

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:
B. MOSHER

) OTA Case No. 19014157
) CDTFA Case ID: 780905
) CDTFA Acct. No. 53-012087
)
)
)

OPINION

Representing the Parties:

For Appellant:

Marc Brandeis, CPA

For Respondent:

Amanda Jacobs, Tax Counsel III
Stephen Smith, Tax Counsel IV
Jason Parker, Chief,
Headquarters Operations Bureau

For Office of Tax Appeals:

Matthew D. Miller, Tax Counsel III

S. BROWN, Administrative Law Judge: Pursuant to California Revenue and Taxation Code (R&TC) section 6561, B. Mosher (appellant) appeals a decision by respondent California Department of Tax and Fee Administration (CDTFA)¹ on appellant’s timely petition for redetermination of an October 30, 2013 Notice of Determination (NOD) for tax of \$526,044.91 and penalties of \$109,964.19, plus applicable interest. The NOD reflects CDTFA’s determination that, pursuant to R&TC section 6829, appellant is personally liable for the unpaid sales and use tax liabilities of Blue Velvet, LLC (Blue Velvet) for the period July 1, 2006, through September 15, 2010.

Office of Tax Appeals (OTA) Administrative Law Judges Suzanne B. Brown, Nguyen Dang, and Kenneth Gast held an oral hearing for this matter in Cerritos, California, on

¹ Sales taxes were formerly administered by the State Board of Equalization (BOE). In 2017, functions of the BOE relevant to this case were transferred to CDTFA. (Gov. Code, § 15570.22; 2017 Stats. 2017, ch. 16, § 5.) For ease of reference, when this opinion refers to acts or events that occurred before July 1, 2017, “CDTFA” shall refer to BOE; when referring to acts or events that occurred on or after July 1, 2017, “CDTFA” shall refer to CDTFA.

February 19, 2020. At the conclusion of the hearing, the record was closed, and this matter was submitted for decision.

ISSUES

1. Whether appellant is liable under R&TC section 6829 for Blue Velvet's unpaid sales and use tax liabilities for the period April 1, 2007, through December 31, 2009.
2. Whether there is reasonable cause to relieve the penalty under R&TC section 6565 (finality penalty) imposed on Blue Velvet that was included in appellant's liability under R&TC section 6829.
3. Whether adjustments are warranted to Blue Velvet's sales and use tax liabilities for the fourth quarter of 2009 (4Q09).
4. Whether CDTFA properly applied certain payments to Blue Velvet's liability.

FACTUAL FINDINGS

1. Blue Velvet, a California limited liability company (LLC), operated two businesses in Los Angeles, California: Moxie coffee shop and Blue Velvet restaurant. It held a seller's permit that was effective March 14, 2006.
2. Blue Velvet's operating agreement designates appellant as Blue Velvet's sole member and Tax Matters Member, authorizing him to represent the company in all examinations of the company's affairs by taxing authorities.
3. During the periods of their employment with Blue Velvet, general manager, R. Hartstein, and bookkeeper, M. Winner, frequently sent emails to appellant regarding Blue Velvet's financial matters, including daily sales reports. In an email dated October 8, 2007, Mr. Hartstein informed appellant that Blue Velvet was having cash flow issues and wrote the following: "As it stands now, every dollar we make goes into keeping the operations running, including revenue generated from sales tax." On the same date, appellant sent a reply email indicating that he and Mr. Hartstein should review Blue Velvet's daily payroll breakdown for the past 30 days.
4. On Blue Velvet's daily financial reports from its Micros point-of-sale system for the period December 1, 2007, through December 27, 2007, the information on each report included a category titled "Sales Tax Month to date," followed by tax amounts for each of Blue Velvet's two locations.

