

BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of:)	
)	
STAR OF INDIA LLC,)	OTA No. 18083620,
)	21088499
Appellant.)	
_____)	

CERTIFIED COPY

TRANSCRIPT OF PROCEEDINGS

Tuesday, May 20, 2025

Reported by:

EMMETT BARNARD
CSR No. 14529

Job No:
55372 OTA

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15 TRANSCRIPT OF PROCEEDINGS, taken at
16 400 R Street, Suite 470, Sacramento, California,
17 commencing at 9:30 A.M. and concluding at
18 12:02 P.M. on Tuesday, May 20, 2025, reported
19 by Emmett Barnard, CSR No. 14529, a Certified
20 Shorthand Reporter in and for the State of
21 California.
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25

1 APPEARANCES:

2
3 Panel Lead: ADMINISTRATIVE LAW
4 JUDGE NATASHA RALSTON

5 Panel Members: ADMINISTRATIVE LAW
6 JUDGE KEITH LONG

7 HEARING OFFICER
8 KIM WILSON

9 For the Department: STATE OF CALIFORNIA
10 FRANCHISE TAX BOARD

11 NALAN SAMARAWICKREMA,
12 HEARING REPRESENTATIVE

13 JASON PARKER,
14 HEARING REPRESENTATIVE

15 STEVE SMITH, TAX COUNSEL

16 For the Appellant: KAI MICKEY
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I N D E X

E X H I B I T S

(Department's Exhibits A through X were received at
page 7)

(Appellant's Exhibits 1 through 4 were received at
page 7)

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By Mr. Mickey.....70

1 Tuesday, May 20, 2025

2 9:30 A.M.

3
4
5 ADMINISTRATIVE LAW JUDGE RALSTON: So we are now
6 on the record in the appeal of Star of India LLC. These
7 matters are being heard before the Office of the Tax
8 Appeals. The OTA case numbers are 18083610 and
9 21088499. Today's date is Tuesday, May 20th, 2025, and
10 the time is approximately 9:35 A.M. Today's hearing is
11 being heard by a panel of three administrative law
12 judges and hearing officers.

13 I am Judge Ralston, and I will be the lead
14 judge. Judge Long and Hearing Officer Wilson are the
15 other members of the this tax appeal panel. All three
16 of us will meet after the hearing and produce a written
17 decision as equal participants. Although I'm the lead
18 judge and I will conduct the hearing, any judge or
19 hearing officer on this panel may ask questions or
20 otherwise participate to ensure that we have all the
21 information that we need to decide this appeal.

22 As I mentioned this hearing is being live
23 streamed to the public. We have our stenographer
24 present, Mr. Barnard, who is reporting this hearing
25 verbatim to ensure that we have an accurate record. We

1 ask that everyone speaks one at a time and does not
2 speak over each other. Even if you think you know what
3 we're going to ask, please let us finish the question.
4 Also, speak clearly and loudly. When needed,
5 Mr. Barnard will stop the hearing process and ask for
6 clarification, and after the hearing Mr. Barnard will
7 produce the official hearing transcript, which will be
8 available on the Office of Tax Appeals' website.

9 I'm going to ask the parties to please
10 introduce themselves for the record starting with Mr.
11 Mickey. Please state your name and who you represent.

12 MR. MICKEY: Yes. I'm Kai Mickey. I'm
13 president of Sales Tax Specialists, and I'm here
14 representing Star of India LLC.

15 ADMINISTRATIVE LAW JUDGE RALSTON: Thank you.
16 And for the CDTFA.

17 MR. SAMARAWICKREMA: Nalan Samarawickrema,
18 representative of the Department.

19 MR. PARKER: Jason Parker, Chief of Headquarters
20 Operation Bureau, CDTFA.

21 MR. SMITH: Steven Smith, attorney. CDTFA.

22 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. Thank
23 you.

24 So we have held the prehearing conference on
25 this matter on April 8th, 2025. The Respondent, CDTFA,

1 have submitted Exhibits A through X, and Appellant
2 indicated at the prehearing conference that they had no
3 objection to Respondent's Exhibits A through X.

4 Mr. Mickey, is that still the case?

5 MR. MICKEY: Yes.

6 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. Thank
7 you. So Respondent's Exhibits A through X shall be
8 admitted -- are admitted without objection.

9 (Exhibits A through X were admitted into
10 evidence.)

11 ADMINISTRATIVE LAW JUDGE RALSTON: And the
12 Appellant has previously submitted Exhibits 1 through 4,
13 and Respondent had no objection to Appellant's
14 Exhibits 1 through 4; is that still correct?

15 MR. SAMARAWICKREMA: Yes, Judge.

16 ADMINISTRATIVE LAW JUDGE RALSTON: Thank you.
17 So Appellant's Exhibits 1 through 4 are admitted without
18 objection.

19 (Exhibits 1 through 4 were admitted into
20 evidence.)

21 ADMINISTRATIVE LAW JUDGE RALSTON: Neither party
22 intends to call any witnesses. As far as the time
23 estimates Mr. Mickey has requested 90 to 120 minutes to
24 use for your opening presentation. The panel members
25 may have questions for you after that, and CDTFA,

1 Mr. Samarawickrema, will go after that. We'll have 45
2 minutes for your presentation, and then lastly we'll go
3 back to the Appellant, and you will have 10 minutes for
4 rebuttal.

5 Does that sound like what we discussed at the
6 prehearing conference for everyone?

7 MR. MICKEY: It does. I don't think I'll take
8 as long as I thought it would, but that is what we
9 discussed. Yes.

10 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. Great.
11 Thank you.

12 MR. SAMARAWICKREMA: If you had any question, 60
13 minutes.

14 ADMINISTRATIVE LAW JUDGE RALSTON: I'm sorry.
15 What?

16 MR. SAMARAWICKREMA: 60 minutes.

17 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. 60
18 minutes?

19 MR. SAMARAWICKREMA: Yes.

20 ADMINISTRATIVE LAW JUDGE: Okay. So depending
21 on how things go and how long things actually take, we
22 may take a break in between that time. I will let you
23 guys know, and the panel members, as I said, may have
24 questions as we go along. So does anyone have any
25 questions before we move on to our opening

1 presentations?

2 MR. MICKEY: No.

3 ADMINISTRATIVE LAW JUDGE RALSTON: Okay.

4 Hearing none, Mr. Mickey, please begin when you're
5 ready.

6
7 PRESENTATION

8 MR. MICKEY: Well, thank you very much. I'm not
9 sure what is the best way to go about doing this so I
10 did it -- I picked a way to do it. We have two audits
11 here. There are some individual specific issues with
12 each audit, and then there are overlapping issues with
13 both audits.

14 So what I've decided to present first is we'll
15 be looking at the second audit period, and during my
16 presentation, rather than referring to your case numbers
17 if it will be okay, we could just refer to audit number
18 one as the old audit and audit number two as the newest
19 audit just to make it easy to present because we're
20 going to have to go back and forth to the exhibits to my
21 worksheets. So it might be more helpful to do that it
22 that way.

23 So I'm going to be focusing on initially on a
24 couple of things with number two, which is the second
25 audit period. We are going to start by going through my

1 exhibits. A little background notes here. Between the
2 two audits there were different people doing the
3 returns. It's pointed out in the audit that in the
4 first audit there was an individual that was running the
5 business. That person is no longer available. They did
6 not participate in the second audit, or at least they
7 were not involved in the second audit.

8 And I got involved late, and so this is a very
9 old case -- as you all are aware -- and unfortunately
10 between the time that the audit was done and when I came
11 on board, most of the records have become unavailable.
12 So some of the -- and we'll discuss that a little bit
13 when we start talking about penalties later, but I'm
14 limiting most of my discussion to what's in the audit,
15 but I wanted to point out that was that the reason --
16 and I'm going to have a little issue with that in a bit,
17 but I just wanted to be transparent and clear that
18 that's what's going on here.

19 So in the first presentation I'd like to look
20 at my Exhibit 1, and the Exhibit 1 has to do with
21 scheduled -- that markup issue in the second audit, and
22 I think my exhibits were clear, but I did want to walk
23 through and kind of explain what I did. I don't know if
24 it's appropriate, but I guess I will start by asking
25 does the staff agree with what I've done here? To make

1 it really easy. Is that about appropriate thing to ask?

2 ADMINISTRATIVE LAW JUDGE RALSTON: We'll just
3 have you give your presentation.

4 MR. MICKEY: Okay. So starting with schedule
5 12B is where this starts, and our 12 -- our 2 12D. In
6 the exhibits, your OTA exhibit file that you presented,
7 that you put everything together on, the original
8 working papers can be found on page 382 and 383 of that
9 document. What I provided you is a revised schedule
10 showing adjustments to the markup area of the audit.

11 The current reaudit is showing \$410,995 in
12 markup sales for the second audit period. Once this
13 adjustment is made you'll see that we come down to an
14 understated taxable sales amount based on the markup of
15 1.5762.

16 (The court reporter asked for clarification.)

17 MR. MICKEY: The original numbers were 410,995,
18 and the adjustment that we're asking for brings the
19 audited understated sales adjusted down to 125,762. And
20 the way this comes about is if you look at my Exhibit 1,
21 page 4 of 8, you'll see down at the bottom there's some
22 yellow boxes and green boxes. This is just a
23 replication of what was the original audit look like on
24 that schedule R 12D, and what the original auditor did
25 -- and there's a lot of back and forth in all this, and

1 I'm trying to clear a lot of that out in this
2 discussion. A lot of it doesn't really have meaning
3 when we look at what we're doing here.

4 Ultimately, in the reaudit -- the first
5 reaudit -- it was accepted that the 2013 income tax
6 return figures would be used as the purchases for the
7 2013 period in this schedule, and you see down there at
8 the bottom. It's row 42, and right now my numbers shows
9 135,017 and reaudit that number is 204,947, and if you
10 look at the next page, page 5 of 8, you see this is a
11 schedule that the Department auditors did not have,
12 didn't even ask for. Or if they did ask for, they
13 didn't get it. I don't know what happened. I wasn't
14 involved in that, but they did not have that, and so
15 they were using the 204,947 as the purchases subject to
16 the markup calculations.

17 They then separated that out in into alcohol
18 and food, but what I discovered, as you can see here, is
19 when you look at the secondary page of the cost of goods
20 sold for the 2013 --

21 (The court reporter asked for clarification.)

