OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeals of:	OTA Case Nos. 18042588. 18124124
OJOGHO AMERICAN ENTERPRISES, INC.	CDTFA Case IDs: 716170, 873160

OPINION

Representing the Parties:

For Appellant:	Willfred I. Aka, Attorney Christian Ojogho, President
For Respondent:	Nalan Samarwarickrema, Hearing Representative Christopher Brooks, Attorney Jason Parker, Chief of Headquarters Operations
For Office of Tax Appeals:	Corin Saxton, Tax Counsel IV

J. ALDRICH, Administrative Law Judge: These consolidated appeals are made pursuant to California Revenue and Taxation Code (R&TC) section 6561. Ojogho American Enterprises, Inc. (appellant) appeals a decision and recommendation (decision) issued by respondent California Department of Tax and Fee Administration (CDTFA)[1] denying, in part, appellant's petition for redetermination of a Notice of Determination (NOD) dated January 29, 2013.[2] The NOD is for a tax liability of $644,208.59, applicable interest, and a negligence penalty of $64,420.80 for the period October 1, 2008, through December 31, 2011 (Liability Period 1).

[1] 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 referring to acts or events that occurred before July 1, 2017, "CDTFA" shall refer to BOE; and when referring to acts or events that occurred on or after July 1, 2017, "CDTFA" refers to CDTFA.

[2] The NOD was timely issued because on July 17, 2012, appellant signed the most recent in a series of waivers of the otherwise applicable three-year statute of limitations for the liability period. (See R&TC, §§ 6487(a), 6488.)

Appellant also appeals a decision and supplemental decision issued by CDTFA denying appellant's petition for redetermination of an NOD dated April 17, 2015. The NOD is for a tax liability of $239,220.63, applicable interest, and a negligence penalty of $23,922.12 for the period January 1, 2012, through December 31, 2014 (Liability Period 2).[3] On March 28, 2017, CDTFA increased the tax liability to $517,146.23, and increased the corresponding negligence penalty to $51,714.65, pursuant to R&TC section 6563.[4] CDTFA issued the increased tax liability in a NOD dated June 6, 2017.

Office of Tax Appeals (OTA) Administrative Law Judges Ovsep Akopchikyan, Natasha Ralston, and Josh Aldrich held an oral hearing for this matter in Cerritos, California, on October 10, 2023. At the conclusion of the hearing, the record was held open for additional briefing. During the additional briefing period, the panel was revised; Administrative Law Judge Andrew Wong replaced Ovsep Akopchikyan. On May 21, 2024, the record closed.

ISSUES

1. Whether any reduction to the amounts of unreported taxable sales is warranted.
2. Whether the negligence penalty was properly imposed for each liability period.

FACTUAL FINDINGS

1. Appellant is a California corporation. Appellant is a retailer of soccer clothing, footwear, equipment, and accessories, with sales for resale and sales in interstate commerce. Appellant makes sales at its Southern California retail locations, as well as over the internet.
2. Appellant's sole corporate officer was the owner of appellant's predecessor, a sole proprietorship that CDTFA audited for the period January 1, 1997, through March 31, 2005. That audit resulted in the determination of unreported taxable sales of $1,140,978.

[3] The NOD was timely issued. (See R&TC, § 6487.)

[4] CDTFA may increase the amount of a determination before it becomes final if CDTFA asserts a claim for the increase at or before an Office of Tax Appeals hearing and, as relevant here, within three years after the first deficiency determination or within three years after the time tax records requested by CDTFA were made available, whichever is later. (R&TC, § 6563(a).) Here, the NOD was not final, and CDTFA asserted the increase within three years of the date that it issued the determination.

3. CDTFA issued appellant a seller's permit with an effective start date of July 1, 2005. On December 5, 2007, appellant added two additional retail stores to the seller's permit: Soccer Shop USA III, located in Van Nuys; and Soccer Ship USA, located in Los Angeles. On January 1, 2009, appellant added A-1 Soccer Warehouse, located in Los Angeles, to its seller's permit.

