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OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of: **R. SIMMS,** **dba Ron Simms Bay Area Custom Cycles**	OTA Case No.: 240215322 CDTFA Case ID: 4436624

OPINION

Representing the Parties:

For Appellant: Stephen Mayer, CPA
Tina Knox, Bookkeeper

For Respondent: Nalan Samarawickrema, Hearing Rep.
Christopher Brooks, Attorney
Jason Parker, Chief of Headquarters Ops.

J. ALDRICH, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 6901, R. Simms (appellant) appeals a decision issued by respondent California Department of Tax and Fee Administration (CDTFA) denying appellant's claim for refund of $7,586.64.[1] Appellant's claim for refund disputes a June 3, 2022 Notice of Determination (NOD) in its entirety. The NOD is for tax of $32,494, plus applicable interest, and a 10 percent negligence penalty of $3,138.73,[2] for the period April 1, 2018, through March 31, 2021 (liability period).[3] The NOD became final on October 23, 2022, when appellant failed to perfect his right to continue the appeal.[4] Pursuant to R&TC section 6565 an additional 10 percent penalty of $3,138.70 was added to the NOD for appellant's failure to timely pay the NOD before it became

[1] Appellant's claim for refund asserts $7,736.64 as the levied amount at issue. However, appellant's bank account was levied for $7,586.64 (i.e., the amount CDTFA received) and his bank charged a $150 bank processing fee.

[2] The 10 percent negligence penalty was applied after a payment or credit of $1,107.

[3] CDTFA timely issued the NOD because appellant waived the otherwise applicable three-year statute of limitations and extended the NOD issuance deadline to July 31, 2022. (See R&TC, §§ 6487(a), 6488.)

[4] The NOD went final without issuance of a decision from which appellant could take an appeal to the Office of Tax Appeals. (See Cal. Code Regs., tit. 18, § 30103(b).) Consequently, only the claim for refund is at issue here.

final (finality penalty). On January 24, 2023, CDTFA added a $570 Collection Cost Recovery Fee (CCRF) pursuant to R&TC section 6833 because the liability had remained unpaid.

Office of Tax Appeals (OTA) Panel Members Michael F. Geary, Natasha Ralston, and Josh Aldrich held a virtual oral hearing for this matter on July 16, 2025. At the conclusion of the oral hearing, the record was closed, and this matter was submitted on the oral hearing record pursuant to California Code of Regulations, title 18, (Regulation) section 30209(b).

ISSUES

1. Whether adjustments to the measure of unreported taxable sales are warranted.
2. Whether the negligence penalty was properly imposed.
3. Whether the finality penalty was properly imposed, and, if it was, whether there is any basis for granting relief.
4. Whether the CCRF was properly imposed, and, if it was, whether there is any basis for granting relief.

FACTUAL FINDINGS

1. Appellant, a sole proprietor, operates a business where customers can purchase apparel, motorcycle accessories as well as parts to customize, repair, or otherwise replace parts on their motorcycles. Appellant's storefront is a large multi-story space that includes a garage where parts can be installed for customization or repair. Appellant also built custom motorcycles for sale. Appellant's seller's permit was changed from a partnership to a sole proprietor with an effective start date of January 1, 2000, and it remains active. During the liability period, appellant held a Vehicle Dealer License with the California Department of Motor Vehicles (DMV) until October 18, 2018. Because the DMV license was no longer valid after October 18, 2018, CDTFA's audit focused on the sale of parts, apparel, and accessories.
2. Appellant was previously audited for the period January 1, 2000, through March 31, 2003 (prior audit period).[5] During the prior audit, CDTFA scheduled appellant's beginning and ending inventories for 2000 and 2001. Appellant began the year 2000 with an inventory of $596,369, purchased an additional $1,634,264 in inventory during the year, and withdrew $1,708,400 from inventory, ending that year with

[5] Appellant's bookkeeper testified that there were two "no-change" audits between the prior audit and the audit at issue. Respondent did not confirm other audits, and there is no corroborating evidence that they occurred.

inventory of $550,645 and an inventory reduction of $45,715. During 2001, appellant purchased additional inventory of $1,534,349 and withdrew $1,573,310 in inventory, ending that year with $529,609 in inventory, a further reduction of $21,045.