5. On February 17, 2009, Blue Velvet filed a statement of information with the California Secretary of State. Appellant signed the statement as Blue Velvet’s “managing member.”
6. Appellant signed business checks on behalf of Blue Velvet, including a February 3, 2009 check to a supplier, West Coast Produce, for \$332.25, and an April 27, 2009 check to CDTFA for \$946.
7. In August 2009, CDTFA began an audit of Blue Velvet, and thereafter issued a Report of Audit Findings dated November 1, 2010. Based on that audit report, CDTFA issued to Blue Velvet an NOD dated January 31, 2011, for the period July 1, 2006, through March 31, 2010 (audit period). Subsequently, CDTFA conducted a reaudit and made various adjustments that reduced Blue Velvet’s audit liability, including eliminating the liability for 3Q06 through 1Q07.
8. On December 24, 2012, CDTFA received a payment of \$23,000 from the sale of Blue Velvet’s liquor license. CDTFA applied that payment towards Blue Velvet’s tax liability. On November 24, 2015, Blue Velvet’s bankruptcy trustee made a payment of \$34,713.82 to CDTFA. CDTFA applied this payment to Blue Velvet’s liabilities for the period April 15, 2010, through September 15, 2010.
9. In the audit of Blue Velvet, the auditor wrote comments entered into CDTFA’s computer system that stated: “Sales tax reimbursements were added to the sales of food and included in the selling price of bar drinks.”
10. On April 15, 2010, Blue Velvet filed a voluntary petition for Chapter 11 bankruptcy in the United States Bankruptcy Court for the Central District of California. Appellant signed the petition as Blue Velvet’s authorized agent. On September 27, 2010, CDTFA received a copy of Blue Velvet’s motion to dismiss the Chapter 11 bankruptcy, stating that the business terminated on September 15, 2010. Based on this information, CDTFA closed Blue Velvet’s seller’s permit effective September 15, 2010.
11. In October 2009, February 2010, and October 2010, appellant signed Waivers of Limitation for CDTFA on behalf of Blue Velvet, listing his title as “managing member” or “owner and managing member.”
12. Blue Velvet’s Alcohol Beverage Control license information lists appellant as Blue Velvet’s “managing member.” On March 31, 2010, appellant signed an agreement for the transfer of Blue Velvet’s liquor license to a third party.

13. On November 12, 2010, Blue Velvet’s bankruptcy was converted to Chapter 7.
14. Blue Velvet did not pay the January 31, 2011 NOD before it became final; as a result, a 10-percent finality penalty was imposed.
15. In June 2013, Mr. Hartstein sent a letter to CDTFA in response to a Responsible Person Questionnaire, and Ms. Winner provided her response to CDTFA’s Business Operations Questionnaire. Mr. Hartstein indicated that he was an employee of Blue Velvet until February 2008, and Ms. Winner indicated that she was an employee of Blue Velvet until August 2008. Their responses indicated that Blue Velvet had charged sales tax or collected sales tax reimbursement on items sold.² According to an Automated Compliance Management System (ACMS)³ entry dated June 17, 2013, Mr. Hartstein confirmed that “sales tax was charged and collected” by Blue Velvet during its operation.
16. On October 30, 2013, CDTFA issued the above-referenced NOD finding appellant personally liable for Blue Velvet’s unpaid sales and use tax liabilities. Appellant filed a timely petition for redetermination, and this appeal followed. On December 6, 2018, CDTFA issued a Decision that removed Blue Velvet’s liability for 2010 from the period of appellant’s liability and decreased the amount of appellant’s liability, specifically by reducing the taxable measure from \$6,043,896 to \$4,070,675.
17. In the present appeal, CDTFA confirmed that April 1, 2007, through December 31, 2009 (liability period), is the only disputed period at issue for appellant’s derivative liability under R&TC section 6829.⁴

² In appellant’s response to a Responsible Person Questionnaire, he indicated that he did not know whether sales tax reimbursement was charged or collected.

³ ACMS is a software program used by CDTFA to document communications between compliance staff and taxpayers or their representatives.

⁴ CDTFA states the earliest quarter in which Blue Velvet has an unpaid liability is 2Q07, and thus the first date of appellant’s derivative liability is April 1, 2007. In its prehearing conference statement and at the hearing, CDTFA also conceded that appellant is not personally liable for any periods after December 31, 2009.