Liability Period 1

4. Appellant was audited for Liability Period 1.
5. During Liability Period 1, appellant reported total sales of $2,017,142. Of the total sales, appellant claimed the following deductions: nontaxable sales for resale of $945,119; nontaxable sales in interstate commerce of $827,435; and sales tax reimbursement of $19,295 included in reported sales. Appellant reported taxable sales of $225,293 for the period.
6. Upon audit, appellant provided federal income tax returns (FITRs) for 2009 and 2010; quarterly sales summary report for Liability Period 1; sales journals for third quarter 2009 (3Q09), 1Q10, 3Q10, and 4Q11; business bank statements and cancelled checks for January 2009 through December 2011; a box of unorganized purchase invoices; sales invoices for October 2008 through December 2010; a vendor list; and a list of customers who purchased items for resale.
7. CDTFA analyzed appellant's sales and use tax returns (SUTRs) and noted that average daily taxable sales per quarter ranged from $137 to $372 for the period October 1, 2008, through December 31, 2014. CDTFA also calculated taxable sale percentages for each quarter of both liability periods and calculated that quarterly reported taxable sale percentages averaged 10.71 percent, ranging from 5.20 percent to 42.28 percent.
8. CDTFA determined that additional investigation was warranted because it considered the average daily taxable sales per quarter and the quarterly reported taxable sale percentages to be very low based on the number, nature, and location of the stores.
9. CDTFA analyzed appellant's FITRs. Appellant and A-1 Soccer Warehouse filed separate FITRs, but appellant's seller's permit identified A-1 Soccer Warehouse as a branch location and appellant reported A-1 Soccer Warehouse's sales through appellant's seller's permit. Further, A-1 Soccer Warehouse's FITRs indicated that its sales were reported on appellant's FITRs. Therefore, in its analysis of appellant's

taxable sales for Liability Period 1, CDTFA utilized both appellant's FITRs and A-1 Soccer Warehouse's FITRs (hereafter collectively referred to as "appellant's FITRs").

10. Gross receipts reported on appellant's FITRs for 2009 and 2010 exceeded total sales reported on appellant's SUTRs for 2009 and 2010 by $2,499,352 ($1,771,021 + $728,331).

11. CDTFA could not verify reported taxable sales using the markup method because appellant did not provide sufficient documentation.[5] CDTFA, however, compared reported total sales to appellant's purchases based on appellant's FITRs. CDTFA calculated negative markups of 77.06 percent and 40.82 percent for 2009 and 2010, respectively.

12. CDTFA also determined that it could not perform a bank deposit analysis because bank deposits for 2009 did not include all proceeds from appellant's sales for that year.[6] Therefore, CDTFA used gross receipts reported on appellant's 2009 FITRs to establish unreported taxable sales.

13. CDTFA subtracted total sales reported on appellant's 2009 SUTRs of $335,827 (minus claimed deductions for sales tax included) from gross receipts reported on appellant's 2009 FITR of $2,106,848 (minus claimed deductions for sales tax included), to compute unreported total sales of $1,771,021. CDTFA then divided this amount by four to compute quarterly unreported total sales of $442,755. CDTFA increased this amount by 20 percent to $531,306 based on a prior audit of the business. At that time, the business was a sole proprietorship. CDTFA then multiplied the quarterly unreported total sales of $531,306 by 13 (the number of quarters in Liability Period 1), to compute total unreported sales of $6,906,978.

14. Since appellant did not provide any documentation to show that this amount was nontaxable, CDTFA determined the entire amount to be taxable, and established a

[5] While some source documents were available for CDTFA's inspection, the majority of appellant's records were not available. Appellant told CDTFA that it did not retain purchase journals, and the purchase invoices appellant provided were disorganized and not in a condition that could be examined. Furthermore, the cancelled checks appellant provided were unclear, and appellant did not provide any record of physical inventory.

[6] CDTFA concluded that bank deposits for 2009 did not include all proceeds from appellant's sales for that year because, although appellant asserted that sales decreased from 2009 to 2010, total bank deposits for 2010 exceeded total bank deposits for 2009. Also, appellant's profit and loss statement for 2010 shows appellant's sales for 2010 exceeded its sales for 2009 by approximately $768,000.

deficiency measure for unreported taxable sales of $6,906,978. CDTFA also imposed a negligence penalty of $64,420.80 on the basis that appellant's books and records were incomplete and inaccurate for sales and use tax reporting purposes.

15. CDTFA issued the NOD dated January 29, 2013, to appellant.

16. Appellant filed a timely petition for redetermination, and CDTFA issued a decision on December 12, 2016, concluding that the 20 percent increase of quarterly unreported total sales lacked adequate support, and that the deficiency measure should be reduced by $1,151,163 to $5,755,815 ($442,755 x 13).[7] According to the reaudit report, the tax liability is $536,840.65, plus applicable interest, and a negligence penalty of $53,684.13. CDTFA otherwise recommended that the petition for redetermination be denied.

