2019 – OTA – 442
Nonprecedential

OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of: **HUKILAU, SAN FRANCISCO, LLC, dba Hukilau**	) OTA Case No. 18042567) CDTFA Case ID: 729474) CDTFA Acct. No. 100-035105)) Date Issued: June 6, 2019)

OPINION

Representing the Parties:

For Appellant: Eric Tao, Member

For the Department: Kevin C. Hanks, Chief
Headquarters Operations Division

For Office of Tax Appeals: Richard Zellmer
Business Tax Specialist III

M. GEARY, Administrative Law Judge: Pursuant to California Revenue and Taxation Code (R&TC) section 6561, Hukilau San Francisco, LLC (appellant) appeals from an action by the California Department of Tax and Fee Administration (Department) determining additional tax measured by $805,299 for the period from July 1, 2009, through April 30, 2012, and recommending that the negligence penalty be deleted, but otherwise recommending that the liability be redetermined without adjustment in accordance with the Notice of Determination (NOD) issued by the Department on March 26, 2013.

Office of Tax Appeals (OTA) Administrative Law Judges Michael F. Geary, Andrew J. Kwee, and Amanda Vassigh, held an oral hearing for this matter in Sacramento, California, on February 26, 2019. At the conclusion of the hearing, we closed the record and took the matter under submission.

ISSUES

1. Whether appellant is entitled to a reduction of the measure of unreported taxable sales.[1]
2. Whether appellant is entitled to a reduction of the measure of unreported self-consumption.
3. Whether appellant is entitled to relief of interest.

FACTUAL FINDINGS

1. During the audit period, appellant operated a restaurant and bar known as "Hukilau" in San Francisco. Mr. Eric Tao was one of three founding members of appellant.
2. In its Daily Sales Journals (DSJs), appellant recorded $179,812 in sales tax reimbursement collected for the period July 1, 2009, through April 30, 2012 (audit period), which equates to recorded taxable sales during the period of $1,952,769.
3. Appellant reported taxable sales for the audit period of $1,393,845, which is $558,924 less than what it recorded in its DSJs.
4. The Department audited appellant for the audit period. It initially used the markup method to compute unreported taxable sales of $1,596,360.[2] After appellant provided point of sale (POS) reports for three months (August 2010, April 2011, and December 2011), the Department recalculated the measure of unreported taxable sales using the POS data and other available records.
5. Appellant's recorded sales tax reimbursement from the three POS reports were higher than the recorded sales tax reimbursement in the DSJs for these three months. The Department computed an error ratio of 11.57 percent by comparing the sales tax reimbursement recorded in the POS reports with the sales tax reimbursement recorded in the DSJs for the three-month test period. Sales tax reimbursement recorded in the DSJs

[1] Because the Department did not know how much of the $784,804 measure of audit item 1 was the result of appellant's failure to report all taxable sales and how much was the result of appellant's collection of excess tax reimbursement, it calculated the deficiency of the audit item as if it was the result of only the former error. This decision should not affect the accuracy of the determination.

[2] The markup method involved computing an audited markup, and then adding the audited markup to audited cost of goods sold to compute taxable sales.

totaled $179,812 for the audit period.[3] The Department multiplied that amount by 1.1157 (1 + the error ratio of 11.57 percent) to compute audited sales tax reimbursement collected of $200,612 for the audit period. The Department compared this amount to reported sales tax due of $129,283, computing unreported sales tax due of $71,329 for the audit period. Finally, the Department divided unreported sales tax due by the applicable sales tax rate on a quarterly basis to compute unreported taxable sales of $784,804 for the audit period.

6. The Department found that appellant recorded in its DSJs self-consumption of $52,241.19 for the period March 1, 2010, through April 30, 2012.[4] Because appellant did not provide DSJ for the period July 1, 2009, through February 28, 2010, the Department used the DSJs for the period March 1, 2010, through April 30, 2012 to compute a monthly average of $2,009.28 ($52,241.19 ÷ 26 months), and multiplied the $2,009.28 amount by 8 to compute self-consumption of $16,074.24 for the period July 1, 2009, through February 28, 2010. When added to recorded self-consumption of $52,241.19 for the period of March 1, 2010 through April 30, 2012, the Department computed audited self-consumption of $68,315.43 for the audit period. The Department concluded that tax applied to self-consumption of alcoholic beverages, but not to self-consumed food. The Department estimated that 30 percent of the self-consumption was related to the taxable beverages[5] and 70 percent was related to nontaxable food. The Department applied the 30 percent ratio to audited self-consumption of $68,315.43, computing unreported taxable self-consumption of $20,495.