DISCUSSION

Issue 1. Whether appellant is liable under R&TC section 6829 for Blue Velvet's unpaid sales and use tax liabilities for the period April 1, 2007, through December 31, 2009.

R&TC section 6829 provides that a person is personally liable for the tax, penalties, and interest owed by a business entity, such as an LLC, if all the following elements are met: (1) the LLC's business has been terminated, dissolved, or abandoned; (2) the LLC collected sales tax reimbursement on its sales of tangible personal property (TPP) and failed to remit such tax reimbursement to CDTFA; (3) the person had control or supervision of, or was charged with the responsibility for, the filing of returns or the payment of tax, or was under a duty to act for the LLC in complying with the Sales and Use Tax Law; and (4) the person willfully failed to pay taxes due from the LLC or willfully failed to cause such taxes to be paid. (R&TC, § 6829(a) & (c); Cal. Code Regs., tit. 18, § 1702.5(a) & (b).) CDTFA bears the burden of proving, by a preponderance of the evidence, that the requirements of R&TC section 6829 have been satisfied. (Cal. Code Regs., tit. 18, § 1702.5(d).)

Here, appellant concedes that Blue Velvet's business operations have terminated. Accordingly, we analyze only the remaining disputed elements.

Collection of Sales Tax Reimbursement

As relevant here, personal liability can be imposed only to the extent the LLC collected tax reimbursement on its sales of TPP in this state, but failed to remit the tax to CDTFA when due. (R&TC, § 6829(c); Cal. Code Regs., tit. 18, § 1702.5(a).)

In this case, we find that Blue Velvet's contemporaneous business records are evidence of collection of sales tax reimbursement. The daily financial reports for December 1, 2007, through December 27, 2007, reveal daily sales totals from the cafe and restaurant by type (e.g., food, liquor, beer, wine) and include a line item for each business's "Sales Tax Month to date." When those amounts of sales tax are added to the amounts of sales for each of Blue Velvet's locations, the totals equal the amounts listed in each report's daily consolidated total revenue; hence, the evidence indicates that the sales tax amounts listed on the reports were charged or collected as tax reimbursement. Accordingly, we find unpersuasive appellant's claim that these reports evidence only Blue Velvet's internal records of sales tax owed, not its collection of sales tax reimbursement.

Moreover, the written questionnaire responses from Mr. Hartstein and Ms. Winner indicate that sales tax was charged on Blue Velvet’s sales, and that Blue Velvet collected sales tax reimbursement. Likewise, the June 17, 2013 ACMS note documents Mr. Hartstein’s statement that Blue Velvet charged and collected sales tax reimbursement. In addition, the audit comments entered into CDTFA’s computer system that “[s]ales tax reimbursements were added to the sales of food and included in the selling price of bar drinks” likewise corroborate that Blue Velvet collected sales tax reimbursement. All of this evidence supports a conclusion that Blue Velvet collected sales tax reimbursement during the liability period.

Appellant contends that CDTFA failed to establish that Blue Velvet included tax reimbursement as part of the sales price pursuant to California Code of Regulations, title 18, (Regulation) section 1700(a)(2). Even assuming for argument’s sake that appellant is correct, this does not preclude a finding that Blue Velvet nevertheless *added* sales tax reimbursement to the sales price of the TPP it sold. Moreover, Regulation section 1700 is not the sole method by which CDTFA may establish the business’s collection of sales tax reimbursement.⁵ Instead, as we have determined above, there is ample evidence showing that Blue Velvet collected sales tax reimbursement.

Appellant also states that CDTFA’s Compliance Policy and Procedures Manual (CPPM) section 764.130 lists types of documentation that CDTFA may use to establish this element, and argues that CDTFA’s failure to provide evidence of some of the key examples listed,⁶ such as receipts showing sales tax reimbursement added to the selling price, demonstrates that CDTFA has not met its burden of proving this element. CPPM section 764.130 contains CDTFA’s own internal procedures for its determination of whether this element has been met, and provides that “sources include, but are not limited to” various types of documentation, including: ACMS notes for statements made by employees or potential responsible persons that sales tax reimbursement was collected; audit comments about whether the entity collected sales tax reimbursement; CDTFA Responsible Person Questionnaires; and CDTFA Business Operations Questionnaires. In the present case, all of the foregoing are in evidence, and we have determined the weight of

⁵ CDTFA did not rely on or reference Regulation section 1700 in its audit of Blue Velvet. Appellant points to CDTFA’s single use of the word “presumed” in comments in the audit working papers. However, it is obvious that the audit comment used the word in an unrelated context.