3. The prior audit found that the books and records were not adequate for sales and use tax purposes; specifically, appellant failed to provide sales contracts, sales invoices, or reports of sale (ROS) for appellant's custom motorcycle sales. The unreported taxable sales were principally sales of custom motorcycles. CDTFA imposed the negligence penalty because of the lack of books and records and because the initial error rate, which is comprised of audited taxable sales compared to reported taxable sales, was 400 percent ($4,387,034 unreported taxable measure ÷ $1,103,255 reported taxable measure). Following the issuance of its decision, CDTFA prepared a reaudit that reduced the taxable measure to $3,741,534, and because of the reduction to the taxable measure, the error rate changed from 400 percent to 339 percent ($3,741,534 ÷ $1,103,255). For the prior audit period, CDTFA determined tax of $305,292.13, plus applicable interest, and imposed the 10 percent negligence penalty.
4. During the liability period, appellant reported on his Sales and Use Tax returns (SUTRs) total sales of $642,965 and claimed deductions totaling $254,125. The claimed deductions include $216,666 in nontaxable labor, $36,463 of sales tax included in reported gross sales, $585 for sales in interstate commerce, $344 for shipping costs, and $67 for environmental fees. After claimed deductions, appellant reported taxable sales of $388,840 for the liability period.
5. Appellant provided the following documents for audit: federal income tax returns (FITRs) for 2018 and 2019; profit and loss statements for April 1, 2018, through December 31, 2019; sales and purchase journals for the audit period; purchase invoices and sales invoices from July 6, 2021, through August 3, 2021; and bank statements from January 2019 through December 2019. The 2018 and 2019 FITRs reported ending and beginning inventories of $59,608. Appellant explained that all sales and purchases were recorded in QuickBooks, and then sales were reported based on QuickBooks reports. Appellant did not provide complete sales or purchase records (e.g., invoices, sales invoices, credit card receipts, or payment information from customers).
6. CDTFA noted that gross receipts reported on appellant's FITRs exceeded appellant's total sales reported to CDTFA by $5,717 and $29,637, for 2018 and 2019, respectively. Next, CDTFA compared reported taxable sales of $388,840 to purchases recorded in

appellant's purchase journal of $511,320 to calculate an overall negative reported book markup[6] of 24 percent.[7]

7. CDTFA compared recorded merchandise purchases to sales recorded on the profit and loss statements, which showed negative markups of 22.74 percent for 2018 and 9.58 percent for 2019. CDTFA expected a book markup of 35 to 80 percent based on appellant's location and type of business. Based on the negative markup and the prior audit that resulted in an assessment based on unreported taxable sales, CDTFA determined that additional analysis was warranted.

8. Since appellant did not provide complete sales records, CDTFA utilized an indirect audit method (i.e., the markup method). CDTFA conducted a shelf test using appellant's sales and purchase invoices for the period July 6, 2021, through August 3, 2021.[8] CDTFA calculated an achieved markup from the shelf test of 42.52 percent. CDTFA spot checked appellant's purchase journal by comparing bank statements to purchases recorded in the purchase journal. CDTFA found that the sources reconciled and, on that basis, accepted the purchase journal as accurate. CDTFA applied the achieved markup of 42.52 percent to the purchases recorded in appellant's purchase journal. CDTFA then deducted claimed nontaxable sales in interstate commerce to calculate total taxable sales of $728,142. Total taxable sales exceeded reported taxable sales of $388,840 by $339,302, which is the taxable measure in dispute.

9. CDTFA imposed the negligence penalty because: (1) appellant had previously been audited, and appellant reported less taxable sales than taxable purchases, so the audited taxable sales were projected based on marking up taxable purchases; (2) the unreported taxable sales for this audit period were material; (3) the average percentage of error of 90.34% was considered high compared to reported taxable sales;

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[6] Markup" is the amount by which the cost of merchandise is increased to set the retail price. For example, if the retailer's cost is $0.70 and it charges customers $1.00, the markup is $0.30. The formula for determining the markup percentage is markup amount ÷ cost. In this example, the markup percentage is 42.86 percent (0.30 ÷ 0.70 = 0.42857). A "book markup" (sometimes referred to as an "achieved markup") is one that is calculated from the retailer's records. A negative markup indicates that the retailer is selling items for less than cost.

[7] Appellant's FITRs indicate that beginning and ending inventories remained constant, which is evidence that the cost of inventory withdrawn for use or sale during the year equaled the cost of inventory purchased during the year.

