

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:)
 RAJESH PRAKASH SHARMA and ZARINA) Account Number: SR KH 97-194303
 ALI SHARMA, dba Hites Market) Case ID 267189
 Petitioner) Sacramento, Sacramento County

Type of Business: Grocery store

Audit Period: 7/1/00 – 6/30/03

<u>Items</u>	<u>Disputed Amounts</u>	<u>Tax</u>	<u>Penalty</u>
Unreported store sales	\$663,367		
Unreported gas sales	\$539,729		
Negligence penalty	\$9,780		
As determined		\$99,282.12	\$9,928.22
Post-D&R adjustment		- 1,480.11	- 148.01
Proposed redetermination		\$97,802.01	\$9,780.21
Less concurred		- 5,416.04	0.00
Balance, protested		<u>\$92,385.97</u>	<u>\$9,780.21</u>
Proposed tax redetermination		\$ 97,802.01	
Interest through 06/30/12		80,729.82	
Negligence penalty		<u>9,780.21</u>	
Total tax, interest, and penalty		\$188,312.04	
Payments		- 8,906.52	
Balance due		<u>\$179,405.52</u>	
Monthly interest beginning 07/01/12		<u>\$444.48</u>	

This matter was scheduled for Board hearing in May 2009, but was postponed because petitioner’s representative requested additional time to submit an opening brief. It was rescheduled for hearing in July 2009 but was deferred because the Sales and Use Tax Department (Department) wished to issue the Notice of Determination to an asserted partner (the landlord) and requested that the Appeals Division conduct another conference on the issue of whether that person was actually a partner in the business (which, as discussed below under Other Matters, we held was not the case).

UNRESOLVED ISSUES

Issue 1: Whether adjustments are warranted to the amount of unreported taxable store sales.

1 We conclude that no further adjustments are warranted.

2 Petitioner operated a grocery store selling the usual items plus gasoline, until it closed out the
3 business on July 28, 2005. Petitioner did not provide adequate books and records for audit. Based on
4 its preliminary review of the records, the Department concluded that reported sales were substantially
5 understated and decided to establish taxable store sales on a markup basis. Based on a shelf test, the
6 Department computed a weighted markup of 27.1 percent, which it added to the audited cost of taxable
7 goods sold (audited purchases, adjusted by \$57 per week for self-consumption and 2 percent for
8 pilferage). The Department also made an adjustment for food stamps for 2000, the only year petitioner
9 accepted food stamps. We recommended a reaudit to increase the allowance for self-consumption to
10 \$300 a month, increase the allowance for pilferage to 3 percent, and allow an additional shrinkage
11 amount of \$1,000 for the first six months of 2003 to account for potential loss of taxable merchandise
12 due to fire damage. After those adjustments, the audited understatement of reported taxable store sales
13 is \$663,367.

14 Petitioner contends that the allowance for pilferage should be increased to 5 percent because
15 the business was located in a gang-infested, high-crime area. Also, petitioner states that Mr. Sharma
16 was incarcerated from June 2001 through December 2003 and, while Ms. Sharma ran the business,
17 employees stole substantial amounts of money and merchandise.

18 Pilferage of 3 percent has already been allowed, based on the location of the business and to
19 account for employee pilferage during Mr. Sharma's absence. Shrinkage of \$1,000 has additionally
20 been allowed to account for a fire at petitioner's business in the first quarter of 2003, even though
21 petitioner provided no evidence of loss due to that fire. Petitioner has not provided any evidence to
22 support additional increases to the pilferage allowance, and we recommend no further adjustment.

23 **Issue 2:** Whether the amount of unreported gas sales is excessive. We conclude that it is not.

24 Petitioner provided its sales summaries for the years 2000 and 2001 and the first six months of
25 2003, which the Department used to compute book markups of about 6 percent for each period. The
26 Department considered the book markups reasonable and concluded that recorded gas sales were
27 substantially accurate. The Department found no differences between recorded and reported gas sales
28 for 2001 or the first six months of 2003, but it found an understatement of \$141,645 for the third and

1 fourth quarters of 2000. Since sales summaries were not provided for the year 2002, the Department
2 decided to establish gas sales on a markup basis for that year, using a markup of 6 percent, based on
3 the book markups it computed for the periods that petitioner provided records. The Department
4 computed an understatement of reported gas sales of \$398,085 for the year 2002, which it added to the
5 \$141,645 understatement for the period July 1, 2000, through December 31, 2000, to compute
6 underreported gas sales of \$539,730 for the audit period. Although petitioner contends the audited
7 understatement of gas sales is excessive, it has provided no evidence to support its contention, and has
8 not even raised any specific arguments. We conclude no adjustment is warranted.

