

HEARING  
OFFICE OF TAX APPEALS  
STATE OF CALIFORNIA

In the Matter of the Franchise/

Income Tax Appeals Hearing of:

M.A.C. COSMETICS, INC.,

OTA Case No. 19014177

Appellant.

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REPORTER'S TRANSCRIPT OF PROCEEDINGS

WEDNESDAY, FEBRUARY 26, 2020

10:52 A.M.

OFFICE OF TAX APPEALS HEARINGS  
HEARING ROOM  
400 R STREET  
SACRAMENTO, CALIFORNIA

Reported by Peter Petty

## APPEARANCES

## Panel Lead:

JEFF ANGEJA, ADMINISTRATIVE LAW JUDGE

## Panel Members:

ANDREW KWEE, ADMINISTRATIVE LAW JUDGE

TERESA STANLEY, ADMINISTRATIVE LAW JUDGE

## For Appellants:

JAMES KUHL, KPMG, REPRESENTATIVE

TED S. MATTHIES, KPMG, REPRESENTATIVE

## For California Department of Tax and Fee Administration:

MENGJUN HE, TAX COUNSEL

CHRISTOPHER BROOKS, TAX COUNSEL

RANDY SUAZO, HEARING REPRESENTATIVE

## EXHIBITS

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(Exhibits pre-marked, described  
and retained by Administrative  
Law Judge.)

1 WEDNESDAY, FEBRUARY 26, 2020 - 10:52 A.M.

2 ALJ ANGEJA: We are now on the record in the Office  
3 of Tax Appeals' oral hearing for the appeal of M.A.C.  
4 Cosmetics. The case ID is 19014177.

5 We are in Sacramento, California. The date is  
6 Wednesday, February 26th, and the time is 10 to 11:00.

7 My name is Jeff Angeja, and I'm the lead  
8 administrative law judge for this hearing. My fellow  
9 co-Panelists today are Teresa Stanley and Andrew Kwee.

10 Appellants, could I get you to introduce yourselves  
11 for the record.

12 MR. KUHL: Yes. My name is Jim Kuhl. I'm a director  
13 at KPMG, in the Sacramento office.

14 MR. MATTHIES: I'm Ted Matthies, tax manager at KPMG.

15 ALJ ANGEJA: Okay. And CDTFA?

16 MS. HE: Mengjun He for CDTFA.

17 MR. BROOKS: Christopher L. Brooks for CDTFA.

18 MR. SUAZO: And Randy Suazo.

19 ALJ ANGEJA: All right. Thank you.

20 This appeal involves one issue, which is whether  
21 Appellant properly claimed deductions on its second quarter  
22 2012 through second quarter 2013 tax returns for the amounts  
23 it overpaid on its second quarter 2011 tax return.

24 During the prehearing conferences, the parties agreed  
25 to the admission into evidence of Appellant's A through G,

1 and I'll stop here. We normally make that numerical. Since  
2 they're already marked, I didn't want to change them. So,  
3 through the course of this hearing, rather than just toss out  
4 numbers, please specify whether it's Appellant's alpha or  
5 CDTFA's alpha.

6 CDTFA proposed Exhibits A through U, which the  
7 parties have previously provided both to OTA and to each  
8 other, and no one had any objections at that point. My  
9 understanding is that's still the case. Is that true?

10 MR. KUHL: Yes, it is.

11 ALJ ANGEJA: All right. So, with no objections, I  
12 will admit Appellant's Exhibits A through G and CDTFA's  
13 Exhibits A through U.

14 Based on the prehearing conference, there are no  
15 witnesses from either party today, so we only have argument.  
16 That's still true, and, as we had agreed, we've got  
17 approximately 40 minutes for Appellant's argument and 30  
18 minutes for CDTFA.

19 You saw the last hearing. We'll give you five  
20 minutes, five to 10 minutes, for rebuttal, and if no one has  
21 any procedural questions, I will remind people to speak  
22 slowly and into the microphone for the benefit of the court  
23 reporter. I'll interrupt if I have to, hopefully politely.

24 With that, I'll turn it over to Appellants, and let  
25 you guys start.

1 MR. KUHL: Thank you, Judge Angeja. The only period  
2 that's the subject of this petition, from April 1st, 2012 --

3 ALJ ANGEJA: Microphone. Thank you.

4 MR. KUHL: The only period that is the subject of  
5 this petition is from April 1st, 2012, through March 31st,  
6 2015. During this period, the taxpayer netted approximately  
7 7.2 million dollars in taxable sales to remedy a duplicate  
8 payment that was made on the second quarter 2011 sales tax  
9 return in the amount of approximately \$600,000 in sales tax  
10 accrued.

11 I thought these facts not to be in dispute, that is,  
12 until I read the DNR and the Department's brief, in which  
13 they accurately quote me as representing that the Department  
14 acknowledges the company's 2011 sales tax overpayment, and  
15 the fact that the taxpayer paid more tax than was rightfully  
16 due. The Department's briefing concludes by saying:

17 "The Department was not able to investigate  
18 Appellant's alleged overpayment, and takes  
19 no position on M.A.C.'s claim that it made  
20 an overpayment."

21 In fairness to the Department, Exhibit C, the sales  
22 tax accrual account of the taxpayer that was used in the  
23 reconciliation, was not provided during the appeals  
24 conference. I believe this to be persuasive, and resolve any  
25 doubts as to whether or not there was, in fact, an

1 overpayment of tax.

2           The case we are presenting here today relies upon  
3 facts pertaining to the prior audit, which we believe gives  
4 us grounds, under the doctrines of equitable tolling and  
5 equitable recoupment, for relief of this unjust assessment of  
6 tax, for which we believe the distinguished members of the  
7 Panel have the full legal and moral authority to grant.

8           In June 2011, an error was made by the taxpayer in  
9 which the transactions for the month were imported twice in  
10 computing their sales tax obligation. Given the doubt  
11 expressed by the Department as to whether or not there was,  
12 in fact, an overpayment of tax, I'd like to step back and  
13 explain the mechanics behind the error, and apologize to the  
14 Department if this has not been clear in prior submissions or  
15 statements.

16           When preparing sales tax returns, the  
17 transactional-level detail for all sales is copied into a  
18 completely separate computer system by the party preparing  
19 the returns. This allows the preparer to manipulate the data  
20 and to prepare returns for the numerous jurisdictions where  
21 the taxpayer has a filing obligation. It also preserves the  
22 integrity of the original data in the even the data is  
23 somehow comprised during the return preparation process. So,  
24 while the sales were erroneously duplicated for June 2011 for  
25 the preparation of returns, the original sales data in the

1 accrual account contained the correct data, which was, in  
2 fact, provided to the auditor.

3 With regard to staff's examination of the account, of  
4 the accrual account, Exhibit E, which is the 414(z)  
5 assignment activity history of the auditor, provides as  
6 follows. On July 24th, 2012, the auditor makes the following  
7 entry:

8 "Auditor requested the detail of general  
9 ledger accounts for sales and use tax  
10 payable for California to reconcile tax  
11 reported versus recorded."

12 In addition, the auditor's narrative comments stated  
13 as follows, on the Appellant's Exhibit D:

14 "Accrued sales and use tax was examined on  
15 an actual basis. Taxpayer provided  
16 monthly general ledger for California  
17 sales and use tax. Tax accrued was  
18 compared to the tax reported on the 414(m)  
19 on Schedule 12(d). A review of the  
20 documentation revealed immaterial errors.  
21 No further investigation is warranted."

22 For the record, the 414(m) is the transcript of  
23 returns that the auditor looks to see what was, in fact,  
24 actually reported by the Appellant.

25 MR. MATTHIES: What do you want?

1 MR. KUHL: The exhibits.

2 We do have a blown-up copy of Exhibits B and C. They  
3 are, in fact, the accrual account, and then the actual  
4 worksheet that was prepared by the auditor.

5 MR. MATTHIES: We just blow up copies.

6 MR. KUHL: If you have vision like me, that helps.

7 If I can direct your attention to Exhibit B, the  
8 prior auditor's Schedule 12(d), the sales tax accrual  
9 reconciliation, if you'll note that for June 2011, the amount  
10 of sales tax accrued is listed as \$1,201,341.

11 Now, if you look at the top of the corresponding cell  
12 formula, the sales tax accrued is drawn from another file.  
13 If you'll note, the formula from June 2011, times two, has  
14 been added to the very end of that formula. There is no  
15 other month where this has occurred. Essentially, the data  
16 was drawn from another file and transported over to this one  
17 for the purposes of accruing -- for reconciling sales tax  
18 accrued.

19 Now, if you look to Exhibit C, this is the one that  
20 had not previously been provided during the appeals  
21 conference process. This is the sales tax account, accrual  
22 account, for the taxpayer. For the most part, these monthly  
23 totals match the sales tax accrual reconciliation prepared by  
24 the auditor. However, if you look at June 2011, the amount  
25 is \$600,670.43. Multiplying this amount times two gives you

1 the \$1,201,341 that the auditor says was in the accrual  
2 account.

3           Clearly, the auditor falsified the entry on the  
4 accrual reconciliation to make these amounts match. If you  
5 find the Department's dismissal of the times two adjustment  
6 to be plausible for an unknown reason, then why wouldn't such  
7 an adjustment have been warranted for all of the other  
8 months?

