

1 review of additional evidence provided by petitioner and the Department's response to the material
2 provided, we now recommend a reduction of the tax to \$129,145.80 and an adjustment of the interest,
3 through March 31, 2014, to \$74,006.37 (with interest continuing to accrue each month until the
4 determined tax is paid in full), as discussed under Post Hearing Developments.

5 **UNRESOLVED ISSUES**

6 **Issue 1:** Whether adjustments are warranted to the unreported sales. We find no further
7 adjustment is warranted other than the post-hearing adjustments.

8 Petitioner has operated a gasoline station with a mini-mart since October 1997. Petitioner is a
9 corporation whose sole shareholder was Rakesh Bhakta until December 31, 2007, when he sold all his
10 stock to Bhupinder Singh Mac. For audit, petitioner provided monthly Point of Sale reports from
11 Mobil Oil for 2006; sales summary worksheets for the period January 1, 2006, through March 31,
12 2008; income statements and gasoline purchase invoices for 2006 and 2007; and federal income tax
13 returns for 2005, 2006, and 2007. The Department found significant differences between recorded and
14 reported taxable sales, which it used to establish an understatement of \$2,853,600, which petitioner
15 does not protest. Based on various audit tests, the Department concluded that recorded taxable sales
16 for 2006 were substantially accurate. However, since petitioner provided almost no records for 2005
17 and the Department computed a negative book markup for gasoline for 2007, the Department decided
18 to use alternate audit methods to establish audited taxable sales for the period April 1, 2005, through
19 December 31, 2005, and for the year 2007.

20 For 2005, the Department established audited sales of gasoline using gallons of gasoline
21 purchased (computed using vendors' reports of sales tax prepayments paid by petitioner) and selling
22 prices published on GasBuddy.com for regular grade gasoline, adjusted by 102 percent (computed
23 from petitioner's records for 2006) for higher prices for mid-grade and premium gasoline. To establish
24 audited taxable mini-mart sales for the period April 1, 2005, through December 31, 2005, the
25 Department used recorded taxable mini-mart sales for the corresponding period of 2006. The
26 Department totaled audited gasoline sales and audited taxable mini-mart sales for the period April 1,
27 2005, through December 31, 2005, and computed that reported taxable sales for that period were
28 understated by \$458,164.

1 For 2007, the Department established audited gasoline sales on a markup basis, using the book
2 markup of 5.24 percent that it had computed for 2006 and audited purchases of fuel for 2007. We
3 found errors in the Department's computation of the book markup for 2006, and we recomputed it at
4 5.02 percent. Thus, we recommended that audited gasoline sales for 2007 be recomputed using
5 5.02 percent. After that adjustment, the understatement of reported gasoline sales for 2007 was
6 \$339,928 at the time the hearing was held. As explained under Post Hearing Developments, we
7 recommend further reductions of \$8,132 and \$52,066, to \$279,730.

8 Petitioner contends that it sold fuel for prices below the industry average selling price in the
9 second and third quarters of 2005 in order to attract customers while the mini-mart was under
10 construction. Petitioner further asserts that gasoline prices remained drastically reduced during the last
11 quarter of 2005. Petitioner also contends that the recorded gasoline sales for 2007 are correct,
12 asserting that it inadvertently sold gasoline below cost because it had changed vendors, and it was
13 confused by the invoices provided by the new vendor, such that it used incorrect gasoline costs when it
14 computed the selling prices. In addition, petitioner alleges that, in anticipation of the sale of the
15 business, it was more concerned about the volume of sales than the net profit in 2007. Further,
16 Mr. Mac states that he was effectively forced to purchase the stock of the business on January 1, 2008,
17 to prevent a default on Mr. Bhakta's loan (which Mr. Mac had personally guaranteed). When he made
18 the decision to purchase the corporate stock, Mr. Mac states that he did not review the books and
19 records but considered only the volume of gasoline purchases.

