

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 RICHARD EMIL & DANIEL JOSEPH) Account Number: SR KH 97-557035
 6 NAVONE, dba North Beach Marine) Case ID 336683
 7 Petitioner) Stockton, San Joaquin County

8 Type of Business: Retailer of watercraft, watercraft trailers, and parts

9 Audit Period: 06/01/99 – 12/31/01

10 <u>Item</u>	<u>Disputed Amount</u>
11 Unreported taxable sales of watercraft	\$3,232,041
12 Excess bank deposits considered additional taxable sales	\$722,657
13 Disallowed claimed exempt or nontaxable sales of watercraft	\$909,794
14 Fraud penalty	\$94,454
15 Amnesty double fraud penalty	\$94,454
16 Amnesty interest penalty	\$72,408

	<u>Tax</u>	<u>Penalty</u>
17 As determined and proposed to be redetermined	\$377,814.19	\$188,907.30
18 Less concurred	- 3,232.52	00.00
19 Balance, protested	<u>\$374,581.67</u>	<u>\$188,907.30</u>

20 Proposed tax redetermination	\$ 377,814.19
21 Interest through 05/31/12	375,366.85
22 Fraud penalty	94,453.65
23 Amnesty double fraud penalty	94,453.65
24 Amnesty interest penalty	<u>72,407.89</u>
25 Total tax, interest, and penalties	\$1,014,496.23
26 Payments	- 4,287.07
27 Balance due	<u>\$1,010,209.16</u>

28 Monthly interest beginning 06/01/12 \$ 2,177.33

24 This matter was scheduled for Board hearing in January 2009, but was deferred because we
 25 received a Request for Reconsideration. It was then rescheduled in December 2010, but since
 26 petitioner did not respond to the Notice of Hearing, the matter was scheduled for decision on the
 27 nonappearance calendar. Before the matter was presented to the Board for decision, petitioner filed a
 28 settlement proposal.

UNRESOLVED ISSUES

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2 **Issue 1:** Whether North Beach Marine was owned by Richard Navone and Daniel Navone, as
3 partners, or instead by Richard Navone as a sole proprietor. We conclude that, at all relevant times, the
4 business was owned by the two individuals, as partners.

5 North Beach Marine (NBM) was a retailer of watercraft, watercraft trailers, and related parts,
6 accessories and service from June 1999 through December 2001. The Sales and Use Tax Department
7 (Department) conducted an audit and issued a Notice of Determination to the partnership of Richard
8 Navone and Daniel Navone and separate Notices of Determination to each partner. Richard Navone
9 alone filed a timely petition for redetermination, protesting an unspecified portion of the audited
10 understatement and contending that he owned NBM as a sole proprietor. Although Richard Navone
11 states that he notified the Board during the first quarter of 2000 and again in the third quarter of 2001
12 that he alone owned NBM and that his son, Daniel Navone, was not a partner, he has not provided a
13 copy of the notice he claims to have provided to the Board.

14 We conclude in the D&R that the business was operated as a partnership. Daniel Navone filed
15 a Request for Reconsideration (RFR) arguing that he was not a partner. In his RFR, Daniel Navone
16 asserts that he does not recollect signing the application for NBM's seller's permit, and that his
17 involvement with NBM was limited to signing personal guarantees to enable Richard Navone to
18 purchase inventory. As support, Daniel Navone submitted copies of his federal income tax returns for
19 the years 1999 through 2001, which do not show that he received any distributive share of loss or gain
20 from the partnership, or indicate that he had any involvement with NBM.

21 The application for a seller's permit indicates that a partnership consisting of Richard Navone
22 and Daniel Navone owned and operated NBM, and each signed the application as "Partner." Sales and
23 use tax returns were filed under the partnership seller's permit during the entire time it was in business
24 and were signed by Richard Navone as "Partner." Additionally, the first time that Richard Navone
25 notified the Board that this partnership might have dissolved prior to closing out its seller's permit was
26 when he raised this issue in the present appeal, long after NBM ceased doing business and NBM's seller's
27 permit was closed out. No corroborating evidence has been provided to show that the partnership
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1 dissolved before the business was closed, or that Richard Navone ever owned NBM as a sole
2 proprietorship. Furthermore, NBM filed a partnership federal tax return for the year 2001.

