

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:)
DK SUPPLIES, INC., dba DK Beauty Supplies) Account Number: SR EA 100-549707
Petitioner) Case ID 509933
Westminster, Orange County

Type of Business: Retailer of beauty supplies and equipment

Audit period: 04/01/06 – 03/31/09

<u>Item</u>	<u>Disputed Amount</u>
Disallowed claimed sales for resale and netted sales	\$2,176,470
Tax as determined and protested	\$168,676.46
Interest through 09/30/12	63,490.29
Negligence penalty	<u>16,867.64</u>
Total tax, interest, and penalty	\$249,034.39
Payments	- 1,000.00
Balance Due	<u>\$248,034.39</u>
Monthly interest beginning 10/01/12	<u>\$ 838.38</u>

A Notice of Appeals Conference was mailed to petitioner’s address of record, and was not returned by the Post Office. Petitioner did not respond or appear at the appeals conference, which was held as scheduled. We thereafter sent petitioner a letter offering it the opportunity to provide any additional arguments and evidence it wished us to consider, but it did not respond. This matter was scheduled for Board hearing in February 2012, but was deferred at the request of the Sales and Use Tax Department (Department) and petitioner to allow time for petitioner to gather additional documentation (no additional documentation was provided). The matter was rescheduled for Board hearing in July 2012, but was postponed to allow petitioner additional time to prepare for the hearing.

UNRESOLVED ISSUE

Issue: Whether adjustments are warranted to the disallowed claimed nontaxable sales for resale. We find no adjustment is warranted.

Petitioner sells beauty supplies and equipment of the type typically purchased by those engaged in the personal care service industry. For the second and third quarters 2006 (2Q06 and 3Q06), the

1 first two quarters of the audit period, petitioner reported total sales of \$26,286 and claimed no
2 deductions. The Department compiled bank deposits for those two quarters, net of sales tax included,
3 of \$401,291, and it regarded the difference of \$375,005 as sales netted from reported total sales
4 because petitioner believed them to be nontaxable or exempt. For the period October 1, 2006, through
5 March 31, 2009, petitioner reported total sales of \$2,499,695 and claimed deductions of \$2,213,546 for
6 sales for resale and, for 4Q06, \$5,869 for sales in interstate commerce. Thus, petitioner netted or
7 claimed deductions totaling \$2,594,420 during the audit period ($\$375,005 + \$2,213,546 + \$5,869$).

8 The Department examined claimed sales for resale for 4Q07 and determined that claimed
9 deduction included claimed sales for resale and claimed sales in interstate commerce. The Department
10 found that the claimed exempt sales in interstate commerce were adequately supported by
11 documentation, but that petitioner had no resale certificates to support claimed nontaxable sales for
12 resale. Petitioner stated that a majority of its customers were nail shops and, since it believed that sales
13 to nail shops were sales for resale, it did not realize it was necessary to request resale certificates. The
14 Department concluded that the items petitioner sold to nail shops (such as nail polish, acrylic nail
15 powders and liquids, lotions, and spa pedicure chairs) would generally be consumed by those shops in
16 providing their services. Accordingly, the Department concluded that all of petitioner's claimed
17 nontaxable sales for resale should be disallowed.

18 In its test of the fourth quarter 2007, the Department computed that 16.11 percent of
19 petitioner's claimed sales for resale actually represented claimed exempt sales in interstate commerce,
20 with the remaining 83.89 percent representing claimed sales for resale. Thus, the Department
21 concluded that 83.89 percent of netted sales and claimed deductions ($\$2,594,420$) should be disallowed
22 as unsupported sales for resale and 16.11 percent should be allowed as supported exempt sales in
23 interstate commerce. Applying that ratio, the Department disallowed netted sales and claimed
24 deductions of \$2,176,470. Petitioner disputes the liability but has not provided specific reasons for its
25 disagreement with the audit (other than its originally stated belief that sales to nail shops would be for
26 resale). Petitioner has not provided any timely, valid resale certificates. Further, when this matter was
27 scheduled for hearing in February 2012, the Department requested that it be deferred in order to
28 provide an opportunity for petitioner to send XYZ letters to its purchasers. The Department explained

1 the XYZ letter process to petitioner, and despite petitioner's expression of interest in pursuing this
2 process, it ultimately stated that it had no more documentation to provide. Thus, petitioner has not
3 produced any evidence to show that the sales were actually sales for resale or that the tax was paid by
4 the purchasers. Accordingly, we find no adjustment is warranted.

5 **OTHER MATTERS**

6 The Department imposed a negligence penalty, which petitioner has not specifically protested.
7 Petitioner did not provide resale certificates to support its claimed nontaxable sales for resale. We find
8 that any businessperson, even one with limited experience, should be aware that it is necessary to
9 provide evidence to support claimed nontaxable sales, particularly when almost 90 percent of total
10 sales are claimed as nontaxable. Petitioner's understatement of \$2,176,470 caused by claiming
11 unsupported sales for resale that were determined to be retail sales represents more than 700 percent of
12 reported taxable sales. We find these facts clearly support imposition of the negligence penalty, even
13 though petitioner had not been audited previously.

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