

**OFFICE OF TAX APPEALS**  
**STATE OF CALIFORNIA**

In the Matter of the Appeal of:	)	OTA Case No. 20106786
<b>PEDROZA CARS, INC.,</b>	)	CDTFA Case ID 221-044
<b>dba Los Compadres Auto Center</b>	)	
	)	
	)	

---

**OPINION**

Representing the Parties:

For Appellant: Juan Guzman, CPA

For Respondent: Jason Parker, Chief of Headquarters Ops.

For Office of Tax Appeals: Richard Zellmer  
Business Taxes Specialist III

J. LAMBERT, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 6561, Pedroza Cars, Inc. (appellant) appeals a decision issued by respondent California Department of Tax and Fee Administration (CDTFA),<sup>1</sup> denying appellant's petition for redetermination of the Notice of Determination (NOD) for tax of \$128,302.41, plus applicable interest, and a negligence penalty of \$12,830.26, for the period October 1, 2014, through December 31, 2016 (audit period).

In its subsequent decision, CDTFA reduced the understated taxable measure from \$1,597,169 to \$1,410,458, reducing the tax and penalty, and denied the remainder of the petitioned amount.

Appellant waived the right to an oral hearing; therefore, the matter is being decided based on the written record.

---

<sup>1</sup> 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.) For ease of reference, when this Opinion refers to acts or events that occurred before July 1, 2017, "CDTFA" shall refer to the BOE; and when referring to acts or events that occurred on or after July 1, 2017, "CDTFA" shall refer to CDTFA.

ISSUE

Whether any further reduction to the measure of tax is warranted.

FACTUAL FINDINGS

1. Appellant operated a used car dealership in Bloomington, California.
2. For the audit period, CDTFA performed an audit, plus two additional reaudits.
3. During the audit period, appellant reported total sales of \$4,334,363, and claimed deductions totaling \$303,082, consisting of \$3,308 for smog certification fees, \$229,700 for gap insurance and license and registration fees, and \$70,074 for bad debts. Appellant subtracted claimed deductions of \$303,082 from reported total sales of \$4,334,363 resulted in reported taxable sales of \$4,031,281.
4. Upon audit, appellant provided federal income tax returns (FITRs) for 2014, 2015, and 2016, bank statements for the audit period, sales journals for the audit period, and dealer jackets for the audit period.<sup>2</sup>
5. CDTFA noted that Reports of Sale (ROS) were missing from 106 of the 382 dealer jackets provided. CDTFA found that gross receipts reported on the FITRs exceeded total sales reported on the sales and use tax returns by \$561,058 for 2015 and \$335,798 for 2016. Also, CDTFA noted that bank deposits exceeded reported total sales by \$1,382,630 for the audit period. Due to these omissions and discrepancies, CDTFA concluded that additional verification of appellant's sales was needed.
6. CDTFA obtained information from the Department of Motor Vehicles (DMV) regarding vehicle sales that appellant reported to DMV on ROS forms. CDTFA compared the vehicle identification numbers (VINs) for the vehicles listed in the information from the DMV to the VINs for the vehicles listed in appellant's sales journal, and found 130 vehicles that were listed in the DMV information that were not recorded in appellant's sales journal. CDTFA questioned appellant about these 130 vehicles, and appellant then provided an additional 123 dealer jackets that were not provided at the inception of the audit. Upon examination of these additional dealer jackets, CDTFA found that 122 of those vehicles were listed in the information from DMV, but one vehicle was not listed in

---

<sup>2</sup> Dealer jackets (or sales jackets) are envelopes utilized by used car dealers to record sales. Dealer jackets usually contain the purchase and sales documents, ROS forms, invoices associated with repairs, delivery, and parts, an odometer statement, and vehicle identification number, stock number, and other records pertaining to the sale.

the information from DMV or appellant's sales journal. Thus, there were 131 unreported vehicle sales (130 from the DMV information + one from the additional dealer jackets). CDTFA established selling prices for these 131 unreported vehicle sales as follows. Using the 123 dealer jackets, CDTFA compiled vehicle sales of \$1,461,902 and taxable smog fees and documentation fees of \$12,915.

7. For the remaining eight vehicle sales, CDTFA used DMV's estimated sales prices to compile taxable vehicle sales of \$73,000.<sup>3</sup> Also, CDTFA found that two of the 131 vehicles had been returned by the purchasers, and appellant had given those two purchasers full refunds. Therefore, CDTFA allowed a credit of \$20,210 for the two returned vehicles. In total, CDTFA calculated unreported sales of \$1,527,608 ( $\$1,461,902 + \$12,915 + \$73,000 - \$20,210$ ).
8. In addition, CDTFA disallowed the claimed deduction for bad debts of \$70,074. CDTFA also allowed a \$513 credit for over-reported taxable sales in the fourth quarter of 2014 (4Q14). In total, CDTFA computed a taxable measure of \$1,597,169 in the original audit ( $\$1,527,608 + \$70,074 - \$513$ ).
9. CDTFA issued an NOD to appellant on March 28, 2018, based on the aforementioned audit, for tax of \$128,302.41, plus applicable interest, and a negligence penalty of \$12,830.26.<sup>4</sup>
10. Appellant filed a timely petition for redetermination of the NOD.
11. CDTFA subsequently prepared a first reaudit in order to allow the claimed deduction for bad debts of \$70,074, and to disallow the \$513 credit for over-reported taxable sales in the fourth quarter of 2Q14. Thus, the taxable measure in the first reaudit was \$1,527,608 ( $\$1,597,169 - \$70,074 + \$513$ ).
12. CDTFA held an appeals conference with appellant on December 10, 2019. Upon re-examination of the first reaudit workpapers, CDTFA found that the selling price one of the unreported vehicle sales had erroneously been scheduled in the audit as \$129,950 instead of the correct selling price of \$12,800.

