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APPEARANCES:

Panel Lead: ALJ DANIEL CHO

Panel Members: ALJ MICHAEL GEARY
ALJ ANDREW WONG

For the Appellant: ANTHONY MANDELLA

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

NALAN SAMARAWICKREMA
RANDY SUAZO
CHRISTOPHER BROOKS

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I N D E X

E X H I B I T S

(Appellant's Exhibits 1-4 were received at page 6.)
(Department's Exhibits A-F were received at page 6)

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California; Tuesday, April 12, 2022

9:32 a.m.

JUDGE CHO: All right. Let's go on the record. This is the Appeal of PMR Enterprises, LLC, OTA Case Number 19014244. Today is April 12th, 2022, and the time is approximately 9:32 a.m. We're holding this hearing in person and live in Cerritos, California.

My name is Daniel Cho, and I'm the lead Administrative Law Judge for this appeal. With me are Administrative Law Judges Andrew Wong and Michael Geary.

Can the parties please identify yourself by stating your name for the record, beginning with Appellant.

MR. MANDELLA: Anthony Mandella, representing PMR Enterprises.

JUDGE CHO: Thank you, Mr. Mandella. Department?

MR. SAMARAWICKREMA: Nalan Samarawickrema, Hearing Representative for the Department.

MR. SUAZO: Randy Suazo, Hearing Representative, CDTFA.

MR. BROOKS: Christopher Brooks, Tax Counsel for CDTFA.

JUDGE CHO: Thank you.

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

3 With respect to the evidentiary record, the
4 Department has provided Exhibits A through F, and
5 Appellant has not objected to these exhibits. And
6 Appellant has provided Exhibits 1 through 4. The
7 Department has not objected to those exhibits. Therefore,
8 all the exhibits will be admitted into the record.

9 (Appellant's Exhibits 1-4 were received
10 in evidence by the Administrative Law Judge.)

11 (Department's Exhibits A-F were received in
12 evidence by the Administrative Law Judge.)

13 As we discussed at the prehearing conference,
14 Appellant, you will be given 20 minutes to provide your
15 testimony and presentation. Afterwards Department will be
16 given 20 minutes, and Appellant will be given 5 minutes on
17 rebuttal.

18 So before we begin with your presentation,
19 Mr. Mandella, I will swear you in in accordance with the
20 Office of Tax Appeals rules and regulations so that we can
21 take your statements as evidence.

22 Would you please raise your right hand.

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ANTHONY MANDELLA,

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

JUDGE CHO: Thank you. You can begin your presentation when you're ready.

PRESENTATION

MR. MANDELLA: Okay. I'll start off by saying that it's been a long process, number one. I think it's getting close to eight years on the date because my daughter is almost at that point, and it started before she was around.

So starting with the initial process, the original auditor had come into my home office and did the audit. Everything was going fairly smoothly. As we got into it, more details and everything, I had a better understanding of what you guys were looking for and different things. So I definitely learned a lot through the process, not just for an audit but, you know, conducting business moving forward and such.

There was a lot of miscommunications going back and forth, which is what led to a lot of this drawn-out process. Partially, in my opinion, to blame on the

1 auditor that was doing it, and also on the supervisor at
2 the time. My first exhibit gets into that, which is the
3 email chains. Just it was an example of some of the back
4 and forth that we had. I tried to setup an appointment.
5 We had some discrepancies in the determination in the
6 spreadsheet that was sent out.

7 And at the time, my liability was in excess of
8 \$40,000. So we were trying to figure out where and how
9 that had happened because we are a small business, and it
10 would have been just more beneficial for us to close the
11 doors at that point in time. So I had requested my
12 accountant to be a part of the meeting, and I had also
13 sent the email off requesting that we meet with the
14 supervisor and the auditor. And she had agreed, and she
15 needed to check with her schedule. So if you guys have
16 the email chain and are looking at that, you can see the
17 date stamps and stuff like that.

18 So I had hired my accountant for the day to meet
19 at my home office. And when the auditor arrived and I
20 answered my door, it's just the auditor and there's no
21 supervisor. So to me that was a really big moment for me,
22 not only because I'm taking time off from my day -- I'm
23 trying to run a small business, and now I'm hiring my
24 accountant to come out and help me iron out some of these
25 things that I'm not an expert on -- and it's just the

1 auditor.

2 So we basically went back and forth over the same
3 issues that we never really got too much resolution there.
4 So then it turned into I had to schedule a meeting it -- I
5 think it was in Riverside, if I recall correctly. So I
6 met with the auditor and the supervisor at that time. I
7 did not bring my accountant with me at that one because I
8 had already invested, you know, too much time and money at
9 that point, so I decided not to.