⁶ CPPM section 764.130 lists some items in bold to indicate that those sources are generally entitled to greater weight.

this evidence establishes that Blue Velvet collected sales tax reimbursement. Moreover, while the types of documentation listed in CPPM 764.130 are examples of relevant evidence to establish collection of sales tax reimbursement, the list is not exclusive, nor is any single type of documentation essential to establish this element. Thus, we find appellant's position unpersuasive. In light of all of the above, we conclude that this requirement for holding appellant liable pursuant to R&TC section 6829 has been met.

Responsible Person

A responsible person includes any person having control or supervision of, or who is charged with the responsibility for the filing of returns, or the payment of tax, or who has a duty to act for the LLC in complying with the Sales and Use Tax Law. (Cal. Code Regs., tit. 18, § 1702.5(b)(1).) Except as otherwise provided by the California Corporations Code, any matter relating to the activity of an LLC is decided exclusively by the LLC manager(s). (Cal. Corp. Code, § 17704.07(c)(1).) As relevant here, personal liability may only be imposed if appellant was a responsible person at the time the LLC made the sales, collected the sales tax reimbursement, and failed to remit it to CDTFA. (R&TC, § 6829(c); Cal. Code Regs., tit. 18, § 1702.5(a).)

Appellant acknowledges that he was the only member of Blue Velvet, but contends that he was not a responsible person because his business partner, Mr. Hartstein, was the responsible person, and appellant delegated all tax compliance matters to Mr. Hartstein and others.

Here, there is extensive evidence supporting appellant's control and supervision of Blue Velvet's business and his role as a person with the duty to act for Blue Velvet in complying with the Sales and Use Tax Law throughout the liability period. Blue Velvet's operating agreement designated appellant as its Tax Matters Member, authorizing him to represent it in all examinations of its affairs by taxing authorities. Appellant signed additional business documents, regulatory filings, and court filings alternatively as Blue Velvet's member, owner and managing member. Given his role as the sole managing member of Blue Velvet, appellant's responsibilities included ensuring Blue Velvet's compliance with provisions of the Sales and Use Tax Law, even if he delegated to other people the duty of filing returns and paying taxes. While appellant points to Mr. Hartstein (whose employment at Blue Velvet ended in February 2008) as a responsible person, this does not refute any of the above evidence showing that appellant had a duty to ensure Blue Velvet's tax compliance.

Accordingly, we find that the evidence establishes that appellant was a person responsible for Blue Velvet's sales and use tax matters during the liability period.

Willful Failure to Pay

The final requirement for a person to be held personally liable pursuant to R&TC section 6829 is that the person must have willfully failed to pay the liabilities at issue. For these purposes, "willfully fails to pay or to cause to be paid" means that the failure was the result of an intentional, conscious, and voluntary course of action. (R&TC, § 6829(d); Cal. Code Regs., tit. 18, § 1702.5(b)(2).) A failure to pay or to cause to be paid may be willful even though such failure was not done with a bad purpose or motive. (Cal. Code Regs., tit. 18, § 1702.5(b)(2).) In order to show willfulness, CDTFA must establish: (1) on or after the date the taxes came due, appellant had actual knowledge that taxes were due, but not being paid; (2) appellant had the authority to pay the taxes or to cause them to be paid; and (3) appellant had the ability to pay the taxes but chose not to. (Cal. Code Regs., tit. 18, § 1702.5(b)(2).)

Regarding willfulness, appellant concedes that he had the ability to pay Blue Velvet's tax liabilities. Thus, the remaining components of willfulness in dispute are: whether appellant had actual knowledge that the taxes were due but not being paid and whether appellant had the authority to pay the taxes or cause them to be paid.

