OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of:	) OTA Case No. 21078284
	) CDTFA Case ID 046-126
JOY & JOSHUA ENTERPRISES, INC., dba Superior Used Cars	)
	)
	)
	)

OPINION

Representing the Parties:

For Appellant:	Ihab 'Bob' Abdelmalek, Representative Atif Kamel, President
For Respondent:	Ravinder Sharma, Hearing Representative Christopher Brooks, Tax Counsel IV Randolph Suazo, Hearing Representative
For Office of Tax Appeals:	Craig Okihara, Business Taxes Specialist III

J. ALDRICH, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 6561, Joy & Joshua Enterprises, Inc., dba Superior Used Cars, (appellant) appeals a decision issued by respondent California Department of Tax and Fee Administration (CDTFA)[1] ordering a reaudit but otherwise denying appellant's petition for redetermination of the Notice of Determination (NOD) dated February 10, 2017. The NOD is for tax of $35,724.61, plus applicable interest, and a negligence penalty of $3,572.48, for the period April 1, 2012, through March 31, 2015 (liability period).[2]

CDTFA performed the reaudit reducing the total measure of tax to $457,828, which will result in reductions to the determined tax and penalty.[3]

[1] Sales taxes were formerly administered by the Board of Equalization (board). Effective July 1, 2017, functions of the board relevant to this case were transferred to CDTFA. (Gov. Code, § 15570.22.) When this Opinion refers to acts or events that occurred before July 1, 2017, "CDTFA" shall refer to its predecessor, the board.

[2] The NOD reflects a November 24, 2014 payment of $1,096.

[3] The tax was decreased from $35,724.61 to $34,327.00, and the negligence penalty was reduced from $3,572.48 to $3,432.68.

Office of Tax Appeals (OTA) Administrative Law Judges Ovsep Akopchikyan, Keith T. Long, and Josh Aldrich held an oral hearing for this matter in Fresno, California, on September 29, 2022. At the conclusion of the hearing, the record was held open for additional briefing pursuant to appellant's request. The record closed on November 30, 2022.

ISSUES

1. Whether CDTFA timely issued the NOD.
2. Whether any additional adjustments to the amount of unreported taxable sales are warranted.
3. Whether the negligence penalty was properly imposed.

FACTUAL FINDINGS

1. Appellant obtained its seller's permit with an effective start date of January 1, 2006. Appellant operated a used car dealership in California and began leasing vehicles in June 2014.
2. CDTFA previously audited appellant for the period January 1, 2008, through March 31, 2011 (prior audit period).
3. For the liability period, appellant reported on its sales and use tax returns (returns) total sales of $1,111,072, claiming deductions of $76,812 for sales tax reimbursement included in reported total sales, resulting in reported taxable sales of $1,034,260.
4. CDTFA obtained a waiver of the statute of limitations (waiver) and four waiver extensions (extensions) relating to the otherwise applicable three-year statute of limitations (SOL).[4] The waiver and extensions were all signed by appellant's president. The details for each are as follows:
    a. The May 20, 2015 waiver extended the SOL deadline to issue a determination to appellant for the period of the second quarter 2012 (2Q12), through 3Q12, to January 31, 2016.
    b. The January 4, 2016 extension extended the SOL deadline to issue a determination for the period of 2Q12, through 1Q13, to July 31, 2016.

[4] Form BOE-122, *Waiver of Limitations*, waives the applicable statute of limitations for a specified period, thereby extending the deadline by which CDTFA may timely issue an NOD. (See R&TC, § 6488.) This Form is used for both the original waiver and any extension thereof.

c. The July 11, 2016 extension extended the SOL deadline to issue a determination for the period of 2Q12, through 2Q13, to October 31, 2016.

d. The September 28, 2016 extension extended the SOL deadline to issue a determination for the period of 2Q12, through 3Q13, to January 31, 2017.

e. The December 7, 2016 extension extended the SOL deadline to issue a determination for the period of 2Q12, through 4Q13, to April 30, 2017.

5. For audit, appellant provided sales reports, dealer jackets, and monthly sales summary reports for the liability period.[5]

6. CDTFA obtained, from the Department of Motor Vehicles (DMV), electronic Report of Sale (ROS) data for the liability period. Using the dealer jackets appellant provided, CDTFA compiled the recorded vehicle sales prices from the sales contracts. Where a sales contract was not provided for a vehicle sale listed in the DMV ROS data, CDTFA estimated[6] the vehicle sale amount. In total, CDTFA compiled taxable vehicle sales of $1,480,998 for the liability period.