9           We believe there are many grounds upon which the  
10 CDTFA could have remedied this in an equitable manner. Field  
11 Audit Manual Section 0401.05 states -- under the heading  
12 "Approach to Auditing Credits and Refunds," in relevant part,  
13 states as follows:

14           "The primary purpose of the audit program  
15 is to provide reasonable assurance that  
16 taxpayers pay neither more nor less tax  
17 than required by law. Consequently, the  
18 CDTFA is just as concerned with refunding  
19 overpayments as well as collecting  
20 underpayments. If a refund situation is  
21 noted in the course of an audit, the  
22 auditor should secure a claim for refund  
23 from the taxpayer utilizing Form 101,  
24 Claim for Refund of Credit."

25           Clearly, the auditor did not follow this procedure.

1 Rather, they intentionally concealed the error and denied the  
2 taxpayer a refund. The auditor should have informed the  
3 taxpayer of the refund that was due, and documented their  
4 instructions in the audit working papers.

5           There are a number of other paths where the CDTFA  
6 could have taken to resolve this matter in the interest of  
7 fair and efficient tax administration. First, California is,  
8 by statute and policy, very lenient regarding filing  
9 requirements. For example, if a taxpayer submits a check  
10 with just the account number on it, it's construed as being  
11 accepted as a tax return being filed.

12           Now, with regard to refunds, the statute only  
13 requires that a refund be in writing and state the specific  
14 grounds upon which it's founded, and it is our contention  
15 that the records provided, that clearly indicate an  
16 overpayment of tax was made, establish an informal claim for  
17 refund, whereby the state was placed on constructive notice  
18 that a refund was due.

19           An informal claim for refund exists when the claim  
20 contains a written component, the claim describes the legal  
21 and factual basis for the refund, and a taxing authority has  
22 actual or constructive notice that the taxpayer is asserting  
23 a right to a refund for a specific period.

24           Correspondence throughout the first audit established  
25 the written component of this claim. In 2012, the auditor

1 became aware of the taxpayer's 2011 overpayment. The auditor  
2 and the taxpayer exchanged various correspondence, written  
3 and otherwise, regarding M.A.C.'s overstated June sales.  
4 M.A.C. providing documentary evidence related to the  
5 reporting error, and generally made itself available with  
6 respect to all inquiries during the course of the first  
7 audit. The totality of these events constitutes an informal  
8 claim for refund.

9           Second, it is our contention that the taxpayer is  
10 entitled to equitable relief through the doctrines of  
11 equitable recoupment or estoppel, and thus equitable tolling  
12 of the statute of limitations should be applied to permit the  
13 current liability to be offset by the prior overpayment of  
14 tax. Equitable tolling suspends the statute of limitations  
15 when there's prejudice to the taxpayer's action (sic) and the  
16 interests of justice so require.

17           Even where equitable tolling may not apply, a  
18 taxpayer can recoup a tax overpayment through the doctrine of  
19 equitable recoupment. This doctrine allows taxes erroneously  
20 paid to be recouped against a properly asserted deficiency  
21 under the following criteria: The same transaction, item, or  
22 taxable event has been subject to two taxes; the taxes are  
23 inconsistent in that the Tax Code authorizes only a single  
24 tax; the tax sought to be recouped is time-barred; and there  
25 is an identity of interest between the parties paying the

1 duplicative tax. In this case, they are, in fact, the same  
2 party.

3 I believe all of these elements are met. The  
4 Department contends that, in this case, the same transactions  
5 have not been subject to two taxes, as evident by the fact  
6 that the overpayment occurred in June 2011, but the  
7 disallowed deductions were taken in the following year, and I  
8 respectfully disagree with this characterization.

9 Each sales transaction was errantly imported twice,  
10 in error, and thus each transaction was, in fact, incorrectly  
11 reported as subject to tax twice. While reviewing the sales  
12 tax accrual account, the sales tax accrual account was  
13 correct. Hence the auditor doubled it to conceal the error,  
14 for reasons that are unclear.

15 The subsequent periods in which the total taxable  
16 sales were underreported do not pertain to a specific  
17 transaction. Within the context of recoupment, a transaction  
18 may include a series of occurrences, dependent not so much  
19 upon the immediateness of their connection as upon their  
20 logical relationship.

21 To uphold the determination that is subject to this  
22 petition would, in fact, constitute a second assessment of  
23 tax on the same transactions. Our position revolves around  
24 the doctrine of equitable remedies, as the taxpayer has, in  
25 fact paid the tax twice, first in the second quarter of 2011,

1 and now they've remitted the tax that was assessed in this  
2 determination, with the CDTFA culpability a determinative  
3 factor in harming the taxpayer.

4 MR. MATTHIES: So I'm going to add a little bit.  
5 There's going to be some repetitiveness here. Is it this one  
6 or this one (indicating)? This one?

7 ALJ ANGEJA: It's both, because it's livestream as  
8 well as record for the court reporter. Go ahead.

9 MR. MATTHIES: There's going to be some things that  
10 are repeated here, but some of them bar repeating -- or bear  
11 repeating -- so bear with me.

12 Our client was harmed based on the representations or  
13 actions of the auditor, resulting in an unjust enrichment to  
14 the state to the tune of approximately \$600,000. Now, how  
15 did that occur? As my colleague mentioned, the duplicate  
16 sales were twice reported in the 2011 period. There was some  
17 confusion in discussion in the decision of recommendation,  
18 and I'll refer to the Department's Exhibit B.

19 There are some e-mails, and there's an e-mail in  
20 particular, August 30th of '18, number four, where the  
21 Appeals Bureau officer sent an after-the-conference e-mail to  
22 the Department, asking for clarification on the times two,  
23 why was there a times two put in that cell? And the  
24 response -- and I can actually read from --

25 "Has the BTFD" -- so Business Tax and Fee

1 Division -- "discussed the formula in  
2 Schedule 12(d), line C53, of the 2012  
3 audit with Ms. Gunik?"

4 I think Ms. Gunik is the auditor:

5 "What insight, if any, can she provide  
6 with respect to the multiplier that was  
7 incorporated into the formula?"

8 The response came back as "Ms. Gunik was able to  
9 provide the source documents for the accrual account," which  
10 we presume is the big exhibit you have there, and she was not  
11 able to provide any insight into how the number two was  
12 incorporated, and I think, in the DNR itself, there was  
13 discussion with regard to the argument number three about  
14 "Well, we don't know who would have inserted number two or  
15 times two into that workpaper."

16 I want to refer to the Appellant's Exhibit A, and why  
17 I contend that this was the auditor and the auditor's work  
18 that did this. Exhibit A, or Appellant's Exhibit A, which is  
19 Audit Manual Section 0101.20, it's "The Relationship of a  
20 Taxpayer and an Auditor":

21 "The auditor should aid the taxpayer in  
22 gaining a correct understanding of the  
23 law, and demonstrate that we are willing  
24 to recommend a refund and an overpayment,  
25 as we are to propose a deficiency

1           determination."

2           I'm going to combine that with Appellant's Exhibit G,  
3 "Audit Working Papers Defined and Described." That is Audit  
4 Manual Section 0301.10, and the term "audit working papers"  
5 as used in this chapter means:

6           "The worksheets and other pertinent  
7 material compiled by the auditor in the  
8 course of making a field audit."

9           So there's no doubt that the facts, the evidence,  
10 shows that the auditor created this workpaper. There would  
11 be no cause for a workpaper to be handed or delivered to our  
12 client and have them -- it just doesn't happen. Exhibit D,  
13 Appellant's Exhibit D -- excuse me. Strike that for a  
14 second.

15           Bear with me one sec. Lost my train of thought  
16 there. Back to Exhibit G, Appellant's Exhibit G. It's also,  
17 I think, further evidence which I haven't provided, but I  
18 think just to talk about it is -- when you look at the Excel  
19 file properties, the Excel file properties do show that this  
20 was a BOE, at the time, template that was created in December  
21 9th of 1997 at 8:59 a.m.

22           It was last saved by Tanya Jenkins from the OHB  
23 office, and it has the date that it was last saved, being  
24 September 11th, 2013, at 1:44. It also shows the author of  
25 that workbook to be the auditor. So I don't think there's

1 any doubt, at least in my mind, that the evidence shows that  
2 this was a workpaper created by the auditor, and the auditor  
3 put in the times two.

4 ALJ ANGEJA: Can I interrupt you? The date that you  
5 said that thing was created, the Excel file?

6 MR. MATTHIES: Yes.

7 ALJ ANGEJA: I heard "'97." I know that --

8 MR. MATTHIES: Yes. And if I may --

9 ALJ ANGEJA: So they're using it and replicating it.

10 MR. MATTHIES: Having worked, you know, many years at  
11 that agency, they had audit templates. They had workbook  
12 templates. So somebody had created a workbook template that  
13 would have, you know, maybe multiple schedules. It would  
14 have the schedule headings kind of prepopulated, some of the  
15 cosmetics to it. So that was December 9th of 1997, and the  
16 last date it was saved was September 11th of 2013. It was  
17 printed August 21st, which is right about the end of the  
18 audit period.

19 MR. KUHL: And that should be visible on the  
20 electronic files you have, just looking at the properties.

21 MR. MATTHIES: Yes. And I did print out -- I didn't  
22 provide it, but I printed it out this morning. I just wanted  
23 to see.

24 Then Appellant's Exhibit D, the audit comments from  
25 the 2012 audit, the verification comments, audit workpaper,

1 Schedule 12, page two, and on that, that auditor's  
2 comments -- so they accrued the sales and use tax on an  
3 actual basis. The taxpayer provided the monthly general  
4 ledger for the California sales and use tax, which is this  
5 exhibit here (indicating), the Appellant's Exhibit C -- no,  
6 that's the formula. The other one. Okay.

