

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:)	OTA Case No.: 21047674
)	CDTFA Case ID: 505-742
H. DAOUDI)	
dba American Quality Used Car and Trucks)	
)	

OPINION

Representing the Parties:

For Appellant:	H. Daoudi, Appellant
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For Respondent:	Jason Parker, Chief of Headquarters Operations
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For Office of Tax Appeals:	Richard Zellmer, Business Taxes Specialist III
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A. KWEE, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 6561, H. Daoudi dba American Quality Used Cars and Trucks (appellant) appeals a July 24, 2020 decision issued by respondent California Department of Tax and Fee Administration (CDTFA).¹ The decision partially denies appellant’s petition for redetermination of the Notice of Determination (NOD) dated July 20, 2018. The NOD is for tax of \$53,865, applicable interest, and a negligence penalty of \$5,386.53, for the period April 21, 2015, through December 31, 2017 (audit period).

In its decision, CDTFA reduced the deficiency measure to \$550,630 and otherwise denied the appeal. CDTFA’s adjustment reduces the tax amount at issue to \$47,246 and the penalty to \$4,724.55.

¹ Sales taxes were formerly administered by the State Board of Equalization (board). In 2017, functions of the board relevant to this case were transferred to CDTFA. (Gov. Code, § 15570.22.) For ease of reference, when this Opinion refers to acts or events that occurred before July 1, 2017, “CDTFA” shall refer to the board.

ISSUE

Whether appellant established a basis for any further adjustments to the audit liability.

FACTUAL FINDINGS

1. Appellant operated a used car dealership in Santa Rosa, California, during the audit period. Appellant obtained a seller's permit with an effective start date of April 1, 2015, and began operating this business on April 21, 2015.
2. During the audit, the field auditor observed that most vehicles offered for sale were priced below \$6,000, and appellant indicated to CDTFA that the business plan involves "a sub \$5,000 lot."
3. For the audit period, appellant reported to CDTFA total sales of \$1,355,297, claimed deductions of \$101,774 for sales tax included in total sales, \$6,800 for nontaxable sales for resale, \$10,910 for exempt sales in interstate commerce, and \$48,202 for unspecified "other" deductions, resulting in reported taxable sales of \$1,187,611.
4. Upon audit, appellant provided the following books and records: federal income tax returns (FITRs) for 2015 and 2016, quarterly sales summaries, bank statements, and dealer jackets.² CDTFA also obtained vehicle purchase records from appellant's suppliers (auction house data).³
5. The field audit disclosed no material differences between gross receipts reported on appellant's FITRs for 2015 and 2016, and total sales reported on the sales and use tax returns for those same years. However, for the audit period, appellant's reported total sales exceeded recorded total sales by \$70,745, and reported total sales also exceeded bank deposits by \$325,511. In addition, appellant's recorded taxable sales exceeded dealer jacket taxable sales data for the fourth quarter of 2017 (4Q17) by \$15,314.⁴

² Dealer jackets are envelopes utilized by used car dealers to record sales. Dealer jackets usually contain the purchase and sales documents, purchase invoices (e.g., for repair parts or upgrades), an odometer statement, the vehicle identification number, the vehicle stock number, and other records pertaining to the sale.

³ During the audit period, appellant purchased vehicles from the following auction houses: Wind River North Bay Action, ADESA Sacramento, ADESA Golden Gate, and Manheim.

⁴ CDTFA did not compile taxable sales based on dealer jacket data for the remainder of the audit period because it concluded that the 4Q17 dealer jacket data was incomplete.

6. CDTFA performed an audit and computed unreported taxable sales of \$630,437, based on using the markup method.
7. Due to an expiring limitations period, CDTFA issued the NOD to appellant on July 19, 2018, which was prior to CDTFA completing the field audit and holding a conference to discuss the audit findings with appellant (exit conference). Appellant timely petitioned the NOD.
8. CDTFA held the exit conference on October 26, 2018, and appellant disagreed with the audit approach set forth in the field audit. Following the exit conference, CDTFA decided to use California Department of Motor Vehicle (DMV) data to calculate appellant's vehicles sales and prepared a "revised audit" to recompute the determined liability.
9. CDTFA obtained DMV information regarding sales that appellant reported to DMV on REG 51, Report of Sale – Used Vehicle, forms (DMV ROS data).⁵
10. Using the DMV ROS data, CDTFA computed audited taxable sales of \$1,682,599 for the audit period. Sales amounts in the DMV ROS data did not include taxable documentation and smog fees. Therefore, CDTFA used data from appellant's dealer jackets for 4Q17 to calculate that those fees represented 5.57 percent⁶ of the selling prices of the vehicles sold in that quarterly period. CDTFA multiplied the taxable sales of \$1,682,599 found in the DMV sales data by 1.0557 (5.57 percent+ 1) to compute audited taxable sales of \$1,776,292. From this amount, CDTFA subtracted reported taxable sales of \$1,187,611 to compute unreported taxable sales of \$588,681. This reduced the tax to \$50,515, and the negligence penalty to \$5,051.44.

