OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of: **MADDMORE SPORTS GROUPS, INC.** **dba Apple Valley Bikes**	OTA Case No.: 240315766 CDTFA Case ID: 4-713-576

OPINION

Representing the Parties:

For Appellant: Kathleen Maddalena, President

For Respondent: Jason Parker, Chief of Headquarters Ops.

N. RALSTON, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 6561, Maddmore Sports Groups, Inc. dba Apple Valley Bikes (appellant) appeals a decision issued by the California Department of Tax and Fee Administration (respondent)[1] denying appellant's timely petition for redetermination of a Notice of Determination (NOD) issued on March 1, 2023. The NOD is for tax of $64,572, plus applicable interest, and penalties of $23,680.33 for the period July 1, 2019, through June 30, 2022 (liability period).

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).

ISSUES

1. Whether appellant has established that reductions to the amount of unreported taxable sales are warranted.
2. Whether appellant has established that reductions to the amount of unreported district tax are warranted.

[1] Sales and use taxes were formerly administered by the State Board of Equalization (board). In 2017, functions of the board relevant to this case were transferred to respondent. (Gov. Code, § 15570.22.) For ease of reference, when this Opinion refers to events that occurred before July 1, 2017, "respondent" shall refer to the board.

3. Whether respondent properly imposed the 40 percent penalty for failure to remit sales tax reimbursement collected but not remitted, and if so, whether appellant is entitled to relief of the penalty.
4. Whether respondent properly imposed the negligence penalty.
5. Whether appellant is entitled to relief of interest.

FACTUAL FINDINGS

1. Appellant is a California corporation dba Apple Valley Bikes. Appellant is a retailer of bicycles and related accessories, components and apparel. Appellant also offers repair services.
2. For the liability period, appellant filed sales and use tax returns (SUTRs) reporting total sales of $1,488,058 and purchases of $487,630 subject to use tax. Appellant also claimed deductions for nontaxable sales of $1,248,651,[2] resulting in reported taxable sales of $727,037.
3. For audit, appellant provided the following books and records: (1) federal income tax returns for 2019, 2020, and 2021; (2) point-of-sale (POS) reports for the liability period; (3) quarterly sales reports for the liability period, generated from appellant's POS system; and (4) a sample of invoices dated for various dates during the liability period.
4. Using the quarterly sales reports, respondent found that appellant recorded sales tax reimbursement (STR) collected from its customers of $116,074, which exceeded appellant's reported taxes of $53,924, thereby establishing STR of $62,150 ($116,074 - $53,924) that appellant collected but did not remit for the liability period.
5. After reviewing appellant's SUTRs, respondent noted that although appellant reported taxable sales of $484,533, appellant failed to report or remit any district tax for the business location for the third quarter of 2019 (3Q19), 1Q20 through 3Q20, and 4Q21 through 2Q22. Because appellant operated a business location in Apple Valley, California (which is subject to the district tax of San Bernadino County), respondent determined that appellant should have reported and paid district tax for the San Bernadino County jurisdiction on the taxable sales of $484,533. Thus, respondent established unreported district taxes of $2,422.
6. Respondent imposed a 40 percent penalty on appellant's unremitted STR collected for the periods 3Q19 through 4Q19, 2Q20 through 3Q21, and 1Q22 based on the following:

[2] The claimed deductions of $1,248,651 consists of nontaxable labor sales of $1,223,791 and bad debts of $24,860.

(1) respondent found that appellant was aware that it collected STR from its customers based on appellant's POS reports, which showed appellant collected STR from its customers, including tax added to its recorded taxable sales; (2) appellant failed to remit the tax reimbursement knowingly collected; (3) the unremitted tax reimbursement collected of $57,720 exceeded the threshold required for imposing the 40 percent penalty for the periods 3Q19 through 4Q19, 2Q20 through 3Q21, and 1Q22. Specifically, respondent noted the following: (1) the collected, unremitted reimbursement of $57,720 averaged more than $1,000 per month;[3] and (2) the collected, unremitted reimbursement divided by the total reimbursement collected exceeded 5 percent for each quarter.[4]

7. Respondent imposed the negligence penalty for the remainder of the liability period (1Q20, 4Q21, and 2Q22) because it determined that: (1) this was appellant's second audit; (2) the unreported taxable sales of $801,935 is more than 110 percent of appellant's reported taxable transactions of $727,037 for the liability period, indicating that appellant substantially understated its taxable sales; (3) appellant had access to information about its sales and use tax reporting, such as its own POS reports; and (4) appellant failed to report any district tax for 1Q20, 4Q21, or 2Q22.
8. Respondent timely issued the NOD to appellant for the liability period for $64,572 in tax, plus accrued interest, the 40 percent penalty of $23,088, and a negligence penalty of $592.33.
9. Respondent held an appeals conference with appellant on October 26, 2023, and issued its Decision on February 29, 2024.
10. Thereafter, appellant filed this timely appeal with OTA.

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).)

[3] The amounts vary between $1,026 and $4,575 per month.

