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BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF, )  
SUN SUN ENTERPRISE, INC., ) OTA NO. 19034415  
APPELLANT. )  
\_\_\_\_\_ )

Transcript of Proceedings, taken at  
400 R Street, Sacramento, California, 95811,  
commencing at 1:22 p.m. and concluding at  
2:41 p.m. on Tuesday, July 28, 2020, reported  
by Ernalyn M. Alonzo, Hearing Reporter, in  
and for the State of California.

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APPEARANCES:

Panel Lead: ALJ JOSHUA LAMBERT

Panel Members: ALJ ANDREA LONG  
ALJ JOSHUA ALDRICH

For the Appellant: SHIRLEY SUN  
PAUL CHAN  
CHRIS HOUSH

For the Respondent: STATE OF CALIFORNIA  
DEPARTMENT OF TAX AND  
FEE ADMINISTRATION  
By: MARIFLOR JIMENEZ  
JASON PARKER  
CHRISTOPHER BROOKS

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I N D E X

E X H I B I T S

(Appellant's Exhibits 1-7 were received at page 8.)  
(Department's Exhibits A-I were received at page 8.)

OPENING STATEMENT

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By Mr. Housh 8  
By Ms. Jimenez 21

APPELLANT'S WITNESSES:

DIRECT      CROSS      REDIRECT      RECROSS  
Shirley Sun      12

CLOSING STATEMENT

PAGE

By Mr. Housh 39

1 Sacramento, California; Tuesday, July 28, 2020

2 1:22 P.m.

3

4 JUDGE LAMBERT: We are now on the record in the  
5 Office of Tax Appeals' oral hearing for the appeal of  
6 Sun Sun Enterprise, Inc., Case Number 19034415. The date  
7 is Tuesday, July 28th, 2020, and the time is approximately  
8 1:22 p.m. This hearing was originally scheduled for  
9 Sacramento, California. However, due to ongoing health  
10 concerns, we're holding these hearings electronically with  
11 the agreement of all the parties.

12 My name is Josh Lambert, and I am the lead  
13 administrative law judge for this hearing. And my  
14 co-panelists today are Andrea Long and Josh Aldrich.

15 Before we proceed, I will swear in the  
16 interpreter, Mr. Tang, at this time.

17 Mr. Tang, could you please state your name for  
18 the record.

19 THE INTERPRETER: My name is Weikuen Tang. Last  
20 name spelled T, like Tom, a-n-g. First name W-e-i-k-u-e-n.

21 JUDGE LAMBERT: Thank you. Briefly, what are  
22 your qualifications as a Cantonese interpreter?

23 THE INTERPRETER: I have been an interpreter for  
24 20 some years, and I hold a bachelor's degree in Chinese  
25 Language and Literature, which I got from the Chinese

1 University of Hong Kong.

2 JUDGE LAMBERT: Okay. Thank you. Can you please  
3 raise your right hand.

4

5 WEIKUEN TANG,

6 produced as a witness, and having been first duly sworn by  
7 the Administrative Law Judge, was examined and testified  
8 as follows:

9

10 JUDGE LAMBERT: Thank you.

11 Now, I'd like to have all the parties introduce  
12 yourselves.

13 Mr. Housh, could you introduce yourself, and  
14 Appellants, Ms. Sun and Mr. Chan, introduce yourselves.

15 MR. HOUSH: Thanks, Your Honor. Chris Housh  
16 attorney and an enrolled agent representing the Appellant.

17 JUDGE LAMBERT: And I believe we have Ms. Sun and  
18 Mr. Chan; is that correct?

19 MS. SUN: My name is Shirley Sun.

20 MR. CHAN: My name is Paul Chan.

21 JUDGE LAMBERT: Thank you.

22 And CDTFA, can you please introduce yourselves.

23 MS. JIMENEZ: Judge Lambert, this is Mariflor  
24 Jimenez. Good afternoon I'm representing the CDTFA.

25 MR. PARKER: I'm Jason Parker, also with the

1 CDTFA.

2 MR. BROOKS: Sorry about that. This is  
3 Christopher Brooks, and I'm tax counsel for CDTFA.

4 JUDGE LAMBERT: Thank you.

5 The issue in this appeal is whether adjustments  
6 are warranted to the determined measure of tax.

7 Appellant, do you agree that this is the issue?

8 MR. HOUSH: Yes, Your Honor. We agree this is  
9 the issue.

10 JUDGE LAMBERT: And CDTFA, do you agree that is  
11 the issue?

12 MS. JIMENEZ: Judge Lambert, this is Mariflor  
13 Jimenez. We agree that is the issue.

14 JUDGE LAMBERT: Thanks.

15 Appellant provides Exhibits 1 through 7. CDTFA  
16 provides Exhibits A through I.

17 Appellant, do you have any objections?

18 MR. HOUSH: Chris Housh for Appellant. We have  
19 no objections.

20 JUDGE LAMBERT: And CDTFA, do you have any  
21 objections?

22 MS. JIMENEZ: We have no objections.

23 JUDGE LAMBERT: Okay. Then I will enter those  
24 exhibits into the record.

25 ///

1 (Appellant's Exhibits 1-7 were received  
2 in evidence by the Administrative Law Judge.)  
3 (Department's Exhibits A-I were received in  
4 evidence by the Administrative Law Judge.)

5 JUDGE LAMBERT: Just to confirm the order of the  
6 hearing, Mr. Housh, you will have 90 minutes. During that  
7 time there will be witness testimony of Ms. Sun and  
8 Mr. Chan, and I'll swear them in before they talk. And  
9 then there will be questions by the OTA Judges and CDTFA  
10 may question the witnesses. After that, CDTFA has  
11 15 minutes, after which there will be questions and then  
12 Appellant's rebuttal, which is 10 minutes.

