

BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF,)
)
 LAI LUCKY, INC.,) OTA NO. 19125548
)
 APPELLANT.)
)
)

TRANSCRIPT OF PROCEEDINGS

Cerritos, California

Tuesday, May 17, 2022

Reported by:
ERNALYN M. ALONZO
HEARING REPORTER

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Transcript of Proceedings, taken at
12900 Park Plaza Dr., Suite 300, Cerritos,
California, 91401, commencing at 9:31 a.m.
and concluding at 11:24 a.m. on Tuesday,
May 17, 2022, reported by Ernalyn M. Alonzo,
Hearing Reporter, in and for the State of
California.

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APPEARANCES:

Panel Lead: ALJ SUZANNE BROWN

Panel Members: ALJ ANDREW WONG
ALJ JOSHUA LAMBERT

For the Appellant: MARC BRANDEIS
I. LAI-BOROR

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

NALAN SAMARAWICKREMA
CHAD BACCHUS
JASON PARKER

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I N D E X

E X H I B I T S

(Appellant's Exhibits 1-24 were received at page 8.)

(Appellant's Exhibit 25 was received at page 10.)

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

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Cerritos, California; Tuesday, May 17, 2022

9:31 a.m.

JUDGE BROWN: We are on the record for the Appeal of Lai Lucky, Inc., OTA Case Number 19125548. Today is Tuesday, May 22nd, 2022, and it is approximately 9:31 a.m.

We are holding this hearing in Cerritos, California. I'm Suzanne Brown. I'm the lead Administrative Law Judge, and my co-panelists are Judge Andrew Wong and Judge Josh Lambert.

I will start by asking each of the representatives to please identify themselves for the record. I'll start with CDTFA.

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

MR. PARKER: Jason Parker, Chief of Headquarters Operations Bureau.

MR. BACCHUS: Chad Bacchus with the Department's Legal Division.

JUDGE BROWN: Thank you. And now for the Appellant. I think your microphone is off.

MR. BRANDEIS: Mark Brandeis CPA for the Appellant. To my right is Iris Lai. She is the manager at the Appellant's restaurant. Behind me is Mr. Johnny Lee. He is a technical support manager for Opus POS. And

1 to his right is Ed Lai. He also worked as a manager at
2 Lai Lucky during the period in question.

3 JUDGE BROWN: Okay. Thank you, everyone.

4 I'm just going to briefly go over the issues, the
5 witnesses, the exhibits, confirm our time frame for today,
6 and once we've done all those logistical things, I will
7 hear the parties' arguments and testimony. All right. We
8 discussed at the prehearing conference what the issues
9 would be. I confirmed them in a prehearing conference
10 minutes and orders on April 29th, 2022. And then after
11 receiving a subsequent submission, I also issued a
12 prehearing order dated May 13th, 2022, and we confirmed
13 that the issues are: First, whether further adjustments
14 are warranted to the audited understatement of reported
15 taxable sales for the liability period, which is July 1st,
16 2011, through June 30th, 2014; and then second, what
17 remedy, if any, is warranted for CDTFA's untimely issuance
18 of the May 8th, 2019, Appeals Bureau decision.

19 I will say, does that confirm what the issues are
20 is accurately -- does that accurately confirm what the
21 issues are? Mr. Brandeis, do you agree?

22 MR. BRANDEIS: Yes.

23 JUDGE BROWN: And CDTFA?

24 MR. SAMARAWICKREMA: Yes.

25 JUDGE BROWN: Thank you.

1 All right. Next I'm going to address the
2 documentary exhibits. We received documents from both
3 parties, and I'll start with -- with CDTFA's we received
4 Exhibits A through I. And Appellant indicated at the
5 prehearing conference that it had no objection to
6 admission of CDTFA's Exhibits A through I. And for
7 Appellant we received Exhibits 1 through 24, and then
8 yesterday we also received proposed Exhibit 25. I'm just
9 going to go through them first. Let's do CDTFA. Let me
10 address CDTFA's exhibits first.

11 Mr. Brandeis, you can confirm that you had no
12 objection to admission of CDTFA's exhibits A through I?

13 MR. BRANDEIS: I have no objection.

14 JUDGE BROWN: Okay. CDTFA's Exhibits A through I
15 are admitted.

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

18 I did have that question about the date of
19 Exhibit I that we had discussed at the prehearing
20 conference. I'm pretty sure it was sometime in
21 March 2018. Do you have an update for that date?

22 MR. SAMARAWICKREMA: This is Nalan
23 Samarawickrema. The NOW report was approved on July 9,
24 2018.

25 JUDGE BROWN: Oh, and I'll just note. Saying

1 your name beforehand is something we do when we're online.
2 I think we don't need to do it for the stenographer today.

3 MR. SAMARAWICKREMA: Okay.

4 JUDGE BROWN: Okay. Thank you.

5 All right. Then first let me address Appellant's
6 Exhibits 1 through 24, then I'll address Exhibit 25
7 separately.

8 CDTFA, did you have any objection to Appellant's
9 Exhibits 1 through 24?

10 MR. SAMARAWICKREMA: No objections.

11 JUDGE BROWN: Okay. Appellant's Exhibits 1
12 through 24 are admitted into the record.

13 (Appellant's Exhibits 1-24 were received
14 in evidence by the Administrative Law Judge.)

15 All right. Then yesterday we received
16 Appellant's proposed Exhibit 25, and my prehearing
17 conference minutes and orders had specified the due date
18 for submission of exhibits was 14 days prior to hearing to
19 the hearing. Per our regulations it's actually 15 days,
20 but because of the day of the prehearing conference, I
21 adjusted it.

22 So Mr. Brandeis, let me ask why we received
23 Appellant's Exhibit 25 late? And -- yeah. That's my
24 first question.

25 MR. BRANDEIS: Well, this is a case that's been

1 going on for -- I've been involved in this case for seven
2 years. There is a tremendous amount of -- a tremendous
3 volume of records and documents to go through. And this
4 document I didn't -- I don't recall reviewing. And I
5 think it's important because it shows the point of view
6 that the auditor had early on and my representation
7 process when I asked him why he did not choose altered --
8 methods that are prescribed in the audit manual. I think
9 his response is indicative of his overall point of view
10 and his biases, if you will, and his audit methodology.

11 JUDGE BROWN: All right. CDTFA, do you have any
12 objection to admission of Appellant's Exhibit 25?

13 MR. BACCHUS: The Department objects only based
14 on the timing -- of the timing of it. Substantively, we
15 don't have any objection.

16 JUDGE BROWN: Just hypothetically, let me ask
17 CDTFA, is there any additional -- if I did admit it, would
18 there be something you would want to admit in response --
19 to submit in response, or would you need -- yeah. Is
20 there some way if we did admit it that you would need
21 additional time for anything?

22 MR. SAMARAWICKREMA: No need. No, we don't.

23 JUDGE BROWN: Okay. All right. Given all the
24 circumstances, I will admit Appellant's Exhibit 25. It is
25 admitted into the record.

1 (Appellant's Exhibits 25 was received
2 in evidence by the Administrative Law Judge.)

3 All right. Let's move on to address the
4 witness -- confirm who the witnesses are going to be.

5 Mr. Brandeis, do you still plan on calling all
6 three witnesses?

7 MR. BRANDEIS: It depends on the questions that
8 may arise from the panel. Ms. Iris -- so, again, I wasn't
9 the original representative. I was brought in -- I don't
10 remember -- eight or nine months after the audit had
11 started. So some of the early meetings with the
12 Department, I wasn't there, but Ms. Lai was. And so I
13 will be calling on her to recall her recollection of
14 certain meetings that were held at her place of business.
15 Mr. Ed Lai, he worked there as well, but he wasn't as
16 involved in the audit as -- this is his sister -- as his
17 sister, Iris, was. So probably will not be calling on
18 him.

19 If there are any questions regarding the
20 operation of the POS system, which is sort of a critical
21 central issue in this case. I mean, I'm a CPA. I'm not
22 an IT guy. So I brought somebody from Opus, who sold the
23 POS system to the Appellant, to answer any technical
24 questions regarding the operation of the POS system. And
25 that would be Mr. Johnny Lee. So it's conceivable that we

1 could be calling on him.

2 JUDGE BROWN: Well, let me ask this way.

3 MR. BRANDEIS: Okay.

4 JUDGE BROWN: When you put on your initial case
5 before -- assuming that the panel doesn't interrupt with
6 questions, who are you going to be calling?

7 MR. BRANDEIS: Ms. Iris Lai and Mr. Johnny Lee.

8 JUDGE BROWN: Okay. And previously you gave me a
9 time estimate of 30 minutes for initial presentation. Is
10 that still accurate?

11 MR. BRANDEIS: Probably won't need a full
12 30 minutes, but I would say a solid 20 minutes at least.

13 JUDGE BROWN: Okay. So, we'll say 30.

14 MR. BRANDEIS: Okay.

15 JUDGE BROWN: Okay. All right. And, CDTFA, let
16 me just confirm you don't have any objection to these
17 witnesses?

18 MR. SAMARAWICKREMA: No objections.

19 JUDGE BROWN: All right. And previously during
20 the prehearing conference your time estimate was
21 30 minutes. Is that still accurate?

22 MR. SAMARAWICKREMA: Yes.

23 JUDGE BROWN: Okay. Thank you.

24 All right. I'm just going to go over our
25 schedule today. First, we're going to have Appellant's

1 presentation, including witness testimony. And then we
2 have witness examination, meaning that the judges may ask
3 questions of the witness, or CDTFA is allowed to ask
4 questions of the witness as well. And after questioning
5 and questions from the panel to Appellant's
6 representative, we then have CDTFA's presentation for 30
7 minutes. There may also be questions from the ALJs after
8 that, and then following the panel's questions we have
9 Appellant's rebuttal argument, which we had an estimate of
10 15 minutes, and that should wrap us up.

