STATE BOARD OF EQUALIZATION
SALES AND USE TAX APPEAL

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:	
WCN, INC.	Account Number: SR AS 97-952302 Case ID 491680
Petitioner	Los Angeles, Los Angeles County

Type of Business: Seller of computers

Audit period: 07/01/04 – 12/31/07

Item	Disputed Amount
Unreported taxable sales	$319,570
Disallowed claimed sales for resale	$175,990
Disallowed claimed interstate commerce sales	$1,158
Negligence penalty	$4,098

	Tax	Penalty
As determined	$127,795.06	$12,779.53
Pre-D&R adjustments	- 8,583.88	- 858.37
Post-D&R adjustments	- 78,231.87	- 7,823.21
Proposed redetermination, protested	$ 40,979.31	$ 4,097.95

Proposed tax redetermination	$40,979.31
Interest through 02/28/14	26,045.09
Negligence penalty	4,097.95
Total tax, interest, and penalty	$71,122.35
Monthly interest beginning 03/01/14	$ 204.90

UNRESOLVED ISSUES

Issue 1: Whether any further adjustments are warranted to the amount of unreported taxable sales. We find no further adjustments are warranted.

Petitioner sells computers and component parts and has been in business since November 2001. Petitioner also repairs computers. For audit, petitioner provided bank statements for the period July 1, 2004, to June 30, 2007, and income statements for 2004, 2005 and 2006. Since petitioner could not provide all of its sales invoices and a detailed summary of its sales, such as a sales journal, the Sales and Use Tax Department (Department) established gross receipts using bank deposits.

Initially, the Department established unreported taxable sales of $1,099,639. Based on documentation provided prior to the appeals conference and after the D&R was issued (in a request for reconsideration), the Department concluded that unreported taxable sales should be reduced to $747,657. However, we found errors in the Department's calculations, and, in a supplemental D&R, we recommended that unreported taxable sales be further reduced to $319,570.

Petitioner contends that the excess bank deposits do not represent unreported taxable sales and that further adjustments are warranted for nontaxable sales of optional maintenance contracts. The Department found that the sales invoices petitioner provided were insufficient to conclude whether the maintenance contracts were optional or mandatory, and more importantly, whether any of the proceeds from the sales of maintenance contracts were included in the bank deposits. We concur with the Department's conclusion, and we reject petitioner's contention that further adjustments are warranted.

Issue 2: Whether further adjustments are warranted to the disallowed claimed sales for resale. We find no further adjustments are warranted.

Initially, the Department disallowed all of petitioner's claimed sales for resale. Subsequent to the appeals conference, petitioner provided sales invoices and documentation to support sales for resale totaling $209,723, which the Department accepted. However, petitioner provided no sales invoices or documentation to support any of the remaining claimed sales for resale.

Petitioner contends further adjustments are warranted and that the remaining disallowed sales for resale should be accepted. In the absence of any supporting documentation, we conclude that no further adjustments are warranted and we recommend none.

Issue 3: Whether further adjustments are warranted to the disallowed claimed sales in interstate commerce. We find no further adjustments are warranted.

Initially, the Department disallowed all of petitioner's claimed sales in interstate commerce. Subsequent to the appeals conference, petitioner provided sales invoices and documentation to support sales in interstate commerce totaling $39,073, which the Department accepted. However, petitioner provided no sales invoices or documentation to support any of the remaining claimed sales in interstate commerce.

Petitioner contends further adjustments are warranted for the remaining disallowed sales in interstate commerce. In the absence of any supporting documentation, we conclude that no further adjustments are warranted and we recommend none.

Issue 4: Whether petitioner was negligent. We conclude that petitioner was negligent.

The Department imposed the negligence penalty because petitioner failed to maintain adequate records, and because the understatement is large relative to reported taxable sales. Petitioner disputes the negligence penalty on the grounds that the understatement is excessive. Also, petitioner notes that this was petitioner's first audit.

A comparison of unreported taxable measure with reported taxable sales shows an error rate of 23,309 percent [($319,570 + $175,990 + $1,158) ÷ $2,131], which is strong evidence of negligence in reporting. Further, with the exception of the bank statements and income statements, petitioner failed to provide complete sales and purchase records for the audit period. Even though this was petitioner's first audit, we find that petitioner was negligent in both reporting and recordkeeping.

RESOLVED ISSUES

Initially, the Department included a separate measure of tax for unreported purchases of machinery and equipment, and a separate measure of tax for unreported purchases of furniture and fixtures. However, petitioner provided documentation supporting that the unreported purchases occurred outside the normal three-year statute of limitations. Consequently, the Department concluded both measures of tax should be deleted, and prior to the appeals conference prepared a reaudit to delete the measures of tax. We concur with the Department's recommendation.

OTHER MATTERS

None.

Summary prepared by Ted Matthies, Business Taxes Specialist III

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