13 So, Mr. Housh, before the witnesses swear in, you  
14 can let -- you can let me know before they testify, and I  
15 can swear them in. So at this time, Mr. Housh, you will  
16 have the opportunity to explain your position starting  
17 now. Please proceed.

18 MR. HOUSH: Thanks, Your Honor.

19

20 PRESENTATION

21 MR. HOUSH: The taxpayers, Sun Sun Enterprise,  
22 Inc., runs a Chinese-style restaurant. And they have been  
23 running this business for many years. The CDTFA performed  
24 its audit, the audit period of July 1st, 2013 through  
25 June 30th, 2016, included a period where the restaurant



1 had been burglarized and had its credit card machine  
2 tampered with on two separate occasions, and their point  
3 of sale system or their computers had also been  
4 burglarized in 2015.

5 As such, when the auditor reviewed the paperwork  
6 of the restaurant and did a check of the software related  
7 to the restaurant, they found that for the period of 2015  
8 and 2016 that had access to the computers, that there was  
9 no changes. All the records were in proper order and that  
10 the sales tax was properly reported.

11 But because they could not go back and read the  
12 software information in the point of sale computer, the  
13 CDTFA using Riley B. as a way of trying to go and impugn  
14 that there can be some way to go and say that the  
15 taxpayer's records are not sufficient from having just the  
16 printed reports determine that the adjustment of amount of  
17 cash transactions had occurred after the credit card  
18 machine had been tampered with that that same cash  
19 percentage should be applied to all the past periods, even  
20 though no bank record reflects more cash; no tax return  
21 reflects more cash; and no other record reflects more cash  
22 in the periods prior to break-ins.

23 The State is attempting to go and say that they  
24 need only a bare whiff of not being able to look at a  
25 document as an excuse to go and deny the accuracy of all

1 other records. This is an extensive revision of what the  
2 findings are in Riley B., that says that if the documents  
3 are not trustworthy, then the State can go and use  
4 whatever other methods to come up with a percentage to  
5 determine the accurate element.

6 The State cited the federal tax return of one  
7 year as having additional income on the Schedule C of the  
8 return, but that additional income was actually the amount  
9 of sales tax reported as part of the gross receipts on the  
10 federal return which then has a deduction of that sales  
11 tax to come out. Again, none of the other items that the  
12 State has reviewed shows any variance. And the State has  
13 agreed that for the periods after the break-in that the  
14 records are accurate and correct, and no changes proposed  
15 for any period post break-in.

16 The State wants to go and make it where they can  
17 use any idea that they can conceive of to then create  
18 additional taxes on the business owner. The State brought  
19 up in one writing that they saw a notation of early 2012  
20 in the refurbished point of sale computer that the company  
21 used. The -- we have contacted the company that  
22 prepared -- provided that point of sale computer. And  
23 they stated that the traditional testing period when they  
24 had refurbished the machine, they enter in July of 2012 to  
25 run sample tests to see if the machine was working

1 properly. Unfortunately, they provided that to us too  
2 late to be able to provide as direct evidence.

3 The restaurant has maintained accurate records to  
4 the best of its ability, throwing out only paper records  
5 when there was an infestation that required them by the  
6 Health Department to toss the original paper receipts.  
7 The computer records that were reviewed, which are done on  
8 a monthly report, the CDTFA's only argument of those  
9 records were not accurate is a desire to go and say that  
10 cash to credit card ratio for the restaurant should have  
11 stayed the same after a known break-in that influenced the  
12 credit card machines. The taxpayers' have continued to go  
13 and operate everything properly.

14 At this time I would like to go and have the  
15 owners of the restaurant explain the situation regarding  
16 the break-in at their restaurant.

17 JUDGE LAMBERT: Okay. Mr. Tang, can you please  
18 translate the following to the witnesses?

19 THE INTERPRETER: Okay. Sorry. Can you repeat?  
20 I'm sorry.

21 JUDGE LAMBERT: Can you please translate this.

22 THE INTERPRETER: Okay. Okay. Please go ahead.  
23 Please go ahead.

24 JUDGE LAMBERT: I'm going to have them swear in  
25 now. Okay. First, we'll do Ms. Sun.

1 Ms. Sun, can you please raise your right hand.

2

3 SHIRLEY SUN,

4 produced as a witness, and having been first duly sworn by  
5 the Administrative Law Judge, was examined and testified  
6 as follows:

7

8 JUDGE LAMBERT: Thank you.

9 And for Mr. Chan. Can you please raise your  
10 right hand.

11

12 PAUL CHAN,

13 produced as a witness, and having been first duly sworn by  
14 the Administrative Law Judge, was examined and testified  
15 as follows:

16

17 JUDGE LAMBERT: Thank you.

18 Mr. Housh, please proceed.

19 MR. HOUSH: Thank you, Your Honor.

20

21 DIRECT EXAMINATION

22 BY MR. HOUSH:

23 Q Shirley, can you tell us how long you've been  
24 operating the business?

25 A For 11 years.

1           Q    How Long have you been using a point of sale  
2 system to record your sales?

3           A    I started using it right from the beginning, so  
4 for 11 years.

5           Q    Can you describe to us the events in 2015 that  
6 affected your point of sale system?

7           JUDGE LAMBERT:  I think -- I think maybe she  
8 should -- Mr. Tang, can you tell her to pause.

9           THE INTERPRETER:  So let me try to interpret what  
10 she said a moment ago.

11          THE WITNESS:  In year 2015 we have a lot of  
12 issues, including we have a 5th break-in and  
13 burglarization problem of -- and within the mall -- the  
14 bigger mall.  And also in our restaurant there was rat's  
15 infestation, and my major issue within the shopping mall  
16 there.  In addition also we have network cable problems.  
17 We also were -- were notified by the credit card company  
18 that there was some customers complaining about  
19 possibility of leakage of their credit card information.