17. The timely appeal of Liability Period 1 followed.

Liability Period 2

18. CDTFA also audited appellant for Liability Period 2.

19. During Liability Period 2, appellant reported total sales of $2,872,318. Of the total sales, appellant claimed the following deductions: nontaxable sales for resale of $1,320,626; nontaxable sales in interstate commerce of $1,232,037; and sales tax reimbursement of $26,210 included in reported sales. Appellant reported taxable sales of $293,445 for the period.

20. Similar to the earlier audit, appellant did not provide complete sales records (e.g., sales receipts or daily sales invoices, credit card sales receipts, resale certificates, shipping documents, payment information from its customers, sales journals, and sales summaries). Appellant also did not provide complete purchase information or purchase journals.

21. CDTFA analyzed appellant's SUTRs in the same manner as it did for Liability Period 1, and concluded that additional investigation was warranted.[8]

22. Similar to the discussion above, CDTFA analyzed appellant's FITRs for 2012, 2013, and 2014. For these years, CDTFA compared reported total sales to appellant's

[7] On March 8, 2017, CDTFA completed a reaudit that incorporated the decision's recommended adjustment.

[8] See Factual Findings 7 and 8, *ante*.

purchases. For 2012, 2013, and 2014, CDTFA calculated appellant's markup as 159.9 percent, 86.89 percent, and 131.6 percent, respectively.

23. To verify the accuracy of purchases recorded on appellant's FITRs, CDTFA conducted a survey of appellant's vendors. Based on the purchase information from the vendors, appellant's vendor purchases exceeded recorded purchases by $6,565,203 ($7,830,603 in audited purchases - $1,265,400 recorded purchases). For 2013 and 2014, vendor purchase information showed that appellant purchased $7,187,864in product, however, appellant recorded only $943,962 on its FITRs for the same period.

24. Based on the audited purchases, CDTFA calculated a negative markup of 63.59 percent for Liability Period 2.

25. CDTFA conducted a bank deposit analysis. From January 2009 through December 2013, appellant deposited $6.6 million, but only reported total sales of $3.5 million for the same period. CDTFA imposed the negligence penalty because appellant had previously been audited, and therefore knew or should have known the types of records to maintain, but still failed to make such records available for audit. CDTFA also imposed the penalty because appellant failed to improve in its reporting from one period to the next.

26. Based on the bank deposit analysis, CDTFA issued the April 17, 2015 NOD.

27. Appellant filed a timely petition for redetermination, and CDTFA conducted a reaudit.

28. During the reaudit, CDTFA obtained IRS Form 1099-Ks (1099-K statements)[9] for 2012 and 2013 from Amazon, American Express, and Wells Fargo showing payments to appellant.[10] Although the original audit used a bank deposit analysis to calculate audited taxable sales, CDTFA determined in the reaudit that the 1099-K statements constitute a

[9] Form 1099-K (*Payment Card and Third Party Network Transactions*) is an IRS form that shows the monthly and annual amounts paid to a merchant by a bank, credit card company, or third party network during a given time period. Form 1099-K includes payments made by any electronic means, including, but not limited to, credit cards, debit cards, and PayPal.

[10] The 1099-K statements listed the following payees: appellant; Soccer Shop USA; and Christian Ojogho (appellant's president). Based on appellant's opening brief, there appears to be no dispute that payments to Soccer Shop USA and Christian Ojogho constitute payments to appellant. CDTFA did not include sales relating to A-1 Soccer Warehouse on 458 South Alameda Street and Soccer Warehouse on 455 Seaton Street. These stores are related to, but not owned by appellant.

more reliable basis for calculating audited taxable sales.[11] CDTFA subtracted appellant's claimed nontaxable sales for resale and sales in interstate commerce for 2012 and 2013 (totaling $1,396,533) from the payments of $4,915,458 listed on the 1099-K statements to establish tax-included taxable sales of $3,518,905. To account for sales tax reimbursement, CDTFA further reduced this amount by $284,849, thereby establishing taxable credit card sales of $3,234,056 for 2012 and 2013.

