

1 CALIFORNIA STATE BOARD OF EQUALIZATION

2 APPEALS DIVISION BOARD HEARING SUMMARY

3 In the Matter of the Petition for Redetermination)
 4 Under the Sales and Use Tax Law of:)
 5 NNADI LINUS UDENGWU,) Account Number: SR AP 97-031177
 dba Ude Auto Sales) Case ID 515515
 6)
 7 Petitioner) Diamond Bar, Los Angeles County

8 Type of Business: Used car dealer

9 Audit period: 4/1/05 – 6/30/08

10 <u>Item</u>	<u>Disputed Amounts</u>
11 Unreported sales	\$2,317,144
12 Disallowed claimed exempt sales	\$82,581
13 Negligence penalty	\$19,798

	<u>Tax</u>	<u>Penalty</u>
14 As determined	\$264,349.22	\$26,434.96
15 Adjustment - Sales and Use Tax Department	- 66,371.84	- 6,637.17
Proposed redetermination, protested	<u>\$197,977.38</u>	<u>\$19,797.79</u>
16 Proposed tax redetermination	\$197,977.38	
17 Interest through 2/29/12	81,816.34	
Negligence penalty	<u>19,797.79</u>	
18 Total tax, interest, and penalty	<u>\$299,591.51</u>	
19 Monthly interest beginning 3/1/12	<u>\$1,154.87</u>	

20 UNRESOLVED ISSUES

21 **Issue 1:** Whether petitioner has established that the audited measure of tax liability includes
 22 nontaxable sales for resale or exempt sales in foreign commerce. We conclude that he has not.

23 Petitioner is a used car dealer who does not maintain a car lot to display his inventory. He
 24 purchases his cars from local auto auctions and usually sells them within days. Upon audit, petitioner
 25 only provided federal income tax returns for 2006 and 2007. He did not maintain sales journals,
 26 contracts, or summary worksheets, and his Department of Motor Vehicle report of sale forms and
 27 purchase invoices were grossly incomplete. The Sales and Use Tax Department (Department) was
 28 unable to reconcile the sales reported on the sales and use tax returns with the gross receipts reported

1 on the federal returns and thus concluded that the reported sales were unreliable. The Department
2 established petitioner's sales by the markup method. It conducted a shelf test using 17 cars from the
3 audit period for which there was sufficient information, and compared Kelly Blue Book selling prices
4 to the purchase prices to calculate a 33.38 percent average markup, and applied the markup to the
5 \$2,732,590 worth of cars (represented by over 240 cars) that petitioner's vendors reported as having
6 sold to petitioner during the audit period. The Department computed total sales of \$3,644,727,
7 resulting in \$2,317,144 unreported sales, all of which the Department regarded as taxable. Petitioner
8 had reported total sales of \$1,327,583, all of which he claimed as nontaxable sales for resale. The
9 Department reviewed the bills of lading provided in support of these claimed nontaxable sales, and
10 determined that sales of \$1,245,002 (78 sales of cars) qualified as exempt sales (they had been shipped
11 to Nigeria) and that \$82,581 of the claimed amount was not supported as nontaxable. Petitioner
12 contends that all of his sales were nontaxable sales for resale or exempt sales in foreign commerce.

13 We note that the claimed sales for resale to Clem's Auto Sales are not supported by a valid
14 resale certificate or a signed XYZ letter confirming sales for resale, and that the dates of shipment on
15 12 bills of lading precede the dates that the vendors reported selling those cars to petitioner. Therefore,
16 we find the Department correctly disallowed the claimed deductions as to those sales. Further, the
17 vehicle identification numbers on three bills of lading could not be traced to purchase information in
18 the audit, and therefore do not support exemption for any of the assessed sales. We thus find that no
19 further adjustment is warranted.

20 **Issue 2:** Whether petitioner was negligent. We conclude that he was.

21 The Department found petitioner to be negligent because it considered petitioner's books and
22 records inadequate for sales and use tax purposes, petitioner failed to maintain resale certificates or
23 bills of lading to support his claimed nontaxable sales, and there is a substantial deficiency. Petitioner
24 contends that he did not make any taxable retail sales and disagrees with the negligence penalty.

25 Petitioner's belief that all of his sales were nontaxable or exempt is not a sufficient reason for
26 failing to report his sales. The amount established for unreported sales of \$2,317,144 represents a
27 175 percent error rate in reported total sales. We find that such a substantial amount of unreported
28 sales is evidence of negligence in reporting. Petitioner's failure to maintain sales journals, contracts,

1 summary worksheets, and documentation to support his claimed nontaxable and exempt sales, are
2 actions contrary to what we expect from a reasonably prudent businessperson. In addition, we find that
3 the incomplete condition of petitioner's report of sale forms and purchase invoices is compelling
4 evidence of negligence in recordkeeping. Accordingly, we conclude that petitioner was negligent.

5 **OTHER DEVELOPMENTS**

6 None.

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8 Summary prepared by Pete Lee, Business Taxes Specialist II
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MARKUP TABLE

Percentage of taxable vs. nontaxable purchases	66% taxable 34% nontaxable
Mark-up percentages developed	33.38%
Self-consumption allowed in dollars	\$0
Self-consumption allowed as a percent of taxable purchases	0%
Pilferage allowed in dollars	\$0
Pilferage allowed as a percent of taxable purchases	0%