20                 The rat infestation that I mentioned moments ago  
21 had an impact on how well we can maintain the network.  
22 And because the rats often times bite on the cable, as a  
23 result we lose internet connection.

24          JUDGE LAMBERT:  Mr. Housh, I believe you're on  
25 mute.

1 MR. HOUSH: I apologize.

2 BY MR. HOUSH:

3 Q During that time that you were experiencing  
4 internet problems, were you having more people paying cash  
5 than credit card?

6 A That's right.

7 Q For how long were you experiencing more people  
8 paying cash than credit card?

9 A I believe it persist for a period of two to  
10 three years.

11 Q In the periods of 2014 and beginning of 2015,  
12 were all sales recorded in the point of sale system?

13 A Yes.

14 Q How often did you receive reports from your POS  
15 system of the sales?

16 A Once a month.

17 Q When you were going through the CDTFA audit, did  
18 you provide those monthly reports to the State's auditor?

19 A Yes, I did.

20 Q Did you make any adjustments to the records that  
21 were given to the State auditor?

22 A No.

23 Q Is there any way to make a sale at your  
24 restaurant without ringing the information up in the point  
25 of sale system?

1 A No, that's not possible.

2 Q Do you, at this time, continue to use the point  
3 of sale system that you received in 2015?

4 A Yes.

5 Q Have you had any problems with the reports or  
6 information that you received from the point of sale  
7 system?

8 A There has been no issue about receiving report  
9 from the system.

10 Q Describe for us the process you had your sales  
11 tax returns prepared?

12 A For sales tax we are putting -- first off, I take  
13 out monthly data from the POS system. And then I turn  
14 these data to our accountant. Then the accountant will  
15 handle from this point onward to report all the numbers to  
16 the authority.

17 MR. HOUSH: At this time I have no further  
18 questions for the witness but will reserve for rebuttal  
19 questions if necessary.

20 JUDGE LAMBERT: Okay. That's fine. Are you  
21 finished with your presentation?

22 MR. HOUSH: Yes. At this time I will end my  
23 presentation, and the other items I'll save for rebuttal

24 JUDGE LAMBERT: Okay. Thank you. I'm now going  
25 to ask CDTFA if they have any questions for the witnesses.

1 MS. JIMENEZ: Judge Lambert, this is Mariflor  
2 Jimenez. We have no questions for the witness.

3 JUDGE LAMBERT: Thank you. And Judge Long do you  
4 have any questions for the witnesses?

5 JUDGE LONG: This is Judge Long. I just have one  
6 question. So did the news of the robbery effect your  
7 business in other ways? Did you lose any customers or did  
8 that -- did business -- the only effect was the increase  
9 in cash sales?

10 THE WITNESS: I don't feel -- I don't sense there  
11 were any loss of customers because of what happened in  
12 part because we were doing promotions around that period  
13 of time. And in addition, a big chunk of our clientele  
14 were senior restaurant goers.

15 JUDGE LONG: Okay. This is Judge Long. Thank  
16 you. I don't have any questions at this time.

17 JUDGE LAMBERT: And Judge Aldrich, do you have  
18 any questions?

19 JUDGE ALDRICH: Hi. This is Judge Aldrich.  
20 Yeah, I have a couple of questions. Could you describe  
21 what you mean by a break-in?

22 THE WITNESS: Our door was broken. So indeed  
23 there were -- there was a burglary.

24 JUDGE ALDRICH: Okay. So there was physical  
25 evidence that somebody entered without your authorization?



1 THE WITNESS: That's right.

2 JUDGE ALDRICH: And did you file a police report?

3 THE WITNESS: We did contact the police. The  
4 incident happened in the middle of the night, must be  
5 early, very early hours of the morning. We didn't know  
6 that until we step our foot into the restaurant the next  
7 morning. And when we contacted the police, the police  
8 said that since there was no one injured, there's no need  
9 for them to come to our restaurant.

10 JUDGE ALDRICH: Okay. And who paid for the door  
11 to be replaced?

12 THE WITNESS: We ourselves pay for the repair.

13 JUDGE ALDRICH: Okay. So insurance was not  
14 involved?

15 THE WITNESS: So we did not alert the insurance.

16 JUDGE ALDRICH: Okay. And how did she come to  
17 know that customers were experiencing issues with their  
18 credit card information being appropriated? Was that  
19 communicated somehow by Heartland?

20 THE WITNESS: Indeed it was. We were notified by  
21 Heartland to the extent Heartland actually stopped our  
22 system from using credit card for a short period of time.

23 JUDGE ALDRICH: Was the notification in writing,  
24 like an e-mail or a letter?

25 THE WITNESS: They telephone us.

1           JUDGE ALDRICH:  And what policy, if any, did she  
2     have regarding the payments of credit cards during that  
3     audit period?  So was there a threshold amount, for  
4     example, below \$25 cash only, more than \$25 credit card  
5     okay?  So what was the policy?

6           THE WITNESS:  My understanding is the manager has  
7     no firm threshold for how much sales, how much purchase  
8     would be eligible to use credit card payment.  But in  
9     general, I think they would say if somebody would ask them  
10    the line is \$25.  But in some cases some customers came  
11    saying that they don't carry enough cash.  Oftentimes, the  
12    manager would allow them to use credit card.