7 The comments say that the tax accrued was compared to  
8 the tax reported, and that there were no material differences  
9 noted, and no further investigation was warranted. Now, why  
10 is that important? If the auditor had not inserted the times  
11 two, the tax accrued for June of 2011, compared to the tax  
12 paid, would have shown an overpayment of approximately  
13 \$600,000.

14 At that time, had that overpayment of \$600,000 been  
15 brought to our client's attention, it could have been acted  
16 upon in the audit. They could have obtained a claim for  
17 refund. They could have investigated to see if it was, in  
18 fact, an overpayment, and that the duplication of sales did  
19 occur.

20 They could have done all that, but, instead, the  
21 auditor puts "times two" to make it equal what was paid, and  
22 makes absolutely no comments. There's no comment anywhere in  
23 the record, anywhere in the workpaper, as to why that "times  
24 two" was in there, nothing to say that "Well, we discussed  
25 it. The overpayment wasn't an overpayment." It appears, you

1 know, that they essentially just wanted to hide that fact, so  
2 they misrepresented to our client that the accrual account  
3 reconciled.

4 Now, why is that important? If you move further --  
5 I'll get to that. I'll get to that. I'm going to talk about  
6 a couple more exhibits, here. I'm going to talk about  
7 Appellant's Exhibit C, which is the accrual account, and you  
8 can see in front of you here -- I apologize, Department, but  
9 we've highlighted in yellow the \$600,000 there, where you can  
10 see that that number is supposed to have been carried over,  
11 and if you look at other numbers that carry over, they're  
12 pretty much the same numbers.

13 There is some -- if you look in some of the cells,  
14 there's \$90 that might be adjusted or added, no explanation,  
15 but that could be common if there was a debit or something,  
16 debit memo or something that was addressed in a  
17 reconciliation. But, for the most part, that's the -- and  
18 that is the only period in the audit that has this  
19 multiplier. There's no other month in that audit.

20 Now, moving forward, you know, if they didn't have  
21 that multiplier, like I said, we would have known. Our  
22 client would have known that there was this potential  
23 overpayment, and could have acted upon it. Because it was  
24 concealed, and the audit was presented with "There was no  
25 difference between the tax accrued and tax paid," our client

1 had no need to go and examine that schedule, to even look to  
2 see if they could find something like this.

3           They were focusing on the other two areas of the  
4 audit at that time. I think there were fixed assets that  
5 were assessed, and, I think, some expenses, where there was  
6 tax assessed. So they had other issues where there was a  
7 liability, so there was no need -- if there's no exposure, no  
8 problem in an area, they're not going to go through and  
9 examine it. So the workpaper presented the way it was  
10 presented. It didn't have the "times two." You had to dig  
11 in to find that.

12           Where I was going earlier with the workpapers, if a  
13 taxpayer provides an auditor with workpapers, or any records  
14 to be incorporated into the workpapers, the Audit Manual  
15 Section 0303.15 says that:

16           "Such schedules should be identified as  
17 prepared by taxpayer, and such data should  
18 have proper headings and be inserted,  
19 indexed, cross-referenced, and filed with  
20 the regular working papers."

21           We don't see that here, so that's additional evidence  
22 that this workpaper was prepared by the auditor and should be  
23 owned by the auditor. So, again, our client acted upon the  
24 auditor's misrepresentation that there were no material  
25 differences in the sales tax accrued and the sales tax paid.

1 The reliance resulted in our client overpaying by  
2 approximately \$600,000. They would have acted differently,  
3 like I had mentioned.

4 Then fast-forwarding, you know, to the second audit  
5 period, our client exercised reasonable care to remedy the  
6 overpayment in a timely fashion using the self-help credits,  
7 but, by the time that the auditor discovered the self-help  
8 credits, the statute of limitations had expired. So they  
9 disallowed those self-help credits, and essentially put the  
10 state in the unjust enrichment of the \$600,000 over the two  
11 audit periods.

12 So these initial -- you know, the auditor's actions  
13 denied our client the ability to act on the overpayment  
14 during the audit of 2012 and 2013. This Panel should have  
15 the ability to correct this injustice. As my colleague  
16 mentioned, equitable tolling states that:

17 "The statute of limitations will not bar a  
18 claim if the plaintiff, despite reasonable  
19 care and diligent efforts, did not  
20 discover the injury until after the  
21 limitations had expired. Equitable  
22 tolling allows a plaintiff to file a claim  
23 beyond the limitation period if, due to  
24 some action or misrepresentation by the  
25 Department or defendant, he was unaware

1           that the cause of action existed.  
2           Similarly, equitable estoppel is available  
3           when a defendant misrepresents a material  
4           fact, reasonably believing that the  
5           plaintiff will rely on that information,  
6           and the plaintiff does so to his  
7           detriment."

8           That's what I contend here, is that we relied -- our  
9           client relied on the presentation of the workpapers, where  
10          there was no material difference in the accrual account, not  
11          disclosing that there was a potential overpayment that could  
12          have been properly investigated. Now, the remedy for that,  
13          the remedy for this Panel, is to find equitable estoppel,  
14          equitable tolling, and allow for that period where the  
15          overpayment existed to be looked at.

16           ALJ ANGEJA: Does that conclude your presentation?

17           MR. MATTHIES: Yes.

18           ALJ ANGEJA: Questions from my panel?

19           ALJ KWEE: So, just to clarify the timeline, I  
20          understand, when your client took the self-help deductions on  
21          those two returns at the end of '12 and beginning of '13,  
22          that was still within the period within which they could have  
23          timely failed a claim for refund. Was that correct? Is  
24          that --

25           MR. MATTHIES: That's correct, yes.

1           ALJ KWEE: But they did not -- so when did they  
2 discover this overpayment? It was after the time of the  
3 audit?

4           MR. MATTHIES: Yes. So they took the self-help  
5 credits, you know, approximately a year or so later, over the  
6 course of, I think, three quarterly periods, and the second  
7 audit, the follow-up audit, with these self-help credits,  
8 that audit period, there was delays in getting that audit  
9 started. So the auditor didn't start that second audit, if  
10 you will, until sometime after the 2011 would have expired.

11           MR. KUHL: The second audit, the audit in question,  
12 the auditor had contacted the taxpayer in around April of  
13 2012. There was some correspondence, and then commenced  
14 fieldwork in July of 2012, and that filing period, the second  
15 quarter of 2012, is when the credits started to be taken.

16           ALJ KWEE: And I think there was some reference in  
17 your brief to there being a waiver of limitations for the  
18 second audit period?

19           MR. KUHL: There was, and the point behind that is  
20 that when an audit commences, a lot of times, audit staff, I  
21 believe, violate policy by soliciting a waiver right up  
22 front. In other words, an auditor should only solicit a  
23 waiver when there are delays requested by the taxpayer that  
24 are excessive, or if the Department has findings that are  
25 preliminary, and wants to give the taxpayer an opportunity to

1 give them additional time to provide records to support their  
2 (indiscernible).

3 ALJ KWEE: Okay.

4 MR. KUHL: So, basically, the auditor requested a  
5 waiver right up front, and that kept the period, the second  
6 quarter of 2012, open, which is when the credit occurred.

7 ALJ KWEE: I guess I was wondering if there was  
8 anything in the second audit which would have constituted  
9 written notice of a claim for refund before the waiver of  
10 limitations expires, because doesn't the waiver of  
11 limitations extend the period to file a claim for refund?

12 MR. MATTHIES: But it didn't extend the period where  
13 the overpayment was made.

14 ALJ KWEE: Okay.

15 MR. MATTHIES: That's why it ended with the audit  
16 period. I think the last quarter there is 2013. So that, I  
17 think, went through March 31st of 2013, and the end of the  
18 audit where the overpayment was made.

19 ALJ KWEE: Okay.

20 MR. MATTHIES: There was already in motion the second  
21 audit. The Department had sent out a notification they were  
22 going to do it, and I think that's when, for whatever  
23 reason -- and that was after the self-help credit, but it was  
24 the audit -- that second audit didn't get started -- had it  
25 got started right away, then both of them would have been

1 within statute. They wouldn't have expired at that point.

2 MR. KUHL: So, to be clear, the first audit period is  
3 April 1st, 2009, through March 31st, 2012, and the second  
4 audit period is April 1st, 2012, through March 31st, 2015.

5 ALJ KWEE: Okay. So there's no --

6 MR. MATTHIES: It's in the spring of 2012 when the  
7 second audit commenced.

8 MR. KUHL: That was bad timing.

9 ALJ KWEE: Okay. There was no overlap. I get it  
10 now. Thank you.

11 ALJ ANGEJA: Any questions?

12 ALJ KWEE: I'll turn it over to you.

13 ALJ ANGEJA: Not at this time. I try to save mine  
14 until the end.

15 So, CDTFA, we'll turn it over to you.

16 MS. HE: Thank you. Good morning. The sole issue  
17 before OTA in this appeal is whether an adjustment is  
18 warranted to Appellant's audited taxable measure for the  
19 three-year audit period of April 1st, 2012, to March 31st,  
20 2013, recalled in the current audit.

21 As evidenced by the report of field audit, and audit  
22 Schedule 12 from the current audit, Appellant underreported  
23 its taxable measure by over 8.4 million dollars. The audited  
24 measure was based on three conceded audit items and one  
25 disputed item of underreported taxable sales due to

1 Appellant's improper noting of these taxable sales by over  
2 \$7,000,000 to claim a time-barred alleged overpayment from  
3 the prior audit period.

