

BEFORE THE OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

IN THE MATTER OF THE APPEAL OF, )  
 )  
JOHNNIE'S PAINT and BODY SHOP, INC., ) OTA NO. 240415983  
 )  
APPELLANT. )  
 )  
 )

TRANSCRIPT OF PROCEEDINGS

Cerritos, California

Tuesday, December 9, 2025

Reported by:  
ERNALYN M. ALONZO  
HEARING REPORTER

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Transcript of Proceedings, taken at  
12900 Park Plaza Drive, Suite 300, Cerritos,  
California, 90703, commencing at 1:00 p.m.  
and concluding at 2:29 p.m. on Tuesday,  
December 9, 2025, reported by Ernalyn M. Alonzo,  
Hearing Reporter, in and for the State of  
California.

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APPEARANCES:

Panel Lead: ALJ JOSH ALDRICH

Panel Members: ALJ STEVEN KIM  
ALJ ANDREW WONG

For the Appellant: MICHAEL O'CONNOR  
GEOFFREY PLOURDE  
VATCHE DERDERIAN

For the Respondent: STATE OF CALIFORNIA  
DEPARTMENT OF TAX AND  
FEE ADMINISTRATION  
  
SUNNY PALEY  
JARRETT NOBLE  
JASON PARKER

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I N D E X

E X H I B I T S

(Appellant's Exhibits 1-4 were received into evidence at page 10.)

(Department's Exhibits A-H were received into evidence at page 10.)

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1 Cerritos, California; Tuesday, December 9, 2025

2 1:00 p.m.

3  
4 JUDGE ALDRICH: This is Judge Aldrich. We're  
5 opening the record in Johnnie's Paint and Body Shop  
6 Incorporated, doing business as Fix Auto Pasadena, before  
7 the Office of Tax Appeals, OTA Case No. 240415983.

8 Today's date is Tuesday December 9th, 2025, and it is  
9 approximately 1:00 p.m. The hearing is being live  
10 streamed on OTA's YouTube channel.

11 This hearing is being heard by a panel of three.  
12 My name is Josh Aldrich. I'm the lead Administrative Law  
13 Judge for purposes of conducting the hearing. I'm joined  
14 by Administrative Law Judges Steven Kim and Andrew Wong.  
15 We three are co-equal decision makers. And as such,  
16 during the hearing, panel members may ask questions or  
17 otherwise participate to make sure that we have all the  
18 information required. After the conclusion of the  
19 hearing, once the record is closed, we will deliberate and  
20 decide the issues presented.

21 As reminder, the Office of Tax Appeals is not a  
22 court. It is an independent appeals body. The panel does  
23 not engage in ex parte communications with either party.  
24 Our opinion will be based on the parties' arguments,  
25 evidence, and the relevant law. And we have read the

1 parties' submissions, and we're looking forward to your  
2 arguments today.

3 So at this time, who is present for Appellant,  
4 beginning with counsel?

5 MR. O'CONNOR: Good morning -- or I'm sorry.  
6 Good afternoon to the panel. My name is Michael O'Connor.  
7 I represent the taxpayer, Johnnie's Auto. To my right is  
8 Vatche Derderian, present CEO of Johnnie's. And to his  
9 right is my associate Geoffrey Plourde.

10 JUDGE ALDRICH: And, Mr. O'Connor, if I could  
11 have you move the microphone a little bit closer, so it's  
12 easier for it to pick up.

13 MR. O'CONNOR: Is that better, Your Honor?

14 JUDGE ALDRICH: I think so. Let me just confirm.

15 MR. O'CONNOR: Did you want me to do a test?

16 JUDGE ALDRICH: That's perfect. All right. It  
17 sounds good on the live stream. So thank you for that.

18 And who is present for Respondent, or California  
19 Department of Tax and Fee Administration, which I may  
20 refer to as CDTFA for short.

21 MS. PALEY: Yes. Sunny Paley with CDTFA,  
22 attorney.

23 MR. NOBLE: Jarrett Noble with CDTFA, also an  
24 attorney.

25 MR. PARKER: Jason Parker, Chief of Headquarters

1       Operations Bureau with CDTFA.

2               JUDGE ALDRICH:   Great.   Welcome everyone.

3               So the issue statements that I'm about to read  
4       are slightly different than the issue statements that are  
5       memorialized on our November 5th, 2025, Minutes and  
6       Orders.   There are a few omissions or errata, and I'll  
7       point those out:   But the first issue is whether any part  
8       of the deficiency determination is barred by the statute  
9       of limitations provided in Revenue & Taxation Code  
10      section 6478.   I'd indicated 6387, which is not relevant  
11      to this appeal; two, whether CDTFA properly imposed a  
12      25 percent fraud penalty for the period of  
13      January 1st, 2008, through December 31st, 2006, or the  
14      liability period, which we refer to it as that; whether  
15      CDTFA properly imposed the 40 percent penalty on  
16      unremitted sales tax reimbursement on the Minutes and  
17      Orders I had admitted; and fourth, whether adjustments to  
18      the measure of unreported taxable sales are warranted.

19              Mr. O'Connor, do these issues statements  
20      correctly reflect the issues before us?

21              MR. O'CONNOR:   Yes, Your Honor.

22              JUDGE ALDRICH:   Ms. Paley?

23              MS. PALEY:   Yes.   Thank you.

24              JUDGE ALDRICH:   Thank you.

25              So regarding exhibits, on November 24th, 2025,

1     OTA distributed a hearing binder to the parties, which  
2     compiled all of the exhibits identified during the  
3     prehearing conference. On the same day, OTA received a  
4     copy of Appellant's exhibit binder, which is 100 pages in  
5     length; and Appellant's index on that exhibit binder  
6     indicates that Exhibit 1 is 3 to 6 pages. Exhibit 2 is  
7     two pages. Exhibit 3 is 8 pages, and Exhibit 4 is  
8     96 pages in length. However, the sum of those pages is in  
9     excess of the pages in Appellant's exhibit binder. So I  
10    want to make sure that OTA's hearing binder includes all  
11    pages that Appellant wishes to introduce into evidence.

12           So I guess my question is, to Appellant's  
13    counsel, what, if anything, is missing from the hearing  
14    binder that was prepared by OTA and distributed to the  
15    parties?

16           MR. O'CONNOR: Not -- nothing that I'm aware of,  
17    Your Honor. If anything, I -- I think that the issue is  
18    probably an estimation on what the pages were. And then  
19    when the actual pages came out, there's -- that's what the  
20    variances, but there's been nothing redacted. The  
21    exhibits have always remained the same. I would also  
22    posit that, in this case, I don't think any of these  
23    exhibits are really at issue. Everybody has kind of seen  
24    everything so far.

25           JUDGE ALDRICH: Okay. All right. I thought I



1 had included everything in preparing the exhibit binder,  
2 but I just wanted to double check.

3 MR. O'CONNOR: No. I think it's on our end, Your  
4 Honor.

5 JUDGE ALDRICH: Okay. Thank you.

6 So going back to that, CDTFA's exhibits are  
7 identified alphabetically as Exhibits A through H. And,  
8 during the prehearing conference, Appellant's counsel  
9 confirmed receipt of A through H. They were sent again,  
10 and Appellant had no objection to admitting CDTFA's  
11 exhibits.

12 Mr. O'Connor, is that still the case?

13 MR. O'CONNOR: That's still the case, Your Honor.

14 JUDGE ALDRICH: Okay. And for Appellant, during  
15 the prehearing conference, Appellant submitted Exhibits A  
16 through D, or identified them. We relabeled them as  
17 Exhibits 1 through 4. And, during the prehearing  
18 conference, CDTFA indicated they had received Exhibits 1  
19 through 4.

20 Does CDTFA have any objections to admitting  
21 Appellant's exhibits?

22 MS. PALEY: No. Thank you.

23 JUDGE ALDRICH: Since there's no objections from  
24 either party, the exhibits are admitted.

25 ///

1           (Appellant's Exhibits 1-4 were received into  
2           evidence by the Administrative Law Judge.)

3           (Department's Exhibits A-H were received into  
4           evidence by the Administrative Law Judge.)

5           JUDGE ALDRICH: Okay. So as we discussed during  
6           the prehearing conference, the hearing will proceed as  
7           follows: For Appellant's opening presentation, including  
8           testimony, we allotted 120 minutes. Next CDTFA requested,  
9           and we received a combined opening and closing statement  
10          for approximately 30 minutes. I've also allotted some  
11          time for questions from the panel, and, finally, we will  
12          reserve 5 to 10 minutes for as closing or a rebuttal.

13          That being said, as was communicated to the  
14          parties, this is now the only hearing we have on the  
15          afternoon calendar, so we have some flexibility. If you  
16          need extra time, ask for it. And then, since this is on  
17          the longer side, I think it would behoove us to have a 5  
18          to 10-minute recess about midway through.

