

CALIFORNIA STATE BOARD OF EQUALIZATION
APPEALS DIVISION BOARD HEARING SUMMARY

3 In the Matter of the Petition for Redetermination)
 4 Under the Sales and Use Tax Law of:)
 5 OUTLOOK UNITED, dba Infinitel) Account Number: SR Y BH 100-401288
 6 Petitioner) Case ID 469679
 7) San Mateo, San Mateo County

8 Type of Business: Cellular phone retailer

9 Audit period: 07/01/04 – 06/30/07

<u>Item</u>	<u>Disputed Amount</u>
11 Understatement of reported taxable sales	\$431,340
12 Tax as determined and protested	\$35,585.69
12 Interest through 9/30/11	<u>16,400.36</u>
13 Total tax and interest	<u>\$51,986.05</u>
14 Monthly interest beginning 10/1/11	<u>\$ 177.93</u>

15 This matter was scheduled for Board hearing on July 27, 2011, but was postponed at
 16 petitioner’s request because of a scheduling conflict.

UNRESOLVED ISSUE

18 **Issue:** Whether adjustments are warranted to the audited understatement of reported taxable
 19 sales. We find no adjustment is warranted.

20 During the audit period, petitioner made sales at retail and for resale of cellular phones and
 21 other wireless communication devices. Most of its retail sales of cellular phones were made in
 22 bundled transactions (that is, the sales contractually required the customer to activate or contract with a
 23 service provider for utility service for a period greater than one month as a condition of the sale). The
 24 only exceptions are sales of cellular phones as upgrades or to replace lost or damaged phones.
 25 Typically, petitioner separately stated a sales price for each phone that was 55 to 60 percent of
 26 petitioner’s cost, and it reported tax on that sales price.

27 The Sales and Use Tax Department (Department) concluded that reported taxable sales were
 28 understated because the amounts reported should have been based on the unbundled selling prices of

1 the phones, rather than the invoiced prices, which were less than cost.¹ However, since petitioner
2 made few unbundled sales of cellular phones, the Department did not have adequate data to determine
3 petitioner's unbundled selling prices. Therefore, based on California Code of Regulations, title 18,
4 section (Regulation) 1585, subdivision (a)(4), the Department established the fair retail selling prices
5 of cellular phones by adding an 18 percent markup to petitioner's cost. Using the second quarter 2007
6 as a test period, the Department found that reported taxable sales were understated by about 111
7 percent, and it applied the percentage of error to reported taxable sales for the audit period to establish
8 the understatement of \$431,340.

9 Petitioner contends that the audited understatement of reported taxable sales is excessive,
10 stating that many of the cellular phones it sold were obsolete and that the correct taxable measure for
11 those sales was the price at which the phones were sold. Petitioner also asserts that the rules for
12 reporting retail sales of cellular phones are so confusing that it is unfair to expect petitioner to
13 understand them. Further, petitioner maintains that it believed it was reporting tax correctly, based on
14 its understanding of an article in the Board's June 1999 Tax Information Bulletin. In addition,
15 petitioner provided invoices from other retailers to show that they also reported tax on the invoiced
16 selling prices of phones sold in bundled transactions.

17 Briefly addressing the last assertion first, we find that any incorrect reporting of tax by other
18 retailers is irrelevant to our analysis of the tax owed by petitioner. Regulation 1585 sets out specific
19 rules for the tax treatment of sales of cellular phones. In accordance with that regulation, since
20 petitioner's sales of cellular phones were almost all made in bundled transactions, it was appropriate
21 for the Department to establish the fair retail selling prices of the phones by applying an 18 percent
22 markup to petitioner's costs. Also, since petitioner did not provide complete sales and purchase
23 records, it was appropriate for the Department to review the transactions in a block sample (the second
24 quarter 2007) and apply the percentage of error computed in that test to the remainder of the audit
25 period. With respect to petitioner's contention that about 50 percent of the phones it sold were
26 obsolete and that the measure of tax for those sales should be the invoiced price, petitioner stated that

27 _____
28 ¹ The Department found that petitioner's claimed nontaxable sales for resale were substantially accurate.