29. Due to the absence of source documentation, such as cash register tapes and invoices, CDTFA estimated the ratio of credit card sales to total sales. Based on CDTFA's experience auditing similar businesses, CDTFA estimated a 10 percent ratio of credit card sales to total sales. Therefore, CDTFA divided ex-tax credit card sales of $3,234,056 by .90 to compute audited taxable sales of $3,593,395 for 2012 and 2013. When compared to reported taxable sales of $172,467 for this period, appellant's unreported taxable sales of $3,420,928 ($3,593,395 - $172,467) represents an error ratio of 1,983.53 percent. CDTFA applied this error ratio to appellant's reported taxable sales of $293,445 for the audit period to calculate unreported taxable sales of $5,820,563 for the audit period.[12]

30. In the March 28, 2017 reaudit report, CDTFA increased appellant's tax liability to $517,146.23 and the negligence penalty to $51,714.65.

31. CDTFA sent appellant a notice with the asserted increased.

32. In its decision and supplemental decision, CDTFA sustained the reaudit report and denied appellant's petition for redetermination.

33. The timely appeal of Liability Period 2 followed.

[11] This determination was based on the fact that the 1099-K information was provided by third parties, as well as the fact that the 1099-K statements listed payments in excess of the bank deposits. In addition, CDTFA conducted a markup analysis using the 1099-K statements and purchase invoices, which resulted in a positive markup (24.88 percent) for the audit period, whereas a markup based on bank statements and purchase invoices resulted in a negative markup (-1.98 percent) for the audit period.

[12] Based on this calculation, the deficiency measure should be $5,820,558, which is a nominal difference.

DISCUSSION

Issue 1: Whether adjustments are warranted to the audited understatements of reported taxable sales.

California imposes upon all retailers a sales tax measured by the retailer's gross receipts from the sale of all tangible personal property sold at retail in this state, 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 evasion of the sales tax, it is presumed that all gross receipts are subject to the tax until the contrary is established. (R&TC, § 6091.)

Taxpayers are required to maintain and make available for examination on request by CDTFA, or its authorized representative, 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 SUTRs. (R&TC, §§ 7053, 7054; Cal. Code Regs., tit. 18, § 1698(b)(1).) Such records include but are not limited to: (a) the normal books of account ordinarily maintained by the average prudent businessperson engaged in the activity in question; (b) bills, receipts, invoices, cash register tapes, or other documents of original entry supporting the entries in the books of account; and (c) schedules or working papers used in connection with the preparation of the tax returns. (Cal. Code Regs., tit. 18, § 1698(b)(1).)

If CDTFA is not satisfied with the returns of the amount of tax required to be paid to the state by any person, CDTFA may compute and determine the amount required to be paid on the basis of any information within its possession or that may come into its possession. (R&TC, § 6481.) If any person fails to make a return, CDTFA shall make an estimate of the amount of the gross receipts of the person based upon any information within its possession or that may come into its possession. (R&TC, § 6511.)

In the case of an appeal, CDTFA has a minimal, initial burden of showing that its determination was reasonable and rational. (*Appeal of Las Playas #10, Inc.*, 2021-OTA-204P.) If CDTFA's determination is not reasonable and rational, then the determination should be rejected. (See *Appeal of Praxair, Inc.*, 2019-OTA-301P; see also *In re Renovizor's, Inc.* (9th Cir. 2002) 282 F.3d 1233, 1237, fn. 1.) If CDTFA's determination is reasonable and rational, then the determination is presumed correct. (See *In re Renovizor's, Inc.*, *supra*, 282 F.3d at 1237, fn. 1; see also *Paine v. State Bd. of Equalization* (1982) 137 Cal.App.3d 438, 445

(*Paine*).) The burden of overcoming this presumption is on the taxpayer. (*Paine*, *supra*, 137 Cal.App.3d at p. 445.)

Generally, appellant bears the burden of proof as to all issues of fact unless the law specifies otherwise. (Cal. Code Regs., tit. 18, § 30219(a).) The standard of proof is by a preponderance of the evidence unless the law specifies otherwise. (Cal. Code Regs., tit. 18, § 30219(b).) That is, a party must establish by documentation or other evidence that the circumstances it asserts are more likely than not to be correct. (*Appeal of AMG Care Collective*, 2020-OTA-173P.) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (*Appeal of Las Playas #10, Inc.*, *supra*.) To satisfy their burden of proof, a taxpayer must prove both that the tax assessment is incorrect and the proper amount of tax. (*Appeal of AMG Care Collective*, *supra*.)

