. SMITH: If I could add one thing. I think to
5 clarify, when Mr. Swartz refers to Mr. Maddox looking at
6 purchase invoices from three vendors and comparing that to
7 sales reports, that wasn't the audit, that was the -- that
8 was the investigatory lead that led the Investigations
9 Division to believe there was underreporting. And it was
10 part of what led to obtaining the search warrant.

11 But after the search warrant was executed and records
12 were seized, the audit was based off of actual records, not
13 just from those three vendors. And so I believe that
14 Mr. Swartz is confused about how the audit was performed.
15 That wasn't the audit, that was just the lead to cause us to
16 perform an audit. And so I think we've been talking past
17 each other a little bit this hearing.

18 MR. ALDRICH: That concludes our closing.

19 ALJ DANG: Thank you, Mr. Aldrich.

20 Mr. Swartz, you have ten minutes for your closing
21 argument.

22 THE APPELLANT: Okay. Trying to go back over a
23 couple things that they're talking about.

24 Tobacco can sit on the shelf for longer than two
25 months or a year. We had plenty of tobacco in the warehouse

1 that was probably several years old, including canceled out
2 cigarette stack. The state comes down and they cancel it
3 out, return us the tax for the purchase of the stamps.

4 And as far as what Mike or the ISOB investigator did.
5 He did do exactly what it states. He took three out-of-state
6 suppliers only and then compared them to tobacco taxes that
7 we paid on a monthly basis that we -- you only pay whatever
8 you sell, so there's no way to really get a tax error from
9 here. There's -- it's impossible.

10 And for as far as them saying that they did an audit,
11 they did not do an audit on inventory which is just as
12 important as the records. You must do both. The records and
13 the inventory to come up with any kind of tax error. That's
14 just the bottom line, there's no way getting around it.

15 There was five search warrants that were served. And
16 all the locations did not meet tobacco licensing as they had
17 stated. Some of them like in one of the warehouses at 114,
18 we just kept miscellaneous merchandise there but yet they
19 claimed there was tobacco there and there wasn't anything, it
20 was never seized.

21 I'm trying to remember what else they were going
22 over. I can't think of -- I mean, other than what I've
23 already stated, there's no way they could have determined
24 that calculation beforehand, it's impossible. And so all
25 that stuff, if you find that to be true in the beginning that

1 they miscalculated, everything after it is false. Because
2 like they stated, we purchase so much a month, and yet we
3 only report it. And it left that differences. It should be
4 that way because it's always carried over.

5 We did not sell -- if I brought in \$200,000 worth in
6 a month, I may have only sold \$100,000 that month. And so
7 the next month I might have sold 150,000. You don't know for
8 sure because unless you do an audit on the full records and
9 inventory, very critical, it's the only way you can tell a
10 tax error.

11 But they show that we reported every month and even
12 we overpaid a couple of times according to them. But that's
13 not neither here or there right now. The main thing is the
14 calculation from the beginning was definitely wrong. There's
15 no way they could have came up with a tax error, it's
16 impossible, without doing a full audit.

17 So today I've shown not through my own doctrine of
18 documentation and warranted statements as to the ISOB and the
19 CDTFA, but today I have shown more holes in the prepared
20 documentation and statements of the CDTFA, ISOB, and the
21 CDTFA Appeal of Bureau's documentations, then should be
22 necessary for automatic dismissal on preponderance alone.

23 I've shown facts upon facts, shown and proven by
24 factual documentation and physical evidence that cannot be
25 denied, it is irrefutable, and it is more likely than not to

1 be true. I've shown and exceeded my requirements of
2 preponderance, I've shown beyond reasonable doubt on the way
3 that they calculated the taxes from the beginning. I'm now
4 asking the Court to serve justice by dismissing this gross
5 negligence of injustice towards Valley Wide Distributors and
6 myself from the miscalculating statements of the ISOB in the
7 beginning. I rest myself. I thank the Court for its time.

