

CALIFORNIA STATE BOARD OF EQUALIZATION
APPEALS DIVISION BOARD HEARING SUMMARY

In the Matter of the Petition for Redetermination)
Under the Sales and Use Tax Law of:)
H K CUISINE, INC., dba Hana Sushi-Red Hawk) Account Number SR EH 100-867040
Petitioner) Case ID 522224
Temecula, Riverside County

Type of Business: Restaurant
Audit period: 03/01/07 – 03/31/09

<u>Item</u>	<u>Disputed Amount</u>	<u>Tax</u>	<u>Penalty</u>
Unreported taxable sales	\$149,400		
As determined		\$36,405.89	\$3,640.61
Post-D&R adjustment		- 12,949.02	- 1,294.90
Proposed redetermination		\$23,456.87	\$2,345.71
Less concurred		- 11,878.35	- 2,345.71
Balance, protested		<u>\$11,578.52</u>	<u>\$ 00.00</u>
Proposed tax redetermination		\$23,456.87	
Interest through 04/30/12		6,572.52	
Negligence penalty		<u>2,345.71</u>	
Total tax, interest, and penalty		\$32,375.10	
Payments		- 1,000.00	
Balance Due		<u>\$31,375.10</u>	
Monthly interest beginning 05/01/12		<u>\$ 131.00</u>	

UNRESOLVED ISSUE

Issue: Whether adjustments are warranted to the amount of unreported taxable sales. We find no further adjustment is warranted.

Petitioner operates a Japanese restaurant with a sushi bar. The Sales and Use Tax Department computed book markups of 103.36 percent for the period March 1, 2007, through December 31, 2007, and 84.21 percent for the first three quarters of 2008, which were much lower than the expected markup of at least 200 percent. It also noted that, of the \$1,480,736 deposited in the bank for the period April 1, 2007, through December 31, 2008, only \$15,751 represented deposits of cash or

1 checks. Further, of that amount, \$14,800 represented petitioner's capital contributions rather than sales
2 receipts. Thus, the Department concluded that petitioner deposited virtually no proceeds from cash
3 sales into the bank. Based on an observation test and the sales summary for August 2008, the
4 Department computed an understatement of reported taxable sales of \$469,753. After the appeals
5 conference, the Department concluded that the August 2008 sales summary was not a reliable
6 representation of petitioner's overall business, and proposed that unreported cash sales be computed by
7 adding bank deposits from credit card sales to cash purchases. Petitioner agreed with this approach but
8 contended that additional reductions should be made for voluntary tips included in bank deposits. It
9 contends that there often was not enough cash in the cash register to pay its employees the tips that had
10 been charged to credit cards. As support, petitioner provided four cancelled checks, one of which was
11 made out to cash, two of which were made out to one of the corporate officers, and the remaining one
12 was made out to another of the corporate officers.

13 We find that the cancelled checks are not persuasive evidence that petitioner withdrew cash
14 from its bank account to pay tips to its employees. Since petitioner held only one business checking
15 account, any payments to the corporate officers must have been made from that account. Accordingly,
16 we find it more likely that the cancelled checks represented payments of wages or other distributions to
17 corporate officers, rather than cash needed to pay tips to employees. Further, we find it unlikely that
18 petitioner would use all available cash for purchases each day and then withdraw cash from the bank to
19 pay tips to employees rather than to use checks to pay for purchases and pay tips to employees from
20 cash on hand. Accordingly, we agree with the Department's proposed approach without the claimed
21 adjustment for tips included in bank deposits, and we recommend no further adjustment.

22 **RESOLVED ISSUE**

23 The Department applied the negligence penalty because it found that petitioner's records were
24 inadequate for sales and use tax purposes and because of the amount of understatement. Although
25 petitioner had disputed the entire amount determined, it conceded at the appeals conference that the
26 understatement was the result of negligence. Thus, it no longer protests the negligence penalty.

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OTHER MATTERS

None.

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