

1 CALIFORNIA STATE BOARD OF EQUALIZATION

2 APPEALS DIVISION FINAL ACTION SUMMARY

3 In the Matter of the Administrative Protest)
 4 and Claims for Refund)
 4 Under the Sales and Use Tax Law of:)
 5 LOUIS JOHN BONACICH, JR., dba) Account Number SR KH 28-910657
 6 Specialty Sales/All Green Hydro) Case ID's 493991, 568375
 7 Taxpayer/Claimant) Orangevale, Sacramento County

8 Type of Business: Manufacturer of outdoor patio furniture
 9 Audit period: 01/01/04 – 12/31/06

10 <u>Item</u>	<u>Disputed Amount</u>		
11 Unreported taxable sales	\$ 52,627		
12 Taxable sales recorded as nontaxable in error	\$ 31,929		
12 Negligence penalty	\$ 649		
		<u>Tax</u>	<u>Penalty</u>
14 As determined		\$7,884.96	\$788.51
14 Finality penalty			788.50
15 Pre-D&R adjustment		- 220.58	- 22.01
15 Post D&R adjustment		- 1,178.80	- 906.39
16 Adjusted tax and penalty, protested		<u>\$6,485.58</u>	<u>\$648.61</u>
17 Adjusted tax	\$ 6,485.58		
18 Interest	2,816.94		
18 Negligence penalty	648.61		
19 Total tax, interest, and penalty	\$ 9,951.13		
19 Payments	- 9,951.13		
20 Balance Due	<u>\$ 00.00</u>		

21 The Board held a hearing regarding this matter on May 30, 2012, granting taxpayer 30 days to
 22 provide additional records and the Sales and Use Tax Department (Department) 30 days to respond.
 23 Based on taxpayer's submissions and the Department's response, we do not recommend adjustments,
 24 as discussed below under Post Hearing Developments.

25 UNRESOLVED ISSUES

26 **Issue 1:** Whether adjustments are warranted to the unreported taxable sales. We find no further
 27 adjustment is warranted.

1 Taxpayer operated a liquor store under this seller's permit from June 1992 through October
2 2001. After he sold the liquor store, he began manufacturing outdoor furniture, and he retained the
3 seller's permit for that new line of business. Taxpayer provided incomplete records for audit, and the
4 Department concluded that the sales invoices and sales summaries taxpayer provided for 2004 and
5 2006 represented the best available evidence of taxpayer's sales. After adjusting the sales summaries
6 for two unrecorded sales and one cancelled sale, the Department computed recorded taxable sales for
7 2004 and 2006. It compared those amounts to reported taxable sales to compute a percentage of error
8 which it applied to reported amounts for 2005 to establish the understatement for that year. In the first
9 reaudit, the correction of a computational error resulted in increases to the amounts of audited taxable
10 sales for 2004 and 2005. However, those increases were offset by an adjustment for a nontaxable sale
11 for which taxpayer provided a resale certificate during the first reaudit. After the determination was
12 issued, taxpayer also provided a reconstructed sales summary for 2005, and sales invoices, cancelled
13 checks, and credit card receipts, which reconciled roughly with taxpayer's reported taxable sales for
14 that year. However, the Department rejected those records as unreliable since it could not be
15 established that the invoices were complete.

16 Taxpayer contends that adjustments should be made for recorded sales that were never
17 consummated. He also claims that the amount of taxable sales established for 2005 is excessive, based
18 on the reconstructed records provided. Alternatively, taxpayer asserts that the average error rate used
19 to establish taxable sales for 2005 is excessive because some sales recorded in 2004 were not
20 completed until 2005.

21 The Department has used taxpayer's sales invoices and sales summaries for 2004 and 2006 to
22 establish audited taxable sales, notwithstanding its reasonable concern that those records may have
23 been incomplete. We find that the Department's audit method was appropriate, and taxpayer has
24 provided no persuasive documentation to support further adjustments for sales that were not
25 consummated. Also, we reject taxpayer's assertion that the reconstructed records for 2005 should be
26 accepted as accurate since there is no evidence to show that the available sales invoices are complete.
27 In addition, taxpayer has provided no documentation that some sales commenced in 2004 were not
28 completed until 2005. Further, even if such documentation were available, an adjustment might not be

1 warranted because those sales would likely be offset by other sales, commenced and recorded in 2003,
2 but not completed until 2004. Thus, we find no further adjustment is warranted.

3 **Issue 2:** Whether adjustments are warranted to the amount of taxable sales recorded as
4 nontaxable sales in error. We find no adjustment is warranted.

5 The Department has allowed sales to two customers as valid nontaxable sales for resale, based
6 on a resale certificate provided during the first reaudit and on the Department's research regarding the
7 purchasers' types of business. Taxpayer contends that all recorded nontaxable sales for resale should
8 be allowed because, while he misunderstood the requirements for retaining valid resale certificates, it
9 was his understanding that the sales were for resale at the time they were made. Although taxpayer
10 sent XYZ letters for the remaining questioned transactions, he received no responses. Also, the
11 Department found no evidence that any of those remaining sales were made to purchasers who held
12 valid seller's permits and were engaged in the business of selling outdoor furniture. Thus, we find the
13 evidence does not support any further adjustments.

