

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:

PHI PHUONG QUACH) OTA Case No. 18083655
) CDTFA Case ID: 930905
) CDTFA Acct. No.: 102-122277
)
) Date Issued: November 8, 2019
)**OPINION**

Representing the Parties:

For Appellant:

Hoang Huu Nguyen, Representative

For Respondent:

Scott A. Lambert, Hearing Representative
Lisa Renati, Supervising Tax Auditor III
Dana Flanagan-McBeth, Tax Counsel IV

For Office of Tax Appeals:

Deborah Cumins,
Business Tax Specialist III

D. CHO, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 6561, Phi Phuong Quach (appellant) appeals an action by respondent California Tax and Fee Administration Department (CDTFA)¹ denying appellant's petition for redetermination of a Notice of Determination (NOD), assessing additional tax of \$10,241.27, plus applicable interest, for the period January 1, 2012, through September 26, 2014.

Office of Tax Appeals Administrative Law Judges Daniel K. Cho, Nguyen Dang, and Richard I. Tay held an oral hearing for this matter in Los Angeles, California, on August 21, 2019. At the conclusion of the hearing, the record was closed, and this matter was submitted for decision.

¹ Prior to July 1, 2017, CDTFA's sales and use tax functions were administered by the State Board of Equalization (BOE). (See Gov. Code, § 15570.22.) Therefore, for ease of reference, when referring to acts or events that occurred prior to July 1, 2017, CDTFA shall refer to BOE.

ISSUE

Whether adjustments are warranted to the determined measure of tax.

FACTUAL FINDINGS

1. Appellant operated a Vietnamese-style restaurant, with sales of beer and wine, in the City of Orange, California, from September 12, 2011, through September 26, 2014.
2. For the audit period, appellant reported total and taxable sales of \$140,944, claiming no deductions.
3. For the audit, appellant provided federal income tax returns for 2011 through 2014, merchant statements (showing credit card deposits) for the audit period, profit and loss statements, and cash register tapes for the first quarter of 2014. According to appellant, the amounts reported on the sales and use tax returns were based on the profit and loss statements.
4. CDTFA prepared six different audit methods² and selected the option that resulted in the lowest liability. Specifically, CDTFA established audited sales using a credit card sales ratio method. It reduced credit card receipts by tips, estimated at 10 percent, and by the amount of tax included. It then used an estimated ratio of credit card sales to total sales of 45 percent, which CDTFA determined based on its experience auditing similar businesses in the area, to establish audited taxable sales of \$270,168, which exceeded reported taxable sales of \$140,944 by \$129,224.
5. The second lowest audit method involved an examination of a similar restaurant, which had reported taxable sales of \$26,526 and \$28,575 for the fourth quarter of 2014 and the first quarter of 2015, respectively. CDTFA computed an average quarterly taxable sales amount of \$27,551 and then applied the average quarterly taxable sales amount³ to the audit period. Based on this method, CDTFA computed an audited total taxable sales amount of \$276,136.

² Although CDTFA's Decision indicates that there was insufficient information for the audit staff to use alternate methods to establish audited taxable sales, the Report of Discussion of Audit Findings outlines the six different audit approaches and the reasoning for choosing the audit liability that was most beneficial to appellant, which occurred prior to the issuance of the NOD. In addition, CDTFA provided these six different methods in the briefing for this appeal.

³ CDTFA reduced the average quarterly taxable sales amount by 5 percent per year to account for yearly price increases.

6. On December 9, 2015, CDTFA issued the NOD for tax of \$10,241.27 and applicable interest.
7. On December 23, 2015, appellant filed a timely petition for redetermination, contending that the credit card to total sales ratio for the restaurant was higher than 45 percent.
8. In a Decision dated July 19, 2018, CDTFA concluded that no adjustment was warranted.
9. This timely appeal followed.

DISCUSSION

California imposes sales tax on a retailer's retail sales in this state of tangible personal property, measured by the retailer's gross receipts, unless the sale is specifically exempt or excluded from taxation by statute. (R&TC, § 6051.) All of a retailer's gross receipts are presumed subject to tax, unless the retailer can prove otherwise. (R&TC, § 6091.) Although gross receipts derived from the sale of food products are generally exempt from the sales tax, sales of food sold in a heated condition and food sold for consumption on or off the premises of the retailer are subject to tax. (R&TC, § 6359, subs. (a), (d)(1), & (d)(7).)

