

BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF,)
)
HITCO CARBON COMPOSITES, INC.,) OTA NO. 18063355
)
 APPELLANT.)
)
)

TRANSCRIPT OF VIRTUAL PROCEEDINGS

State of California

Tuesday, June 15, 2021

Reported by:
ERNALYN M. ALONZO
HEARING REPORTER

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Transcript of VIRTUAL PROCEEDINGS,
taken in the State of California, commencing
at 12:59 p.m. and concluding at 1:40 p.m. on
Tuesday, June 15, 2021, reported by
Ernalyn M. Alonzo, Hearing Reporter, in and
for the State of California.

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APPEARANCES:

Panel Lead: ALJ MICHAEL GEARY

Panel Members: ALJ JOSHUA LAMBERT
ALJ KEITH LONG

For the Appellant: JANET PASS

For the Respondent: STATE OF CALIFORNIA
DEPARTMENT OF TAX AND
FEE ADMINISTRATION

JARRETT NOBLE
SCOTT CLAREMON
JASON PARKER

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I N D E X

E X H I B I T S

(Joint Exhibits J-1 through J-9 were received at page 7.)
(Department's Exhibits A through D were received at page 7.)

P R E S E N T A T I O N

	<u>P A G E</u>
By Ms. Pass	8
By Mr. Noble	15

C L O S I N G S T A T E M E N T

	<u>P A G E</u>
By Ms. Pass	24

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California; Tuesday, June 15, 2021
12:59 p.m.

JUDGE GEARY: Welcome to the Office of Tax Appeals hearing in the Appeal of Hitco Carbon Composites, Inc. The Office of Tax Appeals OTA Case Number 18063355. Today is June 15th, 2021, and the time is approximately 12:59 p.m. This hearing has been noticed for Cerritos, California but is being conducted electronically with the agreement of the parties.

Today's hearing is heard by a panel of three Administrative Law Judges. My name is Michael Geary, and I will take the lead in conducting the hearing. I'm joined on panel by Josh Lambert and Keith Long. After the hearing the three of us will discuss the arguments and the evidence. Each of us will have an equal voice in those discussions, and at least two of us must agree on an issue or issues presented. Pardon me. Any of us on the panel may ask questions or otherwise participate in today's hearing to ensure that we have all the information that we need to decide the appeal.

Now, let's have the parties identify themselves, stating their names and who they represent, beginning with the Appellant.

Ms. Pass, you seem to be muted.

1 MS. PASS: Janet Pass representing Hitco Carbon
2 Composites.

3 JUDGE GEARY: Agency.

4 MS. PASS: I am an attorney. Oh, I'm sorry.

5 JUDGE GEARY: No, no. The agency can identify
6 themselves, please.

7 MR. NOBLE: This is Jarrett Noble representing
8 the Department of Tax and Fee Administration.

9 MR. CLAREMON: This is Scott Claremon
10 representing CDTFA.

11 MR. PARKER: And Jason Parker with CDTFA as well.

12 JUDGE GEARY: Thank you everybody.

13 It's my understanding that there will be no live
14 witnesses today and that we will hear only oral arguments.

15 Ms. Pass, is that correct?

16 MS. PASS: Yes, that's correct.

17 JUDGE GEARY: And, Mr. Noble, is that correct?

18 MR. NOBLE: Yes, sir. That's correct.

19 JUDGE GEARY: Okay. I see that I have already
20 forgotten to identify myself when I speak. I will try to
21 do better.

22 Talking about exhibits. This is Judge Geary
23 speaking. The exhibits marked, thus far, for
24 identification in this appeal consist of Appellant's
25 exhibits marked 1 and 2, and Respondent's exhibits marked

1 A through E -- hold on a second. Check something before I
2 do that. No. Excuse me. We have the exhibits marked,
3 thus far, are Joint Exhibits J1 through J9, and
4 Respondent's only Exhibits A through D. Pardon me for that
5 error. And there have been no objections communicated to
6 my office.

7 And would I be correct, Ms. Pass, that you have
8 no objection to the exhibits offered by Respondent?

9 MS. PASS: That's correct.

10 JUDGE GEARY: All right. Since I know there's no
11 objections to joint exhibits, I'm going to admit all of
12 those exhibits. That is Joint Exhibits J-1 through J-9
13 and Respondents Exhibits A through D now. Excuse me.