20 Petitioner did not provide records for 2005 (other than the federal tax return), and it has not
21 provided documentation to show that gasoline was sold below the average industry price during the
22 last three quarters of 2005. Accordingly, we find no adjustment of the audited selling prices for 2005
23 is warranted. Regarding the selling prices in 2007, petitioner has provided copies of invoices from the
24 "new" vendor and from the vendor from whom it previously purchased gasoline, in an attempt to
25 demonstrate that the invoices issued by the new vendor were confusing. While it is true that one
26 vendor combined the state and federal taxes with the base price of fuel as one line item, and the
27 previous vendor separately stated the state and federal taxes, we are not persuaded that, as a result,
28 petitioner was unable to understand the pricing schedule and therefore inadvertently computed selling

1 prices below cost. Petitioner has provided no convincing evidence that it sold gasoline at prices below
2 cost in 2007. We find it was reasonable for the Department to use the markup of 1.77 percent,
3 computed from additional documentation provided by petitioner after the Board hearing, for February
4 2007, and (as discussed below in Post Hearing Developments) to use an average of 3.39 percent
5 (computed using 1.77 percent and the book markup for 2006 of 5.02 percent) to compute sales for the
6 remainder of 2007. Petitioner has not provided evidence sufficient to support further adjustment.

7 **Issue 2:** Whether petitioner was negligent. We conclude that it was.

8 The Department imposed the negligence penalty because petitioner provided inadequate
9 records and the understatement was significant. Petitioner has not offered a non-negligent explanation
10 for the understatements established by audit, but Mr. Mac states that the business is currently
11 struggling with the mistakes of the prior management, which have been corrected beginning with
12 returns filed for the first quarter 2008.

13 The Department found that petitioner had recorded taxable sales of \$2,853,600 that it did not
14 report, and petitioner does not dispute that audit item. In addition, petitioner did not provide any
15 records for 2005 other than the federal tax return. We find that any businessperson, even one with
16 limited experience, should have recognized a difference of almost \$3 million between recorded and
17 reported taxable sales. We find that the substantial error and the incomplete records are clear evidence
18 of negligence, even though petitioner had not been audited previously. Further, while it is true that the
19 Department found the reported sales for the first quarter 2008 to be substantially correct, that improved
20 reporting does not alter the fact that, during the audit period, petitioner was negligent. We conclude
21 that the penalty was properly imposed.

22 **POST HEARING DEVELOPMENTS**

23 Petitioner argues that the selling prices used to compute audited gasoline sales for 2005 and the
24 markup used to compute audited gasoline sales for 2007 are too high, that relief of interest is
25 warranted, and that the negligence penalty should be deleted. As support, petitioner provided several
26 exhibits, both at and after the Board hearing, and after the Board considered this matter on the
27 adjudicatory calendar in December 2013. We address each issue below.

1 Regarding 2005 gasoline sales, the Department has explained that it used selling prices
2 published in GasBuddy.com to establish audited sales of gasoline for 2005. Although petitioner asserts
3 that its selling prices were lower than average for 2005, it has provided no documentation to support
4 that assertion. Also, as noted by the Department, selling prices published in GasBuddy.com were used
5 to verify recorded gasoline sales for 2006, which the Department concluded were substantially
6 accurate. Since the evidence shows that petitioner's selling prices for gasoline were consistent with
7 industry average selling prices for 2006, and petitioner has not documented that its selling prices were
8 lower than average in 2005, we recommend no adjustment to audited sales of gasoline for 2005.

9 For 2007 gasoline sales, the Department had used petitioner's book markup for 2006 to
10 compute audited gasoline sales. We found that approach reasonable. However, for the month of
11 February, petitioner provided screen shots from GasBuddy.com and evidence of its recorded costs of
12 gasoline to show that the markup was 1.77 percent for that month. Based on its review of information
13 and arguments provided by petitioner since the December 2013 Board meeting, the Department now
14 recommends that the markup for the remainder of 2007 be reduced to 3.39 percent (the average of 1.77
15 percent and the book markup for 2006, 5.02 percent). The reduction of the markup for February 2007,
16 but not for the remainder of the year, reduced the understatement for 2007 by \$8,132, from \$339,928
17 to \$331,796. The recent reduction of the markup for the remainder of the year to 3.39 percent resulted
18 in an additional reduction of \$52,066, to \$279,730.

