

1 CALIFORNIA STATE BOARD OF EQUALIZATION

2 APPEALS DIVISION BOARD HEARING SUMMARY

3 In the Matter of the Petitions for Redetermination)
 4 Under the Sales and Use Tax Law of:)
 5 JOSE AGUSTIN FERNANDEZ,) Account Number: SR AR 97-911585
 6 dba J & S Auto Sales) Case IDs 549411 and 553265
 7 Petitioner) Ventura, Ventura County)

7 Type of Business: Used car dealer

8 Audit period: 1/1/06 – 05/30/10

9 <u>Item</u>	<u>Disputed Amounts</u>	
10 Unreported sales based on vehicle inventory reports		\$897,361
11 Unreported sales based on Report of Sale (ROS) forms		\$476,967
12 Negligence penalty		\$ 10,305

	<u>549411</u>		<u>553265</u>	
	<u>1/1/06 – 6/30/07</u>		<u>7/1/07 – 5/30/10</u>	
	<u>Tax</u>	<u>Penalty</u>	<u>Tax</u>	<u>Penalty</u>
15 As determined	\$34,942.02	\$3,494.21	\$91,536.67	\$9,153.67
16 Pre-D&R adjustments	+32,353.78	+3,235.36	00.00	00.00
17 Post-D&R adjustments	<u>-22,581.20</u>	<u>-2,258.10</u>	<u>-33,198.86</u>	<u>-3,319.88</u>
18 Proposed redetermination	\$44,714.60	\$4,471.47	\$58,337.81	\$5,833.79
19 Less concurred	<u>- 225.69</u>	<u>00.00</u>	<u>- 409.12</u>	<u>00.00</u>
20 Proposed redetermination, protested	<u>\$44,488.91</u>	<u>\$4,471.47</u>	<u>\$57,928.69</u>	<u>\$5,833.79</u>
21 Proposed tax redetermination	\$44,714.60		\$58,337.81	
22 Interest through 07/31/13	22,616.12		18,452.60	
23 Negligence penalty	<u>4,471.47</u>		<u>5,833.79</u>	
24 Total tax, interest, and penalty	\$71,802.19		\$82,624.20	
25 Payments	<u>- 1,000.00</u>		<u>0.00</u>	
26 Balance Due	<u>\$70,802.19</u>		<u>\$82,624.20</u>	

27 Monthly interest beginning 08/01/13 \$218.57 \$291.69

28 This matter was scheduled for Board hearing in April 2013, but petitioner waived his
 appearance at the hearing and the matter was scheduled for decision on the nonappearance calendar.
 However, petitioner subsequently stated that he had waived appearance at the hearing in error.

UNRESOLVED ISSUES

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2 **Issue 1:** Whether additional adjustments are warranted to the measure of unreported taxable
3 sales calculated from vehicle inventory reports or to the measure of unreported taxable sales calculated
4 based on missing ROS forms. We recommend no additional adjustments to either measure of tax.

5 Petitioner operated a used car dealership in Oxnard from 2001 through 2008, and then moved
6 the dealership to Ventura, where he operated it until he discontinued the business in May 2010. The
7 Department compared petitioner's reported total sales for the years 2006 through 2009 with the costs
8 of goods sold recorded on vehicle inventory reports for the same years, and computed an average book
9 markup of 16 percent, which was much lower than the average markup the Department expected for
10 this business (30 – 70 percent). The Department decided to compute petitioner's sales using sales
11 contracts, vehicle inventory reports, and ROS forms. However, in order to prevent the statute of
12 limitations for issuing a determination from expiring before the Department had completed its
13 investigation, the Department issued a determination for the period January 1, 2006, through June 30,
14 2007, based on estimated unreported taxable sales of \$481,959 for that period (Case 549411).

15 Based on a comparison of petitioner's recorded and reported taxable sales, the Department
16 established a deficiency measure of \$8,072 for the difference. To establish the understatement of
17 recorded taxable sales, the Department first examined 78 randomly-selected sales contracts from
18 periods spread throughout the audit period and computed an average vehicle sale price of \$6,187. The
19 Department then compiled a total of 452 vehicles from petitioner's vehicle inventory reports for
20 periods through September 30, 2009, and multiplied the 452 vehicles by the average vehicle sale price
21 of \$6,187 to establish audited taxable sales of \$2,796,524 for periods through September 30, 2009,
22 which exceeded reported taxable sales for those periods by \$897,361. Based on information provided
23 by the DMV, the Department compiled 485 ROS forms issued to petitioner during the period
24 January 1, 2007, through July 8, 2009, and then estimated 200 ROS forms for 2006 and 51 ROS forms
25 for the period July 9, 2009, through September 30, 2009. In all, the Department computed 736 ROS
26 forms for periods through September 30, 2009. Based on a prior audit of petitioner in which the
27 Department found that petitioner voided 11.57 percent of his ROS forms, the Department computed 85
28 voided ROS forms for this audit period. The Department then reduced the 736 total ROS forms

1 available by the estimated 85 voided ROS forms and by the 452 vehicle sales accounted for based on
2 vehicle inventory reports to compute 199 ROS forms that represented unrecorded sales of vehicles.
3 The Department multiplied the average vehicle sale price of \$6,187 by 199 to establish additional
4 taxable sales based on ROS forms of \$1,231,214. The total deficiency measure established in the
5 original audit was \$2,136,647 ($\$8,072 + \$897,361 + \$1,231,214$).

