

FACTUAL FINDINGS

1. During the liability period, appellant operated a gas station with a mini mart in Visalia, California, doing business as Jack's Liquor. Appellant sold gasoline, diesel, and lottery tickets, in addition to taxable and nontaxable items such as soda, beer, wine, cigarettes, tobacco, food items, and other miscellaneous taxable items.
2. Appellant obtained his seller's permit with an effective start date of July 1, 2013, which was closed effective September 30, 2020. This is appellant's first audit under this seller's permit.
3. Previously, appellant held a seller's permit for a food-mart in Farmersville, California, and a seller's permit for two Gas-N-Grubs, one located in Farmersville, and the other in Exeter, California. Appellant underwent an audit for both seller's permits for the period January 1, 2008, through December 31, 2009 (the prior audit), which resulted in unreported taxable sales and the imposition of negligence penalties. The locations were no longer in operation during the liability period.
4. For the liability period, appellant reported total sales of \$7,855,297 and claimed deductions of \$5,471,817, for a total of \$2,383,480 in reported taxable sales, which consisted of \$1,332,294 in reported fuel sales and \$1,051,186 in reported taxable mini mart sales. Appellant's reporting method was unknown.
5. Appellant did not provide any books and records for audit.
6. Due to an absence of source documentation to support sales reported on appellant's sales and use tax returns (SUTRs), CDTFA was unable to verify how appellant computed the reported amounts. CDTFA determined it could not rely on appellant's SUTRs and that it could not verify reported sales by a direct audit approach; therefore, CDTFA used indirect audit methods to verify appellant's reported taxable sales.
7. CDTFA obtained data from the Energy Information Administration (EIA) of the U.S. Department of Energy⁴ to verify appellant's reported gasoline and diesel sales. CDTFA used the statewide average selling prices obtained, adjusted for pricing differentials applicable to appellant's location, and number of gallons of fuel supplied by appellant's vendors. Based on its analysis, CDTFA accepted appellant's reported fuel sales.
8. To verify appellant's reported taxable mini mart beer sales, CDTFA obtained responses to vendor surveys for the first quarter of 2019 (1Q19) through 3Q20 from three vendors

⁴ The EIA surveys gasoline stations in various areas one day each week (typically a Monday) and computes an average selling price for that day.

that distributed to appellant.⁵ Based on the responses, CDTFA compiled total taxable beer purchases of \$212,596 for 2019 and \$368,912 for 1Q20 through 3Q20.⁶ Since appellant did not provide source documentation for recorded beer purchases, CDTFA was unable to compare audited taxable beer purchases to recorded taxable beer purchases. CDTFA was also unable to verify appellant's total cost of goods sold. Due to an absence of source documentation, CDTFA determined that an indirect audit method would be necessary to verify the reported sales.

9. In the prior audit, CDTFA performed a purchase segregation test using purchase invoices provided by appellant to calculate an average ratio of beer purchases to total taxable purchases of 49.97 percent. Since the prior audit not only involved similar businesses, but also ones that were in close proximity to the location for the current audit, CDTFA decided to use this ratio in the current audit. CDTFA divided the beer purchases of \$212,596 for 2019 and \$368,912 for 1Q20 through 3Q20 by the beer purchase ratio of 49.97 percent to calculate audited taxable purchases of \$425,460 for 2019 and \$738,290 for 1Q20 through 3Q20. After allowing a 1 percent adjustment for shrinkage,⁷ CDTFA calculated adjusted taxable purchases of \$421,206 for 2019 and \$730,908 for 1Q20 through 3Q20, for a total of \$1,152,113 in audited cost of goods sold for the liability period.
10. For the current audit, CDTFA determined a shelf test⁸ was not feasible.⁹ During the prior audit, CDTFA conducted a shelf test and calculated a weighted average taxable markup of 21.20 percent. CDTFA decided to use this markup in the current audit. CDTFA

⁵ Appellant did not report any sales from 4Q17 to 1Q19 due to apparent construction and remodeling. During audit, CDTFA noted that vendor reports confirmed appellant did not make purchases during this time.