19 Petitioner continues to argue that its sales summaries for 2007 are accurate. However, those
20 sales summaries reflect negative markups for that entire year, including a negative markup of 4.22
21 percent for February 2007. Since the Department has used selling prices from Gasbuddy.com, which
22 were provided by petitioner, to compute a markup for February 2007 of 1.77 percent, we find that the
23 negative book markup is evidence that the sales summaries are inaccurate or incomplete. We have
24 persistently requested that petitioner provide any other evidence of its actual sales prices for gasoline
25 in 2007, such as original POS tapes, but petitioner states that it is unable to provide any additional
26 information. Accordingly, we recommend no further adjustment to the audited fuel sales.

27 Regarding 2005 mini-mart sales, we note that in recent discussions with the Department and
28 the Appeals Division, petitioner has argued that there were no taxable mini-mart sales in 2005, arguing

1 that prior to 2005 petitioner only had a small kiosk from which to make mini-mart sales, and that
2 construction of a mini-mart on the premises began in 2005, during which time petitioner was unable to
3 make food sales.¹ Petitioner states that it cannot recall the date on which the construction was
4 completed, but believes it was in 2006, even though property tax records from the Orange County
5 Assessor reflect a completion date in the fourth quarter 2007.²

6 Preliminarily we note that petitioner has claimed exempt food sales since 1997, and petitioner
7 listed “mini-mart” on its sales and use tax application, with a start date of October 3, 1997. Next, our
8 review of petitioner’s sales and use tax returns for the subject periods indicates that petitioner claimed
9 exempt sales of food of \$103,174 for 2005 and \$223,130 for 2006. It then claimed food deductions for
10 the four quarters of 2007 of \$3,048, \$9,191, \$6,272, and \$50,034. The significant decrease in claimed
11 food deductions for the first three quarters of 2007 strongly suggests that construction occurred during
12 this period, since petitioner asserts it could not sell food items during the construction. The sharp
13 increase in claimed food deductions in the fourth quarter 2007 (reflecting increased food sales)
14 corresponds with the apparent date of completion of construction of the mini-mart according to the
15 records of the Orange County Assessor. In other words, petitioner’s claimed food sale deductions
16 show consistent, continued food sales throughout 2005, and that any cessation or reduction of food
17 sales due to construction apparently occurred in 2007.³ Thus, we find that the evidence shows
18 petitioner was making mini-mart sales during 2005, and we find no basis for adjustment of the audited
19 taxable mini-mart sales.

20 Regarding the request for interest relief, we note that petitioner had asserted at the Board
21 hearing that the amount of interest through July 31, 2013, had been computed incorrectly. The

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23 ¹ Petitioner states that during construction it made sales from a small table located in one of petitioner’s repair bays, and
could not sell food products due to health code requirements for facilities from which food items are sold.

24 ² Petitioner asserts that paperwork for the permitting and approval of the construction project was not complete until more
than one year after the work was physically complete.

25 ³ During our March 4, 2014 meeting, petitioner suggested that the claimed food sale deductions in 2005 may have actually
26 been nontaxable sales such as lottery sales, check cashing, and money orders; however, petitioner has provided no evidence
to corroborate the suggestion. Our review of the sales and use tax returns for 2005 indicates that petitioner claimed both
27 food sale deductions as well as deductions for “other” in consistent amounts for each quarter of 2005, except for 4Q05
when petitioner did not claim any deductions for “other.” Petitioner specified “other” as “Lotto” for 1Q05. Accordingly
28 we find that the available evidence does not suggest that the claimed food sale deductions in 2005 consist of other
nontaxable sales.

