

1 CALIFORNIA STATE BOARD OF EQUALIZATION

2 APPEALS DIVISION FINAL ACTION SUMMARY

3 In the Matter of the Petition for Redetermination)
 4 Under the Sales and Use Tax Law of:)
 5 FRONT PAGE COMMUNICATIONS, INC.) Account Number: SR AA 97-527716
) Case ID 361961
 6 Petitioner)
) Paramount, Los Angeles County

7 Type of Business: Sales and installation of television satellite equipment

8 Audit period: 04/01/01 – 12/31/04

9 <u>Item</u>	<u>Disputed Amount</u>
10 Unreported measure	\$1,207,169
Relief of interest	\$ 61,483
11 Amnesty interest penalty	\$ 5,143
12 Tax as determined:	\$100,347.98
Adjustment - Appeals Division	- 453.27 ¹
13 - Post Board hearing	- 947.65
14 Proposed redetermination, protested	<u>\$ 98,947.06</u>
15 Proposed tax redetermination	\$ 98,947.06
Interest through 5/31/11	61,482.83 ²
16 Amnesty interest penalty	<u>5,143.38</u>
Total tax, interest, and penalty	\$165,573.27
17 Payments	<u>-35.63</u>
18 Balance Due	<u>\$165,537.64</u>
19 Monthly interest beginning 6/1/11	<u>\$576.98</u>

20 The Board held a hearing regarding this matter on December 15, 2010, granting petitioners 30
 21 days to provide additional records and the Sales and Use Tax Department (Department) 30 days to
 22 respond. The discussion below under “Unresolved Issues” is substantially the same discussion
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 25 ¹ In the D&R, we found that petitioner was the consumer of materials, and thus recommended a reaudit to reduce the
 26 measure of tax due with respect to petitioner’s consumption of materials to cost (i.e., the reaudit was to delete the markup
 27 with respect to the materials, only). The resulting reaudit reduced the measure of tax by \$17,624.68. However, in
 28 preparation for the Board hearing, we discovered that the reaudit had incorrectly reduced the measure of tax with respect to
 all property to cost. The correction of that error reduced the amount of the adjustment.

² This amount is net of interest of \$6,429.27 for the period September 3, 2008, through June 24, 2009, the period for which
 the Board ordered relief of interest.

1 included in the original summary we prepared for this appeal, and remains applicable subject to the
2 post-hearing adjustments we recommend, which are discussed under “Post Hearing Developments.”

3 UNRESOLVED ISSUES

4 **Issue 1:** Whether adjustments are warranted to the amount of unreported sales. We
5 recommend no further adjustments.

6 Petitioner sells and installs television satellite equipment, and it entered into a sales agency
7 agreement (consumer sales agreement) with DirecTV in November 1997. This contract appears to
8 relate exclusively to equipment and programming package subscriptions for single-family dwellings.
9 The introductory paragraph states petitioner operates a retail business selling, installing, and
10 maintaining satellite equipment. The contract further states petitioner conducts the equipment sales
11 and installation business for its own account only and not as the agent for DirecTV. Moreover,
12 paragraph 18.11 places responsibility for sales tax squarely with petitioner. In July 1999, petitioner
13 entered into a commercial dealer agreement with DirecTV, which authorized petitioner to sell
14 programming package subscriptions to commercial establishments. Similar to the sales agency
15 agreement, the commercial dealer agreement states that DirecTV had no responsibility whatsoever in
16 connection with the equipment and that petitioner was an independent contractor. Paragraph 4.11.1
17 states petitioner shall perform all actions “including ... collection of sales ... taxes ...” In October
18 1997 and again in July 2003, petitioner provided a blanket resale certificate to DirecTV’s sales
19 management agent, DSI Distributing (DSI), stating, in part, that petitioner was doing business as a
20 retailer. Petitioner ordered satellite equipment, including receivers, digital video recorders, dish
21 antennae, cable, wire, connectors, and other consumables, as well as other electronic appliances such
22 as televisions, refrigerators and related items, from DSI.

23 A potential customer might have contacted petitioner directly, or if first contacting DirecTV,
24 would have been referred to petitioner. Petitioner then made contact with the customer to install and
25 set up the equipment after the customer signed a Satellite Application under petitioner’s name (copies
26 attached as exhibit 4 to the D&R). As explained in the D&R, DirecTV apparently collected all
27 amounts due (that is, both for the equipment sold by petitioner and for satellite services provided by
28 DirecTV), and remitted petitioner’s portion to petitioner.

1 During the audit, the Sales and Use Tax Department (Department) noted substantial differences
2 between reported sales and the cost of equipment purchased for resale. The Department concluded
3 petitioner was selling bundled transactions and, using California Code of Regulations, title 18, section
4 (Regulation) 1585 as a guide, found that sales tax was due on the selling price of equipment included
5 in the bundled price.³ The Department ascertained that petitioner informed its customers they would
6 be charged \$155 per unit in the event they failed to subscribe to DirecTV programming within a stated
7 period of time after installation of the equipment. The Department regarded \$155 as the “unbundled
8 price,” and it compared that amount to cost to compute a markup of 19.03 percent. Then, to establish
9 the audited sales for 2002 and 2003, the Department applied a markup factor of 1.1903 to the recorded
10 purchases. Since purchase invoices were not available for 2001 or 2004, the Department computed
11 average quarterly sales for the last three quarters of 2001 and the year 2004 using the sales information
12 for 2002 and 2003.

