CALIFORNIA STATE BOARD OF EQUALIZATION

APPEALS DIVISION BOARD HEARING SUMMARY

In the Matter of the Petition for Redetermination Under the Sales and Use Tax Law of: NABIL ABDO M. ABDULLA & TAHERI M. ALDAFARI, dba Four Star Market Petitioner	Account Number SR CH 97-138720 Case ID 569351 Oakland, Alameda County

Type of Business: Small market

Audit period: 07/01/07 – 06/30/10

Item	Disputed Amount
Partnership liability	$554,082 (measure)

	Tax	Penalty
As determined	$51,717.59	$5,171.74
Post-D&R adjustment	00.00	- 5,171.74
Proposed redetermination, protested	$51,717.59	$ 00.00
Proposed tax redetermination	$51,717.59	
Interest through 03/31/13	13,390.44	
Total tax and interest	$65,108.03	
Monthly interest beginning 04/01/13	$ 258.59	

UNRESOLVED ISSUE

Issue: Whether Mr. Abdulla is jointly and severally liable for petitioner's audit liability as a general partner. We conclude that he is.

Petitioner has operated a small market since September 1997. The Sales and Use Tax Department (Department) conducted a markup audit and established an aggregate deficiency measure of $554,082, comprised of unreported taxable sales of $531,953, unreported cost of self-consumed merchandise of $13,378, and unreported cigarette rebates subject to tax of $8,751. Petitioner has not disputed the audit findings or the audit methodology, and our review of the record discloses no errors or inconsistencies in the Department's audit. Thus, the amount of the audited understatement is not an issue here. However, as explained in more detail below, Mr. Abdulla argues that he was not a partner in the business during the audit period.

As herein relevant, in 1997, Mr. Abdulla and Mr. Aldafari formed a partnership to operate a neighborhood market. Apparently, they operated without a written partnership agreement for several years, until they executed a written partnership agreement on October 7, 2004, outlining the general operation and obligations of the business as well as the general obligations of the individual partners. Specifically, the agreement states that Mr. Abdulla and Mr. Aldafari were both equal partners, but that they would alternate between being a managing partner and merely a silent partner, on a yearly basis. However, there was conflict between the partners regarding the transfer of management, as more fully described in the D&R.

Mr. Abdulla contends that he should not be held liable for petitioner's deficiency measure because Mr. Aldafari was in complete control and possession of petitioner's business during the audit period. As evidence, Mr. Abdulla has submitted various documents, including letters, a declaration by Mr. Aldafari, petitioner's federal income tax return for 2007, motions filed in court, and court orders.

There is no dispute that Mr. Abdulla and Mr. Aldafari formed a two-person partnership in 1997 to conduct a business, that the partnership applied for a seller's permit that year, or that they executed a written partnership agreement on October 7, 2004, to govern their roles and responsibilities within the partnership. Therefore, the dispute turns upon whether the partnership dissolved, if at all.

On April 2, 2010, a jury returned a verdict that both Mr. Abdulla and Mr. Aldafari breached certain provisions of the partnership agreement. That verdict is evidence that the partnership continued to exist, since the partnership's existence is implicit in a finding that there was a breach of the partnership contract. Further, as a result of a civil action filed by Mr. Abdulla, the Superior Court, on September 26, 2012, issued a tentative decision addressing the issue of partnership dissolution. The Superior Court discussed Mr. Abdulla's argument that the partnership was dissolved in February 2007, in which Mr. Abdulla asserted that Mr. Aldafari dissociated from the partnership at that time. The Superior Court noted that the business continued to operate under Mr. Aldafari's exclusive control and management and that Mr. Aldafari believed he was acting in accordance with the partnership agreement. Thus, the Superior Court's finding that Mr. Aldafari had not dissociated from the partnership demonstrates that the partnership continued to exist during the audit period. Ultimately, the Superior Court's September 26, 2012 tentative decision ordered the partners to wind up the business, which is evidence that the partnership continued to exist in 2012, on the date of the tentative decision. In line with the civil court cases, petitioner's 2007 through 2010 partnership returns state that Mr. Abdulla received a 50-percent allocation of the profits for petitioner's business, which is additional evidence that Mr. Abdulla remained a partner in the partnership during the audit period.[1] Thus, based on a review of all the evidence, we find Mr. Abdulla remained a partner in petitioner's business throughout the audit period and is jointly and severally liable for petitioner's liability.

RESOLVED ISSUE

The Department imposed a negligence penalty because petitioner's records were not complete and the understatement was substantial. Petitioner did not present an argument that specifically addressed whether the understatement was the result of the partnership's negligence. Further, we concur with the Department's finding that petitioner's records were inadequate, and that the error rate of about 46 percent is higher than expected for a taxpayer that exercised due care in record-keeping and reporting. However, this was petitioner's first audit. Also, the evidence shows that the partners were adverse and hostile towards each other during the course of operating this business. Further, the unique management structure the partners employed may have contributed to petitioner's failure to maintain adequate records and to report accurately. Therefore, giving petitioner the benefit of the doubt, we conclude that it was not negligent and recommend that the penalty be deleted.

OTHER MATTERS

None.

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

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[1] The partnership returns, provided by the Department, were in direct conflict with statements made by Mr. Abdulla's representative at the appeals conference regarding the alleged termination of the partnership in 2007. However, we received no response to our letter asking Mr. Abdulla and his representative to explain this discrepancy.

MARKUP TABLE

Percentage of taxable vs. nontaxable purchases	76.83%
Mark-up percentage developed	32.91%
Self-consumption allowed in dollars	$13,377 for the audit period
Self-consumption allowed as a percent of taxable purchases	1%
Pilferage allowed in dollars	$13,377 for the audit period
Pilferage allowed as a percent of taxable purchases	1%