Liability Period 1

Here, CDTFA examined appellant's SUTRs and found that appellant's daily taxable sales were very low based on the number, nature, and locations of appellant's stores. Appellant had multiple retail stores on its seller's permit. Appellant also reported A-1 Soccer Warehouse's sales on appellant's SUTRs. Further, A-1 Soccer Warehouse's FITRs indicate that its sales were reported on appellant's FITRs. Contrary to appellant's assertion, the records provided did not demonstrate that the reported sales were accurate. The records made available for audit were incomplete, and the records shows that appellant also did not maintain accurate records. Accordingly, CDTFA used appellant's 2009 FITR to calculate audited taxable sales for 2009, which CDTFA reduced by reported taxable sales for 2009, to establish unreported taxable sales for 2009. CDTFA then projected the audited quarterly unreported taxable sales amount to the entire audit period to determine the tax liability. Based on the foregoing, OTA finds that it was reasonable and rational for CDTFA to use appellant's FITRs for one year of the liability period to calculate the determined measure of tax. Accordingly, the burden of proof shifts to appellant to establish error in CDTFA's determined measure of tax.

On appeal, appellant makes the following five arguments: (1) CDTFA arbitrarily and capriciously chose 2009 as the examination year since the records provided for audit were accurate; (2) CDTFA's 20-percent increase was arbitrary; (3) CDTFA inappropriately relied on

records outside the audit period, including bank statements belonging to CIW Sport;[13] (4) Amazon was the retailer of internet sales attributed to appellant, including unreported nontaxable sales; and (5) reductions are warranted for additional sales in interstate commerce and sales for resale.

Regarding appellant's first argument, in the absence of any argument or evidence that appellant's 2009 FITR is anomalous or unrepresentative of appellant's sales during the audit period, OTA finds this first argument unpersuasive. With respect to appellant's second argument that the 20 percent increase was arbitrary, this second argument is moot because CDTFA deleted this amount pursuant to the decision. Regarding appellant's third argument that CDTFA inappropriately relied on records outside the audit period, including bank statements allegedly belonging to CIW Sport, the audit workpapers expressly state that CIW Sport is not a sub-location because it is not included in appellant's Wells Fargo bank statements. While CDTFA utilized bank statements outside of the audit period to examine the reasonableness of the taxable measure, CDTFA did not use the bank records outside the audit period to establish the taxable measure. Thus, appellant's contention is unpersuasive.

As for appellant's fourth argument that Amazon was the retailer of its internet sales, appellant has not provided support for this argument with fact or law. Specifically, during the oral hearing appellant claimed that an operating agreement or contract existed between appellant and Amazon during both liability periods that purportedly showed that Amazon was the retailer. Despite multiple opportunities, appellant did not produce such an operating agreement or contract. All gross receipts are presumed subject to the tax until the contrary is established, and the available evidence (e.g., the seller's permit, the FITRs, an Amazon.com printout indicating that the products were "sold by USA Soccer Shop and fulfilled by Amazon") demonstrates that appellant is the actual retailer. Consequently, OTA finds that this fourth argument unavailing. Similarly, concerning appellant's fifth argument that reductions are warranted for additional sales in interstate commerce and sales for resale, appellant has not provided evidentiary support for this argument, and, given that CDTFA accepted all of appellant's claimed deductions for nontaxable sales, OTA finds no adjustments are warranted for additional nontaxable sales.

[13] CIW Sport was located at 458 South Alameda Street in the same building as A-1 Soccer Warehouse. CIW Sport had a seller's permit that started in 2013 and was closed out on April 1, 2015. During this period CIW Sport filed two returns claiming total sales of 2 million, all exempt.

Liability Period 2

Here, appellant failed to provide complete books and records for audit; thus, CDTFA was unable to verify appellant's reported sales for Liability Period 2 using a direct audit method (that is, compiling audited sales directly from appellant's records). Given appellant's lack of records, CDTFA analyzed appellant's reported sales by examining appellant's FITRs and SUTRs, by performing a bank deposit analysis, conducting a vendor survey for purchase information, as well as other methods. OTA finds that it was reasonable for CDTFA to question reported sales and use an indirect audit method to compute appellant's sales. CDTFA's use of the credit-card-sales ratio method as the basis for its determination in the reaudit is a recognized and accepted accounting procedure. (*Appeal of Amaya*, 2021-OTA-328P.) OTA also finds that Form 1099-K data (e.g., 2012 and 2013 1099-K statements) is evidence from third parties of appellant's sales paid by credit card and is a reliable source of data from which to establish audited sales. Therefore, OTA concludes that CDTFA has established that its determination is reasonable and rational; accordingly, the burden shifts to appellant to show error in the audit.