22 MR. MICKEY: Cost of goods sold. I'll talk
23 closer to this. The second page, page 2, cost of goods
24 sold, you will see that the 204,947 -- which I've
25 highlighted -- it actually consists of two amounts. One

1 amount is purchases less cost of items withdrawn for
2 personal use, 135,071, and then there's cost of labor of
3 69,876.

4 Those two numbers make up the 204,947, and we
5 should all agree that the labor is not subject to the
6 markup, and so all I've done here is replaced the
7 correct amount of 135,071 into the previous amount of
8 204,947, and you'll see that again on page 4 down at the
9 bottom in the yellow box. And then secondarily in the
10 reaudit they used an estimate of -- excuse me --
11 estimate of 2014 purchases based on 2013.

12 Well, we got the 2014 income tax figures, and
13 so we are asking that we substitute the calculated 2014
14 amounts for the actual amounts on the 2014 income tax
15 return, schedule C cost of goods sold, and the original
16 audit -- or the reaudit showed 252,176 as the cost of
17 goods sold, and you can see from page 7 on my Exhibit 1
18 that the total cost of goods sold for that year was
19 actually 193,066.

20 Now, what I did also was I'm going show you
21 that when you look at the 2013 period, you'll see on
22 page 6 of 8 I've highlighted the line 26 where it would
23 be wages, and there are no wages shown, and that's in
24 2013. That should be accepted that the wages are the 37
25 -- line 37 in the cost of goods sold is 69,876.

1 So the taxpayer's CPA had combined purchases
2 of inventory with wages to come up with goods sold, and
3 in 2013 they separately stated those two amounts in the
4 cost of goods sold. That's how we get to 135,017 that
5 replaces the original reaudit figure on schedule 12D.

6 Keeping in line with that same analysis, we
7 look at 2014, page 8 of my exhibit. I, again, have
8 highlighted the wages line, and you'll see there's no
9 wages, and so what I did in 2014 is looked at and
10 considered the 190,366 total cost of goods sold as being
11 inclusive of purchases and the labor.

12 And I used the percentage that was developed
13 from the segregated amounts in 2013 to segregate the
14 2014 amount, and that's how we came up with the 125,642
15 of purposes. That is 66 percent of the 190,366, and in
16 2013 the purchases was 66 percent of the total. That's
17 how we came up with those numbers.

18 And if you look at the totals, just look at
19 reasonableness for 2013 and 2014. In 2013 the total
20 cost of goods sold both labor and purchases was 204,947
21 with two separately stated amounts, and in 2014 the
22 total combined figure was 193,066. Those are materially
23 close, which should be -- should make it able to accept
24 that they're the same kind of number in different years.
25 So when you separate the one number into two in 2014,

1 you get very reasonable numbers that are close to 2013.

2 So now all we've done is gone back to the
3 first page -- or it's actually page 4 and substituted
4 down there at the bottom the 135,071 for 2013 and the
5 125,642 for 2014, and let it flow through because what
6 they get with those numbers, they then needed to break
7 those into alcohol and food.

8 And so the exhibit, if you go to page 3 of 8,
9 and you see a green boxes. Well, the green boxes are
10 allowing you to reference where those numbers are coming
11 from, and this simply taking the formulas that are in
12 the existing reaudit working papers and letting them do
13 their job, and we come up with a new revised percentage
14 of error simply by replacing the incorrect cost of goods
15 sold and estimated cost of goods sold with the new
16 verified amounts from the income tax return.

17 And so by doing so and reducing the percentage
18 of error down to 23.92, 69.3, which you see on page 3 of
19 8 of the exhibit, you factor that in back on our 2 12A,
20 all I did there was change the percentage of error, and
21 we get the understated taxable sales of 125,762 instead
22 of the 410,995.

23 So our adjustment by correcting the cost of
24 goods sold for the same figures that were being used and
25 accepted in the audit -- we've just corrected them --

1 results in the measure of understated taxable sales
2 based on the markup being reduced by \$285,233. So
3 hopefully the schedules are clear to what I did.

4 Again, just to be clear, they have essentially
5 the same audit working papers with the numbers changed
6 for the cost of goods sold, and it all flow through.
7 The only change we made. So that's our presentation for
8 this first item in the audit.

9 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. Thank
10 you. Yeah. You can keep going.

11 MR. MICKEY: Okay. Next, if you look at my
12 Exhibit 2 -- so this is one's going to be a little bit
13 more confusing to show -- and you'd all be sitting
14 around the table, and I could show you all but -- so
15 this is an area where the difference between recorded
16 and reported -- I'm asking for this adjustment because
17 inside this number there are basically two types of
18 transaction.

19 One of these transactions is more coupons, and
20 one of them, the other, is other basic clerical
21 differences, and at the end of this journey here this
22 category of difference between recorded and reported
23 should only be \$37,590. \$37,590 because there is a
24 \$167,565 in coupons that the auditor treats as being
25 recorded in this figure, and when I say auditor treats

1 them as being recorded, here's the explanation for that.

2 Throughout this audit and even the first audit
3 these coupons, which we'll talk about in a bit, have a
4 monetary value to them, and the auditors took the
5 approach in this case that the monetary value of the
6 recorded amount of coupons based on volume, time to
7 sell, was a recorded sales amount, and that is wrong.

8 And I think when you dig into the working
9 papers I did, the Department will see the same thing is
10 they recorded the number of coupons, but it's very clear
11 that within the sales they did not record any sale
12 amount related to these coupons. Just the volume of
13 coupons.

14 And so when the auditor looked at this -- and
15 you will need to look at schedule R2 12F, which I think
16 I gave you -- actually, couple ways you can look at
17 this. So if you will look page 5 of 5 of my Exhibit 2,
18 okay, this is schedule 12H-2b, and this is recorded
19 breakfast coupon food sales per sales journals. That is
20 a slightly misrepresentative title. It would be more
21 properly stated as recorded breakfast coupon food volume
22 of redeemed coupons for the sales journal.

23 (The court reporter asked for clarification.)

24 MR. MICKEY: Yeah. It's recorded breakfast
25 coupons redeemed in volume is really what they should

1 be. There were no food sales recorded for these coupons
2 in the sales journal. So column C, it's referencing
3 sales journal. Number of breakfast coupons redeemed.
4 It gives it an 8.99 value. We will talk about that in a
5 little bit, but that's moot to this discussion.

6 You can follow down. 18,639 coupons. They
7 calculated a price of \$167,565 based on the 8.99 selling
8 price, and then when you follow the schedule through to
9 the next schedule, schedule 12H-2, you see that now they
10 have reported food sales per sales journal and schedule.
11 So now these auditors are bringing forth different
12 elements of a what they call sales and adding them
13 together to get recorded food sales to then use that
14 total recorded food sales to compare it to the food
15 sales that they reported.

16 And so here's where the problem comes in. On
17 page 4 of 5 of my exhibit you see I've highlighted
18 column F. Okay. This 167,565. It is included in now
19 the 492,058, which is total recorded food sales. Okay.
20 The problem is these are not recorded food sales. They
21 may be coupons. Okay. They're the coupons that were
22 redeemed. So that's the other issue, but they were not
23 recorded sales.

24 So you must exclude this 167,565 from column
25 H. This should not be in this calculation, which you

1 would then reduce the 492,058 in column H by the
2 167,565, okay, but it's a little bit more convoluted
3 than that because now you go to 12H-2, and you see that
4 I've also highlighted column F, and this is another way
5 of looking at it. This is actually -- that's the same
6 page. I'm sorry. You go to 12H. When the -- all
7 right.

8 So now they're bringing everything today on
9 this column to come up with their total recorded taxable
10 measure, which you'll see in column G. All right. So
11 column C plus D is going to equal column E, and you see
12 that column E is called total recorded taxable alcohol
13 and food sales, 750,219.

14 They then add some gratuity to it, and they
15 get total recorded taxable measure of 769,025. I hope
16 you're here with me. Then they compare that to total
17 taxable sales 555,769, and this is how they come up with
18 the --

19 (The court reporter asked for clarification.)

20 MR. MICKEY: I'm sorry. I thought I was going
21 slow. I am trying to go slow because this is very
22 complicated. All right. Let me back up. Column C,
23 total recorded alcohol sales. That comes from another
24 schedule, which we're not at right now. Column D, total
25 recorded food sales, XX. This is the number that came

1 from the schedule that I had you look at here just
2 before this that includes the auditor's calculation of
3 the sales price value of the redeemed coupons.

4 So the 492,058 in column D on 12H includes the
5 167,565 in calculated coupon sales. When combining
6 column C and D on schedule 12H, you get the 750,219 in
7 total recorded taxable alcohol and food sales.
8 Remember, the 750,219 includes the calculated sales for
9 the food coupons.

10 They then add some mandatory gratuity, so
11 10,705 to the 750,219. So column E plus column F then
12 equals column G. So the total recorded taxable measure
13 now, as calculated by the auditor, becomes 760,925.
14 Again, remember that number now includes the calculation
15 for those food coupons.

16 So now they take that number in column G and
17 compare it against the reported taxable measure from the
18 sales tax returns in column H, and the difference
19 becomes the 205,155 in column I. So that means that
20 that difference of 205,155 includes the 167,565 from
21 those coupons. Those coupons were not recorded. The
22 value of the coupons are not recorded, and there's
23 comments throughout the audit that confirm that.

24 So all we're asking here is that this category
25 on 12H -- and you'll see my yellow box here -- we're

1 removing the estimated coupon values from the 205,155,
2 and we come up with a revised recorded versus reported
3 of 37,590. Now what we have -- yeah.

4 So that's -- I mean, it's all math, and it's
5 -- hopefully, when you look at the exhibit after hearing
6 me mumble through trying to explain going back and
7 forth, it will make sense, but it's a simple thing that
8 the auditor calculated and audited recorded taxable
9 measure, compared it against reported taxable measure,
10 and got a difference. And when calculating the audited
11 recorded taxable measure, they included an amount that
12 is not a recorded sales amount. That's basically what
13 happened simplified. So the 167,565 should not be part
14 of recorded versus reported differences on the schedule.

15 I guess if you have questions, you'll ask me
16 questions on this after we're done with all of them.
17 What if I don't remember what I said? I'm just kidding.
18 All right. That's our presentation on this one.