First, we analyze whether appellant had actual knowledge that the taxes at issue were due but not being paid. Appellant argues that he was not involved in Blue Velvet's tax matters and had no knowledge that it was underreporting its sales tax liabilities. Appellant alleges that he learned of the underreporting only when he received CDTFA's audit report. At the hearing, appellant argued that while it was "grossly obvious that underreporting was occurring," he was unaware of the underreporting because he was relying solely on the information he received from Mr. Hartstein and Ms. Winner, who never informed appellant of any underreporting. Appellant states that the earliest date he could have had actual knowledge was December 31, 2009, as evidenced by CDTFA's entries on the Assignment Activity History (Form 414-Z) from the audit, which documents that on December 31, 2009, CDTFA informed appellant of Blue Velvet's underreporting. We disagree.

The evidence demonstrates that during the liability period, appellant had actual knowledge of Blue Velvet's underreporting. Appellant received frequent emails from Mr. Hartstein and Ms. Winner about Blue Velvet's financial situation, including daily sales reports

that listed “Sales Tax Month to date.” In particular, the October 8, 2007 email from Mr. Hartstein specifically informed appellant that Blue Velvet was using sales tax revenue to pay for business operations. Appellant also met or spoke with Mr. Hartstein on numerous occasions regarding the business’s sales numbers, budget, and operations, and appellant had access to the business’s books and records. Additionally, there is no question that appellant knew of the underreporting by December 31, 2009, when CDTFA directly informed appellant of Blue Velvet’s underreporting. In light of all of the above, the weight of evidence clearly establishes that on or after when the taxes became due, appellant had actual knowledge that taxes were due, but not being paid.

Next, we examine whether appellant had authority to pay the taxes or to cause them to be paid (i) on the date that the taxes came due, and (ii) when he had actual knowledge. (Cal. Code Regs., tit. 18, § 1702.5(b)(2)(B).) While a person who is “required to obtain approval” from another person would not have the requisite control, a person who had authority to direct payment, but merely deferred to the decision of another individual would have the requisite authority. (See Cal. Code Regs., tit. 18, § 1702.5(b)(2)(B).) Here, there is unequivocal evidence that, as sole owner and tax matters member, appellant had authority to authorize payments on behalf of Blue Velvet. Appellant signed checks on behalf of Blue Velvet, including a check to CDTFA dated April 27, 2009, for \$946. There is no evidence that appellant’s authority was limited at any point. Consequently, we conclude that appellant had the authority to pay the taxes at issue or to cause them to be paid; hence, this requirement for willfulness has been met.

In summary, we find that appellant knew the taxes were due and unpaid, had the authority to pay the liabilities, and had the ability to make the payments because there were funds available, but instead chose to pay other creditors. Accordingly, we find that CDTFA has established by a preponderance of evidence that appellant willfully failed to pay the taxes or cause them to be paid. Therefore, we conclude that appellant is personally responsible for the unpaid tax liabilities incurred by Blue Velvet during the liability period.

Issue 2. Whether there is reasonable cause to relieve the finality penalty imposed on Blue Velvet that was included in appellant’s liability under R&TC section 6829.

Included in appellant’s liability was a finality penalty imposed on Blue Velvet under R&TC section 6565 for failure to pay the January 31, 2011 NOD when it became due and payable. There is no statutory or regulatory authority for relieving penalties in R&TC

section 6829 determinations, but R&TC section 6592 allows for relief if a person's failure to timely pay a final determination was due to reasonable cause and circumstances beyond the person's control, and occurred notwithstanding the exercise of ordinary care and in the absence of willful neglect. (R&TC, § 6592(a).) The person subject to the penalties is the LLC. Thus, if appellant established reasonable cause why Blue Velvet failed to timely pay the determination once it became due and payable, then the finality penalty against the LLC may be relieved and, consequently, appellant's (derivative) liability for the penalty would also be eliminated. (See, e.g., Sales and Use Tax Annotation 320.0205 (3/29/04) (2005–2).)⁷

Appellant submitted a signed statement under penalty of perjury stating that reasonable cause for relief of this penalty exists because, due to the financial stress of the Great Recession, Blue Velvet did not have funds available to pay this NOD, and appellant was not personally aware of the unpaid tax liabilities until the conclusion of the audit and subsequent closure of the restaurants.