13          JUDGE ALDRICH:  Okay.  I don't have any  
14    additional questions so I'm going it turn back over to  
15    Judge Lambert.

16          JUDGE LAMBERT:  Thank you.

17          I guess my question is just kind of along the  
18    same lines.  Just is there any evidence that the credit  
19    card machine or the POS system was breached at all; or  
20    that there was a robbery, like a news report or anything?  
21    Is there any evidence that we can look at to see that  
22    there actually was a breach of the credit card system or a  
23    robbery?

24          THE WITNESS:  I don't think there is any news  
25    report that I can use.  But the main thing was that the

1       there was no -- no one who got injured by this break-in.  
2       And we didn't discover it until we appear at the  
3       restaurant the next morning. Let me add that during that  
4       period of time, we were unable to use the credit card  
5       system to accept customer payments. So that the computer  
6       company should be able to support our information.

7                 JUDGE LAMBERT: If there was no news reports,  
8       then I'm wondering how the public became aware that there  
9       was a credit card breach.

10                THE WITNESS: I think it's more likely because  
11       during that period of time we were unable to use the  
12       credit card system to accept payments. And so our  
13       customers when -- when they were explained the situation  
14       to them, they alert something has happened to the system.  
15       And as for ourselves, we got the notification from the  
16       credit card -- from the -- yeah, from the credit card  
17       company, yes.

18                JUDGE LAMBERT: And how long were they unable to  
19       accept credit card payments for?

20                THE WITNESS: I am not very positive about my  
21       recollection, but I believe it was more or less one week.  
22       The period last for more or less one week.

23                JUDGE LAMBERT: Why were there no guest checks or  
24       daily POS reports provided from the older POS system?

25                THE WITNESS: Can you repeat your question? I'm

1 not surely -- I don't fully understand.

2 JUDGE LAMBERT: Does she have guest checks for  
3 the older -- just to show her sales for the older POS  
4 system. Does she have any -- why does she only have  
5 monthly POS reports for the older system, but she has more  
6 information for the later POS system? Does that make  
7 sense? Why does -- ask her does she have guest checks or  
8 other evidence to show sales besides the monthly POS  
9 reports?

10 THE WITNESS: Yes. We do keep guest checks.  
11 But, unfortunately, because of the rat infestation lots of  
12 these checks were damaged and rat, yeah, make it very  
13 dirty and unsanitary. And as a result, we decided to  
14 dispose of all the paper guest checks.

15 JUDGE LAMBERT: Okay. That's all the questions I  
16 have. Thank you.

17 THE WITNESS: Thank you.

18 JUDGE LAMBERT: Okay. Now, we're going to move  
19 onto CDTFA. You have 15 minutes to give your  
20 presentation.

21 And Mr. Tang, you can just mute your mic, and  
22 we'll come back to you if we need to later on.

23 THE INTERPRETER: Okay.

24 JUDGE LAMBERT: Thank you.

25 And CDTFA, you may begin.

1 MS. JIMENEZ: All right. Thank you,  
2 Judge Lambert. This is Mariflor Jimenez.

3

4 PRESENTATION

5 MS. JIMENEZ: Appellant is a corporation  
6 operating a full-service restaurant selling Chinese-style  
7 food with a location in Fremont, California. This company  
8 also holds an active license to sell beer and wine. It  
9 has a start date of August 8, 2009. And the audit period  
10 for this case is from July 1st, 2013, through June 30th,  
11 2016.

12 The records provided are federal income tax  
13 returns for the fiscal year ending 2014 and 2015; credit  
14 card payment information from Appellant's merchant service  
15 providers; bank statements; month point of sales reports,  
16 and POS data covering the period July 15, 2015, through  
17 January 17, 2017. There are no POS data made available  
18 for the earlier periods from July 1st, 2013 through  
19 July 14th, 2015.

20 Using federal income tax returns for fiscal years  
21 ending in 2014 and 2015, the Department performed a markup  
22 analysis based on sales and cost of goods sold. The  
23 markup for fiscal year ending in 2014 was 142 percent.  
24 And the markup for fiscal year ending 2015 was  
25 129 percent. That's on your Exhibit, B page 37.

1           The Appeals Bureau also did their analysis using  
2 the reported sales to the CDTFA instead of the federal  
3 income tax returns and computed a markup of 117 percent  
4 for fiscal year end 2014 and 107 percent for fiscal year  
5 end 2015 and 111 percent for both years combined. You'll  
6 see that on your Exhibit E, page 71. The markup for both  
7 fiscal years are considered low for a sit-down restaurant,  
8 especially, one that serves beer and wine.

9           When the Department reviewed the monthly POS  
10 reports, we observed a substantial difference in cash  
11 sales for the earlier period, which is third quarter 2013  
12 through first quarter 2015, when compared to the later  
13 period of second quarter 2015 though second quarter 2016.  
14 Even though credit card sales remained relatively stable  
15 during the audit period, the POS report showed quarterly  
16 average cash sales of approximately \$97,000 for the  
17 earlier period, while it showed a quarterly average cash  
18 sales of \$197,000 towards the end of the liability period.

19           The cash amount basically doubled. That is  
20 \$100,000 in cash difference per quarter, which translate  
21 to over \$1,000 in cash per day. I want to give you an  
22 example of this drastic jump in cash sales. On Exhibit B,  
23 page 33, you will see the total cash column. In first  
24 quarter 2015 the cash sale is around \$109,000. While the  
25 second quarter 2015 the cash sale skyrocketed to around

1     \$206,000. That is a \$97,000 in cash difference between  
2     the two quarters alone.

