

BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF, )  
 )  
KHN, INC., ) OTA NO. 18042562  
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 )  
 ) APPELLANT.  
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TRANSCRIPT OF PROCEEDINGS

Cerritos, California

Tuesday, June 16, 2020

Reported by:  
ERNALYN M. ALONZO  
HEARING REPORTER

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Transcript of Proceedings, taken at  
12900 Park Plaza Dr., Suite 300, Cerritos,  
California, 90703, commencing at 9:05 a.m.  
and concluding at 9:53 a.m. on Tuesday,  
June 16, 2020, reported by Ernalyn M. Alonzo,  
Hearing Reporter, in and for the State of California.

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APPEARANCES:

Panel Lead: ALJ NGUYEN DANG

Panel Members: ALJ NATASHA RALSTON  
ALJ ANDREW WONG

For the Appellant: MARTIN SCHWARTZ,

For the Respondent: STATE OF CALIFORNIA  
Department OF TAX AND  
FEE ADMINISTRATION  
By: RANDY SUAZO,  
JASON PARKER,  
CHRISTOPHER BROOKS

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I N D E X

E X H I B I T S

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1 Cerritos, California; Tuesday, June 16, 2020

2 9:05 a.m.

3

4 JUDGE DANG: Good morning everyone. Welcome to  
5 the Office of Tax Appeals.

6 We are opening the record in the Appeal of  
7 KHN, Inc. The case number is 18042562. It is  
8 approximately 9:05 a.m. on June 16th, 2020. This hearing  
9 is being held in Cerritos via Webex video conferencing.

10 Today's case is being heard and decided equally  
11 by a panel of three judges. My name is Nguyen Dang, and  
12 I'm the lead judge for purposes of conducting this  
13 hearing. Also on the panel with me today are Judges  
14 Andrew Wong and Natasha Ralston. Just again, noting for  
15 the record, Judge Ralston is replacing Judge Joshua  
16 Aldrich. He wasn't able to attend today.

17 At this time I'd like to get the appearances of  
18 the parties just for the record. Will the parties please  
19 introduce themselves, beginning with Appellant.

20 MR. SCHWARTZ: Martin Schwartz.

21 JUDGE DANG: Thank you. And is your client also  
22 present, Mr. Schwartz?

23 MR. SCHWARTZ: No he's not present today.

24 JUDGE DANG: Okay. Thank you.

25 And, CDTFA, could you please state your name and

1 any title that you wish to have included with the record.

2 MR. SUAZO: Randy Suazo, Hearing Representative.

3 MR. PARKER: I'm Jason parker, Hearing  
4 Representative. And I believe that Christopher Brooks is  
5 having some audio issues. So I think he's going to call  
6 in to the hearing because he can't hear us talk to him  
7 right now.

8 JUDGE DANG: Okay. Thank you.

9 I just want to confirm that Mr. Brooks is still  
10 on the line before proceeding.

11 MR. PARKER: I believe he's there because I see  
12 his video feed, but he had -- I've been texting him and he  
13 doesn't have any audio. So he hasn't heard us.

14 JUDGE DANG: Okay. Let's give him a few minutes  
15 to get connected before proceeding.

16 MR. PARKER: Okay.

17 (There was a pause in the proceedings.)

18 JUDGE DANG: Let's go back on the record and  
19 continue with this hearing.

20 My understanding from the prehearing conference  
21 was that the issues in this appeal are whether additional  
22 adjustments are warranted to the measure for unreported  
23 taxable sales, as well as the negligence penalty, and  
24 whether Appellant was negligent.

25 Mr. Schwartz, is that correct?

1 MR. SCHWARTZ: That's correct, yes.

2 JUDGE DANG: Thank you.

3 And CDTFA, does that comport with your  
4 understanding as well?

5 MR. SUAZO: Yes. That's what I understand.

6 JUDGE DANG: Thank you.

7 Mr. Schwartz, I received your submission that you  
8 had submitted this past Saturday. It included the summary  
9 of the arguments that you intend to make today as well as  
10 a copy of CDTFA's audit schedule. I believe it's 12A R2.

