

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 LIFE-CARE HOME HEALTH &) Account Number SR AS 99-831665
 6 MEDICAL SUPPLIES, INC.) Case ID 495335
 7 Petitioner) Los Angeles, Los Angeles County

8 Type of Business: Retailer of home medical supplies

9 Audit period: 7/1/05 – 6/30/08

10 Item Disputed Amount

11 Unreported taxable sales \$609,334
 12 Negligence penalty \$5,027

	<u>Tax</u>	<u>Penalty</u>
13 As determined and protested	\$50,270.13	<u>\$5,027.04</u>
14 Interest through 02/28/13	23,524.66	
15 Negligence penalty	<u>5,027.04</u>	
16 Total tax, interest, and penalty	\$78,821.83	
17 Payments	- 679.81	
18 Balance Due	<u>\$78,142.02</u>	
19 Monthly interest beginning 11/1/12	<u>\$247.95</u>	

20 This matter was previously scheduled for Board hearing in April 2012, but was postponed at
 21 petitioner's request due to a scheduling conflict. It was rescheduled for Board hearing in July 2012,
 22 but was postponed by petitioner due to a medical reason. In October 2012, this matter was deferred for
 23 settlement consideration.

24 **UNRESOLVED ISSUES**

25 **Issue 1:** Whether adjustments are warranted to the audited amount of unreported taxable sales.
 26 We find that no adjustments are warranted.

27 Petitioner receives reimbursements from Medi-Cal and Medicare Part B as payment for all of
 28 its sales. During the audit period, petitioner's total bank deposits of \$1,303,042 substantially exceeded
 its reported total sales of \$504,814. The Sales and Use Tax Department (Department) decided that
 further investigation of petitioner's reported sales was warranted. Based on tests of petitioner's Medi-

1 Cal and Medicare reimbursements, the Department established that petitioner made taxable sales of
2 \$867,637 for the audit period. Since petitioner reported taxable sales of \$258,303, the amount of its
3 audited understated taxable sales is \$609,334, representing a reporting error rate of 236 percent.

4 Petitioner states that the understatement resulted from its attempt to take credits for exempt
5 sales that it mistakenly reported as taxable sales during the period July 1, 2002, through June 30, 2005,
6 and also possibly during the early quarters of this audit period. Petitioner requests that its remedy to
7 recover overpaid taxes from the past by understating its taxable sales on current returns without
8 verification or support for the claimed overpayments be allowed.

9 There is no legal authority to allow a taxpayer to grant itself a refund by intentionally
10 understating its taxable sales. A taxpayer must file a timely claim for refund in order to recover any
11 overpayments made on prior returns. Here, the statute of limitations for filing a timely claim for
12 refund for the period July 1, 2002, through June 30, 2005, has expired, and the evidence does not
13 support that petitioner overpaid its taxes during prior periods, or during the early portion of the current
14 audit period. Petitioner's audited taxable sales for this audit period are based on its bank deposits and
15 petitioner does not dispute the amount of taxable sales established by the Department. We conclude no
16 adjustments are warranted.

17 **Issue 2:** Whether relief under Revenue and Taxation Code section 6596 is warranted. We
18 conclude that relief is not warranted.

19 Petitioner contends that its attorney contacted the Board for advice on how to handle the
20 overstatement of taxable sales on returns filed for prior periods, and was advised to claim the exempt
21 sales that occurred in prior periods on its current returns. Petitioner has not provided a written copy of
22 the advice on which it allegedly relied, and states that it does not know when it received the advice, or
23 whether the advice was provided in writing or orally, because the attorney who contacted the Board on
24 its behalf has since passed away. We have reviewed the Board's records, and find no evidence of any
25 written advice given to petitioner on this subject. Furthermore, even if the Department had given
26 written advice to petitioner, which is not supported by the evidence, relief under section 6596 would
27 not be available since relief under section 6596 is limited to qualifying advice as to whether an activity
28

1 is subject to tax. (Rev. & Tax. Code, § 6596, subd. (b)(2).) We conclude that there is no basis for
2 relief under section 6596.

3 **Issue 3:** Whether petitioner was negligent. We conclude that it was.

4 The Department imposed the negligence penalty because the 236 percent audited reporting
5 error rate was far in excess of what would be expected from a normally prudent businessperson, and
6 petitioner had been audited previously. Petitioner contends that the understatement, if any, was due to
7 a misunderstanding of the procedures to amend erroneous returns and is not due to negligence.

8 The Department's prior audit of petitioner for the period July 1, 1999, through June 30, 2002,
9 established a deficiency measure of \$560,639, including \$556,409 for disallowed claimed exempt sales
10 under Medicare Part B. The reporting error rate was 84 percent. The Department did not impose a
11 negligence penalty in the prior audit because it concluded that the errors in reporting were due to
12 petitioner's erroneous beliefs that certain sales of medical supplies were exempt sales of medicines and
13 that some sales to patients who were reimbursed by Medicare were exempt sales to the U. S.
14 Government.

15 Here, the \$609,334 deficiency measure represents a 236 percent error rate, a substantial
16 increase in magnitude. We acknowledge that the types of errors in this audit period are not entirely the
17 same as the errors in the prior audit period, since most of the deficiency measure in the audit at issue in
18 this case cannot be attributed to disallowed claimed exempt sales under Medicare Part B. However,
19 we would expect that petitioner would have become more knowledgeable about the application of tax
20 and proper reporting procedures during that prior audit, and we would not expect the percentage of
21 error to rise dramatically in a second audit. Further, we are not convinced by petitioner's assertion that
22 the audited understatement here is due to petitioner's claiming of overpayments from prior periods on
23 current returns since we find that petitioner's claim that it overstated its taxable sales for periods prior
24 to the audit period is implausible. Moreover, even if we accepted petitioner's assertion that the
25 understatement was simply the result of its misunderstanding of the claim for refund procedure, we
26 note that the Department explained to petitioner, in a letter dated April 15, 2005 (before the start of the
27 audit period under consideration here), that it could file amended returns to correct reporting errors.
28 Thus, we find no merit in petitioner's contention that the understatement was due to petitioner's

1 misunderstanding of the law and procedures for correcting returns for prior periods, and in the absence
2 of any other non-negligent explanation for the understatement, we find that petitioner was negligent in
3 reporting and the penalty was properly imposed.

4 **OTHER MATTERS**

5 None.

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