OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Claims for Reimbursement of:)) **STARBUZZ INTERNATIONAL, INC. AND**) **STARBUZZ TOBACCO, INC.**)))	OTA Case No.: 240415936

OPINION ON REIMBURSEMENT CLAIMS

Representing the Parties:

For Claimants:	Mardiros H. Dakessian, Attorney Joshua Lin, Attorney Alma Martinez, Representative
For Respondent:	Pamela Bergin, Assistant Chief Counsel Stephen Smith, Attorney Andrew Amara, Attorney

A. WONG, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 30458.9 and California Code of Regulations, title 18, (Regulation) section 30701(b), Starbuzz International, Inc., and Starbuzz Tobacco, Inc. (claimants) request reimbursement of fees and expenses from respondent California Department of Tax and Fee Administration (CDTFA). Claimants expended the requested fees and expenses while appealing CDTFA's denials of their separate claims for refund for the combined period of October 1, 2012, through September 30, 2015 (claim period) to the Office of Tax Appeals (OTA).[1] Pursuant to Regulation section 30213.5, claimants also request that OTA sanction CDTFA for statements made in its petition for rehearing (PFR).

Office of Tax Appeals (OTA) Panel Members Andrew Wong, Suzanne B. Brown, and Steven Kim held an oral hearing for this matter in Cerritos, California, on October 14, 2025. At the conclusion of the oral hearing, the record was closed, and this matter was submitted on the oral hearing record pursuant to Regulation section 30209(b).

[1] Claimants' underlying appeals were OTA Case Nos. 19034546 and 19034547 and involved the Cigarette and Tobacco Products Tax Law, which the State Board of Equalization (BOE) formerly administered. On July 1, 2017, BOE administrative functions relevant to claimants' appeals transferred to CDTFA. (See Gov. Code, § 15570.22.) For ease of reference, when this Opinion on Reimbursement Claims refers to acts or events that occurred before July 1, 2017, "CDTFA" refers to BOE.

ISSUES

1. Whether CDTFA's actions and position during claimants' appeals before OTA were unreasonable and warrant reimbursement of claimants' fees and expenses.[2]
2. Whether CDTFA should be sanctioned.

FACTUAL FINDINGS

1. During the claim period, claimants reported and paid to CDTFA the tobacco products excise tax on their distributions of shisha.
2. Shisha is a product containing molasses, flavorings, and tobacco.
3. Claimants' shisha contained less than 50 percent tobacco.
4. Shisha is heated and smoked in a hookah, a type of water pipe.
5. Former R&TC section 30121(b), which was in effect during the claim period, defined taxable "tobacco products," which "includes, but is not limited to, all forms of cigars, smoking tobacco, chewing tobacco, snuff, and any other articles or products made of, or containing at least 50 percent, tobacco, but does not include cigarettes."
6. Claimants filed separate claims for refund asserting that their shisha distributions during the claim period were not subject to tax because their shisha contained less than 50 percent tobacco and thus was not a taxable "tobacco product." As a result, claimants argued that the tax paid to CDTFA should be refunded to claimants.
7. CDTFA denied claimants' refund claims based on its determination that shisha was a taxable "tobacco product"—specifically a form of "smoking tobacco," distributions of which were subject to tax regardless of tobacco content (in CDTFA's view). CDTFA based its determination on its interpretation of former R&TC section 30121(b), which CDTFA summarized in a Cigarette and Tobacco Products Tax Annotation entitled "Tobacco Products—Tobacco Content" (pub. 9/27/1996) (Annotation).
8. In this Annotation, CDTFA wrote that tax "applies to all forms of cigars, smoking tobacco, chewing tobacco, and snuff, regardless of the amount of tobacco they contain. In

[2] This issue statement synthesizes two related issue statements the parties agreed to during a pre-hearing conference with OTA. One issue is whether CDTFA's position regarding the following was unreasonable and warrants reimbursement of claimants' fees and expenses: former R&TC section 30121(b) (in effect from January 1, 1989, through March 31, 2017); the Cigarette and Tobacco Products Tax Annotation entitled "Tobacco Products—Tobacco Content" (published on September 27, 1996) (Annotation); and this Annotation's published backup letter. Another issue is whether CDTFA's petition for rehearing and subsequent briefings constituted unreasonable actions warranting reimbursement of claimants' fees and expenses. OTA addresses these issues below.

addition, the tax applies to any other articles or products which are made entirely of tobacco or contain at least 50 percent tobacco, excluding cigarettes."