11 MR. SCHWARTZ: That's correct, yes.

12 JUDGE DANG: Okay. Just to keep things simple  
13 I'm not going to admit these into evidence today because I  
14 believe CDTFA has already included a copy of their  
15 reaudit. So that should include the schedule you have  
16 attached to your submission. Do you have any objection to  
17 that?

18 MR. SCHWARTZ: No, I do not.

19 JUDGE DANG: Mr. Schwartz.

20 MR. SCHWARTZ: Hello. Hello. Can you hear me?

21 JUDGE DANG: Mr. Schwartz, are you still on the  
22 line?

23 MR. SCHWARTZ: Yeah. I'm here. You're breaking  
24 in and out.

25 JUDGE DANG: Is this -- is this any better?

1 MR. SCHWARTZ: Yeah. I can hear you now.

2 JUDGE DANG: Okay. I'm sorry. I apologize for  
3 that. I just needed to move a little closer to my  
4 microphone. This is Judge Dang speaking again. I was  
5 just commenting on the fact that we received your  
6 submission that you sent to us this past Saturday, which  
7 included a summary of the arguments that you intend to  
8 make today, as well as a copy of one of the Department's  
9 audit schedule. I believe the schedule was 12A R2.

10 MR. SCHWARTZ: Correct. Correct.

11 JUDGE DANG: And I'm suggesting that for  
12 simplicity's sake that I'm simply not going to admit these  
13 into evidence, and I'm going to -- and the reason for that  
14 is because CDTFA has already included that with their  
15 submission. So it will already be in the record. There's  
16 no need to have duplicate schedules.

17 Would that be okay with you?

18 MR. SCHWARTZ: Yes.

19 JUDGE DANG: Okay.

20 MR. SCHWARTZ: That would be okay.

21 JUDGE DANG: Okay. Thank you. And I noticed  
22 also, Mr. Schwartz, that you had indicated during our  
23 prehearing conference that you would be submitting various  
24 inventory-related documents. Did you still intend to  
25 submit those?



1           MR. SCHWARTZ: No. No. The document has already  
2 been entered prior. And when it's my turn, I'll just  
3 spend a couple of minutes on my thoughts about that.

4           JUDGE DANG: Okay. I'd just like to clarify  
5 something for you, Mr. Schwartz. If it has not been  
6 identified -- if these documents have not been identified  
7 by you at this hearing, they will not be entered into  
8 evidence. We will not consider them. I know you had --  
9 were these documents the documents you had attached to  
10 your opening briefs? Are these the ones you were  
11 referring to or were they previously submitted to CDTFA  
12 prior to your appeal here at OTA?

13           MR. SCHWARTZ: Correct. These are documents from  
14 CDTFA, and these were estimates by the vendors.

15           JUDGE DANG: Let me go ahead and ask CDTFA  
16 briefly. Did you have an idea of what the taxpayer is  
17 referring to with these documents? And are they included  
18 in the, I guess, in CDTFA's submission?

19           MR. SUAZO: This is Randy Suazo. Basically, on  
20 the -- there was a few vendors that he had given in one of  
21 the appeals hearings: Southern Wines, Young's Market, and  
22 I believe somebody else. It was submitted. The problem  
23 was there was no way to verify it because it was just a  
24 dollar amount only on there.

25           And I believe on the inventory -- I believe

1 something was given during the appeals hearing, but  
2 whether or not it was for that particular audit period  
3 because the audit period happens at midyear, that's where  
4 the contention lays.

5 JUDGE DANG: This is Judge Dang speaking again.  
6 Mr. Schwartz, I'm just going to err on the side of caution  
7 here because I'm not sure whether or not these documents  
8 are already included with CDTFA's submission. So I'm  
9 going to ask once again that if you submitted documents at  
10 any prior point, that you please -- that you would like us  
11 to consider, you please resubmit those with an exhibit  
12 index identifying and labeling each exhibit. You'll find  
13 the instructions for that in the prehearing conference  
14 minutes and orders that was previously sent to you.

