

**OFFICE OF TAX APPEALS**  
**STATE OF CALIFORNIA**

In the Matter of the Appeal of:	)	OTA Case No.: 21057827
<b>PARTNERSHIP OF G. DELGADO AND</b>	)	CDTFA Case ID: 164-119
<b>M. DELGADO</b>	)	
<b>dba La Morenita Restaurant<sup>1</sup></b>	)	

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**OPINION**

Representing the Parties:

For Appellant: Kent McLellan, Representative

For Respondent: Jason Parker, Chief of Headquarters  
Operations

For Office of Tax Appeals (OTA): Richard Zellmer,  
Business Taxes Specialist III

J. ALDRICH, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 6561, the partnership of G. Delgado and M. Delgado (appellant)<sup>2</sup> appeals a decision issued by respondent California Department of Tax and Fee Administration (CDTFA),<sup>3</sup> denying appellant’s petition for redetermination of the Notice of Determination (NOD) dated April 13, 2016. The NOD is for tax of \$186,561.32, plus applicable interest, for the period January 1, 2012, through December 31, 2014 (audit period).

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<sup>1</sup> The dba is noticed on the NOD. The dba was changed to El Jardin Restaurant on or about May 18, 2016.

<sup>2</sup> G. Delgado and M. Delgado reported the business entity as a husband-and-wife co-ownership, as opposed to a partnership, to CDTFA. Under certain circumstances, an unincorporated business jointly owned by a married couple (i.e., joint venture, co-ownership, or partnership by operation of law) may elect not to be taxed as a partnership for income tax purposes. (See Internal Revenue Code, § 761(f).) Instead of filing taxes as a partnership, the qualifying members (husband and wife) may elect to file as sole proprietors for income tax purposes. (*Ibid.*) Irrespective of federal income tax treatment, a husband-and-wife joint venture is recognized as a partnership by operation of law, and treated as a separate entity, for sales and use tax purposes. (R&TC, §§ 6005, 6015.)

<sup>3</sup> Sales taxes were formerly administered by the Board of Equalization (board). Effective July 1, 2017, functions of the board relevant to this case were transferred to CDTFA. (Gov. Code, § 15570.22.) When this Opinion refers to acts or events that occurred before July 1, 2017, “CDTFA” shall refer to its predecessor, the board.

Appellant waived the right to an oral hearing; therefore, the matter is being decided based on the written record.

### ISSUE

Whether adjustments to the amount of unreported taxable sales are warranted.

### FACTUAL FINDINGS

1. Appellant operated five restaurants and a café in California. The six business locations are referenced herein as the Tuolumne café, the Turlock restaurant, the Murphy's restaurant, the Columbia restaurant, the Santa Cruz restaurant, and the Twain Harte restaurant. All the locations operated for the entire audit period except the Tuolumne café, which operated from October 1, 2012, through the end of the audit period, and the Murphy's restaurant, which operated from January 1, 2014, through November 1, 2014.
2. For the audit period, appellant reported on its sales and use tax returns (SUTRs) total sales of \$6,867,166 and claimed deductions of \$489,756 for sales tax included in reported total sales, resulting in reported taxable sales of \$6,377,410.
3. Upon audit, appellant provided complete bank statements and sales summaries for each business location for the audit period. Appellant provided incomplete sales receipts and POS reports.<sup>4</sup> Appellant did not provide any sales journals, general ledgers, purchase journals, federal income tax returns, or purchase invoices.
4. For the audit period, CDTFA compiled bank deposits totaling \$7,813,272, which was \$946,106 greater than reported total sales. CDTFA's audit report indicated that appellant could not explain the difference. CDTFA determined that additional examination was warranted.
5. CDTFA examined appellant's sales summaries, which reconciled with reported sales. However, because the sales summaries were not supported by complete source documents, such as sales receipts, and because of the unexplained \$946,106 difference between bank deposits and reported total sales, CDTFA concluded the books and records were insufficient to use in determining appellant's sales using a direct audit method (i.e., using appellant's books and records to establish sales). CDTFA decided to compute

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<sup>4</sup> Here we use sales receipts to mean a combination of handwritten sales tickets or guest checks together with credit card slips. According to the audit workpapers, some locations did not have a POS system.