14 (Joint Exhibits J-1 through J-9 were received
15 in evidence by the Administrative Law Judge.)

16 (Department's Exhibits A through D were received
17 in evidence by the Administrative Law Judge.)

18 The issue to be decided in this appeal is whether
19 Appellant is entitled to adjustments -- additional
20 adjustments to the determined liability for use tax
21 accrued and reported in error.

22 Ms. Pass, is that correct?

23 MS. PASS: That is correct.

24 JUDGE GEARY: Mr. Noble, is that correct?

25 MR. NOBLE: That is correct.

1 JUDGE GEARY: All right. Thank you.

2 For time estimates we had a prehearing conference
3 in this case. Actually, I think we had a couple of
4 prehearing conferences. We agreed that Appellant's
5 opening argument would require no more than 15 minutes and
6 that Respondents only argument would require no more than
7 15 minutes, with Appellant having an opportunity to offer
8 a closing argument -- completely optional -- of no more
9 than approximately 5 minutes.

10 Ms. Pass, is that timing still going to work for
11 you?

12 MS. PASS: It will.

13 JUDGE GEARY: And, Mr. Noble, would the timing
14 work for you?

15 MR. NOBLE: Yes, it will.

16 JUDGE GEARY: Thank you.

17 All right. In that case, I think that we're
18 ready to hear the arguments.

19 Ms. Pass, you can begin with your first argument
20 when you're ready.

21

22 PRESENTATION

23 MS. PASS: Janet Pass presenting.

24 What we have are five tool purchases that were
25 made during the audit period where Hitco erroneously

1 reported use tax on tooling that was resold to Lockheed
2 for use on the Joint Strike Fighter Program. We had
3 hundreds of tools purchased, and there are five left in
4 the audit where we are still in disagreement as to whether
5 or not they were resold to Lockheed.

6 So I'm going to go through the line items. They
7 are all from Schedule R2-12I. The first one is Line 29,
8 which is from Exhibit J-4, page 1 through 3. It's a
9 Hampson/Odyssey tool purchase. The CDTFA's comment was
10 they couldn't identify it on the purchase order. I direct
11 you to page 27 of the binder, which is Exhibit J-4, 1
12 through 3. It actually has STOVL's trim tools listed
13 as -- on the master purchase order issued from Lockheed.
14 And so that matches the description on the Hitco PO, as
15 well as the Odyssey invoice.

16 Both the Hitco PO and the Odyssey invoice
17 reference the same tool, as well as the Hitco PO
18 references the Lockheed Martin PO, as well as it will be
19 resold to Lockheed Martin. That language has been
20 accepted for numerous other tools. And the CDTFA had
21 indicated their disagreement was related to the
22 description, unable to tie it. But if you note, the STOVL
23 trim tools are listed on page 27 in that binder. So you
24 can tie the description back.

25 For Line 32, which was a purchase from

1 Visioneering, had the same comment. It was a CV tool.
2 That tool is listed on the page 27. You can see that
3 there are CV tools listed. And that description is both
4 on the Hitco PO, as well as the invoice for Visioneering.
5 And so it is consistent with the master contract language,
6 and that you can see there are STOVL and CV tools listed.

7 Our last three of the tools were all from
8 Futuramic. The CDTFA indicated that their problem was it
9 had a different contract number listed. So, therefore,
10 they weren't tying it to the original JSF contract. The
11 US Government issued an extension to the contract and gave
12 it a new contract number. In Exhibit J-9, pages 1 of 33
13 and 3 of 33, you can tie the new contract number to the
14 prior JSF contract. It says it is an extension of that
15 JSF contract. And so the terms of -- Lockheed's
16 government terms, the flow down terms are all consistent.

17 And flow down -- due to the length of time this
18 audit has been outstanding and that Hitco has been sold,
19 the division that operated for this audit period was sold,
20 we're unable to obtain some of the old original purchase
21 orders from Lockheed. And due to the time frame, we were
22 not able to get from Lockheed when it was noted. It was
23 just noted in the recent time that it was a different
24 contract number. We had focused on the Lockheed Martin
25 information. So we weren't able to get from Lockheed the

1 purchase order that ties exactly to the Futuramic tools,
2 but this contract does tie to the JSF extension.

