

BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF, )  
 )  
V TROPICAL BAKESHOP III, INC., ) OTA NO. 19125594  
VALERIO'S TROPICAL BAKESHOP VI, ) 19125596  
INC., )  
 )  
APPELLANT. )  
 )  
 )

## TRANSCRIPT OF ELECTRONIC PROCEEDINGS

State of California

Tuesday, January 25, 2022

Reported by:  
ERNALYN M. ALONZO  
HEARING REPORTER

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25

BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF, )  
)  
V TROPICAL BAKESHOP III, INC., ) OTA NO. 19125594  
VALERIO'S TROPICAL BAKESHOP VI, ) 19125596  
INC., )  
)  
)  
APPELLANT. )  
)  
\_\_\_\_\_ )

Transcript of Electronic Proceedings,  
taken in the State of California, commencing  
at 9:30 a.m. and concluding at 10:43 a.m. on  
Tuesday, January 25, 2022, reported by  
Ernalyn M. Alonzo, Hearing Reporter, in and  
for the State of California.

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25

APPEARANCES:

Panel Lead: ALJ JOSHUA ALDRICH

Panel Members: ALJ SUZANNE BROWN  
ALJ ANDREW KWEE

For the Appellant: GRAHAM HOAD

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

AMANDA JACOBS  
CARY HUXSOLL  
JASON PARKER

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25

I N D E X

E X H I B I T S

(Appellant's Exhibits 1-3 were received at page 8.)  
(Department's Exhibits A-R were received at page 8.)

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

	<u>PAGE</u>
By Mr. Hoad	9
By Ms. Jacobs	26

CLOSING STATEMENT

	<u>PAGE</u>
By Mr. Hoad	50

1 California; Tuesday, January 25, 2022

2 9:30 a.m.

3  
4 JUDGE ALDRICH: So this is Judge Aldrich. We are  
5 opening the record in the consolidated appeal of  
6 V Tropical III, Incorporated, and Valerio's Tropical  
7 Bakeshop VI, Incorporated, before the Office of Tax  
8 Appeals, OTA Case Number 19 -- or Case Numbers 19125594  
9 and 19125598. Today's date is Tuesday, January 25th,  
10 2022, and time is approximately 9:30. This hearing was  
11 duly noticed for a virtual hearing and with the agreement  
12 of the parties.

13 Today's hearing is being heard by a panel of  
14 three Administrative Law Judges. My name is  
15 Judge Aldrich. I'm the lead judge for purposes of  
16 conducting the hearing. At this point I'd like to ask my  
17 co-panelists to introduce themselves, beginning with  
18 Judge Brown.

19 JUDGE BROWN: Good morning. This is Judge Brown.

20 JUDGE ALDRICH: Thank you.

21 And Judge Kwee.

22 JUDGE KWEE: Hi. Good morning. This is  
23 Judge Kwee.

24 JUDGE ALDRICH: Great. During the hearing panel  
25 members may ask questions or otherwise participate to

1       ensure that we have all of the information needed to  
2       decide this appeal. After the conclusion of the hearing,  
3       we three will deliberate and decide the issues presented.  
4       As a reminder, the Office of Tax Appeals is not a court.  
5       It is an independent appeals body. The panel does not  
6       engage in ex parte communications with either party. Our  
7       opinion will be based on the parties' arguments and  
8       admitted evidence and relevant law. We have read the  
9       parties' submissions, and we are looking forward to  
10      hearing your arguments today.

11               For the Appellant we have representative Graham  
12      Hoad. Welcome.

13               For the Respondent, for the Department, we have  
14      Amanda Jacobs, Cary Huxsoll, and Jason Parker. Welcome.

15               Pursuant to our January 13th, 2022, minutes and  
16      orders of prehearing conference, the issues to be decided  
17      are: Whether Appellants have shown that their sales of  
18      hot meat-filled baked goods are exempt from sales tax;  
19      whether CDTFA timely issued the Notice of Determinations;  
20      and, whether relief from the failure-to-file penalty is  
21      warranted.

22               Mr. Hoad, is that correct?

23               MR. HOAD: Yeah. That accurately summarizes the  
24      issues.

25               JUDGE ALDRICH: Thank you.

1 Ms. Jacobs, this is correct?

2 MS. JACOBS: That's correct. Thank you.

3 JUDGE ALDRICH: Thank you.

4 In the minutes and orders, we noted under the  
5 notice section that it is undisputed that Appellants were  
6 not subject to the 80/80 rule, and we also noted that it  
7 is undisputed that there's no seating at either location.

8 Mr. Hoad, is that correct?

9 MR. HOAD: That's correct.

10 JUDGE ALDRICH: And Ms. Jacobs?

11 MS. JACOBS: That's correct.

12 JUDGE ALDRICH: Also we allowed Appellant to  
13 submit a CDTFA 735 or declaration to the same effect for  
14 the third issue, which we indicated by January 14th, 2022.  
15 We received a CDTFA 735 on January 17th, 2022, which was  
16 executed on January 11th, 2022, by Appellants' vice  
17 president.

18 Ms. Jacobs, do you have any objection to  
19 admitting the CDTFA 735 that Mr. Hoad provided?

20 I didn't hear you, but it looked like you were  
21 voicing no objection.

22 MS. JACOBS: No objection. Can you hear me?

23 JUDGE ALDRICH: Yup. Thank you.

24 Great. So that will be allowed. And next we'll  
25 discuss exhibits. So pursuant to our January 13th, 2022,

1 minutes and orders prehearing conference, we admitted  
2 ahead of time the hearing exhibits for Appellant. Those  
3 are Exhibits 1 through 3 and also for the Department,  
4 Exhibits A through R. Those were without objection and  
5 previously admitted.

6 (Appellant's Exhibits 1-3 were received  
7 in evidence by the Administrative Law Judge.)

8 (Department's Exhibits A-R were received in  
9 evidence by the Administrative Law Judge.)

10 Let's see. Does either party have additional  
11 exhibits that they would like for us to consider today?

12 Mr. Hoad?

13 MR. HOAD: No. I don't have any additional  
14 exhibits which need to be submitted.

15 JUDGE ALDRICH: Great. And then Department?

16 MS. JACOBS: No exhibits.

17 JUDGE ALDRICH: Great. So we plan for the  
18 hearing to proceed as follows. Appellants opening  
19 statement, which we estimated at 20 minutes, and then the  
20 Department will have a combined opening and closing for 20  
21 minutes, approximately a 10-minute period for questions  
22 from the panel, and 5 to 10 minutes for rebuttal or  
23 closing from Appellant. If you need more time, please  
24 ask.

25 But do either of the parties or their



1 representatives have any questions before we move on to  
2 opening statements?

3 No from either. Okay. So we're ready to proceed  
4 with your presentation, Mr. Hoad. And please begin when  
5 you're ready.

6

7 PRESENTATION

8 MR. HOAD: Okay. Thank you very much. Thank you  
9 all for joining us today for this Office of Tax Appeal  
10 hearing.

11 Valerio's Bakeshop III and Valerio's Bakeshop VI,  
12 Inc., dba Valerio's operates Filipino bakeshops offering a  
13 variety of ethnic goods in purely take-out form. Shop  
14 locations consist of a small retail storefront, unheated  
15 display cases, racks, and shelves upon which baked goods  
16 are offered for sale. Neither location offers tables and  
17 chairs, nor other seating facilities where patrons may  
18 consume goods purchased. No heat lamps or other devices  
19 are used to maintain the internal temperature of the baked  
20 goods until purchased, with the exception of a small  
21 portion of baked goods held in a small warming oven inside  
22 the store.

23 The baked goods include traditional non-meat  
24 items such as dinner rolls, pastries, and desserts, but  
25 also baked goods which include meat, such as pork and

1 chicken buns, empanadas, et cetera. Portion sizes range  
2 from two to five ounces and include about one to two  
3 ounces of meat filling.

4 Now, before I go on with my presentation, I would  
5 like to just go through the exhibits briefly and just give  
6 you an idea of what the Appellant is serving. If you can  
7 see the exhibit screen, these are chicken siopao and pork  
8 siopao. They are a Filipino bakery good. They're just a  
9 bun. You can see their net weight for 4 of them is 20  
10 ounces. So they are about 5 ounces with 1 to 2 ounces of  
11 meat. We also have a tuna and a chicken pandesal. Again,  
12 these are 5 ounces with a very small portion of meat. The  
13 corned beef pandesal and tuna pandesal are here. They're  
14 also about the same size, 5 ounces.