7. On March 26, 2013, the Department issued an NOD to appellant.

8. On April 19, 2013, appellant timely filed a petition for redetermination, protesting the NOD.

[3] Sales journals were not available for July and August 2009. Sales tax reimbursement recorded in the DSJ for September 2009 was $5,286. The Department multiplied this amount by 2 to compute sales tax reimbursement of $10,572 for July and August 2009. This amount was added to sales tax reimbursement recorded for the remainder of the audit period to compute sales tax reimbursement from the DSJs of $179,812.

[4] The audited self-consumption consisted of complementary meals and alcoholic beverages provided to employees.

[5] The bases for this 30-percent estimate are not clear, and we do not know whether it includes carbonated beverages.

9. The Department held an appeals conference with appellant on January 6, 2015. In a Decision and Recommendation (D&R) issued on September 24, 2015, the Department recommended that the measure of tax for unreported taxable sales be reduced to $784,804, that the negligence penalty be deleted, and that the petition for redetermination be otherwise denied.[6] This timely appeal followed.

DISCUSSION

Issue 1 - Whether appellant is entitled to a reduction of the measure of unreported taxable sales.

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 served in a restaurant and sales of hot prepared food are subject to tax. (R&TC, § 6359 (a), (d)(2), (d)(7).)

Pursuant to R&TC section 6901.5 and California Code of Regulations, title 18, section (Regulation or Reg.) 1700(b)(1), when an amount represented by a retailer to a customer as constituting reimbursement for sales taxes due is computed upon an amount that is not taxable or is in excess of the taxable amount and is actually paid by the customer to the retailer, the amount so paid is excess tax reimbursement. Excess tax reimbursement is charged when reimbursement is computed on a transaction which is not subject to tax, when tax reimbursement is computed on an amount in excess of the amount subject to tax, when tax reimbursement is computed using a rate higher than the rate imposed by law, and when mathematical or clerical errors result in an overstatement of the tax reimbursement on a billing. (Reg. 1700(b)(1).) When the Department ascertains that a retailer has collected excess tax reimbursement, the retailer will be afforded an opportunity to refund the excess tax to the customers from whom it collected the excess tax reimbursement. (Reg. 1700(b)(2).) In the event of failure or refusal of the retailer to make such refunds, the retailer must pay the excess tax reimbursement to the state. (R&TC, § 6901.5; Regs. 1700(b)(1).)

[6] As recommended in the D&R, the Department prepared a reaudit, which implemented the D&R's recommendations and reduced the determined tax from $149,418.37 to $73,239.58.

When the Department is not satisfied with the amount of tax reported by the taxpayer, or in the case of a failure to file a return, the Department 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, the Department has a minimal, initial burden of showing that its determination was reasonable and rational. (See *Schuman Aviation Co. Ltd. v. U.S.* (2011) 816 F.Supp.2d 941, 950; *Todd v. McColgan* (1949) 89 Cal.App.2d 509, 514; *Appeal of Michael E. Myers* (2001-SBE-001) 2001 WL 37126924.) Once the Department has met its initial burden, the burden of proof shifts to the taxpayer to establish that a result differing from the Department'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 Aaron and Eloise Magidow* (82-SBE-274) 1982 WL 11930.)

At hearing, the Department described the relevant audit events as follows.[7] The Department's comparison of appellant's income tax returns for 2010 and 2011 with its sales and use tax returns for the same years revealed that appellant was significantly underreporting taxable sales for those years.[8] For that reason, the Department first estimated appellant's unreported taxable sales for the audit period at $1,380,625 using a markup method. There is a schedule in the original audit workpapers that suggests the Department also did a credit card and cash sales analysis based on the merchant and bank statements. After appellant provided POS data at the appeals conference, the Department decided to use that data to calculate taxable sales.

The Department noted that the sales tax recorded by the POS system was rarely the same as what was recorded in the DSJs. Appellant did not provide information from the POS system that would back up the summary POS reports. Ultimately, the Department concluded that the sales tax amounts indicated on the POS reports were accurate, and that the POS reports either did not show correct taxable sales or appellant collected excess tax reimbursement. The Department used the sales tax collected per the POS reports to calculate the liability.