3 The Lockheed terms for the new contract number
4 are identical to the original contract where everyone has
5 agreed that the tools provided to Lockheed do pass to the
6 Government and are exempt. We believe that the Hitco
7 details for Lines 34,35, and 37, which are the three
8 Futuramic tool purchases, are sufficient to support the
9 tool should be treated consistently with the other tools
10 that were previously exempted by the CDTFA. And so those
11 are just the five tools that are left.

12 In all these cases my client erroneously reported
13 use tax on them. All of them have the same government
14 contract number and project numbers that they used within
15 Hitco, and so that ties. And those tie to the existing
16 ones that have already been agreed are exempt. And so,
17 you know, they're all government. They are audited by the
18 government in the Department of Defense. They are all for
19 the Joint Strike Fighter Program.

20 And so I think that the documents that we have
21 submitted should be relied on and are sufficient to
22 support that it was for the Joint Strike Fighter, and the
23 tools are resold to the U.S. Government prior to use and
24 should have be exempted. And, therefore, the refund we've
25 requested on the use tax accrued in error should be

1 allowed.

2 Okay. Our last issue from this Schedule is a,
3 what we call a Parpas machine. It was a very
4 sophisticated custom-made machine that was to be used in
5 manufacturing. It has a very long lead time, and Hitco
6 ordered it and started making progress payments on it long
7 before it was delivered. A decision was made that it was
8 no longer needed, and that they were going to resell the
9 machine. It was never placed in service. It was never
10 depreciated. It was delivered and then placed in a
11 storage facility. And immediately a contract was entered
12 into with a company to try -- a machine broker to try to
13 resell it and recapture as much of the money as they
14 possibly could.

15 We accrued use tax. We, as in Hitco, accrued use
16 tax on a couple of the early progress payments. So those
17 are included in the audit. Midway through they realize
18 they were doing that in error and stopped accruing the
19 tax. Ultimately, the machine was resold to a company
20 called the Avcorp. Tax was collected and remitted, and
21 that was in the subsequent audit. It took many years to
22 resell it. But keep in mind that during this period of
23 time was the Recession, and there wasn't much of a market
24 for this machine.

25 But Hitco never placed it in service. Did not

1 depreciate it. Our exhibit J-6, page 26 and 27 of 42,
2 support that the asset was held for sale as inventory.
3 And if you look at the Respondent's Exhibit C, pages 34 of
4 37, it's page 210 of the binder, the auditor verified the
5 above facts and agreed the Parpas machine transaction was
6 exempt from tax. They did not pick up the additional
7 payments in the audit, but they defined to refund the use
8 tax that was accrued in error on the early progress
9 payments.

10 We ask that the refund be issued on the progress
11 payments that were reported as subject to use tax as the
12 auditor did agree that the machine itself was held for
13 resale and did not pick up the subsequent payments; only
14 declined to issue the refund for the others.

15 That concludes my presentation on our points in
16 the six transactions that we still disagree with.

17 JUDGE GEARY: Thank you, Ms. Pass.

18 Let me ask my colleagues if they have any
19 questions of you now or prefer to wait until the
20 Department gives its presentation.

21 Judge Lambert, do you have any questions?

22 JUDGE LAMBERT: This is Judge Lambert. I don't
23 have any questions. Thanks.

24 JUDGE GEARY: Judge Long, do you have any
25 questions?

1 JUDGE LONG: This is Judge Long. My only
2 question is with regard to the Parpas machine, my
3 understanding is that it was sold for \$500,000, just about
4 \$1.2 million less than was paid. If no depreciation was
5 taken, what is the present account for the difference on
6 what was paid and, I guess, what the market value was at
7 the time of sale?

8 MS. PASS: What they did is they took an enormous
9 loss on the sale because there wasn't much of a market for
10 that type of machine. It was a custom-made machine that
11 was intended to be used in their manufacturing of carbon
12 graphite parts, and they ultimately did not need it. And
13 so they were finally able to sell it at half-a-million
14 dollars, but it took them years to find a buyer. There
15 was just not much of a market. And the loss was just
16 written off as a loss on the sale. And the accounting, I
17 believe, pages -- in J-6, 26 and 27 you see the accounting
18 treatment. And they just -- they did record it in the
19 income tax as a loss -- and in the books.