3             Once again, this is over \$1,000 in cash per day.  
4     On the other hand, the POS reflects a quarterly average  
5     credit card sales of approximately \$362,000 at the  
6     beginning of the period. And around \$379,000 towards the  
7     end of the period. It also showed that customer or order  
8     counts did not fluctuate significantly throughout the  
9     liability period.

10            And you'll see that on your Exhibit B. Page 36.  
11     The Department downloaded the POS data directly from  
12     Appellant's POS system on January 18, 2017. But like I  
13     mentioned, the available sales data only covered periods  
14     following July 15, 2015.

15            The 1099 forms were also examined to analyze  
16     credit card sales ratio for the liability period. For the  
17     earlier quarters, the credit card sales were compared to  
18     total sales and established a credit card sales ratio of  
19     79 percent. For the later quarters, the same analysis was  
20     performed, which established a credit card sales ratio of  
21     65.47 percent. And that will be on your Exhibit B,  
22     page 27.

23            The Department again observed that the credit  
24     card sales ratio for the beginning of the audit period  
25     appeared high when compared to the ratio of the later

1       quarters. I want to point out once more that the POS  
2       reports did not show any significant increase in customers  
3       that would support the appearance of a sudden increase in  
4       cash sales beginning in second quarter of 2015.

5               Accordingly, the Department decided to verify for  
6       the sales of the earlier quarters. The available POS  
7       monthly reports for second quarter 2015 through third  
8       quarter 2015 and the POS data for the period fourth  
9       quarter 2015 through fourth quarter 2016 were used.  
10       Department divided recorded credit card sales by recorded  
11       total sales to establish a credit card ratio of  
12       6.65 percent. That will be on your Exhibit B, page 26.

13               Reported taxable sales were accepted for the  
14       periods second quarter 2015 through fourth quarter 2016  
15       because amounts were consistent with the POS sales data.  
16       And the credit card sales ratio of 66.65 percent was  
17       reasonable for Appellant's type of business. However, the  
18       reported taxable sales for the earlier periods were not  
19       accepted since one, the calculated markup is too low for a  
20       sit-down restaurant, especially one that serves beer and  
21       one.

22               Appellant was unable to sufficiently explain the  
23       substantial difference in both amounts of recorded cash  
24       sales and the ratio of credit card sales between this  
25       earlier period and the later periods after



1 April 1st, 2015. Plus, no POS sales data was made  
2 available for this time frame. Therefore, the Department  
3 establishes audited taxable sales for the earlier periods  
4 using the credit card sales ratio method.

5 California imposes a sales tax on the retailers'  
6 retail sales in the state of tangible personal property  
7 measured by the retailer's gross receipt. Unless the sale  
8 is specifically exempt or excluded on taxation by statute.  
9 That's Section 6051. All of the retailer's gross receipt  
10 are presumed subject to tax unless the retailer can prove  
11 otherwise. That's Section 6091.

12 It is taxpayer's responsibility to maintain and  
13 make available for examination on request all records  
14 necessary to determine the correct tax liability under the  
15 sales and use tax law, including bills, receipts,  
16 invoices, or other documents of original entry supporting  
17 the entries in the books of account. That's Section 7053  
18 and 7054.

19 If the Department is not satisfied with a  
20 taxpayer's return, the Department may compute and  
21 determine the amount required to be paid upon the basis of  
22 the facts contained in the return or returns, or upon the  
23 basis of any information within its possession or that may  
24 come into its possession. That's Section 6481.

25 When a taxpayer challenges a Notice of

1 Determination, the Department has the burden to explain  
2 the basis for that deficiency. Where the Department's  
3 explanation appears reasonable, the burden of proof shifts  
4 to the taxpayer to explain why the Department's asserted  
5 deficiency is not valid.

6 Except as otherwise specifically by law the  
7 applicable burden of proof is upon the taxpayer to prove  
8 all issues of fact by a preponderance of the evidence.  
9 That is the taxpayer must establish by documentation or  
10 other evidence that the circumstances it asserts are more  
11 likely than not to be correct.

12 Audited total sales for the period third quarter  
13 2013 through first quarter 2015 is calculated by dividing  
14 the credit cards sales of approximately \$2,543,000 by the  
15 credit card sales ratio of 66.65 percent. This resulted  
16 in audited taxable sales of approximately \$3,816,000. The  
17 Department then adjusted audited taxable sales by the  
18 applicable tax rate of 9 percent and established audited  
19 taxable sales of around 3.5 million.

20 The audited taxable sales amount was compared to  
21 reported taxable sales for the same liability period of  
22 approximately \$2,954,000 and established an unreported  
23 taxable sales of approximately \$547,000. This can be  
24 found on your Exhibit B, page 24.

25 So I want to first address the claim that

1 Appellant was not able to provide the POS sales data that  
2 was used in the earlier periods, as it was damaged during  
3 its break-in and replaced. In addition, Appellant claimed  
4 that it was unable to provide source documents for the POS  
5 monthly reports, such as the guest checks or other  
6 documents because many of the records were destroyed after  
7 a rat infestation. And Appellant's also started a new POS  
8 system in October of 2015 because its previous POS system  
9 failed.

