STATE BOARD OF EQUALIZATION
CIGARETTE AND TOBACCO PRODUCTS TAX APPEAL

**CALIFORNIA STATE BOARD OF EQUALIZATION**

**APPEALS DIVISION BOARD HEARING SUMMARY**

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| In the Matter of the Petition for Redetermination Under the Cigarette and Tobacco Products Tax Law of:<br><br>ASHRAF ALFONOSE YOUSSEF, dba<br>The Liquor Chest, aka Encino Cigar Company<br><br>Petitioner | Account Number CP ET 50-002284<br>Case ID 358704<br><br>Granada Hills, Los Angeles County |

Type of Business: Distributor of tobacco products

Audit period: 10/01/99 – 04/30/02

| Item | Disputed Amount | |
|---|---|---|
| Unreported cost of tobacco products distributed | $1,895,586 | |
| Fraud Penalty | $ 275,701 | |
| | Tax | Penalty |
| As determined | $1,124,383.95 | $281,096.02 |
| Post-D&R adjustment | - 21,579.57 | - 5,394.91 |
| Proposed redetermination, protested | $1,102,804.38 | $275,701.11 |
| Proposed tax redetermination | $1,102,804.38 | |
| Interest through 12/25/12 | 1,073,588.99 | |
| Fraud penalty | 275,701.11 | |
| Total tax, interest, and penalty | $2,452,094.48 | |
| Payments | - 200,900.01 | |
| Balance Due | $2,251,194.47 | |
| Monthly interest beginning 12/26/12 | $ 4,509.52 | |

This matter was scheduled for Board hearing in April 2012, but was postponed at petitioner's request to allow time to hire a new representative. It was rescheduled for hearing in October 2012 and the case was called, but the Board agreed to postpone the appeal to its December meeting because petitioner requested an interpreter.

**UNRESOLVED ISSUES**

**Issue 1:** Whether petitioner is liable for tax on purchases and distributions of untaxed tobacco products and whether any adjustment is warranted. We find petitioner is liable for the tax, and no adjustment is warranted.

Petitioner distributed various products for resale, delivering them to small groceries and liquor stores from his own motor vehicle. The Excise Tax and Fees Division of the Property and Special Taxes Department (Department) investigated petitioner after receiving tips that he was selling tobacco products at prices well below market averages. Using bank records and some source documents seized during the execution of a search warrant and information from unlicensed out-of-state vendors and the United Parcel Service, the Department determined that petitioner had purchased tobacco products from 29 unlicensed out-of-state vendors, 28 of which sold only tobacco products. The Department used the available records to compile petitioner's purchases of untaxed tobacco products during the audit period. Based on additional records provided both before and after the appeals conference, the Department made adjustments to purchases from one vendor, and it made an adjustment for ending inventory. After those adjustments, the audited amount of purchases of untaxed tobacco products from out-of-state suppliers of $1,914,461 exceeds reported amounts of $18,875 by $1,895,586.

Petitioner contends that, without purchase invoices to support every transaction, the Department cannot sustain the established measure of tobacco products purchased, and contends that the established measure should be adjusted for spoilage. In addition, petitioner states that he had a humidor containing unsold tobacco products, and that those products in ending inventory should not be included in the established measure. Finally, based on his allegation that there are so many "open issues" regarding this matter, petitioner argues that the measure should be reduced to the amount determined in the criminal proceedings against him in the Superior Court of California, Los Angeles County, which he asserts totaled approximately $150,000.[1]

The Department may compute and determine the amount to be paid based on any information available to it. (Rev. & Tax. Code, § 30201.) We find that neither court case cited by petitioner, which found that the established amount of income tax had been based on insufficient evidence, is applicable here because the Department has obtained records of purchases of tobacco products from 29 unlicensed out-of-state vendors, and those records provide substantial evidence of the amount of

[1] The Department states that the court ordered petitioner to pay restitution of $199,000, but neither party has provided documentation. In any event, we find that order is irrelevant here, except to the extent payments made per the order are applied to the liability.

petitioner's purchases. Since petitioner has not overcome the presumption that the purchases were untaxed and distributed, except for the product remaining in petitioner's possession, we find the tax is properly imposed. (Rev. & Tax. Code, § 30109.) We find no adjustment is warranted for spoilage because petitioner obtained credit from vendors for spoiled tobacco products, and those credits have been taken into account in the audit calculations. We also find petitioner has not shown that the adjustment already made for ending inventory should be increased. Thus, we find petitioner is liable for tax on the distribution of untaxed tobacco products, and no adjustment is warranted.

**Issue 2:** Whether the Department has proven fraud by clear and convincing evidence. We find that it has.[2]

As support for the finding of fraud, the Department notes, among other things, that: 1) petitioner was found guilty by the Los Angeles Superior Court of a felony count and two misdemeanor counts of tax evasion; 2) petitioner was actively involved in the daily business operations; 3) petitioner knowingly made false statements to the Department; and 4) petitioner's purchases of untaxed tobacco products of $1,914,461 exceeded reported purchases of $18,875 by 10,043 percent. Petitioner disputes the penalty on the basis that his statements to the Department regarding the business should be disregarded because English is not his first language.

Petitioner is an experienced businessman who was very familiar with the tobacco products distribution industry in general and with the excise tax laws in particular. Nevertheless, he reported less than 1 percent of his purchases of untaxed tobacco products from unlicensed out-of-state vendors. Regarding petitioner's argument that English is not his first language, we find that without regard to this factor, the Department has established fraud by clear and convincing evidence. In any event, we have reviewed the statements petitioner made to the Department and find they are clear and detailed, and that there is no indication that petitioner misunderstood the issues. We find that the Department has established fraud by clear and convincing evidence, and that the penalty was properly applied.

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[2] Absent a finding of fraud, the determination would not have been timely for any portion of the audit period, since it was issued more than three years from the last day of the month following the most recent quarterly period in the audit period.



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## OTHER MATTERS

None.

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