7. Appellant began to lease cars in June 2014. Using the monthly sales summary reports, CDTFA compiled sales tax reimbursement collected on rental receipts of $2,248.15 for June 1, 2014, through March 31, 2015. CDTFA divided the sales tax reimbursement on the leases by the tax rate of 7.50 percent in effect during that period and computed taxable rental receipts of $29,975.00.

8. CDTFA added taxable vehicle sales to taxable rental receipts and calculated audited taxable sales of $1,510,973 ($1,480,998 + $29,975) for the liability period. Since audited

[5] Dealer jackets are routinely used by car dealers, and each dealer jacket contains the various documents related to the sale including, but not limited to, the vehicle sales contract, vehicle purchase invoice, and the DMV Report of Sale (ROS).

[6] CDTFA reports that the sales information obtained from DMV included the Vehicle Identification Number, license plate number, year and make of the 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 so 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 within 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 respondent would assign a sales price of $13,000 for sales involving VLF "AA."

taxable sales exceeded reported taxable sales of $1,034,260, CDTFA computed unreported taxable sales $476,713 ($1,510,973 - $1,034,260) for the liability period.[7]

9. CDTFA issued an NOD to appellant on February 10, 2017, with a tax liability of $35,724.61, plus applicable interest, and a negligence penalty of $3,572.48.
10. Appellant filed a timely petition for redetermination disputing the NOD in its entirety.
11. On June 16, 2020, CDTFA issued a Decision that ordered a reaudit be performed to delete duplicate vehicle sales of $18,195 and make an allowance of $11,296 for bad debts as conceded by CDTFA, and include vehicle purchases of $10,605 subject to use tax. Appellant was also allowed 30 days to provide records to support additional adjustments for duplicate vehicle sales and bad debts. The petition was otherwise denied.
12. Since appellant did not provide additional records, CDTFA completed the reaudit based on the available records. CDTFA computed unreported taxable sales of $458,518, a credit measure for unclaimed bad debts of $11,295, unreported vehicles withdrawn from resale inventory subject to use tax of $10,605, and the unreported vehicle sales subject to district taxes of $35,895 for the liability period. Thus, the reaudit reduced the determined measure of tax by $18,885 from $476,713 to $457,828,[8] which is the amount in dispute.
13. On October 7, 2020, CDTFA sent appellant a letter detailing the potential adjustments to the NOD based on the reaudit findings.
14. On February 11, 2021, CDTFA sent appellant a letter detailing the reaudit results and summarizing appellant's disagreement with the findings.
15. On June 22, 2021, CDTFA sent appellant a letter detailing the reaudit results and provided appellant with a blank OTA Form *Request for Appeal*.
16. Appellant timely appealed to OTA.

[7] During its review of the dealer jackets, CDTFA noted that appellant made sales to customers who registered the vehicles in cities where district taxes applied. Since appellant did not report any sales subject to district taxes on its returns, CDTFA established a separate measure for unreported vehicle sales subject to district taxes of $35,895 for the liability period. Appellant does not dispute this item; thus, OTA does not discuss it further. As relevant here, cities and counties may generally impose a transaction and use tax (district tax) pursuant to the Transactions and Use Tax Law. (See Part 1.6, Division 2, of the R&TC.) CDTFA collects the district taxes on behalf of all districts which have adopted a district tax.

[8] Excludes the measure of tax of $35,895 for unreported vehicle sales subject only to district taxes which is reflected under a category on the reaudit report separate from the measure of tax subject to the statewide sales and use tax. CDTFA allowed $6,095 according to its November 23, 2022 letter. Accordingly, this amount subsequently was adjusted by the second reaudit in response to appellant's post-hearing submission ($35,895 to $29,800).

17. On November 18, 2022, CDTFA sent appellant a report of a second reaudit with adjustments to the district taxes.

DISCUSSION

Issue 1: Whether CDTFA timely issued the NOD.

Absent certain exceptions, every NOD must be mailed within three years after the last day of the calendar month following the quarterly period for which the amount is proposed to be determined or within three years after the return is filed, whichever period expires later. (R&TC, § 6487(a).) With an agreement in writing, a taxpayer may waive or extend the deadline prescribed in R&TC section 6487(a). When such a waiver has been obtained, the NOD may be mailed at any time prior to the expiration of the extended period. (R&TC, § 6488; Cal. Code Regs., tit. 18, § 1698.5(b)(3).) The waiver or extension period may be extended by subsequent agreements in writing. (R&TC, § 6488.)