10 So the Department believes that sales data that  
11 was damaged during the break-in and destroyed by rat  
12 infestation still exist on the hard drive that stores the  
13 POS data as well as the backup drive. All the Appellant  
14 needs to do is request the information from their POS  
15 vendor. Appellant is claiming that the older data in the  
16 POS system is not theirs, but there's evidence to support  
17 that Appellant transferred the original database, used  
18 since 2012, into the replacement server in 2015. The  
19 information file has a registration of July 27, 2012. You  
20 will see that on your Exhibit I, page 108.

21 And then if you take a look at the Login Table,  
22 it shows most staff accounts were created on  
23 August 1st, 2012, and were still in use in 2017. You will  
24 see that on your Exhibit I, page 107. If you look at the  
25 Close Shift Table, it shows the same usernames were active

1 from August 1st, 2012, through 2017. You will see that on  
2 your Exhibit I starting on page 118. The transaction  
3 count by waiter shows the same user for staff with the  
4 same names created in 2012 are still consistently  
5 processing the majority of the orders in 2015, 2016 and  
6 2017. That would be on your Exhibit I, page 144.

7 So an increase in cash sales at a restaurant  
8 business should typically correspond to an increase in  
9 customers. In this case, Appellant's POS monthly report  
10 show that customer counts remain stable throughout the  
11 liability period while cash sales increased significantly  
12 starting second quarter 2015. It is common for  
13 restaurants to offer special promotions to generate sales,  
14 but there's no evidence that promotion affected customer's  
15 choice of payment method. Appellant did not require  
16 customers to pay with cash to take advantage of the  
17 promotion as far as my understanding.

18 In fact, when I read Yelp reviews, I noticed that  
19 reviewers were stating that Appellant was only accepting  
20 cash from 2009 to 2010. And then from 2011 through 2014,  
21 the Appellant started to accept credit cards with a  
22 minimum order of between \$20 to \$25. And that would be on  
23 your Exhibit F. And I found that on pages 79, 80, and 88.  
24 There are also reviewer comments that the restaurant would  
25 only accept one credit card per table. So it basically

1 discouraged big party from splitting the bill. So  
2 customers had to cross the street to pull out the cash.  
3 And you will see that on your Exhibit F, pages 79 and 83.

4 Now, I did not see these restrictions after 2014.  
5 With that said I would actually expect the cash sales in  
6 the earlier period to be higher than the later one. If  
7 you look at Exhibit I, page 145, over 35 percent of total  
8 sales are transactions of \$20 or less. And let's not  
9 forget in some cases customers paid cash for transactions  
10 over that amount. Even the big groups who are splitting  
11 their bill ended up paying cash because of the requirement  
12 of just one credit card per table during the earlier  
13 periods.

14 Appellant also claims that the credit card  
15 payment system was breached in 2015 and more customers  
16 began to pay cash after a local story reported on that  
17 breach. The POS report show that the credit card sales  
18 actually increased by 3.14 percent from 2014 to 2015, even  
19 though the total number of customers' transactions  
20 decreased from one 144,000 in 2014 to 141,000 in 2015.  
21 And you see that on your Exhibit B, page 36.

22 Appellant also asserts that it experienced  
23 internet outages during -- which resulted in an increase  
24 in cash sales because the credit card payment system was  
25 unable to process those transactions without an internet

1 connection. But it switched internet provider during  
2 second quarter of '15 and then it stopped experiencing  
3 many of the connection.

4 All right. So the POS report shows that the cash  
5 sales increased towards the later period. The quarterly  
6 credit card ratio did not change significantly from  
7 quarter to quarter. And that would be on your Exhibit B,  
8 page 27. The POS monthly report also show a sustained  
9 increase in cash sales even after the Appellant obtained  
10 reliable internet service in second quarter of 2015.  
11 You'll see that on your Exhibit B, page 35.

12 So Appellant did not provide source documents for  
13 its POS reports. And the available POS sales data only  
14 covered periods after July 15, 2015. The cash sales  
15 substantially increased after April 1st, 2015, while the  
16 credit card remained fairly consistent. The calculated  
17 reported markup is also low for sit-down restaurant.  
18 Appellant has provided several explanations for the  
19 apparent increase in cash beginning in second quarter  
20 2015. However, Appellant has provided no documentary  
21 evidence to support these explanations.

22 The Department's audit findings are reasonable  
23 and fair. Therefore, we request the Appellant's appeal be  
24 denied. This concludes my presentation. I'll be  
25 available to answer any questions you may have.

1 JUDGE LAMBERT: Thank you, Ms. Jimenez.

2 And I'll ask the panel if they have questions.  
3 Judge Long, do you have any questions?

4 JUDGE LONG: Yes, I do. This is Judge Long. So  
5 CDTFA just mentioned that the credit card ratio did not  
6 change, and the number of customers remained steady. I  
7 guess this is really a question for Appellant, if that's  
8 all right.

9 For Appellant's do you have any way of  
10 reconciling that information based on your assertion that  
11 more people began to pay by cash after the robbery.

12 MR. HOUSH: Yes, Your Honor. The tables were  
13 entered into the system almost always as the number of  
14 chairs instead of the actual number of customers sitting  
15 at the table. So there were more transactions that  
16 happened of smaller people -- smaller customers sitting at  
17 that table.

18 The business, again, cannot go and actually do a  
19 sale without running it through the POS system. And  
20 although CDTFA is claiming that there were no POS reports  
21 provided, on the first page -- item on Exhibit B, page 39,  
22 is the auditor reporting with his measure how he did get  
23 the monthly reports from the POS going clear from  
24 July 2013 to 2016.

25 So they did have it where the number of customers

1 entered into the POS has errors just because it could be  
2 two people sitting at a table meant for four, and the  
3 computer system will show four people. But the amount of  
4 sale was always recorded into the system, and the  
5 information of the amount of sale and items of food was  
6 available on that POS system report alongside of what was  
7 cash and what was credit card.