8 ALJ DANG: Thank you, Mr. Swartz.

9 Before I turn this over to my Panel members, one of
10 who looks very eager here, I just have two quick clarifying
11 questions for you regarding your arguments. Are you
12 disputing the total purchase amount of tobacco products from
13 this liability period that had been calculated by the CDTFA?

14 THE APPELLANT: Yes. Because whatever they showed in
15 there, they showed complete. The problem is, like I said,
16 there's no way they could have figured out any kind of tax
17 error without doing the full audit with the inventory
18 included. And since they didn't seize all the inventory,
19 there's no true way to get to the bottom line of that audit.

20 ALJ DANG: I'm sorry, my question was just toward the
21 purchases that had been made for that period of time, not the
22 actual amount that you claim --

23 THE APPELLANT: Yeah, I think if I remember right, I
24 read somewhere --

25 ALJ DANG: Are you guys on the same page with --

1 THE APPELLANT: I dispute -- no.

2 ALJ DANG: No?

3 THE APPELLANT: I dispute that too. Because like --
4 they stated like there was \$202,000 worth of tobacco on
5 purchases, but my calculations from Exhibit Number 5,
6 actually I believe it was closer to eight or nine hundred
7 thousand in tobacco products that they seized.

8 See, they took 2 million, over \$2 million worth of
9 our product that we never got back. And there was never --
10 any criminal prosecution. And they still want tax on a
11 miscalculated tax? I don't get it.

12 ALJ DANG: Are you calculating your purchases from
13 different records than what your --

14 THE APPELLANT: No, what they seized. I calculated
15 from what they seized.

16 ALJ DANG: You're saying that that amount is
17 different than --

18 THE APPELLANT: Yes.

19 ALJ DANG: -- the amount --

20 THE APPELLANT: They say 202,000 or something, mine
21 was 800,000.

22 ALJ ANGEJA: Why don't we have them respond to that.

23 ALJ DANG: CDTF, would you like to respond to that?

24 MR. ALDRICH: Yeah. So just to point out, when we
25 seized the tobacco products and we didn't seize stamped

1 cigarettes, we did seize cigarettes, but those aren't
2 included in the audit because there hadn't been a
3 distribution. So cigarettes and tobacco products are treated
4 differently according to the revenue and tax code. And the
5 tobacco products are calculated using the measure, the
6 wholesale cost as the measure and a rate which is set yearly
7 is applied to that measure. Whereas a cigarette will have a
8 set fee for each stamp on each pack of cigarettes.

9 So that's the reason we didn't seize the stamped
10 cigarettes. And it would be an inappropriate to include the
11 seized cigarettes that were ultimately destroyed by the order
12 of the Court because there hadn't been any distribution. If
13 you include them against the cost of the -- if you had
14 included them in the audit against the measure, then it would
15 have been an overage because he hadn't actually distributed
16 them, the partners --

17 MR. SMITH: Cigarettes are not included in the
18 measure of tax here. For the tobacco products, the way the
19 audit was performed was if we had record of purchase, it was
20 presumed taxable. We gave credit for tobacco product that
21 was seized from licensed locations. Because in that
22 instance, that tobacco product would be included in taxable
23 purchases but it would not yet have been distributed so tax
24 would not yet have been opposed upon that product.

25 And so that was -- we allowed credit and I think it

1 was about \$202,000 worth of credits for that.

2 MR. ALDRICH: For this period, it was 209,000 which
3 was resulted -- after other adjustments resulted in a
4 reduction in the overall measure for two-hundred and two,
5 approximately.

6 MR. SMITH: We also seized tobacco product from
7 unlicensed locations and in that case, we did not allow
8 credits. And the reason for that is tobacco products that's
9 stored in an unlicensed location is already subject to tax.
10 The tax is imposed by the seller use of untaxed product, and
11 the use is the exercise of any right of ownership power.
12 There's an exclusion for licensed distributors who hold on to
13 product for resale. So when it's in inventory in a licensed
14 location, it's not yet subject to tax. But if it's in an
15 unlicensed location, it is. So that's why we treated the
16 product in an unlicensed location differently than a licensed
17 location.