[7] Although the audit activities were by the Department's predecessor, the Board of Equalization, for ease of reference, we will simply refer to the "Department."

[8] For example, appellant reported $617,000 more in income on its federal returns than it reported in gross receipts from sales for those years combined. Appellant stated that it sometimes charged for luaus or other entertainment and included that in income. Appellant did not provide records to explain the discrepancy, which is no longer material to the Department's determination.

The evidence shows that the Department determined the liability by calculating the percentage of difference between sales tax recorded by the POS system and that recorded in the DSJs. The difference was 11.57 percent.[9] The Department multiplied the sales tax reimbursement recorded in appellant's DSJs by 11.57 percent to calculate audited sales tax reimbursement collected of $200,612, deducted reported sales tax of $129,283, and divided the remainder, $71,329, by the applicable sales tax rates to calculate the disputed measure of $784,804.

Because appellant did not provide the detailed information from the POS system that backs up the summary POS reports, the Department did not know for certain why the recorded sales tax reimbursement in the POS reports did not reflect the correct tax rate when compared to the taxable sales recorded in the POS reports. The Department argues that either the amounts of taxable sales recorded in appellant's POS reports may be wrong, or, more likely, appellant collected excess sales tax reimbursement, probably as a result of incorrectly calculating the tax when its customers used a coupon.[10] In any event, the Department argues that it is reasonable and rational to base its calculations on the amounts of sales tax reimbursement recorded in appellant's POS reports, and the burden should shift to appellant to establish a more accurate measure. The Department asserts that appellant has not done this.

In regard to excess sales tax reimbursement, the Department argues that appellant cannot identify which customers were charged excess tax reimbursement, and thus, there is no way for appellant to refund the excess tax reimbursement (if any) to its customers. Therefore, appellant must pay the excess tax reimbursement to the State.

Appellant explained that the restaurant was successful for years, and, despite the owners' lack of experience and business acumen, business was good until the 2008 recession. Mr. Tao

[9] Initially, the Department used data provided for one month, December 2011, to calculate a difference of 19.11 percent. Appellant asked the Department to include data for August 2010, when the difference was only 2.64 percent, so the Department combined the two months for an average difference of 9.54 percent. Ultimately, the Department decided that the percentage should be based on all three months for which appellant provided data, which change resulted in an 11.57 percent difference.

[10] For example, "[w]hen a restaurant agrees to furnish a "free" meal to a customer who purchases another meal and presents a coupon or card, which the customer previously had purchased directly from the restaurant or through a sales promotional agency having a contract with the restaurant to redeem the coupons or cards, the restaurant is regarded as selling two meals for the price of one, plus any additional compensation from the agency or from its own sales of coupons. Any such additional compensation is a part of its taxable gross receipts for the period in which the meals are served. Tax applies only to the price of the paid meal plus any such additional compensation." (See Cal. Code Regs., tit. 18, § 1603(a)(2)(C).)

testified that just as the recession was starting to affect the business, companies like Groupon, Inc.[11] started to proliferate. They facilitated what appellant then thought of as a welcome infusion of cash. However, Mr. Tao testified that it turned out to be more like “loan sharking” than a blessing, as customers started claiming their “free” meals and discounts. Appellant states that its margins decreased, and its financial situation worsened. At the hearing, appellant stated that, once it created an atmosphere of discounts, everyone expected discounts all the time. The quality of the food went down, and quality of the service down. Appellant finally closed the restaurant in 2012.

Appellant acknowledges that it did not accurately report taxes due. It insists that the error was due to inexperience and that there was never an intent to underpay. Appellant argues that the Department’s reliance on the sales tax reimbursement amounts referred to in the POS data is misplaced because the evidence shows that the data is wrong. Appellant begins with the argument that the sales tax reimbursement amounts in its POS reports are inaccurate because, when compared to the sales shown by the POS data, they are consistently in excess of the correct tax rates.[12] Appellant objects to the Department’s reliance on the sales tax data, and it argues that a more accurate approach would be to rely on the sales data, as we explain in more detail below.