19          Do you have something to --

20          MR. O'CONNOR: I do, Your Honor, if -- if you  
21          don't mind. We do have some changes to the witnesses.  
22          There's only going to be the one witness, Mr. Derderian,  
23          who is here, and I don't anticipate it being a lengthy  
24          examination. So I would reduce our time. I think you had  
25          it at 120. I think the majority of the time will be oral

1 argument outside of 10 minutes of interviewing  
2 Mr. Derderian, and then some time for close.

3 JUDGE ALDRICH: Okay. With that being said, if  
4 we do reach the hour mark, I might go ahead and have that  
5 5 to 10-minute recess. I think everyone could probably  
6 use it at that point.

7 MR. O'CONNOR: Agreed.

8 JUDGE ALDRICH: All right. So with respect to  
9 witnesses, we have one witness today. Any objection to  
10 swearing in the witness now and --

11 MR. O'CONNOR: No, Your Honor.

12 JUDGE ALDRICH: Okay. If you could make sure  
13 that microphone is toggled on. All right. And please  
14 state your name.

15 MR. DERDERIAN: Vatche Derderian.

16

17 V. DERDERIAN,

18 produced as a witness, and having been first duly sworn by  
19 the Administrative Law Judge, was examined, and testified  
20 as follows:

21

22 JUDGE ALDRICH: Thank you, sir. And you will  
23 remain under oath until the conclusion of the hearing.

24 Let's see. So as discussed during the prehearing  
25 conference, Appellant's counsel may ask questions of the

1 witness, or the witness may testify in the form of a  
2 narrative. That being said, I want to ask that witness  
3 testimony be constructive or make a constructive use of  
4 time. That is, the testimony should be relevant to the  
5 issues, and extraneous information should be omitted.  
6 Both parties, including the witness, should understand  
7 that we've read the parties' briefs. We have the evidence  
8 available to us, and we're prepared for today, as I assume  
9 both parties are.

10 At this time, we're ready to move over to  
11 presentations. Are you prepared to -- would you like to  
12 begin with an opening or --

13 MR. O'CONNOR: My thought, Your Honor, was maybe  
14 we just do Mr. Derderian's testimony, and then from there  
15 I can switch to my -- my argument.

16 JUDGE ALDRICH: Okay.

17 MR. O'CONNOR: And that way we just kind of box  
18 them into two different items.

19 JUDGE ALDRICH: And since he is providing  
20 testimony, CDTFA will have an opportunity to ask questions  
21 as follow up; but I'm ready when you are.

22 MR. O'CONNOR: We're ready, Your Honor.

23 JUDGE ALDRICH: All right.

24 MR. O'CONNOR: Thank you.

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Q Mr. Derderian, do you operate the business known as Johnnie's Paint and Body Shop?

Q And were you involved in operating the business during the years 2008 to 2013?

Q During those years, did your business routinely generate estimates before performing repair work?

Q During those years, did your business routinely generate estimates before performing repair work?

Q And did every estimate result in completed repair work?

Q Are there common reasons why an estimate might never turn into a repair?

Q What are those reasons?

A A customer could be shopping around. Also, if an assignment is sent to us by an insurance carrier, we could go ahead and do the estimate and photos for the customer. And then the customer could decide not to bring in the

1 vehicle for multiple reasons.

2 Q Got it. So all these estimates that you take in,  
3 not all of them result in repairs; is that correct?

4 A Yes.

5 Q And as an affiliate of Fix Auto, during that  
6 time, were you required to submit completed repair  
7 invoices?

8 A No.

9 Q What about sales figures to the franchise or --

10 A No.

11 Q Do you recall, during that time, how your  
12 franchise fees were calculated?

13 A Yes.

14 Q And how were those calculated?

15 A It was a flat rate.

16 Q And were the franchise fees based on completed  
17 repairs?

18 A No.

19 Q Prior to this audit, had you every seen the  
20 spread shit or -- strike that.

21 Have you ever seen the spreadsheet that the CDTFA  
22 is relying on today?

23 A No.

24 Q During the audit, were you informed that the  
25 spreadsheet included estimates in none-completed work?

1           A    Yes.

2           Q    And during the years 2008 to 2013, did your  
3 business maintain ordinary invoices?

4           A    Yes.

5           Q    What about accounting records?

6           A    Yes.

7           Q    And those are for completed repairs?

8           A    Yes.

9           Q    Did you ever maintain more than one set of books?

10          A    No.

11          Q    Did you ever hide repair work?

12          A    No.

13          Q    Did you ever hide payments?

14          A    No.

15          Q    During those years, did you intend to evade  
16 paying sales tax?

17          A    No.

18          Q    Did you direct anybody else to evade paying sales  
19 tax?

20          A    No.

21          Q    Did you employee any software in an attempt to  
22 evade sales tax?

23          A    No.

24          Q    Based on what you knew at that time, did you  
25 believe your sales were being reported in good faith?

1           A    Yes.

2           MR. O'CONNOR:  No further questions, Your Honor.

3           JUDGE ALDRICH:  Thank you.

4           Ms. Paley, would it be all right if we follow up  
5 with questions after Appellant's argument?

6           MS. PALEY:  Yes.

7           JUDGE ALDRICH:  Okay.  All right.

8

9                                   PRESENTATION

10          MR. O'CONNOR:  Good afternoon, and thank you to  
11 the panel.

12          The power of taxing people and their property is  
13 essential to the very existence of government, but,  
14 nevertheless, the power must be applied with balance and  
15 fairness to the facts at hand.  This has not been the case  
16 here.  The CDTFA today seeks to rely on a fraud claim  
17 without any actual evidence of fraud.  Today we'll show  
18 that, not only is the majority of this liability barred by  
19 the statute of limitations, the 25 percent fraud penalty  
20 was inappropriately applied and incorrectly placed on the  
21 taxpayer.  Also, the 40 percent penalty was also  
22 misapplied.

23          The Respondent opened the business in 2006,  
24 eventually becoming an affiliate of Fix Auto in  
25 approximately 2008.  Roughly in 2014, as part of being an



1     affiliate of Fix Auto, the taxpayer was required to  
2     implement a system called CCC. This is a program that  
3     tracks estimates, invoices. It's basically an operating  
4     system for repair shops. Folks come in, estimates come  
5     in; they're reported in CCC. It's designed to streamline  
6     the shop operations, including repair status, part  
7     ordering. The franchisees have no authority to change  
8     this system, to enter this system, to -- to create  
9     calculations. All the franchisee may do is input an  
10    estimated repair.

11           On/or about November 16, 2016, the taxpayer was  
12    notified that there would be a routine audit. The  
13    taxpayer provided the required books and records. There  
14    were some questions around whether or not 2014 there was a  
15    failure to remit a portion of the tax collected.  
16    Nevertheless, the CDTFA requested the taxpayer provide  
17    electronic sales data from 2014. Three days later,  
18    through their representative, the taxpayer provided that  
19    very data. That data showed that there was a \$72,000 tax  
20    liability due and owing for the year of 2014, and that the  
21    taxpayer had only remitted \$30,000 of that.

22           I want to make sure that we talk about something  
23    that seems to keep getting lost here in this process. The  
24    taxpayer passed audit in 2015 and 2016. There was no  
25    issue with the taxpayer's reporting in Q1 of 2014. Just

1       so we're clear, that's over two-thirds and, by my math,  
2       roughly 75 percent compliance.

3               At all times, the employees responsible for  
4       reporting sales tax were required to take the numbers that  
5       were generated by the CCC report and use those to populate  
6       the sales and use tax returns to file the sales and use  
7       tax returns. Notwithstanding those instructions, there  
8       was an employee that failed to remit the returns in three  
9       quarters in 2014. It was later discovered this was the  
10      same employee that failed to remit other bills related to  
11      accounts payable. The failure to remit those payments  
12      through the accounts payable portion resulted in that  
13      employee's termination. It wasn't until this audit that  
14      we discovered that there was an issue with the reporting  
15      in 2014.

16             On/or around March 8th of 2019, shortly before  
17      the expiration of the statute of limitations, the CDTFA  
18      auditor reached out to Mr. Chris Duran, who is an  
19      executive at Fix Auto U.S.A., the franchisor, requesting  
20      sales data. Mr. Duran was very clear in response. The  
21      franchisor does not collect sales tax data. He told her  
22      that. She refused to listen and required that he send  
23      information, or she would serve him with a subpoena. I  
24      would note that this is done before any finding of fraud.  
25      We've expanded the statute of limitations here with the

1 auditor asking for information from the period spanning  
2 2008 to 2014 without a fraud memo, without an actual  
3 finding of fraud.

4 As I said, Mr. Duran responded that they didn't  
5 track the sales data, and eventually he did send  
6 something. And, again, I would note to the panel the  
7 franchise agreement, at the time, did not require the  
8 taxpayer to report his sales to the franchisor. All that  
9 the franchisor had -- and when you go and you look at this  
10 agreement that's attached as one of our exhibits -- they  
11 had the authority to go into the system and look at  
12 information. That's the only access they had. They  
13 didn't require the taxpayer to tell him what percentage of  
14 your estimates resulted in -- in completed customers.  
15 There's none of that.