1 Department has recomputed the amount of interest, which resulted in a reduction of about \$42,000.
2 Petitioner now agrees that the interest is correctly computed. However, petitioner now argues that
3 relief of interest should be granted because of an unreasonable delay by a Board employee.⁴ On this
4 issue, we first note that relief of interest would be applicable only to the amount of tax related to
5 disputed understatements. In this case, the total understatement of reported taxable measure is
6 \$3,591,494, and \$2,853,600 of that amount represents a difference between recorded and reported
7 taxable sales, which is not disputed. In other words, the disputed tax amount which may be eligible for
8 consideration of interest relief is measured by \$737,894 (\$3,591,194 - \$2,853,600).

9 Petitioner has not identified the periods for which it asserts that there were unreasonable delays
10 or described the types of delays it argues were unreasonable. Instead, petitioner asserts that the
11 Department willfully assessed too much tax for the years 2005 and 2007; that its settlement offer was
12 rejected without consideration; that the Board could not reach a decision at the July 2013 hearing and
13 instead ordered a 30-30-30; and that the Department's assessment of the tax liability has penalized
14 petitioner. Here, petitioner failed to provide any records for its sales in 2005, and did not provide
15 reliable sales records for gasoline sales for 2007, thus increasing the complexity of the audit and
16 contributing to any alleged delay during the audit. Further, neither the failure to accept a settlement
17 proposal, nor the Board's votes to allow additional time for the submission of additional evidence
18 (which *have* resulted in reductions to the disputed measure of tax in this matter) are unreasonable
19 delays. Accordingly, based on our review of the record, we find no evidence of unreasonable delay
20 that warrants relief of interest.

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23 ⁴ Revenue and Taxation Code section 6482 provides that the amount of a deficiency determination shall bear interest from
24 the last day of the month following the quarterly period for which the amount or any portion thereof should have been
25 returned until the date of payment. (Rev. & Tax. Code, § 6482.) The imposition of interest is mandatory, and interest may
26 be relieved only under limited circumstances, such as an unreasonable error or delay by an employee of the board acting in
27 his or her official capacity. (Rev. & Tax. Code, §§ 6482, 6593.5, subd. (a).) To be eligible for relief based on Revenue and
28 Taxation Code section 6593.5, no significant aspect of the error or delay can be attributed to an act or failure to act by
petitioner. (Rev. & Tax. Code, § 6593.5, subd. (b).) A person seeking relief of interest must file with the Board a statement
under penalty of perjury setting forth the facts upon which he or she bases his or her claim for relief and any other
information the Board may require. (Rev. & Tax. Code, § 6593.5, subd. (c).) Petitioner has filed the requisite statement in
this matter.

1 Finally, petitioner continues to dispute the negligence penalty. However, as explained in the
2 Board hearing summary, petitioner had recorded taxable sales of almost \$3 million in its own records
3 that it did not report (and does not dispute on appeal). We find that this substantial difference between
4 recorded and recorded taxable sales is clear evidence of negligence. In addition, petitioner reported
5 taxable sales of \$5,908,378, and the total understatement, after the most recent revisions, is
6 \$3,591,494, reflecting an error ratio of 60.8 percent ($\$3,591,494 / \$5,908,378$). This substantial error
7 ratio is additional evidence of negligence. Finally, petitioner failed to provide adequate records for the
8 audit period. Accordingly, our conclusion remains that the negligence penalty was properly applied.

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10 Summary prepared by Deborah A. Cumins, Business Taxes Specialist III

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28**MARKUP TABLE
(Gasoline sales for 2007)**

Taxable vs. nontaxable purchases	100%
Book mark-up for 2006 applied to purchases for 2007, except February	5.02%
Book markup applied to purchases for February 2007	1.77%
Self-consumption allowed in dollars	None*
Pilferage allowed in dollars	None*

* The book markup incorporates any reductions to cost of goods sold for self-consumption or pilferage.