11 Let's see. Is there anything I haven't covered?
12 Does anyone have any questions or anything in addition to
13 raise -- excuse me. Anything in addition to raise before
14 we proceed with Appellant's presentation?

15 Okay. Mr. Brandeis, if your going to swear in
16 Ms. Lai first -- if you're going to just call Ms. Lai
17 first, then I will just swear her in. If you're going to
18 call additional witnesses, I'll swear them in separately.

19 Could I ask the witness to please -- thank you --
20 turn on your microphone, and please raise your right hand.

21
22 IRIS LAI,
23 produced as a witness, and having been first duly sworn by
24 the Administrative Law Judge, was examined and testified
25 as follows:

1 JUDGE BROWN: Thank you.

2 All right. Mr. Brandeis, you can begin. You
3 have 30 minutes.

4

5 PRESENTATION

6 MR. BRANDEIS: Okay. This is a case that began
7 about eight years ago. The taxpayer operates a dim sum
8 restaurant. It's a Chinese-style restaurant in the City
9 of Westminster, and they offer lunch service and dinner
10 service, and they also have a banquet function. In
11 addition to that, they do offer alcoholic beverages but
12 the alcoholic beverages are not a significant portion of
13 their business.

14 They were selected for audit. They hired their
15 CPA firm as their initial representative, and the initial
16 representative requested that the audit be transferred
17 from the Irvine office to the West Covina office where
18 they, the CPA firm, has their offices. The Department did
19 transfer the case to the West Covina office, and an
20 auditor from that office contacted Mr. Ryan Wong the
21 previous representative and arranged for a meeting -- an
22 initial meeting at the taxpayer's place of business to
23 review the operation of the business and also to get a
24 download of the POS data.

25 I wasn't there. So my understanding is it was

1 Mr. Ryan Wong, and he brought POS representative. Mr. --
2 the auditor was there, and Ms. Lai was there.

3 Was there anybody else's there at the initial
4 meeting.

5 MS. LAI: The tech guy.

6 MR. BRANDEIS: Their computer audit -- CDTFA's
7 computer audit specialist was present as well.

8 I wasn't there at the meeting, but the gist of it
9 from my discussions with both Ryan Wong and also Ms. Lai,
10 were that right off the bat they sort of got off to a
11 rough start. Because the auditor in his opening remarks
12 with the taxpayer declared that all Chinese restaurants
13 cheat on their taxes. So as you can imagine, the
14 representative, Mr. Ryan Wong, took offense to that, as
15 I'm sure Ms. Lai did as well, and it set combative tone
16 for the audit right off the bat.

17 While they were there, they observed the
18 restaurant. They got a feeling for how many tables and
19 chairs they have, how many employees, how many cash
20 registers, and they did, in fact, download partial POS
21 data. So my understanding was they did have a problem
22 with the POS system, I think, about a month before. But
23 nonetheless, they were able to capture half the POS data
24 from first quarter '13 to second quarter'14. So they got
25 half the data.

1 I don't know at what point they analyzed the
2 data, that they analyzed it in their office, and analyzed
3 it. But the bottom line is from that point, the auditor
4 decided that he was going to impeach the taxpayer's
5 records. So this is kind of an important issue. When do
6 you impeach a taxpayer's records, and what does that mean?
7 Impeaching the records means that the records are deemed
8 to be inadequate for sales and use tax purposes. And the
9 initial reason that we were -- that was provided for the
10 impeachment of the records was that the taxpayer's
11 reported markup presumably from their income tax returns
12 was too low.

13 Okay. Based on what? What did you analyze that
14 lead you to believe the markup was too low? So the markup
15 varies from year to year but it was in 120 to 130 percent
16 range. And from what I can see in his notes, that he
17 believes it's too low based on his expense dining at other
18 Chinese restaurants. So how is the taxpayer to counter
19 that? I mean, it's not based on any empirical evidence or
20 analysis. It's based on his expense in dining at other
21 restaurants. This is nonsense.

22 So first off the bat, why did we impeach records?
23 I don't believe the Department had sufficient records to
24 impeach the records. Nevertheless, they did run some of
25 the tests that are noted in the audit manual. They did a

1 bank deposit analysis. And low and behold, they found no
2 issues in the bank deposits that indicated that there was
3 underreporting. They analyzed the six quarters of POS
4 data they had and compared it to report it and found no
5 problems.

6 They did an undercover purchase, and the
7 undercover purchase shows up in the data. Only one. They
8 are only telling us about one. Did they do others? We
9 don't know. They did something called a tablecloth method
10 analysis, which we only see various comments about it, but
11 that didn't go anywhere. That didn't disclose any
12 underreporting. And they ultimately decided on a
13 procedure that's not described in the audit manual called
14 the two-item control test. They decided to analyze
15 purchases of duck and lobster, and then to compare that to
16 what's in the POS data.

17 So presumably if you bought a certain amount of
18 duck and lobster, then there should be a similar
19 corresponding amount in the POS data for sales of duck and
20 lobster. So for three-and-a-half years, we talked about
21 duck-duck-lobster method. Three-and-a-half years. And
22 noted all kinds of problems with this analysis that they
23 had done. What kind of problems? Well, number one, we
24 had issues with -- in the data they're able to filter
25 based on the item purchased.

1 So, for example, they filtered lobster, and they
2 got a certain number of lobsters from the data. However,
3 because they have a banquet business there will also be
4 sales of lobster. And sometimes -- again, I don't work
5 there, but what I can surmise is, there would be like a
6 sale of lobster, quantity one, and then the price was like
7 \$5,000. So, clearly, they didn't sell a lobster for
8 \$5,000. What happened is they had a banquet; it was a
9 certain number of people, certain number of lobsters sold.
10 And so what the person did when they rang it up, is they
11 entered it as an open item, quantity one lobster, \$5,000.
12 They didn't put in the actual number of lobsters sold.

13 So then we have a problem in this
14 lobster-duck-lobster count. How do we convert that --
15 items like that to a number of lobsters sold? Because you
16 got to understand also, lobster -- market prices for
17 lobsters vary, and lobsters come in different sizes and
18 it's sold usually by the pound. So, you know, they would
19 probably have weighed the lobsters.

20 Actually, maybe you can speak to that. How did
21 they -- did they weigh the lobsters when they come up with
22 a price for a banquet and sell it by the pound?

23 MS. LAI: Yes.

24 MR. BRANDEIS: Yes. Okay.

25 So some lobsters are bigger than others, and the

1 market price is always varying. So that adds a complexity
2 to this count.

3 Second, we have self-consumption. So the
4 Department -- they had a banquet book. The Department
5 went through the banquet book and analyzed it, the banquet
6 book and compared banquet dates to the POS data. And,
7 again, we weren't able to -- they weren't able to provide
8 us any evidence that any of the banquets were not in the
9 data, not one. Actually, they thought they had one. I
10 had a meeting with the audit supervisor. She presented
11 evidence that there was a wedding banquet that did not get
12 recorded in the POS data. And I was, of course, when she
13 brought that up, I was shocked. I said, "Well, let's see
14 what you got."

15 So she emailed me a copy. They went on social
16 media and found some photographs and pictures of a wedding
17 that was clearly held at the taxpayer's place of business.
18 And so when I brought this information to the taxpayer,
19 the particular event that they were discussing was a
20 wedding between Ms. Iris Lai and her husband. Well,
21 that's -- Ms. Iris Lai is the taxpayer's daughter. So,
22 yeah, it didn't show up in the POS data because the
23 taxpayer didn't charge his daughter to have her wedding at
24 her father's restaurant.

25 And when we pointed that out to this audit

1 supervisor, she still didn't believe us. And you could
2 read her supervisor comments that she wrote up. It's in
3 the record. The date of her report is April 1st, 2016.
4 And she still, even after presenting evidence, we provided
5 the driver's license, I mean, I said, "What do you want me
6 to do? You want me to get a copy of birth certificate?"

7 What an outrageous lie that would be if we
8 were -- if we made a claim like that if it wasn't true.
9 But she, nevertheless, continued to question whether or
10 not we were being honest about that. But it is true.

11 Did you have your wedding at your father's
12 restaurant and --

13 MS. LAI: Yeah.

14 MR. BRANDEIS: Okay. So there you have it on
15 record.

16 THE STENOGRAPHER: I cannot hear you. When you
17 are speaking, could I have you please get closer to the
18 microphone. Thank you.

19 MR. BRANDEIS: Did you have your father's wedding
20 at your -- or did you have your wedding at your father's
21 restaurant?

22 MS. LAI: Yes.

23 MR. BRANDEIS: Okay. So that went nowhere. So
24 we have her impeaching records based on her experience of
25 dining at other restaurants and other Chinese restaurants.

1 Another problem with this is how do we know that whatever
2 restaurants they are comparing it to are comparable to
3 this taxpayer? We don't know because they won't tell us
4 what restaurants they're comparing it to. And I don't
5 know how they would know what the markup is at a
6 restaurant. You know, I go to restaurants all the time.
7 I have no idea what the markup is on their food.
8 That's -- it's really just sort of an outlandish thing to
9 say, but that's what they're telling us.

10 We did provide evidence of a case that we argued.
11 It was another dim sum restaurant not very far away in
12 Rowland Heights called new Capital Sea Food, Inc. New
13 Capital Seafood also goes by -- their business name is
14 Wing Sang, Inc. It was a case we argued before the Board
15 of Equalization, the predecessor agency to this agency.
16 And they had a markup that was a little bit lower than
17 this taxpayer's markup. I want to say markups on that
18 case were somewhere in the ballpark of 115 percent, and
19 they're at 125 or 130.