Appellant calculated what it contends is its underreported tax due for the audit period as follows.[13] First, it calculated sales tax reimbursement amounts by applying the correct sales tax rate to taxable sales recorded in 11 POS reports (the three mentioned above, plus 8 others), and then compared the newly calculated sales tax reimbursement amounts to the sales tax reimbursement recorded in its DSJs for the same months to compute an error ratio of -8.58 percent, meaning that appellant computed sales tax reimbursement from the POS reports that is less than sales tax reimbursement recorded in the DSJs. Appellant reduced sales tax reimbursement recorded in the DSJs for the period July 1, 2009, through March 31, 2012, by 8.58 percent to compute sales tax reimbursement recorded in the POS reports of $158,943. Appellant asserts that the business was open for only part of April 2012, and it was not open at all during May and June 2012. Thus, appellant estimated sales tax for April 2012 of $2,634 by

[11] We will hereinafter refer to all such companies as “Groupon.”

[12] Appellant never explained how it handled the money it received from Groupon.

[13] As explained below, this is not how appellant calculated its taxable sales for reporting purposes.

calculating the average computed sales tax per month for the remainder of the audit period and dividing that amount by 2. The $2,634 amount for April 2012 was added to sales tax reimbursement of $158,943 for the remainder of the audit period to compute sales tax reimbursement from the POS reports of $161,577. This amount was compared to reported sales tax of $129,283 to compute unreported sales tax of $32,294 (as compared to unreported sales tax of $71,329 computed by the Department).

Appellant also argues that the Department's credit card and cash sales analysis at least appears to reach a conclusion consistent with appellant's proposed findings. In that analysis, part of the original audit, the Department added credit card deposits, cash deposits, and recorded cash payouts[14] to compute taxable sales, which was compared to reported taxable sales to compute unreported taxable sales of $358,820. Using the applicable tax rates for each quarter in the audit period, appellant computed that unreported taxable sales of $358,820 equals unreported tax of $32,434, which, it argues, is close to the $32,294 understatement that appellant computed above. Thus, appellant argues that the auditor's analysis of credit card deposits, cash deposits, and recorded cash payouts, supports appellant's computed tax understatement of $32,294.

Alternately, appellant argued in its brief (but not at the hearing) that even if one were to accept that the amounts of sales tax reimbursement recorded in appellant's POS reports were actually collected by appellant, then appellant should be afforded the opportunity to refund the excess tax reimbursement to its customers.[15]

We find that the Department has provided a reasonable and rational explanation for its determination. The amounts of sales tax reimbursement recorded in appellant's POS reports are persuasive evidence of the amounts of sales tax reimbursement collected by appellant. Those amounts would have been entered by the staff who took payment from the customers at the time

[14] The Department explains that a cash payout occurs when cash from the cash register is used to pay for merchandise purchases, employee salary or tips, or some other business expense. A cash payout represents money received from making sales which was not deposited into the bank account. Thus, in this analysis, the cash payouts were added to bank deposits to compute sales.

[15] Appellant also argued in its brief that some of the entries made in the Department's reaudit schedules regarding information from the POS reports are inaccurate. It provided copies of three cash register tapes (December 9, 2011, December 11, 2011, and December 14, 2011), which show tax amounts that are different from what the Department scheduled for those dates. Appellant concedes in its brief that it did not verify the accuracy of all scheduled tax amounts, and it did not make this argument at hearing. It also did not offer those tapes into evidence or testify to the facts relevant to that argument. We will not address that argument further, except to note that it appears substitution of the amount reflected in the above-referenced three tapes would not be advantageous to appellant.

the payments were tendered. We thus find that it was reasonable for the Department to rely on the amounts of sales tax reimbursement recorded in the POS reports to establish an understatement. Consequently, the burden of proof shifts to appellant to provide evidence to establish a more accurate result.