[8] A shelf test is a comparison of known costs of goods and associated selling prices used to compute markups.

(4) appellant's knowledge regarding record keeping and reporting requirements; and (5) the negative book markups demonstrated incomplete recording of sales and purchases.

10. On June 3, 2022, CDTFA issued the Notice of Determination to appellant.

11. Appellant filed a petition for redetermination (petition) disputing the NOD in its entirety. Appellant asserted that, based on a physical inventory count as of December 31, 2021, the audit findings were based on incorrect inventory amounts for the second quarter 2018 (2Q18), through 1Q21. Appellant did not request an appeals conference with CDTFA's Appeals Bureau.

12. In response to appellant's petition, CDTFA's Tax and Fee Programs Bureau (TFPB) issued a Report of Discussion of Audit Findings (Report of Discussion) on August 15, 2022. Therein, CDTFA explained that the summary worksheet provided with the petition was the same report previously provided, and that documents of original entries were not provided to verify the accuracy of the recorded amounts shown in the summary worksheets. CDTFA rejected appellant's arguments relating to its inventory because: there was no proof that the amended FITRs were filed; and no source documents (e.g., purchase invoices or financial records supporting the infusion of capital) to support an adjustment. CDTFA also rejected appellant's amended inventory amounts because it determined that the average number of days an item was in inventory before being sold (inventory turnover) was unreasonably high (i.e., 414 days). Therefore, CDTFA recommended no change to the audited measure.[9]

13. CDTFA's Appeals Bureau sent an August 15, 2022 letter to appellant explaining that appellant did not previously request an appeals conference and that appellant would have 30 days to make such a request. Appellant did not respond to the letter. Accordingly, CDTFA's Appeals Bureau closed the petition and made no adjustments to the NOD.

[9] On August 23, 2022, TFPB held a telephone conference with appellant. Appellant explained that the amended FITRs were ready to be filed; that ending inventory was approximately $237,000 as of December 31, 2021; and invited an auditor to come to the business to conduct a physical inventory. In response, TFPB indicated that the petition is with the Appeals Bureau; asked appellant to explain the negative markup; and once the amended returns are filed and a copy received, TFPB would review the records to determine if adjustments were warranted. Appellant did not explain the negative markup or provide records in support thereof. Appellant also did not file the amended FITRs until October 2022, or later.

14. Since appellant did not respond to CDTFA's Appeals Bureau August 15, 2022 letter, CDTFA issued a Notice of Redetermination to appellant on September 22, 2022.[10]
15. On October 23, 2022, the NOD became final because appellant did not pay or timely appeal the NOD.
16. On October 24, 2022, CDTFA imposed the finality penalty.
17. According to CDTFA, it issued a demand for immediate payment of the liability (Demand Notice) on October 25, 2022, CDTFA.
18. Appellant filed amended FITRs with revised inventory amounts for 2018 through 2021. The amended FITRs changed reported purchase amounts, beginning inventory, and ending inventory amounts.
19. On November 21, 2022, CDTFA sent a Notice of Levy.
20. On December 2, 2022, CDTFA collected a payment of $7,586.64 through a bank levy.
21. On January 3, 2023, CDTFA's TFPB spoke with appellant explaining that: the Report of Discussion and the August 15, 2022 Appeals Bureau letter were sent in August; CDTFA did not receive a response to either letter; and appellant should contact the Appeals Bureau for additional steps.
22. On January 4, 2023, appellant filed a claim for refund, requesting a refund of the collected amount.
23. According to CDTFA, it sent appellant a Notice of Collection Recovery Fee dated January 24, 2023.
24. On December 21, 2023, CDTFA issued its decision denying appellant's claim for refund in its entirety. CDTFA rejected appellant's amended inventory amounts because it determined the method for performing the physical inventory count was incorrect and produced unreliable results. It found that the average number of days that items were in inventory was 506 days for 2Q18, 406 days for 2019, 403 days for 2020, and 240 days for 2021, which CDTFA considered to be unreasonable. CDTFA also found that the book markup based on the amended costs of goods sold was negative .0027 for 2Q18 through 4Q18, 0 percent for 2019, 1.93 percent for 2020, and a negative .41 for 2021.
25. This timely appeal followed.