- appellant's audited taxable sales using the credit-card-sales-ratio method, which is an indirect audit method.
6. Using a combination of observation tests,<sup>5</sup> available sales receipts, and available POS reports, CDTFA computed the ratio of credit card sales to total sales (credit-card-sales-ratio) of 40.7 percent for the Tuolumne café; 66.19 percent for the Turlock restaurant; 74.33 percent for the Murphy's restaurant; 68.1 percent for the Columbia restaurant; 70.22 percent for the Santa Cruz restaurant; and 71.84 percent for the Twain Harte restaurant.<sup>6</sup> Using the same observation tests, sales receipts, and POS reports, CDTFA calculated an average tip amount of 10.84 percent for the Tuolumne café; 12.87 percent for the Turlock restaurant; 11.63 percent for the Murphy's restaurant; 11.96 percent for the Columbia restaurant; 14.34 percent for the Santa Cruz restaurant; and 12.53 percent for the Twain Harte restaurant.
  7. Using the bank statements, CDTFA compiled credit card deposits for the audit of \$155,521 for the Tuolumne café; \$2,074,551 for the Turlock restaurant; \$376,311 for the Murphy's restaurant; \$1,017,216 for the Columbia restaurant; \$1,986,966 for the Santa Cruz restaurant; and \$1,849,747 for the Twain Harte restaurant. CDTFA deducted tips (at the rates described above) and sales tax reimbursement included in credit card deposits (at the rate applicable to each location) to compute audited taxable sales, of \$316,964 for the Tuolumne café; \$2,539,236 for the Turlock restaurant; \$416,187 for the Murphy's restaurant; \$1,224,184 for the Columbia restaurant; \$2,240,753 for the Santa Cruz restaurant; and \$2,096,545 for the Twain Harte restaurant.
  8. Audited taxable sales were compared to reported taxable sales to compute unreported taxable sales of \$190,904 for the Tuolumne café, \$727,228 for the Turlock restaurant, \$115,575 for the Murphy's restaurant, \$334,438 for the Columbia restaurant, \$451,323

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<sup>5</sup> An observation test is the physical observation and recording of the activity of a business for a specified period of time. (CDTFA Audit Manual, § 0810.30.)

<sup>6</sup> The test days and sources are as follows: observation tests on October 7, 2015, and October 15, 2015, and sales receipts for November 4, 2016, and November 16, 2016, for the Tuolumne café; observation test on August 20, 2015, and POS reports for October 31, 2015, November 1, 2015, and November 2, 2015 for the Turlock restaurant; an observation test on June 25, 2015, and POS reports for November 16, 2015, November 17, 2015, November 18, 2015, and November 19, 2015 for the Murphy's restaurant; observation tests for June 17, 2015, and October 13, 2015, and sales receipts for November 3, 2015, for the Columbia restaurant; POS reports for October 31, 2015, November 1, 2015, and November 2, 2015, for the Santa Cruz restaurant; and an observation test on May 20, 2015, and POS reports for October 31, 2015, November 1, 2015, and November 2, 2015, for the Twain Harte restaurant.

for the Santa Cruz restaurant, and \$636,995 for the Twain Harte restaurant. These amounts were added together to compute unreported taxable sales of \$2,456,463 for all six business locations combined.

9. CDTFA issued the NOD to appellant on April 13, 2016, based on the audit, in the amount of \$186,561.32 tax, plus applicable interest, for the period January 1, 2012, through December 31, 2014.
10. Appellant filed a timely petition for redetermination of the NOD. Appellant cited two specific grounds:
  - a. The audit was processed without benefit of a full and complete exit conference. Appellant claims that this precluded a full understanding of the audit findings and a fully informed response.
  - b. The Observation test was not performed from the days that are most representative of the business. The observation days included two Wednesdays and one Thursday. Having the test comprised of two Wednesdays and no weekend day as called for the by the Audit Manual (section 810.30) has reduced its reliability and as such cannot be accepted.
11. CDTFA held an appeals conference with appellant on December 19, 2018, and appellant provided some additional documentation.
12. In its February 16, 2021 decision, CDTFA ordered that a reaudit be performed to examine the additional documentation provided by appellant, and to allow appellant time to provide any additional records necessary to make adjustments.
13. Appellant did not furnish any documentation to support adjustments, and in a letter dated March 19, 2021, CDTFA informed appellant that it was making no further adjustments, and that it could either appeal to OTA or file a request for reconsideration with CDTFA.
14. Appellant timely filed the instant appeal with OTA.