20 JUDGE LONG: Okay. Thank you. I don't have
21 anymore -- oh, this is Judge Long. I have no more
22 questions.

23 JUDGE GEARY: This is Judge Geary. Thank you,
24 Judge Long.

25 Mr. Noble, are you prepared to give your closing?

1 MR. NOBLE: Yes, sir. We're prepared. We're
2 ready.

3 JUDGE GEARY: You may go ahead.

4

5 PRESENTATION

6 MR. NOBLE: Okay. This is Jarrett Noble
7 presenting for CDTFA.

8 Appellant and manufacturer of carbon composite
9 materials filed a timely claim for refund for the period
10 January 1st, 2010, through December 31st, 2013, asserting
11 that it overpaid use tax measuring \$5,448,640.

12 The Department conducted an audit for the same
13 period, which resulted in an aggregate deficiency measure
14 of \$10,790,084. After several reaudits conducted by the
15 Department and concessions by Appellant, the amount in
16 dispute measures \$3,090,533 and consist of two separate
17 independent issues; whether title to tangible personal
18 property purchased by Appellant measuring \$1,142,733
19 passed to the U.S. Government prior to any use by
20 Appellant; and whether Appellant's purchase of a machine
21 from Parpas for \$1,947,800 is subject to use tax.

22 With respect to the first issue, Lockheed Martin
23 entered into a cost reimbursement supply contract with the
24 U.S. Government for construction of a Joint Strike Fighter
25 jet. Appellant in turn entered into a fixed-price

1 subcontract with Lockheed Martin to supply various carbon
2 composite components for the fighter jet. As part of the
3 subcontract, Appellant purchased special tooling and test
4 equipment that it used to produce the carbon composite
5 aircraft components. Appellant sold the special tooling
6 and test equipment identified in the contract and purchase
7 orders, along with the aircraft components to Lockheed
8 Martin.

9 Pursuant to Revenue & Taxation Code Section 6201
10 and 6401, use tax applies to the storage, use, or other
11 consumption of tangible personal property purchased from
12 any retailer for storage, use, and other consumption in
13 this state unless specifically exempted or excluded from
14 tax. Regulation 1614 provides that sales to the U.S.
15 Government are exempt from sales tax. And pursuant to
16 Regulation 1618, sales to the U.S. Government supply
17 contractors of tools, equipment, direct consumable
18 supplies, and overhead materials are nontaxable sales for
19 resale if the United States takes title to the property
20 pursuant to the U.S. Government supply contract prior to
21 any use of the property by the contractor in performing
22 the function or act for which the property was designed
23 and manufactured.

24 Generally, whether title passes to the United
25 States under a U.S. Government supply contract and the

1 time in which title passes, is determined in accordance
2 with the title provisions contained in the contract.
3 According to Regulation 1628 subdivision (b) (3) (d), unless
4 explicitly agreed that title passes at a prior time, a
5 sale occurs at the time and place in which the retailer
6 completes performance with reference to the physical
7 delivery of the property.

8 Lastly, a taxpayer seeking an exemption from tax
9 bears the burden of establishing that the requirements for
10 the exemption happened. And, likewise, a taxpayer who
11 claims a refund bears the burden of establishing that the
12 refund is warranted.

13 With one exception that I will discuss later, the
14 purchase invoices between Appellant and its vendors
15 identify a contract ending in 10. According to the master
16 purchase agreement between Appellant and Lockheed, which
17 is attached as Joint Exhibit 2, contract 10 was for LRIP 4
18 of the Joint Strike Fighter Program. In all of the master
19 purchase order covers LRIP 4 through LRIP 8. Initially
20 the Department determined that all of Appellant's
21 purchases of special tooling and test equipment were
22 subject to tax because there was no evidence that title to
23 the property passed to Lockheed and, consequently, to the
24 U.S. Government prior to any use by Appellant.

25 However, Appellant subsequently provided Appendix

1 T to the master purchase order between Appellant and
2 Lockheed, which is attached as Department's Exhibit A.
3 Based on the language of Appendix T, the Department
4 concluded the title to the property identified in the
5 documents passed to Lockheed and in turn, the U.S.
6 Government, upon Appellant's acquisition or manufacture of
7 the property, and prior to any use by Appellant, pursuant
8 to Regulation 1628.