4           The audit work papers described this disputed audit  
5 item as "disallowed self-help credits." Before I move on,  
6 however, I note that "self-help credits" is not a term that's  
7 recognized by California sales and use tax law other than  
8 where it had been explicitly disallowed, but, purely for  
9 descriptive purposes and ease of discussion, I'll continue to  
10 refer to the disputed underpayment as "disallowed self-help  
11 credits."

12           With that in mind, now, going back to the current  
13 audit findings, Appellant has never disputed the Department's  
14 audit methodology or the audited taxable measure for the  
15 current audit period at issue, nor does Appellant dispute  
16 that self-help credits are not legally acceptable, since it's  
17 accepted law, as the California Court of Appeal held in  
18 Philips and Ober Electric Company v. State Board of  
19 Accreditation, that a taxpayer that failed to file for a  
20 timely refund could not deduct the alleged overpayment on a  
21 current tax return, which is exactly what the taxpayer did  
22 here.

23           Appellant nonetheless offers several, often  
24 contradictory, justification for its underpayment, primarily  
25 on equitable grounds. These arguments have no merit either

1 factually or legally. Therefore, the Department's  
2 determination should be sustained and this appeal be denied.

3           Although Appellant would have you believe otherwise,  
4 this case is actually very simple, and it can be essentially  
5 described in three basic facts. Fact number one: Appellant  
6 itself allegedly discovered an overpayment due to double tax  
7 accrual for June 2011, and it began taking self-help  
8 deductions on its own before the prior audit even started,  
9 and the Appellant had taken essentially all of the self-help  
10 credits before the prior audit staff initiated any discussion  
11 regarding Appellant's tax accrual differences.

12           Fact number two: There is no evidence whatsoever  
13 that the prior auditor discovered the alleged June 2011  
14 overpayment, much less that she somehow calculated away or  
15 sanctioned Appellant's use of self-help credits. To the  
16 contrary, the audit workpapers from the prior audit found a  
17 tax deficiency of \$109,000, with no credits or overpayments.  
18 It also specifically notes immaterial differences between  
19 reported and recorded accrual, warranting no further  
20 investigation.

21           Fact number three: Appellant never apprised the  
22 Department of the alleged overpayment or its use of the  
23 self-help credits, much less filed a petition for  
24 redetermination of the prior audit findings or filing a  
25 timely refund claim. It was not until 2015, while in the

1 current audit, that the Department discovered for the very  
2 first time that Appellant took self-help credits for some  
3 alleged overpayment for June 2011.

4 I will now go into more details on those basic facts.

5 ALJ ANGEJA: Before you go there, can I interrupt  
6 real quick? I didn't get all the second argument. I'm  
7 sorry.

8 MS. HE: Sorry.

9 ALJ ANGEJA: Or the second fact.

10 MS. HE: Fact number two: There is no evidence  
11 whatsoever that the prior auditor discovered the alleged June  
12 2011 overpayment, much less that she somehow calculated away  
13 and sanctioned Appellant's use of self-help credits. Yes.  
14 To the contrary, the audit workpapers for the prior audit  
15 found a tax deficiency of \$109,000, with no credits or  
16 overpayments, and it also specifically notes immaterial  
17 differences between reported and recorded accrual, warranting  
18 no further investigation.

19 We're done with fact number three, right? So I'll  
20 jump back into the details on this --

21 ALJ ANGEJA: All right. Sorry for the interruption.  
22 Go ahead.

23 MS. HE: Thank you. Sometime in early 2012, around  
24 the same time Appellant discovered the alleged overpayment on  
25 its second quarter '11 sales and use tax return that was

1 filed on June 19th, 2011, Appellant received a notice from  
2 the Department that it had been selected for audit for the  
3 period of April 1st, 2010, through March 31st, 2012, the  
4 prior audit.

5           Instead of waiting for the prior audit to start, and  
6 to verify and to resolve the alleged overpayment Appellant  
7 itself had discovered, starting on April 30th, 2012,  
8 Appellant made a module (sic) entrance in its books for the  
9 current audit period, which, of course, is outside the prior  
10 audit's review, for credits for overpayment in June 2011, and  
11 on July 18th, 2012, Appellant underreported its tax by  
12 \$340,000 on its second quarter 2012 return. That's the first  
13 return for the current audit period, so it was outside the  
14 prior audit period.

15           Five days after Appellant filed that second quarter  
16 2012 return, the prior auditor began her fieldwork and  
17 requested books and records from Appellant. Appellant  
18 continued to record the self-help credits in the current  
19 audit period, and it continued to underreport tax on its  
20 returns in the current audit period.

21           By the time the auditor spoke to Appellant regarding  
22 the differences in tax accrual, on April 8th, 2013, Appellant  
23 had taken essentially all of the self-help credits that  
24 created the liability at issue in the current audit, all but  
25 \$17.

1           In total, Appellant created 188 journal entries for  
2 credits for June 2011, totaling over \$595,000 in tax, spread  
3 systematically in varying amounts in elaborate decimal  
4 fractions, over a period of five tax returns in 13 months,  
5 all outside the prior audit's review. There is no evidence  
6 that Appellant ever brought to the prior auditor's attention  
7 the alleged overpayment or its use of self-help credits.

8           Appellant also did not explicitly take a credit or  
9 deduction on its returns that contained the self-help.  
10 Rather, it simply reduced its taxable sales for those five  
11 periods. So the sales and use tax returns, on its face, as  
12 shown in the Department's Exhibit F, gave no indication that  
13 the credits were taken at all.

14           The prior auditor spent 16 hours in tax accrual  
15 reconciliation, discussed the differences on tax accrual with  
16 taxpayer on April 8th, 2013, and also tested the sales for  
17 one week in April 2011. There is no evidence regarding the  
18 details of the April 8th, 2013, conversation, what accrual  
19 discrepancies the prior auditors questioned Appellant about,  
20 or what information Appellant provided in response.

21           Similarly, the multiplier of two apparently was used  
22 to calculate the tax accrued on Schedule D for June 2011, but  
23 there is no evidence as to how the multiplier came to be  
24 used. The auditor noted in the prior audit verification  
25 comments that:

1           "Accrued sales and used tax was examined  
2           on an actual basis. Taxpayer provided a  
3           monthly general ledger for California  
4           sales and use taxes. Tax accrued was  
5           compared to the tax reported on the 414(m)  
6           on Schedule D. A review of the  
7           documentation revealed immaterial errors.  
8           No further investigation warranted."

9           Those are direct quotes from the Department's  
10          exhibits, and you can find them in Exhibits O and R, and, by  
11          the way, any reference to the exhibit will be the  
12          Department's exhibits unless I specifically note it  
13          otherwise.

14          The audit working papers for the prior audit said no  
15          credit involved, and the resulting (sic) in 109,000  
16          deficiency with no credits or overpayments. There is no  
17          evidence in the prior audit working papers that Appellant  
18          raised the issue of the alleged June 2011 overpayment.  
19          Rather, in August 2013, Appellant explicitly agreed to the  
20          auditor report, and paid off the deficiency determination,  
21          including an interest assessment of about \$20,000. You can  
22          find all those in Exhibits K, R, S, and T.

23          Appellant did not file a petition for redetermination  
24          or claim for refund. The prior auditor did not provide  
25          Appellant a refund claim form, as she saw no grounds for

1 refund, and, further, she did not interpret any particular  
2 document from Appellant as a claim for refund, as there was  
3 no writing stating any specific grounds for refund. Those  
4 were from Exhibit B.

5           In March 2015, the current audit was assigned. In  
6 the course of the current audit, the Department discovered  
7 for the first time that Appellant took self-help credits for  
8 an alleged tax overpayment outside of the current audit  
9 period. Despite these facts, Appellant now alleges that the  
10 Department found an overpayment in the prior audit, helped it  
11 go away, and advised Appellant that a self-help credit was a  
12 problem instead of refund (sic), or, alternatively, Appellant  
13 argues that the prior auditor should have caught the  
14 overpayment, and then provided the Appellant proper advice on  
15 claiming the overpayment.

16           So I guess, at this point, we're not exactly sure  
17 what they're arguing about what happened. Of course, those  
18 two arguments cannot be reconciled with each other. I  
19 noticed the Appellant, in its opening statement, did not  
20 mention anything about a 6596, but, since it was brought up  
21 in one of the briefs, I will cover that, anyway.

22           So Appellant argues that it's entitled to Section  
23 6596 relief from the deficiency measure on the disallowed  
24 self-help credits. This, of course, contradicts the facts I  
25 just summarized, and also falls outside the scope of Section

1 6596 relief.

2 Under Section 6596, a person may be relieved of  
3 taxes, and any penalty or interest added thereto, if the  
4 person's failure to make a timely return or payment is due to  
5 the person's reasonable reliance on written advice it had  
6 requested from the Department regarding the taxability of a  
7 particular activity or transaction.

8 Under Regulation 1705, presentation of the taxpayer's  
9 books and records is deemed to be a written request for the  
10 audit report, which includes the audit comments, schedules,  
11 and other writing prepared by the Department.

12 Here, as I previously described, the audit report  
13 specifically, and the audit working papers generally, contain  
14 no evidence that an overpayment was discovered by the  
15 Department, actualized (sic) that erroneous advice was  
16 provided in writing in the audit report, or advising  
17 Appellant how to deal with such an overpayment.