[10] In appellant's January 3, 2023 letter, appellant acknowledged receiving the Appeals Bureau August 15, 2022 letter, but "just assumed that the entire thing was put on hold, not realizing that we still needed to file the appeal."

26. On June 18, 2025, OTA issued Minutes and Orders of Prehearing Conference (Minutes and Orders). In pertinent part, OTA asked the parties "If appellant's amended [FITRs] were accepted as accurate, what would appellant's markup be for the liability period?"

27. In preparation for the oral hearing and in response to OTA's Minutes and Orders, CDTFA submitted additional audit schedules.[11]

DISCUSSION

Issue 1: Whether adjustments to the measure of unreported taxable sales are warranted.

California imposes sales tax on a retailer's retail sales of tangible personal property sold in this state measured by the retailer's gross receipts, unless the sale is specifically exempt or excluded from taxation by statute. (R&TC, §§ 6012, 6051.) For the purpose of the proper administration of the Sales and Use Tax Law and to prevent the evasion of the sales tax, the law presumes that all gross receipts are subject to tax until the contrary is established. (R&TC, § 6091.) It is the retailer's responsibility to maintain complete and accurate records to support reported amounts and to make them available for examination. (R&TC, §§ 7053, 7054; Cal. Code Regs., tit. 18, § 1698(b)(1).)

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*.)

Generally, the taxpayer bears the burden of proof as to all issues of fact. (Cal. Code Regs., tit. 18, § 30219(b).) To satisfy his burden of proof, a taxpayer must prove both: (1) that the tax assessment is incorrect; and (2) the proper amount of tax. (*Appeal of AMG Care Collective*, 2020-OTA-173P.) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (*Ibid*.)

Upon audit, CDTFA initially noticed gross receipts reported on appellant's FITRs exceeded appellant's total sales reported on SUTRs, for 2018 and 2019. Accordingly, CDTFA

[11] CDTFA also submitted DMV records that show $16,450 in additional unreported taxable sales. CDTFA is not asserting an increase but instead is requesting an offset in the event OTA finds that reductions to the taxable measure are warranted. (R&TC, §§ 6563, 6483.)

concluded that appellant may have underreported taxable sales. CDTFA then compared reported taxable sales to recorded purchases, which showed a negative markup of 24 percent. Next, CDTFA compared recorded merchandise purchases to sales recorded in appellant's profit and loss statements for apparel, motorcycle accessories, and parts. The comparison identified negative markups of 22.74 percent and 9.58 percent, for 2018 and 2019, respectively. CDTFA concluded that an indirect audit method was required to verify appellant's sales based on the negative markups, the incomplete sales records, and the prior audit that resulted in an assessment based on unreported taxable sales. Based on the available information, CDTFA utilized the markup method, which is a recognized and accepted accounting procedure. (*Appeal of Amaya*, 2021-OTA-328P.)

CDTFA conducted a shelf test for the period of July 6, 2021, through August 3, 2021. After performing a spot check, CDTFA accepted appellant's purchase journal as accurate. Based on the shelf test, CDTFA calculated an achieved markup of 42.52 percent, which was then applied to recorded purchases in appellant's purchase journal for the liability period. CDTFA then deducted claimed nontaxable sales in interstate commerce to calculate total taxable sales and then subtracted reported taxable sales to establish unreported taxable sales.

OTA finds that CDTFA correctly concluded that appellant's records could not be relied upon to accurately verify reported taxable sales based on the difference between reported gross receipts and total sales reported as well as the negative markups. OTA also finds that CDTFA rationally designed a methodology, the markup method, for estimating sales based on the available evidence (i.e., appellant's own purchase journal). (See *Appeal of Amaya*, *supra*.) CDTFA took reasonable steps to verify the accuracy of the documents that appellant provided (e.g., performing a spot check by cross-referencing bank statements and purchase journal). CDTFA then applied the achieved markup to appellant's recorded purchases for the liability period to calculate the audited unreported taxable sales. Under these circumstances, it was appropriate for CDTFA to conclude that appellant's reported taxable sales were likely understated, and that CDTFA could not use a direct audit method to verify reported taxable sales. Considering all evidence, OTA finds that CDTFA has met its initial burden to show that its determination is reasonable and rational. Accordingly, the burden shifts to appellant to establish that any adjustments are warranted.