9. The Annotation summarized a backup letter drafted by CDTFA's acting assistant chief counsel in response to a request from the administrator of CDTFA's Excise Taxes Division for an opinion regarding the definition of "tobacco products" in former R&TC section 30121(b).[3]

10. In the Annotation's backup letter, CDTFA wrote, "The definition [of 'tobacco products'] in Section 30121 can be interpreted in two ways, depending on whether the clause 'made of, or containing at least 50 percent[,] tobacco" is read to qualify all the items listed before it in the definition only or only 'any other articles or products.' In interpreting this section, we can be guided by the manner in which similar language in federal law has been interpreted." After analyzing the interpretation of similar language in federal law, the backup letter reached the conclusion summarized in the Annotation: the tax "applies to all forms of cigars, smoking tobacco, chewing tobacco, and snuff, regardless of the amount of pure tobacco they contain. In addition, the tax applies to any other articles or products which are made entirely of tobacco or contain at least 50 [percent] tobacco, but excluding cigarettes."

11. Claimants filed a timely appeal with OTA regarding CDTFA's denial of their refund claims.

12. On January 27, 2021, a panel of three administrative law judges (Original Panel) held an online oral hearing on claimants' appeals.

13. On April 28, 2021, the Original Panel issued a unanimous Opinion (2023-OTA-195) (Original Opinion), which concluded that claimants' shisha distributions for the claim period were not subject to tax and granted claimants' claims for refund in full. Specifically, after analyzing the language of former R&TC section 30121(b), various canons of construction, and extrinsic aids, as well as utilizing reason, practicality, and common sense, the Original Opinion concluded, "In summary, we find the statutory definition of 'tobacco products' to be ambiguous. Although both the interpretations argued by the parties are reasonable when viewed in light of the statutory language and purpose, based on practical considerations, we find [claimants' interpretation] is slightly more so. Moreover, given that these interpretations stand in relative equipoise, we resolve this ambiguity in favor of [claimants]. [Citations.] Accordingly, we find that

[3] The backup letter is available on CDTFA's website at the following web address: https://cdtfa.ca.gov/lawguides/annotations/section-30121b-tobacco-products-che.pdf.

'tobacco products,' as defined in former R&TC section 30121(b), are only those items which are made of, or contain, at least 50 percent tobacco."

14. On May 26, 2021, CDTFA timely filed a PFR with OTA.

15. On September 9, 2021, the majority of a new three-member panel (PFR Panel) issued an Opinion on Petition for Rehearing (2023-OTA-196) (PFR Opinion), which granted CDTFA's PFR.[4] The PFR Panel's majority found the language of former R&TC section 30121(b) to be clear and unambiguous, and concluded that the Original Opinion's findings were contrary to law and the Original Opinion incorrectly disposed of claimants' appeals.[5]

16. Subsequently, claimants petitioned the Orange County Superior Court for a writ of mandate, alleging that the PFR Panel's majority improperly applied the contrary-to-law standard when granting CDTFA's PFR. In their petition, claimants named OTA as respondent and CDTFA as a real party in interest.

17. Ultimately, claimants, OTA, and CDTFA settled the writ-of-mandate matter by agreeing that a third OTA panel (Rehearing Panel) would decide whether the PFR Panel's majority properly granted CDTFA's PFR.[6]

18. On January 19, 2023, the Rehearing Panel held an in-person rehearing in Cerritos, California.[7]

19. On March 15, 2023, the Rehearing Panel issued a unanimous Opinion on Rehearing (2023-OTA-197) (Opinion on Rehearing), which reached the following conclusions: (a) the Original Opinion's conclusion that the statutory definition of "tobacco products" in former R&TC section 30121(b) is ambiguous could be valid according to the law, and could not be contrary to law for lack of direct and binding authority; (b) CDTFA failed to establish that a ground for rehearing existed; and (c) the PFR Panel's majority erred in granting CDTFA's PFR. In reaching these conclusions, the Opinion on Rehearing noted that the PFR Panel's majority conducted an independent analysis of the law instead of

[4] The PFR Panel consisted of one member of the Original Panel and two new members. The two new members formed the majority granting CDTFA's PFR.

[5] The holdover member of the Original Panel dissented, concluding that CDTFA's PFR should be denied because CDTFA failed to establish that the Original Opinion was contrary to law.