18 In addition, Appellant does not allege that its  
19 underpayment on particular transactions in the current audit  
20 was due to reliance on any written advice that any particular  
21 transaction or activity was not subject to tax. Instead, the  
22 alleged erroneous advice is on how to handle an alleged  
23 overpayment, which is not covered by Section 6596.

24 Also, Appellant took essentially all of its self-help  
25 credits before the Department provided the audit report to

1 Appellant, so Appellant's action could not have been in  
2 reliance on the audit advice that came afterwards. The  
3 timeline I just discussed also makes it illogical and  
4 unreasonable for Appellant to now argue that, had the auditor  
5 not hid the overpayment (indiscernible) use of the multiplier  
6 two, Appellant would have discovered it and then filed a  
7 refund claim, but, as stated in fact number one, Appellant  
8 itself had discovered the overpayment, had already used the  
9 self-help credits, before the prior audit even started.

10 Appellant's alternative argument that the prior  
11 auditor failed to perform essential required elements  
12 described in the audit, even if true, does not provide a  
13 basis for Section 6596 relief, because the law only  
14 authorizes relief from tax based on the prior audit report  
15 when the taxpayer establishes that the audit report contains  
16 written evidence demonstrating that the issue in question was  
17 actually examined. As OTA held in its Abdul Salam and Zahida  
18 Perveen precedential opinion -- it's 2019-OTA-041P:

19 "No relief is available based on audit  
20 report that should have caught an error  
21 but did not."

22 For all of these reasons, Section 6596 relief is not  
23 applicable here.

24 Appellant also presented arguments essentially  
25 disputing the prior audit determination or seeking a refund

1 of the alleged overpayment during the prior audit.  
2 Initially, the Department notes that a prior audit  
3 determination issued on October 1st, 2013, for deficiency of  
4 over 1.2 million dollars, became final on October 31st, 2013,  
5 because Appellant did not file a petition for  
6 redetermination.

7           Similarly, in order to obtain a refund for the  
8 alleged second quarter '11 overpayments, Appellant was  
9 required under Section 6902 and 6905 -- that's Revenue and  
10 Taxation Code sections -- to file a timely claim for refund  
11 in writing, stating the specific grounds on which the claim  
12 is founded, no later than three years from the last day of  
13 the month following the quarter at issue, which is second  
14 quarter '11. That will make the deadline July 21st, 2014.

15           Section 6902 mandates that:

16           "No refund shall be approved unless a  
17 claim for refund is filed within the  
18 statutorily prescribed time period."

19           Section 6905 provides that:

20           "Appellant's failure to file a timely  
21 refund claim constitutes a waiver of any  
22 demand to the state on account of such  
23 overpayment."

24           Here, however, no claim for refund was filed on or  
25 before July 31st, 2014, the statutory deadline. In fact, no

1 refund claim has ever been filed with regard to the alleged  
2 overpayment. Nonetheless, Appellant argues that it filed a  
3 timely informal refund claim, in accordance with federal law,  
4 by presenting its journals and other sales and use tax  
5 records for the Department's review in the prior audit, and  
6 also by corresponding with the Department on the prior audit.

7           However, there is no provision in the California  
8 sales and use tax law that would allow for an informal refund  
9 claim. Instead, Section 6904 sets out the requirement that  
10 the refund claim be in writing, stating the specific grounds  
11 for the claim.

12           In addition, as Appellant itself pointed out, the  
13 critical component of an informal refund claim is that it  
14 adequately puts the other party on notice of the amount of  
15 the overpayment and the reasons supporting the claim for  
16 refund. Here, however, as Exhibits K through Q indicate, the  
17 prior auditor noted no overpayment or credit, a finding to  
18 which Appellant explicitly agreed.

19           There is no evidence that the prior auditor knew,  
20 and, in fact, she confirmed she did not know of the alleged  
21 overpayment for second quarter 2011, as documented in Exhibit  
22 B. That's on page three of the e-mails. So there could be  
23 no informal refund claim, even if there is such a thing at  
24 all, which there isn't under California sales and use tax  
25 law.

1           Without a petition for redetermination or refund  
2 claim, timely or otherwise, OTA cannot consider any arguments  
3 related to the prior audit. Nonetheless, we will address  
4 Appellant's remaining arguments that the refund is allowable  
5 based on equitable tolling, equitable estoppel, or equitable  
6 recoupment. First, the Department notes that, in The Appeal  
7 of Estate of Gillespie, precedent decision -- that's  
8 2018-OTA-052P -- OTA held that:

9           "Even when a tax is proved to be  
10           inaccurate, there is no recourse to refund  
11           the taxes paid when the refund is  
12           untimely, because, without a timely refund  
13           claim, respondent does not have the  
14           statutory authorization to refund amounts  
15           paid, and OTA does not have statutory  
16           authorization to require respondents to do  
17           so."

18           That's in that precedential opinion, page 10. OTA  
19 appeals recognize, and we concur that, as the administrative  
20 agency created by statute, OTA could only act when  
21 statutorily authorized to do so, and lacks equitable power.  
22 Moreover, specifically regarding Appellant's argument based  
23 on equitable tolling -- so, as the Supreme Court held in the  
24 Bull Cam (phonetic) case, whether a time bar may be equitably  
25 tolled turned on the language of the statute of limitations

1 in question.

2 Here Section 6902's mandate of a timely refund claim,  
3 without any exception, indicates a legislative intent to  
4 preclude equitable tolling, and, as I just mentioned, OTA  
5 recognized in the precedent opinion, Gillespie, it does not  
6 have statutory authorization to toll the statute on an  
7 equitable basis to grant any untimely refund claim.

8 Regardless, equitable tolling is applicable only when  
9 the purpose of the claim for the refund, which is to put the  
10 tax agency on notice of the plaintiff's claim, has been  
11 satisfied, but that is not the case here because, as I  
12 discussed, the Department was not apprised of Appellant's  
13 alleged overpayment until 2015.

14 Next, regarding equitable estoppel, that doctrine is  
15 applied against the government only in rare and unusual  
16 circumstances, when its application is necessary to prevent a  
17 grave injustice. Taxpayers have the burden of proving all  
18 four elements of equitable estoppel.

19 Number one, the government agency must be apprised of  
20 the facts. Number two, the government agency must intend  
21 that the inaccurate representation shall be acted upon.  
22 Number three, the relying party must be ignorant of the  
23 facts, and, number four, the relying party must have  
24 detrimentally relied upon the representation of the  
25 government agency.

1           Here, based on the facts I discussed, the situation  
2 is almost the inverse of what equitable estoppel is  
3 applicable. Here Appellant itself had already discovered the  
4 alleged payment, and had claimed more than half of the  
5 alleged overpayment as self-help credits before the prior  
6 auditor even started her field audit, and then Appellant had  
7 taken essentially all of the self-help credits before the  
8 prior audit staff initiated any discussion regarding tax  
9 accrual differences, and the record before us gives no  
10 indication that the prior auditor knew of the alleged payment  
11 or credits, much less provided advice that was relied upon by  
12 Appellant. Therefore, none of the elements for equitable  
13 estoppel are satisfied.

14           Finally, the doctrine of equitable recoupment, which  
15 has its origin in federal tax matters, applies only when a  
16 single transaction, item, or taxable event has been subject  
17 to taxes twice based on inconsistent legal theories. The  
18 Department again notes that there's no specific authority  
19 indicating California would apply equitable recoupment, and  
20 OTA has stated in its precedent that it can only act with  
21 statutory authorization.

22           However, even assuming, as the California appellate  
23 court did in Independent Ironworks, Inc., that California  
24 will enforce such doctrine, the doctrine of equitable  
25 recoupment still is not applicable to the set of facts before

1 us. Clearly, Appellants alleged overpayment in the prior  
2 audit, and its underpayment in the current audit did not  
3 arise from the same transaction, item, or taxable event.

4           The alleged overpayment arises from transactions that  
5 occurred in June 2011, while the underpayments are of taxes  
6 owed on completely separate transactions that occurred during  
7 the current audit period of second quarter '12 through second  
8 quarter of 2013.

9           As the U.S. Supreme Court held in Rothensies v.  
10 Electric Storage Battery Co., equitable recoupment has never  
11 been thought to allow one transaction to be offset against  
12 another. As the Court went on to point out, to apply the  
13 equitable recoupment doctrine under these facts would be to  
14 render the statute of limitations meaningless because, if the  
15 doctrine applied such a set of facts, the taxpayer would  
16 resurrect old overpayment claims whenever the government  
17 attempted enforcement of any tax.

18           In its presentation, Appellant argues that the double  
19 accrual in its June 2011 account with the same transactions  
20 in June 2011 have been taxed twice, thereby meeting the  
21 requirements for equitable recoupment, but that misses the  
22 whole point or the whole basis for equitable recoupment. The  
23 crucial requirement for equitable recoupment is that the  
24 overpayment must have been made with respect to the same  
25 transaction or taxable event upon which the later deficiency

1 assessment is based, and then based on inconsistent legal  
2 theories.

3           If we look at the U.S. Supreme Court decisions, the  
4 single transaction, taxable event here, element was  
5 interpreted literally. In Bull, the single transaction or  
6 taxable event was the single receipt by the estate of  
7 post-death partnership profits, these profits being first  
8 treated as a part of the descendants' gross estate for estate  
9 tax purposes, and then later being treated as estate income  
10 for income tax purposes, and when we look at the stone (sic),  
11 there the single transaction was a receipt of income by the  
12 trust, so whether it should be taxed to the trust itself or  
13 the sole beneficiary.