Appellant's central dispute with the audit pertains to the inventory count. Appellant argues that the beginning and ending inventory amounts for 2018 and 2019, all exactly $59,608, substantially understated the actual inventory. Appellant argues that the amended FITRs have higher and more accurate inventory amounts and that using the higher inventory amounts will

show that appellant's SUTRs for the liability period were accurate. Appellant explains that the amended returns are relevant to the audit because purchases, inventory, and sales need to be accurate over the audit period to arrive at the correct taxable sales. Appellant claims that CDTFA used the $59,608 inventory amount, not the higher inventory amounts as reported on appellant's amended 2018 and 2019 FITRs. Accordingly, appellant argues that the entirety of the audited understatement should be reduced to zero. In support, appellant provided the amended FITRs, a schedule without source documents, and the testimony of appellant's bookkeeper.

Ms. Knox, appellant's bookkeeper, testified to the following: (1) she has worked for appellant for a long time, since approximately 1993; (2) she uses QuickBooks to record all of appellant's purchases and sales information, which she summarized monthly, using the summaries to prepare the SUTRs; (3) appellant typically replaced inventory as it was withdrawn, and he like to keep inventory high; (4) during the liability period appellant was purposefully increasing the inventory in anticipation of transferring the business to his sons, and he used funds from a COVID-19 business loan, and perhaps the proceeds from the sale or real estate, to purchase inventory; (5) appellant's prior accountant or CPA came up with the $59,608 beginning and ending inventory amounts reported on the 2018 and 2019 FITRs; (6) Ms. Knox does not know where the accountant got this amount but believes that it may have been from a time when the business was located at a much smaller facility (approximately 25 percent of the size of the current facility); (7) the December 31, 2021 inventory count was probably appellant's first physical inventory, which was completed in two days with the assistance of appellant's son and two unnamed individuals; and (8) Ms. Knox performed another physical inventory in 2023.

OTA does not find Ms. Knox's testimony to be credible. She was appellant's bookkeeper for over 30 years and worked on both of the audits discussed herein. Although Ms. Knox attributes the matching beginning and ending inventory amounts used on the 2018 and 2019 FITRs to a prior accountant, Ms. Knox was appellant's bookkeeper and the person knowledgeable regarding appellant's purchases and sales since long before the prior audit, having begun her employment there circa 1993. During the prior audit, appellant was reporting beginning and ending inventories approximately ten times higher than what he reported for 2018 and 2019.[12] Yet, the changes during those prior audit years (2000 and 2001) represented only 7.7 percent and 3.8 percent, respectively, of the beginning inventory amounts, which is

[12] Beginning inventories for 2000 and 2001 were $596,369 and $550,654, respectively; ending inventories were $550,654 and $529,609, respectively; and the matching beginning and ending inventories reported on appellant's 2018 and 2019 FITRs were $59,608.

consistent with Ms. Knox's testimony that appellant generally tried to replace the inventory that was withdrawn. Ms. Knox's testimony and the other evidence do not explain why the inventory, which she must have reported to the accountant, went from almost $600,000 to less than $60,000. In addition, appellant did not provide credible evidence, such as purchase invoices, to show that the increases in inventory, upon which his argument depends, actually occurred.

OTA is also not persuaded that appellant intentionally tried to increase the inventory during the liability period. Appellant is an experienced business owner. He, and possibly his bookkeeper, must understand that high inventories that do not turn over quickly do not produce income. Inventory produces income only if it is sold or consumed to make something, like one of appellant's custom motorcycles, that is sold. Ms. Knox's explanations – that appellant wanted to turn the business over to his sons with a high inventory and used COVID-19 loan funds (and, perhaps, the proceeds from the sale of real estate) to do that – is not persuasive.[13] Although the amended FITRs show that appellant sold real property during the liability period, appellant has not provided financial documents linking the funds from sale of real property to appellant's business. There is also the matter of how the physical audits were conducted by appellant's long-time bookkeeper, his son, and two other unnamed individuals. There are independent inventory services available. Appellant could have used such a service and called an independent witness to testify regarding the inventory counts. Instead, appellant placed his reliance on the testimony of his long-time bookkeeper. The testimony was unpersuasive.