20 So here, we have -- I don't know what restaurants
21 he's comparing it to, but this is about as close as you
22 can get. I'd say the biggest difference between these two
23 restaurants is I don't think New Capital Seafood had quite
24 as much banquet business as the taxpayer. But I'll be
25 honest with you. I really don't know for sure.

1 The reasoning -- as the case went through the
2 appeals process changed, the reason now that they're
3 citing as the primary reason for impeaching records is
4 that the check number doesn't appear as a printed number
5 on the receipt given to customers. That's not exactly
6 true either. In the evidence that we provided, like we
7 provided copies of receipts -- and what you will notice is
8 there's a bar code on each receipt. That bar code has the
9 check number sequence. So what happens is, when a
10 customer wants to pay their bill, the cashier scans the
11 bar code on the ticket which then automatically brings up
12 that transaction. And then they can run the payment
13 through the POS system.

14 Number two, the data that was downloaded by the
15 Department, and we provided full data later at a hearing
16 with the principal auditor, that data has a field for a
17 transaction number or check number. So the Department, if
18 they're concerned that they can't trace a transaction,
19 even if they didn't know what the check number was, they
20 can trace it based on the date of the transaction and the
21 time of the payment, which would be printed on the receipt
22 given after they've made the payment. So you could use
23 the date, the time, and then of course the amount, and
24 they did an undercover purchase, and we were able to trace
25 that to the data.

1 So we haven't seen evidence of one, not one
2 transaction that's missing from the data. Not one. And
3 the argument that the check number sequence is the reason
4 for impeaching records, number one, there's nothing in the
5 law, there's nothing in the regulations. There's nothing
6 that says you have to put a transaction number or check
7 number on a receipt given to a customer. What the law
8 says is records need to be adequate for sales and use tax
9 purposes.

10 So, clearly, you would need the date of the
11 transaction, the items that are sold, the amount, the
12 amount of tax you're collecting, if you are in fact
13 collecting tax, and if it was an exempt entity, such as
14 the United States government or if it was somebody that
15 was a resale, you would obviously need the name of the
16 purchaser on the document, on the transaction receipt.
17 But this is a restaurant, so we're not selling to the U.S.
18 government, and we're not selling for resale. So
19 that's -- they're making it up.

20 There's nothing in the laws, the regs that says
21 restaurants have to have transaction numbers. In fact, we
22 found under -- in the Audit Manual under Chapter 5 --
23 Chapter 5 of the Audit Manual is where they describe
24 penalties. So one of the penalties an auditor might
25 impose would be a penalty for negligence in keeping

1 records. And in that section, Chapter 5, it says that --
2 it gives an example that the records only need to be
3 adequate, and that the adequacy of records -- and they
4 even cite the example of a small restaurant, which is
5 really what this is. This is a small single-location
6 restaurant. It's not a conglomerate, that the records
7 would not necessarily be as comprehensive and
8 sophisticated as if you were auditing Apple Corporation.

9 So let's talk for a moment about what records
10 were provided. They got complete POS data. They received
11 income tax returns. They received paid bills invoices,
12 bank statements, 1099-K data. They were given access to
13 the banquet books. They were given -- they had access to
14 sufficient records. But the Department is choosing to
15 impeach records based on the auditor's dining experience
16 and the fact that they claim that they can't trace a
17 transaction to the POS data.

18 So if you don't impeach the records, then the
19 Department really has a problem because the Department
20 will acknowledge and the evidence shows that the POS data
21 materially reconciles to the reported amounts. So that's
22 a key piece for you as a panel to decide. Is it
23 appropriate for the Department to impeach records based on
24 the dining experiences of the auditor in question or the
25 claim that we looked at similar businesses, which by the

1 way, they will never tell you which similar business that
2 they looked at.

3 How is a taxpayer to argue that that's not
4 accurate? We won't tell you which similar businesses
5 we've analyzed, but trust us. They're similar enough.
6 And that's the sole basis for impeaching records? It's
7 nonsense. You're putting taxpayers in extreme jeopardy.
8 If they wanted to impeach the records and they believe
9 that the markup was too low, then they should have
10 followed the policies in the Audit Manual. And what does
11 that say? First thing they should have done is a shelf
12 test.

13 These auditors -- this is really embarrassing.
14 These auditors -- the auditor, the audit supervisor and
15 the principal auditor don't know what a shelf test is.
16 I've been telling them. They didn't do a shelf test, even
17 though they keep referring to a shelf test in their
18 narrative comments. I told them, "You didn't do a shelf
19 test." They're calling -- they looked at purchases and
20 sales for a block of time, and they're calling that a
21 shelf test. That is not a shelf test. They did a test on
22 third quarter '15, and they're calling that a shelf test.

23 A shelf test is where you take commonly sold
24 items, say five or six of the most commonly sold items for
25 the taxpayer, and then you cost the amount. How much

1 chicken went into the chicken chow mein? How much
2 vegetables went into the chicken chow mein? How much oil
3 and spices went into the chicken chow mein? Once you have
4 costed it out based on the quantity that goes into each
5 dish, you then have the direct cost. You could then look
6 at the selling price based on either the menus or what is
7 the selling price in the POS data and calculate a markup.
8 Even to that you would still need to make further
9 adjustments.

10 Why? Because you're going to have spoilage.
11 You're going to have self-consumption. You're going to
12 have waste. You're going to have just inventory shrinkage
13 in general. And in addition to that, you would need to
14 then analyze the cost of goods sold to make sure that cost
15 of goods sold doesn't contain any items that don't belong
16 in cost of goods sold. So they didn't do that. They
17 didn't follow the policies in the Audit Manual. They just
18 made it up as they went along. And they made arguments
19 that the taxpayer has no way of defending, because I have
20 no idea what similar restaurants you're analyzing as your
21 basis for impeaching records.

22 At any rate, three-and-a-half years go by where
23 we're talking about duck-lobster. We get to an appeals
24 conference and at the bottom of the ninth inning with two
25 outs and the Department switches the method on us from

1 duck-duck-lobster to a four-week period where they ask the
2 taxpayer to keep receipts and sales transactions. We
3 didn't argue. We didn't analyze that method because we
4 spent the audit -- the audit wasn't based on that. It was
5 based on duck-duck-lobster.

6 Nonetheless, we didn't agree with it, and a
7 decision came out. We filed an RFR -- timely RFR after
8 the decision came out. The appeals conference auditor
9 claimed that the RFR was filed prematurely because the
10 taxpayer was ordered prepare reaudit working papers. I
11 disagree with her that it was filed prematurely. At any
12 rate, I replied in an email back to her, "Well, when would
13 be the proper time to file an RFR?"

14 She said, "We'll get back to you with a proper
15 time." Next thing I know, instead of getting back to me,
16 we get paperwork to file opening brief and bring our
17 appeal to OTA. So at the bottom of the ninth inning, two
18 outs, they change the method on us, and then they don't
19 give us a chance to respond to that. And now here we are
20 explaining why this new method is also improper when we've
21 been denied the opportunity to argue it in the appeals
22 process previous to this.

23 This new method we also have problems with. This
24 is what's known as an indirect-audit approach. An
25 indirect-audit approach is an audit approach where we're

1 not looking at -- a direct-audit approach would be where
2 you look at the taxpayer's sales journal and compare
3 directly the sales recorded in their sales journals or
4 their POS data to report it and then pick up differences.
5 That would be called a direct approach. An indirect
6 approach is where you have to make estimates, and that's
7 what this is.

8 They asked the taxpayer to keep copies of all
9 receipts for the period October 13th, I believe, to
10 November 18th, and then they calculated a cash to credit
11 card ratio on this block period of time. That test
12 resulted in a roughly 50-50 ratio of cash to credit card
13 sales. Whereas, the taxpayer reported over the audit
14 period a 60-40 ratio, 60 being credit card, 40 being cash.

15 Now, just to provide you my experience. I
16 represented probably nearly 200 Chinese restaurants in
17 appeals. And for a sit-down restaurant with wait staff, a
18 typically cash to credit card ratio is in the ballpark of
19 80-20, 80 percent being credit card, 20 percent being
20 cash. Here we have a taxpayer reporting at 60-40. Why is
21 it 60-40? Why is it so low? Because of the banquet
22 business.

23 Most of the banquet transactions are happening in
24 cash. Why? The taxpayer doesn't want to incur a
25 3 percent charge to a merchant card processor on a large

1 transaction like that, number one. And number two, as
2 anybody who has a credit card knows, is that a customer
3 could do a charge back, even after they've had their
4 banquet. So to preclude the potential fees and risk of
5 loss, they have them, generally speaking, paying cash. So
6 that's what drove the cash to credit card ratio down to,
7 from what I would have expected to see around 80-20, down
8 to 60-40.

9 If I was the auditor and I saw a credit card
10 ratio at a restaurant like this at 60-40, I would have
11 walked away from it. I would have said this isn't worth
12 our time. They're reporting a lot of cash. And let's
13 make no mistake about it. This is an audit of cash sales.
14 Why? The Department already knows what the credit card
15 sales are. They have the 1099-K forms from the merchant
16 card processors. What they don't know is what are the
17 cash sales. So when you have a restaurant -- a sit-down
18 restaurant with a wait staff reporting at 60-40, I would
19 have walked away from it. That's a lot of cash that
20 they're reporting.

21 Second, because this case took so long, the
22 Irvine office selected them for audit a second time. This
23 time I was the representative on the second case from the
24 beginning. We downloaded the data. We got the bank
25 statements, the income tax returns, all the normal books

1 and records. We had a meeting with the auditor. I
2 presented the records to him. The second audit had
3 similar ratios, around 60-40. And discussed with the
4 auditor the pending appeal from the first case.