15 MR. SCHWARTZ: Okay. I can do that, but these  
16 are documents that were submitted into the audit by the  
17 vendors, not by the taxpayer or CDTFA. And these  
18 documents were requested by both the taxpayer and the  
19 Department. And the issue was that the first half of the  
20 audit period these -- the vendors did not have the  
21 documents. They were already deleted from their systems,  
22 and the Department estimated those purchases.

23 And since the purchases and cost of goods is a  
24 contention or an issue in this audit, that's why I  
25 reference my letter on November 22nd, 2018. And at this

1 economic downturn in 2008, '09, and '10, the prices were  
2 quite lower than they were at the end of the audit. And  
3 that's what's kind of skewing the numbers a little bit.  
4 That's why I'm asking for a couple of percentage points  
5 reduction in the cost of goods sold, since you're  
6 impeaching it anyway, and closing the audit. And my  
7 client will agree to that and be done with the audit.

8           And the other issue is the penalty, which if it's  
9 only 2 percent reduction, which isn't that much, it should  
10 bring the measure of the sales tax under 10 percent,  
11 thereby, I'm asking for abatement of the penalty, which is  
12 kind of substantial too. And we will agree to that and be  
13 done with the audit. I agree with everything else. I  
14 agree with the markup percentage.

15           The inventory adjustments that were done during  
16 the appeal, they're a little bit off but I'm not going to  
17 argue that in the spirit of settling this case and getting  
18 it behind us. The only other item I have, which the  
19 Department did include in their exhibits, is I think it's  
20 important to note to the board members that this account  
21 was audited again with a no change. So I know that  
22 they're aware of that. And subsequently, I also got a  
23 letter, which unfortunately I don't have because I talked  
24 to him very early this morning because he couldn't make  
25 it.

1 JUDGE DANG: Mr. -- Mr. Schwartz.

2 MR. SCHWARTZ: Yeah.

3 JUDGE DANG: Mr. Schwartz, I'm going to interrupt  
4 you for a second. I think you've kind of gotten a little  
5 ahead of yourself and started making your presentation.

6 MR. SCHWARTZ: Oh, sorry. All right.

7 JUDGE DANG: At this point my only concern is, we  
8 can only consider documents that have been identified to  
9 us and that have been admitted into evidence. And thus  
10 far only CDTFA has identified any documents they would  
11 like us to consider. I'd just like to confirm whether or  
12 not you're okay with that.

13 MR. SCHWARTZ: That I'm okay with -- repeat that?

14 JUDGE DANG: I don't have any documents from you  
15 that you would like us to consider as evidence in this  
16 matter. And I'd like to know whether you will -- you do  
17 intend to submit anything for us to consider or whether  
18 you would just like to rely on what CDTFA has submitted.

19 MR. SCHWARTZ: I can -- I can do both if you  
20 want. I could do both because the information was -- was  
21 not submitted to either party because the vendors didn't  
22 have it, see. And then CDTFA took what they had in the  
23 latter period, where the prices of the goods were higher,  
24 and applied the markup percentage to that number to  
25 determine the measure. So I didn't think I would have to

1 work on that, but I could work on that if you would like  
2 me to.

3 JUDGE DANG: If I'm understanding you correctly,  
4 you have the vendor information for the periods that were  
5 estimated?

6 MR. SCHWARTZ: I have -- we both have, I believe,  
7 the vendor information that was supplied to us by the  
8 vendors, but the dates were -- some of them were halfway  
9 through the audit. They didn't have from the beginning of  
10 the audit. They didn't have it for 2009 and parts of  
11 2010. That's why on that 12A R2, you will see -- and the  
12 board members can see -- that these are estimated numbers  
13 because they're even -- you know, they're the same amounts  
14 for each quarter for the year, which in reality they  
15 should all be different numbers, but that's okay. And  
16 that's -- that's my argument.

17 JUDGE DANG: Okay. Mr. Schwartz, my question to  
18 you is do you have the vendor information for the periods  
19 that were estimated?

20 MR. SCHWARTZ: Yes. So I believe CDTFA or -- I'm  
21 old. I'm calling it the board. They have -- they  
22 estimated from information that has already been  
23 submitted. And they estimated from a latter period and  
24 went back and estimated for the prior period of the  
25 audit -- the beginning of the audit.