18 ALJ DANG: I'm just wondering why the total purchase
19 amounts would be different if everyone's looking at the
20 same --

21 MR. SMITH: I don't know that they are really.

22 ALJ DANG: -- invoices.

23 MR. SMITH: I think sometimes there might be some
24 confusion about whether they're purchase amounts or taxable

25 ALJ DANG: Okay

1 MR. SMITH: -- measure.

2 ALJ DANG: Okay. Thank you.

3 Judge Angeja, do you have questions?

4 ALJ ANGEJA: That answered one of the questions that
5 I had. Because we have -- my experience typically is the
6 unlicensed situation. The problem there is if it's
7 unlicensed, any incident of ownership over the product is a
8 distribution so it's taxable the minute you bring it into the
9 state. We have both, which helps explain some of the
10 confusion.

11 My other question is -- and I understand the argument
12 that you have inventory on hand, sales are less than
13 inventory so there's going to be that discrepancy.

14 THE APPELLANT: Uh-huh.

15 ALJ ANGEJA: You can reconcile -- a person can
16 reconcile ending inventory along with beginning inventory and
17 purchases along with what was reported and should be able to
18 explain that kind of discrepancy. Has that been done?

19 In other words, I understand the argument is pointing
20 out the flaw in the audit method. I'm not -- have we looked
21 at the total records you're saying they didn't look at? Have
22 you been able to provide that and to be able to show there's
23 no errors at all? Because your argument is there's no
24 errors.

25 THE APPELLANT: In what now? I'm confused -- there's

1 a big error from the calculated from the very beginning --

2 ALJ ANGEJA: Yeah. You're comparing total purchases
3 to what was reported and you're saying there's left over
4 inventory on hand.

5 THE APPELLANT: Uh-huh.

6 ALJ ANGEJA: So we should be able to account for that
7 with some sort of an ending inventory reconciliation to show
8 that all that was purchased was sold -- or maybe I'll ask the
9 CDTFA, is it explained by the fact that some of that product
10 was at an unlicensed location and already taxable?

11 MR. SMITH: I think there's two things and Shelly's
12 sending me notes because she spent many hours actually doing
13 the reconciliation of looking at the seized inventory, the
14 seized product, and comparing it to the purchase invoices.

15 There's about \$12,000 in product that couldn't be
16 tied to an invoice so we didn't allow a credit for that, I
17 think that's right.

18 ALJ ANGEJA: And this is wholesale cost measured.

19 MR. SMITH: Yes. There's about \$202,000 worth of
20 product that a credit was allowed forward because it was
21 seized from the licensed location and it could be tied to
22 purchase invoices.

23 MS. ANESLMI: In this audit period.

24 MR. SMITH: In this audit period. And I don't know
25 the amount that was seized from the unlicensed location.

1 MR. ALDRICH: There is \$245,477 in measure seized
2 from the unlicensed location. And then also in the third
3 liability period which was just June '07 to July '07, there
4 was a credit of \$106,465 in measure for the seized tobacco
5 from the licensed location. And you can see that in the
6 exhibit that I submitted. I submitted an audit work paper
7 for -- for the Excel spreadsheet for that third liability
8 period, and it will have included a credit for the seized
9 OCP. I'm just -- provide me one second to find the page.

10 MS. ANESLMI: 120.

11 MR. ALDRICH: Page 120. And so in Columns K, labeled
12 7810, there's a credit C for seized tobacco products --

13 ALJ ANGEJA: Okay.

14 MR. ALDRICH: -- of 106,465.

15 ALJ ANGEJA: Okay. I don't have any more questions.

16 ALJ DANG: I guess following up very briefly
17 Judge Angeja's question. Do you have an explanation for what
18 that difference may be between what you reported and the
19 purchase amounts that were -- sorry, not he purchase -- the
20 amounts computed by CDTFA?