10 So in the meeting with the supervisor and the
11 auditor while we we're going over some things, I had
12 actually discovered an error in the determination in the
13 Excel spreadsheet where someone, something, a computer, or
14 whoever it maybe had double entered our purchases, and it
15 was being grabbed from a separate tab in the spreadsheet
16 and was pulling it all over. So somehow that missed the
17 auditor's eyes. Somehow that missed the supervisor's
18 eyes. And I had found it during that meeting and brought
19 it to their attention, and they go, "Oh, yeah, that's not
20 supposed to be there."

21 So we got it corrected, and at that point that's
22 when the determination had dropped into that -- the, like,
23 10 to \$15,000 range, somewhere in that ballpark. So to
24 kind of sum that part up, that's just -- was one example.
25 I've got a lot of hours in just finding little mistakes

1 here and there and things and going through that.

2 Some of those issues and some of the things that
3 have led to the complex part of all this stuff is some
4 errors on my part and how I was using QuickBooks, which is
5 what we use for our financial stuff. I had misclassified
6 some things in our expense categories not knowing that
7 when we come into an audit like this that it would surface
8 and come about. Things such as consumables that we would
9 use in the shop was getting categorized as materials. And
10 those materials were being lumped together with, not only
11 our business self-consumption but also building
12 improvements and even, like, tools and things like that.

13 To me in my head it was, yeah, materials that
14 we're using for the shop and -- but I was lumping that
15 together with other materials that were being resold
16 for -- to the customers and stuff like that. So we did
17 deeper dives. The CDTEFA was understanding of that, so we
18 did some deeper dives and some shelf tests to try to find
19 those tax-paid purchases and then extrapolate that
20 throughout the audit. Every time we got deeper into that
21 stuff, they would not accept certain things even though
22 everything followed what -- the guidelines they had wanted
23 for some of those things. So I had receipts and different
24 things showing that we had paid the tax on it and some of
25 that stuff.

1 So on Exhibit 2, I -- this was an expense report
2 that was used off of QuickBooks and it's run for the audit
3 period time. And there's been no changes on this
4 particular report. And on there it -- that shows some
5 examples of some tax-paid purchases. It also shows
6 examples of some building improvements and tools and those
7 types of purchases. So, again, mis-categorized by myself.
8 And doing that, just not knowing it would affect the
9 audit.

10 And then there's another example that I don't
11 think it was ever addressed or brought to light. I
12 brought it to their attention, but there was never any
13 compensation for it or allowment [sic] for it. So it's
14 a -- from our job from -- we do we build. We build and
15 fabricate race cars, and so these jobs can be very long
16 term. Some are short-term, but things take a long time.
17 They take two, three years. Some take even longer than
18 that. I have some projects that are in excess of five
19 years.

20 So there may be some purchases that were made
21 during the audit period and -- but they didn't get
22 completed until years later. In fact, I still actually
23 have, I think, one project left over that is not yet
24 completed even during -- from the audit period. So those
25 purchases show up on my report and shelf tests that

1 they're looking at, except there's no record of them being
2 sold yet because the project is still active at our shop.
3 And the way our invoicing and stuff works is, until I get
4 the job completed and built out, then it becomes a final
5 record at that point.

6 So that was never really addressed or taken into
7 consideration, and that's kind of a big part. Some of
8 these jobs can cost up to \$250,000 or more depending on,
9 you know, how large they are. So that's one other area.
10 And in that Exhibit 2, there are some examples of some of
11 those purchases. I went in and highlighted some of those
12 things and made some notes.

13 On to Exhibit 3, it's the same expense report.
14 And what I did was made some modifications, basically,
15 along with some notes. So anything that's highlighted in
16 yellow I basically zeroed out because those were what I
17 consider to be legitimate business improvement,
18 self-consumption and/or tax-paid purchases that had
19 nothing to do with items being resold. They were the
20 items that were mis-categorized, and that's why they show
21 up in the report. They were categorized mainly as
22 material expense when it should not have been.

23 There are some items that are highlighted green
24 for our long-term project examples. And I just went
25 through and did a couple just so you guys could try to

1 find those as easy as possible. Some other highlights
2 basically -- and this is a smaller one, but it's still
3 something this I would like to be considered in. Because
4 there is on occasion, we have zero percent markup in some
5 of our stuff, maybe because I'm trying to maintain a
6 business relationship with another business. Again, we're
7 selling business to business. It's rare, but on some
8 occasion, we do and some of those are larger transactions.

9 So there is one that I pulled up for an example
10 in there and highlighted it that had a zero percent
11 markup. So that one gets a little bit deeper because they
12 made notes in the final determination on that because I
13 had brought that to their attention. But they said they
14 were not going to consider that because it wasn't a
15 regular occurrence. However, they did use that. If they
16 were going to disallow it, they should have taken the
17 transaction completely out of the shelf test, and they did
18 not. So it's a few thousand dollars' worth of shelf test,
19 which turns out to extrapolate out to a decent number that
20 gets out when doing it over a three-year period.