There is no dispute that the three-year statute of limitations set forth in R&TC section 6487 applies here. In the absence of a waiver of the statute of limitations, the statute of limitations would have expired for 2Q12, the first quarter of the liability period, on July 31, 2015. However, CDTFA obtained a waiver and four extensions from appellant. The waiver was signed on May 20, 2015, and each of the extensions were signed before the expiration of the period for issuing an NOD established in the prior waiver and extension. The final extension extended the period for issuing an NOD until April 30, 2017, and CDTFA issued the NOD before that date, on February 10, 2017. Unless appellant proves that the waiver or any of the extensions are invalid, CDTFA timely issued the NOD before the final extension expired.

Appellant has not provided evidence or argument to support its position that the waiver or extensions are invalid. Thus, OTA finds that CDTFA timely issued the NOD.

Issue 2: Whether any additional adjustments to the amount of unreported taxable sales are warranted.

California imposes sales tax measured by a retailer's gross receipts from the retail sale of tangible personal property, unless the sale is specifically exempt or excluded from taxation by statute. (R&TC, §§ 6012, 6051.) All gross receipts are presumed to be subject to tax until the contrary is established. (R&TC, § 6091.) It is the retailer's responsibility to maintain complete

and accurate records 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, or in the case of a failure to file a return, 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, 6511.) 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, appellant's books and records provided for audit were incomplete. CDTFA compiled audited taxable sales of $1,480,998 using vehicle sales contracts from appellant's dealer jackets and DMV ROS data which exceeded reported taxable sales of $1,034,260. Since CDTFA based the determination on appellant's own records in conjunction with the DMV ROS data, OTA finds that CDTFA has met its initial burden to show that its determination was reasonable and rational. Therefore, the burden of proof shifts to appellant to show adjustments are warranted.

Appellant contends that the DMV records are not correct. Appellant also contends that there were duplicate vehicles sales included in the taxable measure. In support appellant submitted a 10-page sales report dated September 2, 2022 (September report) for the audit period. Appellant also contends that it is entitled to additional bad debt deductions. Appellant also claims that it netted bad debts out of its taxable sales consistent with generally accepted accounting practices. After the hearing, appellant submitted approximately 57 pages of additional documents: Bad Debits; Recognized Bad Debits; District Tax; Duplicated ROS; Record Comparison; Duplicated and corrected cars; and miscellaneous files identified as scans 1 through 7 (post-hearing submission).

Duplicate sales

In response to the September report, CDTFA argues that it randomly selected five quarters to analyze (i.e., 2Q12, 3Q12, 4Q12, 1Q14, and 1Q15). CDTFA argues that the September report is unreliable because it contains 65 car sales compared to the 100 car sales that were determined based on the dealer jackets and DMV data. Furthermore, CDTFA found four car sales which were not previously disclosed; and thus, not included in the audit measure. The 39 car sales missing from the September report amount to $276,000 (i.e., the 35 missing from the September report and the 4 not found in the DMV data). Accordingly, CDTFA argues that the September report is incomplete and unreliable.

Regarding appellant's post-hearing duplicate sales documents, CDTFA addresses each of the five claimed duplicates sales as follows: (1) the first duplicate sale, car stock number 310035R2, was sold two times (on May 6, 2013, for $9,605 and then on March 12, 2014 for $11,100) to two different customers; (2) the second duplicate sale, car stock number 320047, was sold twice (on November 2, 2012, for $3,105 and then on February 6, 2013 for $2,710) to different customers; (3) the third duplicate sale, car stock number 320025, was sold twice (on August 24, 2012 for $10,100 and then on September 7, 2012 for $10,100) to the same person; (4) the fourth duplicate sale, car stock number 320042, was already allowed as an adjustment; and (5) the fifth duplicate sale, car stock number 320036, was already allowed as an adjustment. Regarding the third duplicate sale, CDTFA argues that the DMV report shows that the sales were prepared with different ROS numbers so it appears that the first car may have been returned and another car was sold for the same price with the same stock number. However, CDTFA argues that appellant failed to provide any documentary evidence to show that the full sale price, including that portion designated as "sales tax," was refunded either in cash or credit, and the customer, in order to obtain the refund or credit, was not required to purchase other property at a price greater than the amount charged for the car that was returned as required by Regulation section 1655(a)(1).

After review, OTA notes that the September report appears to be a self-generated schedule, which is not accompanied by supporting source documents. Given the conflict of information between the September report and the other available records, OTA finds the September report to be unreliable. Thus, OTA finds the September report to have little evidentiary value.