1           JUDGE DANG: Okay. This is Judge Dang speaking  
2 again. I'm going to just keep the record open, as I  
3 mentioned at the prehearing conference, due to COVID-19.  
4 The deadline for submitting evidence has been extended to  
5 45 days past the hearing date today. So I'll give you --  
6 I'll allow you until that time to submit any documents  
7 you'd like us to consider.

8           MR. SCHWARTZ: Oh, okay. Yes. I'll be happy to  
9 do that, and that would be after July 15th. So once I  
10 survive July 15th, I'll have time to work on this.  
11 That'll be great.

12           JUDGE DANG: Okay. And CDTFA -- I'm sorry. This  
13 is Judge Dang speaking again. CDTFA, you'll have 30 days  
14 to respond to any new submissions that the taxpayer will  
15 present.

16           Okay. And moving along. CDTFA, we received your  
17 Exhibits A through E; is that correct?

18           MR. SUAZO: This is Randy Suazo. Yes, that's  
19 correct.

20           JUDGE DANG: This is Judge Dang again. Thank  
21 you. Mr. Schwartz, do you have any objections to the  
22 admission of any of these exhibits?

23           MR. SCHWARTZ: No.

24           JUDGE DANG: This is Judge Dang again. Thank  
25 you.

1 CDTFA's exhibits are now admitted into evidence.

2 (Department's Exhibits A-E were received in  
3 evidence by the Administrative Law Judge.)

4 JUDGE DANG: Okay. So moving along to our  
5 presentations now. Mr. Schwartz, if you're ready to begin  
6 your presentation, you have 15 minutes.

7

8 PRESENTATION

9 MR. SCHWARTZ: Oh, okay. I think I've already  
10 run through it, but I'll summarize it again.

11 The two issues that were our contentions are that  
12 the cost of goods should be a little bit lower, and I've  
13 estimated that at 2 percent. I will submit information to  
14 back that up. And once that's done, the measure can be  
15 easily -- which I did on my letter to you -- figured out  
16 what the measure will be, and my client will pay the tax  
17 on it. And we're asking for abatement of the penalty  
18 because nothing was intentional, and the subsequent audits  
19 are no change and to close the case. That's the only two  
20 things that I wanted to discuss today.

21 JUDGE DANG: Thank you, Mr. Schwartz. Does that  
22 conclude your presentation for now?

23 MR. SCHWARTZ: For now, yes, it does.

24 JUDGE DANG: Okay. Thank you so much. Let me  
25 turn to my panel members at this time. Judge Wong, do you

1 have any questions for the taxpayer?

2 JUDGE WONG: This is Judge Wong. No questions.

3 JUDGE DANG: This is Judge Dang speaking again.

4 Judge Ralston, do you have any questions at this time?

5 JUDGE RALSTON: This is Judge Ralston. No  
6 questions.

7 JUDGE DANG: Thank you.

8 And CDTFA, if you're ready to begin your  
9 presentation, you have 15 minutes.

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PRESENTATION

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MR. SUAZO: This is Randy Suazo again. The Appellant operates a convenience store in Imperial Beach, California, selling cigarettes, beer, wine, liquor, soda, sundry items, periodicals, and food. The Appellant's start date was March 27, 2004. The prior audit was completed of the business for the period of July 1st, 2004, through June 30th, 2007.

The Department performed an examination for the audit period of July 1st, 2009, through June 30th, 2012. The Department compared gross sales for federal income tax returns and profit and loss statements through the Appellant's sales and use tax returns. No material differences were noted. The Appellant's profit and loss statements, Exhibit A, page 105, included amounts for both



1 taxable and nontaxable purchases and separate recorded  
2 amounts for taxable and nontaxable sales.

3           Using these amounts the Department computed the  
4 recorded markup of cost percentages for the period of  
5 July 2009 through December 2011. The recorded taxable  
6 markup was only 11.65 percent, which is much lower than  
7 expected taxable markup for a business of this size and  
8 location. Due to the low markup of cost achieved, the  
9 Department used an indirect markup of cost of goods sold  
10 method to compute audited taxable measure.