[6] The Rehearing Panel would also have decided a second issue: whether claimants' shisha distributions for the claim period were subject to the tobacco products excise tax. However, the Rehearing Panel ultimately determined that this second issue was moot because of the Rehearing Panel's conclusion on the first issue of whether the PFR Panel properly granted CDTFA's PFR.

[7] The rehearing was OTA Case No. 21098578.

evaluating whether the Original Opinion could be valid according to the law.[8] The Opinion on Rehearing also noted that the issue of how to interpret former R&TC section 30121(b) was an issue of first impression.

20. The Rehearing Opinion became final on April 14, 2023.

21. On April 12, 2024, claimants timely filed with OTA their claims for reimbursement of fees and expenses from CDTFA. Claimants further asked OTA to consider sanctioning CDTFA for certain statements made in its PFR.

22. On October 14, 2025, OTA held a hearing on this matter.

DISCUSSION

Issue 1: Whether CDTFA's actions and position during claimants' appeals before OTA were unreasonable and warrant reimbursement of claimants' fees and expenses.

In their claims for reimbursement, claimants assert that CDTFA took two actions that were unreasonable. First, claimants allege that CDTFA disregarded its own "published guidance" in arguing that former R&TC section 30121 was clear and unambiguous throughout OTA's appeal process. Second, claimants allege that CDTFA's filing of a PFR was unreasonable because the PFR lacked any basis in law or fact. Specifically, according to claimants, rather than addressing whether OTA's Original Opinion was contrary to law based on the applicable legal standard for granting a PFR, CDTFA's PFR "did nothing more than rehash its losing arguments" regarding the substantive issue decided by the Original Opinion.

Every taxpayer is entitled to be reimbursed for any reasonable fees and expenses related to an appeal before OTA if, as relevant here, OTA, in its sole discretion, finds that the action taken by a governmental agency that is a party to an appeal before OTA was unreasonable. (Cal. Code Regs., tit. 18, §§ 30102(d), 30701(b), 30702; see also R&TC, § 30458.9(a).) To determine whether a governmental agency's action was unreasonable, OTA will consider whether that governmental agency has established that its position was "substantially justified." (Cal. Code Regs., tit. 18, § 30702; see also R&TC, § 30458.9(b).)

"Substantially justified" does not mean "justified to a high degree." (*Pierce v. Underwood* (1988) 487 U.S. 552, 565.) Rather, a "substantially justified" position means one which is justified to a degree that would satisfy a reasonable person or has a reasonable basis both in law and fact. (*Agnew v. State Bd. of Equalization* (2005) 134 Cal.App.4th 899, 909.) Using the word "reasonable" to explain "substantially justified" implies an objective standard that does not

[8] In dicta, the Opinion on Rehearing also mentioned that it would not have reached the Original Opinion's conclusions on the merits of the substantive issue in the underlying appeal.

depend on an analysis of the subjective motivations of the government in taking the position it did. (*Ibid*.) As relevant here, CDTFA's position does not need to be accepted by OTA; so long as CDTFA's position is one that a reasonable person could think is correct, it may be substantially justified even in the face of conflicting evidence. (See *ibid*.)

Here, as a preliminary matter, OTA echoes the Opinion on Rehearing: how to interpret the definition of "tobacco products" in former R&TC section 30121(b) was an issue of first impression. The parties did not present (and OTA was not aware of) any direct and binding authority, including any precedential opinions from the California Supreme Court or appellate courts, dictating how this subdivision must be interpreted.[9] Against this backdrop, the Original Opinion, after extensive analysis, found the statutory language of former R&TC section 30121(b) to be ambiguous, and that both interpretations backed by claimants and CDTFA stood in "relative equipoise" and were reasonable (though claimants' interpretation was slightly more reasonable). Thus, as relevant here, CDTFA's position on the underlying merits of that appeal (i.e., how to interpret former R&TC section 30121(b)) was substantially justified.

Regarding claimants' first argument that CDTFA disregarded its own "published guidance" in arguing that former R&TC section 30121 was clear and unambiguous throughout their underlying appeal, the "published guidance" referenced by claimants is the backup letter (a.k.a., a legal ruling of counsel) to CDTFA's Annotation.