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

10 The Department asserted the negligence penalty because petitioner failed to provide adequate
11 books and records. Petitioner disputes negligence penalty because Mr. Sharma was an absentee owner
12 for most of the audit period, and Ms. Sharma was not experienced in running the business.

13 We find petitioner's failure to provide adequate records, and the substantial understatement of
14 \$1,242,211, which represents an understatement in excess of 65 percent in comparison to reported
15 taxable sales of \$1,882,891, are clear evidence of negligence, particularly since petitioner had been
16 audited previously. We find petitioner's argument unpersuasive because petitioner underreported a
17 substantial amount of taxable sales during the period when Mr. Sharma was not incarcerated. We
18 conclude that petitioner was negligent, and that the negligence penalty was properly applied.

19 OTHER MATTERS

20 The amnesty interest penalty is not applicable in this case because petitioner filed an
21 application for amnesty and entered into a qualifying installment payment plan.

22 Seven Grant's, Inc. owned the property on which the business was located, and it is listed as the
23 business landlord on petitioner's application for a seller's permit. In February 1998, the Department
24 became aware that petitioner was listed on Seven Grant's liquor license, and, based on this, decided
25 that Seven Grant's would have to be included on petitioner's seller's permit as a partner. So that the
26 Sharmas could obtain a seller's permit for the business, Seven Grant's submitted an application for
27 seller's permit indicating that it only held the liquor license. The Department reflected in its records
28 that Seven Grant's was a partner along with the Sharmas in the business known as Hites Market. The

1 Notice of Determination in this case was issued to Hites Market, with a copy sent to Rajesh Sharma
2 and a copy sent to Zarina Sharma. No copy was sent to Seven Grant's, and it did not participate in the
3 first appeals conference. Nevertheless, since Seven Grant's was reflected in the Board's records as a
4 partner, we mailed to Seven Grant's a copy of the D&R and a copy of the later reaudit options letter.
5 Seven Grant's filed a request for Board hearing, and in its hearing brief contended that it was only the
6 landlord and was never a partner.

7 After reviewing the procedural history, the Department recognized that it had not actually
8 issued the Notice of Determination to Seven Grant's, and Seven Grant's had not been given the
9 opportunity to present its dispute to the Appeals Division. Thus, the Department issued a copy of the
10 Notice of Determination to Seven Grant's, and we thereafter held two appeals conferences on the
11 issue, one with the Sharmas and one with Seven Grant's.

12 The Department contended that, since Seven Grant's was listed on the seller's permit, it was a
13 partner. Petitioner asserted that Seven Grant's was a silent partner in the business, stating that it had
14 interfered with petitioner's attempts to sell the business in 2004 and 2005, demanding 50 percent of the
15 proceeds of the sale. Seven Grant's asserted that the only reason petitioner was added to Seven
16 Grant's liquor license was that petitioner had applied for a new liquor license but such licenses were
17 not being granted in the area where the business was located, and that the alleged interference with the
18 contract of sale is not evidence of a partnership.

19 We conclude that there is no evidence of a partnership between petitioner and Seven Grant's.
20 Rather, the evidence shows that Seven Grant's was merely the Sharmas' landlord. Accordingly, we
21 conclude that Seven Grant's is not properly part of this dispute (Seven Grant's was advised that final
22 action on its appeal would be withheld until the Sharmas' appeal is resolved).

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24 Summary prepared by Deborah A. Cumins, Business Taxes Specialist III
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28**MARKUP TABLE**

Percentage of taxable vs. nontaxable purchases	83.80%
Mark-up percentages developed	27.1%
Self-consumption allowed in dollars	\$3,600 per year
Self-consumption allowed as a percent of total purchases	.79 %
Pilferage allowed in dollars	\$47,644
Pilferage allowed as a percent of total purchases	3 %