19 ADMINISTRATIVE LAW JUDGE RALSTON: Yeah. We're
20 taking notes, and yeah. We'll ask questions if we need
21 to.

22 MR. MICKEY: Okay. Okay. So now we're going to
23 move on to Exhibit 3. This one hinges on the adjustment
24 we just talked about. It's a flowthrough. If you look
25 at the differences in Exhibit 2, if you look at page 4

1 of 5 my of my Exhibit 2, you'll see that in the forth
2 quarter of '12 there's zero. Okay. So they did not
3 have the information to calculate the differences in
4 schedules 12H for the fourth quarter 12th. So they
5 calculated for first quarter '13 forward.

6 They then needed to calculate an average to
7 plug into the fourth quarter of 2012. So essentially
8 what they did is they took the quarterly average
9 difference for the period for first quarter '13 to third
10 quarter '15, and applied that difference into the fourth
11 quarter of 2012 on schedule 12G.

12 So if you go to my Exhibit 3, from first
13 quarter '13 to third quarter '15 -- I am in row 11 now.
14 You see I've highlighted the 324,493, okay, and then if
15 you scroll over -- the best way I can describe this --
16 you see the difference if column J of 37,591. That's
17 the new difference that I gave you in the other exhibit.

18 So the original difference was 205,155. They
19 got an average based on that in the original reaudit.
20 We've now corrected that number down to being 37,590,
21 rounded 591, which means that the quarterly average is
22 3,417. 3,417. So we look at schedule 12G. It did show
23 \$18,651 as the plugged calculated estimated difference
24 for that period. It should now be 3,417 after making
25 the adjustment we just talked about in the other

1 schedules.

2 So really 12H and 12G are addressing the same
3 issue. 12H was done for the period where they had all
4 the records. 12G was the straggling early period where
5 they did not have the records for, so they did an
6 average based on 12H. So since we corrected 12H, we now
7 need to correct 12G's average as well, and that's the
8 3,417 instead of 18,651. That's it for that one. Okay.

9 Okay. So now we're going to look at -- start
10 looking at a couple of things having to do initially
11 with really the percentage of error. Now we're going to
12 go back to the first audit. There's no difference --
13 we've already addressed the differences between recorded
14 and reported in the second line.

15 There's now -- in the first audit there's
16 schedule 12B and 12C differences. What happened here
17 was the auditor -- and this is the unfortunate part
18 having to do with the length of time this has gone on,
19 and there were a number of remodeling efforts at the
20 location, change in personnel, and so unfortunately what
21 has happened is I don't have access to the records that
22 the auditor used to come up with the differences in the
23 12B and 12C of the first audit.

24 Audit schedules 12C in the first audit were
25 differences based directly on calculations that the

1 auditor performed based on sales records that the
2 auditor had in their possession. 12B is, again, a
3 projection based on the results of 12C. So they kind of
4 go together, and the issue that we have here is
5 multifold.

6 On schedule -- there are comments in the audit
7 that the auditor showed up, and that there were 12 boxes
8 of records for the auditor to look at the accountant's
9 office, the original accountant's office. I don't have
10 those 12 boxes of records. We have searched upside down
11 and backwards, everywhere we could.

12 So unfortunately I don't have those, but the
13 auditor had them, and those 12 boxes of records --
14 there's also other comments that talk about -- had the
15 sales journals in it, had daily receipts, what they call
16 the dailies, and then the monthlies.

17 So the auditor in the 12C schedule used
18 monthly summaries for second and third quarter of --
19 second and third quarter of '18 and accepted the monthly
20 sales summaries, and then used the dailies to add up the
21 dailies for two quarters, and you'll see those in
22 schedules 12E and F, I think, on the audit, and the
23 auditor claims that the amounts that they compiled from
24 the dailies exceeded the amounts that were on the
25 monthlies, and so for the remaining period from 1/1 of

1 2009 until the third -- March of 2011 the auditor
2 disregarded the monthly summaries and did a projection
3 based on the results of second quarter 2008 through the
4 second quarter of 2009.

5 Herein lines our issue. We believe that the
6 auditor should have done more work at the time before
7 just projecting this, and had the auditor done that, the
8 projected clerical differences would have been less.
9 And on schedule 12C of the audit -- of the reaudit, the
10 auditor makes a comment that says scheduling dailies was
11 taking an excessive amount of time, and there were
12 multiple days missing so our percentage of error was
13 computed using the above quarters.

14 So I fully understand that the auditors have
15 the right to, you know, basically do whatever they
16 want -- disregard records and so on -- but at the same
17 time there should be some accountability held towards
18 the audit staff to recognize that when there are issues
19 that they're finding, that they should be able and
20 willing to do enough work to reasonably support what
21 they are doing, and not just throw their hands up and
22 say this is taking too much time.

23 This is a significant amount of purported
24 understatement that could have been calculated based on
25 actual figures, and they weren't. They did have the

1 monthly summaries for the entire period, and they're
2 still in existence, and so we are asking that because
3 the auditor chose not to do sufficient sampling, a
4 sufficient review, a sufficient analysis in light of the
5 a circumstances with the records that they were
6 provided, that we should not have to live with these
7 results. We should be able to use the amounts that the
8 auditor should use at the beginning that still exist,
9 and those are what's in the audit.

10 The auditor does not have -- secondarily, the
11 auditor does not have more than, I think, a few days'
12 worth of these dailies that the auditor used. There's
13 some in the exhibits, but for the most part they don't
14 exist either, and so we're just asking that we base the
15 reconciliation on the monthly summaries that are
16 available instead of these daily summaries, and at least
17 they'll be based on recorded amounts that we know. I
18 trust that makes sense.

19 Okay. Next area that we're going to talk
20 about is the unreported breakfast coupons, and this is
21 an interesting area. Throughout -- these unreported
22 breakfast coupons represent coupons that were redeemed
23 or purportedly redeemed by hotel guests in the
24 restaurant, and the hotel guests had received these
25 coupons from the hotel upon renting a room, getting

1 accommodations.

2 Throughout the whole audit period, both first
3 and second audit period, it's real clear that these
4 breakfast coupon dollar amounts were not included as
5 sales in the sales journal, and the auditors in the
6 first audit based their revenue estimate of these
7 coupons based on a single amount that they found on one
8 of the worksheets that shows \$7.95. And I might add
9 it's the same worksheet that is of a series of we asked
10 to use in the reconciliation. So this was acceptable
11 for this, and so we don't really take issue with the
12 calculation of the dollar amount in the second -- in the
13 first audit.

14 This is kind of -- hedging whether I should
15 just address the first audit and the second audit, but
16 they kind of go together. The second audit has the same
17 thing, unreported breakfast coupons, and this is right
18 now they're 658,428 --

19 (The court reporter asked for clarification.)

20 MR. MICKEY: On schedule R2 12F of the second
21 audit, there is an unrecorded breakfast coupons and
22 banquet sales based on an average from prior audit, and
23 the total's now sitting at 658,428. When analyzing the
24 worksheets, you will see that in that number there's
25 actually \$475,605 worth of calculated coupon values.

1 Okay. That number. So between the first audit, which
2 has \$582,215 in these coupons at a calculated dollar
3 amount based on the auditor's calculations, and then
4 there's 475,605 in the second audit. So right around a
5 million dollars worth of these coupons between the first
6 and the second audit period.

7 In the second audit period the auditors took a
8 position -- two positions. Number one, they could
9 not -- would not rely upon the recorded amount of
10 coupons that were redeemed. There is a schedule in the
11 audit. It is schedule 12F 2 is the schedule that shows
12 the number of reported breakfast coupons for the second
13 audit period, and it's in column E and F, and so the
14 taxpayer had recorded these coupons of 18,639 in volume
15 for the period.

16 The auditors really arbitrarily decided that
17 that was not sufficient numbers of these coupons, and so
18 they proceeded to then use an estimated quarterly amount
19 of coupons based on the first audit. So they totally
20 disregarded the 18,639, and they took an average from
21 the 61,031 that were redeemed in the first audit. So
22 basically equated the number of coupons that were
23 redeemed in the second audit period to the number of
24 coupons that were redeemed in the first audit period.

25 Now, in another memo, the issue we have that

1 now is that in a memo dated March 4th, 2021, David
2 Hofer, district principal auditor for Sacramento,
3 responded to the petition section and said, records were
4 determined to be inadequate per review of both the prior
5 and current audits. It was determined that the
6 accounting procedures, types of sales, and quantity of
7 sales were substantially the same. There's not a large
8 gap between the audit periods.

9 So they are just looking at this. Now,
10 remember they would not accept the journals, the sales
11 summaries. They're accepting the -- they're not
12 accepting the number of coupons, and they're also
13 raising the value of the coupons by a dollar. So
14 they're all over the place as far as what they're doing
15 with these coupons, and what we believe should happen is
16 they should accept the number of coupons that were
17 recorded.

18 There was also a coupon discussion where the
19 coupons were at 3.49. Instead of using 7.95, they
20 should use the 3.49 coupon value -- that's also exhibits
21 in the working papers -- and reduce that 475,605 in the
22 second audit period considerably based on what was
23 recorded.

24 Now, secondarily on the coupons. This is
25 something that was really missed all the way along the

1 road, and remember as I explained earlier they do not
2 treat these as sales. They're not recorded. They're
3 not rung up. The idea was that the restaurant would be
4 reimbursed by the hotel for the number of coupons. Now,
5 if that happened, then I guess the sales between the
6 hotel or the restaurant and the hotel, according to
7 Regulation 1603 would be taxable sales.

8 However, after investigating this and asking
9 the right questions, it was determined that money never
10 changed hands between the hotel and the restaurant for
11 these coupons. So, really, everything we're talking
12 about -- the selling price, the value, the number, the
13 quantity is kind of moot because there were no sales
14 because there were no transfers of money.

15 Now, you can argue there was a sale, and if
16 you argue that there was a sale, it was never paid, then
17 there's a bad debt deduction. So either way you look at
18 it, the unreported breakfast coupons are -- should not
19 be set up as taxable sales in the audit.

20 And to support this we go Exhibit 4, and these
21 are the three affidavits that I've obtained from three
22 individuals that were knowledgeable about what was going
23 on in time, and they're self-explanatory. They say
24 essentially the same thing, but these three
25 individuals -- the officer manager Alan Bocast; Vinod

1 Sharma, the owner of the hotel or part owner of the
2 hotel; and Albert Bashir, who's general manager of the
3 hotel -- all confirming, verifying, validating, and
4 certifying that the hotel did not end up paying the
5 restaurant for these coupons.