Blue Velvet filed for Chapter 11 bankruptcy on April 15, 2010, and the case was converted to a Chapter 7 bankruptcy on November 12, 2010. Given that Blue Velvet was in the process of liquidation under Chapter 7 bankruptcy prior to the time that the January 31, 2011 NOD was issued and then became final, Blue Velvet would not have been able to pay the determination at the time it became due and payable. Thus, Blue Velvet's failure to timely pay was due to reasonable cause and circumstances beyond its control and occurred notwithstanding the exercise of ordinary care and in the absence of willful neglect. For these reasons, relief of this finality penalty is warranted, subject to the condition that appellant pay the tax portion of the liability within 30 days from the issuance of CDTFA's Notice of Redetermination in this matter. (BOE Memorandum Opinion in *Davinder Singh Pabla, et al.* (2005 WL 2377713).)

Issue 3. Whether adjustments are warranted to Blue Velvet's sales and use tax liabilities for 4Q09.

California imposes a sales tax on a retailer's retail sales in this state of TPP, measured by the retailer's gross receipts, unless the sale is specifically exempt or excluded from taxation by statute. (R&TC, § 6051.) All of a retailer's gross receipts are presumed subject to tax, unless the

⁷ An annotation is a legal ruling of counsel that does not have the force or effect of law; however, a legal interpretation in an annotation is entitled to some consideration by OTA. (*Yamaha Corp. of America v. State Bd. of Equalization* (1998) 19 Cal.4th 1, 15.)

retailer can prove otherwise. (R&TC, § 6091.) Although gross receipts from the sale of “food products” are generally exempt from sales tax, sales of hot food and sales of food served in a restaurant are subject to tax. (R&TC, § 6359(a), (d)(1), (d)(2), and (d)(7).) It is the taxpayer’s responsibility to maintain and make available for examination on request all records necessary to determine the correct tax liability, including bills, receipts, invoices, or other documents of original entry supporting the entries in the books of account. (R&TC, §§ 7053, 7054; Cal. Code Regs., tit. 18, § 1698(b)(1).) When CDTFA is not satisfied with the amount of tax reported by the taxpayer, CDTFA may determine the amount required to be paid on the basis of any information which is in its possession or may come into its possession. (R&TC, § 6481.)

In the case of an appeal, CDTFA has a minimal, initial burden of showing that its determination was reasonable and rational. (See *Schuman Aviation Co. Ltd. v. U.S.* (D. Hawaii 2011) 816 F.Supp.2d 941, 950; *Todd v. McColgan* (1949) 89 Cal.App.2d 509, 514; *Appeal of Myers* (2001- SBE-001) 2001 WL 37126924.) Once CDTFA has met its initial burden, the burden of proof shifts to the taxpayer to establish that a result differing from CDTFA’s determination is warranted. (*Riley B’s, Inc. v. State Bd. of Equalization* (1976) 61 Cal.App.3d 610, 616.) Unsupported assertions are not sufficient to satisfy a taxpayer’s burden of proof. (See *ibid.*; see also *Appeal of Magidow* (82-SBE-274) 1982 WL 11930.)

Here, the books and records Blue Velvet provided for the audit period were incomplete. CDTFA compared gross receipts reported on Blue Velvet’s federal income tax returns to taxable sales reported on Blue Velvet’s sales and use tax returns for tax years 2006 and 2007 and found differences of \$18,516 and \$913,158, respectively. Additionally, CDTFA compared Blue Velvet’s total sales reported on its federal income tax returns with total sales recorded on its profit and loss statement for tax year 2007 and found a difference of \$85,151.39. Based on this information, CDTFA determined that Blue Velvet’s records and returns were unreliable and therefore used a bank deposit analysis to determine Blue Velvet’s taxable sales. A bank deposit analysis is a recognized method for determining gross receipts. (CDTFA Audit Manual, § 0405.25.) The large discrepancies provided sufficient reason to question the reliability of Blue Velvet’s reported taxable sales, and CDTFA was justified in computing Blue Velvet’s taxable sales using an alternate method. (R&TC, § 6481.)

