

1 CALIFORNIA STATE BOARD OF EQUALIZATION

2 APPEALS DIVISION SUMMARY FOR BOARD HEARING

3 In the Matter of the Petition for Redetermination)
 4 Under the Sales and Use Tax Law of:)
 5 RAUL BECERRIL) Account Number: SR AS 053-002538
 6 Petitioner) Case ID 358820
)
) La Habra, Orange County

7 Type of Liability Responsible person liability

8 Liability Period: 4/1/99 – 3/31/02

9 Items Amounts in Dispute

10 Responsible person liability \$118,134.21

	<u>Tax</u>	<u>Penalties</u>
11 As determined	\$117,915.33	\$11,791.53
12 Adjustment: Sales and Use Tax Department		+19,912.71
Appeals Division		<u>-19,912.71</u>
13 Proposed redetermination	\$117,915.33	\$11,791.53
14 Less concurred	<u>-11,572.65</u>	
14 Balance, protested	<u>\$106,342.68</u>	<u>\$11,791.53</u>
15 Proposed tax redetermination	\$117,915.33	
16 Interest to 3/31/11	72,969.73	
16 Finality penalty	<u>11,791.53</u>	
17 Total tax, interest, and penalties	\$202,676.59	
17 Payment adjustments	<u>-111,300.00</u>	
18 Balance due	<u>\$91,376.59</u>	
19 Monthly interest beginning 4/1/11	<u>\$38.59</u>	

20 This matter was scheduled for Board hearing on October 20, 2010, but the oral hearing was
 21 postponed because petitioner's representative had a scheduling conflict.

22 **UNRESOLVED ISSUES**

23 **Issue 1:** Whether the disputed liability of 310 Motoring Inc., SR AS 97-547042 (3MI) is
 24 excessive or resulted from disallowed claimed exempt sales for which no sales tax reimbursement was
 25 collected. We conclude that the audited liability of 3MI is not excessive and that the disputed liability
 26 is not from disallowed claimed exempt sales but instead from sales for which 3MI collected sales tax
 27 reimbursement.

1 3MI sold auto parts and accessories and customized luxury cars from January 1, 1999, through
2 September 30, 2003, the effective date of the close out of its seller's permit. 3MI had an outstanding
3 liability based on a Notice of Determination issued on March 26, 2004, for an audit of the period April
4 1, 1999, to March 31, 2002. Since 3MI did not file a timely petition for redetermination, the
5 determination became final, and a finality penalty was added. The Sales and Use Tax Department
6 (Department) found that petitioner is a responsible person pursuant to Revenue and Taxation Code
7 section 6829 for the unpaid liability and issued a Notice of Determination to him on that basis.¹

8 Petitioner acknowledges he is liable as a responsible person pursuant to section 6829 for the
9 unpaid liabilities incurred by 3MI at issue here. However, he asserts that unreported taxable sales
10 established in the audit resulted from disallowed claimed exempt sales, not sales for which sales tax
11 reimbursement was collected and not remitted. On that basis, petitioner contends that the liability
12 related to those sales should be deleted from his liability as a responsible person (a responsible person
13 can be held liable under section 6829 for the sales tax incurred by a corporation only if sales tax
14 reimbursement was added to or included in the sales prices of the tangible personal property sold).

15 According to the audit work papers, the Department found discrepancies between recorded and
16 reported taxable sales, accrued and reported taxes, recorded and claimed exempt sales, and recorded
17 and claimed nontaxable sales for resale. The Department also found that 3MI claimed deductions for
18 tax-paid purchases resold although none were recorded; that bank deposits exceeded reported total
19 sales; and that total sales reported on sales and use tax returns exceeded gross receipts reported on
20 federal income tax returns. In addition, the Department was unable to trace sales invoices to the
21 general ledger and, although the invoices were numerically sequenced, the sequencing was not in
22 chronological order. As a result of these discrepancies and issues with the records, the Department
23 concluded that, except for the recorded sales during 2002, 3MI's records were incomplete, inaccurate,
24 and unreliable. The Department decided to establish taxable sales on a markup basis.

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28 ¹ 3MI also had a liability from a Notice of Determination issued to it for the third quarter 2003, but the Department did not pursue petitioner for that liability as a responsible person under section 6829.

1 3MI's controller could not explain the differences, claiming that he was new to the
2 organization, having been hired after the audit started, but claimed that sales were accurately recorded
3 for the year 2002 because of better internal controls. Thus, the Department used the records for the
4 year 2002 to establish an average markup of 46.21 percent by comparing gross receipts from taxable
5 and nontaxable sales of parts and accessories with the corresponding cost of sales. The Department
6 also examined sales invoices for March 2002 to establish that 22.32 percent of petitioner's sales were
7 taxable. The Department applied the average markup of 46.21 percent to the audited cost of sales to
8 establish audited total sales, and applied the taxable percentage of 22.32 percent to establish audited
9 taxable sales, which exceeded reported taxable sales by \$1,316,828.

10 Petitioner argues that the audited taxable sales were excessive and that the Department should
11 have used recorded nontaxable labor in place of reported nontaxable labor to compute estimated
12 taxable sales. We note that 3MI's books and records contained many unexplained differences between
13 recorded and reported amounts, and many invoices could not be traced to the general ledger.
14 Accordingly we find that the Department was justified in not accepting 3MI's books and records and in
15 using the markup method to establish understated taxable sales. The Department established the mark
16 up based on actual information obtained from 3MI's records for 2002, which 3MI's controller
17 indicated were fairly accurate due to a better system of internal controls. Thus, we find the
18 Department has used the best available information, and petitioner has not met its burden of proving
19 that the audited amount of taxable sales is excessive. In addition, petitioner has provided no evidence
20 that the recorded amount of exempt sales is accurate or more reliable than the reported amounts, which
21 the Department used in its calculations.