21 So that was put into the calculation for the
22 markup test, basically, and it does not work into my
23 favor. So they didn't allow it for me to use it on my
24 end, but then they used it on their end for the
25 calculation of how much I'm purchasing and stuff. So I

1 didn't think that was particularly fair in that regard.

2 There is on Exhibit -- oh, on Exhibit 3. So if
3 we end up scrolling all the way down on that and getting
4 to the end, you know, that's a significantly different
5 number when it comes to how much money shows up on the
6 cost of goods sold section. So which in turn is what is
7 factoring into, you know, the increase and the liability
8 and what we're -- what I'm seeing is part of the errors on
9 here.

10 So at -- move onto the Exhibit 4 here so I can
11 try to stay on time for you. There's another example of
12 an error that was never corrected. And, in fact, I just
13 recently found it in just kind of putting some of the
14 notes together. So on Exhibit 4 on Tab 120-1, if you look
15 at lines 233 -- and those are going to be the reference
16 lines -- 233 and 234, there's a specific transaction that
17 relates to a verified tax-paid purchase. I apologize.
18 1R-120-1, and then reference line 269 and 270 on that
19 particular one. Yes. 269 and 270 down towards the bottom
20 there. So those are --

21 JUDGE CHO: I'm sorry to interrupt you, Mr.
22 Mandella.

23 MR. MANDELLA: Yes.

24 JUDGE CHO: Give me one second while I get to
25 that page.

1 MR. MANDELLA: Oh, yes. Absolutely.

2 JUDGE CHO: Sorry about that.

3 MR. MANDELLA: I was hoping I'd maybe have a
4 screen to project to so it could help but --

5 JUDGE WONG: Mr. Mandella, is it page -- which
6 page of the PDF?

7 MR. MANDELLA: I don't know that I submitted
8 Exhibit 4 as a PDF, so I don't know. I didn't submit
9 Exhibit 4 as a PDF. I submitted it as an Excel
10 spreadsheet. It was going to be impossible to try to find
11 things.

12 JUDGE CHO: Yes. It looks like it's pages --
13 give me one second. It's a very long schedule -- 113 on
14 the all-briefing file. When we sent out the all-briefing
15 file, did you take a look at that, the hearing binder that
16 was sent to --

17 MR. MANDELLA: Yes. I saw it, yeah. But I --

18 JUDGE CHO: So it looks like your Schedule
19 1R-120-1 is page 113 of that hearing binder.

20 MR. MANDELLA: Let me pull up. I just want to
21 make sure you guys are looking at the right spot real
22 quick here. When I submitted the spreadsheet, I had asked
23 if that was okay because I wanted a live working copy and
24 there was -- I didn't get a response back that it was not
25 going to be okay. So I apologize if --

1 JUDGE WONG: Who is the vendor for that
2 transaction just to verify.

3 MR. MANDELLA: Danchuk.

4 JUDGE WONG: Okay. Got it.

5 MR. MANDELLA: Okay. Yeah. So we should be
6 looking at the right one then.

7 So that's labeled as "Additional Nontax-Paid
8 Purchase Invoices." So that particular item, if we were
9 to reference exhibit, I believe -- let's see. So on the
10 CDTFA's exhibit it was on 4 of 4 of their attachment. And
11 I apologize. I don't know which one it is in their -- in
12 the binder. But they have at the top it ends up being
13 pages 1 through 3, and they're basically copies of those
14 receipts that clearly show that the tax was paid on there
15 and -- in that particular instance.

16 So, again, it's a fairly small dollar amount but
17 it's just another example of yet another error that I
18 discovered and worked through. And then as I would
19 discover some of these during the process, they'd -- it
20 was just constant back and forth. I mean, I have over a
21 couple of 100 emails back and forth, and we couldn't ever
22 get to a, like, a clear resolution. And that was probably
23 the most frustrating part.

24 But -- so there is a copy of the receipt there,
25 which I have up on mine. But it was -- when CDTFA had

1 submitted the documents, it was the fourth document, and
2 its pages 1 through 3 out of 126 pages on that particular
3 exhibit from them. So nonetheless, that was a sales tax
4 paid but did not get recorded that way. And so there just
5 came a point where I had to stop looking for errors. I
6 had a business I needed to run, and I had to get back to
7 doing what I needed to do. So then we just started that
8 process, and I said we'll just go through the appeals. So
9 that is one of those things in regards to that.

10 I had on -- had another audit worksheet that I
11 was looking at, and it was the most recent of the emailed
12 copy for the final determination. So there was an
13 allowance that the shelf test had come up with, and it
14 said your total tax-paid purchases, and it basically came
15 out to \$4,454. Okay. If we were to zero that dollar
16 amount out, my liability actually goes down. And that
17 part didn't make sense to me. So it's -- that shelf test
18 was performed to try to help eliminate some of the items
19 that we had paid for already. Right?