Because CDTFA could not obtain Blue Velvet’s bank statements for 2009 or 2010, it estimated unreported taxable sales for those years using bank statements for 2007 and 2008. For

2009 and 2010, CDTFA divided Blue Velvet's unreported taxable sales for 2008 of \$1,902,633 by four to calculate average unreported taxable sales of \$475,658 for 2008 and applied this average to each quarter of 2009 and 2010 to find unreported taxable sales of \$2,378,291. Subsequently, Blue Velvet provided CDTFA bank statements for the first three quarters of 2009 showing the following total deposits: \$438,203 for 1Q09; \$241,855 for 2Q09; and \$191,114 for 3Q09. Based on these submissions, CDTFA reduced its determinations of unreported taxable sales for 1Q09 through 1Q10 by \$1,044,422, from \$2,378,290 to \$1,333,868. To determine Blue Velvet's unreported taxable sales for 4Q09 and 1Q10, CDTFA calculated the average of bank deposits for the period 1Q09 through 3Q09 of \$290,391 (i.e., $(438,203 + 241,855 + 191,114) \div 3$.) CDTFA reduced the \$290,391 average by the tax rate of 8.25 percent to determine ex-tax bank deposits of \$266,774 for 4Q09 and 1Q10. CDTFA compared the reported taxable sales for 4Q09 of \$127,722 and 1Q10 of \$183,251 with \$266,774 and determined that Blue Velvet underreported its taxable sales by \$139,052 in 4Q09.

In light of the above, the evidence establishes that CDTFA has met its initial burden of showing that its determination of Blue Velvet's unreported taxable sales using a bank deposit analysis was reasonable and rational. (See *Schuman Aviation Co. Ltd. v. U.S.*, *supra*, 816 F.Supp.2d 941, 950; *Todd v. McColgan*, *supra*, 89 Cal.App.2d 509, 514; *Appeal of Myers*, *supra*.) Because CDTFA has met its initial burden, appellant must establish that a result differing from CDTFA's determination is warranted. (*Riley B's, Inc. v. State Bd. of Equalization*, *supra*.)

Appellant disputes CDTFA's determination of the amount of the taxable measure for 4Q09.⁸ Appellant contends that to calculate Blue Velvet's unreported taxable sales for 4Q09, CDTFA should project Blue Velvet's taxable sales based on average bank deposits from 2Q09 through 3Q09 only, and it should disregard 1Q09. Appellant argues that after making a reduction by the tax rate of 8.25 percent, CDTFA should compare an ex-tax bank deposit of \$197,761 to Blue Velvet's reported taxable sales of \$127,722 for 4Q09, to find unreported taxable sales of \$70,039 instead of \$139,052.

Appellant contends that excluding 1Q09 from the calculation more accurately reflects the understatement because Blue Velvet's sales were falling dramatically due to the "Great

⁸ Previously appellant also disputed CDTFA's calculation of the taxable measure for both 4Q09 and 1Q10. However, as we confirmed at the hearing, appellant's dispute regarding 1Q10 is no longer at issue because, as stated above, 1Q10 is no longer included in appellant's liability period.

Recession,” and in all likelihood, sales would have continued to decline after 3Q09. Appellant provides no evidence to support his contention that Blue Velvet’s sales declined after 3Q09, such as Blue Velvet’s books and records or its bank statements for 4Q09 and 1Q10. Unsupported assertions are not sufficient to satisfy a taxpayer’s burden of proof. (*Appeal of Magidow, supra.*) Furthermore, Blue Velvet’s own reporting indicates that sales increased for this period. For 1Q09, 2Q09, and 3Q09, Blue Velvet reported taxable measures of \$11,456, \$10,789, and \$7,923, respectively. However, for 4Q09 and 1Q10, Blue Velvet reported taxable measures of \$127,722 and \$183,251, respectively. Therefore, the evidence shows that appellant has not met his burden to establish that a result differing from CDTFA’s determination is warranted. Consequently, adjustments to Blue Velvet’s sales and use tax liabilities for 4Q09 are not warranted.