15 This is a -- on the left-hand side, we have just  
16 a regular pandesal. These are not filled with any type of  
17 meat or any type of filling. Cheese pandesal -- and then  
18 you can see the cheese pandesal is 20 ounces in a package,  
19 but there are 6 of them. So you can see they are a little  
20 bit less than 4 ounces. On the right-hand side we have  
21 two pandesals, which are identical to the tag. Anybody  
22 who is coming in, you can see from the outside they look  
23 identical. One has chicken. One does not.

24 You can guess which one, if you want to play a  
25 game or flip a coin. But the one on the left is the

1 chicken pandesal. And on the bottom on the right-hand  
2 picture is the inside of chicken pandesal versus the  
3 inside of the regular pandesal. And you can see the  
4 inside of the chicken pandesal. Again, these are very  
5 small. They're about maybe three inches in diameter.  
6 Again, cheese pandesal -- the inside of a cheese pandesal.  
7 This is an empanada. Again, it's very small. It's about  
8 three inches in diameter. It has a little bit of meat  
9 filling, one to two ounces. Pork siopao. You can see the  
10 inside of a pork siopao.

11 So these are baked goods. The only difference  
12 between what the Department considers to be an exempt  
13 baked goods and these baked goods is that they contain a  
14 small portion of meat. It's ethnically -- there are other  
15 ethnicities that put meat in their baked goods. It makes  
16 no difference to them whatsoever. It's still a snack.  
17 It's not a meal.

18 This is a picture of the outside of the Filipino  
19 bakeshop. It's just a bakeshop. They don't serve any --  
20 any kind of food other than baked goods. And we just have  
21 a variety of tuna, chicken pandesals -- and a pork meat  
22 pandesals. These are the items that are -- that the  
23 taxpayer sells -- the Appellant sells.

24 The second exhibit is the bottom of section 6359,  
25 and it refers to a case, Treasure Island Catering Company

1       versus State Board of Equalization. And the annotated  
2       portion of the case states that the sale of hot dog and  
3       hamburger sandwiches, even when served with beverages from  
4       sandwich stands or booths where neither chairs nor tables  
5       are provided for customers, does not constitute a meal  
6       within this section. A paper napkin is not tableware  
7       within this section, since the rule of ejusdem generis is  
8       applicable. I'm not going to get into the Latin  
9       definition of ejusdem generis because I could barely say  
10      it. But I'll leave it to you attorneys to -- to research  
11      that.

12               The third exhibit is the actual case of Treasure  
13      Island versus State Board of Equalization. And if you  
14      scroll down to approximately 5, one of the sections that I  
15      want to highlight is that the generally accepted concept  
16      of a meal is that it not only consist of a larger quantity  
17      of food than that which ordinarily comprises a single  
18      sandwich, but that it usually consists of a diversified  
19      selection of foods which would not be susceptible to  
20      consumption in the absence of at least some article of  
21      tableware, and which could not be conveniently consumed  
22      while standing -- while one was standing or walking about.

23               So we basically create a three-part test to  
24      determine what is a meal. It's a larger quantity of food.  
25      It usually consist of a diversified selection of foods

1       which would not be susceptible to consumption, the absence  
2       of at least some article of tableware, and it could not be  
3       conveniently consumed while one was standing or walking  
4       about.

5               So I think coming out of the gate, we can assume  
6       that these are not meals. They do not meet that  
7       three-part test of what is a meal. They can easily be  
8       consumed while standing or walking about. They don't need  
9       tableware. So the consumption of these under -- under  
10      Treasure Island, that these items of baked goods are not  
11      meals.

12             So one of the things that you're going to be  
13      asked to decide -- which I'll go over -- is, are these  
14      items, when they are served hot out of the warming oven,  
15      do they more -- are they more similar to hot prepared food  
16      products, which are taxable, or are they hot bakery goods,  
17      which are nontaxable. And the hot -- the examples that  
18      the CDTFA gives for hot prepared food products include  
19      sandwiches, pizza, barbecue chicken, soup, consommé,  
20      bouillon, steak, and so forth.

21             And so are these items the taxpayer sells more  
22      like these? Or are they more like bread, croissants,  
23      pastries, muffins, cookies, bagels, and the like. So this  
24      is really what we're deciding. Are these hot prepared  
25      food products, examples given here? Or are they hot

1 bakery goods, examples given here.

2 So now, I'm going to go into -- now, that we've  
3 covered that and, really, what we're talking about what  
4 the issues are, I'm going to go ahead and go into my  
5 written presentation. So the issue here is really whether  
6 the Department -- whether the petitioner appropriately  
7 relied on the Department's own guidance when he treated the  
8 sale of meat-filled hot bakery goods as exempt. So the  
9 Department -- or excuse me.

10 The petitioner relied on the following guidance.  
11 First, Regulation 1603, taxable sales of food products.  
12 Regulation 1603 discusses the application of tax to food  
13 products, specifically, paragraph E1 states -- and I want  
14 to read this into the record. Tax applies in the sale of  
15 all hot prepared food products, unless otherwise exempt.  
16 Prepared food items mean those items and components which  
17 have been prepared for the sale and heated condition and  
18 which is sold in a temperature which is higher than air  
19 temperature of the room or place where they are sold. The  
20 mere heating of a food product constitutes preparation of  
21 a hot prepared food product; example, grilling of  
22 sandwich, dipping a sandwich in a bun in hot gravy using  
23 infrared lights, steam tables, et cetera.

24 If the sale is intended to be of a hot food  
25 product, such sale is of a hot food product regardless of

1       cooling, which incidentally occurs. For example, a sale  
2       of a toasted sandwich intended to be sold in a heated  
3       condition when sold -- excuse me -- such as a fried ham  
4       sandwich on toast is a sale of a hot prepared food  
5       product, even though it may have cooled due to delay. On  
6       the other hand, a sale of a toasted sandwich which is not  
7       intended to be in a heated condition when sold, such as a  
8       cold tuna sandwich on toast, is not a sale of a hot  
9       prepared food product.

10               However, the regulation further states, tax does  
11       not apply to the sale for a separate price of bakery  
12       goods, beverages classed as food products, or cold or  
13       frozen food products. So bakery goods are not subject to  
14       tax when they are served hot. It's important to note that  
15       neither Regulation 1603 nor its corresponding Section 6359  
16       make any distinction between hot bakery goods containing  
17       meat and non-meat products.

18               Furthermore, neither the taxpayer nor the patrons  
19       make any distinction between not -- between meat and  
20       non-meat products. They're treated exactly the same when  
21       baked. They are offered for sale side by side in  
22       non-heated display cases, in refrigerated condition far  
23       below room temperature and in some cases, from self-served  
24       warming ovens. Nowhere in Regulation 1603 does it state  
25       that by adding meat to a hot-bakery good change its nature

1 to a hot prepared food product.

2 Petitioner is a bakery selling only bakery goods  
3 and the regulation carves out a specific exemption for hot  
4 bakery goods. Petitioner reasonably relied on Regulation  
5 1603 in determining that its sales met the definition of  
6 hot bakery goods and were, therefore, exempt.

7 Now, in addition, the second article, the  
8 guidance that petitioner relied on was Publication 22.  
9 And this is a publication that reversed the dining and  
10 beverage industry. Publication 22 states in part that  
11 to-go sales of hot prepared food products are taxable.  
12 See exception for hot bakery goods, for hot bakery items.  
13 And it goes on to list some examples. The food product is  
14 considered a hot-food product if it is in a heated --  
15 heated to a temperature above room temperature.

16 Examples of heating a product above room  
17 temperature include grilling a sandwich, dipping a  
18 sandwich in hot gravy, or using infrared lights, steam  
19 tables, or microwave ovens. Now, examples of hot prepared  
20 food products include -- and this is the slide I just  
21 showed you -- hot sandwiches, pizza, barbecue chicken,  
22 soup, consomme, bouillon, steak, and so forth. Food is  
23 considered hot even if it is cooled by the time of sale,  
24 and so it's intended to be sold as a hot-food item.