11           First, shelf tests were performed for the  
12 categories of cigarettes, liquor and wine, beer, soda, and  
13 miscellaneous taxable items, including periodicals. The  
14 markup for each cat -- cost -- the markup of cost for each  
15 category was computed, Exhibit A, page 32. For cigarettes  
16 many of the retail selling prices posted were less than  
17 the corresponding cost for purchase invoices.

18           As a result, many of the line items included a  
19 negative markup of cost with an overall markup of cost for  
20 cigarettes of only 3.23 percent. Upon investigation, the  
21 Department found that the Appellant received rebates from  
22 their cigarette vendors as an incentive to sell certain  
23 brands of cigarettes at lower sales prices.

24           The Appellant failed to report the taxable rebate  
25 income with their sales and use tax returns. Therefore,

1 the Department included the rebate amounts with the audit  
2 findings and accepted the lower than normal 3.23 percent  
3 markup for cigarettes. This is in Exhibit A, page 97 to  
4 101.

5 Next, the Department asked the Appellant to  
6 provide copies of all purchase invoices for October and  
7 November 2011 so that a purchase segregation could be  
8 performed to weigh the markup of cost percentages. During  
9 the segregation of the purchase invoices, the Department  
10 noted that it appeared some purchases were missing or  
11 understated. So the Department surveyed 96 percent of the  
12 Appellant's vendors to verify recorded purchase amounts.

13 An analyses of purchase information received  
14 versus recorded taxable purchases showed that the  
15 Appellant's recorded purchases were understated by  
16 11 percent. The Department summarized the total vendor  
17 survey purchase amounts for the audit period and  
18 calculated taxable segregation percentages. Using the  
19 shelf-test markups and the segregation percentages, the  
20 Department computed an audited weighted taxable markup of  
21 23.63 percent, which was accepted as reasonable.

22 Next, the Department computed audited cost of  
23 goods sold for the audit period. First, the total  
24 purchases for vendor services were reduce by a 1 percent  
25 shrinkage allowance, and then accordingly average purchase

1 amounts for each year were computed.

2           During the appeals process, the Appellant claimed  
3 a purchase additional inventory during the audit period to  
4 increase their store shelves and that an inventory  
5 adjustment was warranted. The Department reviewed the  
6 Appellant's claim in the beginning and any inventory  
7 amounts for the federal income tax returns and noted that  
8 there was a large difference between the inventory amounts  
9 claimed in year 2009 versus year 2012, exhibit page 109 to  
10 110.

11           However, the Appellant did not have any  
12 documentation or independent inventory reports to support  
13 their claim, and apparently estimated yearly inventory  
14 amounts. Despite the lack of documentation, the  
15 Department conceded that an inventory adjustment is  
16 warranted. Since the audit begins and ends at midyear  
17 points, the Department decided to use the average  
18 inventory numbers of 2009 and for 2012 to establish  
19 estimated beginning and ending inventory amounts.

20           To compute the allowable amount, the Department  
21 used the claim beginning and ending inventory amounts for  
22 the Appellant's federal income tax returns for both years  
23 2009 and 2012. Beginning inventory in 2009 for the  
24 federal income tax returns was at \$438,677. Ending  
25 inventory for federal income tax returns for 2009 is

1 \$588,311. An average inventory of \$513,494 was the  
2 beginning point of the audit period for the inventory. In  
3 the year 2012, beginning inventory stood at \$803,345. The  
4 ending inventory was \$798,251.

5 If you average the two out, the 2012 average  
6 inventory came out to \$800,798. The beginning inventory  
7 of 803 and the ending -- excuse me. The difference  
8 between these two amounts is \$287,000. That is the  
9 \$800,798 at the end or midpoint of 2012 and \$513,494 at  
10 the midpoint of 2009. This amount represents the  
11 Department's recommended combined taxable and nontaxable  
12 inventory change for the audit period.