16 He played -- he paid a fixed fee during this  
17 time. And moreover, as I mentioned, this is not similar  
18 to other cases where you have an employee that's saying  
19 this is the amount of money we generate in a given week.  
20 Mr. Duran has no inside knowledge as to what goes on at  
21 Fixed Auto Pasadena. He has no inside knowledge on the  
22 sales. He has no idea what actually goes on, the  
23 breakdown between the different income items.

24 Then on September 30th, of 2019, the CDTFA then  
25 goes ahead and issues this fraud memo. The fraud memo, if

1     you look at it, it's flimsy at best. It basis the entire  
2     opening of the statute of limitations on the 40 percent  
3     penalty for the period of Q2 2014 through Q4 of 2014.  
4     That's three quarters. There's no allegation of any  
5     wrongdoing in the memorandum itself. I'll talk more about  
6     the memorandum as we -- we that there. But again, 2019  
7     issued -- in October 22nd, 2019, the CDTFA issued its  
8     verified audited amounts, and again, the taxpayer passed  
9     audit on 2015 and 2016. The CDTFA took it upon themselves  
10    to go back and create a fictitious calculation to assess  
11    sales tax.

12           Now, really, what our argument comes down to in  
13    the first portion is the CDTFA does not have the authority  
14    to open up the statute of limitations without a finding of  
15    fraud. Section 6487(a) provides that, except in cases of  
16    fraud or intent to evade, all Notices of Decision must be  
17    mailed in three years. The three-year limitation is  
18    tolled if there's clear and convincing evidence of fraud  
19    or intent to evade for each quarter during the Notice of  
20    Decision period. That didn't happen in this case.  
21    There's quarters where the CDTFA found that the taxpayer  
22    was completely compliant.

23           Moreover, federal courts have concluded that the  
24    mere omission of reportable income is not by itself  
25    sufficient to warrant a finding of fraud, but repeated

1 understatement in successive years, coupled with other  
2 circumstances showing intent to conceal or misstate  
3 taxable income. Again, we would first pause at this  
4 language from Madfish establishes that without successive  
5 years of underpayment within the Notice of Decision  
6 period, there can be no fraud, unless by the clear  
7 language of the case law. It says there has to be  
8 successive years of fraud.

9           They can't blow open the statute of limitations  
10 and go all the way back to 2008 and say there has to be  
11 successive years of fraud. This is meant to show -- and  
12 if you convert this into a mathematical formula, you're  
13 basically telling the taxpayer, if you report one out of  
14 three, that's no good. That's 30 percent. I get that.  
15 But the taxpayer, if they report properly for two out of  
16 three years, that's not indicative of fraud. So we would  
17 first posit that you can't even open the statute of  
18 limitation because there's no consecutive years of fraud  
19 as required by Madfish. And the mere omission of income  
20 is not sufficient. It's got to be repeated. That's not  
21 here.

22           So even if the panel were to find that there were  
23 successive years of understated income, there still has to  
24 be a fraud portion of this. And I understand that actual  
25 fraud is -- is hard to find and hard to prove. That's

1     been the panel's job for years here, but, at the same  
2     time, fraud is odious. It smells. It's tangible. You  
3     could see it. There's circumstantial evidence of fraud.

4             The courts have already stated you can find it  
5     with understated income, inadequate records, implausible  
6     inconsistent behavior, concealed assets, failure to  
7     cooperate, lack of credibility. They don't even allege  
8     that here. There's no allegation of actual fraud  
9     committed by the taxpayer, other than he underreported.  
10    For all we know, that could be a problem with the system  
11    that -- that they used to report sales and use tax.

12            So, again, I'll go back to that memo that we  
13    talked about where they base fraud on these three quarters  
14    of collected but unreported taxable sales. First, I --  
15    let's be very clear about something. That 40 percent  
16    penalty, there's no fraud required to be liable for that  
17    penalty. That's not one of the elements. It's simply  
18    whether or not the tax was collected and whether or not it  
19    was remitted to -- to the government. Nothing in there  
20    establishes fraud. Even if that was the case, they would  
21    still have to go and prove fraud in some way, shape, or  
22    form. They haven't done that.

23            And if we forget the timing of the memo, the  
24    timing looks like it's meant to provide -- to preserve  
25    their case, and that they rushed to judgement and are

1 forcing a square peg into a round hole. I'm not saying  
2 that these folks have to ignore this data that they have  
3 from outside the -- the statute of limitation period, but  
4 they don't get to go and start fishing for no reason.  
5 They went out, went around the taxpayer trying to get data  
6 outside of statute of limitation period without any  
7 evidence of fraud. They can't do that.

8 It's not like they had an employee come to them  
9 and say, hey, this is what I see where they ran an  
10 interview and -- and were able to find somebody on the  
11 ground that was reporting something. They went out and  
12 intentionally tried to get around the statute of  
13 limitations. Moreover, they then used this spreadsheet to  
14 bolster -- or at least attempt to bolster their argument  
15 of fraud. There's -- again, the underreporting by itself  
16 isn't fraud. They need to point to something else in that  
17 time period. Even if they have that spreadsheet, it's --  
18 the duty is incumbent on them to go and find other  
19 evidence of fraud. That's not enough. The previous  
20 decisions have all said that's not enough. It's  
21 understatements in successive years plus something else.  
22 And in here, there's no understatement in successive  
23 years, and there's no plus anything else.

24 There's no direct evidence of fraud. There's not  
25 even circumstantial evidence of fraud. The amount of

1 underreporting is insignificant. It's one -- or it's 3  
2 quarters out of a 12-quarter period. As I said earlier,  
3 that's a 75 percent accuracy rate for the taxpayer.  
4 Seventy-five percent. That's better than more likely than  
5 not. Extremely better more likely than not. There's been  
6 no criminal charges against my client. There's never been  
7 the inkling of criminal charges against my client. I get  
8 it. A lot of time, fraud is easy because there's a  
9 criminal aspect here. Here there's no criminal aspect.  
10 There's never even been a hint of it. There's never been  
11 these concealed books and records.

12 Oftentimes, fraud is found when there's a second  
13 book of records. There's handwritten notes. That's not  
14 the case here. If anything, our guy, the proof is he  
15 turned over records that show he underreported. If I'm  
16 trying to commit fraud, why would I turn over records that  
17 show that I've underreported. It may -- it's nonsensical.  
18 And again, I would urge the service that this -- this  
19 whole time they've never even tried to explain why this  
20 taxpayer would be non-compliant in three quarters of 2014,  
21 and just decide one day, hey, I'm going to comply. It's  
22 unlike any other case that this panel has seen because he  
23 did comply. He did pass audit in '15 and '16.

24 Again, go back to 2008 to 2013 in that period.  
25 There's nothing other than the understatement that is



1 showing fraud. They need more than that. And, again, the  
2 spreadsheet they -- the reliance provided by a  
3 non-employee based on numbers that they're not required to  
4 report. It's not like this was a franchisor requiring  
5 that they report daily, weekly, monthly sales figures.  
6 The franchisor didn't care what their sales numbers were.  
7 They get paid regardless. It's a flat fee. It doesn't  
8 matter. They had access to look and see the data. This  
9 was a new program. We know that the program works because  
10 three quarters later in '15 and '16, that same program  
11 where they went and pulled the same data from the same  
12 spreadsheets passed audit.

13 I'll turn to the 40 percent penalty because I  
14 think that the taxpayer itself admitted that in Q2 2014  
15 through Q4 of 2014 there was an issue with the data. But  
16 what the CDTFA fails to -- to really talk about is the  
17 fact that in Q1 of 2014 that -- that same issue resulted  
18 in the taxpayer overpaying sales tax in Q1 of 2014. So  
19 they can't have it both ways where they say, hey, this  
20 program screwed up, and you didn't remit enough tax, but,  
21 at the same time, completely ignore the -- the Q1 of '14  
22 where the program screwed and my client remitted too much  
23 tax.

24 So the CDTFA -- and I'll talk about this more  
25 when we get into the -- the calculation. The CDTFA seems

1 to cherry-pick which information it wants to use and which  
2 information it wants to ignore. But as I said, the  
3 taxpayer isn't saying they didn't underreport. His own  
4 records say he underreported in -- in Q2 through Q4. The  
5 issue is, was that reasonable? Okay. Was it reasonable?  
6 Is it excusable? Because the 40 percent penalty is  
7 excusable for reasonable cause. At all times, the  
8 taxpayer relied on an employee who filled out and filed  
9 the sales and use tax returns. He filed for every year.  
10 There's no evidence of any negligence by the employee. If  
11 anything, my client was more than reasonable in hiring  
12 specifically for sales tax.

13 Moreover, California courts have interpreted that  
14 reasonable cause in a tax penalty case requires that the  
15 failure to remit occurred despite the exercise of ordinary  
16 care and the absence of willful neglect. There's no  
17 evidence of willful neglect here. There's none. If  
18 anything, as soon as he found an issue with the employee,  
19 the employee was terminated. That's been his story all  
20 along. There was an issue with this new program, and  
21 there was an issue with this employee. That hasn't  
22 changed. My client has been at this now for a decade.  
23 The story has remained the same for the last decade. The  
24 problem employee was terminated and, clearly, the CCC  
25 program now works well.