⁵ CDTFA did not obtain original copies of DMV ROS forms submitted to DMV; instead, CDTFA obtained an electronic summary of all the pertinent data for the vehicle sales appellant reported to DMV, which contained pertinent information from the DMV ROS forms. The DMV ROS data included the Vehicle Identification Number (VIN), license plate number, year and make of vehicle, vehicle registration date, and a two-letter Vehicle License Fee (VLF) code designating a range of sales prices in \$200 increments. CDTFA considered the registration date to have occurred shortly after the actual date of sale, and thus CDTFA used the vehicle registration date to group the vehicles into quarterly periods in which the vehicles were sold. CDTFA used the VLF code to assign the lowest estimated sales price in the \$200 range designated by a particular code. For example, VLF code "AA" designates that the sales price of the vehicle was between \$13,000 and \$13,200, and BTFD would assign a sales price of \$13,000 for sales involving VLF "AA."

⁶ We rounded this percent to the nearest hundredth (5.57); however, the actual percent used by CDTFA in its calculation was $\$7,360 / \$132,176$ (not rounded).

11. CDTFA completed the revised audit on November 8, 2018. CDTFA issued an updated billing statement on December 20, 2018. Thereafter, CDTFA scheduled an appeals conference with appellant to be held on January 29, 2020. Appellant failed to appear at the appeals conference and otherwise failed to provide any argument or documentation to support his appeal during the appeals process with CDTFA's Appeals Bureau.
12. Upon reviewing the appeal, CDTFA discovered two errors in the revised audit calculations. First, there were 19 vehicles that were sold twice during the audit period. CDTFA concluded that these 19 vehicles had been returned by the customers to appellant for full refunds (unwinds),⁷ and then appellant resold the vehicles to other customers. CDTFA decided to remove the first sale of each of these 19 vehicles totaling \$31,450. Second, the auditor used the wrong denominator in calculating the 5.57 percent ratio for documentation and smog fees. CDTFA found that calculating the ratio using the correct denominator results in a ratio of 5.27 percent for documentation and smog fees ($\$7,360$ of documentation and smog fees for 4Q17 \div taxable sales of $\$139,536$ for 4Q17).
13. CDTFA's decision ordered a reaudit to correct these two errors, but otherwise denied the petition. The reaudit further reduced the unreported taxable sales from $\$588,681$ to $\$550,630$, which further reduced the tax to $\$47,246$, and the negligence penalty to $\$4,724.55$. CDTFA issued an updated billing statement on February 17, 2021.
14. Appellant timely appealed the decision to the Office of Tax Appeals (OTA). The entirety of appellant's appeal to OTA consists of two sentences and a one-page document. The document is a letter from CDTFA informing appellant of his appeal rights to OTA. The two sentences explain, respectively, his two reasons for the appeal: (1) CDTFA did not review all the documents; and (2) CDTFA estimated the liability because the auditor ran out of time to complete the audit. Appellant raises no other argument, and provided no supporting documents, for his positions on appeal to OTA.⁸

⁷ An "unwind" (or "roll back") is a term used to describe a cancelled sale of a vehicle, or a transaction for which the purchaser either does not take possession of the vehicle or returns the vehicle shortly after purchase and receives a refund of all amounts paid. (See CDTFA Audit Manual, § 0640.05.).

⁸ We do not address the negligence penalty because it was not specifically disputed on appeal. According to CDTFA's decision, although it listed all items as disputed, it noted that appellant raised no arguments and presented no evidence to CDTFA's Appeals Bureau in connection with that penalty.

DISCUSSION

California imposes sales tax on a retailer's retail sales of tangible personal property sold in this state, measured by the retailer's gross receipts, unless the sale is specifically exempt or excluded from taxation by statute. (R&TC, §§ 6012, 6051.) For the purpose of the proper administration of the Sales and Use Tax Law and to prevent the evasion of the sales tax, the law presumes that all gross receipts are subject to tax until the contrary is established. (R&TC, § 6091.) It is the retailer's responsibility to maintain complete and accurate records to support reported amounts and to make them available for examination. (R&TC, §§ 7053, 7054; Cal. Code Regs., tit. 18, § 1698(b)1.)

If 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. (*Appeal of Talavera*, 2020-OTA-022P.) 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. (*Ibid.*) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (*Ibid.*)

Here, we find that the DMV ROS data is evidence of appellant's taxable sales because that data is based on sales that appellant reported to DMV on ROS forms. It is standard audit practice for auditors of used car dealerships to obtain DMV ROS data. CDTFA's Compliance Policy and Procedures Manual (CPPM) and Audit Manual set forth CDTFA's policy and procedure, respectively, for a field auditor to obtain this information from DMV and use it in an audit.⁹ (CPPM, § 645.120; CDTFA Audit Manual, § 0607.35.) Thus, we find that using the DMV ROS data to compute appellant's taxable sales is a standard and generally accepted auditing procedure. (See *Riley B's, Inc. v. State Bd. of Equalization* (1976) 61 Cal.App.3d 610, 612-613.) CDTFA also made reasonable efforts to ensure the accuracy of its determination by including taxable fees based on a ratio from 4Q17, and by removing customer returns from the audited measure of tax. Thus, we find that CDTFA has met its initial burden to show that its

⁹ While CDTFA's audit and procedure manuals provide relevant information to the public and we may look to them for guidance, they are not law and do not have the force or effect of law. (*Appeal of Michelle Laboratories*, 2020-OTA-290P.)

determination was reasonable and rational. Therefore, the burden of proof shifts to appellant to show errors in the audit. Appellant did not provide any documentation to carry his burden; however, he raised two contentions, which we will address, in turn.