14           So, when we look at these cases, which I can tell the  
15 doctrine only applies, basically, in two situations, number  
16 one, when you have an item of transaction that can  
17 potentially be subject to two taxes, one or two taxes, but it  
18 can never be subject to twice, to both taxes, and in the  
19 other situation, we look at the case. That's  
20 (indiscernible). The two taxes are so intertwined that a  
21 deficiency in one automatically means there's an overpayment  
22 of the other.

23           So, in those situations, the reason that the courts  
24 apply equitable recoupment is because, in those situations,  
25 because of the automatic effect of one tax giving rise to the

1 deficiency of the other, there's really nothing left to be  
2 determined with respect to the barred claim, which clearly is  
3 not the case here, because we don't know if it was an actual  
4 overpayment.

5           The tax Appellant's underreporting of \$7,000,000 of  
6 taxable sales recorded for the current audit period doesn't  
7 tell us anything about what they did or did not do in the  
8 prior audit period. So the double taxation of the same  
9 transactions in June doesn't give us the same single  
10 transaction or taxable event, as called for by the equitable  
11 doctrine.

12           While it's not brought up in the oral argument,  
13 again, it was in the Appellant's submission to the  
14 Department. They brought up the board decision in Solvay.  
15 So the Department also wants to note that the board's  
16 decision in Solvay has no relevance here, as it's not a  
17 precedential opinion, and, further, there's no indication  
18 that the board's decision to grant appeal there was based on  
19 equitable recoupment at all, and further, even if any of the  
20 equitable doctrines would apply at all, the doctrine of  
21 laches and of unclean hands would preclude the application of  
22 any of them.

23           Lastly, Appellant would not be entitled to a refund  
24 claim unless it can establish that it, in fact, actually  
25 overpaid its taxes. Appellant has the burden of proving an

1 overpayment existed in second quarter 2011. The record  
2 before us, however, does not establish such an overpayment.  
3 Instead, the prior audit found no overpayments or credits,  
4 and Appellant itself contemporaneously agreed with those  
5 findings.

6 Therefore, Appellant has failed to meet its burden,  
7 establishing that a refund is actually owing, regardless of  
8 whether there was a timely refund claim or whether any  
9 equitable doctrine can apply to allow an otherwise  
10 time-barred refund claim. For all of these reasons, this  
11 appeal should be denied.

12 ALJ ANGEJA: And that concludes your presentation?

13 MS. HE: Actually, just a couple of brief comments on  
14 some of the points that was brought up in the Appellant's  
15 presentation.

16 So, number one, about the waiver for the current  
17 audit, the Appellant was saying there was no basis, unless  
18 the taxpayer requested an unreasonable long delay, it should  
19 not be requested at all, but when we look at the audit  
20 working papers for the current audit, it was actually  
21 documented in one of the letters. That's in the Department's  
22 Exhibit C that's submitted with our electronic audit working  
23 papers under the correspondence subfolder and the letters.

24 The Department sent a letter on May the 8th, 2015, to  
25 the taxpayer. In the letter, it says -- I quote:

1           "The purpose of this letter is to confirm  
2           our agreement to delay the start of the  
3           audit. As I explained in our  
4           conversation, in consideration of this  
5           delay, please have available signed" --

6           So, number one, this document, there was an agreement  
7           by the taxpayer, and then, when you look at the 414(z), the  
8           auditor assignment history report, it shows the exact reason  
9           for the waiver is because the Department was also starting  
10          the audit on some related entities.

11           So there was a sufficient basis for the waiver,  
12          because of the related entity examinations going on at the  
13          same time, and, of course, because, as you can see, the prior  
14          audit did disclose a significant deficiency of over 1.2  
15          million dollars.

16           So there was a reason to suspect there could be a  
17          deficiency again, and then there was reason to allow more  
18          time so the Department could audit other related entities at  
19          the same time. So, contrary to Appellant's argument, there  
20          is a sufficient basis for that waiver.

21           ALJ ANGEJA: Which exhibit were you referring to,  
22          that letter?

23           MS. HE: The letter, it's under the Department's  
24          Exhibit C, but, of course, Exhibit C, it's a huge electronic  
25          file, but it's under the correspondence subfolder and the

1 letters. I believe there's only one letter there. That's  
2 the only letter, May 8th, 2015. So it's agreed, because of  
3 the related audit going on at the same time.

4 Then, as to the focus on the multiplier two, as I  
5 mentioned in the presentation, there's no -- I guess,  
6 unfortunately, there's nothing before us that shows the  
7 reason for the multiplier two, but, if I may, it's very  
8 common for auditors to make various adjustments when  
9 reconciling the tax accrual accounts or any taxable records,  
10 and the multiplier two is not the only adjustment on Schedule  
11 D. If you march over (sic) to all the other quarters, it  
12 will show formulas, too.

13 Appellant is right that June 2011 is the only one  
14 with the multiplier two, but all the other months, they have  
15 formulas of subtractions, additions for thousands of dollars,  
16 sometimes hundreds of thousands of dollars.

17 So, clearly, because of the documented inquiry in the  
18 414(z) by the auditor to the taxpayer, which the taxpayer  
19 then responded by saying it would provide information, so the  
20 multiplier two, and all the formulas of the subtraction or  
21 additions to the formula, would be based on whatever  
22 documentation the taxpayer had provided the auditor, and at  
23 the end of the day, Appellant knew there was an overpayment,  
24 which the auditor obviously did not know, at least at that  
25 time, and then, even though the auditor said there was no

1 overpayment, Appellant still agreed to that, paid off the  
2 deficiency. So there was no overpayment.

3 There's no intentional concealment or anything by the  
4 auditor. There's no reason for the auditor to do that, and,  
5 of course, the timeline doesn't support the whole argument  
6 about a concealment. How can you conceal something when the  
7 other party was already very widely aware of that, and had  
8 already been taking multiple actions to get the overpayment  
9 back?

10 Yes. I think that will conclude my presentation for  
11 now.

12 ALJ ANGEJA: All right. Do you want to have rebuttal  
13 before questions, or you have questions? Go ahead.

14 ALJ KWEE: Just a quick follow-up with CDTFA, because  
15 I understand the taxpayer's position on that multiplier two  
16 was that it was evidence that the auditor had concealed or  
17 hid the amount of the overpayment owed to the taxpayer, and  
18 if I'm understanding CDTFA's position, you're saying that the  
19 multiplier two could have reasonably been based on  
20 documentation that was provided by the taxpayer to the  
21 auditor? Was that what you were explaining?

22 MS. HE: That is correct, because the records did not  
23 contain any mention of an overpayment, which is close to  
24 \$600,000 in tax and over \$7,000,000 in measure. So this  
25 amount is significant. The number, on itself, is

1 significant. If that had been brought to the attention of  
2 the prior auditor, there is no reason at all the auditor  
3 would not have noted that.

4           So the only reason, I guess -- I don't want to go  
5 into speculation, but all I can tell, based on the trail of  
6 the record file, is the auditor questioned it, the taxpayer  
7 then provided the information, and then the auditor, after  
8 looking at all the information, said, "Everything looks  
9 good." There was only a difference of two dollars after  
10 reconciliation.

11           So that's the -- I think that's a very reasonable  
12 conclusion to draw from that, from the fact that she was able  
13 to reconcile, concluding only two dollars difference, which,  
14 by the way, the Appellant readily agreed to and then paid.  
15 You know, that signifies it must be something the taxpayer  
16 provided that prompted the multiplier two, but in no way  
17 would have evidenced overpayment, because we don't know what  
18 the other side of the records would look like.

19           ALJ KWEE: So I guess, for the other quarters --  
20 because you mentioned that, for other quarters, there were  
21 adjustments, also, and I'm just curious. Was the multiplier  
22 two -- was that an outlier compared to how the other quarters  
23 were adjusted?

24           MS. HE: That is correct. The multiplier two is --  
25 that's the -- June 2011 is the only month with the multiplier

1 two, but the subtractions and additions for the other months  
2 are significant as well. I don't have the exact number here.  
3 I think there are eight or nine different entries that either  
4 added thousands or hundreds of thousands of dollars to the  
5 raw number from the source document, or maybe subtractions.

6 There's no argument by the Appellant that there was  
7 any overpayment or underpayment based on those formulas, so I  
8 don't see how they can argue this multiplier two is proof of  
9 an overpayment, when there's no corresponding argument saying  
10 the other ones evidence underpayment.

11 ALJ KWEE: Okay. Thank you.

12 MS. HE: The whole point of reconciliation is to look  
13 at all of the numbers and see, you know, what's missing after  
14 you compare the raw documents to whatever other documentation  
15 the taxpayer may have provided.

16 ALJ KWEE: Thank you for the clarification.

17 ALJ ANGEJA: Any other questions?

18 ALJ STANLEY: I have one. I have a question, and I  
19 don't think this microphone is working.

20 I was just wondering if it's the Department's  
21 position that the Office of Tax Appeals has the authority,  
22 under certain circumstances not present in this case, per  
23 your opinion, to apply equitable remedies at all.

24 MS. HE: I think, as I mentioned in my argument,  
25 really, that's not an issue that needed to be decided here

1 because, at the end of the day, the facts do not establish  
2 any equitable doctrine, and we do have, as I cited, the  
3 Appeal of Gillespie case, but OTA itself -- I mean, sorry,  
4 OTA itself -- had stated that OTA, as an administrative  
5 agency created by statute, can only act when statutorily  
6 impelled to do so.