1           So turning to the last point or the last issue  
2     before the court, the calculation; and I'll touch on this  
3     briefly. We would posit that this calculation is  
4     arbitrary and inconsistent with audit methodology. They  
5     alternated among different indirect methods using bank  
6     account -- bank deposits, federal income tax returns,  
7     gross receipts without any kind of record-based  
8     justification. They always selected the higher yielding  
9     method. As I state earlier, nothing was ever decided in  
10    favor of the taxpayer. Oftentimes '15 and '16 were  
11    excluded from calculations because those amounts would  
12    have helped the taxpayer's percentage numbers.

13           The OTA has already rejected such higher up  
14    switching as arbitrary and racking national base --  
15    rational bases. The CDTFA also used a blended or mixed  
16    markup projection across comparable periods. They fail to  
17    establish inadequacy of records before resorting to these  
18    estimation. It's pretty clear that they had good books  
19    and records. They passed -- my client passed audit in '15  
20    and '16. They weren't asked to provide additional records  
21    in '15 or '16. The records were fine. Asked to provide  
22    additional records in '14; provided in three days.

23           So as soon as the CDTFA found numbers it didn't  
24    like, it resorted to making up imaginary numbers. It's  
25    not what they get to do here. There's no overstatement

1 from treating nontaxable items as taxable. There's no  
2 regard for the bifurcation of different tax treatments of  
3 different items. They failed to credit the taxpayer for  
4 purchases that were -- or for resale items. They double  
5 counted data and other items combining bank deposits and  
6 sales ledgers. They misapplied markups across the board  
7 and projected sample errors inappropriately.

8 Finally, this whole calculation seems to be  
9 penalty driven in its bias. The methodology layers  
10 negligence and fraud penalties on top of an inflated -- an  
11 inflated base that's derived from arbitrary, higher of  
12 method, and contravenes the requirement that the  
13 Department seek the most accurate measure. Here, it seems  
14 that the department was looking for the highest measure  
15 possible, not the most accurate. They saw a crack in the  
16 door and tried to bust through it.

17 And to close, I would just remind the panel, the  
18 only thing that's shown is an under remittance in 2014  
19 caused by a faulty error -- a faulty system and an  
20 incompetent employee. I've already told you, at least  
21 three times today, that the taxpayer passed audit in 2015  
22 and 2016. If you look at this fraud memo, they don't say  
23 that. They -- they don't even recognize the fact that --  
24 that he passed audit two out of three years. Technically  
25 more than that because of the Q1 of 2014, 75 percent.

1       Seventy-five percent.

2               So my question -- well, I apologize because I  
3       shouldn't posing questions to the other side -- but what's  
4       enough? Three out of four transactions are properly  
5       reported, and that's not enough for the CDTFA? They're  
6       looking for perfection, and that's impossible. The 40  
7       percent penalty was used to open the statute of limitation  
8       without an actual showing of fraud. So, again, I would  
9       bring the panel back to our original threshold argument.  
10      There needs to be consecutive years of underreporting.  
11      Our position is that needs to happen within the NOD time  
12      frame. That's that three-year initial audit period.  
13      There needs to be back-to-back or consecutive years. Then  
14      you can go and look into the fraud finding. But at some  
15      point, you have to give the taxpayer the benefit of the  
16      doubt, and it makes sense. That makes sense because  
17      you're going from a one-third reporting accuracy to a  
18      two-thirds. More likely than not that they reported  
19      correctly, versus there's no way they reported correctly  
20      because one out of three is correct.

21              Finally, they use this sheet from -- from 2014 to  
22      2008 [sic]. Other cases it found that this data from  
23      outside sources can be used by the CDTFA. And I think  
24      that our case is different than every other case that  
25      they've allowed that. Every other case, that information

1 is provided by an employee, is provided by a franchisor  
2 that's interested in the sales that are going on. We have  
3 none of that here. If anything, this is a highly inflated  
4 number, and there was no -- no need to even get there.  
5 There's no inkling of fraud at this -- in this case  
6 whatsoever.

7 And so with that, we would posit that the statute  
8 of limitations has closed the period of 2008 to 2014  
9 because the CDTFA has failed to establish any fraud. The  
10 25 percent penalty is null and void because they failed to  
11 establish any kind of fraud. The 40 percent penalty is  
12 justified, given the reasonable cause, and should be  
13 stricken. And then in the alternative, the methodology  
14 used here was just completely and utterly inappropriate.

15 And with that, I'll close.

16 JUDGE ALDRICH: Thank you. I do have a couple of  
17 questions, but first I'm going to refer to my panel  
18 members.

19 Judge Wong, did you have any questions for  
20 Appellant?

21 JUDGE WONG: Yeah, just maybe one or two  
22 questions specifically for the witness, Mr. Derderian.

23 Could you back into a little bit of your  
24 background. You've been involved in other paint and body  
25 shops; is that correct?

1           MR. DERDERIAN: I've worked at before my time at  
2       Fix Auto. So I'm second generation of Johnnie's Paint and  
3       Body Shop. It was my father's company before, but I  
4       did -- I have worked at other facilities, body shops.

5           JUDGE WONG: Okay. And then so Johnnie's Paint  
6       and Body Shop, it's been in existence. You said it was  
7       second generation. So it was your father's shop or  
8       something?

9           MR. DERDERIAN: Correct.

10          JUDGE WONG: And that he operated as a sole  
11       proprietorship, or is it a corporation?

12          MR. DERDERIAN: It was a corporation.

13          JUDGE WONG: Okay.

14          MR. DERDERIAN: It was before then. They had  
15       Derderian Brothers Corporation. It was a C corp. And  
16       Johnnie's Paint and Body Shop was underneath that  
17       corporation. And that was, I believe, part of that. If  
18       it's an S corp or C corp, I don't know.

19          JUDGE WONG: Okay. And when did you become  
20       involved with Johnnie's Paint and Body Shop?

21          MR. DERDERIAN: I took it over in 2006.

22          JUDGE WONG: 2006. Okay. And you are the CEO or  
23       CFO or do you have several hats?

24          MR. DERDERIAN: The owner, yeah. CEO.

25          JUDGE WONG: Okay. And so the other question I

1 had was involving the employee that your counsel had  
2 mentioned. So they were misreporting and not remitting  
3 the proper amount of tax to the state; is that correct?

4 MR. O'CONNOR: Our position is that they were  
5 required to take the spreadsheet printout out from CCC.  
6 And for some reason, she decided after Q1 of 2014 that she  
7 wasn't going to do that anymore. So she stopped remitting  
8 the sales tax, but they found out that she was a problem  
9 employee from her failure to remit payments under the  
10 account payable umbrella. So she -- she had -- her one  
11 silo was sales and use tax reporting. Her other silo was  
12 accounts payable.

13 Taxpayer gets in a bunch of notices from various  
14 customers -- or I should say service providers, hey, our  
15 bill hasn't been paid. Our bill hasn't been paid. They  
16 turn around to the employee, why haven't you paid the  
17 bill? Oh, I didn't know. I'm not -- I didn't know I had  
18 to do that. Blah, blah, blah. Terminated because she  
19 wasn't following her duties. But we wouldn't have found  
20 out about that sales and use tax issue without the audit  
21 because everything was filed by then. She wasn't  
22 terminated, I think, until 20 -- like towards 2015.

23 JUDGE WONG: Okay. And you had mentioned that it  
24 was because of incompetence. It wasn't -- was she  
25 stealing or --



1           MR. O'CONNOR: No. It was incompetence. It  
2 was -- the real issue was the failure to pay bills on  
3 time. You can't do that as business. And usually, you're  
4 going to terminate somebody rather quickly if their  
5 responsibility is paying bills, and the bills aren't paid.

6           JUDGE WONG: Okay. And, Mr. Derderian, is that a  
7 correct --

8           MR. O'CONNOR: That's correct.

9           JUDGE WONG: Okay. And then the last question I  
10 had was about -- so once you discovered what was going on  
11 with this employee -- and I think your counsel had  
12 mentioned before, but did you pay back the remittance that  
13 had been collected to the state or --

14          MR. O'CONNOR: I think this is where there's,  
15 like, some -- it's interesting to me on the record because  
16 there's a portion here where I think that we had tried and  
17 attempted to pay back that differential, and I'm not sure  
18 what happened. I don't think we were really given the  
19 opportunity to make that payment to treat as an  
20 understatement and move on.

21           Is that the -- the question you're asking?

22          JUDGE WONG: So okay. Yes. But that brings up  
23 another question. You said you weren't allowed the  
24 opportunity. Like, what is that?