Annotations are summaries of the conclusions reached in selected legal rulings of counsel. (Cal. Code Regs., tit. 18, § 35101(a)(1).) A "legal ruling of counsel" is a legal opinion written and signed by CDTFA's Chief Counsel or an attorney who is the Chief Counsel's designee, addressing a specific inquiry, including an inquiry from a taxpayer or taxpayer representative, a local government agency, or CDTFA staff. (Cal. Code Regs., tit. 18, § 35101(a)(2).) Annotations provide notice of the existence of, and conclusions reached in, selected legal rulings of counsel regarding the application of the statutory law, regulatory law, or judicial opinions to a particular factual circumstance. (Cal. Code Regs., tit. 18, § 35101(c)(1).) Annotations are published as a research tool to locate selected legal rulings of counsel and thus provide guidance regarding the interpretation of statutes and CDTFA regulations as applied by CDTFA staff to specific factual situations in legal rulings of counsel. (Cal. Code Regs., tit. 18, § 35101(c)(2).) Annotations do not have the force and effect of law. (Cal. Code Regs., tit. 18, § 35101(a)(1).)

[9] This case is distinguishable from *Lucent Technologies, Inc. v. Board of Equalization* (2015) 241 Cal.App.4th 19, where CDTFA's arguments regarding technology transfer agreement statutes were foreclosed by existing precedent (much of it by the California Supreme Court) and federal copyright law, and were also rejected by the Legislature and a binding, on-point appellate court case.

Here, an acting assistant chief counsel of CDTFA drafted the Annotation's backup letter in response to a request from the administrator of the Excise Taxes Division for an opinion regarding the definition of "tobacco products" in former R&TC section 30121(b). The alleged "published guidance" in question is the following sentence appearing in the backup letter: "The definition in Section 30121 can be interpreted in two ways, depending on whether the clause 'made of, or containing at least 50 percent tobacco' is read to qualify all the items listed before it in the definition or only 'any other articles or products.'" However, contrary to claimants' first argument, OTA finds that this does not constitute "published guidance," but rather context for the analysis provided in, and the conclusion reached by, the backup letter, which the Annotation subsequently summarized. The "published guidance" is the conclusion summarized in the Annotation, not the background information prefacing the backup letter's analysis. Thus, OTA finds that CDTFA did not disregard its own "published guidance" in arguing that former R&TC section 30121 was clear and unambiguous.

Further, even if CDTFA had changed its interpretation of former R&TC section 30121(b) over time, an administrative tax agency may change its interpretation of a statute, rejecting an old construction and adopting a new one. (See *Fujitsu IT Holdings, Inc. v. Franchise Tax Bd.* (2004) 120 Cal.App.4th 459, 471.) An administrative tax agency is not disqualified from changing its mind. (*Ibid*.) Thus, even if CDTFA "disregarded" a prior interpretation of former R&TC section 30121(b), OTA finds that it was permitted to do so.

Finally, OTA notes that in granting CDTFA's PFR, the PFR Panel's majority independently analyzed former R&TC section 30121(b), and, contrary to the Original Opinion's analysis and holding, found the statutory definition of "tobacco products" to be plain, clear, and unambiguous. This accords with CDTFA's argument during the underlying appeal. If reasonable minds differ on the merits of a tax agency's position, then the tax agency's position is, by definition, "substantially justified." (*Lennane v. Franchise Tax Bd.* (1996) 51 Cal.App.4th 1180, 1189.) Here, at least two different OTA panels reached different conclusions on the clarity and ambiguity of former R&TC section 30121(b), indicating that CDTFA's position was reasonable and thus substantially justified. Accordingly, for the reasons stated, OTA is not persuaded by claimants' first argument.

Regarding claimants' second argument (i.e., CDTFA unreasonably rehashed its "losing arguments" in its PFR rather than addressing whether OTA's Original Opinion was contrary to law based on the applicable legal standard for granting a rehearing on that basis), OTA cannot conclude that either CDTFA's action of filing a PFR or the position taken in the PFR were unreasonable. According to claimants, from the time OTA began hearing appeals in 2018 until

CDTFA filed its PFR in the underlying appeals on May 26, 2021, parties before OTA filed 87 PFRs (77 by taxpayers and 10 by tax agencies). In 44 of those 87 PFRs, parties reiterated their arguments on the underlying merits of their appeal (41 out of 77 taxpayer-filed PFRs; 3 out of 10 tax agency-filed PFRs). If parties in at least half of the PFRs filed with OTA through May 26, 2021, were reiterating their arguments on the merits, OTA cannot say that such an action was unreasonable or that such an approach would not satisfy a reasonable person.

