

## 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 ANDY'S BP, INC., ) Account Number: SR Y BH 100-181379  
 6 dba Shell Gas & Shop ) Case ID 546362  
 7 Petitioner ) South San Francisco, San Mateo County

7 Type of Business: Gas station and mini-mart

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9 Audit period: 1/1/06 – 12/31/08

<u>Item</u>	<u>Disputed Amount</u>	
10 Disallowed claimed exempt food sales		\$89,675
11 Overreported taxable sales of merchandise consumed by employees		85
12 Unreported taxable costs of merchandise consumed by employees		6,096
13 Unreported purchases subject to use tax		153,336
14 Unreported taxable cigarette rebates		126,798
15 Overclaimed sales tax prepaid for motor vehicle fuel		3,259

	<u>Tax</u>	<u>Penalty</u>
15 As determined <sup>1</sup>	\$32,215.43	\$3,221.58
16 Post-D&R adjustment	0.00	-3,221.58
17 Less concurred <sup>2</sup>	- 3,040.99	<u>0.00</u>
18 Balance, protested	<u>\$29,174.44</u>	<u>\$ 0.00</u>
19 Proposed tax redetermination	\$32,215.43	
20 Interest through 12/31/13	<u>13,936.24</u>	
21 Total tax and interest	<u>\$46,151.67</u>	
22 Monthly interest beginning 01/01/14	<u>\$161.08</u>	

22 <sup>1</sup> The determined tax is comprised of overclaimed prepaid sales tax on fuel of \$3,259.00 and \$28,956.43 tax computed on  
 23 the audited understatement of reported taxable measure of \$351,335. The audited understatement of reported taxable  
 24 measure of \$351,335 is net of a concurred credit of \$61,552 for erroneously reported sales of tangible personal property.  
 25 Since petitioner has filed a claim for refund, a refund may be made if petitioner prevails in this matter.

26 <sup>2</sup> At the appeals conference, petitioner stated that, with its post-conference submission, it would present arguments and  
 27 evidence pertaining to the deficiency measures for unreported purchases subject to use tax and unreported taxable cigarette  
 28 rebates, and pertaining to the amount established for overclaimed sales tax prepaid for motor vehicle fuel purchases.  
 However, after petitioner did not present any arguments or evidence regarding these three items with its post-conference  
 submission, the Appeals Division advised petitioner in two email messages that, unless petitioner presented arguments or  
 evidence, these three items would be regarded as undisputed. Petitioner did not respond to the email messages and  
 consequently, these three items were not addressed as disputed items in the D&R. However, since petitioner did not  
 specifically concede these three items, we have included them as unresolved issues in this summary. The amount  
 concurred relates to petitioner's specific concessions regarding unreported taxable costs of merchandise consumed by  
 employees.

1 This matter was scheduled for Board hearing in March 2013, but was postponed for Settlement  
2 consideration.

### 3 UNRESOLVED ISSUES

4 **Issue 1:** Whether adjustments to the deficiency measure for disallowed claimed exempt sales of  
5 food products are warranted. We conclude that no adjustments are warranted.

6 Petitioner operated multiple gas stations and mini-marts during the audit period. At each  
7 location except one (Capital Car Wash), petitioner used an integrated point of sale system in which a  
8 computer system classified each sale as taxable or nontaxable when employees scanned the  
9 merchandise. For sales at these locations, the Sales and Use Tax Department (Department) accepted  
10 the accuracy of petitioner's recorded taxable sales of fuel and mini-mart merchandise based on its  
11 observations during site visits. For sales at Capital Car Wash, petitioner's employees determined  
12 whether each sale was taxable or not and hit the corresponding key on the cash register. When the  
13 Department visited Capital Car Wash and purchased an energy drink, petitioner's employee  
14 misclassified the transaction as nontaxable and did not collect sales tax reimbursement. The  
15 Department found the ratio of reported taxable to total sales of 44 percent for this location to be  
16 significantly lower than expected, based on the types of items sold. Based on a segregation of  
17 petitioner's mini-mart purchases for this location for the second quarter of 2008, the Department  
18 computed ratios of 63.96 percent and 37.04 percent for purchases of taxable and exempt merchandise,  
19 respectively. The Department multiplied petitioner's recorded mini-mart sales of \$471,837 for Capital  
20 Car Wash by 37.04 percent to establish audited exempt sales of food of \$174,768 for this location for  
21 the audit period, and established a deficiency measure of \$89,678 for the difference between  
22 petitioner's claimed exempt food sales of \$264,446 for this location and audited exempt food sales.

23 Petitioner contends that its employees properly categorized sales as taxable or nontaxable and  
24 submitted two signed declarations from its employees stating that they rang up sales correctly. In  
25 addition, petitioner asserts that Capital Car Wash did not sell cigarettes, and therefore had a lower  
26 taxable sales ratio than its other locations. We find that petitioner has not provided sufficient evidence  
27 to demonstrate that Capital Car Wash had an exempt food sales ratio higher than the ratio of  
28 37.04 percent established in the purchase segregation test. Therefore, we recommend no adjustments.