9 The Department allowed all purchases as
10 nontaxable where the property identified in Appellant's
11 purchase invoices could be traced back to property
12 identified in the master purchase order, Attachment D to
13 the master purchase order, or the amended purchase order
14 with Lockheed Martin, based on the whether the property
15 had the same name as property in the Lockheed documents
16 and whether the price Appellant paid corresponded to the
17 price in those documents.

18 It was our impression that there were six
19 purchases remaining in dispute. For the three that relate
20 to the primary contract we thought that they were
21 Line Items 27, 29, and 32. So our presentation will
22 include those three. All these transactions are contained
23 in audit Schedule R1-12I. They remained in the audit
24 because the Department was unable to trace the property
25 identified in Appellant's purchase invoices in Joint

1 Exhibit 6, with special tooling and test equipment
2 identified in Appellant's master purchase order with
3 Lockheed, which is Joint Exhibit 2, the amended purchase
4 order with Lockheed, which is Joint Exhibit 3, or
5 Attachment D to the master purchase order, which is Joint
6 Exhibit 4.

7 In addition the Department notes that the price
8 Appellant paid for these purchases does not correspond
9 with any of the prices in the Lockheed documents. For
10 example, Line 29 shows a purchase of an STOVL strap trim
11 fixture for \$250,569. But none of the Lockheed documents
12 actually identified this particular property matching this
13 name or listed a corresponding price.

14 Accordingly, there's insufficient evidence to
15 conclude that these purchases were part of the special
16 tooling and test equipment identified in the Lockheed
17 documents. And thus, Appellant has failed to establish
18 the title of this property passes to the U.S. Government
19 prior to use.

20 With respect to the remaining three transactions,
21 which are Line Items 34, 35, and 37, the purchase invoices
22 reference a contract number between Lockheed and the
23 Government ending in 02, not 10. Unlike with contract 10,
24 Appellant has not provided a master purchase order with
25 Lockheed or attachments and appendixes to the purchase

1 order. While Appellant asserts that the contract ending
2 in 02 was an extension to the contract ending in 10, this
3 is not actually supported by the documents provided by
4 Appellant.

5 Rather, Appellant has provided one news article,
6 which states that the contract ending in 02 was modified
7 with increased funding, and another article which states
8 that the contract ending in 10 was also modified with
9 increased funding. Neither article states that one
10 contract was an extension of the other.

11 Furthermore, according to page 4 of Joint
12 Exhibit 9, the contract ending in 02 is for LRIP 9 of the
13 Joint Strike Fighter. However, as I previously stated,
14 the master purchase order only governs LRIP 4 through 8.
15 Thus, there is no evidence that the master purchase order
16 between Appellant and Lockheed, Appendix T, or the
17 documents identifying the special tooling and test
18 equipment to be transferred to Lockheed applies to these
19 three purchases.

20 Accordingly, Appellant has failed to provide any
21 evidence establishing the title to the property at issue
22 transferred to Lockheed, and in turn the U.S. Government,
23 prior to use. Therefore, these purchases are subject to
24 use tax. We further note that even if we were to accept
25 that these purchases were covered by the documents that

1 have been provided, the same issues that exist with the
2 other three purchases exist with these, that is that the
3 property identified in Appellant's purchase invoices for
4 these transactions, does not match any of the property
5 identified in the Lockheed documents, nor are there any
6 prices that correspond to the special tooling identified
7 in those documents.

8 As for Appellant's purchase of the machine from
9 Parpas, as previously noted, use tax applies to tangible
10 personal property that is purchased for storage, use, or
11 other consumption in this state. In addition, pursuant to
12 Section 6246, it is presumed that property shipped or
13 brought to this state by the purchaser was purchased for
14 storage, use, or other consumption in this state.

15 Lastly, Regulation 1701 provides that a retailer
16 who resells property prior to any use thereof, other than
17 retention for demonstration or display while holding it
18 for sale in the regular course of business, may take a
19 deduction for the purchase price of the property if they
20 have reimbursed the vendor for sales tax or the purchaser
21 has paid the use tax. Here the available evidence shows
22 that Appellant purchased this machine in the fourth
23 quarter of 2011 for approximately \$1,947,800.

