CALIFORNIA STATE BOARD OF EQUALIZATION

APPEALS DIVISION BOARD HEARING SUMMARY

In the Matter of the Administrative Protest Under the Sales and Use Tax Law of: RAFAEL NAVARRO MARTINEZ, dba Sinaloence #02 Taxpayer	Account Number SR AP 100-619680 Case ID 587802 Los Angeles, Los Angeles County

Type of Business: Catering truck

Liability period: 07/01/07 - 06/30/10

Item	Disputed Amount
Unreported taxable sales	$242,670[1]
Negligence penalty	$ 2,128
Finality penalty	$ 1,928

	Tax	Penalty
As determined and protested	$21,281.99	$2,128.24
Finality penalty	0.00	1,928.20
Balance	$21,281.99	$4,056.44

Proposed tax redetermination	$21,281.99
Interest through 2/28/13	5,392.37
Negligence penalty	2,128.24
Finality penalty	1,928.20
Total tax, interest, and penalty	$30,730.80
Less payments	-11,399.00
Balance Due	$19,331.80
Monthly interest beginning 3/1/13	$ 49.41

A Notice of Appeals Conference was mailed to taxpayer at his addresses of record and to taxpayer's representative, and the notices were not returned by the Post Office. Taxpayer did not respond to the notice or appear at the appeals conference, which was held as scheduled. We thereafter sent letters to taxpayer and his representative offering taxpayer the opportunity to provide any additional arguments and evidence in writing he wished us to consider, but the letter sent to taxpayer's

[1] Taxpayer disputes a portion of the unreported taxable sales, but has not identified the amount with which he concurs. Therefore, we show the entire amount as disputed.

representative was returned as undeliverable and, while the letter sent to taxpayer was not returned by the Post Office, taxpayer did not respond.

UNRESOLVED ISSUES

Issue 1: Whether any adjustments are warranted to the amount of unreported taxable sales. We find no adjustments are warranted.

Taxpayer has operated a catering truck making taxable sales of Mexican-style food and beverages from a single location since May 2002. When asked how he prepared his sales and use tax returns, taxpayer told the Sales and Use Tax Department (Department) that he provided purchase totals to an outside accountant who computed his sales by marking up the purchases by 200 percent. The Department compared taxable sales reported on taxpayer's sales and use tax returns with the cost of goods sold reported on his federal income tax returns and calculated book markups of 124 percent for 2007 and 120 percent for 2008, which were lower than expected. After finding that taxpayer's bank deposits substantially exceeded his reported sales, the Department concluded that taxpayer had understated his reported sales. Initially, the Department attempted to establish audited taxable sales based on a markup analysis but found that the purchase information available was insufficient to reliably establish audited costs of goods sold. Therefore, the Department decided to establish audited taxable sales based on a site observation test.

On Thursday, October 28, 2010, the Department observed taxpayer making taxable sales of $451. Taxpayer objected to the use of a single day's taxable sales to establish audited taxable sales for the audit period. Accordingly, the Department asked taxpayer to record his daily taxable sales and maintain corresponding purchase invoices for a three-week period from April 25, 2011, through May 13, 2011. On Tuesday, May 3, 2011, the Department also performed a second site observation test. At the end of the three-week period, the Department compared taxable sales of $4,971 recorded by the taxpayer on daily sales worksheets with food purchases of $1,847 shown in the purchase invoices that taxpayer provided for the test period to compute a markup of 169 percent, which the Department considered to be reasonable. Also, the Department noted that taxpayer's recorded taxable sales of $319 for May 3, 2011, were comparable to taxable sales of $333 that the Department had observed on that day. Thus, the Department concluded that taxpayer's recorded taxable sales for the three-week test period were reasonable, consistent, and complete.

The Department combined the results of the first site observation test with the results of the three-week test, and computed average daily taxable sales, excluding sales tax reimbursement, of $339. Based on 242 operating days per year ((52 weeks × 5 days per week) – 8 holidays – 10 estimated rainy days), the Department computed audited taxable sales for a year of $82,038 ($339 × 242 days). A comparison of audited taxable sales of $82,038 with reported taxable sales of $12,907 for the last year of the audit period showed unreported taxable sales of $69,131, and an error rate of 536 percent, which the Department used to compute unreported taxable sales of $242,670 for the audit period.

Taxpayer concedes an understatement exists but contends the audit computations fail to take into consideration external factors such as closures on rainy days. Taxpayer asserts that his average daily sales are $390 per day, which is confusing since the audit results show lower average daily taxable sales of $339. However, since taxpayer did not appear at the conference or respond to our post-conference letter, we have no other information regarding taxpayer's dispute. Since the Department did make an adjustment to account for closures on rainy days (10 days per year), we reject taxpayer's argument that the Department did not do so, and find that there is no other basis on which to recommend any reductions to the measure of tax.

Issue 2: Whether taxpayer was negligent. We conclude that he was.

The Department imposed the negligence penalty because the understatement is substantial and taxpayer failed to provide adequate records. The taxable sales understatement of $242,670 represents an error ratio of 535.61 percent when compared to reported taxable sales of $45,307. We find that the large error ratio is strong evidence of negligence in reporting. Since taxpayer did not provide for audit any summary records, such as sales and purchases journals, or any source documentation other than purchase invoices, which were found to be incomplete, we find that taxpayer also was negligent in recordkeeping. Taxpayer has not raised any specific contentions regarding the issue of negligence. Although this was taxpayer's first audit, we conclude that any taxpayer, even one with limited experience, should have recognized errors of this magnitude. Thus, we find the penalty was properly applied.

OTHER MATTERS

Since taxpayer did not pay the tax portion of the determination in full by August 25, 2011, the date the determination became final, a finality penalty in the amount of $1,928.20 was added to the liability. Although we informed taxpayer in our post-conference letter that he could file a request for relief of the finality penalty, and attached a form he could use to do so, he has not filed a request for relief. Therefore, we have no basis on which to consider recommending relief of the finality penalty.

Summary prepared by Lisa Burke, Business Taxes Specialist III