---

<sup>3</sup> CDTFA did not calculate an amount of taxable smog fees or documentation fees for these eight vehicle sales.

<sup>4</sup> Appellant has not raised any dispute regarding the negligence penalty, and thus, it will not be discussed further.

13. In its Decision issued on May 4, 2020, CDTFA ordered that the selling price of the aforementioned vehicle be corrected from \$129,950 to \$12,800, thus reducing the taxable measure computed in the first reaudit by \$117,150 (\$129,950 - \$12,800), from \$1,527,608 to \$1,410,458. CDTFA otherwise denied appellant's petition.
14. CDTFA prepared a second reaudit in which the taxable measure was reduced from \$1,527,608 to \$1,410,458 (\$1,527,608 - \$117,150).
15. Appellant filed the instant appeal with the Office of Tax Appeals (OTA).

### DISCUSSION

California imposes a sales tax on a retailer's retail sales in this state of tangible personal property, 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 retailer can prove otherwise. (R&TC, § 6091.)

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. (*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.*)

In this case, ROS were missing from 106 of the 382 dealer jackets provided. Also, gross receipts reported on the FITRs exceeded total sales reported on the sales and use tax returns by \$561,058 for 2015 and \$335,798 for 2016. Also, bank deposits exceeded reported total sales by \$1,382,630 for the audit period. Therefore, CDTFA was justified in questioning the reliability of recorded and reported sales. Appellant's sales journals and dealer jackets are evidence of appellant's sales. Obtaining information from DMV regarding vehicle sales that appellant reported to DMV on ROS forms is a standard and accepted audit procedure. (See *Riley B's, Inc. v. State Bd. of Equalization* (1976) 61 Cal.App.3d 610, 612-613.) OTA finds that it was appropriate for CDTFA to compute appellant's taxable sales using the sales journals, dealer jackets, and information from DMV. Thus, 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 errors in the audit.

Appellant does not dispute that it made the 131 specific vehicle sales that result in the taxable measure of \$1,410,458 computed in the second reaudit. Appellant contends that it is entitled to a larger allowance for bad debts. Appellant specifically asks for an additional allowance of \$185,932 for bad debts.

In general, a retailer is relieved from liability for sales tax or from liability to collect use tax insofar as the measure of the tax is represented by accounts found worthless and charged off for income tax purposes. (R&TC § 6055; Cal. Code Regs., tit. 18, § 1642(a).) A retailer may claim a bad debt deduction provided that the sales tax, or amount of use tax, was actually paid to the state. (R&TC § 6055; Cal. Code Regs., tit. 18, § 1642(a).) If the amount of an account found to be worthless and charged off is comprised in part of nontaxable receipts such as interest, insurance, repair, or installation labor and in part of taxable receipts upon which tax has been paid, a bad debt deduction may be claimed only with respect to the unpaid amount upon which tax has been paid. (Cal. Code Regs., tit. 18, § 1642(b).) In determining that amount, all payments and credits to the account may be applied ratably against the various elements comprising the amount the purchaser contracted to pay (pro rata method), may be applied as provided in the contract of sale (contract method), or may be applied by another method which reasonably determines the amount of the taxable receipts (alternative method). (Cal. Code Regs., tit. 18, § 1642(b).)

In support of deductions or claims for refund for bad debts, retailers must maintain adequate and complete records showing the date of original sale, the name and address of the purchaser, the amount the purchaser contracted to pay, the amount on which the retailer paid tax, the jurisdiction(s) where the local taxes and, when applicable, district taxes were allocated, all payments or other credits applied to account of the purchaser, 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 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).)

First, OTA notes that CDTFA has allowed the claimed bad debts of \$70,074. Appellant seeks an additional allowance of \$185,932. However, appellant has not provided the necessary documentation as required in California Code of Regulations, title 18, (Regulation) section 1642(e) to support any additional allowance for bad debts. Also, appellant did not claim a bad debt expense on its FITRs for 2014, 2015, and 2016, and thus, appellant has not charged off bad debts for income tax purposes in accordance with Regulation section 1642(a).<sup>5</sup> Accordingly, no additional allowance for bad debts is warranted.

Based on all of the above, OTA finds that appellant has failed to provide any documentation or other evidence from which a more accurate determination could be made. Thus, appellant has failed to meet its burden of establishing that a reduction to the measure of unreported taxable sales is warranted.

HOLDING

Appellant has not shown that further reductions to the measure of tax are warranted.

DISPOSITION

CDTFA’s action in reducing the taxable measure to \$1,410,458, and otherwise denying the petition, is sustained.

DocuSigned by:  
*Josh Lambert*  
CB1F7DA37831416...  
\_\_\_\_\_  
Josh Lambert  
Administrative Law Judge

We concur:  
DocuSigned by:  
*Suzanne B. Brown*  
47F45ABE89E34D0...  
\_\_\_\_\_  
Suzanne B. Brown  
Administrative Law Judge

DocuSigned by:  
*Natasha Ralston*  
25F8FE08FF56478...  
\_\_\_\_\_  
Natasha Ralston  
Administrative Law Judge

Date Issued: 10/5/2023

<sup>5</sup> CDTFA allowed the claimed bad debts of \$70,074 even though appellant did not charge off those bad debts for income tax purposes or provide any documentation to support those bad debts.