20 So the higher that number would go, technically,
21 the lower my liability should get because those were items
22 I already paid taxes on. Right? So my liability, that
23 should reflect that. Does that make sense? So if you
24 were to take the spreadsheet and type in zero, just for
25 example, and you go back to the liability side where it

1 shows where you -- it actually goes down. Vice versa, if
2 you type in, say, \$100,000 and you raise that total
3 tax-paid purchases to a higher dollar amount, it raises my
4 liability to go up.

5 So I stopped looking to see why that formula was
6 doing it that way. It seemed very concerning to me that
7 that was working that way, but I don't have the time to go
8 in and start, you know, continually trying to figure out
9 the, you know, some of the errors and some of that stuff.
10 So that was probably another big one that had me more
11 concerned because then I questioned all of the -- some of
12 the formulas that had gotten used at that point. So,
13 again, that shelf test was supposed to be used to create a
14 credit for us for those purchases that we had already paid
15 tax on.

16 And just to recap that, if that number were to go
17 up and just unmodified, if you just type in a high-dollar
18 amount in that particular section so that would have been
19 on that same -- it would be on that same page, on that
20 spreadsheet where we saw the Danchuk tax paid. So there's
21 a couple of lines above that it says, "Total tax-paid
22 purchases." And that's the number if you were to change
23 that and raise that higher, it would actually make my
24 liability go up. So that pretty much sums that one up.

25 So in all to kind of recap a little bit on my

1 side of things, the -- I had used -- we were using
2 QuickBooks. You know, we were just coming out of 2008
3 with a bunch of -- obviously, everybody knows the economic
4 downturn from that point, and we were, you know,
5 scratching to stay relevant. And we, fortunately, made it
6 through. Myself just coming out of college basically
7 right at that time, coming in and trying to fix things and
8 get things back on track.

9 And using QuickBooks is just a learning process.
10 And, you know, same thing. I mischaracterized some of
11 those items. So I'm definitely taking some responsibility
12 when it comes to how I characterized those things. So
13 there's definite errors on my part that didn't help the
14 audit process by any means and didn't make your job, on
15 the CDTFA's part, any easier. But once when we dived deep
16 into figuring those things out, they -- there was just --
17 there was no clear communication that we could ever get
18 down to a resolution to help fix those things.

19 And then, again, constant errors and the amount
20 of time I had to put into this particular, you know,
21 audit, it put a lot of undue stress onto our company. You
22 know, I am trying to run a small business and it's hard to
23 take a day off to do things, you know. We've definitely
24 grown as a company. Since then I've learned a lot from
25 this process. I've made changes. We've done things

1 better. We've probably tripled our annual revenues and
2 stuff since then, you know.

3 So we're bringing money back to California.
4 We're doing our job to create more local sales for all
5 that stuff. And part of that is because I've learned a
6 lot from the process, but I just didn't feel like anybody
7 was really trying to help me out to -- it was on my own
8 trying to figure it out versus the, you know, the State
9 actually trying to reach out and help fix some of those
10 things at the end of the day.

11 So that's pretty much it.

12 JUDGE CHO: Thank you very much for your
13 testimony and presentation.

14 Before we move on, Department, would you like to
15 cross-examine the witness as to any facts he stated?

16 MR. SAMARAWICKREMA: This is Nalan
17 Samarawickrema. No, we don't have any questions.

18 JUDGE CHO: Thank you. I'll start with my panel
19 to see if there's any question from the panel.

20 Judge Wong, do you have any questions for the
21 witness?

22 JUDGE WONG: I just have a question about the
23 exhibits you mentioned. There are highlights and notes in
24 there, and I see those. Are those pointing out all the
25 errors, or is that just a sampling?

1 Samarawickrema.

2 Appellant, a limited liability company, operates
3 a business selling race car components, parts, and
4 accessories in Rancho Cucamonga, California. Appellant
5 also provides installation and repair labor on used cars.

6 The Department audited Appellant's business for
7 the period of January 1st, 2011, through December 31st,
8 2013. During the audit period, Appellant reported around
9 \$1.5 million in total sales and claimed various types of
10 deduction resulting in reported taxable sales of around
11 \$93,000. And that will be on your Exhibit A, pages 23 and
12 24. But the audit has found that Appellant had over
13 \$112,000 of unreported taxable sales for the audit period.
14 And that will be on your Exhibit A, page 2.

15 During my presentation I will explain why the
16 Department rejected Appellant's reported taxable sales,
17 why the Department used an indirect audit approach, and
18 how the Department determined Appellant's unreported sales
19 tax for the audit period. During the audit, Appellant
20 failed to provide sufficient sales records. Appellant did
21 not provide complete sales invoices, sales journals, or
22 sales summaries to support its reported sales for the
23 audit period. In addition, Appellant failed to provide
24 complete purchase invoices or purchase journals for the
25 audit period.