25          MR. O'CONNOR: I think there was some early

1 discussions. And this is just from me reading the record  
2 early on that there was something discussed back when the  
3 audit first started about filing something for 2014. And  
4 then after that, there was a turn, and that's when  
5 actually Mrs. Derderian was brought into an auditor's  
6 office and threatened that, we're gonna -- you guys are  
7 doing something wrong. We're going to get you. And that  
8 kind of shut everything down and kind of changed the  
9 cadence of the audit from something where we had been  
10 providing books and records and this is fairly  
11 non-adversarial, here's what you need, to they just  
12 threatened the taxpayer's wife. Maybe it's time to take a  
13 step back, and maybe it's not as cordial as we think it  
14 is. And I think that kind of broke down right at that  
15 time. And if you look back at some of the records,  
16 you'll -- you'll see that.

17 JUDGE WONG: Okay. Thank you. That's all the  
18 questions I had at this time.

19 JUDGE ALDRICH: Judge Kim?

20 JUDGE KIM: Hi. Yeah. I actually had a question  
21 about the information that the franchisor had access to.  
22 Did something change in 2015 and 2016 with regards to  
23 those records?

24 MR. O'CONNOR: I think it was twofold. I think  
25 that you have one, you've got a system that's been up and

1 running for a year; and I think the system got a little  
2 bit better. And I think the other issue or the other kind  
3 of reason for the change was that there was a new sales  
4 and use tax person that was brought in that may or may not  
5 have been a little more -- well, I shouldn't say that.  
6 She was definitely more savvy with the industry. So  
7 whether or not that changed anything, but I would tell you  
8 that when I did speak with Ms. Granden who was the sales  
9 and use tax preparer for '15 and '16.

10 She prepared sales and use tax returns the same  
11 way. Take that CCC report -- and she did say that she  
12 made some minor adjustments to it, and away it went. But  
13 she uses the same thing, that CCC report. So the main  
14 change was maybe a sharper eye from a better accountant.  
15 But really, the better change is that CCC report is there.  
16 And I you can see it too if you go back and look at the  
17 CDTFA's exhibits. That 15 and 16 is where -- what they  
18 used to prepare the sales and use tax reports in 15 and  
19 16.

20 JUDGE KIM: So the CCC reports, that started  
21 in -- when did that start?

22 MR. O'CONNOR: In '14.

23 JUDGE KIM: In '14. And when that started, that  
24 didn't include the estimates that were not eventual --  
25 actual sales or --

1           MR. O'CONNOR: Well, let's back up a second.  
2           Just I think it may be helpful to talk about how the CCC  
3           program works. So what happens is car comes in or damage  
4           comes in or someone comes into the auto shop. The  
5           appraiser comes -- there's a guy with like a tablet,  
6           pushes some buttons and says, okay. Hey, this is what we  
7           think it is, right. That goes out into the ether. It  
8           goes into the CCC program. That's what they have access  
9           to is that estimate.

10           Later on the back end, there's a spit out because  
11           you've got to do some reconciliation as Mr. Derderian  
12           testified to earlier. That's just an estimate. The  
13           estimate doesn't include the folks that never come back,  
14           or that doesn't even take into account the folks that, hey  
15           we looked at, right. We saw the damage to the door, but  
16           now that we've opened it up and taken the door off,  
17           there's not this other underlying issue. So the estimate  
18           has change. And I think that's part of the issue with  
19           that 2014, is that they've got these inflated numbers from  
20           the estimates where the CCC program runs these iterations.  
21           And it's in the -- the exhibits.

22           You'll see the length of the data that's been  
23           provided and all these -- I -- I think I did the count a  
24           while ago. It's like 8,400 line items. And you can kind  
25           of see the data line by line. So there's -- it's a lot,

1 but there's a reconciliation that goes on. And if you  
2 look across, there's a sales tax calculation. They take  
3 out -- and it's got a system that apportions between  
4 taxable and nontaxable sales. So it's a pretty  
5 sophisticated system, but it seems like there were some  
6 issues getting it off the ground in 2014.

7 Like I said, that same system that they used,  
8 they over reported in Q1 of '14. So they actually  
9 overpaid based on those numbers. And then in Q2, Q3, and  
10 Q4, they underpaid, and then in '15 and '16 they're fine.  
11 So, if anything else, that looks to me like there's an  
12 issue with the system, and then the system worked itself  
13 out.

14 JUDGE KIM: Okay. Thank you.

15 JUDGE ALDRICH: Okay. I had a couple of  
16 questions. So going back to that -- so prior to 2008,  
17 Johnnie's Body was not part of the Fix Auto?

18 MR. O'CONNOR: That's correct.

19 JUDGE ALDRICH: Okay. And, at some point, either  
20 they approach you or you approach them and enter into some  
21 sort to franchisor and franchisee relationship?

22 MR. DERDERIAN: I approached them in 2007. And  
23 then they vet you out of where -- if you're an upstanding  
24 facility, if you have a management system, if you have  
25 certifications, you know, of a good standing facility.

1       2008 we were -- it was considered a network. It wasn't  
2       even a franchise at that time.

3               JUDGE ALDRICH: I see. And so you -- I guess I'm  
4       wondering, like, you're paying a flat monthly fee or a  
5       flat fee to be a part of the Fix Auto. What do you --  
6       what were you hoping to get in exchange? Was that, like,  
7       the goodwill of Fix Auto? Was that, like, the CCC  
8       program?

9               MR. DERDERIAN: So the collision business is  
10       becoming a -- like, it's a consolidated, right. So  
11       there's insurance carriers that minimize their cost. As  
12       an independent owner you are basically more of a cost to  
13       an insurance company comparison to a -- like, an MSO, a  
14       multi-shop owner or regional owner, because they have a  
15       single point of contact. And there's -- in the Fix Auto  
16       network, you get to see -- as I put it in a conference  
17       when I was on a panel, we said that before Fix Auto, you  
18       have to go look at the encyclopedia to get your  
19       information.

20               With Fix Auto, it was more of an ability to have  
21       the internet of information of getting better how you  
22       operate because of you would have your peers that you  
23       would work with. And then also having the ability of the  
24       support to have, like, national accounts where insurance  
25       carriers would refer work to you.

1 JUDGE ALDRICH: So more likely to get referrals  
2 from, like, insurance carriers and being able to better  
3 price, like, a new bumper or whatever?

4 MR. DERDERIAN: Yes.

5 JUDGE ALDRICH: Okay. And so the -- the data  
6 that was received by CDTFA from the franchisor, the  
7 arguments have made that that's estimates. How many  
8 estimates were made in the process? Was it just the  
9 initial estimate? Is it -- is the estimate then updated?  
10 Like, I believe counsel was indicating that, like,  
11 sometimes when you open it up there's more work to do.  
12 Like, if you don't see a bit frame, for example, that  
13 might be more costly.

14 MR. DERDERIAN: The difference between estimates  
15 and repair orders; so estimate -- or it could be of where,  
16 Judge, you decided to come into our facility and learn how  
17 to write, and we could write an estimate -- 10 estimates  
18 on the same car. It could be of where a customer comes in  
19 and wants a cost of finding out if they want to go through  
20 an insurance, or if they want to pay for it themselves.  
21 So there could be thousands of estimates. There could be  
22 500. It depends on facility of how much foot traffic they  
23 get. Comparison to a repair authorization, that is a  
24 contract between the repair facility and the customer.  
25 That's your sale.

1 JUDGE ALDRICH: And so the CCC program, did it  
2 record the repair authorizations and the estimates, just  
3 the estimates?

4 MR. DERDERIAN: It record -- it records all of  
5 it. That's -- that information that the CDTFA got was  
6 everything that we had in our management system.

7 JUDGE ALDRICH: And then prior to the CCC, did  
8 you have a system in place for recording the estimates  
9 versus the repair authorization?

10 MR. DERDERIAN: Yes. And that system no longer  
11 exist. It's called "Summit." It's a management system  
12 that was there. But in that process, CCC was a -- like,  
13 there's Mitchell and ADP and CCC. Those are estimate  
14 systems.

15 JUDGE ALDRICH: Okay. All right. I think that  
16 answers all of my questions.

17 We'll move along to CDTFA, I think.

18 MS. PALEY: Would it possible to take a restroom  
19 break prior to my beginning?

20 JUDGE ALDRICH: Yeah. I think that's a good  
21 transition point.

22 We're going to go off the record, and we'll meet  
23 back in 10 minutes.

24 (There is a pause in the proceedings.)

25 JUDGE ALDRICH: Okay. We're going to go back on



1 the record and, at this time, hand it over to the CDTFA  
2 for their combined opening and closing.

3 MS. PALEY: Thank you.

4  
5 PRESENTATION

6 MS. PALEY: Johnnie's Paint and Body Shop  
7 Incorporated operates an auto body repair and paint shop  
8 doing business as Fix Auto Pasadena, a franchise of Fix  
9 Auto USA. The corporation was registered in 2004. During  
10 the audit, which began in 2016 as shown in the assignment  
11 activity histories, Exhibit G, binder page 230, the  
12 Department found unreported taxable sales by comparing  
13 sales data and franchisor reports. The Department  
14 established unreported taxable sales of \$4.9 million for  
15 the liability period 2008 through 2014 as shown in the  
16 audit work papers, Exhibit H, binder page 236.  
17 Specifically, the audit revealed \$4.2 million in first  
18 quarter 2008 through first quarter 2014, Audit Item 1, and  
19 additional unreported taxable sales of \$735,000 for second  
20 quarter 2014 through fourth quarter of '14 based on  
21 comparison of reported to reported taxable sales, Audit  
22 Item 2.