6 So we either need to remove the coupons from
7 the audit as there being no sales because there was no
8 exchange so there's just nothing there, or we need to
9 add in a bad debt allowance for these items. Either
10 way, there should be no tax due on the breakfast
11 coupons. So that will address the specific issues that
12 we have in the audit.

13 There are a few other items in the audit, but
14 due to materiality I'm not addressing them today, and so
15 now I want to move on to talking about the penalties.
16 There are three penalties. We have negligent penalty on
17 the first audit, we have a negligence penalty on the
18 second audit, and a fail -- finality penalty on the
19 second audit.

20 For the finality penalty, which we touched on
21 at the prehearing conference, due to the age and the
22 time lapsed I believe that we'd like to ask that the
23 OTA, that you consider the information that has already
24 been provided in -- it's in O -- Exhibit Q in the
25 CDTFA's exhibit.

1 Okay. We would just ask that you consider
2 that. The information is already there. There's
3 nothing more that I can add. The only thing I would add
4 is if we need to file -- what I think would be
5 appropriate would be a declaration of timely mailing,
6 that if you determine that's necessary, that we be
7 allowed to meet that specific requirement based on the
8 information that's in that exhibit, but I have nothing
9 more to present on that penalty today.

10 On the negligence penalty with the first audit
11 I would like to address the fact that it was the
12 taxpayer's first audit. A sizable chunk of that is due
13 to misunderstanding -- that audit is due to
14 misunderstandings of the law and an amount that we don't
15 believe is taxable anyway.

16 The taxpayer did have books and records at
17 that time. They presented a large volume of records to
18 the auditor. I know that it talks later about, you
19 know, this wasn't provided, this wasn't provided, but
20 they had 12 boxes at least of records. There was
21 significant items that were presented later that were
22 ignored by audit staff in various different intervals.

23 Those are things that don't really apply to
24 any of the issues that we have with the numbers now, but
25 they had records. They made a diligent effort to report

1 correctly, and it is generally the CDTFA's policy to
2 have some leniency on taxpayers when it's their first
3 audit. So we would ask that that be considered and
4 taken in its totality, and the penalty in the first
5 audit be removed.

6 Now, at the second audit when we look at the
7 adjustments that are in the second audit, the bulk of
8 the liability is going to be the these coupons. We've
9 already addressed the markup and brought it down to a
10 negligible amount. The difference between recorded and
11 reported should be brought down to a very minor,
12 negligible amount.

13 The additional taxable sales based on average,
14 that should be a small amount, and the unrecorded
15 amounts of 658,428, that is substantially these coupons,
16 which are still an issue and really not subject to taxes
17 in the first place. So based on that, even though this
18 was a repeated audit, they had similar errors as pointed
19 out in the audit working papers. The errors are still
20 reasonable and not due to negligence.

21 They had records in that audit. The records
22 were accepted in that audit, and no issue with the --
23 minor exception of the markup, which ended up being,
24 again, almost eliminated, and so we do don't believe the
25 negligence should apply in that audit either, and we ask

1 that it be removed based on that. That will conclude my
2 presentation right now.

3 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. Thank
4 you for your presentation. I did have a question for
5 you. When you were talking about the recorded versus
6 reported value of the coupons, and you had mentioned --
7 I think you said that the value of the coupons was not
8 recorded, and that there was evidence in the record to
9 support that. Can you explain a little bit more about
10 that and maybe point out some of what that evidence is?

11 MR. MICKEY: Well, there are comments that
12 clarify that the way the coupons were handled -- and you
13 can see it on the first audit. If you look at the sales
14 summaries -- let me see where they're at here. So if
15 you go to Exhibit C in the first audit, you'll see that
16 there are monthly summaries, and on monthly summaries
17 there is a column called breakfast coupon.

18 Those are the numbers of coupons that were
19 redeemed, but there's also comments and auditor's
20 verification talking with the taxpayer that the value of
21 the coupons -- I mean, I wish it was -- value of the
22 coupons is not record in the sales. Just the volume of
23 coupons are recorded in the sales.

24 So then what they were supposed to be doing is
25 they're going to take these coupons, multiply it by the

1 amount of the value, and the hotel was going reimburse
2 the restaurant, and nobody realized it was not taxable.
3 That's why the restaurant calculated the number, and the
4 auditor explains they put them in there and took them as
5 a deduction, and that's the best that we have.

6 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. Thank
7 you. Now I'm going check in with my co-panelist.

8 Judge Long, did you have any questions?

9 ADMINISTRATIVE LAW JUDGE LONG: Yes. Just a few
10 questions. First, regarding the reduction of unreported
11 taxable sales \$125,762, the wage ratio question, do you
12 have any documentary evidence for the wage ratio in 2014
13 other than the projected calculation from the 2013
14 federal return?

15 MR. MICKEY: No.

16 ADMINISTRATIVE LAW JUDGE LONG: No. There's no
17 documentation of wages paid in the hearing binders,
18 right?

19 MR. MICKEY: Not that I'm aware of.

20 ADMINISTRATIVE LAW JUDGE LONG: Okay. And then
21 I wanted to go to also the difference between the
22 recorded and reported that the redeemed coupons. I'm
23 not quite sure how to word this so bear with me.

24 If I'm the hotel guest, and I give the
25 restaurant my coupon, that is what you mean by

1 reduction, right?

2 MR. MICKEY: Yes.

3 THE COURT: And so I, the hotel guest, receive
4 the food?

5 MR. MICKEY: Yes.

6 ADMINISTRATIVE LAW JUDGE LONG: And can you
7 explain to me how that is not a sale?

8 MR. MICKEY: Oh. I'm not saying it wasn't a
9 sale. I'm saying there was no money transferred
10 between -- the way the law says -- 1603 says that that
11 type of transaction is basically a -- the hotel is the
12 consumer so the sale from the restaurant to the hotel
13 would be a taxable sale, but I don't disagree with that.

14 What we're saying is that if there was a sale
15 that took place, the restaurant was never reimbursed for
16 it. So the hotel never paid that. So if there is no
17 money exchanged, you still have a sale perhaps, but no
18 consideration is ever changed. So at worst you have a
19 bad debt deduction.

20 ADMINISTRATIVE LAW JUDGE LONG: Okay. And then
21 with respect to the affidavits and just in regard to how
22 much weight we should apply to that, is there an
23 relationship Mr. Sharma, the owner of India Star, and
24 Mr. Sharma, the owner of the hotel?

25 MR. MICKEY: Vinod Sharma is a member or part of

1 the hotel, and part of the restaurant.

2 ADMINISTRATIVE LAW JUDGE LONG: Okay.

3 MR. MICKEY: The LLC.

4 ADMINISTRATIVE LAW JUDGE LONG: And then --

5 MR. MICKEY: The other two are completely
6 independent, and I want to add that during the first
7 audit period -- this is very important. You bring up a
8 good point.

9 During the first audit period, Vinod Sharma
10 was active in the restaurant, but he did not -- was not
11 active -- I mean, he was active in the hotel. I'm
12 sorry. I misspoke -- active in the hotel, but another
13 gentleman, Harnek something, was running and in charge
14 of the restaurant, and so Vinod Sharma was not active in
15 the restaurant during the first audit period.

16 ADMINISTRATIVE LAW JUDGE LONG: Okay. And then
17 I just want to make sure that I'm clear. Regarding the
18 later -- the newer audit with respect to the breakfast
19 coupons, obviously, you argued that this measure of tax
20 should be reduced on the older audit for the breakfast
21 coupons. Is your position that the second audit's
22 unreported breakfast coupons should be reduced to zero
23 or to how much?

24 MR. MICKEY: Well, I believe they should be
25 reduced -- there's two arguments. They should be

1 reduced to zero because there was no money exchanged for
2 any of this, but the second audit period -- there's two
3 reasons why the breakfast coupons should be reduced.

4 It should be reduced because the volume of
5 redeemed coupons should be reduced down to what was
6 recorded, and the selling -- the value, if you will, of
7 the coupons should either should be the 3.49, which was
8 used during that period as evidenced by a sample of the
9 coupons that were provided and not the \$9 that was used
10 by the auditor; or secondarily, there's no basis for
11 using \$9 in that audit period if they're going to base
12 it on the first audit period, which was 7.95. So yes.
13 They should either be reduced for those two reasons or
14 eliminated entirely for the other reason.

15 ADMINISTRATIVE LAW JUDGE LONG: Okay. And then
16 I just have one last question regarding -- obviously bad
17 debt deductions kind of have their own set of rules.
18 Were bad debts deducted on Appellant's federal income
19 tax return?

20 MR. MICKEY: I don't know that.

21 ADMINISTRATIVE LAW JUDGE LONG: Okay. No
22 further questions. Thank you.

23 ADMINISTRATIVE LAW JUDGE RALSTON: Okay.
24 Hearing Officer Wilson.

25 HEARING OFFICER WILSON: Yes. I have a

1 question. In going Exhibit 1 on 12D, how did you
2 determine the split between alcohol and food on that?

3 MR. MICKEY: Okay. So that is the -- that's the
4 auditor's calculation. So on 12D if you look at
5 Exhibit 1 page 4 of 8, the -- let me find this. Okay.
6 So at the bottom. You see the yellow boxes and the
7 green boxes? So the green boxes and the -- so the
8 42,223 as an example for alcohol from 2013 and the
9 92,848, those are formulas inside there from the
10 auditor's schedule.

11 They did a segregation test and determined all
12 of that. So all we did was plug the different number --
13 that's why we have the black box around the yellow. The
14 only number we changed ourself were the two yellow ones.
15 The green, that changed because of the formulas in
16 there.

17 HEARING OFFICER WILSON: Okay. And then for the
18 markups that -- the new markups calculated, do you find
19 those to be reasonable?

20 MR. MICKEY: Well, actually, I find the food to
21 be high now, but --

22 HEARING OFFICER WILSON: And the alcohol?

23 MR. MICKEY: They look reasonable. I think
24 they're still reasonable. I think that they are --
25 yeah. I think they're reasonable.

1 HEARING OFFICER WILSON: Okay. So the next
2 schedule --

3 MR. MICKEY: I take that back. I don't think
4 the food is high, actually, for the type of food. I
5 think that's reasonable. It's in the range.