6 Petitioner agrees with the measure of \$8,072 for the difference between recorded and reported
7 taxable sales. However, petitioner contends that audited sales based on vehicle inventory reports are
8 overstated because, according to petitioner, many of the vehicles recorded on his vehicle inventory
9 reports were consigned vehicles that he did not sell, but instead, eventually returned to the consignors.
10 Regarding the sales established based on ROS forms, petitioner asserts that the amount is overstated
11 because he returned 256 ROS forms to the DMV. On that issue, petitioner provided documentation
12 after the appeals conference showing that he had returned 36 ROS forms. Based on this
13 documentation, the Department recommended that the audited measure of \$1,231,214 for unreported
14 sales based on ROS forms be reduced by \$222,732 ($36 \times \$6,187$) to \$1,008,482.

15 Regarding petitioner's contention that his vehicle inventory reports include consigned vehicles
16 that he never sold, we first note that petitioner has provided no documentation to support a reduction.
17 In any event, an adjustment in the number of unreported sales represented by vehicle inventory reports
18 would not alter the overall understatement, which is based on the number of ROS forms, since this
19 number represents the total number of vehicles sold at retail. Thus, any reduction to the measure for
20 unreported sales based on vehicle inventory reports would result in a corresponding increase to the
21 measure for unreported sales based on ROS forms. Therefore, we recommend no adjustment for any
22 consigned vehicles returned to the consignors.

23 Regarding petitioner's claim that he had returned many of the ROS forms that are not
24 accounted for in the audit to the DMV, we note that petitioner has provided documentation to show
25 only that he returned 36 ROS forms to the DMV. However, we have reviewed the prior audit and
26 DMV records, and we compute that there were 672 ROS forms available for petitioner's use during the
27 audit period, rather than the 736 ROS forms used in the audit. We multiplied 672 ROS forms by the
28 void ratio of 11.57 percent to compute 78 voided ROS forms, and then subtracted 78 voided ROS

1 forms and 36 ROS forms returned to the DMV from 672 available ROS forms to compute 558 ROS
2 forms used for retail vehicle sales. Multiplying 558 ROS forms by the average vehicle sale price of
3 \$6,187 results in audited taxable sales of \$3,452,346 for the audit period, which exceeds reported
4 taxable sales of \$2,069,945 by \$1,382,401. In the D&R, we recommended that the total measure of tax
5 be reduced to \$1,390,473 (\$1,382,401 + \$8,072). However, upon our review of this matter in
6 preparation for the Board hearing, we noted that the computations in the D&R compare audited and
7 reported taxable sales. As a result, we found that the deficiency measure of \$8,072 for the difference
8 between recorded and reported taxable sales duplicated audited taxable sales otherwise established and
9 recommended that the measure of \$8,072 be deleted. Upon review of the reaudit prepared pursuant to
10 the D&R, we also noted errors in reallocating a portion of the deficiency measure to sales in the later
11 quarters in the audit period, and recommended that these errors be corrected. The Department made
12 those revisions in a second reaudit that resulted in a total deficiency measure of \$1,382,400.¹

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

14 The Department imposed the negligence penalty due to the inadequacy of petitioner's books
15 and records and because the same types of errors were found in the prior audit. Petitioner contends
16 that he reported all of his sales and therefore the penalty is not applicable.

17 In the prior audit for the period January 1, 2003, through December 31, 2005, the Department
18 found that petitioner's failure to maintain adequate records resulted in his failure to report taxable sales
19 of \$1,794,264. For the audit at issue in this case, the Department found that the same types of errors
20 led to an audited understatement of \$1,382,400, which represents an error rate of 66.8 percent when
21 compared to reported taxable sales of \$2,069,945. We find that petitioner was negligent because he
22 did not correct the errors noted by the Department in the prior audit, and because the magnitude of the
23 reporting error rate constitutes substantial evidence of negligence in reporting.

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27 ¹ Since a portion of the taxable measure was reallocated to the quarters beginning April 1, 2009 in the second reaudit, and
28 the statewide sales tax rate increased from 7.25 percent to 8.25 percent on that date, the understatement of tax and penalty
increased by \$874.87 and \$87.48, respectively, in the second reaudit. However, with respect to accrued interest, the
reallocation of the measure to later quarters in the audit period resulted in a reduction of \$4,136.01 to accrued interest.

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RESOLVED ISSUE

Although petitioner had protested the entire liability, he now agrees with the measure of \$8,072 for the difference between recorded and reported taxable sales. Therefore, we regard that difference as a resolved issue, even though we have recommended deleting the specific audit item since it duplicates audited taxable sales otherwise established.

OTHER MATTERS

None.

Summary prepared by Lisa Burke, Business Taxes Specialist III