25 Exception, specifically stated in Publication 22,



1 sales of hot bakery goods are not taxable when sold to go  
2 unless they are sold as part of a combination package. So  
3 Publication 22 provides specific examples of hot prepared  
4 food products. However, none of the items listed remotely  
5 resembles a bakery good. Furthermore, no mention is made  
6 regarding a distinction between hot bakery goods and  
7 meat-filled bakery goods.

8 Publication interprets it -- excuse me.  
9 Publication 22 interprets Regulation 1603 but goes a step  
10 further by highlighting the one exception to the exempt  
11 sale of a hot bakery good, and that is when it is sold as  
12 part of a combination package. From the taxpayer's  
13 perspective based on the guidance in Publication 22, the  
14 intent of Regulation 1603 is clear. The only instance  
15 where a hot-bakery good is taxable is when it is sold as  
16 part of a combination package.

17 Had the Department intended for taxpayers to  
18 treat meat-filled hot bakery goods as taxable, they should  
19 have said so by adding "or they contain meat" to the  
20 language of Publication 22 or Regulation 1603. However,  
21 they did not. Thus, the Department incorrectly interprets  
22 its own guidance by concluding that hot bakery goods  
23 containing meat are by their nature not exempt hot bakery  
24 goods. So that's Publication 22.

25 The next guidance is the Audit Manual. Audit

1 Manual Section 811.30 states in part, sales of hot  
2 beverages, such as coffee, tea, cocoa, or cider are not  
3 taxable if sold for a separate price on a to-go basis.  
4 Similarly, bakery items such as bread, croissants,  
5 pastries, muffins, cookies, bagels, and the like, are also  
6 not taxable if sold on a to-go basis. Now first, the  
7 guidance provided by the Audit Manual further confirms the  
8 nontaxable status of hot bakery goods.

9 But it also includes the phrase, "and the like,"  
10 which without specifically excluding meat-filled items  
11 from the definition. So it includes "and the like," but  
12 it doesn't exclude meat-filled items from the definition.  
13 As mentioned previously, based on the Department's own  
14 guidance, there's no difference between a hot-bakery good  
15 containing meat and one without.

16 The next guidance is the annotations. Now,  
17 annotations don't have the force and effect of the law,  
18 but they do provide some guidance. This is Annotation  
19 550.1775. The Department relies on Annotation 550.1775  
20 and 550.1712 -- both have the same backup -- to compare  
21 the taxpayer's hot bakery goods to a Cornish pasty.

22 The annotation states, "Pasties. A pasty is not  
23 a bakery good within the meaning of Revenue & Taxation  
24 Code Section 6359(e). It is actually an entire meal  
25 compacted into a form more convenient than the ingredients

1 would be if sold as a conventional meal on a plate or  
2 cardboard tray. Therefore, sales of pasties in a heated  
3 condition constitute taxable sales of hot prepared food  
4 products under Regulation 1603(e) (1) ."

5 So the Annotation 550.1775 distinguishes a  
6 Cornish pasty from a hot-bakery good by noting that the  
7 Cornish pasty is actually an entire meal, and I just spoke  
8 about Treasure Island. We're going to go into that a  
9 little bit more. So let's talk about an entire meal.  
10 Section 6359 discusses a general exemption from the sales  
11 and use tax and, again, states the taxes do not apply to  
12 the sale for a separate price of bakery goods. At the  
13 bottom of the code section, the Department annotates the  
14 following court case, which is Treasure Island.

15 It states, "The sale of hot dog and hamburger  
16 sandwiches, even when served with beverages from sandwich  
17 stands or booths where neither chairs nor tables are  
18 provided for customers, does not constitute a meal within  
19 this section." A paper napkin is not tableware within  
20 this section, since the rule of ejusdem generis is  
21 applicable."

22 So as we noted before in the fact section, each  
23 baked good that we're presenting contains between one and  
24 two ounces of meat, but are otherwise indistinguishable  
25 from petitioner's non-meat filled goods. Furthermore, the

1 ingredients contained within the taxpayer's products would  
2 in no way be considered a meal if served as an entire  
3 portion of a conventional meal. As noted in 6359, the  
4 issue of whether a serving was considered an entire meal  
5 was litigated in Treasure Island versus the State Board of  
6 Equalization.

7 In that case, the taxpayer sold hot dogs and  
8 hamburger sandwiches during the Golden Gate Exposition.  
9 At issue was whether the hot dog and hamburger sandwiches  
10 constituted meals and were, therefore, subject to sales  
11 tax when sold. After July 1st of 1939 change in statute,  
12 the exemption for food products was not applicable to be  
13 meals served on or off the premises of the retailer. We  
14 went to a hot versus cold items interpretation or statute.

15 In its opinion, the court citing Samuel and  
16 Collins stated, as I mentioned before, the generally  
17 accepted concept of a meal is that it not only consists of  
18 a larger quantity of food than is ordinarily comprised --  
19 comprising a single sandwich, but that it usually consists  
20 of a diversified selection of foods which would not be  
21 susceptible to consumption in the absence of at least some  
22 sort of -- some article of tableware, and which could not  
23 be conveniently consumed while one was standing or walking  
24 about.

25 So there's, again, Treasure Island creates a

1 three-part test: A meal is a larger quantity; it's a  
2 diversified selection of foods requiring tableware, and  
3 it's not conveniently consumed while standing or walking  
4 about. Taxpayer's own items, as you can see from the  
5 exhibits, obviously do not meet those definitions. So the  
6 backup to Annotation 550.1775 states that the reason  
7 Cornish pasties are taxable is that they're more properly  
8 meals sold wrapped in a pastry and not the kind of item  
9 the law contemplated to be exempt as hot bakery goods.

10 First, taxpayer's bakery goods are not entire  
11 meals as contemplated by either Treasure Island or  
12 Annotation 550.1775. They do not contain a diversified --  
13 a diversity of ingredients that would ordinarily be  
14 recognized as conventional meals sold separately. And the  
15 portion sizes of the bakery good is not that which would  
16 ordinarily be considered an entire meal. Furthermore,  
17 hamburgers and hot dogs were not considered meals, even  
18 though they obviously contain meat.

19 Cornish pasties, on the other hand, are widely  
20 accepted as being an entire meal. They are generally  
21 served as a single portion meal on a plate with utensils  
22 and is often accompanied by a side of vegetables, et  
23 cetera. The portion sizes are more substantial than what  
24 the taxpayer sells, and they're generally advertised as a  
25 meal, not a bakery good. Taxpayer's baked goods, whether

1 meat filled or not, are generally eaten by hand.

2 So the Department's reliance on Annotation  
3 550.1775 to demonstrate that the taxpayer's hot-bakery  
4 item are meals and therefore taxable, is not supported by  
5 Treasure Island case. Furthermore, annotations are to be  
6 used as guidance only, and do not have the force and  
7 effect of law. To wit no taxpayer seeking guidance on the  
8 taxability of hot bakery goods would be reasonably  
9 expected to seek the guidance of the backup of an  
10 annotation and then draw the conclusion that its hot  
11 bakery goods were taxable because they were akin to  
12 Cornish pasties. This is an unreasonable burden on any  
13 taxpayer, and it's misguided in the first place.

14 So that concludes my presentation for the first  
15 item, which is the taxable ability of the hot bakery goods  
16 that contain meat.

17 The second issue is whether the applicable  
18 statute of limitations should extend beyond the normal  
19 statute of limitations for taxpayers who file returns  
20 would have. So in each equities tend for taxpayers, the  
21 taxpayers file returns would have. So in each report of  
22 field audit prepared by the Department, the penalty and  
23 statute comments state, and I quote for the penalty  
24 comment, "No penalty is recommended. Due to the  
25 technicality of Regulation 1603(e)(1), hot prepared food,

1 and the taxpayer interpretations/understanding of the  
2 regulation, the penalty for this audit period is being  
3 waived. No intentional negligence was noted. Penalty  
4 will be assessed in future audits if the same errors will  
5 be noted."

6 Under the statute of limitations comment they  
7 state, "Start of the audit period was back dated to  
8 7/01/07. Start of the business operation, taxpayer did  
9 not obtain a seller's permit until a scope team advised  
10 that there were -- that there are taxable items in the  
11 product line. Discovery date is 1/29/2014.

12 So as noted above, the taxpayer relied on the  
13 Department's own guidance in determining that its sales  
14 were not subject to tax. As result of the Department's  
15 misguided conclusion that the taxpayer's sales of hot  
16 bakery goods are taxable, the taxpayer was assessed tax  
17 for the extended tax statute of limitations under  
18 Section 6487, as well as a failure to file penalty.

