

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:)	OTA Case No.: 231114664
V. VASQUEZ,)	CDTFA Case ID: 03-104-611
dba Auto Motriz Michoacan)	
)	
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)	

OPINION

Representing the Parties:

For Appellant: V. Vasquez

For Respondent: Jason Parker, Chief of Headquarters Ops.

For Office of Tax Appeals: Crystal Spratley, Business Taxes Specialist III

S. KIM, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 6561, V. Vasquez (appellant) appeals a decision issued by respondent California Department of Tax and Fee Administration (CDTFA) denying, in part, appellant’s timely petition for redetermination of a Notice of Determination (NOD) issued on September 2, 2021. The NOD is for tax of \$196,275,¹ plus applicable interest, and a negligence penalty of \$19,627.55 for the period January 1, 2018, through December 31, 2020 (liability period).²

CDTFA subsequently conducted a reaudit, which reduced the determined tax to \$191,647 and the negligence penalty to \$19,164.71.

Appellant waived the right to an oral hearing; therefore, the matter was submitted to the Office of Tax Appeals (OTA) on the written record pursuant to California Code of Regulations, title 18, section 30209(a).

¹ The NOD reflects total tax of \$254,802 and a \$58,527 credit, which results in a net tax of \$196,275 (\$254,802 - \$58,527). It is unclear why tax was computed at a higher rate, which then required a credit to reduce the tax to the proper amount. The negligence penalty was correctly computed on the net tax amount.

² CDTFA timely issued the NOD because, on February 12, 2021, appellant signed a waiver of the otherwise applicable three-year statute of limitations for the period January 1, 2018, through June 30, 2018, which extended the deadline for issuing an NOD to October 31, 2021. (See R&TC, §§ 6487(a), 6488.)

ISSUE

Whether appellant has demonstrated that further adjustment is warranted to the audited measure of unreported taxable sales.

FACTUAL FINDINGS

1. Appellant, a sole proprietor, operated a used car dealership located in Colton, California. Appellant's seller's permit was opened with an effective date of December 1, 2009.
2. For the liability period, appellant reported total and taxable sales of \$9,084,632 with no claimed deductions.
3. CDTFA audited appellant for the liability period.³ Appellant provided sales contracts, sales journals, and bills of lading for the liability period. Appellant also provided a federal income tax return for 2019, bank statements for 2020, and auction purchase information obtained from third-party auction houses. CDTFA also obtained electronic vehicle registration data for the liability period from the California Department of Motor Vehicles (DMV).
4. During the audit, CDTFA examined appellant's sales records and computed recorded taxable sales of \$11,467,003 for the liability period.⁴ CDTFA compared appellant's recorded taxable sales to appellant's reported taxable sales for the liability period and found unreported taxable sales of \$2,391,371. CDTFA also found that appellant had collected excess tax reimbursement of \$2,373.⁵ Although appellant did not claim any bad debt deductions for the liability period, CDTFA determined that appellant's records supported a bad debt deduction and computed a bad debt allowance of \$6,917 using a pro rata method.⁶ CDTFA also imposed a negligence penalty of \$19,628.

³ CDTFA previously audited appellant for the period October 1, 2013, through September 30, 2016, which resulted in a deficiency determination for unreported taxable sales and a negligence penalty.

⁴ During preliminary audit testing, CDTFA conducted a bank deposit analysis of two of appellant's bank accounts, which showed that total deposits between the two accounts far exceeded appellant's reported taxable sales for the liability period. However, CDTFA concluded that some of the deposits may have included taxes, license fees, interest, sales for resale, and transfers related to other accounts. Moreover, because appellant provided other sales records documenting its taxable sales, CDTFA did not rely on the bank deposit analysis during the audit.

⁵ Appellant does not dispute the excess tax reimbursement collected, and OTA does not discuss it any further.

⁶ The pro rata method is a method of computing loss where only the portion of a bad debt loss attributable to the amount on which the retailer paid tax may be used to claim a bad debt deduction for sales and use tax purposes. (Cal. Code Regs., tit. 18, § 1642(f)(2).)