6 HEARING OFFICER WILSON: So the next schedule,
7 12B.

8 MR. MICKEY: 12B. Which one?

9 HEARING OFFICER WILSON: Your schedule 12B.

10 MR. MICKEY: Oh, yes. Okay.

11 HEARING OFFICER WILSON: So is the reason the
12 that only alcohol is because --

13 MR. MICKEY: That's what the auditors did. They
14 accepted the food markups as they were before, and they
15 only marked up the alcohol.

16 HEARING OFFICER WILSON: So with the adjustments
17 that you provided did you recalculate what the food --
18 if there was an error on the food since it's different?

19 MR. MICKEY: Actually, the percentage of markup
20 for both of them for the food increased based on what we
21 did because there were fewer purchases. So the
22 reflected markup went up on the food, and we just used
23 the same markup that the auditor used on the alcohol,
24 the 3.692. We didn't change that.

25 HEARING OFFICER WILSON: I might have some

1 questions later. That's it for now.

2 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. Thank
3 you.

4 Mr. Barnard, before we move on to the next
5 presentation, CDTFA is going to have about an hour to do
6 their hour presentation. Did you need break?

7 THE COURT REPORTER: Yes, please.

8 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. Great.
9 Then we'll take a break for about ten minutes, and --
10 well, we'll take a ten-minute break. Just remember if
11 you're staying in the room, that the microphones are on,
12 and it's still recording.

13 (The proceedings went off the record.)

14 ADMINISTRATIVE LAW JUDGE RALSTON: We are back
15 on the record in Star of India.

16 Mr. Samarawickrema, you have 60 minutes, and
17 please begin when you're ready.

18
19 PRESENTATION

20 MR. SAMARAWICKREMA: Thank you, Judge.
21 Appellant is a California limited liability company that
22 operated a restaurant with a bar located inside --

23 (The court reporter asked for clarification.)

24 MR. SAMARAWICKREMA: Appellant is a California
25 limited liability company that operates the restaurant

1 with a bar located inside of a hotel in Chico,
2 California. The hotel was operated by a separate
3 corporation. However, Mr. Vinod Kumar Sharma was an
4 officer at both the Appellant and the hotel.

5 The hotel had 172 guest rooms, and several
6 rooms for meetings and special events. Appellant also
7 offered room service to hotel guests and onsite special
8 events and banquet services. Hotel provided their
9 guests with breakfast coupons and discount coupons that
10 can be redeemed at Appellant's restaurant and bar.

11 Two audit periods are subject of this appeal.
12 For easier difference the Department is going to refer
13 to the audit April 1st, 2008, to March 31st, 2011, as
14 the first audit, and refer to the audit October 1st,
15 2012, to September 30th, 2015, as the second audit.

16 During the first audit period, Appellant
17 recorded total sale of around \$1.4 million and claimed
18 exempt food sales of around of \$1.1 million resulting in
19 reported taxable sale of around \$305,000, and this is
20 shown on Exhibit A, pages 16 and 17.

21 During the second audit period Appellant
22 reported total sale of around \$695,000 and claimed
23 exempt food sale of around \$25,000, and sales tax
24 reimbursement included a total sale of around \$16,000,
25 resulting in reported taxable sale of around \$654,000,

1 and this is shown on Exhibit J, pages 28 and 29.

2 During our presentation we will explain why
3 the Department rejected Appellant's reported total and
4 taxable sales for both audit periods; why the Department
5 used an indirect audit approach; how the Department
6 determined Appellant's unreported taxable sales; why the
7 Department recommended an egregious penalty; and why the
8 Department recommended a finality penalty for the second
9 period of for this Appellant.

10 During both audits Appellant failed to provide
11 complete sale records. Appellant did not provide
12 complete documents of original entry, such as cash
13 register receipts or guest receipts, credit cards sales
14 receipts, banquet sales contracts, banquet sales
15 invoices, complete sales journals, sales summaries to
16 support their reported sales for both audit periods.

17 In addition, Appellant failed to provide
18 complete purchase information or purchase journals for
19 both audit periods. For the first period Appellant
20 informed the Department that their manager was
21 responsible for preparing the sales and use tax returns
22 no longer worked for them, and therefore Appellant could
23 not explain how they reported their sales on their sales
24 and use tax returns.

25 Appellant was also unable to explain what

1 source they relied upon to find sales and use tax return
2 for the first audit period. For the second audit
3 Appellant informed they use guest checks to record
4 sales. The guest checks and credit cards sales
5 transactions were recorded onto the sales spreadsheet,
6 then the sales from the sales spreadsheets were recorded
7 onto a monthly sales journal, and these sales journals
8 are on Exhibit N.

9 These sales journals include sales for the
10 restaurant, bar, and banquets and also included the
11 number of breakfast coupons redeemed. In addition,
12 these sales journals segregated sales by method of
13 payment such as cash, credit cards, or room charge, and
14 these are shown on Exhibit N and Exhibit O.

15 Appellant indicated that these sales journals
16 were used to prepare their sales and use tax return for
17 the second audit period. However, Appellant failed to
18 provide source documents to verify the completeness of
19 sales reflected on these sales journals. Therefore, the
20 Department did not accept Appellant's reported taxable
21 sales for both audit periods due to lack of reliable
22 records.

23 The Department also determined that Appellant
24 did not provide complete records that could be verified
25 that are reported taxable sales for audit periods. The

1 Department completed five verification methods to
2 evaluate the accuracy of Appellant's reported taxable
3 sales. First, the Department analyzed Appellant's
4 reported sales for both audit periods, and these are
5 shown on Exhibit X, pages 2 through 5.

6 The Department ordered average daily reported
7 taxable sales of \$399 ranging from as low as \$111 to as
8 high as \$1072. Based on the business capacity, location
9 of the business, customer base, and the number of days
10 open for business, the Department views this as a very
11 low daily taxable sales for this business. For
12 comparison, Appellant's average taxable daily sales
13 based on our auditor taxable sales for both audits were
14 \$1,900.

15 Second, the Department analyzed Appellant's
16 profit and loss statement for periods April 2008 through
17 June 2009 and January 2013 through December 2014, and
18 compared the sales reflected on profit and loss
19 statement of around \$1.6 million with Appellant's
20 reported total sales for the same period. The
21 Department calculated an overall difference of around
22 \$563,000, and the information required to calculate
23 these differences are shown on Exhibit A, page 16;
24 Exhibit B, page 45; Exhibit J page 28; and Exhibit M.

25 Third, the Department reviewed

1 Appellant-provided federal income tax returns schedules
2 for years 2012 and 2013, and compared the sales
3 reflected on federal income tax return of around
4 \$629,000 with Appellant's reported total sales tax for
5 the same period. The Department calculated an overall
6 difference of \$198,000, and this calculation is on
7 Exhibit X, page 13.

8 The Department also analyzed cost of goods
9 sold amounts and other expense items reflected on
10 Appellant-provided federal income tax return schedules
11 for years 2012 and 2013. The Department noted explained
12 variances on cost of goods sold, wage expenses, rent
13 expenses, insurance expenses, and utilities.

14 For example, Appellant's cost of goods sold
15 was around \$63,000 for year 2012, around \$205,000 in
16 2013. Rent expenses were around 4,400 for year 2012 and
17 around \$67,000 in 2013, and utilities were \$15,000 for
18 year 2012 and around \$46,000 in 2013.

19 Appellant did not provide any source documents
20 or other reliable information to verify the information
21 reflected on Appellant's federal income tax returns
22 schedules. Based on these analyses the Department
23 determined that Appellant's federal income tax returns
24 schedules were unreliable and unacceptable.

25 Fourth, for the second audit the Department

1 compared reported total sale of around \$431,000 with a
2 cost of goods sold of around \$260,000 reflected on
3 Appellant's federal income tax returns schedules and
4 calculated and overall reported book mark of around
5 61 percent, and this calculation is on Exhibit X,
6 page 13. Based on the items sold, many prices, customer
7 base, services provided, and the location of the
8 business, the Department expected to see a higher book
9 markup than the reported book markup for this business
10 for this period.

11 Fifth, the Department attested Appellant did
12 sales worksheets for fourth quarter 2008, first
13 quarter 2009, and second quarter 2009, and noted total
14 sale of around \$353,000, but Appellant only reported
15 \$86,000, and these calculations are on Exhibit B,
16 page 17, and pages 33 through 42. Appellant did not
17 report more than 75 percent of their recorded sales on
18 daily sales worksheets for this period.

19 The Department also noted that Appellant
20 failed to record some of their daily sales amount in
21 their daily sales worksheets. Appellant was unable to
22 explain reasons for low average daily reported taxable
23 sales, sales differences in profit and loss statements,
24 federal income tax returns, daily sales worksheets, and
25 lower reported markups.

1 Therefore, the Department conducted further
2 investigation by analyzing Appellant's daily sales
3 worksheets for fourth quarter 2008, first quarter 2009,
4 and second quarter 2009, and monthly sales summaries for
5 second quarter 2008 to second quarter 2009 for the first
6 audit period. The Department used the information from
7 the first audit period, available sales journals for
8 first quarter 2013 through third quarter 2015, available
9 guest checks for September 2015, and available purchase
10 invoices for third quarter 2015 for the second audit
11 period.

12 For the first audit the Department noted that
13 guests of the hotel received coupons for breakfast in
14 Appellant's restaurant. For each coupon redeemed at the
15 restaurant the hotel paid Appellant \$7.95, excluding
16 sales tax reimbursement, and this is shown on Exhibit C,
17 page 40.

18 Using the 30 monthly summaries, the Department
19 noted that Appellant had accepted around 61,000
20 breakfast coupons, a monthly average of around 2,000
21 coupons. The Department used the recorded breakfast
22 coupons for 30 months, average monthly coupons, and the
23 price per coupon to determine auditor taxable breakfast
24 sales of around \$582,000 for the first audit period, and
25 these calculations are shown on Exhibit B, pages 23 and

1 24.

2 In addition to unreported taxable breakfast
3 sales the Department used Appellant's sales summaries
4 for second quarter 2008 and third quarter 2008, and
5 daily sales sheets for fourth quarter 2008 through
6 second quarter 2009, and determined that Appellant
7 collected sales tax reimbursement of around \$48,000
8 comprised of around \$5,900 from banquets for second
9 quarter 2008 and third quarter 2008, and around \$19,000
10 from the restaurant and around \$23,000 from the bar for
11 second quarter 2008 through third quarter 2009, and
12 these calculations are shown on Exhibit B, page 28.