23 On November 21st, 2019, the Notice of  
24 Determination, Exhibit E, was issued for approximately  
25 \$491,000 in tax, plus interest, a 40 percent penalty of

1 approximately \$16,000 for second quarter 2014 through  
2 fourth quarter 2014, and the 25 percent fraud penalty of  
3 approximately \$112,000 for first quarter 2008 through  
4 first quarter 2014. As held in the precedential opinions  
5 of the Appeals of AJ Berry Corporation, 2024, Landeros,  
6 2024, Senehi, 2023, and ISIF Madfish, 2019, imposition of  
7 the 40 percent penalty, under Revenue & Taxation Code  
8 section 6597(a), provides that an person who knowingly  
9 collects sale tax reimbursement and fails to timely remit  
10 it to the state is liable for a penalty of 40 percent of  
11 the amount not timely remitted, if the failure to remit  
12 exceeds certain thresholds. In this case, over \$1,000 a  
13 month and more than 5 percent of the tax due, an  
14 imposition of the 25 percent fraud penalty per Revenue &  
15 Taxation Code 6485 applies if any part of the deficiency  
16 for which the deficiency determination is made is due to  
17 fraud or an intent to evade the sales and use tax law or  
18 rules and regulations.

19 Fraud, as held by Bradford versus Commissioner in  
20 1986, is intentional wrongdoing on the part of the  
21 taxpayer with the specific intent to avoid a tax known to  
22 be owing. Fraud must be established by clear and  
23 convincing evidence. Fraud may not be presumed, but it's  
24 rare to find direct evidence that a fraud has occurred.  
25 And so it's often necessary to make the determination

1 based on circumstantial evidence. As cited in the  
2 aforementioned Appeal of ISIF Madfish Incorporated, badges  
3 of fraud may include understatement of income, inadequate  
4 records, failure to file tax returns, implausible or  
5 inconsistent explanations of behavior, concealment of  
6 assets, failure to cooperate with tax authorities, lack of  
7 credibility in the taxpayer's testimony, falsified  
8 records, a substantial discrepancy between recorded and  
9 reported amounts that cannot be explained, and tax or tax  
10 reimbursement properly charged evidencing knowledge of the  
11 requirements of the law but not reported.

12 As stated in Madfish, a finding that any part of  
13 a deficiency determination was due to fraud is sufficient  
14 to suspend the statute of limitations to issue a  
15 deficiency determination as to the entire reporting period  
16 in which any part of the deficiency was due to fraud,  
17 Madfish, page 9. Revenue & Taxation Code section 6485  
18 imposes the 25 percent penalty if any part of a deficiency  
19 determination was due to fraud or intent to evade the law  
20 or authorize rules or regulation.

21 The evidence before us establishes that Appellant  
22 knowingly and consistently understated their taxable sales  
23 and kept for their own use over \$491,000 in sales tax  
24 reimbursement that they collected. The 25 percent fraud  
25 penalty was applied based on a multitude of factors,

1 including but not limited to a significant total  
2 unreported taxable measure for the liability period of  
3 approximately \$5 million; a substantial overall  
4 underreporting error of 209 percent, a scope indicating  
5 intentional evasion; Appellant's sales data and CCC  
6 workflow data, A-5, page 145 of the binder, demonstrates  
7 that tax was properly charged but not properly reported  
8 indicating knowledge of the requirement to accurately  
9 report sales and remit the tax reimbursement collected  
10 despite keeping the money.

11 Both the sales data records and the franchisor  
12 reports show material discrepancies to Appellant's  
13 reported sales demonstrating that the data was available  
14 to them from multiple sources and yet, chose to  
15 underreport. There's also Appellant's decades of  
16 experience with sales and use tax and prior business  
17 experience. As noted in the decision, Mr. Derderian  
18 maintained an active seller's permit for two other  
19 businesses, Derderian Brothers and Direct Auto Repair,  
20 during liability period and another, RCC Goodies prior to  
21 the liability period. The evidence is clear on the  
22 showing of fraud.

23 Additionally, as elaborated in the penalty  
24 memorandum, Exhibit C, page 198, and specifically, the  
25 chart on hearing binder page 200, the 40 percent penalty

1 was applied to the \$40,093 of unremitted sales tax  
2 reimbursement that was collected for second quarter 2014  
3 through fourth quarter '14 since the amount average more  
4 than \$1,000 a month, specifically \$4,455, and exceeded 5  
5 percent of the reported sales tax reimbursement, 191  
6 percent. Again, that was based on the sales data that was  
7 provided on audit.

8 Appellant argues that the determination is  
9 incorrect, claiming that the records relied on are  
10 unreliable and erroneous, and that the determination is  
11 barred by the three-year statute of limitations. But  
12 there is no statute of limitations when the underreporting  
13 is a result of fraud or intent to evade the payment of tax  
14 per Revenue & Taxation Code 6487(b). Here, the Department  
15 obtained Appellant's franchisor reports for first quarter  
16 2008 through fourth quarter 2013, which provided sales  
17 information that revealed substantial discrepancies.  
18 Moreover, for first quarter 2014 through fourth  
19 quarter '14, the Department established unreported taxable  
20 sales of over \$988,000 for that one year alone. The  
21 Department has met its burden of clear and convincing  
22 evidence for proof of fraud.

23 Forty percent penalties may be relieved, pursuant  
24 to Revenue & Taxation Code 6597 subdivision (a)(2)(B), if  
25 the failure to make a timely remittance of sales tax

1 reimbursement is due to reasonable cause or circumstances  
2 beyond the person's control, and occurred regardless of  
3 the person's exercise of ordinary care, and in the absence  
4 of willful neglect. Revenue & Taxation Code section 6597  
5 subdivisions B(1)(a) through (f) enumerates six examples  
6 of reasonable cause or circumstances beyond the person's  
7 control, none of which apply here.

8           There is no evidence of a credible explanation  
9 for Appellant's failure to comply with the sales and use  
10 tax reporting requirements and report the tax reimbursed  
11 it had collected from its customers. There's no showing  
12 of reasonable cause or circumstances beyond their control.  
13 Even if Appellant had sufficiently supported the claim of  
14 a rogue employee, that doesn't overcome the imputation of  
15 the principle. Also, based on the evidentiary record and  
16 the law, there are no adjustments warranted to the taxable  
17 measure established by the audit. The Department's  
18 determinations are reasonable and rational and thus,  
19 Appellant must establish that the circumstances it asserts  
20 are more likely than not to be correct. Unsupported  
21 assertions are not sufficient.

22           Appellant has not put forth any verifiable  
23 contrary information to show that the deficiency measures  
24 are incorrect. The franchisor reports are reliable and  
25 were found consistent with the records that were provided

1 by Appellant. That is, the franchisor report total sales  
2 largely match the gross receipts reported on Appellant's  
3 provided federal income tax returns for 2011 through 2016,  
4 but not with reported sales.

5 We submit to the panel that fraud has been  
6 demonstrated by clear and convincing evidence and that no  
7 adjustments are warranted, and that both the 25 and  
8 40 percent penalties should be upheld.

9 Thank you.

10 JUDGE ALDRICH: Thank you.

11 With respect to the 40 percent penalty,  
12 6597(b)(1), that list isn't intended to be exhaustive; is  
13 it?

14 MS. PALEY: Correct.

15 JUDGE ALDRICH: Okay. Or that's not the  
16 Department's position?

17 MS. PALEY: Correct.

18 JUDGE ALDRICH: Okay. Okay. And then with  
19 respect to inadequacy of the records provided, in what  
20 ways were the records inadequate? If there are different  
21 periods, could you specify?

22 MS. PALEY: Yes. And if I may refer to  
23 Mr. Parker for that portion, please.

24 MR. PARKER: So if you look at the sales data  
25 that they provided for 2014, the -- the amounts that they

1       had recorded in their system --

2               JUDGE ALDRICH: Are you looking at a particular  
3 point in the exhibit binder?

4               MR. PARKER: I'm looking at the Schedule 12B-1 --

5               JUDGE ALDRICH: Okay.

6               MR. PARKER: -- which is, I think, page 338 of  
7 the exhibit binder.

8               JUDGE ALDRICH: All right.

9               MR. NOBLE: And so the -- obviously, the sales  
10 data that they had in their system, the taxable sales  
11 recorded in there were far excessive over the amounts that  
12 they actually reported to the State.

13              JUDGE ALDRICH: Okay. Any other periods you'd  
14 like to point out?

15              MR. PARKER: Not at this time. 2015 and 2016, we  
16 did accept those periods. The sales data did match.

17              JUDGE ALDRICH: Okay. All right. I have a  
18 question for Mr. Derderian.

19              So your counsel indicated there was a problematic  
20 employee around 2014 that you ended up letting go.