[4] The amounts vary between 44.91 percent and 77.29 percent per quarter.

If respondent is not satisfied with the amount of tax reported by the taxpayer, or in the case of a failure to file a return, respondent 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, respondent has a minimal, initial burden of showing that its determination was reasonable and rational. (*Appeal of Talavera*, 2020-OTA-022P.) Once respondent has met its initial burden, the burden of proof shifts to the taxpayer to establish that a result differing from respondent's determination is warranted. (*Ibid*.) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (*Ibid*.)

Issue 1: Whether appellant has established that reductions to the amount of unreported taxable sales are warranted.

Using appellant's own POS records, respondent identified recorded STR collected of $116,074 for the liability period. Respondent compared the collected STR to appellant's reported tax due of $53,924, which resulted in unremitted STR collected of $62,150 ($116,074 - $53,924). Respondent thereafter multiplied this amount of unremitted STR by the applicable sales tax rate to establish unreported taxable sales of $801,935. Respondent established the amount of unreported taxable sales in accordance with recognized audit procedures. Further, respondent used appellant's own records which is direct evidence of sales. Thus, respondent's determination is reasonable and rational. (*Appeal of Micelle Laboratories, Inc*., 2020-OTA-290P.) As respondent has met its initial burden, the burden of proof shifts to appellant to establish that a different result is warranted.

Appellant does not specifically dispute the audited amount of unreported taxable sales but rather states that appellant does not agree with the amount listed under appellant's account. As appellant has not raised any argument or evidence to support any adjustments to the determination, appellant has not met its burden of proving a different result is warranted. Thus, no adjustment is warranted.

Issue 2: Whether appellant has established that reductions to the amount of unreported district tax are warranted.

Under the Sales and Use Tax Law (R&TC, § 6001 et seq.), California may impose sales tax or use tax at statewide rates. In addition, under both the Uniform Local Sales and Use Tax Law (R&TC, §§ 7200 et seq., including §§ 7202, 7203, and 7203.1) and the Transactions and Use Tax Law (R&TC, §§ 7251 et seq., including §§ 7251.1, 7261(a), 7262(a)), local jurisdictions may impose sales tax on the gross receipts from retail sales of tangible personal property within the jurisdiction or use taxes on the sales price of property sold for use, storage, or consumption

within the jurisdiction (collectively, district taxes). A retailer engaged in business in a jurisdiction imposing the district tax is required to collect and remit the tax. (R&TC, §§ 7261(a), 7262(a); see also Cal. Code Regs., tit. 18, § 1827(a).)

Appellant has not specifically disputed the audited amount of unreported district tax but rather states that appellant does not agree with the amount listed under appellant's account.

Respondent has established that appellant reported taxable sales of $484,533 for the periods 3Q19, 1Q20 through 3Q20, and 4Q21 through 2Q22, for which appellant did not report or remit any district taxes. Appellant operated one business location in San Bernadino County. Respondent's determination of unreported district tax measured on sales of $484,533 is reasonable and rational because it is based on figures recorded by appellant. Therefore, the burden of proof shifts to appellant to establish a different result. As appellant has not raised any argument or evidence to support any adjustments to the determination, appellant has not met its burden of proving a different result. Thus, no adjustment is warranted.

Issue 3: Whether respondent properly imposed the 40 percent penalty for failure to remit sales tax reimbursement collected but not remitted, and if so, whether appellant is entitled to relief of the penalty.

Any person who knowingly collects STR and fails to timely remit it to the state is liable for a penalty of 40 percent of the amount not timely remitted if the failure to remit exceeds certain thresholds. (R&TC, § 6597(a)(1).) The penalty does not apply if the person's liability for unremitted STR averages $1,000 or less per month or does not exceed 5 percent of the total amount of the tax liability for which the STR was collected for the period in which the tax was due, whichever is greater. (R&TC, § 6597(a)(2)(A).) In order for OTA to sustain respondent's imposition of the 40 percent penalty, respondent must establish that: (1) appellant knowingly collected STR from its customer(s); (2) appellant failed to timely remit the sales tax for which it collected the reimbursement; and (3) the amount of sales tax collected but not remitted exceeds the applicable threshold. (R&TC, § 6597(a)(1)-(2).) The applicable standard of proof is by a preponderance of the evidence. (*Appeal of ISIF Madfish, Inc*., 2019-OTA-292P.)

The law provides for relief of the 40 percent penalty if the taxpayer establishes that its actions were due to a reasonable cause or circumstances beyond the taxpayer's control and occurred notwithstanding the taxpayer's exercise of ordinary care and the absence of willful neglect. (R&TC, § 6597(a)(2)(B).) R&TC section 6597 provides six examples of reasonable cause, none of which are relevant to the facts under consideration. R&TC section 6597 does not establish a procedure for requesting relief. OTA interprets R&TC section 6597 to require the taxpayer or its designee to request relief and prove a factual basis for the request.

Appellant does not specifically address the 40 percent penalty but rather states that appellant does not agree with the amount listed under appellant's account. Appellant also states that appellant did not receive federal money during the COVID-19 pandemic and did not lay off any of its employees.