3 Daniel Navone asserts only that he does not recall signing the application for a seller's permit,
4 and has not disputed that he did, in fact, sign the return. We note also that copies of Daniel Navone's
5 California Driver's License and social security card were provided with the petitioner's application for
6 a seller's permit, reflecting his active participation in the application process. Whether he remembers
7 doing so or not, we conclude that Daniel Navone signed petitioner's application for seller's permit as a
8 partner. Daniel Navone has not provided any documentation showing that he withdrew from the
9 partnership before NBM closed its doors or that he notified the Board of any change in the ownership
10 of the business. We conclude that NBM was owned and operated by the partnership of Richard
11 Navone and Daniel Navone, and that both are individually and severally liable for the liability incurred
12 by NBM.

13 **Issue 2:** Whether adjustments to the additional taxable sales or disallowed claimed nontaxable
14 or exempt sales are warranted. We find no adjustments are warranted.

15 The Department reconstructed the taxable watercraft sales petitioner made for the entire audit
16 period, using the worksheets attached to sales and use tax returns, sales contracts, and other available
17 information. Based on a reconciliation of recorded taxable sales on which petitioner had collected tax
18 reimbursement and reported taxable sales, the Department established unreported taxable sales of
19 \$3,232,041. In addition, the Department conducted a bank deposit analysis and established an
20 understatement of recorded taxable sales of \$722,657. Petitioner disputes both audited
21 understatements on the basis that there were numerous errors in the audit working papers. Further,
22 petitioner states that reported amounts were based on Excel spreadsheets, and that the worksheets
23 attached to its returns were merely lists of names and numbers irrelevant to sales and use tax reporting.
24 We find these arguments unconvincing. The Department conducted its audit based on records
25 petitioner made available, which did not include the Excel spreadsheets petitioner asserts it used for
26 reporting, and petitioner has not provided evidence to explain the disparities between its books and
27 records and reported amounts.

1 Regarding disallowed claimed exempt or nontaxable sales, the Department determined that
2 petitioner could not provide sufficient documentation to support 12 claimed exempt or nontaxable
3 sales of watercraft. Petitioner did not establish that these sales were made outside California or
4 delivered to a point outside California by providing bills of lading or properly completed forms BOE-
5 448, *Statement of Delivery Outside California*. Petitioner argues that all 12 sales were exempt sales in
6 interstate commerce, and that the evidence provided (signed affidavits and copies of driver's licenses
7 showing out-of-state residency) is adequate to show that the property sold was delivered out-of-state.
8 However, the Department indicates that petitioner stated during the audit that it had delivered the
9 watercraft at issue to the purchasers at locations in California, and that it later contended that the
10 questioned transactions were not subject to tax and provided some supporting documentation, which
11 the Department rejected. We find that petitioner has failed to establish that these were not California
12 sales subject to California sales tax.

13 Furthermore, some of the 12 disallowed claimed exempt or nontaxable sales were made to
14 persons who were California residents. Even where a sale was made outside California or qualifies as
15 an exempt sale in interstate commerce, that just resolves the issue of whether *sales tax* applies. Where
16 the purchaser is known to the retailer as a California resident, it is presumed that the purchase is for use
17 in California and the retailer has the burden of proving the contrary unless it takes in good faith a
18 timely written statement from the purchaser that the property was purchased for use at a designated
19 point or points outside this State. (Rev. & Tax. Code, § 6247.) The Board has prepared a form, BOE-
20 447, that can be used for this purpose. However, petitioner has not provided completed statements
21 from the purchasers or otherwise shown that the purchases were not for use in California. Thus, even
22 if petitioner could show that the sales were not subject to sales tax (which it has not done), we would
23 find that it is liable for use tax with respect to its sales of the subject watercraft to purchasers it knew
24 were California residents.

25 We conclude that no adjustment is warranted to the disallowed claimed exempt or nontaxable
26 sales.

27 **Issue 3:** Whether the Department has established fraud by clear and convincing evidence. We
28 find that the Department has done so.

1 The Department applied the fraud penalty because it found that petitioner willfully understated
2 its taxable sales. Petitioner disputes the penalty on the basis that it did not attempt to evade the tax and
3 asserts that the audited amount of understatement is excessive. Also, petitioner contends that the fraud
4 penalty should not be applied because any audit liability at issue is subject to the tax amnesty program.