7 Of course, the statute for the refund claim is, if  
8 you don't file the refund claim by the statutorily prescribed  
9 time limitation, no refund shall be granted, and then the  
10 failure to file the refund claim shall constitute --  
11 basically, you forfeit your right to demand the state to  
12 forward the money back. That's 6902, 6904, and 6905.

13 ALJ STANLEY: Thank you.

14 ALJ KWEE: Just to clarify, the Gillespie case was a  
15 federal income tax case, not a sales and use tax case,  
16 correct?

17 MS. HE: That's OTA's own precedential opinion in the  
18 state income tax setting involving FTB.

19 ALJ KWEE: Okay.

20 MS. HE: Yes. FTB, income tax demand, and the  
21 taxpayer was trying to argue for want of the refund claim,  
22 untimely refund claim based on equitable grounds, and OTA  
23 said in response, "We can only act when statutorily impelled  
24 to do so," and FTB does not have power to do that. So OTA  
25 cannot order FTB to grant the refund.

1           It also cites to the U.S. v. Bull Cam case, which  
2 basically said not all subjects are subject to equitable  
3 tolling. So, even though, in the court of general  
4 jurisdiction, there may be situations where a statute of  
5 limitations can be subject to equitable tolling, that's in  
6 the court of general jurisdiction, but, even then, not all  
7 statutes are subject to equitable tolling. It really depends  
8 on the language and the mandate of the statute.

9           In that Supreme Court case, the Court looked at the  
10 statute of limitations section there, and said the language  
11 was so clear, the mandate said, "Shall" -- actually, when I  
12 compared the statute, it's very similar to the California  
13 sales and use tax refund claim statute.

14           It said, basically, no refund shall be granted, and  
15 then, of course, if you don't file by the prescribed period,  
16 there's a forfeiture of overpayment, even if for justly (sic)  
17 owed. Of course, there's no case -- there's no factual proof  
18 here of overpayment, on top of all the other issues. So,  
19 yes.

20           It's clear, even leave (sic), there is equitable  
21 power at all. The statute, the specificity of statute, makes  
22 it clear that the refund claim statute is not subject to  
23 equitable tolling. So that's our position. Thank you.

24           ALJ ANGEJA: We'll turn it over to Appellants for  
25 rebuttal.

1           MR. KUHL: Thank you, your Honor. I'm sure both of  
2 us will want to weigh in, here, but I did want to address --  
3 and first thank the Department for their spirited  
4 presentation, but I do want to take exception to at least one  
5 issue and one characterization by the staff, and that is, we  
6 keep referring to this payment as an "alleged overpayment."

7           I think the Appellant has provided a very plausible,  
8 reasonable, and rational explanation as to the exact cause of  
9 this overpayment. It was a duplication of the transactions  
10 in one specific month that resulted in an overpayment of tax,  
11 and if you look to the accrual account, the auditor's actions  
12 support that, by adding that multiplier times two.

13           So to say that there's an alleged overpayment, I  
14 think, if you just look at that accrual account, on the  
15 surface, in defense of the Department and the auditors,  
16 especially those in New York, quite frankly, they're better  
17 than that. Just look at those numbers, and if you look at  
18 the two months preceding and the two months after, that  
19 1.2-million-dollar accrual in June, you see amounts from 418  
20 to \$499,000. The amount in June of 2011 is almost triple of  
21 any of those months.

22           So, on its surface, that should be a big red flag to  
23 any auditor, to say, "Hey. That number stands out. Never in  
24 history has there been that much California sales tax  
25 accrued," and it deserves scrutiny, which the auditor has

1 clearly given it, if you look to the Appellant's Exhibit E,  
2 the second page, the 414(z), the comment by the auditor, and  
3 she says:

4 "The auditor spoke with the taxpayer  
5 regarding differences on tax accrual. He  
6 is working on getting support for these  
7 differences."

8 So, clearly, this was analyzed, and, clearly, there  
9 was, in fact, an overpayment of tax. I just don't know how  
10 much more I can emphasize the fact that each individual  
11 transaction was erroneously duplicated in May, and we've  
12 owned that error that was made by the taxpayer, and, again,  
13 it explains exactly what has transpired.

14 So, with regards to the Department's characterization  
15 that they checked with the auditor and she wasn't aware of an  
16 overpayment, if you look at the e-mails the Department is  
17 referencing, I object to that characterization, because what  
18 it is, it's an e-mail from a hearing officer to a supervisor  
19 in the current auditor to say, "Hey. Can you please check  
20 with the prior auditor," five years after the audit was  
21 complete, "and let us know if she thinks there was any sales  
22 tax over-accrual in the prior audit."

23 I mean, again, first of all, it's not the auditor's  
24 own words and own representation. It's someone else saying  
25 that they talked to this auditor about an audit from five

1 years ago to represent whether or not there was, in fact, an  
2 overpayment of tax.

3 MR. MATTHIES: Okay. I have three points, if you  
4 have a couple minutes. With regard to the comment that the  
5 Department made about unclean hands, unclean hands, the way I  
6 understand it, would be if our party -- if our client acted  
7 unethically or did something in bad faith, and in this case,  
8 they did not do that. They made an overpayment. They  
9 attempted, in good faith, to remedy it, albeit maybe wrong,  
10 with the self-help credits. So I don't believe that the  
11 unclean hands argument really prevails here.

12 The other adjustments that you'll see there, it is  
13 common. When you have an audit workpaper, there can be  
14 adjustments, but it's very common that you would have  
15 comments why you did certain things. There's nothing in this  
16 workpaper to disclose why they multiplied it times two. Had  
17 they not done that, this clearly would have shown that  
18 \$600,000 overpayment, and caused other actions, and our  
19 party, our client, to do something differently.

20 With regard to the equitable doctrines, I think  
21 equitable estoppel, the Department said, "In rare and  
22 unusual." I think this is a rare and unusual circumstance.  
23 You don't see an auditor multiplying tax accrued, \$600,000 by  
24 two, just so it will equal what is paid, and so there's no  
25 difference -- so there's no cause for the client to go in and

1 do that.

2 Now, I know I don't have much time, but there are  
3 four conditions for equitable estoppel, and I'm prepared to  
4 tell you why I think these four conditions have been met, if  
5 I have the time to do so.

6 ALJ ANGEJA: So, yes, I have a quick point of  
7 clarification. That argument was not in the briefs. We have  
8 the informal claim for refund. We have equitable tolling,  
9 equitable recoupment, and then the argument regarding the  
10 waiver. I didn't see anything regarding equitable estoppel.  
11 They raised --

12 MR. MATTHIES: I'm rebutting. They brought it up.

13 ALJ ANGEJA: They brought it up, so I'll let you  
14 address it.

15 MR. MATTHIES: So the four conditions that must be  
16 satisfied before the doctrine of equitable estoppel can be  
17 applicable -- and there's City of Long Beach v. Mansell and  
18 Strong v. County of Santa Clara. There are California  
19 Supreme Court cases, and there has been some -- my  
20 understanding, there was some BOE board hearings that also  
21 addressed equitable estoppel, maybe not successfully, but  
22 they address them.

23 But the four conditions: The party to be estopped  
24 must be apprised of the facts. Two, he must intend that his  
25 conduct shall be acted upon, or must so act that the party

1 asserting the estoppel has the right to believe it was so  
2 intended. The other party must be ignorant of the true state  
3 of the facts, and he must rely on the conduct to his injury.

4 With condition one, I mentioned Appellant's Exhibit  
5 D, the audit comments that the accrual account was examined  
6 on an actual basis. There were no material differences. We  
7 find the Appellant's Exhibit C the source of the -- and that  
8 was provided based on the Department's Exhibit B, e-mail. I  
9 think they had mentioned that the auditor -- in question  
10 number four -- that that was provided.

11 So that audit -- that's an audit workbook that was  
12 provided by the client, our client, and those numbers were  
13 then carried forward to the Department's audit workpapers.  
14 So that was provided. It shows 600,000. It doesn't show 1.2  
15 million dollars. Appellant's Exhibit B, which is Audit  
16 Schedule 12(d), shows the multiplier in that cell.

17 So all of this, in my opinion, supports that, and  
18 then Exhibit G, the audit workpaper, described, Appellant's  
19 Exhibit G, that workpapers are worksheets and other pertinent  
20 material compiled by the auditor. So these were documents --  
21 this "times two" was compiled by the auditor, with absolutely  
22 no comments as to why, and that would be normal procedure. I  
23 mean, if you're going to multiply \$600,000 times two to make  
24 it match, you would expect to see comments in there. You  
25 would expect to see why, and the understanding, and any

1 conversation that went on, to document that. You don't just  
2 do that.

3           So I contend, or we contend, that this evidence  
4 demonstrates that the auditor was aware that there was a  
5 potential overpayment in that period, and our client would  
6 have acted differently. So I believe that demonstrates  
7 condition number one.

8           Number two, he must intend that his conduct shall be  
9 acted upon, or must so act that the party asserting the  
10 estoppel has the right to believe it was so intended. We  
11 have Appellant's Exhibit A, "Relationship of the Taxpayer":

12           "The taxpayer should be assured that the  
13 tax auditor's function is to determine  
14 whether the amount of tax has been  
15 reported correctly. The tax auditor  
16 should aid the taxpayer in gaining a  
17 correct understanding of the law, and  
18 demonstrate that it is willing to  
19 recommend a refund of an overpayment, as  
20 we are to propose a deficiency. Care  
21 should be taken to inform taxpayers of  
22 their rights and privileges in connection  
23 with such determinations."