5 So they knew. The Irvine office and the auditor
6 knew about it. And what was the result of the second
7 audit? It was a -- I'm going to call it a no change, but
8 they called it N-O-W, no opinion warranted. What's the
9 difference? Well, without getting too far off topic, NOW
10 has become an overused vehicle for the Department. Why?
11 Because when they claim that no opinion is warranted,
12 they're trying to close the door on 6596 claims, claims of
13 reliance on erroneous written advice.

14 When I was an auditor, if you were going to waive
15 an audit, you had eight hours to do it. Which means that
16 you did a cursory review and you decided after a cursory
17 review it wasn't worth the State's time to conduct a
18 full-scale audit. So I don't know exactly how much time
19 the second auditor put on the case, but we had a meeting
20 in my office. We had some back and forth, and then the
21 next thing you know I get a NOW letter.

22 But make no mistake about it. They knew -- they
23 knew about the prior audit. They knew the issues. They
24 had a similar cash to credit card ratio, and they decided
25 this isn't worth -- there's nothing here. Now, the

1 appeals conference auditor claims that the fact that
2 there's a NOW is that the Department is taking no
3 position. That's nonsense. They looked at all of the
4 data. They looked at the records.

5 I had -- I was with them in my office for two
6 hours, and the Department is picking up almost \$200,000 in
7 tax. So they would just walk away from that if they
8 thought there was a problem? They're making a statement.
9 They're saying there's nothing here.

10 JUDGE BROWN: And I'll just mention you have
11 about five minutes left.

12 MR. BRANDEIS: Okay. I'm going to close it up by
13 saying looking at -- sort of doing a recap of what
14 procedures were done. Bank deposit analysis, no errors
15 noted, no disclosure of any kind that there's
16 underreporting. They refused to do an observation test.
17 Now they're going to say we refused to do it. And that
18 may have happened in the discussion with the prior rep,
19 but at some point, that issue came up with me. And as you
20 can see in Exhibit 25, I asked the auditor why are you not
21 doing an observation test? Why are you doing this
22 duck-duck-lobster method, which is a method that you guys
23 made up yourself?

24 It's not in the Audit Manual. If you're going to
25 deviate from the Audit Manual, wouldn't you document as to

1 why. Why are you deviating from all these methods that
2 are documented in the Audit Manual? And to make short of
3 it, his response to me is, "We can do," -- "I can do what
4 I want. I'm the auditor. It's up to me. I can do what I
5 want." To me that -- auditors are granted a tremendous
6 amount of leeway, but they -- they don't have absolute
7 power. This isn't a dictatorship.

8 They have an Audit Manual. There are guidelines
9 in the Audit Manual. And if they're going to deviate from
10 them -- maybe he had a reason to deviate from them, but
11 you should document it. Why? Why are we deviating from
12 the established procedures in the Audit Manual? The
13 answer should never be "because I can." So for the --
14 this panel to rule in favor of the Department, you're
15 going to have to agree that it's okay to impeach records
16 based on your dining experience, or we looked at similar
17 establishments, but we won't tell you what they are.
18 There's no way for a taxpayer to counter those claims
19 because I have no idea what you're looking at.

20 In addition to that, you also have to agree that
21 it's okay for the Department to violate the rules in the
22 Audit Manual, just totally disregard them. Because when
23 you do base an audit on an indirect approach, what the
24 Audit Manual says is that, "You must," -- they use the
25 word must. That's a very unforgiving word, must. They

1 use the words, "You must have a secondary approach that
2 substantiates the first." They don't. They don't have a
3 secondary approach. So you have to agree that it's okay
4 that they don't -- they violated that rule as well.

5 And then we get to the decision. When the
6 Appeals Bureau holds a hearing, they have 90 days from the
7 hearing date or the close of post-conference submissions
8 to issue a decision. They can get an extension, but they
9 need permission to do that from the chief counsel. This
10 decision was issued 135 days after the last
11 post-conference submission with no approval from the chief
12 counsel. They broke the rules again. What's the remedy?
13 It doesn't describe a remedy in the rules for tax appeals.
14 And I've been asked, "Well, what remedy are you seeking?"

15 You know, I would choose the remedy that would be
16 the remedy if we failed to timely file petition for
17 redetermination, which is that you throw the case out. I
18 believe our case is so strong as it is we don't need to
19 have it thrown out on a technicality. But also, why would
20 you let the Department break all these rules and have
21 absolutely zero consequences for it?

22 That concludes our opening statement.

23 JUDGE BROWN: Thank you very much.

24 And now we may have questions from the panel.

25 Panelists, do you want to -- Judge Wong, do you

1 want to proceed with questions?

2 JUDGE WONG: Sure. I just had a couple. Sorry
3 feedback. I had a couple of questions for the witness
4 regarding just the restaurant. How many seats or tables
5 does the restaurant have -- or did the restaurant have
6 during the audit period? I think it was around 2011 to
7 2014.

8 MS. LAI: About 40 tables.

9 JUDGE WONG: 40 tables. And how many seats
10 total?

11 MS. LAI: 250.

12 JUDGE WONG: 250. Okay. And also, Mr. Brandeis
13 had mentioned the Appellant only has one restaurant. I
14 was just wondering because on the invitation to your
15 wedding it mentions a Seafood Cove No. 2. Is there a
16 No. 1?

17 MS. LAI: Yes, but Number 1 is separately owned.

18 JUDGE WONG: Okay. Is there a Number 3? Just --

19 MS. LAI: No.

20 JUDGE WONG: Okay. The last question is actually
21 for Mr. Brandeis. You mentioned injunction relief. Do
22 you have any cite or authority for that remedy that you're
23 seeking?

24 MR. BRANDEIS: No, I don't. The rules for tax
25 appeals doesn't describe it. It says that, "A decision

1 must be issued within that 90-day frame, unless they get
2 permission, which they must get approval from chief
3 counsel," which they didn't do. There's no remedy
4 described in that law section or in that regulation. So I
5 would just be making it up if I were to propose -- I -- I
6 can propose one, but it's just my opinion.

7 JUDGE WONG: Thank you. No further questions at
8 this time.

9 JUDGE BROWN: Thank you.

10 Oh, I realize I did forget to CDTFA if they had
11 any questions for the witness.

12 MR. SAMARAWICKREMA: No, we don't have any
13 questions for the witness.

14 JUDGE BROWN: Okay. Thank you very much.

15 Judge Lambert, do you have any questions.

16 JUDGE LAMBERT: I don't have any questions at
17 this time. Thanks.

18 JUDGE BROWN: Okay. Thank you.

19 I think I may have some questions. Hold on just
20 a minute. I have a question for the witness.

21 From what I can see in the records, there weren't
22 any contracts for the banquets produced. Did you have
23 your customers, when they're going to have a banquet, did
24 they sign contracts?

25 MS. LAI: Yes, we have contracts for everything,

1 for wedding banquets. Can -- can you address that?

2 MR. BRANDEIS: So they have a banquet book, and
3 they do have written contracts. And they -- she brought
4 it our meeting, and it looks like they write in the date
5 and what not. And I don't know if you keep the actual
6 contracts in a separate file. But the Department had
7 these books, and each wedding or each event has --
8 remember I described they had a tablecloth method.

9 So, for example, I'm having a wedding. My colors
10 for my wedding are purple and white. So all the
11 tablecloths are going to be purple. So you can see it in
12 their emails and even in some of the narrative comments in
13 the original audit. They're referencing a tablecloth
14 approach, which is where they try to count the number of
15 tablecloths based on the color of the tablecloth matching
16 it to -- they wrote the color in the contract. So the
17 Department had this information. It ultimately didn't go
18 anywhere. My hunch is they couldn't find anything wrong.

19 JUDGE BROWN: So but my question is the producing
20 of the contracts for the banquets. I guess part of what
21 I'm interested in is if there were any provisions in the
22 contracts about whether payment would by cash or check or
23 credit card.

24 MS. LAI: So we do deposits by cash so we can
25 record the actual sale on the actual wedding day. And

1 then the night of the banquet is paid with cash or credit
2 card, the balance.

3 JUDGE BROWN: And you accept either cash or
4 credit cards for the balance?

5 MS. LAI: For the balance, correct.

6 JUDGE BROWN: Okay. And I guess I'm wondering
7 then, why haven't I seen any of that in the evidence in
8 either Appellant's evidence or CDTFA's evidence. There is
9 no -- I haven't found -- I might be missing it but --

10 MR. BRANDEIS: They dropped this issue.
11 Initially, the auditor tried to do -- again, I wasn't
12 there. This was with the first representative. But if
13 you read the narrative comments in the original audit,
14 they tried to do some kind of analysis with the banquet
15 books, the banquet contracts, and then comparing that to,
16 I believe, orders that they had received.

17 Because the tablecloths themselves, do you order
18 that from a linen service?

19 MS. LAI: Yes.

20 MR. BRANDEIS: Okay. So my understanding is they
21 tried to look at contracts with the linen service to
22 see -- I'm assuming they were looking for contracts with
23 orders from the linen services that don't have a
24 corresponding contract in the banquet book. And like I
25 said, this didn't go anywhere. They dropped that,

1 ultimately, and decided to go with duck-duck-lobster.

2 JUDGE BROWN: Okay. Thank you. Oh, and I also
3 wanted to just confirm with Mr. Brandeis, I think.

4 Part of your argument is that, as I understand
5 it, is that two days should be removed from the
6 credit-card ratio calculation because they were skewed by
7 payments by cash or check?

8 MR. BRANDEIS: So I ran an analysis. There -- I
9 looked -- I ran a filter on that test period, and I
10 found -- I -- I looked for transactions over \$5,000. Why?
11 I just picked that number. There were some that were in,
12 I want to say, in the 3 or \$4,000, but I just chose \$5,000
13 as a cut off. There aren't very many transactions for
14 that high dollar. Because as you can imagine, most of the
15 transactions are below \$200. And we found over \$5,000 --
16 I'm going off memory. I want to say it was two
17 transactions in that four-week period.