1 Appellant was unable to explain how it reported
2 its sales on its sales and use tax returns. Appellant was
3 unable to explain what sources it relied upon to complete
4 its sales and use tax returns. The Department did not
5 accept reported taxable sales due to lack of reliable
6 records and negative reported book markup. It was also
7 determined that Appellant's record was such that sales
8 could not be verified by a direct audit approach.
9 Therefore, the Department estimated sales using cost-plus
10 markup method for year 2011 and quarterly average
11 unreported taxable sales for years 2012 and 2013.

12 The Department completed two verification methods
13 to verify the reasonableness of Appellant's reported total
14 and taxable sales. First, the Department compared
15 Appellant's reported total sales for the audit period,
16 which sales reflected on Appellant's federal income tax
17 return, and calculated an overall negative difference of
18 around \$84,000. And that will be on your Exhibit B,
19 page 154.

20 Second, the Department compared recorded parts
21 and material sale of around \$400,000 to claim cost of
22 goods sold of around \$585,000 reflected on Appellant's
23 profit and loss statement and calculated an overall
24 negative reported book markup of 32 percent. And that
25 will be on your Exhibit B, page 113.

1 This means Appellant was losing money every time
2 it made a sale of parts and materials. Accordingly, the
3 Department did not accept Appellant's recorded total parts
4 and material sales for the audit period. However, based
5 on the analysis available, sale prices, and related cost,
6 the audited markup was around 21 percent. And that will
7 be on our Exhibit B, page 101. Appellant was unable to
8 explain the reasons for negative recorded book markups.
9 Therefore, the Department conducted further investigation
10 by analyzing Appellant's purchase information and pricing
11 policies. The Department reviewed cost of goods sold
12 reflected on Appellant federal income tax returns and
13 detailed profit and loss statements. And that will be on
14 your Exhibit B, pages 132, 133, pages 162 through 313.

15 The Department noted that the recorded cost of
16 goods sold included other expenses not related to the cost
17 of parts and materials sold. Therefore, Appellant
18 obtained purchase information for year 2011 directly from
19 Appellant's vendors to calculate Appellant's purchases.
20 And that will be on your Exhibit B, pages 134 to 140.

21 Using the purchase data, the Department compiled
22 merchandise purchases of around \$127,000, which was
23 comprised of around \$122,000 in merchandise purchases
24 without sales tax paid to vendors, and around \$5,000 in
25 merchandise purchases where sales tax was paid directly to

1 vendors for year 2011. And that will be on your
2 Exhibit A, pages 44 to 50 and Exhibit B, pages 316
3 through 322.

4 However, Appellant did not obtain merchandise
5 purchase information from its vendors for years 2012 and
6 2014. The Department calculated Appellant's recorded
7 nontaxable sales for resale of almost \$25,000 and exempt
8 sales in interstate and foreign commerce of \$57,000 using
9 Appellant's sales report for the year 2011. And that will
10 be on your Exhibit B, page 98.

11 Appellant performed his own shelf test of parts
12 and materials sold for resale and sale in interstate and
13 foreign commerce by comparing the selling prices on the
14 sales reports for second quarter 2011 and cost from the
15 merchandise purchase invoices for the same period. And
16 the shelf test resulted around 10 percent markup for sales
17 for resale and 19 percent markup for sales in interstate
18 and foreign commerce. And that will be on your Exhibit B,
19 pages 102 through 106. The Department reviewed
20 Appellant's shelf test and did not find material errors.
21 Therefore, the Department accepted Appellant's computed
22 shelf test on exempt sales.

23 The Department then calculated the cost of
24 merchandise purchases for sales for resale of almost
25 \$23,000 and cost of merchandise purchases for sales in

1 interstate and foreign commerce of \$48,000 for 201.1 and
2 that will be on your Exhibit B, page 98. The Department
3 calculated the audited taxable sales -- I'm sorry --
4 taxable purchases available for retail sale of around
5 \$55,000 for year 2011 using audited purchases, customer
6 merchandise purchases for sale for resale, and sales in
7 interstate and foreign commerce and 1 percent shrink rate.
8 And that will be on your Exhibit A, page 40.

9 To understand the Appellant's retail pricing
10 policies, the Department performed a shelf test using
11 selling prices on the sales report for fourth quarter 2013
12 and October 2014 with cost from merchandise purchase
13 invoices for the same period. And that will be on your
14 Exhibit B, pages 107 and 108. The result of the shelf
15 test reveal around 24 percent markup for parts and
16 41 percent markup for materials. The Department also
17 completed a purchase segregation test using Appellant's
18 profit and loss statement for the audit period. And that
19 will be on your Exhibit B, pages 132 and 133.

