

1 CALIFORNIA STATE BOARD OF EQUALIZATION

2 APPEALS DIVISION FINAL ACTION SUMMARY

3 In the Matter of the Petition for Redetermination)
 4 Under the Sales and Use Tax Law of:)
 5 KNA CHO CORPORATION,) Account Number SR EH 52-043548
 6 dba Joey's Pizza) Case ID's 611137, 658121
 7 Petitioner) Ontario, San Bernardino County

7 Type of Business: Restaurant

8 Liability periods: 07/01/08 – 05/30/10 (Case ID 611137)

9 06/01/10 – 06/30/11 (Case ID 658121)

10 Item	Case ID 611137	Case ID 658121		
11 Unreported taxable sales	\$107,826	\$93,490		
	<u>611137</u>	<u>658121</u>		
	<u>Tax</u>	<u>Penalty</u>	<u>Tax</u>	<u>Penalty</u>
13 As determined and protested	\$17,886.76	\$1,788.70	\$12,483.47	\$1,248.35
14 Post-D&R adjustments	- 6,165.79	<u>-1,788.70</u>	<u>- 4,303.08</u>	<u>-1,248.35</u>
15 Post-Board hearing adjustment	<u>- 2,486.13</u>			
15 Proposed redetermination	<u>\$ 9,234.84</u>	<u>\$ 00.00</u>	<u>\$8,180.39</u>	<u>\$ 00.00</u>
16 Proposed tax redetermination	\$ 9,234.84		\$8,180.39	
16 Interest through 12/31/14	<u>3,016.62</u>		<u>1,923.69</u>	
17 Total tax, and interest	<u>\$12,251.46</u>		<u>\$10,104.08</u>	
18 Monthly interest beginning 01/01/15	<u>\$ 46.17</u>		<u>\$ 40.90</u>	

19 The Board held a hearing regarding this matter on October 15, 2014, granting petitioner 20
 20 days to provide additional records and the Sales and Use Tax Department (Department) 20 days to
 21 respond. Based on petitioner's submissions and the Department's response, we recommend that the
 22 liability determined for the third quarter 2008 (3Q08) and 4Q08 be deleted, since the waiver of the
 23 statute of limitations for those quarters was invalid. We recommend no other adjustment, as discussed
 24 below under Post Hearing Developments.

25 UNRESOLVED ISSUE

26 **Issue:** Whether further reductions are warranted to the amounts of unreported taxable sales.
 27 We find no further reductions are warranted, other than the deletion of the liability determined for
 28 3Q08 and 4Q08.

1 Petitioner has operated a restaurant since March 2006 serving hot food products such as pizza,
2 pasta, chicken, and steak. The restaurant is open seven days a week. Two Notices of Determination
3 are at issue. Both determinations were the result of field billing orders (FBO's) issued after an
4 examination of petitioner's books and records. The Department issued the first determination for the
5 period July 1, 2008, through May 30, 2010, due to an expiring statute of limitations waiver. The
6 Department issued the second determination for the period June 1, 2010, through June 30, 2011, after
7 completing its examination. For the FBO periods, petitioner provided its federal income tax return for
8 2008, some merchandise purchase invoices, daily sales summaries, and bank statements. Petitioner did
9 not provide any guest checks or cash register tapes to support the sales recorded in its daily sales
10 summaries. The Department found that total sales recorded in the sales summaries substantially
11 agreed with total sales reported on the sales and use tax returns, but that gross receipts reported on the
12 federal income tax return exceeded total sales reported on the sales and use tax return for 2008.
13 Further, the Department concluded that gross receipts reported on the federal income tax return for
14 2008 were also understated. Consequently, the Department concluded that petitioner's books and
15 records were not reliable and that recorded sales were understated. Thus, the Department decided to
16 establish audited taxable sales using a credit card sales ratio analysis.

17 On October 13, 2011, from 10:14 a.m. to 8:45 p.m. the Department observed petitioner's
18 business operations. Using the cash register tape, the Department calculated a ratio of credit card sales
19 to total sales of 47.58 percent. Similarly, for the period October 14, 2011, through October 19, 2011,
20 petitioner used cash register tapes to calculate a credit card sales ratio of 45.72 percent. The
21 Department combined the results to calculate a credit card sales ratio of 45.87 percent, and it used that
22 percentage and recorded credit card deposits to establish unreported taxable sales of \$356,170 for both
23 FBO periods combined. In preparing these matters for Board hearing, we found that both the
24 Department and Appeals had concluded that petitioner's credit card sales ratio for "catering sales"
25 would be higher than the credit card sales ratio of 45.87 percent, but the Department had not
26 incorporated that higher ratio in its audit computations. Consequently, after further consideration, the
27 Department conducted a reaudit that allowed a credit card sales ratio of 70 percent on catering sales
28 that resulted in a reduction of unreported taxable sales to \$233,395 for both FBO periods combined.

1 The computation of the understatement in the adjusted FBO's effectively considered the entire
2 understatement to represent catering sales. Thus, the Department computed the amount of credit card
3 receipts that would have been applicable to reported taxable sales, by multiplying reported taxable
4 sales by 45.87 percent. The Department then used the remaining credit card receipts and the credit
5 card to total sales ratio of 70 percent to compute the understatement. We find that the use of the higher
6 estimated credit card to total sales ratio to compute the entire understatement was favorable to
7 petitioner, especially since this adjustment was made in the absence of supporting evidence.

8 Petitioner contends that taxable sales were properly reported for the FBO periods. Further,
9 petitioner asserts that there was duplication in the measure of unreported taxable sales established for
10 the period April 1, 2010, through May 30, 2010, in a separate NOD that was allegedly issued to sole
11 proprietor Kyung S. Cho (SR EH 100-731448). We find the evidence petitioner provided insufficient
12 to support its contention that taxable sales were properly reported. Petitioner has not provided any
13 documentation to support any additional adjustments. Further, we find the NOD issued to the sole
14 proprietor was cancelled and that there was no duplication in the measure of unreported taxable sales.
15 Accordingly, we find no further reductions are warranted.

16 **RESOLVED ISSUES**

17 At the conference, the Department recommended deletion of the negligence penalties on the
18 basis it was petitioner's first audit and because the Department concluded that petitioner made a
19 reasonable effort to properly report its taxable sales by hiring an accountant to prepare its sales and use
20 tax returns. We concur in the Department's recommendations and we recommend the penalties be
21 deleted.

22 **POST HEARING DEVELOPMENTS**

23 During the Board hearing, the Department conceded that the liability determined for 3Q08 and
24 4Q08 should be deleted since the waiver of the statute of limitations for that period was invalid.
25 Specifically, the waiver had been signed by Mr. Kyung S. Cho, as a sole proprietor, at a time when the
26 Department knew that the business was a corporation, rather than a sole proprietorship. As noted
27 above, the adjustment to delete the liability for those two quarters has been made.

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At the Board hearing, petitioner also argued that the understatement for the entire period was excessive, and, as stated previously, the Board granted petitioner 20 days to provide records related to catering sales and dining room sales. Petitioner’s representative provided four credit card receipts for catering sales made in October 2014 and December 2013. The representative provided nothing further, although the Department asked him to provide detailed merchant statements for two quarters. The Department concluded that the additional records were not sufficient to support further adjustment, and we concur.

Summary prepared by Deborah A. Cumins, Business Taxes Specialist III