5 Petitioner was aware of its sales and use tax reporting requirements, and Richard Navone was
6 an experienced businessperson, who had been a partner in a similar business before he became a
7 partner in petitioner. Petitioner maintained double-entry records showing taxable sales significantly
8 greater than reported sales. The records show that petitioner collected \$507,088 in tax reimbursement
9 during the audit period, but only reported \$252,171, retaining \$254,917, more than half of the amount
10 collected, for its own account. Moreover, the total amount of unreported tax also disclosed by audit,
11 \$377,814, represents approximately 149 percent of reported tax ($\$377,814 \div \$252,171$), and the
12 understatement occurred throughout the audit period. Petitioner has not shown that its consistent
13 failure to report more than half of the tax for which it had collected reimbursement was the result of
14 negligence or honest mistake. Additionally, petitioner has not explained how it could accurately
15 prepare federal tax returns and profit and loss statements, but only report about half of its taxable sales
16 on sales and use tax returns. We conclude that the Department has established fraud by clear and
17 convincing evidence, and the fraud penalty was properly applied.

18 With respect to petitioner's argument that the amnesty program precludes the application of the
19 fraud penalty, petitioner is mistaken. While the amnesty program did include a provision for waiver of
20 penalties, and petitioner could have qualified for waiver of the fraud penalties had it satisfied the
21 requirements of the amnesty program, petitioner did not apply for amnesty. Since petitioner did not
22 participate in the amnesty program, it obviously does not qualify for waiver of the fraud penalty under
23 the amnesty program's provision.

24 **Issue 4:** Whether relief of the amnesty related penalties is warranted. We find relief is not
25 warranted.

26 Since petitioner did not participate in the amnesty program, an amnesty double fraud penalty of
27 \$94,453.65 was added to the determination, and an amnesty-interest penalty of \$72,407.89 will be
28 added when the determination becomes final. Petitioner has requested relief of the amnesty penalties

1 on the basis that it was unable to determine its amnesty-eligible liability since the Department failed to
2 complete its audit in a timely fashion, and the Department had possession of the records. Petitioner
3 further asserts that inaccuracies in the Department's audit have resulted in erroneous penalties and
4 argues that it had no liability prior to the audit.

5 In January 2005, the Department provided explicit information to petitioner regarding the
6 amnesty program and the consequences for not participating. Also, the available evidence indicates
7 that petitioner had access to the records necessary to establish the amount of understatement.
8 Alternatively, petitioner could have requested an estimate of the potential audit liability from the
9 Department. Accordingly, we find that petitioner knew of the amnesty program and had information
10 available regarding the understatement of tax, and could have participated had it wished to do so.
11 Petitioner has not shown that its failure to participate in the amnesty program was due to reasonable
12 cause and circumstances beyond petitioner's control. Thus, we find that relief of the amnesty penalties
13 is not warranted.

14 **RESOLVED ISSUE**

15 The Department issued a determination to the partnership and separate determinations to
16 Richard Navone, Daniel Navone, and Mary Olvera Arnold. However, we are unaware of any evidence
17 that Ms. Arnold ever held any ownership interest in NBM. Accordingly, we recommend that the
18 determination issued to Ms. Arnold be cancelled.

19 **OTHER MATTERS**

20 Richard Navone claims that the Department has collected \$62,045.30 from him by an earnings
21 withholding order and a lien sale on property located in Stockton, California. However, the
22 Department indicated that it has no records of such collection and Richard Navone has provided no
23 documentation.

24 Richard Navone asserted he filed for bankruptcy protection in April 2005, he is destitute, and
25 he has no resources to retain counsel or representation to assist him in his appeal, or to pay the
26 liabilities of NBM. These are unfortunate circumstances, but not relevant to petitioner's liabilities.
27 Richard Navone has also argued that he has had difficulty pursuing this appeal because of the amount
28 of time that has lapsed, due to missing records which the Department had not returned and due to the

1 Department's rejection of the documents he has provided. The available evidence indicates that
2 certain records were returned to NBM, and that Richard Navone was informed that other records were
3 available for pick up. We are unaware of evidence that the Department retained any of petitioner's
4 records.

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

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