19 In this audit an undue burden was placed on the  
20 taxpayer. First, by the Department's own admission, the  
21 technicality of Regulation 1603 and the taxpayer's  
22 reliance on the regulation created no basis for assessing  
23 a penalty. However, the taxpayer is not only being  
24 assessed a penalty in the form of a failure to file  
25 penalty, but it is also being assessed additional tax due

1 to the extended statute of limitations.

2 Had this taxpayer been required to hold a permit  
3 due to providing seating facilities, for example, the  
4 liability would be limited to the normal three-year  
5 statute, and the taxpayer would not have been assessed a  
6 failure to file penalty. To treat this taxpayer different  
7 than a bakery who holds a permit, or a restaurant, for  
8 example, is patently unfair and burdensome. In short, the  
9 Department admits that its regulation in its guidance is  
10 technical, and it says no penalty is recommended, yet  
11 assesses a penalty and an extended statute of limitations  
12 due to the taxpayer's reliance on the Department's own  
13 guidance.

14 Consequently, we believe that it is in the  
15 interest of fairness and uniformity that the taxpayer be  
16 afforded the benefit of a statute of limitations used for  
17 filing taxpayers, as well as relief from the penalty for a  
18 failure to file returns. In summary, taxpayer is a bakery  
19 selling baked goods. The Department's own guidance,  
20 including Section 6359, Regulation 1603, Publication 22,  
21 and even its own Audit Manual clearly state that hot  
22 bakery goods are exempt. Nowhere is there any guidance  
23 stating that hot bakery goods containing meat are taxable.

24 The Department replies on its own annotations,  
25 which do not have the force and effect of law to argue



1       that a meat-filled hot bakery item is taxable because a  
2       Cornish pasty is a meal. Yet, in their own annotated  
3       case, hot dogs and hamburgers are not meals because they  
4       are served in a napkin and not tableware, just as the  
5       petitioner's hot bakery goods, and despite containing  
6       meat. Due to its reliance on the Department's guidance,  
7       the taxpayer was also unfairly assessed a failure to file  
8       penalty as well as extended statute of limitation.

9               Guidance provided by the Department should be  
10      clear and unambiguous, and in this instance it is. Sales  
11      of hot bakery goods are exempt when sold for a single  
12      price. Consequently, we believe that the petitioner  
13      properly relied on the above guidance when he treated as  
14      exempt the sale of meat-filled hot bakery goods.

15             That concludes my opening statement. Thank you  
16      very much for your attention.

17             JUDGE ALDRICH: This is Judge Aldrich. Thank  
18      you, Mr. Hoad. Just as a notice that your second  
19      screen is still -- oh, it looks like you took care of  
20      that. Thank you very much.

21             So instead of going into questionings for the  
22      panel, I was going to transition to the Department for  
23      their presentation and defer the questions until after  
24      both parties have presented.

25             So, Ms. Jacobs, are you ready to proceed with

1 your opening and closing presentation?

2 MS. JACOBS: I am. Can you hear me?

3 JUDGE ALDRICH: I can hear you. Please proceed  
4 when you're ready.

5 MS. JACOBS: Great. Thank you.

6

7 PRESENTATION

8 MS. JACOBS: This is Amanda Jacobs from -- for  
9 the California Department of Tax and Fee Administration.

10 The Appellants in this case are related entities  
11 under common ownership and operate bakeries located in  
12 California. Each location is comprised of a small retail  
13 storefront containing warmers, refrigerators, and unheated  
14 display cases, racks, and shelves from which food products  
15 are offered for sale. Appellants sell baked goods for  
16 take-out or to-go orders, including some pastry and bread  
17 products filled with meat and vegetables directly from a  
18 heated appliance called a warmer. None of the locations  
19 offer seating facilities or allow food consumption on the  
20 premises.

21 As part of the statewide compliance outreach  
22 program or SCOP, Appellant v Tropical Bakeshop III was  
23 visited by Department staff on January 29th, 2014;  
24 Exhibits G and M. During this visit the SCOP team  
25 determined that the sales of Appellants' meat-filled

1     pastry and bread products were taxable. Appellants'  
2     management was advised to obtain a seller's permit, and  
3     both Appellants were issued a permit in August 2014.

4             However, Appellants disregarded the Department's  
5     advice and reported all sales as exempt. Appellants were  
6     each audited; V Tropical Bakeshop III for the period of  
7     July 1st, 2007, through December 31st, 2013, and Valerio's  
8     Tropical Bakeshop VI for the period of January 1st, 2010,  
9     through December 31st, 2014. Appellants were each  
10    reaudited as recommended by the appeals decision.

11            The issue in this appeal -- the issues in this  
12    appeal are whether Appellants are entitled to further  
13    adjustments to the audit liabilities for the period of  
14    July 1st, 2007, through December 31st, 2014, in the matter  
15    of V Tropical Bakeshop III, Incorporated, in  
16    January 1st, 2010, through December 31st, 2014, in the  
17    matter of Valerio's Tropical Bakeshop VI, Incorporated,  
18    with the respect to the following: One, whether  
19    Appellants have shown that their sales of meat-filled  
20    baked goods from a warmer are exempt from tax; two,  
21    whether the NODs were issued timely; and three, whether  
22    relief of the failure to file penalties are warranted.

23            The first issue is whether Appellants have shown  
24    that their sales of meat-filled baked sales goods from a  
25    warmer are exempt from tax. Alternatively stated, whether

1 Appellants' sale of meat-filled pastry and bread products  
2 from a warmer are sales of hot prepared food products are  
3 subject to tax. We confirm that they are.

4 As you know California imposes sales tax on a  
5 retailer's retail sales of tangible personal property in  
6 this state unless the sale is specifically exempt or  
7 excluded from taxation by statute, Revenue & Taxation Code  
8 6051. All of a retailer's gross receipts are presumed  
9 subject to tax unless the retailer can prove otherwise,  
10 Revenue & Taxation Code Section 6091. Sales tax generally  
11 does not apply to sales of food products for human  
12 consumption. That's Section 5359 subdivision (a).

13 However, sales tax does apply to sales of hot  
14 prepared food products whether served on or off the  
15 premises, Section 6359(d)(1) and (d)(7), and  
16 Regulation 1603(a)(2)(a). Hot prepared food product is  
17 defined as, quote, "Those products, items, or components  
18 that have been prepared for sale in a heated condition and  
19 are sold at any temperature that is higher than the air  
20 temperature of the room or place where they are sold," end  
21 quote.

22 The mere heating of a food product, such as by  
23 grilling or using infrared lights or steam tables, for  
24 example, constitutes preparation of a hot prepared food  
25 product. And if the sale is intended to be of a hot

1 prepared food product, such sale is of a hot prepared --  
2 is of a hot food product regardless of cooling which,  
3 incidentally, occurs, Regulation 1603(e)(1).

4 While sales of hot prepared food products are  
5 subject to tax, there is an exception for hot bakery goods  
6 sold at a separate price. As an exemption it must be  
7 narrowly construed, Revenue & Taxation Code Section 6359  
8 subdivision (e), and Regulation 1602 subdivision (a)(2)(a)  
9 and (e). It's been the consistent position of the  
10 Department that the sale of meat-filled pastry or bread  
11 products are not exempt sales of hot bakery goods.

12 Rather, it has been the Department's  
13 long-standing position that sales of items consisting of  
14 pastry or dough, filled with meat, and sold in a heated  
15 condition are taxable sales of hot prepared food products.  
16 For example, the 1995 sales and use tax Annotation  
17 550.1712 states that while a fruit or cream-filled  
18 croissant is a bakery good within the meaning of Section  
19 6359(e), a croissant filled with meat and cheese is not a  
20 bakery good, but is instead in more -- is more in the  
21 nature of a sandwich.

22 The backup letter further explains that, quote,  
23 "In determining if a filled item is a food product, the  
24 Department looks to the nature of the filling," end quote,  
25 and gives several examples of food items and the

1     taxability of their respective sale based on how they are  
2     filled, including the fruit or cream-filled croissants  
3     versus hot meat and cheese filled croissants and also  
4     Cornish pasty.