In this case, the imputed tax rate (that is, the tax rate that is achieved by dividing the sales tax reimbursement recorded in the POS reports by the taxable sales recorded in the POS reports) is not the determining factor, because appellant could have collected excess tax reimbursement. Therefore, appellant must provide documentary evidence to show that it did not collect some of the sales tax reimbursement recorded in its POS reports. One way of doing this might be to trace source documents, such as guest checks, to the POS reports, in an effort to show that the amounts of sales tax reimbursement recorded in the POS reports are greater than the amounts of sales tax reimbursement actually charged to and collected from the customers. Appellant has not done this or provided any other convincing evidence that it did not collect the amounts of sales tax reimbursement recorded in its POS reports. Its evidence includes declarations from three "frequent customer[s]" of the restaurant, Brandt Fuse, Kim Kohara, and Alan Omoto, all of whom stated that they were not aware of any irregularities in the tax charged at the restaurant, and testimony from Mr. Tao to the same effect.[16]

We can give little weight to the declarations. First, as we cautioned appellant during the prehearing conference in this matter on February 7, 2019, OTA's Rules for Tax Appeals require that the opposing party be allowed to ask questions of a proposed declarant. (Cal. Code Regs., tit. 18, § 30420.) Appellant indicated at the conference that this would not be possible, and we advised appellant that the declarations would be given limited weight. From a more substantive perspective, there is inadequate information in the declarations to establish the bases for the declarants' claimed knowledge. In essence, the declarants and Mr. Tao state they did not notice any "irregularities in taxes" and none of the regular customers ever complained to them about any such irregularities. Even if we were able to accept every factual statement contained in the declarations and in the similar testimony of Mr. Tao, that evidence does not contradict, much less refute, what appellant's POS system tells us about collected sales tax.

[16] It is unclear whether declarant Alan Omoto is the same "Al Omoto" Mr. Tao identifies as one of the three founding members of appellant.

Appellant explained in one of its briefs that its daily DSJs are not prepared using the POS reports, but are instead prepared using Daily Closeout Sheets. This could explain why the amounts of sales tax recorded in the POS reports do not match the amounts of sales tax recorded in the DSJs. According to appellant, cash in the register at the beginning of the day is subtracted from cash in the register at the end of the day to calculate net cash sales. Credit card charges from credit card merchant statements are added to tips paid for with credit cards to compute net credit card sales. Net cash sales are added to net credit card sales, and then POS tips and tips paid for by credit card are subtracted from the result to compute daily sales. We note that when cash sales reported on the POS reports are different from the net cash sales computed using the Daily Closeout Sheet, appellant uses the amount from the Daily Closeout Sheet in its DSJs. We also note that the Daily Closeout Sheets do not calculate tax amounts, and in its additional brief, appellant acknowledges that it does not know how the sales tax amounts in the DSJs are calculated.[17]

Sales are entered into the POS system as they occur, which is why we find, above, that the POS system is persuasive evidence of the amounts that were charged to and collected from the customers. The sales amounts recorded in the DSJs are calculated using the Daily Closeout Sheets (as explained above) and may not reflect the amounts that were charged to customers. Furthermore, appellant acknowledges that it does not know how the sales tax amounts in the DSJs are calculated. Appellant has not identified any specific errors in the POS reports, except that it disagrees with the sales tax amount. In cases where the amounts in the DSJs are different from the amounts in the POS reports, we find that the POS reports are more reliable than the DSJs because the POS reports are based on entries made at the time of the sale.

We are not persuaded by appellant's argument that the Department's credit card and cash sales analysis supports appellant's argument. Sales tax collected, which is the cornerstone of the Department's determination, is not considered in that analysis. The Department does not rely on credit card and cash sales analysis here. That does not prevent appellant from relying on the analysis and the resulting schedule, but in this case, appellant's reliance is misplaced. The analysis was based on estimated data for 16 of the 34 months analyzed because appellant did not provide all monthly merchant statements and payout information. Also, it is apparent from the

[17] Mr. Tao testified that there was a substantial influx of money from Groupon during the audit period, but he did not explain how appellant accounted for that revenue. The "gross receipts" received by appellant included amounts paid to appellant by Groupon. (R&TC, § 6012; Cal. Code Regs., tit.18, § 1603(a)(2)(C).)

data that appellant did not deposit all cash receipts into the bank account, and in some months, it made no cash deposits at all. Appellant's own DSJs shows that appellant failed to report at least $558,924 in taxable sales while this analysis estimates unreported taxable sales at $358,820.[18] Finally, although appellant's argument states that the results of the credit card and cash sales analysis (approximately $32,433 in tax underreported) are remarkably close to the results of its analysis of taxable sales from the POS data ($32,294 in tax underreported), it appears to us that appellant's math is incorrect, and that former number should be $39,530.19. Based on the evidence, we find that the Department's credit card and cash sales analysis does not establish a more accurate measure of tax.