18 So then I looked at the audit period in question,
19 and I ran a similar filter on the data in the audit period
20 in question. And I'm expecting to see, are we going to
21 see roughly, you know, two transactions over \$5,000 for
22 each month, and the answer was no. It's way less.

23 So what happened was the period that they chose
24 to base this audit on just happened to be -- it was skewed
25 because if you get just one extra banquet in there for a

1 significant amount, it can skew the results of the whole
2 test and, therefore, it's not representative, which is why
3 the Audit Manual says, "If you're using an indirect
4 approach, you have to back it up with something else."
5 Which, again, they didn't do.

6 They're calling their second approach -- they
7 took the resulting additional taxable sales that they came
8 up with and then they recalculated a markup. Obviously,
9 they're going to get a higher markup based on the new
10 audit result. They're calling that the second approach.
11 That's -- that's absolutely false.

12 JUDGE BROWN: So --

13 MR. BRANDEIS: There's several second approaches
14 described in the Audit Manual Chapter 8, and that's not
15 one of them.

16 JUDGE BROWN: So is it my understanding that
17 you're arguing that --

18 MR. BRANDEIS: It's not representative.

19 JUDGE BROWN: All right. The two banquets in a
20 four-week period is not typical?

21 MR. BRANDEIS: Is not typical.

22 JUDGE BROWN: Can I ask the witness, how many
23 banquets do you typically do per month?

24 MS. LAI: It's hard to say. There are some
25 months that have more and some months have none.

1 MR. BRANDEIS: So we provided -- we calculated
2 based on reported amounts the cash to credit card ratio.
3 That's in one of our exhibits. I believe that's
4 Exhibit 5. Hold on. Oh, it was provided in our opening
5 brief. And in the opening brief, we calculated the
6 reported cash to credit card ratio for both the first
7 audit period and the second audit period. And you can see
8 it's all over the map. It -- it swings wildly. It went
9 from a high of around say 60, 65 percent credit card to a
10 low of around 53, 54 percent. It's an exhibit in our
11 opening brief. So --

12 JUDGE BROWN: You put it in your exhibits -- in
13 your exhibits that we have marked.

14 MR. BRANDEIS: Well, we've given it to the
15 Department. We submitted it as an RFR to the Appeals
16 Bureau. And when we filed the opening brief with OTA, we
17 included it as an exhibit there.

18 JUDGE BROWN: Briefs are still, you know, they're
19 still what I consider, and I don't think it's a problem if
20 it's not admitted into evidence because it sounds like
21 it's part of your argument.

22 MR. BRANDEIS: Its part of the argument.

23 JUDGE BROWN: Got it. Okay. Anyway, I don't
24 know if you had finished your response.

25 MR. BRANDEIS: Yeah. The point being is that the

1 test is not representative. The chart that we provided in
2 the exhibit shows for both audit periods, a quarterly cash
3 to credit card ratio. And, again, you can see the
4 variation from one quarter to the next. So if we pick
5 a -- if you get unlucky and you just happen to pick a
6 period where you have one too many banquets, yeah, it can
7 skew the results wildly when you're looking at such a
8 short period of time. In this case we're not even looking
9 at a quarter. We're looking at a month.

10 So, again, what does the Audit Manual say? You
11 got to have a secondary approach to back it up. There is
12 none. So, again, for this panel to rule against this
13 taxpayer, you have to agree that no secondary approach is
14 necessary. You can impeach records based on your dining
15 experiences. I mean, this isn't even really an audit, in
16 my opinion.

17 JUDGE BROWN: And I noticed that -- I just wanted
18 to confirm the two days that you're arguing should have
19 been removed from the test period.

20 MR. BRANDEIS: Well, one -- one of those days
21 after -- I went back and looked at it. So one of the days
22 you'll notice that there was like \$10,000.

23 JUDGE BROWN: Is that November 2nd, 2014?

24 MR. BRANDEIS: I think so. Let me -- actually,
25 you know what, the ratio we provided is -- it is in the

1 list of exhibits. Wait a second. I'm -- it's Exhibit 3.
2 So it is in the record.

3 JUDGE BROWN: Okay.

4 MR. BRANDEIS: There were two days. So one of
5 the days was November 2nd and you see the check amount is
6 \$10,587. I thought that was a banquet. But once I went
7 back to the data and filtered for that day, somebody -- an
8 employee at the restaurant -- instead of using the cash
9 key to tender payment, they were using the check key to
10 tender the payment. So that actually is not a banquet on
11 November 2nd. And if you look cash on that day is \$2,800.
12 So somebody was just using the wrong key.

13 But there were two transactions in that block
14 period over \$5,000. And when you run that same filter
15 over the audit period, you're not going to find -- the
16 audit period has 36 months, you're not going to find 72
17 transactions over \$5,000. So they just got unlucky. They
18 got a period rich in banquets, and one of those banquets I
19 want to say was for an amount higher than normal banquets.
20 I want to say it was \$15,000. I don't know.

21 What is your typical banquet? Well, going back
22 seven years ago, what would have been your -- okay. If
23 you don't remember that's fine.

24 JUDGE BROWN: So let me just check. So are there
25 still two days that you're arguing are skewed from that

1 period?

2 MR. BRANDEIS: Well, I would modify the argument.
3 There's -- I would have analyzed this taxpayer separately
4 by separating out banquet transactions from regular
5 restaurant transactions and then analyze them separately.
6 But in the data period there are two dates -- there are
7 two transactions over \$5,000, which I'm calling a banquet.
8 And when you run that similar test over the audit period
9 there's nowhere -- you would expect to see 72 transactions
10 over \$5,000. There's nowhere near that.

11 JUDGE BROWN: And those two --

12 MR. BRANDEIS: And so the result -- the result is
13 that test period is skewed. It's not representative.

14 JUDGE BROWN: And those two days are -- is it
15 still November 2nd, 2014?

16 MR. BRANDEIS: If you give me a second, I'll --

17 JUDGE BROWN: Sure. I'll tell you what. You
18 can -- why don't we pick it up on your rebuttal.

19 MR. BRANDEIS: Okay.

20 JUDGE BROWN: All right. Let me see if I have
21 anything else. Okay.

22 Judge Lambert, did you have any questions for the
23 Appellant?

24 JUDGE LAMBERT: No. Not at this time.

25 JUDGE BROWN: Oh, I'm sorry. It was Judge Wong.

1 JUDGE WONG: Hi. Just a few more questions.
2 Sorry. Hi. Just a few more questions regarding the
3 operations of the restaurant regarding banquet. Were
4 banquets pretty consistent throughout the year, or is it
5 seasonal? Are there times where there's more banquets,
6 like holidays or graduation or whatnot?

7 MS. LAI: It's -- well, during graduations. But
8 I think the banquets we're talking about are more wedding
9 banquets. Those are really hard to say. Sometimes
10 certain years have more banquets than other years.

11 JUDGE WONG: Do these banquets usually reserve
12 the entire restaurant, all 40 tables or do they sometimes
13 get -- reserve part of the restaurant?

14 MS. LAI: It's both. So sometimes it partial
15 restaurant, and sometimes it's the whole restaurant.

16 JUDGE WONG: Do you have a set banquet menu.

17 MS. LAI: Yes.

18 JUDGE WONG: Do you recall around 2011
19 through 2014, the period we're talking about, what the
20 options for the banquet menus were or, like, the prices
21 per table?

22 MS. LAI: I don't remember. Prices have changed.

23 JUDGE WONG: Okay. What are they now? Just
24 curious.

25 MS. LAI: Our lowest is \$428 per table, and then

1 our highest is 6 -- no -- \$718 per table. I can't
2 remember. I'm sorry.

3 JUDGE WONG: That's fine. And that's per -- 10
4 seats per table?

5 MS. LAI: Correct.

6 JUDGE WONG: Okay. I just had a question about
7 Seafood Cove No. 1. Do you know the ownership of that
8 restaurant? Are they related somehow to the ownership of
9 Seafood Cove No. 2?

10 MS. LAI: It was sold to a family member.

11 JUDGE WONG: I see.

12 MS. LAI: Or a family member owns that one, and
13 then --

14 JUDGE WONG: Okay. Are you familiar with the
15 operations of Seafood Cove -- no?

16 MS. LAI: No. I'm not involved in the operations
17 at all.

18 JUDGE WONG: Okay. No further questions. Thank
19 you.

20 MS. LAI: Thank you.

21 JUDGE BROWN: Okay. Then thank you.

22 I think we've concluded with questions for
23 Appellant at this point. And so I will now turn to CDTFA.

24 If CDTFA is ready to make its presentation, you
25 have 30 minutes whenever you're ready.

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1 Department's rules for appeals, Section 35065 subdivision
2 (b) .

3 Appellant contends that the late mailing of the
4 decision effects the adequacy of the Department's notice.
5 However, the Department's notice of Appellant's liability
6 is contained in the Notice of Determination. There's no
7 dispute that the Notice of Determination in this case was
8 issued timely. Therefore, the adequacy of notice was not
9 affected by the late mailing of the decision, which
10 occurred years after the Notice of Determination was
11 timely issued. Therefore, the Department's position is
12 that the Office of Tax Appeals does not have jurisdiction
13 to determine the appropriate remedy for the late mailing
14 of the decision.

15 The proper remedy for the late mailing of a
16 decision is the relief of interest. According to
17 Revenue & Taxation Code Section 6593.5 subdivision (c) and
18 Regulation 35049, interest may be relieved where the
19 taxpayer was charged interest due to an unreasonable error
20 or delay by the Department staff acting in his or her
21 official capacity.