14 **Issue 3:** Whether taxpayer was negligent. We conclude that he was.

15 The Department imposed the negligence penalty because taxpayer's records were not adequate.
16 Taxpayer disputes the penalty on the basis that reported sales were accurate and his records were
17 adequate. Regarding 2005, taxpayer states the records were unavailable because they were lost in a
18 move precipitated by his divorce.

19 Taxpayer's records were incomplete and conflicting. Also, the understatement of \$84,556
20 represents an understatement of about 44 percent when compared to reported taxable sales of
21 \$192,321. We find that the inadequacy of the records and the magnitude of the understatement are
22 evidence of negligence, particularly since taxpayer is an experienced business person who had been
23 audited previously when he operated a liquor store under this seller's permit number. Accordingly, we
24 find that the negligence penalty was properly applied.

25 **RESOLVED ISSUE**

26 Since taxpayer did not timely pay the determination or file a petition for redetermination, a
27 finality penalty was automatically applied. Taxpayer submitted a request for relief of the finality
28 penalty on the basis that he thought he had filed a timely appeal and that his case was in the appeals

1 process. We find it credible that taxpayer misunderstood the requirements for filing a timely petition,
2 particularly since he had expressed his disagreement with the audit in writing prior to the issuance of
3 the determination. Thus, giving taxpayer the benefit of the doubt, we recommend relief of the finality
4 penalty (the tax, interest, and negligence penalty have been paid in full).

5 **OTHER MATTERS**

6 Taxpayer has filed claims for refund, which we find are timely-filed for payments totaling
7 \$2,750.00. While reviewing the case for the previously scheduled Board hearing, the Department
8 identified errors in the audit computations, and it prepared a second reaudit to eliminate duplications of
9 certain transactions. That adjustment reduced the difference between recorded and reported taxable
10 sales by \$15,378, from \$68,005 to \$52,627. Based on the second reaudit, taxpayer has made an
11 overpayment of \$828.85, and that amount has been applied to a liability on a related account, SA V UT
12 84-150579. Since there is no other overpayment, we recommend that the claims for refund be denied.

13 **POST HEARING DEVELOPMENTS**

14 At the Board hearing, taxpayer's primary argument was that the audited amount of unreported
15 taxable sales is excessive because it includes transactions that were not consummated. Taxpayer
16 asserted that the audited sales were based on a list prepared for audit by the prior bookkeeper that
17 included all purchase orders, rather than a list of completed sales for which the items had been
18 delivered to or picked up by the purchasers. The Members granted taxpayer 30 days to provide
19 evidence to show that the audited amount of unreported taxable sales included transactions that were
20 never consummated. Taxpayer also stated that money was seized from his bank accounts without
21 notice, and the Members requested additional information about the levy procedure.

22 After the Board hearing, taxpayer provided sales summaries for 2004, 2005, and 2006
23 (allegedly representing the completed transactions), and, for 2005, copies of delivered sales invoices
24 and copies of checks and credit card receipts. The Department noted, however, that the sales
25 summaries were prepared for the purpose of this appeal, and taxpayer did not provide sales summaries
26 prepared contemporaneously with the sales. Also, the total sales listed on the sales summaries were
27 less than taxpayer's reported taxable sales by \$1,115 for 2005, \$27,479 for 2005, and \$2,391 for 2006.
28 In addition, taxpayer did not provide evidence of any canceled orders, and, since the invoices were not

1 sequentially numbered, it was not clear whether the available invoices were complete. Thus, the
2 Department concluded the available evidence does not establish that the sales shown on the recently-
3 prepared sales summaries represented all of taxpayer's consummated sales. As a separate observation,
4 the Department noted that taxpayer has reported no wage expense on his federal tax returns, which
5 belies his assertion at the hearing that the deposits for merchandise were paid directly to commissioned
6 salespeople. Further, the Department noted that the amount of sales reported on federal tax returns for
7 the three years exceeded total sales based on taxpayer's analysis by about \$108,000, and taxpayer has
8 not explained the reason for that discrepancy. In the absence of evidence that the sales listed by the
9 prior bookkeeper included any transactions that were not completed, we recommend no adjustment.

10 Regarding the funds obtained by levy from taxpayer's bank accounts, the Department states
11 that a Demand for Immediate Payment was mailed to taxpayer's address of record, with a copy to his
12 CPA on May 11, 2009. In a letter dated July 17, 2009, taxpayer's late appeal was accepted as an
13 administrative protest, and the letter advised taxpayer that collection efforts would not be withheld.
14 On October 16, 2009, taxpayer promised to pay the balance due on receipt of the reaudit or to arrange
15 an installment payment plan. Taxpayer did neither. A levy was sent on November 25, 2009, and
16 taxpayer was notified of the levy by letter on that date. Thus, the evidence contradicts taxpayer's
17 assertion that the funds were seized from his accounts without any prior notice.

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