24 There appears to be no dispute that the machine
25 was initially purchased for Appellant's own use in this

1 state and, thus, tax applied to the purchase. The only
2 evidence provided by Appellant on pages 26 and 27 of Joint
3 Exhibit 6 is an internal ledger showing that the machine
4 was being held for sale in December of 2014 for \$500,000,
5 approximately three years after the purchase. Given the
6 length of time between Appellant's purchase and the
7 subsequent journal entry showing the machine was held for
8 sale and the reduction in the sales price, Appellant has
9 not provided sufficient evidence establishing that the
10 machine was not used prior to being resold.

11 While Appellant claims that Parpas would not
12 cancel the sale, that the property was shipped to a
13 third-party warehouse where it remained until it was sold
14 by Appellant, and it did not make a taxable use of the
15 property, Appellant has not provided any evidence
16 supporting this chain of events; such as internal
17 documentation, or communication with Parpas, or documents
18 showing that the machine was actually resold.

19 In the absence of any evidence verifying
20 Appellant's assertions, it has failed to meet its burden
21 to show that the machine was not used in some way prior to
22 any sale and is not entitled to a refund for this
23 transaction. With respect to the audit comments that were
24 noted by Appellant, it's unclear whether those were the
25 auditor's statements or whether that was a recording of

1 the Appellant's assertions for why tax wouldn't apply.

2 However, I would note that audit Schedule R3-12 I
3 at Line 31 contains the auditor's comments for why the
4 refund was not approved. And it noted that there was a
5 lack of documentation concerning the use and the
6 subsequent resale of the Parpas machine.

7 For all the foregoing reasons, no further
8 adjustments are warranted, and this appeal should be
9 denied.

10 Thank you.

11 JUDGE GEARY: Thank you, Mr. Noble.

12 Let me just check with my colleagues.

13 Judge Lambert, do you have any questions?

14 JUDGE LAMBERT: I don't have any questions.
15 Thanks.

16 JUDGE GEARY: Thank you. Judge Geary again.

17 Judge Long, do you have any questions?

18 JUDGE LONG: This is Judge Long. No questions
19 from me. Thank you.

20 JUDGE GEARY: Thank you. Judge Geary, again.

21 Ms. Pass, would you like to give a closing
22 argument?

23 MS. PASS: I would, yes.

24 JUDGE GEARY: You may proceed when ready.
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1 audit but declined to issue the refund on the payments
2 that were made. And so we had inconsistent treatment
3 there.

4 But the comments are her comments because she did
5 not pick up the difference between the \$8.8 and the \$1.9.
6 While she declined to issue the refund, she also did not
7 assess on the remaining payments made for the Parpas
8 machine. And so those comments, if you read them in full,
9 are indicative that they are the auditor's comments and
10 not ours, and that she did see sufficient evidence that
11 the machine was not placed into use, and that the decision
12 was to resell it was prior to it being placed into use.

13 And, therefore, it was reasonably treated as
14 inventory and, therefore, not subject to use tax since
15 there was not storage for use. It was held for inventory
16 purposes and resale from the moment it was delivered. The
17 tax was accrued on progress payments before there was
18 actually a machine. Even delivered to the company,
19 because there was an accounting error on the accruals.

20 We believe going back to the Lockheed purchases,
21 I think we had submitted sufficient evidence that they are
22 all for the Joint Strike Fighter Program. I think it is
23 irrefutable that the Lockheed contract, the tools under
24 it, whichever version or number of steps because they were
25 continual purchases by the government in additions to this

1 contract over many years. And I believe they're still
2 producing the JSF plane or were until very, very recently.

3 I don't think there's any doubt that they all
4 went to Lockheed for the JSF program. The language in the
5 purchase orders that were provided as well as the invoices
6 are clear that they were for Lockheed Martin; and that our
7 internal contract, members and all are consistent with
8 that. And we believe that we have provided sufficient
9 documentation to support that they were sold to Lockheed
10 Martin and the Lockheed Martin contract for the JSF all
11 provide that Title 2, the tools go to the U.S. Government
12 prior to use. And, therefore, they weren't subject to use
13 tax for Hitco and that Hitco should not have reported use
14 tax on their purchases of the tools since they were resold
15 to Lockheed.