22 Here, the Department has determined that there
23 was an unreasonable error or delay by Department staff
24 that caused interest to accrue. Accordingly, the
25 Department has recommended relief of the interest that

1 accrued during the period of delay, which was
2 February 8th, 2019, through May 8th, 2019. The relief of
3 interest will only be granted when Appellant submits the
4 requisite statement under the penalty of perjury to
5 request relief from interest and sets forth the facts on
6 which the request is made.

7 Similarly, whether the Department engaged in ex
8 parte communication during the appeals proceeding also
9 falls outside the jurisdiction of the Office of Tax
10 Appeals because this also details with alleged violations
11 of due process. According to Regulation 35064 subdivision
12 (a), the appeals conference will be held by an Appeals
13 Bureau conference holder who has not had any prior
14 involvement in the appeal being discussed at the appeals
15 conference.

16 It is the responsibility of the Appeals Bureau to
17 consider the contentions presented by the parties, gather
18 the applicable facts, conduct any investigations it deems
19 warranted, and analyze and apply the law to the facts as
20 determined by the conference holder in order to make an
21 objective determination of the correct resolution of the
22 appeal.

23 Subdivision (c) (2) states that at Appeals Bureau
24 may request that a party submit additional written
25 argument or documentation. And when it does so, will

1 inform the party when the requested submission is due.
2 The Appeals Bureau will determine whether a response
3 should be submitted by another party and, if so, will
4 advise that party when the response is due. While the
5 Appeals Bureau strides to keep communications with the
6 parties to an appeal open and transparent, the
7 Department's regulation do not specifically prohibit ex
8 parte communication and do not provide any sanctions when
9 it does happen.

10 Moreover, regardless of Appellant's contentions
11 regarding the Department's handling of the matter through
12 the appeals process, Appellant is now getting a de novo
13 hearing before the Office of Tax Appeals, which is an
14 independent trier of fact.

15 MR. SAMARAWICKREMA: Appellant is a California
16 corporation that operates a full-service dining restaurant
17 specializing in Chinese-style cuisine in Westminster,
18 California. The restaurant is open daily from 8:30 a.m.
19 to 8:00 p.m. Appellant's serve dim sum for breakfast and
20 lunch and offer a separate menu for dinner. Appellant
21 also serves liquor and provides banquets for weddings and
22 special occasions.

23 The Department audited Appellant's business for
24 the period July 1st, 2011, through June 30th, 2014.
25 During the audit period, Appellant reported taxable sales

1 of around \$10.3 million, and that will be on your
2 Exhibit A, page 29. During my presentation I will explain
3 why the Department rejected Appellant's reported taxable
4 sales, why the Department used an indirect-audit approach,
5 and how the Department determined Appellant's unreported
6 sales tax for the audit period.

7 JUDGE BROWN: Can I interrupt just for a minute
8 to say I'm having a little trouble hearing you. Is your
9 microphone on?

10 MR. SAMARAWICKREMA: Yeah.

11 JUDGE BROWN: Okay. Thank you very much. Sorry
12 to interrupt. Go ahead.

13 MR. SAMARAWICKREMA: During the audit, Appellant
14 failed to provide complete sales records. Appellant did
15 not provide complete documents of original entry, such as
16 actual POS downloads, report folders, POS sales receipts,
17 credit card sales receipts, guest checks, the dim sum
18 cards, or dim sum sales tickets, or copies of contracts
19 and booking documents for banquet sales for the audit
20 period. In addition, Appellant failed to provide complete
21 purchase invoices or purchase journals for the audit
22 period.

23 The Department did not accept Appellant's
24 reported taxable sales due to lack of reliable records,
25 low reported book markups, and high credit card sales

1 ratios. It was also determined that Appellant's record
2 was such that sales could not be verified by a direct
3 audit approach. Therefore, the Department determined
4 audited sales using credit card sales ratio approach for
5 the audit period. The Department completed four
6 verification methods to evaluate the reasonableness of
7 Appellant's reported taxable sales.

8 First, the Department mailed its engagement
9 letter to Appellant on January 24th, 2014, to inform the
10 Appellant that its account has been selected for an audit.
11 And that will be on your Exhibit A, page 22. Appellant
12 filed sales and use tax returns for fourth quarter 2013,
13 first quarter 2014, and second quarter 2014 after the
14 Department's mailed its engagement letter. The Department
15 analyzed Appellant's reported taxable sales for the audit
16 period. And that will be on your Exhibit A, page 29.

17 The Department noted an average reported daily
18 sale of around \$8,800 ranging from as low as \$8,000 to as
19 high as \$9,400 for the period July 1st, 2011, through
20 September 30th, 2013. However, after the notice of the
21 audit, Appellant increased its average reported daily
22 sales by around \$2,500 per day. Appellant reported
23 average daily sale of around \$11,100 for fourth quarter
24 2013, \$11,000 for first quarter 2014, and \$11,900 for
25 second quarter 2014.

1 Based on the four-week test, Appellant's average
2 recorded daily sales of around \$11,300 ranging from as low
3 as \$4,200 to as high as \$27,200. And that will be on your
4 Exhibit A, pages 41 through 43. This is an indication
5 that not all of Appellant's sales had been reported in its
6 sales and use tax returns.

7 Second, the Department compared reported taxable
8 sales of around \$6.6 million to cost of goods sold of
9 around \$3 million reflected on Appellant's 2012 and 2014
10 federal income returns and calculated an overall reported
11 bookmark up of around 124 percent. And that will be on
12 your Exhibit C, page 308. However, based on the items
13 sold, menu prices, customer base, services provided, and
14 the location of the restaurant, the Department expected to
15 see a higher bookmark up than the reported book markup for
16 a full-service restaurant with a banquet facility and
17 license for sale of alcoholic beverages. And that will be
18 on your Exhibit F, page 345, line 15 and line 16.

19 Third, Appellant did not provide its complete POS
20 download for the audit period. Appellant claimed that its
21 POS system was crashed on or before October 9th, 2014, and
22 sales records prior to the year 2014 were not available on
23 the POS system. And that will be on your Exhibit B, pages
24 91, 92, Exhibit C, pages 305 and 306, and Exhibit 24,
25 page 40. However, Appellant provided POS download for the

1 period January 1st, 2014, through June 30th, 2014, and
2 guest checks for March 2014. Appellant also provided an
3 Excel copy of the sales records for the year 2013. And
4 that will be on your Exhibit B, pages 91, 92, and
5 Exhibit C, pages 305 and 306.

6 At the time of the field work, sales records
7 prior to year 2013 were not available from the Appellant.
8 And that will be on your Exhibit B, pages 91, 92, and
9 Exhibit C, pages 305 and 306. The Department reviewed and
10 analyzed Appellant's POS download with printed guest
11 checks provided by Appellant for March 2014. The
12 Department noted that the Appellant turned off the POS
13 check counter function and, therefore, Appellant's guest
14 checks were not numbered making it practically impossible
15 to determine if all sales were included in its POS sales
16 information.

17 Appellant also did not provide the cards used to
18 record sales of dim sum dishes or banquet contracts for
19 the audit period. The Department finds that the failure
20 to assign guest check numbers in conjunction with the
21 other evidence, is also an indication that Appellant did
22 not report all its sales in the sales and use tax returns.

23 Fourth, Appellant did not provide complete sales
24 information for the audit period. Therefore, the
25 Department obtained Appellant's credit card sales

1 information for the audit period from its internal
2 sources. And that will be on your Exhibit A, pages 48
3 through 51. The Department compared the reported total
4 sales to credit card sales and calculated an overall
5 credit card ratio of around 60 percent, ranging from as
6 low as 54 percent to as high as 65 percent for the
7 audit percent. And that will be on your Exhibit A,
8 page 54.

9 Based on his experience in audit of similar
10 restaurants in Appellant's area, the Department viewed
11 this has a high credit card sales ratio for a restaurant
12 selling alcoholic beverages and providing banquets for
13 wedding and special occasions. This is an indication that
14 not all of Appellant's cash-sales transactions had been
15 reported in its sales and use tax return for the audit
16 period. In contrast, based on the four-weeks sales
17 information, the calculated credit card sales ratio was
18 around 51 percent which is the Department determined to be
19 a more reasonable credit card sales ratio. And that will
20 be on your Exhibit A, pages 41 through 43.

21 Appellant was unable to explain the reason for
22 low average reported sales, low reported book markups, and
23 high reported credit card sales ratios. Therefore, the
24 Department conducted further investigation by analyzing
25 Appellant's purchase information, pricing policies, credit

1 card sales, credit card sales ratios, and credit card tip
2 ratios. The Department requested Appellant to provide the
3 purchase information for the four-week test period,
4 Saturday, October 18th, 2014, through Thursday,
5 November 13, 2014. Appellant did not provide the purchase
6 information for the test period.

7 The Department also requested Appellant to
8 provide the POS download for the four-week test period,
9 Saturday, October 18th, 2014, through Thursday,
10 November 13, 2014, and have the POS check counter function
11 turned on to record the sequential number of all guest
12 checks. And that will be on your Exhibit A, pages 22 and
13 23. The Department also made a controlled purchase on
14 October 26th, 2014, to verify the completeness of the
15 four-week test period. And that will be on your
16 Exhibit 8.

17 The Department then, with the assistance of
18 Appellant, downloaded its POS system for the period
19 Saturday, October 18th, 2014, to Thursday, November 13th,
20 2014, and verified with a sequential numeric gift check.
21 The Department reviewed the test period and notes two
22 days, Saturday, October 25th, 2014, and Sunday,
23 November 2nd, 2014, which include one large cash payment
24 and one large check payment.

25 The Department determined that these large cash

1 and check payments were for banquet services. A review of
2 Appellant's bank statements for year 2013 show large cash
3 and check deposits in April 2013 and October 2013.