22 Petitioner also argues that the Department has failed to produce a single invoice that impeached
23 the amounts recorded in the general ledger or on which sales tax was billed and collected but not
24 remitted to the Board. With respect to the audit item in dispute, petitioner notes that the item is labeled
25 "estimated *underreported* taxable sales," rather than sales for which tax was collected but not *remitted*.
26 Accordingly, petitioner argues that "estimated unreported taxable sales" are actually unsubstantiated
27 exempt sales which cannot be assessed against him as a responsible person because they are sales with
28 respect to which 3MI did not collect tax reimbursement.

1 Of necessity, because of inadequate records, 3MI's sales were estimated on the basis of an
2 alternate audit approach (the markup method). The Department then computed a percentage of taxable
3 sales to total sales by comparing sales invoices in which sales tax reimbursement was added to the total
4 sales invoices. Thus, contrary to petitioner's contention, the amount of underreported taxable sales
5 was based on a sample percentage calculated from sales invoices which *included sales tax*
6 *reimbursement*, and therefore does not represent disallowed exempt sales. Additionally, disallowed
7 claimed nontaxable and exempt sales were calculated separately and were not included in the
8 assessment against petitioner. Accordingly, we find the Department correctly included the liability
9 based on underreported taxable sales in the liability against petitioner as a responsible person, and we
10 conclude no adjustments are warranted.

11 **Issue 2:** Whether reasonable cause has been established to relieve the finality penalty incurred
12 by 3MI. We conclude there is no basis for relief.

13 Petitioner submitted a request for relief of the finality penalty on behalf of 3MI, signed under
14 penalty of perjury, asserting that 3MI did not timely pay the liability or timely file a petition for
15 redetermination because it was going to file a bankruptcy petition by the time the audit determination
16 became final, and therefore believed the audit liability would be settled by the bankruptcy court.
17 Petitioner also repeats the argument in Issue 1 that we reject. In addition, petitioner believes that
18 imposing the finality penalty before issuing a bill to a corporate officer is equivalent to imposing a
19 penalty before issuing a tax assessment.

20 The audit determination was issued to 3MI on March 26, 2004, and became final on April 25,
21 2004, 30 days after issuance. 3MI did not enter bankruptcy until August 2004. Thus, 3MI could have
22 filed a petition for redetermination with the Board, or entered into an installment payment plan, before
23 the liability became final, but chose not to do so. Further, petitioner's argument that all sales tax
24 reimbursement collected by 3MI has been remitted to the Board (which we reject) does not address the
25 question of why petitioner did not timely pay the determination or file a petition for redetermination.
26 Based on the foregoing, we find that petitioner has not shown that 3 MI's failure to timely petition or
27 pay its tax liability was the result of reasonable cause and circumstances beyond its control. With
28 respect to the argument that the finality penalty was imposed prior to issuing a tax assessment,

1 petitioner is mistaken. The penalty was imposed *after* issuance of the *relevant* assessment, that is, the
2 Notice of Determination issued to 3 MI which it failed to timely petition or pay. The penalty was
3 billed to petitioner as a responsible person for 3 MI personally liable under section 6829, and he
4 therefore became liable for all the penalties that had been incurred by 3MI. We conclude that relief of
5 the finality penalty is not warranted.

6 **Amnesty**

7 Since 3MI did not participate in the amnesty program, an amnesty interest penalty of
8 \$19,912.71 was imposed on 3MI. This amount was not included in the Notice of Determination to
9 petitioner. The Department asserted an increase to the determination in this amount pursuant to
10 Revenue and Taxation Code section 6563.

11 3MI filed for Chapter 7 bankruptcy protection in August 2004, long before the amnesty
12 program began. By the time of the amnesty program, 3MI's assets had been liquidated and it would
13 have had no means to pay the liability or enter into a payment plan. Thus, we conclude 3MI's failure
14 to participate in the amnesty program was due to reasonable cause and circumstances beyond its
15 control. Accordingly, we recommend that relief from the amnesty interest penalty be granted, subject
16 to timely payment of the amounts due. We note that the usual payment conditions imposed on relief of
17 amnesty penalties are payment of the amnesty-eligible tax and interest due within 30 days of the final
18 decision, or, within that same 30-day period, entry into a qualifying installment agreement and
19 successful completion of it. However, in the D&R, our recommendation used a 60-day period rather
20 than a 30-day period. Since the D&R was issued more than two years ago and because we do not
21 believe this will make any practical difference under the circumstances, we are not changing our
22 recommendation in this matter at this time. Accordingly, we recommend that the amnesty interest
23 penalty be relieved if, within 60 days of the issuance of the Notice of Redetermination in this matter,
24 petitioner either pays the amnesty-eligible tax and interest due or enters into a qualifying installment
25 agreement to pay such amounts within 13 months and successfully completes that agreement.

26 **OTHER DEVELOPMENTS**

27 The Department also issued responsible person determinations for the same liabilities of 3MI to
28 Marc Laidler (SR AS 53-002537), Constantina Susie Frial (SR AS 53-002540), and Dornell Griffin

1 (SR AS 53-002539). Mr. Laidler and Ms. Frial timely filed petitions for redetermination, and their
2 hearings are scheduled for the same meeting as petitioner's appeal. Mr. Griffin did not timely petition
3 the determination and his liability is now final.

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Summary prepared by Rey Obligacion, Retired Annuitant