5             Annotation 550.1712 is consistent with the  
6     Department's position that Appellants' meat-filled pasty  
7     and bread, such as empanadas, siopao, and pandesal are  
8     taxable sales of hot prepared food products. As you know  
9     a retailer's gross receipts are presumed to be taxable  
10    until proven otherwise, and the burden is on the retailer  
11    to establish that its retail sales are not subject to tax.  
12    Statutes granting a tax exemption are strictly construed  
13    to avoid enlarging or extending the concession by beyond  
14    the plain meaning of the language used in granting it.  
15    See Associated Beverage Company versus Board of  
16    Equalization 1990 case.

17            Appellants bear the burden of showing they come  
18    within the terms of the exemption by a preponderance of  
19    the evidence. See Regulation 35003(a), and Paine versus  
20    State Board of Equalization, which is 137 cal.app.3d 438.  
21    Appellants take issue with Appeals Bureau's citation of  
22    Annotation 550.1775, which shares the same backup letter  
23    as Annotation 550.1712, and which the Department states  
24    that Cornish pasties, a traditional meat and vegetable  
25    filled pastry, is not a bakery good within the meaning of

1 Revenue & Taxation Code Section 6359(e) when sold in a  
2 heated condition, but it's actually an entire meal.

3 And sales of pasties in heated condition  
4 constitute taxable sales of hot prepared food products  
5 under Regulation 1630 -- 1603(e)(1). Appellants cite the  
6 1941 case, Treasure Island Catering Company versus State  
7 Board of Equalization, which was decided before the  
8 exclusion of hot prepared food products from the food  
9 products exemption, and the exception for hot bakery goods  
10 were added to Section 6359 in 1971. So Treasure Island  
11 was a 1941 case. Hot prepared food product was added to  
12 Section 6359 in 1971.

13 However, the fact that the annotation states that  
14 a Cornish pasty is a meal is not the dispositive  
15 distinction. There is no rule that an item must be a meal  
16 to be considered a hot prepared food product. The  
17 Department has consistently held that meat-filled pastries  
18 and bread products served warm are not exempt sales of hot  
19 bakery goods, but are taxable sales of hot prepared food  
20 products. The Department has been consistent in  
21 application of that standard dating back to at least 1995.

22 Appellants argue that the items at issue are  
23 exempt bakery goods, and the Department is incorrectly  
24 interpreting its own guidance. They cite to  
25 Publication 22 and the Audit Manual highlighting that they

1 do not make a distinction of meat-filled pastry in their  
2 mention of bakery goods. However, the evidence shows the  
3 Department has written guidance regarding its meat-filled  
4 pastry and bread products -- its position on meat-filled  
5 pastry and bread products. And it has been consistent in  
6 applying its position that the sale of meat-filled pastry  
7 or bread is not exempt -- is not an exempt sale of  
8 hot-bakery good. In fact, sales of such items are taxable  
9 sales of hot prepared food products under 6359(e) and  
10 Regulation 1603(e) (1) .

11 In sum, Appellants have not met their burden and  
12 proved by a preponderance of the evidence that the items  
13 at issue come within the terms of the hot-prepared -- of  
14 the hot -- come within the terms of the food products  
15 exemption simply by stating so. We reiterate that  
16 Appellants' sale of meat-filled pastry and bread products  
17 from a warmer are sales of hot prepared food product  
18 subject to tax pursuant to 6359 and Regulation 1603.

19 The next issue in this appeal is whether the  
20 Department issued Appellants timely Notices of  
21 Determination. The evidence shows that timely NODs were  
22 issued. According to Revenue & Taxation Code  
23 Section 6487, in the case of failure to file a return, a  
24 Notice of Determination must be mailed within eight years  
25 after the last day of the calendar month following the



1       quarterly period for which the amount is proposed to be  
2       determined, and in case the failure to make a return for  
3       taxpayer's filing returns on an annual basis within eight  
4       years after the last day of the calendar month following  
5       the one year period for which the amount is proposed to be  
6       determined.

7               The Department issued in October 20th, 2016, NOD  
8       to V Tropical for the period of July 1st, 2007, through  
9       December 31st, 2014, and issued a November 21st, 2016, NOD  
10       to Valerio's for the period of January 1st, 2010, through  
11       December 31st, 2014; Exhibit B. There's an eight-year  
12       statute of limitations period in which returns were not  
13       filed and not made in V Tropical executing a valid waiver  
14       of limitations for the period of January 1st, 2007,  
15       through December 31st, 2007; Exhibit F. The statute of  
16       limitations remained open until January 31st, 2017, for  
17       V tropical and April 30th, 2018, for Valerio's. The NODs  
18       were issued well within this time -- before this time.

19               Appellants argue that in the interest of fairness  
20       and uniformity, the statute of limitations should not  
21       extend beyond the three-years limitation period for  
22       taxpayers who file returns. Appellants reference comments  
23       in the revised audit reports, Exhibits J and N, which  
24       recommend against the imposition of the negligence penalty  
25       due to Appellants' misunderstanding and misinterpretation

1 of, quote, "The technicality of Regulation 1603(e)(10),"  
2 end quote, to reflect that they consider -- what they  
3 consider to be a unique burden placed on them.

4 However, there's no basis to reduce the statute  
5 of limitations for these particular taxpayers.  
6 Furthermore, applying Section 6487, which states the  
7 taxpayers in Appellants' situation are subject to an  
8 eight-year statute of limitations, ensures uniformity and  
9 fairness for all taxpayers. Also, any taxpayers uncertain  
10 of their reporting responsibilities are encouraged to  
11 request written advice from the Department regarding the  
12 application of tax to the tangible personal property they  
13 sell, which helps them avoid the risk of misinterpretation  
14 and misapplication of the law and exposure to potential  
15 tax liabilities.

16 The evidence shows that the Department issued  
17 Appellants timely Notices of Determination. As an  
18 administrative agency, OTA has no authority under the  
19 California Constitution to decline to enforce the clear  
20 and unambiguous provisions of the Revenue & Taxation Code  
21 Section 6487.

22 Finally, the last issue is whether relief of the  
23 failure to file penalties are warranted. We received  
24 Appellant's CDTFA or -- yes -- 735 on January 14th, 2022,  
25 and we relieved the penalties. The penalty amounts have

1       been adjusted off both V Tropical and Valerio's accounts  
2       as of the time of this hearing.

3               In summary, the sales of meat-filled pastry and  
4       bread products sold by Appellants from a warmer are  
5       taxable sales of hot prepared food products, and their  
6       sale is not exempt under Section 6359. Furthermore, the  
7       October 20th, 2016, NOD issued to V Tropical Bakeshop III  
8       and November 21st, 2016, NOD issued to Valerio's Tropical  
9       Bakeshop VI were timely.

10              Since Appellants have not otherwise disputed the  
11       audit methodology or audited measure, no adjustments to  
12       the Department's timely issued audit determinations are  
13       warranted. For these reasons, we request the appeal be  
14       denied.

15              Thank you.

16              JUDGE ALDRICH: This is Judge Aldrich. Thank  
17       you, Ms. Jacobs.

18              I'm going to refer to Judge Kwee. Did you have  
19       any questions for either party?

20              JUDGE KWEE: Hi. This is Judge Kwee. Yeah, I  
21       believe -- so just to make sure I'm understanding the  
22       issue that OTA is being asked to decide today. So,  
23       essentially, we have hot bakery goods sold for a separate  
24       price under Regulation 1603. Those can be, you know,  
25       nontaxable under certain elements if they're, you know,

1 sold to go, and the seller isn't meeting the 80/80 rule  
2 with things that are met here. And based on the decision  
3 of CDTFA and the annotations or annotation cited, if you  
4 add meats that basically drops it from being an excluded  
5 hot-bakery good and makes it into a hot prepared food  
6 product, which is taxable.

7 So, essentially, the issue that OTA is being  
8 asked to decide is whether adding the meat disqualifies it  
9 from being a hot-bakery good under that Regulation 1603  
10 and the applicable statute of 6359. Is that, essentially,  
11 the gist of what we are looking at, or is that as far as  
12 my understanding is that what the parties are also  
13 understanding what we're being asked to look at?

14 MR. HOAD: I'll go ahead. I believe what the  
15 Department is saying is that, yes, simply adding meat to a  
16 hot-bakery good that would otherwise be exempt somehow  
17 makes it a hot prepared food product.