5. CDTFA issued appellant the September 2, 2021 NOD.
6. Appellant timely filed a petition for redetermination disputing the NOD. Appellant submitted additional information regarding unwinds, returned vehicles, and buybacks.⁷
7. CDTFA conducted a reaudit based on the additional information and reduced the measure of unreported taxable sales by \$53,930, from \$2,391,371 to \$2,337,441. CDTFA also increased the bad debt allowance by \$1,045, from \$6,917 to \$7,962. CDTFA did not make any changes to the amount of excess tax collected. CDTFA reduced the negligence penalty accordingly.
8. On March 4, 2022, CDTFA issued appellant a notice of proposed liability for \$191,647 in tax, plus accrued interest, and a negligence penalty of \$19,164.71.⁸
9. On October 9, 2023, CDTFA issued a decision reducing the determined measure of tax in accordance with the reaudit but otherwise denying appellant's petition for redetermination.
10. Appellant timely filed this appeal.

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).) The retailer also bears the burden of establishing its entitlement to any claimed deduction or exemption. (*Paine v. State Bd. of Equalization* (1982) 137 Cal.App.3d 438, 443.)

A retailer is relieved from liability for sales tax that became due and payable, insofar as the measure of tax is represented by accounts that have become worthless and charged off for income tax purposes by the retailer or, if the retailer is not required to file income tax returns,

⁷ An unwind (also called a "roll back" or "buyback") is the same as a canceled sale; It occurs when a vehicle is purchased and operated on a Report of Sale and then returned to the dealer (because credit was unavailable, the customer changed his or her mind, etc.) prior to completion of the transaction and issuance of the title. (See CDTFA Audit Manual, §§ 0640.05, 0607.75.)

⁸ In this appeal to OTA, appellant does not dispute the negligence penalty, and OTA does not discuss it any further.

charged off in accordance with generally accepted accounting principles. (R&TC, § 6055(a); Cal. Code Regs., tit. 18, § 1642(a).) If the worthless and charged off amount of an account 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)(1).)

When a retailer makes a repossession, a bad debt deduction is allowable only to the extent that the retailer sustains a net loss of gross receipts upon which tax has been paid. (Cal. Code Regs., tit. 18, § 1642(f)(1).) A net loss is sustained when the amount of all payments and credits allocated to the purchase price of the merchandise, including the wholesale value of the repossessed article, is less than that price. (*Ibid.*) 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; (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).)

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, CDTFA considered appellant's books and records adequate for sales and use tax audit purposes. CDTFA reviewed appellant's own sales records and determined that appellant had recorded more taxable sales than it had reported during the liability period. Appellant's sales records are direct evidence of its taxable sales. CDTFA also reviewed information obtained from the DMV and identified additional vehicle sales not recorded in appellant's

records. CDTFA made allowances for transactions that qualified as unwinds, repossessions, returns, canceled transactions, or buybacks. CDTFA also made allowances for bad debt supported by appellant's records, even though appellant did not claim any bad debt deductions for the liability period. OTA finds that CDTFA's determination was reasonable and rational. The burden of proof now shifts to appellant to establish a different result is warranted.

On appeal, appellant appears to argue that CDTFA made an audit error related to unexplained bank deposits. Appellant also asserts that he "disagree[s] with total unclaimed vehicles," and appears to argue that CDTFA should have allowed additional bad debt deductions.

Although CDTFA found unexplained excess bank deposits in its preliminary audit testing, CDTFA did not rely on a bank deposit analysis in determining the audited measure of unreported taxable sales; CDTFA relied on appellant's own sales records and DMV information. Furthermore, appellant has not provided any new evidence to support any additional bad debt deductions, and OTA finds the evidence in the record does not support any additional deductions. Therefore, appellant has failed to establish that CDTFA's determination is incorrect.

HOLDING

Appellant has not demonstrated that any further adjustment is warranted to the audited measure of unreported taxable sales.

DISPOSITION

Sustain CDTFA’s action in reducing the taxable measure from \$2,391,372 to \$2,337,442 and increasing the allowance for bad debt deduction from \$6,917 to \$7,962, with interest and penalty adjusted accordingly, but otherwise denying appellant’s petition for redetermination.

DocuSigned by:
Steven Kim

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Steven Kim
Administrative Law Judge

We concur:

DocuSigned by:
Suzanne B. Brown

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Suzanne B. Brown
Administrative Law Judge

DocuSigned by:
AW

8A4294817A57463...
Andrew Wong
Administrative Law Judge

Date Issued: 12/4/2024