⁶ CDTFA included only taxable beer purchase amounts in its calculations.

⁷ During CDTFA's appeals conference, appellant indicated there was not any self-consumption of taxable merchandise.

⁸ A shelf test is a comparison of known costs and selling prices and is used in audit to calculate the markup of specific items or classes of items.

⁹ CDTFA made numerous requests that appellant provide CDTFA with the selling prices for purchases recorded on the merchandise purchase invoices for a selected period of time, or to allow CDTFA to conduct a shelf test of the business. Since appellant did not respond to the requests, CDTFA determined a shelf test was not feasible.

applied the audited weighted taxable markup factor¹⁰ of 1.212 (21.20 percent markup + 100 percent) to the audited cost of goods sold of \$1,152,113 and calculated audited taxable mini mart sales of \$1,396,361. CDTFA subtracted \$1,051,186 in reported taxable mini mart sales from \$1,396,361 in audited taxable sales, calculating \$345,175 in unreported taxable sales based on the markup method for the liability period.

11. Appellant accepted Supplemental Nutrition Assistance Program (SNAP)/CalFresh program for purchases; therefore, CDTFA contacted the United States Department of Agriculture to verify redemption amounts.¹¹ Based on redemption amounts of \$36,382 and a SNAP/CalFresh allowance of 28.83 percent from prior similar businesses that were audited, CDTFA calculated \$10,488 in credit for exempt goods paid for with SNAP/CalFresh. CDTFA applied a credit of \$10,489¹² towards the taxable measure for a total taxable measure of \$334,686 (\$345,175 - \$10,489).¹³
12. On August 27, 2021, CDTFA issued the aforementioned NOD to appellant.
13. Appellant filed a timely petition for redetermination disputing the NOD and filed a protective claim for refund, which CDTFA denied.
14. Appellant filed this timely appeal.

DISCUSSION

California imposes sales tax on a retailer's retail sales of tangible personal property sold in this state measured by the retailer's gross receipts, unless the sale is specifically exempt or excluded from taxation by statute. (R&TC, §§ 6012, 6051.) For the purpose of the proper administration of the Sales and Use Tax Law and to prevent the evasion of the sales tax, the law presumes that all gross receipts are subject to tax until the contrary is established. (R&TC, § 6091.) It is the retailer's responsibility to maintain complete and accurate records to support

¹⁰ Markup factor is the amount by which a product's cost is increased to determine its selling price. The markup factor is calculated by dividing sales by the cost of goods sold. The markup factor is equal to the markup (the amount by which the cost of merchandise is increased to set the retail price) plus 100 percent.

¹¹ CalFresh is California's implementation of SNAP, formally known as the federal Food Stamp Program. Sales of eligible food items purchased with CalFresh benefits are exempt from tax, even if the sale of the food item is normally taxable. (R&TC, § 6373; Cal. Code Regs., tit. 18, § 1602.5(c).)

¹² OTA finds the \$1 difference de minimis.

¹³ OTA notes that on the SUTRs for the liability period, appellant claimed deductions totaling \$5,471,817, which consisted of \$311,820 in claimed exempt sales of food products. It is unclear from the record if the claimed exempt sales of food products included purchases paid with SNAP/CalFresh; however, as the \$10,489 credit is in taxpayer's favor, OTA will discuss it no further.

reported amounts and to make them available for examination. (R&TC, §§ 7053, 7054; Cal. Code Regs., tit. 18, § 1698(b)(1).)

If CDTFA is not satisfied with the amount of tax reported by the taxpayer, or in the case of a failure to file a return, CDTFA may determine the amount required to be paid on the basis of any information which is in its possession or may come into its possession. (R&TC, §§ 6481, 6511.) In the case of an appeal, CDTFA has a minimal, initial burden of showing that its determination was reasonable and rational. (*Appeal of Talavera*, 2020-OTA-022P.) Once CDTFA has met its initial burden, the burden of proof shifts to the taxpayer to establish that a result differing from CDTFA's determination is warranted. (*Ibid.*) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (*Ibid.*)