13 The taxable purchase percentage per profit and  
14 loss statement of 90.07 percent was applied. The total  
15 inventory changed to calculate the Department's  
16 recommended taxable inventory adjustment for the audit  
17 period. This came out to be \$258,775. The Department's  
18 recommended inventory adjustment was spread evenly over  
19 the audit period to account for periodic increase of  
20 inventory purchase throughout the entire audit period.

21 This means that the audit purchases per the  
22 vendor survey were reduced by \$21,565 for each quarter in  
23 the audit period. This is in Exhibit B, page 124. Net  
24 purchase amounts represent the cost of goods sold for the  
25 surveyed vendors. The Department then calculated audited

1 taxable cost of goods sold by all vendors by dividing the  
2 net cost of goods sold by the surveyed vendor percentage  
3 of 96.5 percent, which are the ones they actually surveyed  
4 to get total taxable purchases.

5 The audited taxable cost of goods sold was  
6 multiplied by the audited markup of cost to calculate the  
7 audited taxable sales for the audit period. A comparison  
8 with reported taxable measure amounts resulted in  
9 understated taxable measure of over \$326,000. The  
10 Appellant contends that the audited taxable measures are  
11 incorrect because no inventory adjustment was provided.  
12 However, this contention is incorrect. As noted in this  
13 presentation and as can be found on Exhibit B, page 124,  
14 the Department made an inventory adjustment of \$258,775.

15 Additionally, the Department has reviewed the  
16 Appellant's proposed calculated of taxable inventory  
17 adjustment for their opening brief and recommends no  
18 adjustment to the audit findings or calculations. The  
19 Appellant has failed to present any substantial  
20 documentation for the periods within the audit period to  
21 prove the estimated amount was more accurate than the  
22 Department's recommended allowance.

23 Additionally, the Appellant's calculation is  
24 based on year 2009 beginning inventory and year 2011  
25 ending inventory, amounts multiplied by an amount of

1 88 percent taxable percentage which is unsubstantiated.  
2 The audit period is July 2009, which is the midpoint of  
3 the year, through June 30th, 2012, which is again the  
4 midpoint throughout the year. The Appellant's proposed  
5 calculation includes beginning inventory amounts from  
6 2009, which do not account for the inventory purchase for  
7 the 6 months prior to the start of the audit on  
8 July 1st, 2009.

9 And the calculation also does not account for the  
10 amounts purchased in the first six months of 2012, which  
11 are part of the audit period. A review of the Appellant's  
12 claim of cost of goods sold per federal income tax return  
13 show significantly less purchases in 2012 at the  
14 corresponding drop in sales. This is Exhibit A, page 109.  
15 These indicate the Appellant sold more inventory on hand  
16 in year 2012, which would likely include months within the  
17 audit period.

18 The Department's recommended inventory adjustment  
19 accounts for gradually -- for a gradual increase of the  
20 inventory purchase, periodically, the taxable percentages  
21 based on the purchase amounts. Thus, the audit findings  
22 are reasonable and fair.

23 The Appellant's response for hearing, dated  
24 6/13/2020, which was Saturday, as requested a 2 percent  
25 reduction in several tax purchases claimed that some

1 vendor information is estimated because the vendors had  
2 purged data from earlier time periods in an average -- and  
3 an average of periods were supplied and was used to  
4 compute the amounts where no data was available. This is  
5 Exhibit A, page 53.

6 Basically, it's dealing with three -- with two  
7 main vendors where six quarter are being estimated,  
8 Trepco, T-R-E-P-C-O, and Southern Wine and Spirits. Pepsi  
9 has an estimate for two quarters. All the other vendors  
10 are on an actual basis. There's no estimate made. Review  
11 of the reported sales, that's review -- reported sales  
12 show that taxable sales of \$1,391,907 were actually higher  
13 in periods from third quarter '09 through fourth quarter  
14 2010. That's the first six quarters of the audit period.

15 Then the \$1,330,194 taxable sales for periods  
16 from first quarter 2011 through second quarter of 2012.  
17 That's the last six quarters of the audit period, which is  
18 when an actual data was provided for all vendors surveyed.  
19 The higher sales in the beginning part of the period  
20 should mean a higher purchase amount in earlier periods.  
21 Therefore, we think that the findings are correct, or the  
22 estimate is correct.