Regarding appellant's post-hearing submission, the evidence demonstrates that the first two claimed duplicates each are multiple sales to two separate individuals. Regarding the third claimed duplicate sale, appellant has provided sufficient credible evidence to support an adjustment. OTA infers that the third claimed duplicate sale is a duplicate sale based on the following: the timing of the sales (i.e., the 14 day period between August 24, 2012, and September 7, 2012), the identical amount of the sale ($10,100), the fact that the purchaser was the same individual; the same car stock number (320025), and appellant's business practices. As to the fourth and fifth claimed duplicate sale, CDTFA already made adjustments to the taxable measure that account for these duplicate sales.

Based on the foregoing analysis, OTA finds that appellant has meet its burden of proof to show that an adjustment to the audited measure for a duplicate sale of $10,100 is warranted.

Bad Debt Deduction

Retailers may generally take a bad debt deduction for amounts reported as taxable and thereafter found worthless and charged off for income tax purposes. (R&TC, §§ 6055(a), 6203.5.) In support of deductions for bad debts, retailers must maintain adequate and complete records showing: (1) the date of original sale; (2) the name and address of purchaser; (3) the amount the purchaser contracted to pay; (4) the amount on which the retailer paid tax; (5) the jurisdiction(s) where the local taxes and, when applicable, district taxes were allocated; (6) all payments or other credits applied to the account of the purchaser; (7) evidence that the uncollectible portion of gross receipts on which tax was paid actually has been legally charged off as a bad debt for income tax purposes or, if the retailer is not required to file income tax returns, charged off in accordance with generally accepted accounting principles; and 8) the taxable percentage of the amount charged off as a bad debt properly allocable to the amount on which the retailer reported and paid tax. (Cal. Code Regs., tit. 18, § 1642(e).)

Here, appellant's post-hearing submission regarding bad debts does not provide supporting documents such as sales contracts, payment history (from date of the sale until repossession), date of repossession, or other information that is required to support a bad debt deduction. The requisite information is also not otherwise found in the record. Thus, appellant has not supported the claimed bad debts with evidence as required by Regulation section 1642(e). Accordingly, OTA finds appellant has failed to meet its burden of proof to show that additional adjustments are warranted for bad debts.

Other adjustment issues

With respect to appellant's post-hearing claim of one nontaxable sale for resale, CDTFA states that the car with stock number 300043R1, sold for $2,135, was not included in the audit work papers. Since the alleged nontaxable sale was not included in the audited measure, OTA finds that no adjustment is warranted.

In response to appellant's post-hearing claim of six voided and one changed car sale, OTA notes that appellant did not provide any supporting documentation (car stock numbers: 320022, 320014, 310063R1, 320047, 300027R2, and 320053r1). As such, OTA finds appellant is not entitled to adjustments for voided or changed car sales.

In response to appellant's Scan 7-2, OTA finds appellant is not entitled to adjustments for its vehicles leases because appellant did not provide documentary evidence to show that the assessed amount is incorrect. Based on OTA's review of the available evidence, appellant has not met its burden of proof to show additional adjustments are warranted.

Other matters

Appellant makes several contentions or assertions regarding the audit process. Appellant asserts that CDTFA recommended "a new audit because the first audit was prepared unfairly and wrongfully." Appellant contends that CDTFA did not contact appellant about the reaudit and the reaudit report was not provided to it. Appellant argues that the decision to perform a reaudit was based on samples and all of its records have not been reviewed. Appellant alleges that it was treated unfairly, that the auditor lied to his supervisor and to the appellant, and that the auditor submitted untruthful information.

During CDTFA's appeals process, appellant provided documentation it claimed support bad debt deductions. After examining the information, CDTFA computed allowable bad debts to which it conceded. CDTFA recommended a reaudit to make the identified adjustments but also allowed appellant 30 days to provide additional records. Other than appellant's unsupported assertions, the record is silent regarding any alleged improper conduct or misrepresentations by the auditor. The record also is silent on what attempts appellant made, if any, to contact CDTFA and provide records to support additional adjustments. However, the record does show that on October 7, 2020, CDTFA sent a letter to appellant indicating that it completed its review together with the initial reaudit results. Then, on February 11, 2021, CDTFA sent appellant and its

representative a letter with the results of the reaudit, appellant's position based on discussions with appellant's representative, and the reaudit work papers. CDTFA sent appellant a letter dated June 22, 2021, indicating that CDTFA reviewed appellant's available books and records in accordance with the Decision and made the recommended adjustments. And, finally, on November 18, 2022, CDTFA sent appellant a second reaudit with adjustments to the district taxes.

OTA notes that it does not have the authority to address actual or alleged violations of due process at the agency (CDTFA) level. (Cal. Code Regs., tit. 18, § 30104(d).) To the extent that appellant believed it was being treated unfairly, it may contact CDTFA's Taxpayers' Rights Advocate Office or pursue some other remedy, if available.