16 That concludes my rebuttal. I have nothing else
17 to add.

18 JUDGE GEARY: This is Judge Geary. Thank you,
19 Ms. Pass.

20 I'll turn it over to my co-panelists in a minute,
21 but I have at least one question for Mr. Noble. And that
22 has to do with the assertion that use tax was paid on only
23 fairly relatively small portion of the payments made for
24 the Parpas machine was not made -- use tax was not
25 self-assessed or paid with respect to the lion's share of

1 what Ms. Pass indicates was approximately an \$8 million
2 purchase. But does CDTFA acknowledge or agree that the
3 actual total purchase price of the machine was closer to
4 \$8 million dollars, and that there's been no claim by
5 CDTFA that use tax was due in connection with most of that
6 purchase price?

7 MR. NOBLE: To be honest, I was unaware that the
8 purchase price was \$8 million. It does appear that is
9 correct, that the Department did not pick up the remainder
10 of the tax there. That specific information about the
11 total purchase price wasn't explicit in the audit working
12 papers when I reviewed them.

13 JUDGE GEARY: Judge Geary, again. As a follow
14 up, can you be a bit more clear and tell me whether or not
15 Respondent concedes that the Appellant's contention about
16 the price actually paid for the machine and the relatively
17 small portion of which Respondent assess use tax on, do
18 you concede that those numbers are roughly accurate?

19 MR. NOBLE: I'm just thinking about the question.
20 One second.

21 JUDGE GEARY: This is Judge Geary, again. Let me
22 see if I can make it easier for you. Did Respondent
23 assess tax on only a small portion of the purchase price
24 of the Parpas machine?

25 MR. NOBLE: Judge Geary, this is Jarrett Noble

1 with CDTFA. We concede to your question. The numbers
2 appear to be approximately correct, yes.

3 JUDGE GEARY: And Judge Geary, again. Would the
4 Respondent's position or is the Respondent's position that
5 it simply, for whatever reason, neglected to collect the
6 tax that it should have, or assert the tax that it should
7 have, or is there some other position that it has with
8 respect to that difference?

9 MR. NOBLE: Fail to assert, yes.

10 JUDGE GEARY: Judge Geary speaking. Thank you.

11 Ms. Pass, I also have a question for you. And
12 I'm just actually requesting some clarification. You
13 indicated during your final closing that if you look at
14 some of the numbers in the schedule, you're contention is
15 that it is actually -- the number in the schedule actually
16 represents the cost of several, two or three of the items
17 combined. Is that what you said?

18 MS. PASS: Yeah. That's correct. It's that some
19 of those tools there may be multiple parts to a tool. And
20 that's maybe why the Department was having difficulty
21 tying it together, is that they had the mandrels and
22 things. It's that without a doubt, you can tie one of the
23 STOVL to middle of page 27 where that number is sufficient
24 to tie-back to one of the purchases.

25 And the remainder, if you look at the

1 descriptions and all, I think there are sufficient dollars
2 that it matches to an extent of the different purchases.
3 I don't think it's as difficult to tie the numbers when
4 you look at the individual ones.

5 JUDGE GEARY: Judge Geary, again. Can you give
6 us line numbers by any chance to -- of the lines that you
7 think represent those various items?

8 MS. PASS: Let's see. I'll look at my --
9 Line 29. And I do have a question. I had noted in our
10 prehearing conference from Mr. Noble that 27 was agreed
11 to, but today he had mentioned that it was still in the
12 audit. I was under the understanding that had been agreed
13 to at our prehearing that that was one of the transactions
14 that had been taken out.

15 JUDGE GEARY: Let me take a look at -- I don't
16 think that my prehearing conference order specified which
17 items, did it? I can look at it if you want.

18 MS. PASS: Yeah. I had -- I had made notes and
19 had crossed that one out that that had been agreed to.

20 JUDGE GEARY: Hold on. I'm going to take a
21 minute to look at that prehearing conference order.

22 This is Judge Geary. I looked at my prehearing
23 conference order. I don't indicate in that order what
24 specific line numbers are still in dispute. I recall,
25 generally, there was a discussion regarding the number of

1 line numbers.

2 Let me ask you this, Ms. Pass. Do you believe
3 that you have in some way been denied an opportunity to
4 argue with respect to the one item that you believe was
5 resolved and that Mr. Noble indicated was still in
6 dispute? Or do you believe you've been offered an
7 opportunity today to make the arguments that you wish to
8 make with respect to that item?