Appellant's POS reports show that appellant charges its customers for "sales tax" which indicates that appellant knowingly collected STR of $89,981. Furthermore, the amount of STR collected exceeded appellant's reported tax by $57,720, indicating appellant failed to timely remit STR collected for the nine applicable quarterly periods of 3Q19 through 4Q19, 2Q20 through 3Q21, and 1Q22. The unremitted STR averages more than $1,000 per month and totals more than 5 percent of the STR collected.[5]

The evidence shows that, in every quarter within the liability period to which respondent applied the penalty, appellant knowingly collected STR and failed to timely remit the sales tax for which it collected the STR. In addition, the amount of sales tax collected but not remitted exceeds the minimum thresholds set forth in R&TC section 6597(a)(2). Therefore, OTA finds that respondent correctly imposed the 40 percent penalty. Additionally, appellant does not argue and the record does not show that the penalty should be relieved.

Issue 4: 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; *see also People v. Superior Court* (*Sokolich*) (2016) 248 Cal.App.4th 434, 447.) Generally, 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 also *Independent Iron Works, Inc. v. State Bd. of Equalization* (1959) 167 Cal.App.2d 318, 321-324.)

[5] Specifically, the amount of unremitted STR averages between $1,026 and $4,575 per month and between 44.91 percent and 77.29 percent per month.

Respondent imposed the negligence penalty for the following reasons: (1) this was appellant's second audit, and respondent also found unreported taxable sales in the prior audit; (2) the audited amount of unreported taxable sales of $801,935 is more than 110 percent of appellant's reported taxable transactions of $727,037 for the liability period; (3) appellant's own POS reports showed the amount of STR appellant collected, and thus indicate that appellant had access to information regarding the amount of STR collected, and therefore, appellant could have avoided the substantial understatements had appellant acted with ordinary care; and (4) appellant did not report or remit any district tax for 1Q20, 4Q21, or 2Q22 and did not provide an explanation for its failure to do so.

Appellant requests relief of the negligence penalty because appellant alleges that the negligence penalty was improperly calculated. Respondent imposed a negligence penalty of $593 for the periods 1Q20, 4Q21, and 2Q22. Appellant argues that the negligence penalty should be $496.80. Appellant has not explained how it calculated that figure and there is no evidence in the record to conclude that respondent's calculation is incorrect.

Here, respondent has provided evidence that appellant was negligent. This was appellant's second audit and appellant repeated the same errors in the current audit as in the prior audit. In addition, the understatement was substantial and appellant has not provided a non-negligent explanation for the understatement. Further, appellant collected a substantial amount of STR but failed to remit it and also failed to remit any district tax for 1Q20, 4Q21, or 2Q22. Thus, OTA finds that the negligence penalty was properly imposed.

Issue 5: Whether appellant is entitled to relief of interest.

There is no statutory right to interest relief. The law allows respondent, in its discretion, to grant relief of all or any part of the interest imposed on a person under the Sales and Use Tax Law in certain circumstances, including where the failure to pay the tax was due to a disaster, where the failure to pay the tax was due in whole or in part to an unreasonable error or delay by an employee of respondent acting in their official capacity, and where the failure to pay the tax was due to erroneous advice received from respondent. (R&TC, §§ 20, 6593, 6593.5(a)(1), 6596.) Any person requesting interest relief must include a statement under penalty of perjury setting forth the facts on which the request is based. (R&TC, §§ 6593(b), 6593.5(c), 6596(c)(2).)

Respondent has determined that the current interest balance is overstated by $430.48 because respondent inadvertently included interest for March 2023. Respondent will make an adjustment to interest when the appeals process is completed.

Appellant argues that it is entitled to relief from interest on the basis that it is not appellant's fault that the audit took so long. Appellant also requests relief due to hardships experienced due to the COVID-19 pandemic. Appellant does not allege or offer any evidence to prove an unreasonable error or delay by an employee of respondent acting in their official capacity or that any other basis exists to relieve interest. Therefore, OTA finds that appellant is not entitled to relief of interest.

HOLDINGS

1. Appellant has failed to establish that reductions to the amount of unreported taxable sales are warranted.
2. Appellant has failed to establish that reductions to the amount of unreported district tax are warranted.
3. Respondent properly imposed the 40 percent penalty for failure to remit sales tax reimbursement collected but not remitted, and appellant is not entitled to relief of the penalty.
4. Respondent properly imposed the negligence penalty.
5. The amount of interest shall be reduced by $430.48. Appellant is not entitled to any additional relief of interest.

DISPOSITION

Respondent's action is sustained, with the exception that interest shall be reduced by $430.48 as conceded by respondent.

Signed by:
Natasha Ralston
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Natasha Ralston
Administrative Law Judge

We concur:

Signed by:
Josh Lambert
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Josh Lambert
Administrative Law Judge

DocuSigned by:
Steven Kim
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Steven Kim
Administrative Law Judge

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