24           Our client acted upon the auditor's representation  
25 that there were no material differences, and that reliance of

1 that misinterpretation resulted in our client unknowingly  
2 agreeing to that audit, and paying on the other items in the  
3 audit, and not having cause to look at this potential  
4 overpayment, due to the fact of the misrepresentation and  
5 hiding of that by multiplying it times two.

6           The third condition: "The other party must be  
7 ignorant of the true state of the facts." Our client was  
8 unaware the auditor multiplied the sales tax accrued by two  
9 in order for sales tax accrued to agree with sales tax paid.  
10 Combined with the audit comments in Appellant's Exhibit D,  
11 our client had no reason to question the auditor's  
12 reconciliation, given our client believed it actually  
13 remitted sales tax collected.

14           Additionally, I mentioned there are two other areas  
15 of understatement that our client was drawn to in the audit  
16 workpapers. They're going to focus on what they may owe, not  
17 something where they don't owe anything.

18           The fourth condition, "Must rely upon the conduct to  
19 his injury." Because the auditor knew there was a potential  
20 overpayment, but failed to draw proper attention to the  
21 potential overpayment, our client relied on the auditor's  
22 representation, or misrepresentation, and was injured  
23 financially by an amount in excess of \$600,000."

24           So the very basis of equitable estoppel is to avoid  
25 injustice. The injustice here is that the auditor acted

1 against professional conduct, resulting in financial harm to  
2 our client and unjust enrichment to the state. The auditor  
3 acted in such a way as to amount to constructive fraud.

4           The auditor knew the sales tax accrual account didn't  
5 reconcile. The auditor knew a potential overpayment existed.  
6 The auditor knowingly and consciously multiplied the sales  
7 tax accrued by two. The auditor knew potential overpayment  
8 should be addressed, and that the taxpayer should have been  
9 informed.

10           In the interests of justice, we ask that this panel  
11 correct an injustice and take action to make it right, and  
12 toll the statute of limitations.

13           ALJ ANGEJA: Okay. Thank you. And I have one,  
14 hopefully, last question. I know we're running over on time.  
15 For the assertion that they were ignorant of the facts, how  
16 do you reconcile that statement with the concept that they  
17 had already engaged in the self-help credits prior to the  
18 auditor even setting foot on the premises, at least to the  
19 tune of half of it, if not all of it?

20           In other words, they must have known there was an  
21 overpayment, because they had already started helping  
22 themselves to a remedy before the auditor -- if I've got my  
23 notes right, that return for the period with the overpayment  
24 was filed July 18th, 2012. The auditor didn't start the  
25 audit until July 25th -- or 23rd, five days later.

1 MR. MATTHIES: I think you're talking about two  
2 different audits.

3 ALJ ANGEJA: Perhaps I am. That's why I'm asking the  
4 question.

5 MR. MATTHIES: Could you repeat your question?

6 ALJ ANGEJA: They had made the statement that more  
7 than half of the self-help credits had been claimed before  
8 the audit started.

9 MS. HE: Judge Angeja, if I may, with respect to the  
10 (indiscernible) I mentioned, if you look at Department's  
11 Exhibit G, and then referencing Department's Exhibit U, it's  
12 very clear that, July 18th, 2012, Appellant filed its first  
13 sales and use tax return for the audit period of second  
14 quarter 2012, which underreported its tax by over \$340,000,  
15 and then, when you look at Exhibit J, P, and R, there's a  
16 prior audit started July 23rd, 2012. So the timeline is  
17 exactly as you just discussed.

18 ALJ ANGEJA: I did misspeak. I said the  
19 "overpayment." The overpayment occurred in 2011, not 2012.  
20 The self-help started in 2012.

21 MS. HE: The overpayment. That's correct. Yes.

22 ALJ ANGEJA: Self-helps had started before the audit  
23 did. Am I incorrect?

24 MR. BROOKS: You're correct, your Honor.

25 MS. HE: You are correct.

1 MR. KUHL: Well, I'm not sure that I agree with that,  
2 and just to clarify that my dates are right, yes, the  
3 overpayment was made in June 2011, on what would be the  
4 second quarter of the 2011 return. In 2012, the taxpayer was  
5 contacted for audit in April. There had been an extension.  
6 The actual fieldwork started in July, and the second quarter  
7 of 2012 return was the first return were, in fact, there was  
8 a self-help credit claimed, and that return is due on July  
9 31st, 2012.

10 ALJ ANGEJA: That was filed before the audit started,  
11 before there would have been a multiplier of 2X or any advice  
12 given.

13 MR. MATTHIES: No, that's a totally different audit.  
14 The multiplier of 2X happened back in 2011. This is 2011.  
15 So you had the overpayment happen, and then, a year later,  
16 the self-help credits started, and sometime after that, the  
17 second audit started. So what they did is, they had this  
18 overpayment, and then they attempted to remedy that by taking  
19 the --

20 ALJ ANGEJA: Well, I understand that. You're saying  
21 that they missed it, and/or concealed it.

22 MR. MATTHIES: The first audit --

23 ALJ ANGEJA: When did that first audit start?

24 MR. MATTHIES: That first audit started -- gosh.

25 When did the first audit start?

1 MR. KUHL: The audit period was 2009 through -- April  
2 1st of 2009 through March 31st of 2012. It was completed in  
3 2013. So, if you start an audit for the second quarter of  
4 2009, presumably, it probably commenced around the second  
5 quarter of 2012, or three years later.

6 ALJ ANGEJA: Right.

7 MR. KUHL: So, right around that time --

8 MR. MATTHIES: Was your question when did the first  
9 audit start?

10 ALJ ANGEJA: It's in the exhibits. I'm not going to  
11 take our time to figure that out at this point.

12 MR. KUHL: If you have an audit period from April 1st  
13 of 2009 --

14 ALJ ANGEJA: Well, I understand that.

15 MR. KUHL: -- expires in July of 2012, presumably  
16 would have started in the spring of 2012.

17 ALJ ANGEJA: Right, and I'm looking at the timeline,  
18 and the argument is that the taxpayer did not know of the  
19 overpayment in June of 2011, and the auditor should have  
20 caught it, didn't, and concealed it, but that audit, that  
21 auditor's actions, did not start before July 23rd of '12, by  
22 which time the self-help deduction had already been claimed  
23 in second quarter 2012.

24 MR. KUHL: I believe in July of -- is it 2012?

25 MR. MATTHIES: No. I believe you're mistaken, your

1 Honor, that -- the audit in question, where the multiplier  
2 was, started in -- there is an exhibit here. I've got to  
3 find it. This is an assignment activity. Whose exhibit is  
4 this? This is Appellant's Exhibit --

5 MR. KUHL: Exhibit E.

6 MR. MATTHIES: Exhibit E, which is the Department's  
7 assignment activity history report. That audit was assigned  
8 to an auditor in March of 2012.

9 ALJ ANGEJA: Right. The reconciliation didn't happen  
10 in March of 2012.

11 MR. KUHL: It happened in July of 2012.

12 ALJ ANGEJA: Right. Thank you. Okay. I have no  
13 further questions. I presume my Panel does not. All right.

14 MS. HE: Judge Angeja, since there was a question  
15 that was brought up about how the argument of equitable  
16 estoppel came up, I just want to make a clarification. The  
17 Department did not bring up the equitable estoppel argument  
18 on its own, because I guess I (indiscernible) to that in my  
19 opening statement.

20 The Appellant's argument is kind of a moving target  
21 at different times. So, previously, it was informal refund  
22 claim, and then equitable recoupment, but, in its prehearing  
23 conference statement, when we look at the statement, they say  
24 the two things they're going to discuss are equitable  
25 estoppel and equitable recoupment, which is why we addressed

1 that as a response.

2 So they said they're going to bring up the equitable  
3 estoppel, and then we responded, saying, basically, number  
4 one, OTA does not have the equitable power, per its own  
5 precedential opinion.

6 Number two, equitable estoppel doesn't apply in this  
7 set of facts here, and we did not basically -- by discussing  
8 that, it doesn't mean the Department is giving any validity  
9 of that argument, or the applicability of that argument to  
10 this set of the case (sic) at all. It's just for the sake of  
11 completeness of the record. So we're addressing everything  
12 they brought up.

13 The same thing goes with the Section 6596 argument,  
14 and, as you can see right now, the argument is that the  
15 auditor concealed the overpayment, but, previously, they  
16 mentioned that the auditor -- they discussed the overpayment  
17 with the auditor, discussed the self-help credits with the  
18 auditor. The auditor said everything was good, "You can do  
19 self-help credits."

20 So it just keeps -- the argument, the factual  
21 scenario, keeps on shifting, so it's hard for us to narrow  
22 down and lock down exactly what they are focusing on, which  
23 is why we are basically hitting everything.

24 ALJ ANGEJA: Okay. All of which are legal arguments,  
25 which we now have thoroughly, on the record, been addressed

1 by both parties. So I don't feel the need for anything else  
2 for equitable estoppel, if you don't. All right.

3 If there's no more facts to be addressed, I think  
4 we're good. So we would conclude this hearing at this point,  
5 and -- hold on. Where is my note? I will close the record  
6 and conclude the hearing.

7 I'd like to thank each party for coming in today. My  
8 co-Panelists and I will meet and confer to discuss this case,  
9 and then issue a written opinion within 100 days.

10 Let's go off the record.

11 (Whereupon the proceedings were  
12 adjourned at 12:25 p.m.)

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