In addition, OTA notes that the current audit used appellant's own purchase journal to estimate appellant's taxable sales based on the audited markup. Appellant has not expressly contested the accuracy of his own purchase journal. Rather, Ms. Knox's testimony supports the accuracy of the purchase journal (Ms. Knox explained that all of the purchases were recorded in QuickBooks on a monthly basis). This is persuasive evidence against the unsupported inventory counts as well as persuasive evidence against the associated amounts in the amended FITRs. Further, the amended FITRs show additional purchases totaling $30,081 for 2018 and 2019 combined ($35,081 in additional purchases for 2018 and $5,000 fewer purchases for 2019). Thus, the purchase journal and the amended FITRs are in conflict. Since the entries in the purchase journal were made approximately within a month of the actual purchases, OTA gives more weight to the purchase journal. While appellant has submitted detailed schedules, appellant has not provided source documentation for each of the items

[13] Appellant provided no credible evidence to support most of Ms. Knox's testimony.

scheduled and, as previously explained, OTA found that other evidence was entitled to more weight. OTA's examination, however, does not end there.

In response to OTA's inquiry in the Minutes and Orders, CDTFA submitted an additional schedule regarding the markup and underreporting based on the amended FITRs. In contrast, appellant did not respond to the inquiry in his submissions or in oral argument. According to CDTFA's submission, the markups on taxable sales based on the FITRs would be approximately 19 percent for 2018, zero percent for 2019, 1.9 percent for 2020, and approximately 0 percent for 2021 for a combined markup of 2.75 percent for the period. These markups are each substantially less than the achieved markup CDTFA calculated during the shelf test. Regarding the low markup, a lower markup would be expected during a period in which inventory was being increased for appellant's purported purpose, but appellant has not substantiated the infusion of capital with documentary evidence. Even when considering appellant's unsubstantiated purpose of increasing inventory for the future transfer of the business, OTA finds the markups based on the amended FITRs to be unreasonably low. Moreover, appellant's FITRs do not support appellant's argument that the SUTRs are accurate because they show that appellant reported more gross receipts on the FITRs than on the SUTRs, approximately 14 percent ($922,682 ÷ $1,067,486).

In light of all of the above, OTA finds that appellant has not established that adjustments are warranted.

Issue 2: Whether the negligence penalty was properly imposed, and if it was, whether there is any basis for granting relief.

Generally, if any part of a liability for which a deficiency determination is made is due to negligence, respondent must add a penalty equal to 10 percent of the determined tax deficiency. (R&TC, § 6484.) Although the term "negligence" is not specifically defined in the Sales and Use Tax Law, it is a common legal concept and is generally defined in this context as a failure to act as a reasonably prudent person would have acted under similar circumstances. (*Warner v. Santa Catalina Island Co.* (1955) 44 Cal.2d. 310, 317; *Acqua Vista Homeowners Assn. v. MWI, Inc.* (2017) 7 Cal.App.5th 1129, 1157-1158.)

A taxpayer must maintain and make available for examination on request by respondent all records necessary to determine the correct tax liability under the Sales and Use Tax Law and all records necessary for the proper completion of the returns. (R&TC, §§ 7053, 7054; Cal. Code Regs., tit. 18, § 1698(b)(1).) Such records include, but are not limited to, the following: (1) the normal books of account ordinarily maintained by the average prudent

businessperson engaged in the activity in question; (2) bills, receipts, invoices, cash register tapes, or other documents of original entry; and (3) schedules or working papers used in connection with the preparation of the tax returns. (Cal. Code Regs., tit. 18, § 1698(b)(1).) Failure to maintain and provide accurate records is evidence of negligence and may result in imposition of a negligence penalty. (Cal. Code Regs., tit. 18, § 1698(k).) The court in *Independent Iron Works, Inc. v. State Board of Equalization* ((1959) 167 Cal.App.2d 318, 323), held that a negligence penalty is warranted where the same or similar errors are continued from one audit to the next.

Appellant contends that the imposition of the negligence penalty was not warranted because the SUTRs were accurate. As such, appellant's position is that the tax liability should be reduced to zero with a corresponding reduction to the negligence penalty.

Here, CDTFA imposed the negligence penalty because appellant had been previously audited, and appellant reported less taxable sales than taxable purchases, so the audited taxable sales were projected based on the marking up taxable purchases; the high percentage of error when compared to reported taxable sales appellant had additional knowledge of his record keeping and reporting requirement, and the negative markups demonstrated incomplete recording of sales and purchases.