18 If I can clarify something for a moment before we  
19 kind of get into that? I'd like to kind of rebut what the  
20 Department says just a little bit. If I can get maybe a  
21 couple of minutes, Judge Aldrich, is that acceptable to  
22 you.

23 JUDGE ALDRICH: Why don't you hold off on that  
24 for your rebuttal or closing argument, and then that way  
25 we can get through some questions and -- we'll certainly

1       give you time or an opportunity to make that rebuttal.

2               MR. HOAD:   Great.   Thank you.

3               JUDGE ALDRICH:   This is Judge Kwee.   So I guess I  
4       was going to go to my questions then.   So the first  
5       question -- and that was for Appellant -- is we had cited  
6       or you had cited to the Treasure Island case, which was  
7       interpreting, you know, the Retail Sales Act, which was  
8       the prior law.   And then now we have the sales and use tax  
9       law -- the current sales and use tax law.   So I was just  
10      to clarify, if I'm understanding the reasoning for citing  
11      the Treasure Island case, was that to get to the  
12      historical intent and to say that, you know, like, adding  
13      a meat product shouldn't it be something that's ex --  
14      causing it to be excluded from, I guess, qualifying as a  
15      bakery good.   Is that essentially why you're citing the  
16      Treasure Island case?   I'm just trying to understand what  
17      the --

18              MR. HOAD:   No.   No.   The reason I'm citing the  
19      Treasure Island case is because the backup to Annotation  
20      550.1712, which is what the Department is relying on, the  
21      backup to that annotation says that, "We determine" -- and  
22      this is quote -- "we determine at the time that such items  
23      were more properly," quote, unquote, "meals sold wrapped  
24      in a pastry, and not the kind of item the law  
25      contemplated."

1           So the back up to the annotation references that  
2     the reason Cornish pasties are taxable is because they are  
3     more appropriately meals. And, therefore, we have to look  
4     why did they -- where do they come up with the "it's more  
5     appropriately a meal and, therefore, taxable," the backup  
6     to that annotation, that language comes from the Treasure  
7     Island case. So the Department in the -- they're the ones  
8     that have referenced the Treasure Island case. So if you  
9     look to the back of -- if you look down below the -- as I  
10    mentioned, below the language of 6359, it references the  
11    Treasure Island case, which discusses whether a hamburger  
12    or hot dog sandwich is a meal.

13           So the reason we reference that is because the  
14    Department references it in their own case and says that a  
15    Cornish pasty is taxable because it is more properly a  
16    meal. So that's the Department's reference to that case,  
17    not mine. But I think it's appropriate.

18           JUDGE KWEE: Okay. I understand now. Thank you.  
19    And I did also want to clarify with you. So from my  
20    understanding, the way the Department determines the two  
21    bakeries' taxable sales of these type of pastry -- these  
22    types of products was they came up with some observation  
23    tests and the records, and then they came up with, like,  
24    6.3 percent for one bakery and, like, 8.19 for another  
25    bakery based on the observation tests, and I just wanted

1 to clarify. Does Appellant dispute, I guess, how much tax  
2 was calculated, like, the percentage that was coming up  
3 with, you know, because -- or is that something that  
4 you're disputing that the amount is accurate or not  
5 accurate?

6 MR. HOAD: I -- I don't have any way to gage.  
7 When the auditor went in and did the observation test,  
8 that's what he found at the observation test. Subsequent  
9 to those audits, the Appellant did remove the hot ovens,  
10 and there is the question as to -- as to what date those  
11 ovens were actually removed. We don't have actual  
12 documentation of that. So in the subsequent audits there  
13 may be issues that, you know, in -- like, for instance, I  
14 went into the one in Carson and there was no hot -- there  
15 was no self-serving warming oven, nor was there one in  
16 Concord or other Northern California locations.

17 So they removed those, but the only issue is what  
18 date they removed them. But other than that, I don't  
19 really have a problem with the auditor's methodology. I  
20 do believe that when he went in and counted the sales that  
21 came out of the warming oven that those were accurate, and  
22 then those were projected over the audit period.

23 JUDGE KWEE: Okay. Thank you. And I also had a  
24 question or clarification for CDTFA's rep. So, you know,  
25 during your presentation, you were citing CDTFA's

1       longstanding position that adding meat essentially means  
2       it's a hot prepared food product as opposed to a  
3       hot-bakery good. I know that the regulation uses the term  
4       hot-bakery good and hot prepared food product. I was just  
5       curious. Is there -- aside from the annotation, is there  
6       any authority in the regulation of statute which would  
7       specifically provide for drawing a distinction based on  
8       adding meat, or is that distinction based solely on, you  
9       know, the annotation that you have and maybe other  
10      published guidance but necessarily, you know, regulations  
11      or statutes?

12               MS. JACOBS: So -- hi. This is Amanda Jacobs for  
13      CDTFA. So the hot prepared food products in  
14      Section 6359(e) talks about hot -- like, hot sandwiches,  
15      hot pizza, things like that, with regard to hot prepared  
16      food products. And so that would be -- you know, we  
17      believe that our position is reflected in the statute.  
18      But as for other guidance, you know, there -- there's  
19      nothing that distinctly says, other than that annotation  
20      that I'm aware of, that says specifically meat, you know,  
21      that parses out meat. But it has been our longstanding  
22      position that the audit staff have used.

23               JUDGE KWEE: Okay. One other question. So I did  
24      notice that the statute says bakery goods, but the  
25      regulation says hot bakery goods may be exempt. I'm just



1       curious if you know the reason for it. You know,  
2       potentially the regulation seems to be more expansive  
3       there by allowing hot bakery goods to qualify. Do you  
4       know what the intent was in allowing that expansion?  
5       Because the statute says bakery goods, but then the  
6       regulation says -- the regulation says hot bakery good.  
7       Do you know why that was expanded to include hot bakery  
8       goods or the purpose behind that?

9               MS. JACOBS: Can you just give me a moment. I  
10       wanted to read it again quickly.

11              JUDGE KWEE: Okay.

12              MR. HUXSOLL: This is Cary Huxsoll for the  
13       Department. The -- are you -- I'm trying to follow the  
14       question in terms of your saying -- 6359(e) specifically  
15       says that if paragraph 7 of subdivision (d) does not apply  
16       to sale for a separate price of bakery goods or beverages,  
17       and that's referring to hot prepared food products. So  
18       the regulation talks about the sale of hot prepared food  
19       products for a separate price not being subject to tax.

20              Cold prepared food products would not be subject  
21       to tax for a separate price because it's a sale of a food  
22       product pursuant to regulation -- pursuant to  
23       Section 6359. There would not be another basis for taxing  
24       that. It would be just a cold food product taxed in the  
25       same way as other cold food products.

1           JUDGE KWEE: Right. Yeah. I was just looking at  
2 the language in 6359 which says, you know, paragraph 7  
3 subdivision (d) does not apply to the sale or a separate  
4 price of bakery goods or beverages. And 1603(e) it says  
5 hot bakery goods, and I am -- my understanding was that  
6 that was how you had that annotation, which was doing --  
7 distinguishing, like, if you heated, you know, jelly, then  
8 that would be exempt, but if you heated meat, you're  
9 saying it's not exempt.

10           And I was just wondering if the history would  
11 have -- the regulation history and adding the word hot  
12 before bakery goods in the regulation, since that word  
13 isn't in the statute, might have potentially included some  
14 guidances on -- on what was intended to be covered and --  
15 or specifically potentially excluded like meat. If you  
16 don't have that, that's fine. I was just curious what  
17 the -- if there was any history there that might have  
18 clarified the intent.

19           MR. HUXSOLL: I do not have the specific history.  
20 I just have the connection to the language of the statute.  
21 My understanding that that was why that was used, but I'm  
22 not -- I don't have any further information as to that.

23           JUDGE KWEE: Okay. Thank you. So I think that  
24 was everything that -- oh, I -- I'm sorry. I'm kind of  
25 hogging the screen here. I did have one last question for

1 Appellant, and this was in connection with the request for  
2 relief of the penalty form. So I saw you submitted that  
3 request for relief after the prehearing conference. And  
4 then during today's hearing you were also mentioning that,  
5 you know, they imposed the penalty but then you were  
6 relying on guidance by CDTFA. So, I guess, were you  
7 requesting relief of the failure to file penalty also on,  
8 I guess, a misunderstanding of the law or reliance on the  
9 available guidance by CDTFA? Is that what you were  
10 saying?