Appellant first contends that CDTFA failed to review all his documentation. There is no legal requirement that CDTFA complete audits based on performing an actual basis review of a retailer's records. To the contrary, CDTFA "has a duty and an obligation to utilize its audit resources in the most effective and efficient manner possible." (Cal. Code. Regs., tit. 18, § 1698.5(b).) The purpose of an audit is to efficiently determine whether or not the amount of tax has been reported correctly. (Cal. Code. Regs., tit. 18, § 1698.5(b)(1).) It would be unreasonably burdensome and inefficient to require all audits be conducted on an actual basis. Furthermore, in the instant case, CDTFA's examination of appellant's dealer jackets for 4Q17 established that those records were incomplete because they did not include all of appellant's reported sales. As such, it would have served no reasonable audit purpose for CDTFA to review the remaining source documents for the remaining quarters. And, as previously stated, appellant has not provided documentation or other evidence to demonstrate error in CDTFA's audit. Therefore, we find that an actual basis examination of appellant's record would not result in a more accurate computation of appellant's unreported taxable sales.

Appellant's remaining contention is that CDTFA estimated the liability because it ran out of time to complete the audit. An exit conference is a meeting CDTFA staff holds with taxpayers to explain the audit findings and schedules. (Cal. Code. Regs., tit. 18, § 1698.5(a)(6), (c)(11).) Taxpayers and their representatives "shall be invited" to an exit conference prior to completion of an audit, shall be provided a copy of the audit working papers, and are generally given an opportunity after the exit conference to provide additional information to adjust the audit findings. (*Ibid.*) An exit conference was not held prior to issuance of the NOD on July 9, 2018. The statute of limitations for CDTFA to issue the NOD was set to expire on July 30, 2018, for the earliest expiring period.¹⁰ (R&TC, § 6487.) Here, it appears that appellant's assertion that CDTFA estimated the liability because it ran out of time to complete the audit is partially correct. CDTFA did compute the audit liability based on a markup method, and CDTFA did issue the NOD for said liability prior to completing the audit due to an expiring

¹⁰ Typically, we would expect to see a field billing order or waiver of limitations when there is concern about an expiring limitations period.

limitations period. CDTFA’s audit working papers include the field auditor’s statement that the “audit [is] estimated based on cost markup.” This statement only describes the state of the field audit; however, there was a subsequent revised audit and then a reaudit.

The record also demonstrates that appellant refused to sign a waiver of limitations which would have allowed the field auditor additional time to complete the audit. Nevertheless, after issuing the NOD, CDTFA subsequently held an exit conference to discuss the audit approach with appellant. Based on the discussion, CDTFA performed a “revised” audit.¹¹ The revised audit used DMV ROS data to compute appellant’s liability based on compiling all the vehicle sales that appellant reported to DMV during the audit period, instead of using a markup method. The revised audit approach resulted in a \$6,620 reduction to the tax, and a corresponding reduction to the 10-percent negligence penalty. Thus, we find that while CDTFA did run out of time to complete the audit prior to issuance of the NOD, those circumstances were fully addressed through the adjustments afforded in CDTFA’s revised audit and the reaudit. As such, we find no basis to order any further adjustments.

Appellant offers no other arguments or documentation to support additional adjustments. As such, we conclude that appellant failed to meet his burden of establishing that a further reduction to the measure of unreported taxable sales is warranted.

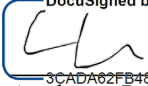
¹¹ CDTFA’s audit work papers identify the examination as a “revised audit,” which makes logical sense because CDTFA had not completed the field audit. Although we refer to the examination as a revised audit for consistency with CDTFA’s exhibits, we note that per CDTFA’s Audit Manual, the examination is properly identified as a first “reaudit” because it occurred after issuance of the NOD. (CDTFA Audit Manual, § 0702.10.)

HOLDING

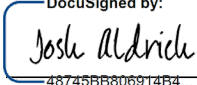
Appellant failed to establish a basis for any further adjustments to the audit liability.

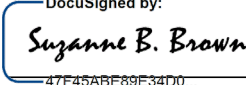
DISPOSITION

CDTFA’s action in reducing the deficiency measure to \$550,630, and otherwise denying the petition, is sustained.

DocuSigned by:

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Andrew J. Kwee
Administrative Law Judge

We concur:

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Josh Aldrich
Administrative Law Judge

DocuSigned by:

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Suzanne B. Brown
Administrative Law Judge

Date Issued: 4/13/2022