In the prior audit, CDTFA established an initial error ratio of 400 percent, which was later reduced in the reaudit to 339 percent. After the reaudit, CDTFA determined tax of $305,292.13, plus applicable interest, and imposed a negligence penalty based on the lack of records on the sales of motorcycles (e.g., sales invoices, sales contracts, and ROS). The current audit still pertains to taxable sales, but is focused on the retail sale of parts, apparel, and accessories.

During the current audit, the records were not sufficient for a direct audit, and appellant described his inventory records as poor despite operating for more than 20 years.[14] While record keeping dramatically improved between the prior audit and current audit, the error rate of 87 percent ($339,302 unreported taxable sales ÷ 388,840 reported taxable sales = 0.872) together with the understated measure is evidence of negligence. This shows that, despite the knowledge gained from operating the business long term and the knowledge gained from going through a prior audit (or possibly three prior audits), that similar errors occurred from one audit to the next. Accordingly, OTA finds that appellant was negligent, and the negligence penalty was properly imposed.

[14] Appellant indicated that the business has been operating since the early 1970s. The business was previously categorized as a partnership.

Issue 3: Whether the finality penalty was properly imposed, and, if it was, whether there is any basis for granting relief.

R&TC section 6565 provides that a determination is due and payable at the time the determination becomes final. If the determination is not paid when due, a penalty of 10 percent of the determination, exclusive of interest and penalties, shall be added thereto. (R&TC, § 6565.) Here, CDTFA issued the Notice of Redetermination on September 22, 2022. The NOD became final on October 24, 2022.[15] Thus, the penalty was properly imposed. Appellant has not argued otherwise.[16] While the finality penalty can be relieved pursuant to R&TC section 6592, appellant has not requested such relief, and OTA finds that there is no basis for granting relief.

During the oral hearing, CDTFA agreed to waive the finality penalty if appellant pays the liability within thirty days of respondent's issuance of a Notice of Redetermination after this Opinion is final.

Issue 4: Whether the collection cost recovery fee (CCRF) was properly imposed, and, if it was, whether there is any basis for granting relief.

A CCRF is imposed on any person who fails to pay an amount of tax, interest, penalty, or other amount due and payable under the Sales and Use Tax Law. (R&TC, § 6833(a).) The CCRF shall be imposed only if CDTFA has mailed its demand notice to the person for payment, advising that continued failure to pay the amount due may result in collection action, including the imposition of a CCRF. (R&TC, § 6833(a).)

If a person's failure to pay any amount under the Sales and Use Tax Law is due to reasonable cause and circumstances beyond the person's control, and occurred notwithstanding the exercise of ordinary care and the absence of willful neglect, the person shall be relieved of the CCRF. (R&TC, § 6833(d)(1).) To be relieved of the CCRF, appellants must file a statement under penalty of perjury setting forth the facts upon which the person bases the claim for relief. (R&TC, § 6833(d)(2).)

According to CDTFA, it issued the Demand Notice on October 25, 2022, which set forth a ninety-day deadline, January 23, 2023, to pay. Since the ninety-day deadline lapsed and the liability remained unpaid, CDTFA issued a Notice of Collection Recovery Fee, assessing a

[15] Generally, NODs become due and payable 30 days after they are issued. Here, the 30th day fell on a Saturday, which extended the date that the NOD became due and payable to the following Monday.

[16] Appellant's argument against penalties is that there is no tax liability, so no penalty due.

CCRF of $570. Appellant makes no argument, specific or otherwise, with respect to the imposition of the CCRF. Further, appellant has not submitted a statement under penalty of perjury that complies with R&TC, section 6833(d)(2). Therefore, OTA finds that the CCRF was correctly imposed, and there is no basis for granting relief.

HOLDINGS

1. No adjustments to the measure of unreported taxable sales are warranted.
2. The negligence penalty was properly imposed.
3. The finality penalty was properly imposed, and there is no basis upon which to grant relief.
4. The collection cost recovery fee (CCRF) was properly imposed, and there is no basis upon which to grant relief.

DISPOSITION

CDTFA's action denying the claim for refund is sustained.

DocuSigned by:
Josh Aldrich
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Josh Aldrich
Administrative Law Judge

We concur:

DocuSigned by:
Michael F. Geary
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Michael F. Geary
Administrative Law Judge

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

Date Issued: 10/15/2025