21              MR. O'CONNOR: That's correct.

22              JUDGE ALDRICH: Okay. And I guess I wondering  
23 when you discovered issues relating to that employee?

24              MR. DERDERIAN: That employee was having personal  
25 problems we realize, and then we found out that accounts



1       payables was delayed. Exact timing through that year, I  
2       don't recall. But when we noticed that those -- those  
3       were problems, that's when we let her go. But did not  
4       know that there was something going on with the CDTF.

5               JUDGE ALDRICH: Okay. But I believe the argument  
6       was that there's an accounts receivables problem in your  
7       vendors --

8               MR. DERDERIAN: Right.

9               JUDGE ALDRICH: -- or service providers weren't  
10      getting paid. Was that 30 days? Was that 60 days? Was  
11      that --

12              MR. DERDERIAN: We -- we found out that -- when I  
13      found the problem, that it was a 90 day. We had vendors  
14      call us and we were 90 days behind.

15              JUDGE ALDRICH: Okay. And then on a typical  
16      basis with your service providers and your vendors, is  
17      there a grace period. Like, you know, a service is  
18      provided and they give you 30 days or they give you --

19              MR. DERDERIAN: Yes. It's about a 30 to 45 day.  
20      We have a couple of vendors that are at 60 days. But  
21      again, it wasn't every vendor. Like, it wasn't 100  
22      percent. It was very spotty, and that's how we found out  
23      at 90 days.

24              JUDGE ALDRICH: At 90 days. Okay. And so maybe  
25      a quarter into 2014?

1           MR. DERDERIAN:   Correct.

2           JUDGE ALDRICH:   Okay.   And then, I guess, do you  
3   oversee the hiring and firing?   Is there somebody else?

4           MR. DERDERIAN:   At that time I believe it was a  
5   manager that was doing the hiring and firing.

6           JUDGE ALDRICH:   Okay.   And are you in regular --  
7   were you in regular communication with that person?

8           MR. DERDERIAN:   Yes.

9           JUDGE ALDRICH:   Okay.   All right.

10          Judge Wong, did you have any questions for either  
11   of the parties?

12          JUDGE WONG:   Yeah.   I had one question for  
13   Appellants.   So CDTFA had mentioned that they took data  
14   from the franchisor's reports back to 2008, so 2008  
15   through 2016; and that data matched what was reported on  
16   the federal income taxes returns, gross receipts  
17   generally.   So do you have -- could you address that?   So  
18   they're basically saying that the franchisor reports that  
19   they had since 2008 were pretty accurate to what Appellant  
20   reported on the federal income tax returns, but it didn't  
21   show -- it didn't match what was coming out of -- for the  
22   sales and use tax returns to CDTFA.

23          MR. O'CONNOR:   Right.   I think -- I think the  
24   issue is that it's not the -- the total number.   It's how  
25   the tax was calculated.   And, again, there's going to be

1 variations in every year. But really, it's more about how  
2 the tax was being calculated as opposed to that's the top  
3 line number. And even then, the top line number should  
4 still be fairly similar. But then you're talking about  
5 that's a gross number that doesn't divide or account for  
6 taxable v nontaxable sales. So it's going to be a  
7 different number. But relatively -- I would assume maybe  
8 relatively the same. But again, that number our -- we  
9 still posit that that spreadsheet again, is inaccurate,  
10 and they haven't verified those numbers in there at all.

11 JUDGE WONG: Okay. Because you had also  
12 mentioned earlier that the numbers -- you asserted that  
13 the numbers in that spreadsheet were inflated because  
14 there was estimates, and then there's on the same  
15 prospective car jobs there are multiple estimates based on  
16 training and things like that. Is that --

17 MR. O'CONNOR: Yeah. Correct.

18 JUDGE WONG: Okay. Okay. But then -- okay. But  
19 then if you're reporting those similar numbers to the  
20 feds, I mean, are you over reporting to the feds as well,  
21 or you --

22 MR. O'CONNOR: We -- we might be. We haven't had  
23 to -- there was no audit from the feds. So for however  
24 long and how bad those numbers are, we don't know. She  
25 was reporting the numbers based off spreadsheets. But I

1 would say that they could be close, but they're not going  
2 to be the same. And again, that's a gross number that's  
3 still jumbled up. And again, I think our -- our bigger  
4 issue with the spreadsheet is the fact that it was taken  
5 outside the normal process. There was no establishment of  
6 fraud first to open up the statute, and that they  
7 requested, specifically, information going back outside  
8 the audit period.

9 JUDGE WONG: Okay. So your position is that the  
10 reporting to the feds could be over inflated, but you're  
11 not sure. There's no evidence of that.

12 MR. O'CONNOR: No. You're talking about numbers  
13 that are now a decade old to ask Mr. Derderian to go back  
14 and analyze if other issues -- given what happened with  
15 the employee, is it possible that there are other issues  
16 that exist out there? Absolutely. Have we gone back and  
17 audited his federal income tax returns? No, we have not.

18 JUDGE WONG: Okay. Thank you. That's all the  
19 questions I had.

20 JUDGE ALDRICH: Judge Kim?

21 JUDGE KIM: Yes, I have some questions.

22 So Appellant incorporated in 2004; is that  
23 correct, Johnnie's Paint and Body Shop, Inc.?

24 MR. DERDERIAN: I believe so.

25 JUDGE KIM: But it was reporting its sales under

1 a different business' seller's permit?

2 MR. O'CONNOR: Yeah. There were some issues, I  
3 think, right when the -- the takeover happened, that there  
4 was an issue between which entity had, like, the -- the  
5 seller's permit. But, at the end of the day, I think that  
6 issue is kind of a red herring because all the sales were  
7 reported, whether or not it's on Johnnie's. But I think  
8 that the sales permit issue has since been remedied. But  
9 I think that was an issue early on, but it's not an issue  
10 that impacts what we're doing here because the sales  
11 were -- were still reporting. It was more of a -- I think  
12 they had issues going back. It was, like, a parent  
13 subsidiary relationship. And, at that time, I think the  
14 thought was that you could use the parent's seller's  
15 permit for everything underneath. And then that was  
16 explained that you couldn't do that, and then they went  
17 and got the proper seller's permit.

18 JUDGE KIM: So Johnnie's Paint and Body Shop,  
19 Inc., was wholly owned by the other corporation?

20 MR. O'CONNOR: Is that -- is that the right  
21 structure?

22 MR. DERDERIAN: Johnnie's Paint and Body Shop was  
23 under Derderian Brothers Corporation, which Derderian  
24 Brothers Corporation owned also Johnnie's Tow. And  
25 Johnnie's Tow, when it sold, my father and his brother

1 split, and we kept Derderian Brothers Corporation, which  
2 was Johnnie's Paint and -- Johnnie's Paint and Body Shop.  
3 Johnnie's Tow was shutdown. I'm sorry.

4 But then after that fact, when I took it over,  
5 and if the corporation was at 2004, I believe it was my  
6 brother and I. 2006 is when I completely took it over,  
7 from what I recall. And I did talk to this -- the agent,  
8 whoever I spoke to, because they came to our facility and  
9 spoke to us about the resale number being on Derderian  
10 Brothers name, and we're operating with a tax ID number of  
11 Johnnie's Paint and Body Shop. He said if you're an  
12 officer of that corporation, you're fine with using that  
13 resale number, but it'll be better off if you later on do  
14 that change. My CPA told me it's better if you do it as  
15 soon as you can when they brought it to our attention that  
16 the resale was under Derderian Brothers.

17 JUDGE KIM: And when did that come to your  
18 attention?

19 MR. DERDERIAN: I -- I can't tell you the date.  
20 I don't recall exactly.

21 JUDGE KIM: And when did Johnnie's apply for a  
22 seller's permit?

23 MR. DERDERIAN: I don't recall that either.

24 JUDGE KIM: So during Johnnie's, the time it  
25 operated, it had its own bank account?

1 MR. DERDERIAN: Yes.

2 JUDGE KIM: Okay. And did Derderian Brothers  
3 Corporation, that's -- any other business besides  
4 Johnnie's?

5 MR. DERDERIAN: No. It's an entity -- it's an  
6 entity that owns the property.

7 JUDGE KIM: It just owns Johnnie's?

8 MR. DERDERIAN: Yes.

9 JUDGE KIM: Okay.

10 MR. O'CONNOR: But I'd assume if it owns  
11 Johnnie's, it owns the land. It's collecting rent. There  
12 may be some other items on that 1120 at the top.

13 JUDGE KIM: Okay. So I see Johnnie's federal  
14 income tax returns in the record for 2014 and 2015. Is  
15 that -- is 2014 when they first started filing federal  
16 returns?

17 MR. O'CONNOR: No. I -- I don't think so. The  
18 2014 is significant because that's the first year they  
19 become a franch -- or an affiliate of Fix Auto.