4 Moreover, Appellant's Exhibit 4 show similar large check
5 deposits in third quarter 2011, fourth quarter 2011, third
6 quarter 2012, fourth quarter 2012, first quarter 2013, and
7 second quarter 2014.

8 Based on this evidence, the Department determined
9 that Appellant's banquet customers often pay for events in
10 cash or by check, and that these events occur regularly.
11 Therefore, the Department concluded that the two large
12 payments during the four-week test period were
13 representative of the audit period. And that information
14 obtained from the test period was reasonable to calculate
15 its credit card sales ratio.

16 Based on the four-week sales information, the
17 Department calculated and audited credit card sales ratio
18 of around 51 percent ranging daily from as low as
19 12 percent to as high as 60 percent. And that will be on
20 your Exhibit A, pages 41 to 42. The Department also noted
21 average daily sale of around \$11,300 ranging as low as
22 \$4,200 to as high as \$27,200. And that will be on your
23 Exhibit A, pages 41 through 43.

24 The Department calculated the credit card sales
25 tip percentage of around 9 percent using available sales

1 information for the audit period. And that will be on
2 your Exhibit A, page 46. During the field work, Appellant
3 failed to provide credit card merchant statements or
4 1099-K forms to calculate credit card sales for the audit
5 period. Therefore, the Department obtained Appellant's
6 credit card sales information for the period
7 July 1st, 2011, through June 30th, 2014, from the
8 Department's internal sources. And that will be on your
9 Exhibit A, pages 48 to 51.

10 Then the Department used a total credit card
11 sales of around \$7.3 million for the audit period, audited
12 credit card sales ratio of around 51 percent, a credit
13 card tip ratio of around 9 percent and applicable sales
14 tax rate factors to determine audited taxable sales of
15 around \$12.1 million. And that will be on your Exhibit A,
16 pages 40 and 44. The Department then compared the audited
17 taxable sales for the audit period to report a taxable
18 sale of around \$10.33 million to compute unreported
19 taxable sales of around \$1.8 million. And that will be on
20 your Exhibit A, page 39.

21 Had the Department used the audited average daily
22 sale of \$11,900 and 1,095 operating days for the audit
23 period to determine audited taxable sales, this would
24 increase the audited taxable sales by around \$900,000 from
25 \$12.1 million to \$13 million for the audit period. In

1 addition, Appellant's sales receipts disclose that
2 Appellant added another 15 percent to sales receipt as
3 mandatory for large parties of 15 people or more.
4 Appellant did not charge sales tax on amount charged to
5 customers for mandatory tips it added to the guest checks.

6 These tips are taxable as these tips amount
7 automatically added by Appellant to the guest check
8 presented to and paid by the customer is a mandatory
9 charge. Based on March 2014 sales information, the
10 Department calculated an audited mandatory tip of
11 0.3 percent. And that will be on your Exhibit B,
12 page 108. The Department determined the mandatory tip of
13 around \$31,000 using mandatory tip rate and reported sales
14 instead of audited sales to give a benefit of around
15 \$6,000 to Appellant. And that will be on your Exhibit A,
16 page 47 and 55.

17 In total the Department determined unreported
18 taxable sales of around \$1.9 million dollars, and that
19 will be on your Exhibit A, page 38. The Department then
20 compared the unreported taxable sales with the reported
21 taxable sale of around \$10.3 million to calculate the
22 error rate of around 18 percent for the audit period.

23 Appellant believes it reported the correct amount
24 of sales tax on its sales and use tax return for the audit
25 period. As support, Appellant provided its POS sales

1 information in Excel work sheets for the audit period.
2 The Department reviewed and analyzed this information and
3 ultimately rejected them. Upon examination of Appellant's
4 Excel POS sales information, the Department noted that the
5 Appellant did not provide actual POS download with all
6 folders, guest check, credit card sales receipts, cards
7 used to record sale of dim sum dishes and banquet
8 contracts to collaborate the figures listed in this Excel
9 sales information.

10 Therefore, the Department was not able to verify
11 the completeness and recordkeeping accuracies of
12 Appellant's Excel POS information. Based on 2013 sales
13 and purchase information, the Department noted Appellant
14 did not record more than 20 percent of Appellant's lobster
15 and duck sales into his sales reports. And that will be
16 on your Exhibit B, page 104.

17 JUDGE BROWN: And I'll just mention I think you
18 have about five minutes left. Go ahead.

19 MR. SAMARAWICKREMA: The Department also reviewed
20 and analyzed Appellant's subsequent no warranted report
21 finding for the period October 1st, 2014, through
22 September 30th, 2017, and that will be on your Exhibit I.
23 According to Department's records, this report was
24 completed and approved on July 9th, 2018. The Department
25 noted Appellant reported more than \$1 million sales per

1 year during the subsequent audit period. And that will be
2 on your Exhibit C, page 309, and Exhibit I, page 396.

3 Appellant also reported more than \$100,000 net
4 profit per year during the subsequent audit period. And
5 that will be on your Exhibit C, page 309 and Exhibit I,
6 page 396. The Department also noted that the reported
7 credit card sales ratio of around 58 percent ranging from
8 as low as 53 percent to as high as 62 percent for the
9 period October 1st, 2014, to September 30th, 2017. And
10 that will be on your Exhibit I, page 390.

11 Since the Department now has two different credit
12 card sales ratios of around 51 percent for year 2014 and
13 60 percent for year 2017, the Department is able to
14 mathematically determine Appellant's credit card sales
15 ratios for years 2011, 2012, and 2013 using compound
16 annual growth rate formula. And that will be on your
17 Exhibit A, page 53. Based on the compound annual growth
18 rate formula, the Department mathematically determined the
19 credit card sales ratio of 44 percent for year 2011, 46
20 percent for year 2012, and 49 percent for year 2013. And
21 that will be on your Exhibit A, page 53.

22 If the Department used these credit card sales
23 ratios, this would increase the audited taxable sales by
24 around \$1 million from \$12.1 million to \$13 million for
25 the audit period. And that will be on your Exhibit A,

1 page 52. The Department did not perform a re-audit to
2 account for the additional understatement of around \$1
3 million. And that will be on your Exhibit A, page 52.
4 The amount assessed in this audit is reasonable and
5 benefits Appellant.

6 Appellant says that the Department did not do any
7 alternate audit methods to support the unreported sales
8 based on credit card sales and credit card sales ratio.
9 The Department could not perform any other alternate audit
10 methods other than the original audit method of using
11 lobster and duck purchases and recorded sales to estimate
12 unreported taxable sales. Audited sales using average
13 audited daily sales and number of operating days and the
14 post-audited markup using audited sales and available cost
15 of goods sold reflected on Appellant's federal income tax
16 returns because Appellant did not provide complete sales
17 and purchase information for the audit period. And that
18 will be on your Exhibit B and Exhibit H.

19 Appellant cites Exhibit 11 and Exhibit 12 in its
20 argument, which is a Board of Equalization decision and a
21 decision and recommendation for a different taxpayer, for
22 a different audit period with a different set of facts.
23 And that will be on your Exhibit 22, page 33. Conclusion
24 made in another audit is not evidence and have no
25 precedential value in this appeal. Appellant add the

1 arguments only as a perception of what happened during the
2 other unrelated audits. And that will be on your Exhibit
3 18, Exhibit 19, and Exhibit 20.

4 These arguments do not establish that the
5 Department's ultimate determination was unreasonable or
6 lack any rational basis. For example, Appellant does not
7 dispute the sufficiency of the evidence the Department
8 used to determine Appellant's total taxable sales, no
9 actual calculation of the audit liability. The audit
10 calculation of unreported taxable sales based on the
11 credit card sales and four-week sales information was
12 reasonable and was in Appellant's favor since it was the
13 lowest of the differences determined.

14 Ultimately, the Department decided to use an
15 audit method, which is the lowest deficiency measured to
16 give a benefit to the Appellant. As mentioned earlier,
17 Appellant did not provide complete source documentation,
18 such as POS download, POS sales receipt, guest checks,
19 credit card sales receipts, the dim sum cards or dim sum
20 sales tickets, and copies of contracts for banquet sales.

21 JUDGE BROWN: CDTFA, if I can interrupt and say
22 it is your time. How much more time do you need?

23 MR. SAMARAWICKREMA: Another two minutes.

24 JUDGE BROWN: Okay. Go ahead.

25 MR. SAMARAWICKREMA: Appellant did not complete

1 purchase invoices. Appellant failed to provide
2 documentary evidence to support his taxable sales for the
3 audit period. The Department was unable to verify the
4 accuracy of reported sale tax using a direct audit method.
5 Therefore, an alternative audit method was used to
6 determine unreported sales tax.

7 Accordingly, the Department determined the
8 unreported sales tax based upon the best available
9 information. The evidence shows that the audit produced
10 fair and reasonable results. Appellant has not provided
11 any reasonable documentation or evidence to support an
12 adjustment to the audit finding. Therefore, the
13 Department requests the appeal be denied.

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

16 JUDGE BROWN: Thank you.

17 I will ask my co-panelists if either want to
18 start with questions for CDTFA? Go ahead.

19 JUDGE WONG: Hi. Appellant's representative had
20 questioned the expected markup of 160 percent claiming
21 that the auditor had based this on personal experience
22 eating at -- own personal experience eating at Chinese
23 restaurants. Could you address that argument?

24 MR. SAMARAWICKREMA: We disputed taxpayer's
25 record not only based on the markup. Markup was low.

1 It's only 124 percent based on two-year information, but
2 there were other reasons behind. For example, the average
3 daily sales were increase by \$2,500 per day after the
4 Department sent the engagement letter. The credit card
5 sales ratio was also high compared to the other
6 restaurants. So the typical -- the markup for these types
7 of restaurants should be more than 124 percent.