20 The purchase segregation test disclosed around 88
21 percent parts and 12 percent materials. And that will be
22 on your Exhibit B, pages 132 and 133. The Department
23 weighted the shelf test markups using the corresponding
24 purchase ratios determining the purchase segregation test
25 to compute the retail weighted markup of around

1 27 percent. And that will be on your Exhibit B, page 101.

2 Appellant also performed its combined retail
3 shelf test of parts and materials using selling prices on
4 the sales report for second quarter 2011 with cost for
5 merchandise purchase invoices for the same period. And
6 the shelf test resulted around 16 percent markup for parts
7 and materials combined. And that will be on your
8 Exhibit B, pages 102 through 106. The Department accepted
9 Appellant's completed combined shelf test of around
10 16 percent to give a benefit to the Appellant and average
11 it with its markup of 26 percent to compute an average
12 retail markup of around 21 percent. And that will be on
13 your Exhibit B, page 101.

14 The Department then estimated audited taxable
15 sales of around \$67,000 for the year 2011 using audited
16 purchases available for sale at retail and the audited
17 retail markup factor. And that will be on your Exhibit A,
18 page 40. In lieu of establishing a separate deduction for
19 tax-paid purchase resold, the Department reduced audited
20 taxable sales by tax-paid merchandise purchases of around
21 \$5,000 to compute adjusted audited taxable sales of around
22 \$62,000 for the year 2011. And that will be on your
23 Exhibit A, page 14.

24 Adjusted audited taxable sales were compared with
25 reported taxable sales of around \$25,000 to compute

1 unreported taxable sales of around \$37,000 for the year
2 2011. And that will be on your Exhibit A, page 40. The
3 Department compared the unreported taxable sales with the
4 reported taxable sales of around \$25,000 to compute an
5 error rate of around 151 percent for year 2011. The
6 Department did not have merchandise purchase information
7 from Appellant's vendors for years 2012 and 2013.
8 Therefore, the Department evaluated the unreported taxable
9 sales for those years using three different methods.

10 First, estimating purchases for years 2012 and
11 2013 and marking up those purchases. Second, using
12 average quarterly unreported taxable sales of 2011. And
13 third, using the 2011 percentage of error around
14 151 percent. And that will be on your Exhibit A, pages
15 33, 38, 40, and Exhibit B, page 155. Those methods showed
16 projected unreported taxable sales of around \$90,000 from
17 the first method, \$75,000 from the second method, \$103,000
18 from the third method. And that will be on your
19 Exhibit A, pages 33, 38, 40, and Exhibit B, page 155.
20 Therefore, the Department based the unreported taxable
21 sale for years 2012 and 2013 on average quarterly
22 unreported taxable sales of year 2011. And that will be
23 on your Exhibit A, pages 33 and 38.

24 This audit approach reduced Appellant's
25 unreported taxable sales by around \$28,000. And that will

1 be on your Exhibit A, pages 33, 38, and Exhibit B,
2 page 155. In total, the Department calculated unreported
3 taxable sales of around \$112,000 for the audit period.
4 And that will be on your Exhibit A, page 2. Then the
5 Department compared the total unreported taxable sales
6 with the reported taxable sales of around \$93,000 to
7 compute the overall error rate of around 121 percent for
8 the audit period.

9 The audit calculation of unreported taxable sales
10 based on vendor information for year 2011 and shelf test
11 information was reasonable, and was in Appellant's favor
12 since it was the lowest of the difference determined.
13 Ultimately, the Department decided to use an audit method
14 which use the lowest deficiency measure to give a benefit
15 to Appellant. As mentioned earlier, Appellant did not
16 provide complete source documentation, such as complete
17 sales invoices. Appellant did not provide complete
18 purchase invoices. Appellant failed to provide
19 documentary evidence to support its taxable sales for the
20 audit period.

21 The Department was unable to verify the accuracy
22 of reported sales tax using a direct audit method.
23 Therefore, an alternate audit method was used to determine
24 unreported sales tax. Accordingly, the Department
25 determined the unreported sales tax based upon the best

1 available information. The evidence showed that the audit
2 produced fair and reasonable results. Appellant believe
3 that it is entitled to additional adjustments to the audit
4 finding.

5 As support, Appellant provided an email chain,
6 adjusted and unadjusted parts and material expense report
7 for the audit period. And that will be on your Exhibit 1,
8 2, and 3. The Department reviewed and analyzed this
9 information, and ultimately rejected them. The adjusted
10 and unadjusted parts and material expense report for the
11 audit period only listed the method of payment, date,
12 expense category, some description of the parts and
13 materials, and the amount. And that will be on your
14 Exhibit 2 and 3.

15 Upon examination of Appellant's adjusted and
16 unadjusted parts and material expense reports, the
17 Department noted that Appellant did not provide any source
18 document or vendor information to collaborate the figures
19 listed in adjusted and nonadjusted parts and material
20 expense reports. Therefore, the Department was not able
21 to verify Appellant's newly provided Exhibit 2 and
22 Exhibit 3 for report keeping accuracy.