8 JUDGE LONG: Thank you. I don't have any  
9 additional questions for either party.

10 JUDGE LAMBERT: Judge Aldrich, do you have any  
11 questions?

12 JUDGE ALDRICH: Hi. This is Judge Aldrich.  
13 Yeah, I have a brief question for the Department. So  
14 Ms. Jimenez, you mentioned a couple of times that the  
15 markup was low for this type of business compared to what?  
16 Compared to other restaurants with beer or liquor license  
17 or --

18 MS. JIMENEZ: Judge Aldrich, this is Mariflor  
19 Jimenez. That is correct. The average restaurant markup  
20 ones that especially sells -- that serves beer and wine is  
21 going to be around 200 percent.

22 JUDGE ALDRICH: And is that for that local area,  
23 or are you talking in general for the state?

24 MS. JIMENEZ: That's correct. It will be for  
25 that area.



1 JUDGE ALDRICH: Okay. Thank you.

2 JUDGE LAMBERT: I just have a question,  
3 Ms. Jimenez. You mentioned that the data is there to be  
4 accessed for the older POS system. And maybe you could  
5 expand upon what that means and what the difference  
6 between what that data is versus the monthly reports.

7 MS. JIMENEZ: Judge Lambert, this is Mariflor  
8 Jimenez. Let me just explain. The monthly point of sales  
9 reports, all of those were provided for the audit period.  
10 What's missing is the POS data for the prior period from  
11 July 2013 through July 14, 2015. As far as the data,  
12 those data that's transmitted from their POS system to  
13 their vendor, those are stored by their vendor in their  
14 hardware. And most of the time they should also have a  
15 backup of that. All they have to do is ask the vendor.

16 JUDGE LAMBERT: And did you request that they ask  
17 their vendor for that data?

18 MS. JIMENEZ: We did.

19 JUDGE LAMBERT: And do you have any -- what is  
20 CDTFA's experience or comments on the possibility of the  
21 credit card information breach or POS system breach  
22 effecting sales on the system?

23 MS. JIMENEZ: Right. So if -- if it was breached  
24 the credit card sales would decrease because my -- their  
25 explanation is that they actually have customers who are

1 now paying cash instead of credit card. Actually, the  
2 credit card from 2014 to 2015 increased.

3 JUDGE LAMBERT: Okay. Thanks. And I think Judge  
4 Aldrich may have a couple of more questions.

5 JUDGE ALDRICH: This is actually for the  
6 Appellant not for the Department. So if Ms. Sun could  
7 reply. I don't know. Is she still on the line?

8 MR. HOUSH: Yes, Your Honor. Ms. Sun is still on  
9 the line.

10 JUDGE ALDRICH: Okay. So I was just wondering if  
11 she could briefly describe how tips or gratuity were  
12 handled during the audit period.

13 THE INTERPRETER: Can you repeat the question  
14 again.

15 JUDGE ALDRICH: Sure. Could she briefly describe  
16 how tips or gratuity were handled during the audit period?

17 THE WITNESS: The tips, of course, would be given  
18 to the waitresses or the waiters.

19 JUDGE ALDRICH: Okay. And then earlier you  
20 testified that all sales went through the POS system. I  
21 was just wondering who was authorized to void sales or  
22 change sales, if anyone?

23 THE WITNESS: Only this happened only when  
24 individual customers decided to cancel an order, or they  
25 order take out, but they decided they're not going to

1       come. They won't come to pick it up.

2               JUDGE ALDRICH: Okay. This question is for  
3 Mr. Housh. So on Exhibit B -- page 36 of Exhibit B, I was  
4 wondering if you had a comment regarding the auditor's  
5 comment where it explains that, "Tips remained constant  
6 during the audit period when there was a 25 percent  
7 increase in sales." I was hoping you could help explain  
8 that.

9               MR. HOUSH: I'm sorry. Can you repeat the  
10 question?

11              JUDGE ALDRICH: So Exhibit B, page 36, there's an  
12 audit comment that says that, "Tips remained constant  
13 during the audit period when there was a 25 percent  
14 increase in sales." Can you help explain that issue or  
15 address it?

16              MR. HOUSH: Okay. Well, it's saying that the  
17 tips income is consistent. Oh, I'm sorry. I'm trying to  
18 find the line here with that. So I do apologize. I'm  
19 trying to find the exact line that reference this.

20              JUDGE ALDRICH: Take your time.

21              MR. HOUSH: The periods that is discussed by the  
22 auditor is the periods '13, '14 and then fiscal year '14,  
23 '15. So those are the periods that were not available by  
24 POS. He leaves out the period that --

25              JUDGE ALDRICH: Okay.

1           MR. HOUSH:  -- it'll be reviewed in the POS and  
2   the report.

3           JUDGE ALDRICH:  Okay.  I don't have any further  
4   questions.  I'm going to turn it back over to  
5   Judge Lambert.

6           JUDGE LAMBERT:  Okay.  Thanks.

7           I guess since we're asking Appellant questions,  
8   I'll just have one more question for the witness.  And  
9   that is just that CDTFA says that they asked you to  
10   request the POS data for the prior from the POS company.  
11   And can you ask them if they asked the POS company for  
12   that data?

13          THE WITNESS:  Yes, I did.  I asked the POS  
14   company to supply me with that information.  But,  
15   unfortunately, they said that they did not have it, and  
16   they explained that unless individual customers asked them  
17   to backup the information.  Otherwise they won't have back  
18   up copies in their system.