Appellant correctly points out the law provides that the retailer should be afforded an opportunity to refund the excess tax collections to the customers from whom they were collected, and in the event of failure or refusal of the retailer to make such refunds, the retailer must pay the excess tax reimbursement to the State. (R&TC, § 6901.5; Cal. Code Regs., tit. 18, § 1700, subd. (b)(1).) Given the nature of the business, the fact that appellant did not provide source documents indicating that it knows from whom it collected excess tax, and the period of time that has passed since the sales occurred, it seems unlikely that appellant seriously contemplates any success in that endeavor. Furthermore, Regulation 1700 provides that it was incumbent upon appellant to either prove it refunded the excess tax to its customers or, alternatively, prove that it informed its customers regarding their right to a refund (or credit) and the customers acknowledged such notice. (Regulation 1700(b)(3).) Failing that, the regulation required the Department to issue a determination against appellant for the amount of excess tax reimbursement collected. Given appellant's failure to carry its evidentiary burden, we find that the Department's actions in this regard were appropriate and that the excess tax is payable to the state.

In summary, the Department provided a reasonable and rational explanation for its determination that appellant collected $71,329 more in sales tax reimbursement than it reported as due on taxable sales. It also provided a reasonable and rational explanation for its conclusion that this difference between the recorded sales tax reimbursement collected and the reported sales tax due was the result of appellant failing to report all taxable sales, collecting excess tax,

[18] Appellant's DSJ shows that it collected at least $179,812 in sales tax reimbursement from its clients, which translates to sales of $1,952,769, of which appellant reported only $1,393,845.

or both. Appellant has not carried its burden of establishing a more accurate measure. Based on the evidence, we conclude that appellant is not entitled to a reduction of the measure of unreported taxable sales.

Issue 2 – Whether appellant is entitled to a reduction of the measure of unreported self-consumption.

While the sale or use of many food products are exempt from tax, alcoholic and carbonated beverages are not included in that exemption. (Cal. Code Regs., tit. 18, § 1602(a)(2).) When sales tax does not apply, use tax applies to the storage, use, or other consumption of TPP purchased from any retailer for storage, use, or other consumption in this state, measured by the sales price, unless that use is specifically exempted or excluded by statute. (R&TC, §§ 6201, 6401.) As previously stated, when the Department has met its initial burden of establishing a reasonable and rational basis for its determination, the burden of proof shifts to the taxpayer to establish that a result differing from the Department's determination is warranted, and unsupported assertions are not sufficient to carry that burden. (See *Riley B's, Inc.* and *Appeal Magidow, supra*.)

The Department calculated inventory withdrawals by employees for themselves and others. Total self-consumption (food and beverages) was recorded in the DSJs for most months. Appellant did not provide the DSJs for the months prior to March 2012, and there were no entries for self-consumption in the journals for January through April 2012. The Department calculated the average total for the months for which amounts were recorded (March 2010 through December 2011) and used that amount, $2,009.28, for July 2009 through February 2010. It used zero for the months of January through February 2012 for which there was no entry. The total thus calculated was $60,315.63 for food and beverages. According to the evidence, the Department estimated that 30 percent of the merchandise consumed would have been taxable beverages, based on its experience auditing similar businesses in the same general vicinity, and it applied that percentage per month to calculate the $20,495 measure of consumed merchandise subject to use tax.

Appellant agrees that it owes use tax on the cost of self-consumed alcoholic beverages. However, appellant disagrees with the 30 percent ratio computed by the Department. In its brief, appellant estimated that 10 percent of the meals by employees at lunch included alcoholic beverages, and 20 percent of the meals consumed by employees at dinner included alcoholic beverages. Based on this, appellant argued that a 15 percent taxable percentage would be more reasonable. At the hearing, appellant testified that during at least some of the audit period, it had a policy that prohibited alcoholic beverages during the day. On that basis, appellant argues that the taxable percentage should be reduced from 30 percent to 15 percent, and that the measure of self-consumed taxable merchandise should be reduced from $20,495 to approximately $10,250. Appellant did not provide any documentation to support its arguments regarding self-consumption.

