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:	)	
DEANNA ROBINSON INTERIORS, INC.	)	Account Number: SR X EA 97-130375 Case ID 519485
Petitioner	)	Newport Beach, Orange County

Type of Business: Interior decorator

Audit period: 4/1/05 – 3/31/08

Item	Disputed Amount
Negligence penalty	$21,929

	Tax	Penalty
As determined	$219,294.52	$21,929.47
Less concurred	-219,294.52	0.00
Balance, protested	$ 0.00	$21,929.47

Proposed tax redetermination	$219,294.52
Interest through 2/29/12	105,757.20
Negligence penalty	21,929.47
Total tax, interest, and penalty	$346,981.19
Monthly interest beginning 3/1/12	$1,279.22

UNRESOLVED ISSUE

Issue: Whether petitioner was negligent. We conclude that it was.

Petitioner entered into contracts with its purchasers for interior decorating and the sale of tangible personal property. The contracts provided that title to the property passed to the purchasers when the goods were paid in full, including sales tax reimbursement. For some contracts, petitioner held the furnishings it had sold to its purchasers for up to a year or more during completion of the construction of the residential property for which the furnishings were purchased. Petitioner did not report its sales to the Board when payment was received, that is, per the contracts, when the sales occurred, but rather did not report the sales until the furnishings were delivered. The Sales and Use Tax Department (Department) determined that the gross receipts reported on petitioner's federal income tax returns matched petitioner's recorded payments from its purchasers, but discovered discrepancies between the amounts reported on federal returns and sales and use tax returns. The Department reconstructed petitioner's sales based on when payment was made and title passed, reconciled the audited taxable sales with reported amounts, and established a taxable sales understatement of $2,829,606. Petitioner does not dispute this deficiency.

The Department imposed the negligence penalty because: (1) petitioner failed to maintain adequate books and records and underreported its tax liability for the audit period; (2) the audit deficiency represents a 164.26 percent understatement; (3) petitioner has operated under this seller's permit since 1997; and (4) although petitioner was advised as to the proper method of reporting taxable sales for the interior decorating industry during a previous audit, it failed to correct its reporting methods.

Petitioner asserts that it was not negligent because it: (1) exercised due care that a reasonable and prudent person would exercise in similar circumstances; (2) prepared its returns following the guidelines set forth in the Board's Interior Design Pamphlet, which provides that items sold are not taxable until the merchandise is delivered (i.e., possession transferred); and (3) did not deliberately disregard its duty to keep adequate records (the documents not provided to the Department pertained to jobs marked incomplete).

We note that the business was previously operated by Deanna Robinson as a sole proprietor since 1977 (SR EA 24-696454) prior to its incorporation in 1997. Thus, petitioner's principal has had over 30 years of experience in this business, including the filing of sales and use tax returns. In petitioner's prior audit, the Department assessed a negligence penalty. We conclude petitioner's continuation of the same error from the prior audit constitutes negligence. We also find that the 164.26 percent error rate in reporting sales is egregious and is strong evidence of negligence. Although petitioner has not produced the publication which it claims to have followed in preparing its returns, we note that Publication 35, Interior Designers and Decorators, expressly states that tax is due when *ownership or possession* of the product sold transfers to the client, and here, ownership clearly passed under petitioner's contracts prior to delivery. We note also that the "incomplete" status of a project does not negate petitioner’s duty to provide records of those sales to the Department. We find that petitioner was negligent and the penalty properly imposed.

OTHER DEVELOPMENTS

None.

Summary prepared by Pete Lee, Business Taxes Specialist II