23 However, the Department compared the January and
24 May 2011 recorded purchases reflected on adjusted parts
25 and material expense report with the purchases reflected

1 on vendor responses and determined that purchases listed
2 on adjusted parts and material expense reports are more
3 than the purchases reflected on vendor responses. And
4 that will be on your Exhibit A, pages 44 through 50 and
5 Exhibit 3.

6 JUDGE CHO: I'm sorry, Department. Just to let
7 you know, your time is up if you can wrap it up in the
8 next minute or two. Thank you.

9 MR. SAMARAWICKREMA: Therefore, included
10 Appellant provided Exhibit 3 would increase the year 2011
11 purchases and, thus, resulting in higher unreported
12 taxable sales. Appellant also claim parts purchases
13 during the audit period were not used until after the
14 audit period. Therefore, purchases available for sale
15 were overstated. Cost of goods sold is calculated by
16 adding beginning inventory to merchandise purchases and
17 subtracting ending inventory.

18 Thus, for the purpose of computing the cost of
19 goods sold in an audit, an inventory adjustment would be
20 in order only if it could be verified that beginning
21 inventory is different from ending inventory. In this
22 audit the merchandise purchases may be considered the cost
23 of sales if there is evidence that inventories were
24 substantially consistent.

25 The Appellant reported beginning inventory of

1 around \$77,000 and ending inventory of \$76,000 on its
2 federal income tax return for year 2011 or a difference of
3 around \$1,000. And that will be on your Exhibit B,
4 page 154. Since the beginning inventory is more than the
5 ending inventory, including adjustment for inventory in
6 this audit, it would increase the cost of goods sold and,
7 thus, resulting in higher unreported taxable sales.

8 Appellant also benefit from lower audited taxable
9 sales based on a projection of year 2011 unreported
10 taxable sales rather than using the mark up method to
11 estimate unreported taxable sales for years 2012 and 2013.
12 Appellant has not provided any reasonable documentation or
13 evidence to support an adjustment to the audit finding.
14 Therefore, the Department request the appeal be denied.

15 This concludes my presentation, and I'm available
16 to answer any question the panel may have. Thank you.

17 JUDGE CHO: Thank you, Department.

18 Panel members, do you have any questions for the
19 Department? I'll start with Judge Wong.

20 JUDGE WONG: Just at the end of your
21 presentation, I had a question about source documentation
22 regarding Exhibit 2 and 3. If Appellant could provide
23 source documentation for some of the alleged errors that
24 he pointed out, would an adjustment be warranted? Just a
25 point to clarify.

1 particular method of the audit.

2 Our business is unique for what we do. That
3 wouldn't, I guess, surprise me. But, again, I think it
4 brings to light the fact that part of our long-term
5 projects that we have surface those types of methods and
6 that those methods can't be used for, you know, our
7 particular business. I'm not an automotive business. I
8 don't do used car. I don't do -- we do race cars, and we
9 build race cars and build custom stuff. And we install
10 parts, and we do a lot of that.

11 And, you know, their methods of the audit show
12 that it doesn't calculate out, you know. I'm clearly not
13 losing money between -- on my invoices. I provided very
14 specific invoices. We went through and pulled up every
15 single invoice almost and showed them. And then I even
16 pulled up actual purchase receipts. The exhibits are
17 here. You guys provided them yourself as your own deal,
18 but you're saying I didn't -- I didn't provide enough of
19 the purchase invoices. And you're saying none of that got
20 provided, but that's -- none of that is true,
21 unfortunately.

22 Going back to the markup method and your guys'
23 method for the cost-plus markup, I'll just reiterate my
24 zero percent markup factor was never taken into
25 consideration, yet, was used in that example in showing in

1 their exhibit. And then same thing with the tax-paid
2 purchases. All those documents were provided. They're in
3 your exhibits specifically, and it shows that. And it
4 clearly shows that the errors are right there, that it's
5 being classified as nontax paid, even though the tax was
6 paid.

7 I don't think it's one particular area that is
8 causing it to be out of proportion. I think it's several
9 areas of the audit with errors and miscalculations and
10 some of those other things. And at the end, I'm just --
11 would hope that you're able to see the amount of errors
12 and stuff that have gone into it and the kind of -- the
13 back and forth that I've had to deal with going back and
14 forth with them trying to get documentation that they
15 don't accept, and then they're saying I didn't provide it,
16 which I did, and the amount of time involved in doing all
17 that stuff. Just it's added up, and that's all I have.

18 I really wouldn't even be interested in providing
19 any further documentation. I guess it's time to move on.
20 It's been eight years, you know. And because all it's
21 going to do is lead to more back and forth. It's -- I can
22 already hear it just in their answer with some of that
23 stuff.