1           **Issue 2:** Whether the deficiency measure for the cost of self-consumed taxable merchandise  
2 should be reduced. We conclude that no adjustments are warranted.

3           Petitioner provided its employees an allowance of \$5 per diem per shift to consume items in the  
4 store. Petitioner recorded the self-consumed merchandise at the retail sales price and included these  
5 recorded amounts of \$61,637 in its reported taxable sales. The Department concluded that petitioner  
6 was entitled to an allowance for the erroneously reported taxable sales measuring \$61,552, but owed  
7 tax on the cost of the taxable merchandise consumed by employees. The Department computed a  
8 markup of 42.86 percent for petitioner's sales of soda, and used that markup to compute costs of  
9 \$43,078 for the merchandise consumed by employees. Petitioner concedes that it owes use tax on  
10 costs of \$36,982, which it computed based on a markup of 66.67 percent. However, petitioner has  
11 provided no explanation for using the markup of 66.67 percent to compute these costs, and we find the  
12 Department's use of the markup for soda to be reasonable since it is probable that a significant  
13 percentage of merchandise consumed by employees would be soda. Since petitioner has not provided  
14 sufficient evidence to support adjustments to the audited measure related to self-consumed  
15 merchandise by employees, we conclude that no adjustments are warranted.<sup>3</sup>

16           **Issue 3:** Whether adjustments to the audited amount of unreported purchases subject to use tax  
17 are warranted. We conclude that no adjustments are warranted.

18           The Department examined petitioner's purchases of consumable supplies from out-of-state  
19 retailers on an actual basis and found that petitioner had purchased fuel pumping equipment and parts  
20 from two retailers without payment of tax. Since petitioner had reported no purchases subject to use  
21 tax on its returns for the audit period, the Department established a deficiency measure of \$153,336 for  
22 these purchases. Petitioner contends that some of its purchases from one of the out-of-state retailers  
23 were purchases for resale, but has provided no documentation or other evidence to support this  
24 contention or to show that any other adjustments to the measure are warranted. Therefore, we  
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26 <sup>3</sup> Petitioner also disputes the Department's use of \$61,552, rather than \$61,637 as the credit measure for reported sales to  
27 employees. The Department has concluded that the additional measure of sales to employees of \$85 (\$61,637 - \$61,552)  
28 was recorded in error for a location that only sold cigarettes and gum. Although the Department has not provided evidence  
of such error, we note that the amount truly in dispute is only \$26 (\$85 - \$59 cost). Since the tax on that difference is  
immaterial, we have not addressed the matter in detail.



1 of claims for refund filed by petitioner's president, the Department sent petitioner's president two  
2 letters (before the beginning of the audit period) informing him of the proper application of tax to  
3 cigarette rebates. Petitioner claimed that it had been trying to report its sales accurately and pointed  
4 out that its reported mini-mart sales at all but one of its locations were accurate.

5 In the D&R, we noted that petitioner reported its gasoline sales correctly and that the error rate  
6 of 0.34 percent calculated from a comparison of unreported taxable measure of \$351,335 with reported  
7 taxable sales of \$102,768,815 is minimal. However, based on petitioner's president's experience in  
8 this type of business and the written advice provided to petitioner's president regarding the proper  
9 application of tax to cigarette rebates, we found that petitioner's failure to report its purchases subject  
10 to use tax and its taxable cigarette rebates is evidence that petitioner was negligent. Therefore, we  
11 concluded that petitioner was negligent and that the penalty was properly applied.

12 However, upon further consideration, we note that petitioner accurately reported all of its  
13 gasoline sales for the audit period and installed an integrated point of sale system in all but one of its  
14 mini-marts, which enabled it to accurately report its taxable sales of mini-mart merchandise for every  
15 location but one. We also note that petitioner recorded and reported sales to its employees, which  
16 indicates conscientious effort to report all taxable sales. Although we continue to have concerns about  
17 petitioner's failure to properly report taxable cigarette rebates after petitioner's president received two  
18 letters from the Department informing him about the proper application of tax, we note that petitioner  
19 continued to dispute the application of tax to cigarette rebates upon completion of the audit, arguing  
20 that the rebates represented nontaxable purchase discounts rather than taxable sales. Therefore, we  
21 find that petitioner's failure to report taxable cigarette rebates could have been due to petitioner's  
22 failure to understand the Department's advice rather than negligence. In any event, we conclude that  
23 petitioner's overall recording and reporting accuracy is evidence that the understatement was not the  
24 result of negligence. Therefore, we recommend that the negligence penalty be deleted.

#### 25 OTHER MATTERS

26 None.

27 Summary prepared by Lisa Burke, Business Taxes Specialist III