21 THE APPELLANT: My estimates there -- is that Number
22 5 you're talking about is --

23 ALJ DANG: Yes.

24 THE APPELLANT: -- the total of all product that they
25 had seized. They're claiming that part of it's not -- or is

1 seizable because there wasn't a license on that particular
2 building even though we rented the whole building out. And
3 there are different suite numbers but we connected all
4 together all the time except for 114, it was a separate unit
5 but we never kept tobacco there, we only kept miscellaneous
6 merchandise there.

7 ALJ DANG: I guess my question is, are you saying
8 that I didn't purchase this many tobacco products or are you
9 saying that I simply didn't distribute as many as they're
10 claiming I distributed?

11 THE APPELLANT: How much -- you're claiming that we
12 distributed how much?

13 ALJ DANG: CDTFA, you've got the --

14 MR. ALDRICH: The --

15 ALJ DANG: The total measure.

16 MR. ALDRICH: The additional measure --

17 MR. SMITH: Is like 1.4.

18 MR. ALDRICH: -- is eight hundred and --

19 MR. SMITH: Oh. Total distributions.

20 MR. ALDRICH: Total distributions, that would be --

21 ALJ DANG: It's okay, Mr. Aldrich, I --

22 MR. SMITH: We'll get it for you.

23 ALJ DANG: You're saying in essence that you have
24 eight hundred some thousand, odd thousand of distributions
25 are unaccounted -- unaccounted for. Are you saying --

1 THE APPELLANT: That it's not --

2 ALJ DANG: -- you have an explanation for that or are
3 you saying --

4 THE APPELLANT: There's eight hundred --

5 ALJ DANG: -- I simply didn't purchase that many
6 tobacco products?

7 THE APPELLANT: No, there's over \$800,000 worth of
8 tobacco that they seized.

9 ALJ DANG: Okay.

10 THE APPELLANT: So it's kind of funny that they come
11 up with the same calculation.

12 ALJ DANG: Okay. I understand. Understand. Okay.
13 Thank you.

14 THE APPELLANT: And again, one other thing I'd like
15 to point out, too, is they did not seize it all because there
16 was still some tobacco there and stamped cigarettes.

17 So again, there is no way to do an accurate tax error
18 without having it all there.

19 ALJ DANG: I see -- see -- Mr. Aldrich, did you want
20 to respond to?

21 MR. ALDRICH: Well, they continued to receive OTP
22 after the search warrant but -- so it wouldn't have been
23 possible to seize it at that time. But all the purchase
24 invoices were reconciled to the actual products.

25 ALJ DANG: Okay. Thank you.

1 THE APPELLANT: Excuse me, I'm not talking about
2 after the fact, I'm talking after they had left, there was
3 still tobacco products there that they did not seize.

4 ALJ DANG: Okay. I think we understand the position
5 now.

6 THE APPELLANT: Yeah. Okay. Thanks.

7 ALJ DANG: Thank you, Mr. Swartz for the
8 clarification.

9 My Panel members, any further questions before we
10 conclude?

11 ALJ ANGEJA: No.

12 ALJ CHENG: No, no questions.

13 ALJ DANG: Okay, thank you everyone for your
14 presentations and for coming out today. We really appreciate
15 that.

16 The record and this appeal is now closed. And this
17 appeal's submitted for decision.

18 So we'll endeavor to issue a written decision after
19 meeting and deliberating on your presentations and the
20 exhibits here sometime within 100 days. Thanks again.

21 THE APPELLANT: Okay.

22 ALJ DANG: This hearing is now adjourned.

23 MR. SMITH: Thank you.

24 . . .

25 . . .

1 MR. ALDRICH: Thank you.

2 (Whereupon the proceedings were
3 adjourned at 9:56 a.m.)

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