24 So like I said, I had mistakes on my side of
25 which I think made the corrections for in doing better

1 classifications and stuff like that, which led to some of
2 the mischaracterization, which they just weren't willing
3 to fully accept all of those in their determination. So
4 that's all.

5 JUDGE CHO: Thank you very much.

6 Before we conclude this hearing, let me just
7 check back with my panel to see if there are any final
8 questions.

9 Judge Wong, do you have any final questions?

10 JUDGE WONG: No final questions. I appreciate
11 both parties' time and presentations.

12 JUDGE CHO: Judge Geary, do you have any final
13 questions?

14 JUDGE GEARY: No. Thank you. And thank you to
15 everybody who appeared this morning.

16 JUDGE CHO: I just have a quick question for you,
17 Mr. Mandella. You said the information is in -- you
18 provided it to the Department. Are you able to point to
19 an exact actual exhibit in the record to tell us exactly
20 where all the purchase invoices are for 2011 that would
21 support your Exhibits 2 and 3?

22 MR. MANDELLA: I mean, specifically, if you look
23 at -- and, again, I'm looking at the file attachments from
24 the first email, not the hearing binder. So I apologize
25 for that, but it's their Exhibit 4 of 4. I mean, it's a

1 bunch of scanned images of our -- of a lot of our
2 purchases there. So those are purchase invoices direct
3 from some of our companies. I'd have to go through and
4 pull up all of my records to see if it's a complete list
5 of them.

6 But, I mean, it's just an example that I
7 literally gave them everything that I had at that point
8 and scanned them in. So he's claiming that we didn't
9 provide them, yet, they're right here. So that's where I
10 don't understand that -- his claim that we didn't provide
11 any of the purchase invoice or didn't provide sufficient
12 documentation for purchase invoices.

13 JUDGE CHO: So when you say Exhibit 4 of 4 --

14 MR. MANDELLA: Yeah. That was --

15 JUDGE CHO: -- is it part of Exhibit A, B, or C
16 in this case? The Department's exhibits are labeled
17 alphabetically.

18 MR. MANDELLA: In the one email that was sent
19 when I got a copy of their exhibits, they were labeled --
20 let me see if it's --

21 JUDGE CHO: Is there a page number at the bottom?

22 MR. MANDELLA: Page 380, yeah. Yeah. So those
23 aren't part of the original document. So it looks like it
24 starts off at page 374 then.

25 JUDGE CHO: Okay. I see them. So just this

1 section?

2 MR. MANDELLA: So, I mean, that entire exhibit
3 appears to be scanned images of purchase invoices all
4 appearing to be in 2011. Like I said, he mentioned that
5 we did not provide sufficient document or adequate
6 documentation of purchase invoices. And I just don't know
7 how much more of a scanned copy image that I can provide,
8 you know, for them. I even provided 2012 and 2014 as
9 well, and they're claiming that I didn't. I don't have
10 those with me here.

11 But, again, it's just for me and my rebuttal,
12 it's just an example of the constant either
13 miscommunication or the back and forth of trying to get to
14 a resolution. Like, this is a basic concept right here in
15 my eyes of these are purchase invoice, and we're arguing
16 over the fact that I didn't provide them, you know.

17 JUDGE CHO: Okay. Quick question for the
18 Department. So these invoices that the taxpayer has
19 pointed out, were these the vendor responses or are these
20 from the taxpayer itself?

21 MR. SAMARAWICKREMA: This is Nalan
22 Samarawickrema. That's from the taxpayer, from Appellant.
23 That's for the shelf test. Those are the invoices, sales
24 invoices that were related to the shelf test.

25 JUDGE CHO: All right.

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MR. MANDELLA: If I may?

JUDGE CHO: Sure, Mr. Mandella.

MR. MANDELLA: Thank you. Yeah. And scrolling down through even some of them, so some of those are actual documents that I had provided to them. Later on if you scroll down even further through, those are actual responses from the vendors themselves that they provided. Basically, a statement of invoices for the year. Some of the vendors couldn't do it, some could. But most of these are all responses direct from the vendors in just scrolling through some of these right now. So it's a little mix of both is what it appears to be.

JUDGE CHO: All right. Thank you very much for your explanation.

That was the only question that I had. I just wanted to make sure that I knew where to look in the file and make sure I did not miss anything. Give me one second while I just go through my notes.

Okay. So this concludes the hearing. The three judges will meet and decide the case based on the documents and testimony presented today. We will issue our written decision no later than 100 days from today.

The case is submitted, and the record is now close.

(Proceedings adjourned at 10:34 a.m.)

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HEARING REPORTER'S CERTIFICATE

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

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

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

I have hereunto subscribed my name this 5th day of May, 2022.

ERNALYN M. ALONZO
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