11 MR. HOAD: My understanding is that based on what  
12 the Department just mentioned that they have since deleted  
13 the failure to file penalty, so that issue is now moot.

14 JUDGE KWEE: Okay. I'm sorry. Okay. I got it.  
15 Thank you. Then I don't have any other questions. I'll  
16 turn it back to Judge Aldrich.

17 JUDGE ALDRICH: Hi. This is Judge Aldrich.  
18 Judge Brown, did you have any questions for either party?

19 JUDGE BROWN: This is Judge Brown. I'll try to  
20 be brief. I have a question for Appellants. I'm just  
21 wondering about the issue of the measure of use tax for  
22 fixed assets, which I know is not in dispute in this  
23 hearing. But I'm wondering how that fits in with the  
24 statute of limitations issues.

25 MR. HOAD: So the Appellant was unable to provide

1 records for the purchase of fixed assets that were beyond  
2 the regular -- the normal statute of limitations. So in  
3 the periods that were -- let's call it prior to the Notice  
4 of Determination date -- four to eight years prior to the  
5 Notice of Determination date, they were unable to provide  
6 records. So if the statute of limitations is revised down  
7 to three years, then those purchases of fixed assets will  
8 be beyond the statute of limitations.

9 I would note Section 1698 records does mention  
10 how long the records should be kept, and I believe it says  
11 four years. I'm looking at it briefly, but I don't think  
12 I can find it while I'm talking to you. But -- but they  
13 recommend the taxpayer keep records for four years,  
14 obviously, the extended statute of limitations would  
15 require. And the support that the fixed assets were tax  
16 paid at the source would require the taxpayer to keep  
17 records beyond that recommended period pursuant to  
18 Regulation 1698.

19 So if the statute of limitations is reduced to  
20 the normal three-year statute, then those items would fall  
21 off, and that is generally why. But other than that, we  
22 don't have any support for the purchase of fixed assets  
23 because they were, you know, five, six, seven, eight years  
24 prior, and the taxpayer got rid of their own -- got rid of  
25 those records.

1 JUDGE BROWN: I guess then -- this is  
2 Judge Brown. I understand your position about why  
3 Appellants didn't dispute the purchase of fix assets. I  
4 guess I'm wondering the flip side is if we -- I'm just  
5 wondering if the existence of the issue about the purchase  
6 of fixed assets means that effects the analysis of whether  
7 the NODs were timely. I guess what I'm thinking about is  
8 if the taxpayers had to file, theoretically, because of  
9 they had this purchase of fixed assets issue. It would  
10 really, I guess, go to the failure to file penalty that  
11 they had if they had theoretically had this obligation.  
12 But since we just heard the failure to file penalty has  
13 been relieved, maybe it's not at issue. Sorry. I guess I  
14 kind of answered my own question.

15 MR. HOAD: Yeah. So -- so if this was a  
16 restaurant, let's see they had a little -- like, you go to  
17 Cheesecake Factory, and there's a restaurant. And they  
18 have a little bakery good, you know, that sells cheesecake  
19 on the side. And those cheesecakes are -- let's just say  
20 they're hot bakery goods. If Cheesecake Factory got  
21 audited, then they get -- they have to pay the tax, and  
22 the Department said, oh, you have meat filled hot bakery  
23 goods. They are subject to tax. Then they would pay the  
24 tax for the past three years. There would be no failure  
25 to file.

1           But because this is a bakery selling hot baked  
2 goods, and they're not required to hold a permit under the  
3 law, when they -- when the Department comes in and tells  
4 them that their meat filled hot bakery goods are subject  
5 to tax, now they have an extended statute of limitations.  
6 So they're not being treated the same as a Cheesecake  
7 Factory that is required to hold a permit because they  
8 also own a restaurant. That's my point. They're not  
9 being treated the same.

10           So all I'm asking is that there be consistent  
11 uniform treatment between this taxpayer and a taxpayer  
12 that, say, held a permit because either they provided  
13 seating facilities, or they own a restaurant, or they sold  
14 a bunch of other taxable stuff; hamburgers. Hot dogs. Et  
15 cetera. So that's -- that's the point. We just want  
16 uniformity among all taxpayers. This taxpayer is being  
17 unfairly treated because they're being subject to the  
18 extended statute of limitations.

19           JUDGE BROWN: Let me move on to another question  
20 for Appellant. I'll just clarify that we understand that  
21 Revenue & Taxation Code Section 6596 is not at issue here.  
22 You're not -- which is a, you know, a separate thing  
23 because the taxpayer didn't -- the Appellants didn't --  
24 don't meet the facts of that they've formally requested a  
25 written opinion on these facts. But Appellants are still

1     arguing reliance, and I'm just wondering what the legal  
2     theory is here.

3             MR. HOAD:   We -- we're arguing reliance on the  
4     guidance which is in the form of the regulation, the Audit  
5     Manual, the publications, and the annotation.  We are not  
6     arguing reliance on written advice issued by the Board --

7             JUDGE BROWN:  Right.

8             MR. HOAD:   -- under Section 6596.  If I had  
9     intended for that to be our argument, I would have  
10    specifically stated we are relying on written advice  
11    issued by the Board under regulation -- under Section  
12    6596.  That is not the case.  It's a matter of semantics  
13    perhaps.  We are relying on guidance such as 6359,  
14    Regulation 1603, the Audit Manual, and the annotation.  
15    That is the guidance.  I'm not arguing reliance on written  
16    advice under 6596.

17            JUDGE BROWN:  This is Judge Brown.  I understand  
18    that.  What I'm saying is what's the legal theory that  
19    would allow us to -- that would allow OTA to say that  
20    reliance on, say, CDTFA's publication is the basis for  
21    finding that these sales were exempt.

22            MR. HOAD:   Well, I mean, if you're a -- if you're  
23    a -- if you go into business and you're selling a widget,  
24    how are you supposed to know whether to charge tax on that  
25    widget.  You go, and you look at the law.  Are widgets

1     subject to tax? You go to the regulation, Regulation 1603  
2     interprets 6359. Is a widget subject to tax? No, it's  
3     not. You go to the annotation. Is a widget subject to  
4     tax? No. Pasties are subject to tax, and ham and cheese  
5     croissants are subject to tax. But we don't -- we don't  
6     sell those. We sell widgets, and it doesn't say widgets  
7     are subject to tax.

8             You go to the Audit Manual. The Audit Manual  
9     doesn't say that widgets are subject to tax. So what's a  
10    taxpayer supposed to do? Nowhere in the Regulations, the  
11    code, the section, the Audit Manual, the annotations does  
12    it say that widgets are subject to tax. So I'm going to  
13    assume that my widgets are exempt. What -- I don't -- I  
14    guess other than that, I don't really understand the  
15    question.

16            JUDGE BROWN: This is Judge Brown. That's okay.  
17    I think I don't have any more questions at this time.  
18    Thank you.

19            MR. HOAD: Thank you.

20            JUDGE ALDRICH: Hi. This is Judge Aldrich. I  
21    have a question for the Department regarding the Cornish  
22    pasty. Would it matter if it were, say, a micro-Cornish  
23    pasty, a normal Cornish pasty, or a really large Cornish  
24    pasty as far as whether or not it would -- it's excluded  
25    from the exemption?



1 MS. JACOBS: No. What matters is whether or not  
2 it is filled with meat and sold in a heated condition.

3 JUDGE ALDRICH: Okay. And then so in a similar  
4 line, does a mere peppercorn of meat turn the hot bakery  
5 item into -- excluded from the exemption?

6 MR. HUXSOLL: This is Cary Huxsoll. It -- just a  
7 minimal amount of meat? Well, it's -- that's not before  
8 us with respect to these products. These products are  
9 similar to the ham and cheese croissants cited in  
10 550.1712, which the Department found was in the nature of  
11 something more similar to a sandwich and not a hot -- a  
12 hot bakery good, and these products would be treated in  
13 the same manner.

14 As to your example of, say, doughnut with a  
15 slight amount of bacon garnish, that's -- that's not  
16 before us right now. The issue is these products, and  
17 they should be treated the same way as the ham and cheese  
18 croissant in the annotation. And that's consistent with  
19 the Department's position for at least the last 27 years.