When CDTFA is not satisfied with the amount of tax reported by the taxpayer, or in the case of a failure to file a return, CDTFA may determine the amount required to be paid on the basis of any information which is in its possession or may come into its possession. (R&TC, §§ 6481, 6511.) In the case of an appeal, CDTFA has a minimal, initial burden of showing that its determination was reasonable and rational. (See *Schuman Aviation Co. Ltd. v. U.S.* (D. Hawaii 2011) 816 F.Supp.2d 941, 950; *Todd v. McColgan* (1949) 89 Cal.App.2d 509, 514; *Appeal of Myers* (2001-SBE-001) 2001 WL 37126924.) Once CDTFA has met its initial burden, the burden of proof shifts to the taxpayer to establish that a result differing from CDTFA's determination is warranted. (*Riley B's, Inc. v. State Bd. of Equalization* (1976) 61 Cal.App.3d 610, 616.) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (See *ibid.*; see also *Appeal of Magidow* (82-SBE-274) 1982 WL 11930.)

Of the six different audit methodologies to determine appellant's total taxable sales, CDTFA decided to use option three (i.e., credit card ratio) because it resulted in the lowest tax liability. Specifically, CDTFA used appellant's merchant statements, which contained the credit card deposits, and divided appellant's total credit card deposits by a 45 percent credit card sales ratio to arrive at audited taxable sales. CDTFA explained that it used this 45 percent ratio based

on its experience with similar businesses in this area, but CDTFA declined to provide specific details regarding the similar businesses due to confidentiality reasons.

While we understand the obstacle that CDTFA faces in this situation, it is not necessary for CDTFA to disclose any identifying taxpayer information to support its determination. For example, we would expect CDTFA to provide the actual credit card versus cash data from a similar business in which it calculated its average credit card sales ratio just as CDTFA did in its alternative audit approach option four. It is insufficient for CDTFA to provide an estimate of a credit card sales ratio without some supporting information. (See *U.S. v. Janis* (1976) 428 U.S. 433, 442 [“proof that an assessment is utterly without foundation is proof that it is arbitrary and erroneous.”].) Had CDTFA’s alleged “experience with similar businesses” been the only information available, it is unlikely we would have found the determination to have been reasonable and rational; however, as previously stated, CDTFA actually performed six alternative audits and selected the lowest liability, which was to appellant’s benefit.

Alternative audit approach option four (the use of average reported sales in a similar restaurant) was the second lowest liability amount.⁴ In this alternative audit approach, CDTFA found a similar restaurant and calculated an average quarterly taxable sales amount of \$27,551. It is important to note that CDTFA provided the actual total reported taxable sales for the fourth quarter of 2014 and the first quarter of 2015 of the similar business in calculating the average quarterly taxable sales. CDTFA then computed an audited total taxable sales amount of \$276,136, which was greater than the audited taxable sales of \$270,168 at issue in this appeal. Because this audit approach meets the minimal foundation requirement and is higher than the determined amount, we conclude that CDTFA’s determination is reasonable and rational. Accordingly, the burden of proof shifts to appellant to show an error with the determined measure of tax.

Appellant argues that his reported taxable sales should be accepted instead of CDTFA’s determined measure of tax. Appellant also contends that the estimated ratio of credit card sales to total sales should be increased. Appellant explains that the restaurant, a noodle shop, was located in a depressed area of Anaheim, never made a profit, and, as a result, eventually had to be sold. Although appellant concedes that he discarded guest checks and cash register z-tapes

⁴ It appears that CDTFA has not provided specific information regarding the similar restaurant due to concerns regarding confidentiality.

when the business closed, he states that all sales were recorded in the Quickbooks records, which were provided as part of his opening brief and supports his contentions.

With respect to appellant’s Quickbooks records, appellant has not provided any original source documentation such that we are able to confirm the accuracy of this information. As a result, we are unable to give this evidence any weight in this appeal because it is unclear whether the Quickbooks records are an accurate representation of all of appellant’s taxable sales. Furthermore, the Quickbooks records only list appellant’s sales, by individual item sold, without any grouping to show the total sale to each customer. For each year, there are hundreds of pages of these lists of sales, with no segregation by transaction; no daily, weekly, or monthly totals; and no information regarding the method of payment. Accordingly, not only are we unable to determine whether these records are complete and accurate, but we also are unable to determine what percentage of appellant’s customers paid in cash versus credit card to evaluate CDTFA’s estimated credit card ratio. Therefore, we find that this evidence is not sufficient to support appellant’s contentions, and appellant has not met his burden of proof.

HOLDING

No adjustment is warranted to the determined measure of tax.

DISPOSITION

CDTFA’s decision to deny appellant’s petition for redetermination is sustained.

DocuSigned by:
Daniel Cho
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Daniel K. Cho
Administrative Law Judge

We concur:

DocuSigned by:
Nguyen Dang
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Nguyen Dang
Administrative Law Judge

DocuSigned by:
Richard I. Tay
F8E81582726E448...
Richard I. Tay
Administrative Law Judge