13 For each monthly periods the Department
14 divided the recorded sales tax reimbursement collected
15 by applicable sales tax rates to determine audited
16 taxable sale of around \$653,000 for second quarter 2008
17 through second quarter 2009, which exceeded Appellant's
18 reported taxable sales for that period by around
19 \$497,000, and this calculation is shown on Exhibit B,
20 pages 27 and 28.

21 The Department also noted that Appellant's
22 daily sales sheets and monthly sales summaries showed
23 that Appellant recorded sales tax reimbursement of
24 around \$19,000 from the restaurant for second
25 quarter 2008 through second quarter 2009, and this is

1 shown on Exhibit B, page 29.

2 Using the applicable sales tax rates the
3 Department calculated that Appellant had collected sales
4 tax reimbursement on taxable restaurant sales of around
5 \$257,000 for this period. However, the Department noted
6 that Appellant had recorded total restaurant sale of
7 around \$292,000, excluding sales tax reimbursement for
8 the same period, and determined a difference of around
9 \$35,000 as additional unreported taxable restaurant
10 sales, and this is shown an Exhibit B, page 29.

11 The Department found that Appellant recorded
12 sales tax reimbursement of around \$5,900 from banquet
13 sales in their monthly sales summaries for second
14 quarter 2008 and third quarter 2008. It found no
15 recorded banquet sales for periods after third
16 quarter 2008. The Department determined that Appellant
17 had made banquet sales through the audit period.

18 Based on Appellant's recorded sales tax
19 reimbursement for banquet sales for second quarter 2008
20 and third quarter 2008, the Department determined
21 average taxable banquet sale of around \$41,000 per
22 quarter, and used this quarterly average to determine
23 unrecorded taxable banquet sale of around \$122,000 for
24 three quarters from fourth quarter 2008 to second
25 quarter 2009, and this is shown on Exhibit B, pages 31

1 and 32.

2 The Department found Appellant did not record
3 total daily sale amounts for seven days for restaurant
4 and 11 days for bar for fourth quarter 2008, and total
5 daily sales amount for six days for restaurant and three
6 days for second quarter 2009. Using average recorded
7 daily restaurant and bar sales amounts, the Department
8 determined the sales for these unrecorded sales amount
9 of around \$20,000 for fourth quarter 2008 and second
10 quarter 2009, and these calculations are shown on
11 Exhibit B, pages 35 through 41.

12 Based on these findings the Department
13 determined sales summaries for the first audit period,
14 except second quarter 2008 and third quarter 2008 to be
15 incomplete and unreliable because the amounts recorded
16 in the daily sales sheets exceed the amounts recorded in
17 monthly sales summaries.

18 As explained earlier the Department used the
19 monthly sales summaries and the daily sales sheets to
20 determine audited taxable sales, excluding audited
21 taxable breakfast sales for second quarter 2008 to
22 second quarter 2009, and these calculations are shown on
23 Exhibit B, pages 26 and 27.

24 The audited taxable sales, excluding audited
25 taxable breakfast sales, were compared with the

1 corresponding reported taxable sales to determine the
2 error rate of around 35 percent for second quarter 2008
3 through second quarter 2009. Appellant did not provide
4 any sales records for third quarter 2009 to first
5 quarter 2011. Therefore, the Department used this error
6 rate and reported taxable sales to determine unreported
7 taxable sale of around \$652,000 for third quarter 2009
8 to first quarter 2011, and this calculation is shown on
9 Exhibit B, page 25.

10 In total the Department determined unreported
11 taxable sale of around \$1.9 million for the first audit
12 period, and this calculation is shown on Exhibit B,
13 page 14. The Department then compared the total
14 underreported taxable sales with a reported taxable sale
15 of around \$306,000 to calculate the error rate of around
16 624 percent for the first audit period. Appellant also
17 did not provide complete sales record for the second
18 audit period.

19 Therefore, the Department conducted further
20 investigation by analyzing Appellant's available records
21 and the first audit information for the second audit
22 period. The Department analyzed the available guest
23 checks for September 2015 and sales amounts recorded in
24 Appellant's sales journals for first quarter 2013
25 through third quarter 2015. The Department noted that

1 the Appellant's redeemed coupons are recorded in their
2 sales journals, but sales amounts were not.

3 Therefore, based on the available guest checks
4 and sales journals the Department calculated sales made
5 with coupons redeemed for first quarter 2013 through
6 third quarter 2015, computing restaurant alcohol sale of
7 around \$16,000, bar alcohol sale of around \$248,000,
8 banquet alcohol sale of around \$900, and coupon alcohol
9 sale of around \$13,000, resulting in total sale of
10 alcohol beverage of around \$278,000, and these
11 calculations are on Exhibit J, pages 74 and 75.

12 The Department adjusted the alcohol beverage
13 sales for sales tax reimbursement, determining alcohol
14 beverage sales of around \$258,000. Similarly, the
15 Department determined the food sales from each source,
16 resulting in total for sale of around \$492,000, and
17 these calculations are on Exhibit J, pages 82 and 83.

18 Appellant added an 18 percent mandatory
19 gratuity charge to banquet sales and room services.
20 Based on recorded mandatory gratuities from room
21 services and total restaurant and bar tips reflected on
22 Appellant's guest checks for September 2015, the
23 Department determined the mandatory gratuity charge for
24 room service of around 14 percent, and this calculation
25 is on Exhibit J, page 93.

1 The Department used the recorded food and
2 alcohol banquet sales and 18 percent mandatory gratuity
3 rate to determine mandatory gratuities for food and
4 alcohol banquet sales and other banquet fees, and this
5 calculation is shown on Exhibit J, pages 90 and 91. The
6 Department then determined the mandatory gratuities of
7 around \$11,000 for first quarter 2013 through third
8 quarter 2015.

9 The Department then combined taxable sale of
10 around \$258,000 for alcohol beverages, \$492,000 for
11 food, \$11,000 in mandatory gratuities and fees, and
12 determined recorded taxable sale of around \$761,000 for
13 first quarter 2013 through third quarter 2015. The
14 Department then compared the recorded taxable sale of
15 around \$761,000 with reported taxable sale of around
16 \$556,000, and calculated unreported taxable sale of
17 around \$205,000 and an error rate of around 37 percent
18 for first quarter 2013 through third quarter 2015, and
19 these calculations are shown on Exhibit J, page 73.

20 Appellant did not provide sales journals for
21 fourth quarter 2012. In order to give a benefit to
22 Appellant the Department determined unreported taxable
23 sale of around \$19,000 for this period based on average
24 unreported taxable sale approach instead of 14 error
25 rate approach for fourth quarter 2012, and this is shown

1 an Exhibit J, page 72.

2 Had the Department determined the unreported
3 taxable sales using reported taxable sales and the error
4 rate of around 37 percent for fourth quarter 2012, then
5 the unreported taxable sales would increase by around
6 \$18,000 from around \$19,000 for \$37,000. As mentioned
7 earlier the Department noted Appellant recorded their
8 number of redeemed coupons in their sales journals but
9 not the sales amounts.

10 Therefore, the Department used Appellant's
11 sales journals for first quarter 2013 through third
12 quarter 2015 and scheduled around 19,000 breakfast
13 coupons redeemed during the 33-month period, and this is
14 shown on Exhibit J, page 86. When compared to the
15 around 16,000 breakfast coupons redeemed during the
16 30-month period in the first audit period, the
17 Department determined that the number of breakfast
18 coupons redeemed during the second audit period were
19 low, and this comparison was shown on Exhibit J, pages
20 68 and 69.

21 Appellant redeemed 68 breakfast coupons per
22 day during the first audit period, and Appellant
23 recorded only 19 breakfast coupons redeemed per day
24 during the second audit period. The Department compared
25 these average daily breakfast coupons with the number of

1 guest rooms in the hotel of 172 and determined average
2 daily breakfast coupon number of 19 for the second audit
3 is not reasonable. Therefore, the two breakfast coupon
4 averages were compared, and a monthly amount of about
5 1,500 and a quarterly difference of around 4,000 were
6 calculated, and this has shown on Exhibit J, page 69.

7 The Department determined the difference as
8 unrecorded breakfast coupons. Appellant contends that
9 the value of the breakfast coupon is only \$3.49 and has
10 provided sample coupons to support their contentions.
11 This is shown an Exhibit S, page 68.

12 However, at the time of the audit fieldwork
13 for second audit, Appellant's manager indicated that the
14 value of the coupons were \$8.99, and also based on
15 Appellant's own sales tax worksheets for second
16 quarter 2008. It was determined Appellant was being
17 reimbursed and \$7.95 by the hotel, and that Appellant
18 was taking a deduction for the reimbursed breakfast
19 amounts. Therefore, the quarterly unreported breakfast
20 coupons were multiplied by \$8.99 value received from the
21 hotel to determine unrecorded breakfast sale of \$476,000
22 for the second audit period, and these calculations are
23 shown Exhibit J, page 64.

24 Similarly, the Department used the taxable
25 banquet alcohol sale of around \$900, banquet food sale

1 of around \$8,300, and service charge of around \$1,900
2 recorded in the sale journal for first quarter 2013
3 through third quarter 2015 and divided them by 11
4 quarters to calculate the average quarterly taxable
5 banquet sales, totaling \$80 for alcohol, \$750 for food,
6 around \$200 for taxable service charge, and these
7 calculations are on Exhibit J, pages 67, 75, 76, 82, 83,
8 84 and 91.

9 In the first audit Appellant provided the
10 sales journals for second quarter 2008 and third
11 quarter 2008 with some detailed information on the
12 banquet sales, which were divided by two quarters to
13 calculate average quarterly taxable sale of around
14 \$2,000 for alcohol, around \$12,000 for food, and around
15 \$29,000 for service charges, rentals, and other fees.

16 The quarterly averages for second quarter 2008
17 and third quarter 2008 were compared to the quarterly
18 averages for first quarter 2013 through third quarter
19 2015, and the differences of around \$1,700 for alcohol,
20 \$11,000 for food, and around \$29,000 for service
21 charges, rentals, and other fees were calculated.

22 The service charge was substantially higher in
23 the first audit period, and therefore in order to give a
24 benefit to Appellant the Department calculated an
25 average quarterly service charge of around \$2,600 using

1 a percentage of around 20 percent derived from recorded
2 monthly averages of banquet food sales, alcohol sales,
3 and service charges.