During the appeal at OTA, appellant was given ample opportunity to submit additional documents at various stages during the OTA appeal process. OTA notes that appellant submitted approximately thirteen hundred pages in support of its position. Except for the September report and the post-hearing submission, appellant's submissions were largely duplicative of documents that had already been addressed in the audit or reaudit. Accordingly, OTA finds appellant has not established grounds for adjustments or relief based on its other arguments.

Issue 3: Whether the negligence penalty was properly imposed.

R&TC section 6484 provides that, if any part of a deficiency for which a deficiency determination is made is due to negligence or intentional disregard of the law or authorized rules and regulations, a penalty of 10 percent of the amount of the determination shall be added thereto. Negligence is generally defined as a failure to exercise such care that a reasonable and prudent person would exercise under similar circumstances. (*Warner v. Santa Catalina Island Co.* (1955) 44 Cal.2d. 310, 317; *Acqua Vista Homeowners Assn. v. MWI, Inc.* (2017) 7 Cal. App. 5th 1129, 1157; see also *People v. Superior Court (Sokolich)* (2016) 248 Cal. App. 4th 434, 447.)

Typically, a penalty for negligence or intentional disregard should not be added to deficiency determinations associated with the first audit of a taxpayer in the absence of evidence establishing that any bookkeeping and reporting errors cannot be attributed to the taxpayer's good faith and reasonable belief that its bookkeeping and reporting practice were in substantial compliance with the requirements of the Sales and Use Tax Law or authorized regulations. (Cal. Code Regs., tit. 18, § 1703(c)(3)(A); see *Independent Iron Works, Inc. v. State Bd. of Equalization* (1959) 167 Cal.App.2d 318, 321-324.)

A taxpayer shall maintain and make available for examination on request by CDTFA, all records necessary to determine the correct tax liability under the Sales and Use Tax Law and all records necessary for the proper completion of the sales and use tax return. (R&TC, §§ 7053, 7054; Cal. Code Regs., tit. 18, § 1698(b).) Such records include but are not limited to the following: (1) the normal books of account ordinarily maintained by the average prudent businessperson engaged in the activity in question; (2) bills, receipts, invoices, cash register tapes, or other documents of original entry; and (3) schedules of working papers used in connection with the preparation of the tax returns. (Cal. Code Regs., tit. 18, § 1698(b)(1)(A)-(C).) Failure to maintain and keep complete and accurate records is considered evidence of negligence or intent to evade the tax. (Cal. Code Regs., tit. 18, § 1698(k).)

Appellant contends that the negligence penalty should not be imposed and that it reported its taxable sales correctly.

CDTFA argues that the negligence penalty was properly imposed because appellant's audited taxable sales substantially exceed its reported taxable sales. In support of the negligence penalty, CDTFA also compares the error percentage between the prior audit period and the audit at issue. The deficiency measure in the prior audit period represented a 12.35 percent error rate ($322,034.00/$2,606,896.00), whereas the error rate for the reaudit was approximately 44.00 percent ($457,828.00/$1,034,260.00).[9]

In the instant appeal, appellant has been previously audited. The audited measure which was derived from appellant's own records in conjunction with the DMV data show that appellant underreported a substantial amount of taxable sales. After going through an audit, a reasonably prudent person would likely have fewer reporting errors or a lower error rate. Here, in contrast, appellant's reporting error rate increased from 12.35 percent to approximately 44.00 percent. OTA also notes that the records that appellant provided are lacking in supporting or source documentation which supports a finding of negligence. In light of the foregoing, OTA finds that the negligence penalty was properly imposed in light of the audited measure, the increased error rate, and the lack of record keeping, which all support a finding that appellant was negligent.

[9] The prior audit work papers are not in the record. However, there are several references to the prior audit period in evidence and appellant has not specifically disputed the prior audit figures.

HOLDINGS

1. CDTFA timely issued the NOD.
2. Appellant has shown that an additional adjustment to the amount of unreported taxable sales is warranted for the duplicate sale in the amount of $10,100.
3. The negligence penalty was properly imposed.

DISPOSITION

Reduce the audited amount of unreported taxable sales by $10,100 as determined by OTA; and recalculate the determined liability, corresponding negligence penalty, and interest accordingly. Otherwise, CDTFA's action is sustained.

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Josh Aldrich
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Josh Aldrich
Administrative Law Judge

We concur:

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Keith T. Long
Administrative Law Judge

DocuSigned by:
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Ovsep Akopchikyan
Administrative Law Judge

Date Issued: 3/6/2023