23 In addition, the Appellant has argued that they  
24 did have more purchases earlier in the audit period as  
25 they were increasing their inventory. While their vendor

1 information was in complete, the Department used the best  
2 information available and believes this information fairly  
3 and reasonably estimates the purchase during the audit  
4 period -- the purchases during the audit period.

5 Appellant's response for hearing, dated again  
6 6/13/2020, has also requested that the negligence penalty  
7 be removed. Penalty is appropriate in this case for  
8 several reasons. The fact that an indirect method was  
9 used to arrive at the taxable sales. The fact that the  
10 Appellant did not keep complete and accurate records, and  
11 vendors needed to be contacted to compute the proper  
12 amount of taxable purchases, and the fact that this is the  
13 Appellant's second audit in the same type -- with the same  
14 type of error, are substantial reasons for the negligence  
15 penalty to remain.

16 The Appellant has not provided any documentation  
17 to support their contentions. Therefore, the Department  
18 request that the appeal be denied. This concludes my  
19 presentation, and I'm available to answer any of your  
20 questions you may have.

21 JUDGE DANG: This is Judge Dang speaking. Thank  
22 you for your presentation. Just to make sure I'm  
23 understanding CDTFA's position correctly, the reason for  
24 why CDTFA did not allow the requested 2 percent adjustment  
25 to inventory purchases is because for the period where



1 actual invoices were available, purchases had declined  
2 over time, so that would have, essentially, compensated  
3 for any price differential; is that correct?

4 MR. SUAZO: That's what it seem to be. Because  
5 the sales were higher in the earlier periods, which means  
6 that he would have to -- he would have had to purchase  
7 more items, more cost of goods sold in the earlier  
8 periods. I think it's roughly around a 3 percent decline  
9 from the beginning of the audit period to the end of the  
10 audit period. So, actually, he was given a favorable  
11 estimate.

12 In addition, he also asked -- he's also been  
13 requesting or stating that there was a buildup of  
14 inventory. In most of the buildup of inventory, if you  
15 look at the federal income returns, happens within the  
16 first two years of the audit period, again, when he's  
17 saying that the estimates are higher than they should be.

18 JUDGE DANG: This is Judge Dang speaking again.  
19 Thank you. I apologize if I've been cutting in and out.  
20 I wanted to take the opportunity at this time to ask my  
21 co-panelists if they had any questions of CDTFA.

22 JUDGE WONG: This is Judge Wong. I have no  
23 questions.

24 JUDGE RALSTON: This is Judge Ralston. I have no  
25 questions.

1           JUDGE DANG: Thank you. I wasn't sure if I was  
2 getting through there.

3           This is Judge Dang speaking. Let me turn to  
4 Judge Wong. Did you have questions for CDTFa?

5           JUDGE WONG: This is Judge Wong. I have no  
6 questions.

7           JUDGE DANG: Mr. Schwartz, are you able to hear?

8           MR. SCHWARTZ: Yeah. Well, I did hear no  
9 questions from Mr. Wong and the lady. That's all I heard.  
10 No questions. Can you hear me?

11          JUDGE DANG: Mr. Schwartz, this is Judge Dang  
12 speaking. I can hear you. Are you able to hear me?

13          MR. SCHWARTZ: Seems like you're breaking in and  
14 out.

15          JUDGE DANG: Let me go ahead and go off the  
16 record for a minute and just take a quick chance to  
17 reconnect my internet and see if I can improve things.  
18 I'll be back momentarily.

19          MR. SCHWARTZ: Okay.

20                 (There is a pause in the proceedings.)

21          JUDGE DANG: Let's go back on the record.

22                 I believe I was asking my co-panelists,  
23 Judge Wong, did you have questions for CDTFa?

24          JUDGE WONG: This is Judge Wong. I have no  
25 questions.

1 JUDGE DANG: Thank you.

2 Mr. Schwartz, if you're ready, you have five  
3 minutes on rebuttal.

4 MR. SCHWARTZ: Oh, okay. Thank you.

5

6 CLOSING STATEMENT

7 MR. SCHWARTZ: Thank you for taking the time to  
8 listen to us and to take our side into consideration. I  
9 listened to the presentation by the Board, and I  
10 understand it all. Parts that were a little difficult was  
11 it took several years to get through the audit, and there  
12 were lots of ups and downs and lots of different people  
13 involved within the audit and numbers changed and so  
14 forth, which I do understand because things happen, and  
15 things change.