4 The quarterly differences of banquet sales
5 alcohol, food, and service charges were multiplied by 12
6 quarters to determine unrecorded banquet sale of around
7 \$183,000 for the second audit period, and these
8 calculations are shown on Exhibit J, page 65. In total
9 the Department determined around \$658,000 in additional
10 unrecorded breakfast coupon sales and banquet sales for
11 the second audit period, and these calculations are on
12 Exhibit J, page 65.

13 To verify the reasonableness of the recorded
14 and unrecorded food and alcohol sales, the Department
15 analyzed Appellant's product mix, available purchasing
16 information, and pricing policies. To understand
17 Appellant's product mix the Department conducted a
18 purchase segregation using available merchandise
19 purchases invoices for second quarter 2015, and this
20 purchase segregation is shown on Exhibit J, pages 61
21 through 63. Based on this purchase segregation the
22 alcohol purchases total around \$7,000 and food purchases
23 total around \$30,000. Combined, the purchases for the
24 third quarter 2015 total around \$37,000.

25 The Department also scheduled alcohol and food

1 purchases in the first audit from the profit and loss
2 statement for second quarter 2008 through fourth
3 quarter 2009, and this is shown on Exhibit J, page 16.
4 The Department estimated that five percent of recorded
5 food purchases from the first audit were supplies so an
6 adjustment of five percent was made to the recorded
7 purchases for second quarter 2008 through fourth
8 quarter 2009. Based on the recorded alcohol purchases
9 and adjusted food purchases for second quarter 2008 to
10 fourth quarter 2009, the Department calculated average
11 quarterly purchases for alcohol of around \$20,000 and
12 food of around \$43,000.

13 The Department noted that the alcohol and food
14 purchases for third quarter 2015 was substantially lower
15 than for second quarter 2018 through fourth
16 quarter 2009. Based on this information the Department
17 determined that the merchandise purchase invoices for
18 third quarter 2015 were incomplete, and it appears that
19 Appellant failed to provide their complete purchase
20 invoices for this period.

21 Therefore, the Department used Appellant's
22 first audit purchase information to determine purchases
23 of around \$252,000 for year 2014. Even though the
24 Department did not accept the amount listed on
25 Appellant's federal income tax return schedules, it used

1 the cost of goods sold amount on Appellant's 2013
2 federal income tax return, which totaled around
3 \$205,000.

4 The Department also calculated the alcohol
5 purchase percentage of around 31 percent and food
6 purchase percentage of around 69 percent, and these
7 percentages are shown on Exhibit J, page 60. The
8 Department used this information with a recorded and
9 unrecorded food and alcohol sales for years 2013 and
10 2014 to calculate an alcohol markup of around 48 percent
11 and a food markup of around 153 percent for these four
12 years combined, and this is shown on Exhibit J, page 58.

13 To verify the reasonableness of alcohol
14 markup, the Department performed short shelf test using
15 Appellant's available alcohol purchase invoices with the
16 respective over pour and breakage allowances and
17 available selling prices, and calculated a weighted
18 average alcohol markup of around 269 percent, and this
19 calculation is shown on Exhibit J, page 56.

20 At the time of the audit fieldwork for second
21 audit the Department attempted to get additional
22 information to conduct the full shelf test. However,
23 Appellant did not provide the information that is
24 required to complete a full shelf test. This obstructed
25 the Department's ability to gather additional complete

1 facts to understand Appellant's pricing policies. It
2 also prevented the Department from determining
3 Appellant's actual alcohol markup.

4 Therefore, the Department used the best
5 available information to determine Appellant's alcohol
6 markup for the second audit period. Based on this shelf
7 test results the Department determined that it is
8 required to markup Appellant's alcohol purchases to
9 determine accurate alcohol sales for the second audit
10 period.

11 Even though the Department determined that
12 Appellant's federal income tax return schedules were
13 unreliable, it used the cost of goods sold reflected on
14 Appellant's 2013 federal income tax returns. Also, in
15 order to give a benefit the Appellant, the Department
16 assumed Appellant had the same cost of goods sold
17 amounts for year 2014 instead of estimating purchases
18 using the purchase information from the first audit, and
19 this is shown on Exhibit J, page 55.

20 Then the Department used the alcohol purchases
21 available for sales and weighted alcohol markup factor
22 of around 370 percent to determine audited alcohol sale
23 of around \$464,000 for years 2013 and 2014. The
24 Department then compared the audited alcohol sales with
25 recorded and unrecorded alcohol sales to determine

1 additional alcohol sales based on cost plus markup audit
2 method of around \$255,000 for the same period.

3 The additional alcohol sales based on cost
4 plus markup method was compared with recorded alcohol
5 sales and unrecorded alcohol sales at banquets to
6 calculate respective error rates for years 2013 and
7 2014, and these calculations are shown on Exhibit J,
8 page 55.

9 The Department used recorded alcohol sales and
10 unrecorded alcohol sales at banquet with respect to
11 error rates to determine additional alcohol sale of
12 around \$411,000 for the second audit period, and these
13 calculations are shown on Exhibit J, page 53. In total,
14 the Department determined unreported taxable sale of
15 around \$1.3 million for the second audit period, and
16 this calculation is shown on Exhibit J, page 52.

17 The Department then compared the total
18 unreported taxable sales with a reported taxable sale of
19 around \$654,000 to calculate the error rate of around
20 198 percent for the second audit period. The audit
21 calculation of unreported taxable sales for both audit
22 periods are based on the best available information was
23 reasonable.

24 When the Department is not satisfied with
25 accuracy or the sales and use tax return file, it may

1 rely upon any facts contained in the return or upon any
2 information that comes into the Department's possession
3 to determine if any tax liability exists, a taxpayer
4 shall maintain and make available for examination on
5 request by the Department all records necessary to
6 determine the correct tax liability under the sales and
7 use tax laws and all records necessary for the proper
8 completion of the sales and use tax returns.

9 When a taxpayer challenges a notice of
10 determination, the Department has the burden to explain
11 the basis for that deficiency. When the Department's
12 explanation appears reasonable, the burden of proof
13 shifts to the taxpayer to explain why the Department
14 asserted deficiencies not valued.

15 Since Appellant failed to provide necessary
16 records for both audit periods, the Department used the
17 best available information to determine the unreported
18 taxable sales for both audit periods. The audit
19 calculation of unreported taxable sales based on the
20 best available information was reasonable.

21 Appellant did not agree with the audit finding
22 for both audit periods. Prior to prehearing conference
23 statement dated April 4th, 2025, Appellant contended
24 that the value of the breakfast is only \$3.49 rather
25 than the value using the second audit of \$8.99 per

1 person. This is shown on Exhibit R, page 2.

2 However, Appellant changed their previous
3 argument and now claim that the hotel did not reimburse
4 them for the breakfast coupons provided to hotel guests
5 for the period April 2008 to September 2015. Now
6 Appellant is arguing that Appellant provided free
7 breakfast for guests of the hotel, and this is contrary
8 to Appellant's previous representative email
9 communication, and this is shown an Exhibit R, page 2.

10 Appellant also contended that the sales
11 calculated in the second audit period are incorrect
12 because the Department used the results of the first
13 audit period. Moreover, Appellant disputed estimated
14 alcohol purchases for years 2013 and 2014. As support,
15 Appellant provided a declaration from office manager and
16 the general manager of the hotel and Appellant's member,
17 and they're stating that the hotel did not reimburse
18 Appellant for the breakfast coupons provided to hotel's
19 guests for the period April 2008 to September 2015.

20 Appellant also provided part of their federal
21 income tax returns for years 2013 and 2014 to argue that
22 the cost of goods sold amount reflected on Appellant's
23 federal income tax return include wages. Using this
24 information Appellant calculated alcohol sales
25 adjustment of around \$285,000 for the second audit

1 period, and these calculations are shown on Appellant's
2 Exhibit 1.

3 Appellant also requested several other
4 adjustments, including \$168,000 for breakfast coupon
5 sales, and these other adjustments are on Appellant's
6 Exhibit 2 and 3. The Department analyzed the
7 information and ultimately rejected it.

8 The Department ordered that Appellant made
9 inconsistent arguments regarding the arrangement that
10 they had with the hotel regarding breakfast coupons, but
11 Appellant failed to provide any agreements that they had
12 with the hotel, and any of the area of viable
13 information other than three new declarations.

14 Appellant also failed to provide their
15 complete alcohol and food purchase invoices to support
16 the purchase amount reflected on Appellant's Exhibit 2.
17 As stated previously the Department used Appellant's
18 cost of goods sold reflected on their 2013 federal
19 income tax return to give a benefit to Appellant.

20 Had the Department estimated the purchases
21 based on the purchases reflected on Appellant's first
22 audit period to determine alcohol sales for the second
23 audit period, then the unrecorded alcohol sales would
24 increase by around \$167,000 from around \$411,000 to
25 \$578,000, and the information Appellant required to

1 calculate these amounts are on Exhibit J, pages 54 and
2 55.

3 Therefore, the Department finds that the
4 estimated amount, as is in these two audits, are not
5 only reasonable but also benefit the Appellant. The
6 Department imposed a negligence penalty for both audit
7 periods based upon its determination that Appellant's
8 books and records were incomplete and inadequate for
9 sales and use tax returns and because Appellant failed
10 to accurately report their taxable sales for both audit
11 periods.

12 The Department generally does not impose an
13 negligence penalty with the taxpayer has not been
14 previously audited. Nevertheless, even in connection
15 with the first audit, the imposition of the negligence
16 penalty is warranted if there's evidence established
17 that any bookkeeping and reporting errors cannot be
18 attributable to the taxpayer's good faith, and a
19 reasonable belief that its bookkeeping and reporting
20 practices were in substantial compliance with the
21 requirements of the sales and use tax floor or
22 regulations.

23 Relevant factors such as general state of the
24 books and records and the Appellant's business
25 experience must be considered, and when the evidence

1 clearly shows that the understatement is due to
2 negligence, then the penalty applies even when the
3 Appellant has not been previously audited.

4 Specifically, the Department noted that the
5 Appellant failed to provide complete records for both
6 audit periods, and Appellant failed to provide complete
7 books and records to support their reported taxable
8 sales. Appellant's failure to provide complete books
9 and records for the both audit periods are evidence of
10 negligence.

11 In addition, the audit examination disclosed
12 unreported taxable sale of around \$3.2 million, which,
13 when compared with the reported taxable sale of around
14 \$960,000 for both audit periods, resulted in a combined
15 error rate of around 333 percent. This high combined
16 error rate is additional evidence of negligence.