20 JUDGE ALDRICH: Thank you.

21 So Mr. Hoad, I believe you had wanted to do a  
22 rebuttal or closing. I wanted to extend that opportunity  
23 to you. Are you ready for that, or would you need --

24 MR. HOAD: Yes. Yes, I am. Thank you.

25 JUDGE ALDRICH: Okay.

- 1
- 2
- 3
- 4
- 5
- 6
- 7
- 8
- 9
- 10
- 11
- 12
- 13
- 14
- 15
- 16
- 17
- 18
- 19
- 20
- 21
- 22
- 23
- 24
- 25

2

3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13

14  
15  
16  
17  
18  
19  
20  
21  
22

23

24

25

1       So it doesn't -- that's not dispositive.  Furthermore,  
2       this discusses ham and cheese croissants and Cornish  
3       pasties.  The taxpayer does not sell a ham and cheese  
4       croissant, nor do they sell a Cornish pasty.

5               The issue of whether a Cornish pasty is taxable  
6       because it's more like a ham and cheese croissant has to  
7       do with whether it's an entire meal, which we've already  
8       discussed that whether it's a meal or not has to do with a  
9       three-part test.  It's a larger quantity, therefore, your  
10      previous question, would it matter?  Yes.  Under Treasure  
11      Island under this case, it would matter if it's a larger  
12      quantity because Treasure Island tells you that if it's a  
13      larger quantity it's a meal.  And ours are smaller  
14      quantities.  They're not meals.

15             Furthermore, they talk about this ham and cheese  
16      croissant sandwich.  We know nothing of this ham and  
17      cheese croissant sandwich.  We don't know whether it  
18      includes other ingredients such as lettuce, tomatoes,  
19      mayonnaise; whether the taxpayer that sold this ham and  
20      cheese croissant sandwich was a restaurant or actually a  
21      bakery.  We don't know whether this ham and cheese  
22      croissant sandwich was listed on the menu as an appetizer  
23      item, or whether it was listed as entre item or a meal.

24             We know nothing of this -- of these items that  
25      the taxpayer is -- or that the Department is saying are

1 taxable and, therefore, the Appellants' bakery goods are  
2 taxable. So -- and, furthermore, annotations have the  
3 force -- do not have the force and effect of law. This is  
4 merely guidance. I think this backup to the annotation is  
5 wrong. I think it's bad. It's a bad annotation. It's  
6 poorly written. It explains a situation where the nature  
7 of the filling is -- makes the item taxable. But that's  
8 because the filling is a non-food item.

9 If you put a non-food item in a food item,  
10 obviously it becomes a non-food item. Alcohol is taxable  
11 as a non-food item. So I still -- I -- I don't understand  
12 when the Department says it's been their longstanding  
13 position. They're relying on an annotation which has  
14 patently wrong information on it. It's a bad annotation.  
15 And when you look at the regulation, the statute, the  
16 Audit Manual, the publication, all of these say that hot  
17 bakery goods are not subject to tax. The taxpayer doesn't  
18 sell any of the items listed in the annotation that the  
19 Department is relying on. And they cannot provide one  
20 example, other than this annotation, that hot bakery goods  
21 that contain meat are subject to tax.

22 That concludes my presentation for my follow up.

23 JUDGE ALDRICH: Thank you.

24 This is Judge Aldrich. I just wanted to reach  
25 out to my panel to see if they had any follow-up questions

1 before we conclude.

2 Judge Brown, did you have any questions?

3 JUDGE BROWN: This is Judge Brown. I don't think  
4 so. No.

5 JUDGE ALDRICH: Okay. And, Judge Kwee, did you  
6 have any follow-up questions?

7 JUDGE KWEE: This is Judge Kwee. I guess maybe  
8 just a quick question for CDTFA, since there was a lot of  
9 discussion about the Treasure Island case and the  
10 annotation, the backup annotation. I just -- does the  
11 CDTFA want to offer a position on, you know, the relevance  
12 of an annotation and the difference between annotation and  
13 the backup annotation, or to what extent that OTA would --  
14 should -- or would give difference to either an annotation  
15 or a backup to the annotation?

16 MS. JACOBS: This is Amanda Jacobs for CDTFA.  
17 I -- it's known that annotations don't have the force and  
18 effect of law, but it is -- it's also known that  
19 annotations are used by the -- I mean, the Department's  
20 position can be found in annotation, and we don't --  
21 again, that annotation which is discussing this sales and  
22 use tax law and Section 6359, which was added in 1971, we  
23 don't believe that the Treasure Island case would apply to  
24 it, as Treasure Island was decided in 1941 in relationship  
25 to a different -- to the retail sales tax.

1           I don't know if Cary wants to add anything  
2 further, but --

3           MR. HUXSOLL: This is Cary Huxsoll for the  
4 Department. The annotations are entitled to great weight,  
5 and to the Department longstanding interpretation with the  
6 Department. So your entitled to great weight, and they're  
7 construing a statute that the Department administers, and  
8 it's a longstanding interpretation by the Department. And  
9 so they are entitled to great weight by OTA. They don't  
10 have the full force and effect of law, but they are to be  
11 given that weight.

12           As to the backup letter versus the actual  
13 annotation, in this particular case, the annotation itself  
14 is clear that it contains the same language that the  
15 Department relied on in the backup letter as far as  
16 550.1712. And so there does not need to be a distinction  
17 made between what the language is in the backup letter for  
18 that and the annotation itself. And I would just note  
19 that -- that we look to the language of 5503.1712 for the  
20 guidance in this case, and that's been our position since  
21 dating back to at least 1995 for similar products to the  
22 ones sold by Appellants.

23           Because in that case, it was a filled ham and  
24 cheese croissants. In this case, it's -- it's dough  
25 filled with meat and cheese. The Department has taken a

1       longstanding position that that was similar vein to a  
2       sandwich, and that product is similar to ones that the  
3       Appellant is selling. And so we rely on that annotation.  
4       And like I said, it's entitled to great weight as  
5       longstanding interpretation by CDTFA.

6               JUDGE KWEE: Thank you.

7               I didn't have any further questions. I turn it  
8       back to Judge Aldrich.

9               JUDGE ALDRICH: Hi. This is Judge Aldrich.  
10       Mr. Hoad, I'd like to give you the last word. And so if  
11       there's anything else you would like to add, please go  
12       ahead.

13              MR. HOAD: I think the only thing I would look to  
14       add is, again, the Department has no other, you know,  
15       they -- they mention 1971 as the date the statute changed  
16       to hot bakery -- to hot food items. If they wanted to add  
17       language that says that hot bakery goods that contain meat  
18       are subject to tax or excluded from the exclusion or  
19       exemption for hot bakery goods, they've had well over  
20       50 years to incorporate that into 6359, 1603, Publication  
21       22, to revise the annotation. Nowhere do they do that.  
22       They've had 50 -- well over 50 years to do that. They  
23       haven't done it because it's not what the intent of the  
24       law is.

25              My -- Appellant does not sell ham and cheese

1 croissants. They do not sell Cornish pasties. And there  
2 is enough ambiguity in this annotation and the backup  
3 to -- to allow an appellant to not have to rely on this  
4 annotation when determining whether their items are  
5 subject to tax.

6 It's been a long-held standing that hot bakery  
7 goods are not subject to tax. The taxpayer is a bakery.  
8 They sell hot bakery goods. That's all they sell.  
9 Whether a bakery good has meat in it or not does not  
10 change the definition of a hot bakery good to a hot  
11 prepared food product under the law, the regulation, the  
12 annotations, or the publications.

13 So we believe that we are in the right. We  
14 believe the taxpayers properly relied on the Department's  
15 guidance, and that they should not be held responsible for  
16 tax on the sale of hot bakery goods that for all intents  
17 and purposes under the law are exempt.

18 Thank you.

19 JUDGE ALDRICH: This is Judge Aldrich. Thank  
20 you.

21 Thank you everyone for your time and for being  
22 flexible with the hearing format. We're ready to conclude  
23 the hearing, and the record is closed.

24 The panel will meet and decide the case based on  
25 the evidence and arguments presented today. We will send



1 both parties our written decision no later than 100 days  
2 from today.

3 And while this hearing has concluded, there are  
4 more hearings today. The hearing calendar will resume at  
5 approximately 1:00 p.m. this afternoon. Thank you  
6 everyone.

7 (Proceedings adjourned at 10:43 a.m.)

8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25

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 7th day  
of February, 2022.

---

ERNALYN M. ALONZO  
HEARING REPORTER