9 MS. PASS: I think I have. My argument for that
10 item is consistent with my arguments for the other five
11 items that they all belong to the Strike Fighter Program.
12 To respond to your earlier question, if you look at
13 Line 29, it was a \$250,569.50 tool, and there is an
14 invoice for STOVL trim for two. There are two of them for
15 \$286,791. And so amounts are reasonable. Our purchase
16 price is lower than what we are invoicing Lockheed, which
17 is what's to be expected. So one would expect that there
18 would a profit to be made from Hitco to Lockheed based on
19 the contract prices.

20 There are other parts where -- and keep in mind
21 that because of the nature of the purchase order, we have
22 things that are close in price. Some are going to be
23 higher. Some are going to be lower, depending on what it
24 cost at the time they ordered. Because when the purchase
25 orders were issued, we didn't necessarily know. We, as in

1 Hitco, did not necessarily know what it would cost them
2 and what the venders might charge them later. Because the
3 original contract was issued in 2009, and some of these
4 later tools were purchased in 2011.

5 And so you may have slight differences in amounts
6 where some may be above or below based on the contract and
7 what they felt they could get based on the timing. But we
8 were -- you know, we had a fixed price contract Lockheed,
9 and so we did not have the option to potentially bill
10 more, even if a price was slightly different. But there
11 are plenty of STOVL purchases, if you look at J-2, page 11
12 and 12 that are sufficient in dollars and close to match
13 what our tools were purchased here as well.

14 And so I think when you look at, you know, page
15 11 and 12 in the master contract, it is not that
16 difficult. I -- I did not go through and tie them to the
17 specific line items on the master purchase order, but the
18 amounts in the master purchase order are consistent. The
19 descriptions are consistent with the purchase orders in
20 our opinion.

21 JUDGE GEARY: Thank you. Judge Geary, again.
22 One last question, I think, for you Ms. Pass. Just again,
23 by way of clarification, are you saying that the reasons
24 the numbers in the schedules may not match the numbers
25 that are in the purchase orders is because the price of

1 the machine may have been changed or because the price
2 charged to the customer may have changed? The cost of the
3 equipment or the price charged to the customer?

4 MS. PASS: The price charged to the customer was
5 unchangeable under the terms of the contract. The price
6 we paid to our vendors may not have been consistent with
7 what we might have anticipated our purchase cost would be
8 when we bid it to Lockheed. And so that --

9 JUDGE GEARY: And it could be --

10 MS. PASS: -- can result in a difference between
11 we may have paid more to our vendor for certain parts, the
12 certain tools, than we were able to bill to Lockheed when
13 we resold it to Lockheed.

14 JUDGE GEARY: And it could be a higher number or
15 a lower number?

16 MS. PASS: Exactly.

17 JUDGE GEARY: Thank you. This is Judge Geary.
18 Thank you, Ms. Pass.

19 I'm going to turn it over to my colleagues.
20 Judge Lambert, do you have any questions?

21 JUDGE LAMBERT: This is Judge Lambert. I don't
22 have any questions. Thanks.

23 JUDGE GEARY: Thank you. Judge Geary between.
24 Judge Long, do you have any questions?

25 JUDGE LONG: This is Judge Long. I do not have

1 any questions. Thank you.

2 JUDGE GEARY: Thank you.

3 Bear with me a moment, please. Okay. Let me
4 just confirm then. This concludes our argument and should
5 conclude this hearing. Let me just confirm with the
6 parties.

7 Ms. Pass, you submit the matter for decision?

8 MS. PASS: Yes, I do.

9 JUDGE GEARY: Thank you.

10 And Mr. Noble, does CDTFA submit the matter for
11 decision?

12 MR. NOBLE: Yes, we do. Thanks.

13 JUDGE GEARY: Thank you. This case is submitted
14 on June 15th, 2021, at approximately 1:40 p.m. The record
15 is now closed.

16 I want to thank everyone for participating in
17 this hearing today. In the coming weeks the panel will
18 meet to consider the matter, and we will issue and send to
19 you a written opinion within 100 days.

20 I'm going to ask the court reporter to go off the
21 record now.

22 (Proceedings adjourned at 1:40 p.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
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I further certify that I am in no way interested
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I have hereunto subscribed my name this 2nd day
of July, 2021.

ERNALYN M. ALONZO
HEARING REPORTER