Appellant generally bears the burden of proof as to all issues of fact. (Cal. Code Regs., tit. 18, § 30219(a).) The standard of proof is by a preponderance of the evidence. (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.) To satisfy its burden of proof, a taxpayer must prove both that the tax assessment is incorrect and what the proper amount of tax should be. (*Appeal of AMG Care Collective*, *supra.*)

Generally, CDTFA prefers to determine the accuracy of reported amounts using a direct audit methodology.¹⁴ However, CDTFA is authorized to determine a liability on the basis of any information in its possession (R&TC, § 6481; *Appeal of Amaya*, 2021-OTA-328P); and if a taxpayer's records are insufficient for a direct audit methodology (or if the provided records are deemed unreliable), it becomes necessary for CDTFA to compute the taxpayer's sales using an indirect audit methodology. (R&TC, § 6481, *Appeal of Las Playas #10, Inc.*, 2021-OTA-204P.)

Here, appellant failed to provide *any* books and records, let alone business records that were adequate, for a sales and use tax audit. The consequences of appellant's failure to maintain and provide adequate business records correctly fall on appellant, who had the legal obligation and the ability to maintain and provide them. Those consequences include the use of an indirect audit methodology and the resulting estimate of taxable sales. Therefore, CDTFA's decision to employ an alternative, indirect audit methodology was appropriate.

¹⁴ A direct audit method is one that enables CDTFA to determine taxable sales directly from business records without estimates or extrapolation, such as by simple tabulation of taxable sales evidenced by sales invoices or cash register tapes. A direct audit methodology based on complete and accurate business records is generally the most accurate.

CDTFA contacted three vendors that distributed to appellant, obtaining survey responses from them indicating the items appellant bought from each vendor. CDTFA used the vendor survey responses to calculate the amount of beer products appellant purchased during the liability period. Appellant did not provide CDTFA with source documentation; therefore, CDTFA was unable to compare audited taxable beer purchases to recorded taxable beer purchases and to verify appellant's total cost of goods sold. Since CDTFA was unable to perform verifications, it decided to use the average ratio of beer purchases to total taxable purchases calculated during the prior audit to calculate audited cost of goods sold for the liability period. CDTFA continued to use the results from the prior audit since a shelf test was not feasible. CDTFA took the weighted average taxable markup factor calculated from the shelf test performed during the prior audit and applied it to the audited cost of goods sold, calculating audited taxable mini mart sales. After subtracting taxable mini mart sales appellant reported for the liability period, CDTFA calculated \$345,175 in unreported taxable sales based on the markup method for the liability period. Considering the complete lack of books and records, OTA finds that it was rational for CDTFA to use the results of a prior audit to calculate appellant's audited taxable sales and the results are reasonable. Accordingly, the burden shifts to appellant to show error in the audit.

On appeal, appellant contends that the estimated cost of goods sold are overstated and, therefore, the unreported taxable sales are also overstated. Appellant did not provide books and records for audit, despite CDTFA's numerous requests. Additionally, due to appellant's lack of response, a shelf test was not feasible. Appellant, having not cooperated with CDTFA during the audit, now points to the audit findings and proclaims the unreported taxable sales are "overstated." On appeal, appellant still has not provided supporting documentation, let alone substantiating evidence. OTA is astounded by the temerity of appellant.

Appellant bears the burden of establishing that a result different from CDTFA's determination is warranted. (See *Appeal of Talavera, supra.*) Appellant has not provided any evidence or substantive information to show that the taxable measure should be adjusted or was calculated improperly. Appellant's unsupported assertions are not sufficient to satisfy appellant's burden of proof. (*Ibid.*) Accordingly, OTA finds no basis to adjust the taxable measure.

HOLDING

Adjustments to the amount of unreported taxable sales are not warranted.

DISPOSITION

CDTFA's decision to deny appellant's petition for redetermination and claim for refund is sustained.

DocuSigned by:
Sheriene Anne Ridenour
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Sheriene Anne Ridenour
Administrative Law Judge

We concur:
Signed by:
Natasha Ralston
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Natasha Ralston
Administrative Law Judge

DocuSigned by:
Keith T. Long
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Keith T. Long
Administrative Law Judge

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