8 MR. BACCHUS: And if I can just supplement that
9 response. In general, as you can imagine, the Department
10 audits many different types of restaurants and compiles
11 data based on specific industries and specific types of
12 restaurants. So in the Department's experience -- and I
13 use the Department the audit staff as a whole -- they
14 expect to see certain markups when they audit certain
15 types of businesses. So in this case that -- the markup
16 percentage that was calculated using the information from
17 Appellant was lower than the Department expected to see
18 based on their experience auditing similar restaurants in
19 the area.

20 JUDGE WONG: Thank you. And does that factor
21 into geographic differences? Because I know the auditor
22 in this case was from West Covina, which is in L.A. County
23 and then the restaurant at issue is in Orange County,
24 Westminster. Is it factored in, like, the geographic
25 differences? Does that go into the estimated expected

1 markup of 160 percent? Is the geographic area that that's
2 based on Southern California, L.A. County, Orange County,
3 the whole of California? Just curious, if you know.

4 MR. SAMARAWICKREMA: It's based on the location
5 of the restaurant. So if it's in Orange County, then it's
6 Orange County.

7 JUDGE WONG: Thank you. No further questions.

8 JUDGE BROWN: Judge Lambert?

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

11 JUDGE BROWN: I have a few questions, I think. I
12 wanted to ask CDTFA. One of Appellant's arguments is that
13 the 51.17 percent audited credit card ratio is similar to
14 the credit card ratio in Appellant's own records for the
15 fourth quarter of 2014. I believe the ratio is
16 55.94 percent. And I wanted to ask if you could address
17 that argument. Do you agree that the credit card ratio
18 and the test is similar to the credit card ratio for the
19 fourth quarter of 2014 and, if so, what does that tell us?

20 MR. SAMARAWICKREMA: There's so many issues the
21 Department noted. The guest checks were not available,
22 and the dim sum card was not available. Credit card sales
23 receipts were not available to verify the completeness of
24 the Excel worksheet or the POS download for the limited
25 period. And the 51 percent is based on the four-week

1 test, and it's like 28 days. It's in Department's
2 position, you know, the credit card ratio should be
3 51 percent or lower. And also based on no opinion
4 warranted, we had two different credit cards. 2014 is
5 51 percent and 2017 is 61 percent.

6 So if we're using the compound growth rate
7 formula, we can compute backwards and identify the correct
8 credit card ratio for 2011, '12, and '13. And at the time
9 of the field work, 51 was reasonable and representative
10 for the audit period. And that's the reason we use
11 51 percent. And using the average daily sales approach
12 and also the compound of the credit card ratio determined
13 from the compound growth rate formula, it shows that the
14 51 percent was reasonable and represent the audit period.

15 MR. PARKER: I would also like to add that we did
16 the observation or the test for the four-week period and
17 had 51 percent, and that is part of the fourth quarter
18 '14. And so the total amount of the fourth quarter '14
19 includes that four weeks. So the credit card ratio for
20 the remainder of that period is much higher than the 55.94
21 that ended up being the amount for the -- all of fourth
22 quarter '14.

23 So we verified the information for that four-week
24 test period. We did the undercover purchase during that
25 period and verified those sales. So the remainder of that

1 quarter, the credit card ratio is higher than during our
2 four-week period. That's the overall for the whole
3 quarter.

4 JUDGE BROWN: I also wanted to ask the argument
5 that I heard earlier about how the results were skewed
6 because Ms. Lai's own wedding banquet was included in the
7 calculations. Is that still -- is that still in the
8 current calculations, or is that only from the previous
9 audit of the duck-lobster audit, the two-item control
10 test?

11 MR. SAMARAWICKREMA: The sales related to the
12 wedding was never recorded. I mean, it is a
13 self-consumption. So it was never in the POS system. And
14 for the four-week test period it's not part -- we
15 didn't -- the Department did not take that amount or, you
16 know, there's no sales amount. So indirectly we can say
17 when the Department concluded the credit card ratio from
18 the four weeks that was not included.

19 JUDGE BROWN: Okay. I think that's all I have
20 for CDTFA at this time.

21 Co-panelists?

22 Okay. So we can now return back to Appellant's
23 rebuttal.

24 And, Mr. Brandeis, you had estimated 15 minutes.

25 MR. BRANDEIS: That should be enough. That

1 should be enough time.

2 JUDGE BROWN: Okay. Whenever you're ready.

3 And I'll just remind the witness if this next
4 part of the argument involves your testimony, you are
5 still under oath.

6

7 CLOSING STATEMENT

8 MR. BRANDEIS: So the Department is saying that
9 they keep statistics by geographic location for expected
10 markups and presumably other ratios. But yet, the Irvine
11 office who had all of this information decided that it's a
12 NOW. That doesn't fit.

13 JUDGE BROWN: Oh, I'm sorry. Is your microphone
14 on?

15 MR. BRANDEIS: Yes.

16 JUDGE BROWN: Okay. I was having trouble hearing
17 you. Go ahead.

18 MR. BRANDEIS: You heard testimony from the
19 Department that they keep information on markups and
20 various ratios by geographic location. But yet, in the
21 subsequent audit the Irvine office who had all this --
22 presumably had all this information, including having the
23 information regarding the disputes from the prior audit,
24 still decided that it was a NOW. Which office is right?
25 They couldn't both be right.

1 Second, this is really disturbing to me, but I
2 keep hearing the Department saying that we didn't provide
3 POS data. That's not true. I have several emails.
4 Exhibit 17 has an email from the auditor thanking us for
5 providing the POS data for the audit period. We provided
6 it. The reconcile -- in fact, they came on three separate
7 occasions with a computer audit specialist to download the
8 data, and they reconciled it.

9 They're getting their facts wrong. They're
10 saying that they only got it for 2014 for first and second
11 quarter. The audit workbook that I have, they did a
12 reconciliation of POS data from first quarter '13 to
13 second quarter '14 and found -- disclosed no material, no
14 errors. And we subsequently provided the POS data for the
15 entire audit period. If they analyzed it like they
16 claimed they would, or maybe they didn't because they come
17 to the conclusion that it's been altered. That's the only
18 conclusion that you can come to because they must have
19 deleted cash sales.

20 But if they have found a discrepancy, they would
21 have noted that. And it doesn't take very long to compare
22 the sales data and the POS data we provided to report it.
23 That doesn't take very long. A skilled person -- a
24 skilled auditor could probably do that in 30 minutes. But
25 we've never heard them say that the amounts don't

1 reconcile. And their own worksheet from the original
2 audit where they reconciled it for first quarter '13, not
3 first quarter '14, but first quarter '13 to second quarter
4 '14 disclose no material errors.

5 Second, they're saying we didn't provide 1099-K
6 forms. I wasn't -- I wasn't the initial representative,
7 but they clearly had them. They're in the record, and the
8 Department has access to that information anyways. I --
9 again, I've done probably 200 restaurants with the
10 Department, and they always have the 1099-K data. So this
11 is data that they get directly from the merchant card
12 processors. They have that information.

13 Same with income tax returns. They can order
14 that information from FTB. They can even order it from
15 IRS. So this argument that they keep trying to bring up
16 that they provided incomplete records is simply not true.
17 They had complete POS data. They had 1099-K forms. They
18 had bank statements. They had income tax returns.

19 If they didn't have the merchant card statements,
20 they may not have had it. I don't know, but that's really
21 summarized on the bank statements because all the credit
22 card transactions have to be deposited into a bank
23 account. So it would have been on the bank statements,
24 and it also would be on the 1099-K forms. So it's kind of
25 redundant to get ahold of merchant card statements. Yeah,

1 I just don't understand how they argue that they have --
2 the basis for impeaching records on that it's incomplete,
3 which the record shows clearly, they had normal books and
4 records.

5 And then too, they're supposedly keeping track of
6 ratios but, yet, the subsequent audit done by the Irvine
7 office basically says no, you guys are wrong. Irvine is
8 telling West Covina they're wrong. They can't -- they
9 can't reconcile that. They have no answer to that.

10 Okay. So on the issue of that there was more
11 banquets or more sales in fourth quarter '14, Iris is
12 saying that it's not atypical for them to have year-end --
13 companies having year-end banquets parties at their
14 offices. So, again, that could be. Banquets can really
15 skew the results of these ratios. It really should have
16 been analyzed separately from the restaurant operation
17 itself, but they never brought that up.

18 The other thing is they talk about an increase in
19 sales. Well, the original audit period covers half of
20 '11, all of '12, all of '13, and half of '14. So if you
21 recall this period, this is in the wake of the Great
22 Recession. And also, if you recall from this period, food
23 prices were increasing. So as we go from 2011 to 2017,
24 which is going through the second audit period, of course
25 sales are going up. Of course average daily sales are

1 going up. Why? Because the economy is recovering from
2 the Great Recession. And pick up any periodical and read
3 about food price inflation during that period of time.
4 Food prices were going up, so sales were going up.

5 That's all I have.

6 JUDGE BROWN: Okay. Thank you.

7 I'll say co-panelists, do you have any further
8 questions?

9 JUDGE LAMBERT: I have no questions.

10 JUDGE BROWN: Okay. Give me just a minute.

11 All right. I think I've asked all of my
12 questions. So if no one has anything further, I believe I
13 can say that this concludes the hearing and the record is
14 closed and the case is submitted today.

15 The Judges will meet and decide the case based on
16 the evidence, arguments, and applicable law, and testimony
17 we have received today. We will mail both parties our
18 written decision no later than 100 days from today.

19 The hearing is adjourned, and this is the end of
20 the morning session. Thank you.

21 (Proceedings adjourned at 11:24 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 8th day
of June, 2022.

ERNALYN M. ALONZO
HEARING REPORTER