20 JUDGE KIM: Okay. And they were filing federal  
21 returns --

22 MR. O'CONNOR: Well before that.

23 JUDGE KIM: -- well before that?

24 MR. O'CONNOR: Yeah.

25 JUDGE KIM: Okay. That's the questions I have

1       for now.

2               MR. O'CONNOR:   Thank you.

3               JUDGE ALDRICH:   Just to be clear, there's  
4       Derderian Incorporated -- or Derderian Brothers  
5       Incorporated and they were the land holder?   The actual  
6       business was on -- that was operating there was Johnnie's  
7       Paint and Body Shop, and then Johnnie's Paint and Body  
8       switched its DBA around 2014 to Fix Auto Pasadena.   Is  
9       that an accurate --

10              MR. DERDERIAN:   I believe that the DBA came  
11       earlier than that.

12              JUDGE ALDRICH:   The Fix Auto DBA came earlier  
13       than that?

14              MR. DERDERIAN:   Yes.

15              JUDGE ALDRICH:   Do you have a --

16              MR. DERDERIAN:   Exact date, I don't recall what  
17       year.

18              JUDGE ALDRICH:   Okay.   All right.

19              Anything further?

20              All right.   So yeah.   Did you have a point of  
21       clarification?

22              MR. O'CONNOR:   Just wondering if we still had  
23       time reserved for the closing?

24              JUDGE ALDRICH:   Absolutely.   You only used, I  
25       think, around 35 minutes or -- approximately.



1           MR. O'CONNOR: I -- I apologize, Your Honor. I  
2           thought you were shutting the record off here.

3           JUDGE ALDRICH: Oh, no. Absolutely. Are you  
4           ready to proceed with that rebuttal or closing?

5           MR. O'CONNOR: Absolutely.

6           JUDGE ALDRICH: Ms. Paley, did you have something  
7           to add before we transition?

8           MS. PALEY: No. Thank you.

9           JUDGE ALDRICH: Okay. Go ahead when you're  
10          ready.

11          MR. O'CONNOR: Okay.

12

13                           CLOSING STATEMENT

14          MR. O'CONNOR: After listening to the  
15          Department's argument, I still haven't heard any  
16          allegation of fraudulent behavior here. The Department's  
17          position is really improperly conflating underreporting  
18          with fraud here. Just because a party underreports does  
19          not necessarily make it fraudulent. The statute requires  
20          clear and convincing evidence of intentional wrongdoing.  
21          That's their job. They haven't done. They haven't said  
22          there's been any wrongdoing.

23                 The only thing that's been wrong is there was an  
24          amount underreported in 2014, per his own records. He  
25          didn't hide it. He didn't cover it up. He didn't send

1 the wrong records. There's none of that there.  
2 Underreporting without more, it's not fraud. They can't  
3 simply presume there's fraud. It's got to be shown by  
4 clear and explicit evidence. They haven't done that. She  
5 -- she's -- opposing counsel cited Bradford. This defines  
6 fraud as intentional wrongdoing with the specific purpose  
7 of evading a tax known to be due.

8           Bradford is equally clear that the presence of  
9 badges, such as understatements or records issues may be  
10 circumstantial indicators, but those indicators must point  
11 at evasion. Not negligence. Not oversight. Not the  
12 misapplication of software. They have to confirm the  
13 circumstantial evidence. They haven't done that. All  
14 they've done is support the fact that there possibly been  
15 a mistake or an issue with the taxpayer's internal  
16 controls.

17           Again, going back to ISIF Madfish, it underscores  
18 that the analysis turns on whether those badges  
19 convincingly demonstrate the taxpayer's specific intent to  
20 evade. The presence of tax separately stated on invoices  
21 or other internal sales data can show awareness of tax  
22 obligations. But without management directing, ratifying,  
23 or knowingly tolerating misreporting, those facts were  
24 equally consistent with clerical errors. There's nothing  
25 here that shows that my client committed fraud, directed

1       anybody else to commit fraud, anything. There's no  
2       inference.

3               The Department invokes the imputation principles  
4       outlined in their Audit Manual, but vicariously --  
5       vicarious responsibility for an employee's acts does not  
6       answer the legally dispositive question under 68 -- 6485,  
7       whether the taxpayer had the specific intent to evade.  
8       California law requires proof that the taxpayer acted with  
9       fraudulent intent. Negligent supervision or failure to  
10      catch an employee's error does not suffice. Clear and  
11      convincing standard in prior case law shows that that does  
12      not meet that inference.

13             The Department's own condition provided there are  
14      no plausible and consistent non-fraudulent expect --  
15      explanations is not met. The record reflects a plausible  
16      consistent non-fraudulent explanation; reporting  
17      breakdowns during a software transition and an employee  
18      error. My client fully cooperated throughout this audit  
19      process. He provided books and records, provided  
20      documents, provided time, provided follow up. But here,  
21      the Department would have you think that magnitude is  
22      determinative. Courts have repeatedly cautioned that the  
23      size of understatement, while a factor, does not convert  
24      negligence into fraud.

25             Finally, the Department points to unremitted tax

1 reimbursement. The question again, is intent. There's no  
2 proof in their 40 percent underpayment argument that the  
3 taxpayer every intended to commit fraud. Without this,  
4 this panel cannot find that the statute of limitations can  
5 be opened. The panel cannot find that the 25 percent  
6 penalty is applicable. Opposing counsel stated that  
7 there's no basis under the enumerated factors to deny the  
8 40 percent, or to grant reasonable cause for the 40  
9 percent penalty. That's not true. There's two.

10 One, the internal controls that we talk about  
11 earlier. But two, there's a specific exception when  
12 there's one instance over a three-year time. They're  
13 talking about one year in a three-year period to apply  
14 this 40 percent penalty. One year. That's not enough.  
15 By their own plain language of the statute, that 40  
16 percent penalty wasn't good to start the -- the fraud  
17 memo. It's not good to -- to assess the penalty in the  
18 side. There's nothing here that amounts to fraud. And I  
19 would posit to the panel that this case, after reviewing  
20 multiple cases at length, this case is very specific in  
21 that there's one major glaring difference. My client  
22 properly reported tax in two years and one quarter of the  
23 audit period. That's 75 percent accuracy. He passed  
24 audit two of three years. Even if you throw away the one  
25 quarter, he has still passed audit upwards of 67 percent

1 of the time. That's not fraud.

2 They didn't give him the benefit of the doubt at  
3 all. Not once did they look at that and say, hey, he  
4 passed audit in '15 and '16. Maybe there was an error.  
5 Look, the books and records show that he underreported.  
6 Maybe there's an error. They didn't do that. They turned  
7 around, called him a fraud, called him a cheat over what?  
8 Three quarters of an error? He uses somebody else's  
9 software that he has no ability to impact. It's shown  
10 this on the record.

11 So my final thought to this panel is this is  
12 pretty simple for you guys to kick here. There's no  
13 consecutive years of fraud. That's the plain language in  
14 Madfish; consecutive years of underreporting. They don't  
15 get to go on a fishing expedition because there's three  
16 quarters and say, give me all the books and records from  
17 2008. That basically destroys the statute of limitations.  
18 What's the point of the statute of limitations then, if we  
19 don't have to come and fraud first if they can say, hey, I  
20 think there may be some underreporting. Because I -- I  
21 would love for you guys to go back and look at that, their  
22 Exhibit C, because that's what it says.

23 In Exhibit C, it says the auditor believes there  
24 may be underreporting in prior periods. That's what they  
25 used; not the auditor believes there was fraud in prior

1 periods; not that the auditor believes there's fraud now.  
2 There might be an understatement, and that's what we're  
3 going to have the taxpayers deal with now is the standard  
4 is, hey, the auditor thinks might be an understatement.  
5 So give me everything you've got for the last decade. To  
6 find any -- any other way but for my client is to  
7 eviscerate the statute of limitations.

8 Thank you.

9 JUDGE ALDRICH: Thank you.

10 Well, I want to thank everyone for their time.

11 We're ready to conclude the hearing, and the  
12 record is now closed.

13 The panel will meet and decide the case based on  
14 the admitted evidence, the arguments presented today, and  
15 the relevant law. We will send both parties our written  
16 decision no later than 100 days from today.

17 OTA's hearing calendar has concluded for the day,  
18 and we will resume tomorrow morning at 9:30.

19 Please cut the live stream.

20 Thank you.

21 (Proceedings concluded at 2:29 p.m.)

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HEARING REPORTER'S CERTIFICATE

I, Ernalyne M. Alonzo, Hearing Reporter in and for  
the State of California, do hereby certify:

That the foregoing transcript of proceedings was  
taken before me at the time and place set forth, that the  
testimony and proceedings were reported stenographically  
by me and later transcribed by computer-aided  
transcription under my direction and supervision, that the  
foregoing is a true record of the testimony and  
proceedings taken at that time.

I further certify that I am in no way interested  
in the outcome of said action.

I have hereunto subscribed my name this 31st day  
of December, 2025.

\_\_\_\_\_  
ERNALYN M. ALONZO  
HEARING REPORTER