Further, regarding CDTFA's position in its PFR in the underlying appeals, OTA need not accept that position for it to be reasonable or substantially justified. A taxing agency's position need not be accepted by OTA as long as the tax agency's position is one that a reasonable person could think is correct. (See *Agnew v. State Bd. of Equalization*, *supra*, 134 Cal.App.4th at 909; see also *Fujitsu IT Holdings, Inc. v. Franchise Tax Bd.*, *supra*, 120 Cal.App.4th at 487.) But here, CDTFA's position *was* accepted by OTA when the PFR Panel's majority granted CDTFA's PFR. Although the Opinion on Rehearing later concluded that the PFR Panel's majority erred in doing so, the fact remains that the PFR Panel's majority accepted CDTFA's position in its PFR. On these facts, OTA cannot conclude that CDTFA's PFR position was unreasonable even though it was ultimately unsuccessful. Thus, for the reasons stated, OTA is not persuaded by claimants' second argument.

In summary, OTA concludes that CDTFA's position regarding former R&TC section 30121(b), the Annotation, and the Annotation's backup letter were reasonable. Further, OTA cannot conclude that CDTFA's PFR, its subsequent briefings, and the positions it took therein constituted unreasonable actions or positions. Accordingly, OTA concludes that reimbursement of claimants' fees and expenses is not warranted.

Issue 2: Whether CDTFA should be sanctioned.

In their claims for reimbursement, claimants argue that CDTFA, in its PFR, "mocked and attacked the integrity" of the members on the Original Panel and this conduct is reprehensible, unreasonable, and sanctionable. In response, CDTFA contends that it did not engage in sanctionable conduct, arguing that its briefings criticized the Original Opinion's analysis but never attacked OTA's integrity.

Pursuant to OTA's Rules for Tax Appeals, OTA may issue orders and sanctions to the parties to facilitate the fair, efficient, and orderly resolution of appeals. (Cal. Code Regs., tit. 18, § 30213.5.) Orders may be enforced under the provisions of Government Code sections 11455.10 through 11455.30. (*Ibid*.) As relevant here, a person is subject to the

contempt sanction for any of the following in an adjudicative proceeding before an agency:[10] (a) disobedience of or resistance to a lawful order; (b) refusal to take the oath or affirmation as a witness or thereafter refusal to be examined; (c) obstruction or interruption of the due course of the proceeding during a hearing or near the place of the hearing by: (1) disorderly, contemptuous, or insolent behavior toward the presiding officer while conducting the proceeding, (2) breach of the peace, boisterous conduct, or violent disturbance, or (3) other unlawful interference with process or proceedings of the agency; (d) violation of the prohibition of ex parte communications; or (e) failure or refusal, without substantial justification, to comply with a deposition order, discovery request, subpoena, or other order of the presiding officer, or moving, without substantial justification, to compel discovery. (Gov. Code, § 11455.10.)

Based on the above, claimants' allegations against CDTFA could only possibly implicate Government Code section 11455.10(c)(1), which involves obstructing or interrupting the due course of the proceeding during a hearing or near the place of the hearing by disorderly, contemptuous, or insolent behavior toward the presiding officer while conducting the proceeding. However, subdivision (c)(1) only authorizes OTA to sanction parties for conduct occurring during, or at least relating to, evidentiary hearings and proceedings, not for arguments found in a party's briefs. Accordingly, OTA finds that nothing in CDTFA's PFR, which is a brief, is sanctionable under Regulation section 30213.5. Thus, OTA concludes that CDTFA should not be sanctioned.

[10] "Adjudicative proceeding" means an evidentiary hearing for determination of facts pursuant to which an agency formulates and issues a decision. (Gov. Code, § 11405.20.)

HOLDINGS

1. CDTFA's actions and position during claimants' appeals before OTA (including CDTFA's PFR) were not unreasonable and do not warrant reimbursement of claimants' fees and expenses.
2. CDTFA should not be sanctioned.

DISPOSITION

Claimants' claims for reimbursement of fees and expenses and request for sanctions are denied.

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Andrew Wong
Administrative Law Judge

We concur:

Signed by:
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Suzanne B. Brown
Administrative Law Judge

DocuSigned by:
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Steven Kim
Administrative Law Judge

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