16 But I would like an opportunity to revisit the  
17 beginning period and the estimated percentage or how they  
18 estimated those purchases, because that's an issue.  
19 Because during the recession, which is almost 10 years ago  
20 now, the prices were a lot lower, and they were estimated  
21 based upon prices that were higher. So I would like to  
22 take that opportunity to maybe submit that and get some  
23 reduction in the cost of goods and close the case.

24 And on the segregate rebates, the taxpayer was  
25 elderly and not from the United States, probably didn't

1 know a whole lot was going on. But in subsequent periods,  
2 he corrected everything, and that's why in the subsequent  
3 audits there was a no change, and his inventory pretty  
4 stable in the last few years. So that's all been correct  
5 and done. And still, we would like to have the penalty  
6 abated please.

7 So that's my rebuttal.

8 JUDGE DANG: This is Judge Dang speaking again.  
9 Thank you, Mr. Schwartz.

10 And once again I'd like to ask my co-panelists,  
11 starting with Judge Wong, do you have any questions for  
12 the Appellant?

13 JUDGE WONG: This is Judge Wong. I just had one  
14 question. Mr. Schwartz, regarding the negligence  
15 penalty --

16 MR. SCHWARTZ: Yes.

17 JUDGE WONG: -- would you like to provide a  
18 reason for your contention to delete the negligence  
19 penalty?

20 MR. SCHWARTZ: Yes. Because I think if a slight  
21 adjustment is made, the measure, hopefully, will fall  
22 within the less material amount and have the penalty  
23 abated. So I'm not sure what the materiality percentage  
24 is, but either have the penalty abated or maybe even just  
25 cut in half.

1           JUDGE WONG: This is Judge Wong. Thank you. I  
2 have no further questions.

3           JUDGE DANG: This is Judge Dang speaking again.  
4 I would just like to piggyback briefly off of Judge Wong's  
5 earlier question. If this panel were to decide that no  
6 further adjustments are warranted to the taxable measure,  
7 is Appellant, in essence, conceding the negligence penalty  
8 in that case?

9           MR. SCHWARTZ: No. I would like the negligence  
10 penalty abated either way.

11          JUDGE DANG: This is Judge Dang. Thank you for  
12 your response.

13          I'd like to turn to Judge Ralston. Did you have  
14 any final questions for the Appellant?

15          JUDGE RALSTON: This is Judge Ralston. No  
16 questions.

17          JUDGE DANG: This is Judge Dang speaking again.  
18 Thank you everyone for your presentations. I apologize  
19 for all the technical difficulties. I appreciate your  
20 patience as we work through these.

21          As a reminder the record will remain open for  
22 45 days in this matter for the submission of new evidence  
23 from either party. If anything new is submitted, rest  
24 assured the opposing party will have 30 days to respond to  
25 the submission of that evidence. Once the record is

1 closed this panel will meet and deliberate upon the  
2 arguments and the evidence that have been presented to us,  
3 and we will endeavor to give you our written opinion  
4 within 100 days from that date.

5 Thank you everyone. Once again, this hearing is  
6 now adjourned.

7 (Proceedings adjourned at 9:53 a.m.)

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HEARING REPORTER'S CERTIFICATE

I, Ernalyne M. Alonzo, Hearing Reporter in and for the State of California, do hereby certify:

That the foregoing transcript of proceedings was taken before me at the time and place set forth, that the testimony and proceedings were reported stenographically by me and later transcribed by computer-aided transcription under my direction and supervision, that the foregoing is a true record of the testimony and proceedings taken at that time.

I further certify that I am in no way interested in the outcome of said action.

I have hereunto subscribed my name this 29th day of June, 2020.

\_\_\_\_\_  
ERNALYN M. ALONZO  
HEARING REPORTER