#### DISCUSSION

California imposes a sales tax on a retailer's retail sales in this state of tangible personal property, measured by the retailer's gross receipts, unless the sale is specifically exempt or excluded from taxation by statute. (R&TC, § 6051.) All of a retailer's gross receipts are presumed subject to tax, unless the retailer can prove otherwise. (R&TC, § 6091.) Although gross receipts from the sale of "food products" are generally exempt from the sales tax, sales of

hot food and sales of food served in a restaurant are subject to tax. (R&TC, § 6359(a), (d)(1), (d)(2), and (d)(7).)

If CDTFA is not satisfied with the amount of tax reported by the taxpayer, it may base its determination of the tax due upon the facts contained in the returns or upon any information that comes within its possession. (R&TC, § 6481.) It is the retailer's responsibility to maintain and make available for examination complete and accurate records necessary to determine the correct tax liability, including bills, receipts, invoices, or other documents supporting the entries in the books of account (i.e., books and records). (R&TC, §§ 7053, 7054; Cal. Code Regs., tit. 18, § 1698(b)(1).)

When a taxpayer challenges an NOD on appeal to OTA, CDTFA has a minimal, initial burden of showing that its determination is reasonable and rational. (*Appeal of Talavera*, 2020-OTA-022P.) Once CDTFA has met its initial burden, the burden of proof shifts to the taxpayer to establish that a result differing from CDTFA's determination is warranted. (*Ibid.*) The applicable burden of proof is by a preponderance of the evidence. (Cal. Code Regs., tit. 18, § 30219(c); *Appeal of Estate of Gillespie*, 2018-OTA-052P.) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (*Appeal of Talavera, supra.*)

Here, appellant did not provide sales journals, general ledgers, purchase journals, federal income tax returns, or purchase invoices for the audit period. Furthermore, the sales receipts and POS reports provided for audit were incomplete. Also, CDTFA found that bank deposits exceeded reported total sales by \$946,106. Appellant could not explain the excess bank deposits. Under these circumstances, we find that it was appropriate for CDTFA to utilize an indirect audit method. The credit-card-sales-ratio method is a standard and accepted accounting procedure. (*Appeal of Amaya*, 2021-OTA-328P; see also, *Riley B's, Inc. v. State Bd. of Equalization* (1976) 61 Cal.App.3d 610, 612-613.) We find that CDTFA acted reasonably and rationally in calculating credit-card-sales-ratios and tip ratios by using a combination of observation tests, sales receipts, and POS reports. Since sales made by credit cards are generally required to be deposited directly into appellant's bank account, the credit card deposits recorded on appellant's bank statements provide a verifiable source of information. Thus, it was reasonable for CDTFA to apply the credit-card-sales-ratios to the amounts of credit card deposits recorded in the bank statements, after adjusting for tips and sales tax reimbursement. Accordingly, we find that

CDTFA has met its initial burden to show that its audit determination was reasonable and rational. As such, the burden of proof shifts to appellant to show errors in the audit.

On appeal to OTA,<sup>7</sup> appellant argues that COVID-19 presented challenges, both personal and to the business, which proved overwhelming in preparing a defense for the CDTFA audit. Appellant contends that the credit card ratios used in this audit are not accurate and have resulted in an overstatement of taxable sales. Appellant requested the opportunity to provide records and argument to support this contention.

However, during the briefing period appellant did not submit documents, make additional argument, or request additional time to provide the same. (See, Cal. Code Regs., tit. 18, §§ 30302(f) and 30303(a).) After the briefing period had concluded, and the matter was submitted on the written record; we reopened the record and requested additional briefing on January 24, 2022. (See, Cal. Code Regs., tit. 18, § 30304(a).) We did not receive a response to our additional briefing request from appellant. Notwithstanding the multiple opportunities, appellant has not provided any evidence or additional argument in support of its position. Therefore, we find that appellant has failed to prove facts from which a more accurate determination can be made, and on that basis, we conclude that reductions to the measure of unreported taxable sales are not warranted.

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<sup>7</sup> It its appeal with CDTFA, appellant cited two grounds for its petition for redetermination. (See Factual Finding 10.) On appellant's request for appeal to OTA, appellant did not renew the grounds of its petition for redetermination or otherwise provide support for its argument, as such, we will not address them further.

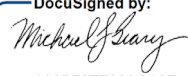
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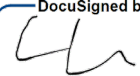
Appellant has not shown that adjustments to the amount of unreported taxable sales are warranted.

DISPOSITION

Respondent’s action in denying the petition is sustained.

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Josh Aldrich  
Administrative Law Judge

We concur:  
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Michael Geary  
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Andrew J. Kwee  
Administrative Law Judge

Date Issued: 4/20/2022