Both the Department and appellant agree that appellant owes use tax on the cost of self-consumed alcoholic beverages. Appellant's records do not break down total self-consumption into categories of alcohol and food. We find that it was reasonable for the Department to estimate that 30 percent of the total self-consumption represented alcohol, based on its experience in auditing similar businesses. Therefore, the burden of proof shifts to appellant to provide evidence to support a lower amount of taxable self-consumption.

Using different arguments with different factual bases, appellant has somehow reached the same conclusion that the Department's determined taxable percentage should be halved from 30 percent to 15 percent. But it has not provided any documentation to support its 15 percent estimate. Appellant's unsupported estimate is not sufficient to support a lower amount of taxable self-consumption. Therefore, we conclude that appellant is not entitled to a reduction of the measure of unreported self-consumption.

<u>Issue 3 - Whether appellant is entitled to relief of interest</u>.

Interest is mandatory. (R&TC, § 6482.) It accrues at the modified adjusted rate per month, or fraction thereof, from the last day of the month following the quarterly period for which the amount or any portion thereof should have been returned until the date of payment. (*Ibid*.) The law provides for relief of interest only under very narrow circumstances, such as the occurrence of a disaster, or unreasonable error or delay by a Board employee in his or her official capacity. (R&TC, §§ 6593, 6593.5.) To be eligible for relief, no significant aspect of the error or delay can be attributed to an act or failure to act by the taxpayer. (R&TC, § 6593.5 (b).) A person making a request for relief must make a statement in writing, under penalty of perjury, setting forth the factual basis for the claim. (R&TC, § 6593.5 (c).)

Appellant states that interest should not apply beyond January 6, 2014, which is the date that appellant states it filed its petition for redetermination with the Department.[19] Appellant argues that, at the time it filed its petition for redetermination, it was willing to accept the results of the auditor's analysis of credit card deposits, cash deposits, and cash payouts for purposes of establishing an understatement. Appellant believes that, after it filed its petition for redetermination, the Department acted wrongly in pursuing other methods of establishing the understatement, and thus, the delay in resolving this appeal is the result of an unreasonable act on the Department's part.

In its response brief, the Department states that the position it has taken during the appeals process was not unreasonable, and thus, interest should not be relieved.

We note, first, that appellant's request for relief of interest (which was contained in its opening brief) was not signed under penalty of perjury as required in R&TC section 6593.5(c). Nevertheless, we will address the substance of appellant's request for relief of interest. We also note that appellant could have paid the tax it agreed is due, which we estimate at $32,294, thus stopping the accrual of interest on that substantial portion of the liability.

In addition, the Department appears to have used at least three methods in its effort to estimate appellant's tax liability: the markup method that was used in the original audit, the analysis of credit card deposits, cash deposits, and cash payouts, which was also part of the first audit, though the Department chose not to rely upon it, and the analysis of recorded versus reported sales tax reimbursement, which the Department relies upon now. Neither party argues that the markup method leads to the most accurate result. Appellant has provided no authority that would require the Department to choose the one appellant favors. We find that the Department was free to choose whichever audit method it concluded would produce the most accurate result. Arguments have been made for and against the two contested audit methods. We have found that the Department acted correctly in computing the understatement based on sales tax reimbursement recorded in appellant's POS reports, and we have considered and rejected appellant's argument in favor of the analysis of the credit card deposits, cash deposits, and cash payouts analysis as a more accurate alternative. On that basis, we reject appellant's argument that the Department unreasonably relied upon a less accurate audit method, thereby committing an unreasonable error or unreasonably delaying resolution of this appeal. Thus, even

[19] The petition for redetermination was actually filed on April 19, 2013.

if appellant were to file a request for relief of interest on this basis and signed under penalty of perjury, we would find that appellant is not entitled to relief of interest.

HOLDING

1. Appellant is not entitled to a reduction of the measure of unreported taxable sales.
2. Appellant is not entitled to a reduction of the measure of unreported self-consumption.
3. Appellant is not entitled to relief of interest.

DISPOSITION

The Department's action in reducing the measure of tax for unreported taxable sales to $784,804, deleting the negligence penalty, and otherwise denying appellant's petition for redetermination is sustained.

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Michael F. Geary
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Michael F. Geary
Administrative Law Judge

We concur:

DocuSigned by:
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Andrew J. Kwee
Administrative Law Judge

DocuSigned by:
Amanda Vassigh
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Amanda Vassigh
Administrative Law Judge