19          And I'm not very sure about the possibility of  
20   retrieving information from the POS machine.  So I have no  
21   idea about any backup within the machine.  I also asked  
22   the computer company about any data that we may somehow  
23   find within the machine.  They replied saying that within  
24   the machine there are only manual and also some basic  
25   information so that when technicians need to come to

1 repair the machine, they know how to do it.

2 JUDGE LAMBERT: Okay. Thank you.

3 Mr. Housh, please take this time to make your  
4 rebuttal. You didn't spend much time in your original  
5 presentation, but make a rebuttal, like, 10 minutes. Or  
6 if you need a little more time, just let me know. Thanks.

7 MR. HOUSH: Thank you, Your Honor.

8

9 CLOSING STATEMENT

10 MR. HOUSH: The CDTFA has continued to go and say  
11 that they did not get any reports about the earlier  
12 period, although, again, Exhibit B, page 39, specifically  
13 states bank statements, point of sale monthly reports, tax  
14 returns, and Heartland statements were provided of all the  
15 2013, 2014 and beginning of 2015 periods that the State is  
16 claiming there's no documentation.

17 In regard to the statement that the markup is low  
18 for the restaurant, again, when the State reviewed all the  
19 information of 2015 and 2016, they found out the  
20 information was correct and was consistent, that the  
21 markup is still the same as in the other period and the  
22 State alleged no errors in the third quarter 2015 through  
23 the end of the audit period. It's only the period that  
24 they can't review the POS hardware that the State is  
25 alleging any errors are happening in the paperwork.

1           If the numbers that are in the reporting are  
2 consistent of income and everything else of the standards  
3 are consistent, then the fact that their markup is low  
4 does not mean that they had a different amount of sales  
5 happening in previous period. And the State, obviously,  
6 does not have the ability to mandate that the markup of a  
7 certain percentage should happen as much as it could be  
8 great advice for how to run the business in the future to  
9 make more profit.

10           The taxpayer made the efforts to try and get the  
11 information that the State wanted for the older periods.  
12 But when they are not able to obtain, when they have  
13 become a victim of a crime, they go and further penalize  
14 them by going and saying that the largest number that the  
15 State can find a basis to go and compare on to be also  
16 paid out as a sales tax on top of that is a misreading of  
17 the situation in Riley B.

18           Riley B. and the other cases that I cited in our  
19 brief all have where there was an error that was found by  
20 the auditors for a blatant misstatement in the  
21 documentation making it where the documentation is  
22 unreliable. Here the State is only able to go and say  
23 that because they cannot look through the additional  
24 hardware, that they want to make conjecture that there  
25 must be errors in that report despite the other evidence

1 that they receive.

2 There's no elements out there outside of that,  
3 again, in the standard situation if there's a break-in,  
4 that people are going to increase the amount of cash that  
5 you get right out of business instead of relying on the  
6 credit card and that have then adjusted forward so people  
7 feel confident using credit cards again. That amount did  
8 not mean that conjecture is that there must have always  
9 been a credit card in the past, and to increase without a  
10 real basis the amount of sales that are alleged.

11 With regard to the credit card company  
12 information about the breach, as Shirley stated, yes, they  
13 received contact from the credit card company. That is  
14 documentation that, unfortunately, we have not received  
15 and be able to provide over to the State. And,  
16 unfortunately, evidence in expecting about how the credit  
17 card company and POS company set up their systems to  
18 explain the elements of why there's entries from 2012,  
19 unfortunately, the company provided it to us on Monday and  
20 that makes it where, unfortunately, it was too close to  
21 hearing time to be allowable.

22 But they stated that they traditionally used that  
23 date in 2012 as the starting point to run the test entries  
24 and go use it as the setup date. We provided the receipt  
25 of the refurbished POS system purchase to when it was

1 given to the restaurant and when it became accurate. So  
2 the State's allegation that this is just the same POS is  
3 inaccurate and the evidence showed that.

4 At the time, I believe that the evidence that has  
5 been provided shows that that the information is correct.  
6 As the State said, Riley B. has as its ruling -- I  
7 apologize -- that code I quoted before clearly  
8 contemplates an examination behind books, so to speak, in  
9 with the original records such as purchase invoice, sales  
10 slip, cash register tapes, and input records may be  
11 audited and analyzed.

12 There's no requirement that such audit be  
13 restricted to point out the falsifications, errors, and  
14 errors and omissions. But at the same time it is supposed  
15 to be done on the basis of any information which is in the  
16 possession of -- or that it may come into its possession.  
17 What the State is doing in this case is making conjectures  
18 based not on any record that it has or that it may obtain,  
19 but solely going in and trying to find a calculation on  
20 which to run a number to come up with a new tax.

21 At this time I will rest.

22 JUDGE LAMBERT: Thank you.

23 Judge Long, do you have any final questions?

24 JUDGE LONG: This is Judge Long. I have no other  
25 questions. Thank you.



1                   JUDGE LAMBERT:  And Judge Aldrich, do you have  
2 any final questions?

3                   JUDGE ALDRICH:  I don't have any final questions.  
4 Thanks.

5                   JUDGE LAMBERT:  Well, if there's nothing further,  
6 I'm going to close the record and conclude the hearing.  I  
7 want to thank each party for coming in today and thank the  
8 interpreter for all his help.  We will issue a written  
9 opinion within 100 days.  Thank you.

10                   This hearing is now closed.

11                   (Proceedings adjourned at 2:41 P.M.)

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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 1st day of September, 2020.

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ERNALYN M. ALONZO  
HEARING REPORTER