Issue 4. Whether CDTFA properly applied certain payments to Blue Velvet’s liability.

During the pre-hearing conference in this matter, appellant indicated that he disputed CDTFA’s application of both a \$23,000 payment from the sale of Blue Velvet’s liquor license and a \$34,713.82 payment from the bankruptcy trustee. In an email submission on January 30, 2020, appellant noted that a September 20, 2017 Statement of Account for Blue Velvet shows that the \$23,000 payment for the sale of the liquor license was applied entirely to tax, and stated the following: “If that is in fact the case, we do not protest the application of this payment.” The evidence confirms that CDTFA applied the \$23,000 payment entirely to Blue Velvet’s tax liability; thus, application of this payment is not in dispute, and only application of the \$34,713.82 payment from the bankruptcy trustee is in dispute.

Appellant asserts that the payment from the bankruptcy trustee should have been applied to Blue Velvet’s liability pursuant to the provisions of CDTFA’s Compliance Policy and Procedures Manual (CPPM) section 707.020. Appellant claims that the payment should have been applied entirely to reduce Blue Velvet’s tax liability, but instead was also applied to reduce the interest and penalties, and hence this misapplication of the payment has increased appellant’s derivative liability by causing additional interest to accrue.

The CPPM section relied upon by appellant does not specify how payments made during bankruptcy are to be applied and is therefore not applicable here. Instead, the applicable section is CPPM section 740.220(1), which states that payments made by an estate, trustee, or debtor for payment of a bankruptcy claim through the bankruptcy court must be applied to the periods specified in CDTFA’s proof of claim. On December 19, 2012, CDTFA filed in Blue Velvet’s

bankruptcy case an Administrative Expense Claim for Taxes, which claimed taxes, interest, and penalties totaling \$34,713.82 for the period April 15, 2010, through September 15, 2010. On November 24, 2015, Blue Velvet's bankruptcy trustee made that \$34,713.82 payment to CDTFA. Thus, pursuant to CPPM 740.220(1), CDTFA should have applied that payment to Blue Velvet's liability for the period April 15, 2010, through September 15, 2010. A Statement of Account dated September 20, 2017, shows that CDTFA applied the \$34,713.82 payment to Blue Velvet's liability for the period April 15, 2010, through September 15, 2010. Thus, because CDTFA's application of the \$34,713.82 payment complied with the applicable provisions of the CPPM, CDTFA properly applied the payment to Blue Velvet's liability.

HOLDINGS

1. Appellant is liable under R&TC section 6829 for Blue Velvet's unpaid sales and use tax liabilities for the period April 1, 2007, through December 31, 2009.
2. The finality penalty imposed on Blue Velvet for failure to timely pay the January 31, 2011 NOD shall be relieved, subject to the condition that appellant pays the tax portion of the liability within 30 days from the issuance of CDTFA's Notice of Redetermination in this matter.
3. Adjustments to Blue Velvet's sales and use tax liabilities for 4Q09 are not warranted.
4. CDTFA properly applied certain payments to Blue Velvet's liability.

DISPOSITION

The finality penalty shall be relieved, subject to the condition that appellant pays the tax portion of the liability within 30 days from the issuance of CDTFA's Notice of Redetermination in this matter. Otherwise, CDTFA's actions in reducing the amount of appellant's liability and deleting appellant's liability for any period after December 31, 2009, but otherwise denying the remainder of the petition, are sustained.

DocuSigned by:

Suzanne B. Brown

47F45ABE89E34D0...

 Suzanne B. Brown
 Administrative Law Judge

We concur:

DocuSigned by:

Nguyen Dang

4D465973FB44469...

 Nguyen Dang
 Administrative Law Judge

DocuSigned by:

Kenneth Gast

FD75A3136CB34C2...

 Kenneth Gast
 Administrative Law Judge
Date Issued: 5/22/2020