With respect to Liability Period 2, appellant makes the following three arguments: (1) payments listed on the 1099-K statements were payments made to other entities (specifically, Soccer Kingdom and/or M. Ojogho); (2) the deficiency measure consists of sales made by Amazon, not appellant; and (3) sales made over the internet are exempt as sales in interstate commerce. In support of these arguments, appellant submitted spreadsheets identifying sales purportedly made by Amazon and/or in interstate commerce.

With respect to appellant's argument that payments listed on the 1099-K statements do not reflect payments made to appellant, OTA notes that the reaudit working papers indicate that appellant was the payee listed on the 1099-K statements, and appellant has not presented any evidence to demonstrate otherwise. Regarding appellant's arguments that the deficiency measure consists of sales made by Amazon, not appellant, and that sales made over the internet are exempt as sales in interstate commerce, OTA is not persuaded for the same reasons indicated above.

In summary, OTA finds that CDTFA computed taxable sales based on the best available evidence. Appellant has not identified any errors in CDTFA's computation of audited taxable sales or provided documentation or other evidence in support of its contention from which a more accurate determination could be made. The taxpayer cannot carry its burden of proof

simply by asking OTA to find unidentified errors in CDTFA's determination. (*Appeal of Amaya*, *supra*.) Based on the foregoing, OTA finds that appellant has not met its burden of establishing an error with CDTFA's determined measure of tax.

Issue 2: Whether the negligence penalty was properly imposed for each liability period.

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.)

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 SUTRs. (R&TC, §§ 7053, 7054; Cal. Code Regs., tit. 18, § 1698(b).) All records required to be retained under this regulation must be preserved for a period of not less than four years. (Cal. Code Regs., tit. 18, § 1698(i).) Failure to maintain and keep complete and accurate records will be considered evidence of negligence or intent to evade the tax and may result in penalties or other appropriate administrative action. (Cal. Code Regs., tit. 18, § 1698(k).)

For Liability Period 1, CDTFA imposed the negligence penalty on the basis that appellant's books and records were incomplete and inaccurate for sales and use tax reporting purposes. For Liability Period 2, CDTFA imposed the negligence penalty on the same basis.

On appeal, appellant argues that it maintained adequate books and records. Specifically, appellant argues that it meets this standard because it could report total sales based on its bank deposits and claimed deductions based on a ratio of taxable sales to exempt sales.

While Liability Period 1 represents appellant's first audit, OTA notes that the predecessor entity, a sole proprietorship, was audited. The owner of the sole proprietorship was appellant's president. Therefore, appellant's president knew or should have known of the recordkeeping requirements. Further, the audit working papers state that the majority of appellant's records were unavailable, which is evidence of negligence. In addition, the differences between gross receipts reported on appellant's FITRs and the total sales reported on appellant's SUTRs should have apprised appellant of the fact that it was underreporting total sales on its SUTRs. Furthermore, a comparison of unreported taxable sales of $5,755,815 (established in the decision) with appellant's reported taxable sales of $225,293 shows a reporting error rate of 2,554.8 percent. An error rate of this magnitude is strong evidence of negligence.

For Liability Period 2, this was appellant's second audit, and the third audit involving appellant's sole corporate officer. The records continued to be inadequate, which is evidence of negligence. Further, the tax liability ($517,146.23) is similar in magnitude to the tax liability in the prior liability period ($536,840.65 in the reaudit of Liability Period 1). This shows that appellant not only continued to keep inadequate records after Liability Period 1, but also continued the inadequate reporting methods. The failure to improve record keeping and the continued errors in reporting are evidence of negligence.

Based on the foregoing, OTA finds that appellant's understatement in Liability Period 1 cannot be attributed to a bona fide and reasonable belief that the bookkeeping and reporting practices were sufficiently compliant with the requirements of the Sales and Use Tax Law. OTA also finds that appellant acted negligently for Liability Period 2. Therefore, OTA finds that CDTFA properly imposed the negligence penalty for each liability period.

HOLDINGS

1. No reduction to the measure of unreported taxable sales is warranted.
2. Appellant was negligent, and CDTFA properly imposed the negligence penalty for each liability period.

DISPOSITION

CDTFA's actions are sustained in full.

DocuSigned by:
Josh Aldrich
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Josh Aldrich
Administrative Law Judge

We concur:

DocuSigned by:
8A4294617A67463...
Andrew Wong
Administrative Law Judge

Signed by:
Natasha Ralston
25F8FE08FF56478...
Natasha Ralston
Administrative Law Judge

Date Issued: 8/27/2024