17 Finally, the Department imposed a finality
18 penalty because the determination for the second period
19 became final on February 20th, 2016, and Appellant did
20 not file a timely petition for redetermination and did
21 not make a full payments towards the determination by
22 this date. However, the Department recommended waiving
23 the finality penalty for the second audit period if
24 Appellant pays the full liability within 30 days of the
25 date of notice of the redetermination for the second

1 audit period.

2 In conclusion, when Appellant did not provide
3 complete books and records, the Department was unable to
4 verify the accuracy of reported taxable sales using a
5 direct audit method. Therefore, an alternate audit
6 method were used to determine unreported taxable sales
7 for both audit periods.

8 Accordingly, the Department determined there
9 are reported taxable sales for both audit periods based
10 upon the best available information. The evidence shows
11 that the audits produced reasonable results. Appellant
12 has not provided any reasonable documentation or
13 evidence to support an adjustment to the audit finding.

14 Therefore, for all of these reasons the
15 Department requests appeal be denied. This concludes
16 our presentation. We are available to answer any
17 questions the panel may have. Thank you.

18 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. Thank
19 you. I did have a question. I know you addressed it,
20 but I didn't catch everything you said. So if you could
21 just answer again where the Appellant has stated that
22 some of the federal information tax returns incorrectly
23 contain wage information in the -- I believe in the cost
24 of goods sold.

25 So what was CDTFA's response to that?

1 MR. SAMARAWICKREMA: I didn't understand your
2 question.

3 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. So the
4 Appellant stated that -- I think it was the 2014 federal
5 tax return contained labor amounts or wages in the cost
6 of goods sold, and I thought you addressed it during
7 your presentation, but I missed part of what you said.

8 MR. SAMARAWICKREMA: Yeah. Exhibit X. The last
9 page of the exhibit. Exhibit X, page 13.

10 ADMINISTRATIVE LAW JUDGE RALSTON: Okay.

11 MR. SAMARAWICKREMA: We compared the line 17,
12 the cost of goods sold according to the federal income
13 tax return, but instead of 62,000, compared 2013. And
14 also --

15 MR. PARKER: Judge Ralston, one thing we did
16 note in the 2014, they had cost of goods sold of 190,000
17 without any adjustment for the wages. The Appellant's
18 representative made an adjustment for that so there's no
19 evidence of that. On the 2013 the information on cost
20 of goods sold does show a line item four, wages.
21 However, the taxpayer hasn't provided the purchase
22 invoices to verify that the information on the income
23 tax returns is correct.

24 The information for the cost of wages may be
25 other items that they may have separated out -- food

1 purchases versus alcohol purchases. Obviously, we can't
2 verify the information because we don't have the
3 purchases available. So we were going with the best
4 available information we had, and as Mr. Samarawickrema
5 mentioned in the presentation, the cost of goods sold in
6 the earlier audit period were significantly higher, and
7 if we used similar amounts in this -- in the second
8 audit period, the alcohol sales would have gone up
9 tremendously. Does that sort of answer the question?

10 ADMINISTRATIVE LAW JUDGE RALSTON: Yes. Thank
11 you. So I think that is all my questions. Judge Long,
12 did you have any questions?

13 ADMINISTRATIVE LAW JUDGE LONG: No questions.
14 Thank you.

15 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. And
16 Hearing Officer Wilson, did you have any questions?

17 HEARING OFFICER WILSON: I do not. Thank you.

18 ADMINISTRATIVE LAW JUDGE RALSTON: Thank you.
19 Okay.

20 So Mr. Mickey, you have about ten minutes for
21 rebuttal. So please begin when you're ready.

22
23 CLOSING STATEMENT

24 MR. MICKEY: Okay. Regarding the income tax
25 return figures, the -- I know that the Department is

1 going to argue exactly what they argue, but we're
2 looking at what the best available information is. They
3 used that repeatedly. Best available information. The
4 CDTFA auditors routinely look at income tax returns and
5 whether they have backup documents or not. If it serves
6 their purpose, they use the information on income tax
7 returns. Countless audits are based on income tax
8 returns.

9 Auditors generally take the cost of goods sold
10 or the purchases sometimes, don't even -- and ignore the
11 cost of goods sold off the income tax returns almost
12 routinely. Now, I get that there were records that were
13 maybe not provided. I don't know whether they were in
14 those 12 boxes of records that the auditor initially had
15 -- well, this is the second audit so I don't know what
16 happened on this audit, but this information, to say
17 that the cost of labor might be something else like food
18 purchases, that's not very reasonable in our opinion.

19 And when you look at the tax returns, you can
20 see -- even if you look at the Exhibit X, page 13, you
21 see that for 2012 there is a wage amount, okay, and
22 there's a wage amount of 96,000 on there, and the
23 purchases are lower, 62,000. And then in 2013 it goes
24 up to 204,000. So by the preponderance of the evidence
25 it's real clear that the 204,947 that's on the income

1 tax return is the most accurate number that they had.

2 You might also note that in the file there are
3 copies of the P&Ls that the auditors just ignored based
4 on their argument that the records weren't shown to
5 verify them. Those purchases are less than what's on
6 here.

7 So this is even a higher number, and to say
8 now that if they would have used an estimate based on
9 the prior audit, it would have been higher, I mean, they
10 could use any estimate and make it higher if they wanted
11 to. We're looking for what the right number is here,
12 the best number, and so to say you can't use or you
13 shouldn't use the 2013 figures because they could have
14 used another kind of estimate and come up with a higher
15 number, that's not reasonable, either. They should look
16 and be consistent with what they do, and so we will hold
17 that the 2013 simple change in the cost of goods sold
18 figure is valid.

19 Now, in their presentation there's a lot of
20 other information that leads up to how they did the
21 whole audit, and I can't disagree with most of what he
22 said. It's just a play-by-play action of what happened
23 with the audit. We're not even addressing those issues.

24 I'm simply saying that the best information
25 available for the 2013 markup analysis is the tax return

1 that they previously accepted. Whether they did a
2 benefit or not, they recognized it, they accepted it.
3 I'm just now directing that number. That's all we're
4 asking for.

5 And when it comes to 2014, again, yes, you're
6 absolutely right. I don't have a breakdown for it, but
7 when you -- auditors do this all the time, too. They
8 look at the reasonableness, and they look at the all
9 these other facts. They have comment after comment
10 based on their -- you know, looking at the business
11 location and the nature of the business, they make the
12 decisions.

13 We're just simply saying that if you look at
14 the 2013-2014 total figures, and you acknowledge that on
15 those tax returns, which I've shown you, there is not a
16 line item for wages. That is very, very reasonable --
17 in my view meets the preponderance of the evidence --
18 that the 2014 in total is a lump sum figure that also
19 includes the wages, and that's why we did what we did.
20 That's how we calculated the 34 percent being for wages,
21 and the 66 percent for cost of goods sold -- the true
22 cost of goods sold.

23 I don't know what else to say. I think that
24 this is the best information. I think it's typically
25 information that is used by auditors. It would have

1 been used if they would have had this information, this
2 breakdown, they probably would have used it. I can't
3 speak for them, but the fact is we have it now, and it
4 should be used. It's a simple change in the audit
5 calculations.

6 Second thing, on the difference between
7 recorded and reported. In the second audit period where
8 I've explained and shown you that there's 167,565 in
9 coupons there. I'm simply asking you to recognize that
10 that 167,565 is not a difference between recorded and
11 reported. That, if anything, it should have been part
12 of the column K, and it should be added to the 475,605.

13 I'm just identifying that. Within that
14 205,155 there is the 167,565 in coupons that are not in
15 there, and by their admission they acknowledge that the
16 -- you asked the question earlier, too. They answered
17 it there -- is that these coupons were recorded in the
18 sales journal at volume, but the sales amounts were not.
19 So you can't include the 167,565 in that difference. It
20 needs to be moved and combined with the other coupons of
21 475,605.

22 Then when you make that adjustment, that
23 followthrough adjustment from the 18,651 on schedule
24 12G, which is my Exhibit 3 I think it was, that's just a
25 natural mathematical follow through based on the

1 procedure, and that's why that changes. And so there
2 shouldn't be any question with that, and that -- I don't
3 have anything more, any other questions.

4 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. Thank
5 you. I'm just going the check in with my panel one more
6 time to see if they have any questions.

7 Judge Long.

8 ADMINISTRATIVE LAW JUDGE LONG: No questions.
9 Thank you.

10 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. And
11 Hearing Officer Wilson.

12 HEARING OFFICER WILSON: No questions. Thank
13 you.

14 ADMINISTRATIVE LAW JUDGE RALSTON: Okay. So it
15 looks like we are ready to conclude the hearing.
16 Today's hearing in the Star of India LLC is now
17 adjourned, and the record is closed. The panel will
18 meet and decide your case later on, and we will send you
19 a written opinion of our decision within 100 days.
20 Thank you, everybody, for attending.

21 (The proceedings concluded at 12:02 P.M.)
22
23
24
25

C E R T I F I C A T E O F R E P O R T E R

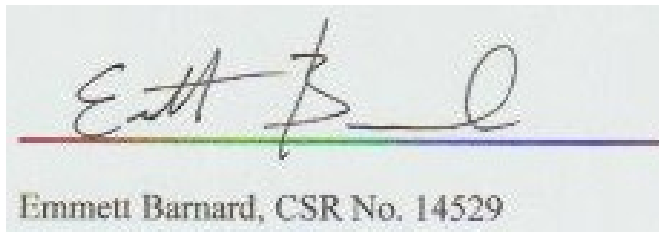
I, EMMETT BARNARD, do hereby certify:

That I am a disinterested person herein; that the foregoing Office of Tax Appeals hearing was reported in shorthand by me, Emmett Barnard, a Certified Shorthand Reporter of the State of California.

That the said proceedings were taken before me, in shorthand writing, and was thereafter transcribed, under my direction, by computer-assisted transcription.

I further certify that I am not of counsel or attorney for any of the parties to said hearing nor in any way interested in the outcome of said hearing.

IT WITNESS WHEREOF, I have hereunto set my hand this 12th day of June, 2025.



Emmett Barnard, CSR No. 14529

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\$			
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\$1,700 57:19	\$23,000 49:10	\$492,000 53:16	1,500 56:5
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