13 Petitioner contends it was not the retailer of the satellite equipment. In essence, petitioner
14 claims that customers purchased equipment from DirecTV and that petitioner only held the equipment
15 on behalf of DirecTV until its delivery of the equipment to the customer as the agent of DirecTV. As
16 support, petitioner provided a copy of a September 14, 2007 internal memorandum from the
17 Department regarding a different matter which, according to petitioner, reached a different result.⁴
18 Petitioner also alleges that the audited amount of taxable sales is excessive. Regarding paragraph
19 18.11 of the consumer sales agreement, petitioner claims that its obligation to collect sales tax
20 reimbursement from its customers was never triggered because DirecTV never gave it the correct rate
21 as required by that provision.

22 It was petitioner who actually contracted with the customer (in its own name per the Satellite
23 Application) for the sale of the equipment, and thus it is clear that petitioner was the retailer of the
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26 ³ Although Regulation 1585 applies expressly to wireless telecommunication equipment and there is no specific regulation
27 that governs satellite television equipment, the way petitioner sold the equipment is substantially similar to the way bundled
28 wireless telecommunication equipment is sold. Accordingly, we find the Department’s reference to Regulation 1585 to
establish the deficiency here is reasonable.

⁴ Petitioner has not argued that the deficiency is due to its reasonable reliance on erroneous written advice and, in any event,
we note that the memorandum related to an entirely different taxpayer and find that it does not provide any basis for relief.

1 equipment to the customers with whom it contracted.⁵ That the parties agreed that DirecTV would
2 collect all amounts due, including for the sale of the equipment, and remit petitioner's portion to
3 petitioner does not alter the fact that petitioner had made the retail sales of equipment. We note that
4 this conclusion is consistent with petitioner's having purchased the equipment under a resale
5 certificate, and with the terms of the agreement between petitioner and DirecTV. That agreement
6 states that petitioner operated a retail business selling satellite equipment, that petitioner conducted the
7 equipment sales and installation business for its own account only and not as an agent for DirecTV,
8 and that petitioner was responsible for sales tax. Since petitioner has not provided evidence to support
9 any adjustment other than as noted above, we recommend no further adjustments.

10 **Issue 2:** Whether relief of interest is warranted. The Board has ordered relief of the interest for
11 the period September 3, 2008, through June 24, 2009, which is a reduction of the interest due of
12 \$6,429.27.⁶ We recommend no further relief of interest.

13 Petitioner submitted a Request for Relief of Penalty, signed under penalty of perjury, which
14 requests relief from penalties assessed for the period January 1, 2000, to the present, stating that the
15 audit issue has yet to be resolved "due in large part to delays by the Board of Equalization." We have
16 asked petitioner on at least two occasions to submit arguments and evidence to support its request for
17 relief, but have received no response. In the absence of clarification and in an abundance of caution,
18 we have treated this request as one for relief of all interest imposed (since the audit period begins
19 April 1, 2001, more than a year after the date specified in the request), based on unreasonable delay,
20 under Revenue and Taxation Code section 6593.5.

21 Some of the delays in processing this case were the result of actions by petitioner, and some of
22 the delays were the result of an unforeseen and unavoidable series of retirements and transfers in the
23 Appeals Division during the pendency of the appeal. The Board has ordered relief of the interest that
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25 ⁵ As noted above, we found that petitioner was the consumer of materials such as cable and connectors that it furnished and
26 installed, and this reduced the deficiency by the amount of the markup the Department calculated with respect to those
27 materials. Petitioner owes tax on the cost of those materials without regard to whether it sold the other property to the
28 customers at retail (as we find) or was selling the other property to DirecTV for resale (which we reject).

⁶ The Department's February 23, 2011 memorandum to the Appeals Division mistakenly refers to the amount of the
amnesty interest penalty, \$5,143.38, as the amount of interest to be relieved per the Board's order.

1 accrued during the period September 3, 2008, through June 24, 2009, to account for delays in issuing
2 the D&R. Thus, the Board has already ordered the relief of interest it deemed appropriate, and we
3 recommend no further relief of interest.

4 **Issue 3:** Whether relief of the amnesty interest penalty is warranted. We find it is not.

5 Since petitioner did not apply for amnesty or pay the amnesty-eligible tax and interest by
6 March 31, 2005, an amnesty interest penalty \$5,143.38 (after the post-Board hearing reaudit) will be
7 added when the liability becomes final. In an abundance of caution, we have treated petitioner's
8 request for relief as covering this penalty even though the statements in that request do not relate
9 specifically to petitioner's failure to participate in the amnesty program. Although we requested that
10 petitioner clarify its request, it has not done so. Accordingly, we find that petitioner has not stated a
11 basis for relief of the amnesty interest penalty, and find that relief is not warranted.

12 **POST HEARING DEVELOPMENTS**

13 . At the Board hearing, the Board concluded that satellite dishes attached to real property were
14 fixtures and that there was no transfer of title before installation. Accordingly, applying the applicable
15 provisions of California Code of Regulations, title 18, section 1521, the Board ordered that the
16 measure of tax related to satellite dishes attached to real property be reduced to the cost of those
17 satellite dishes to petitioner. That is, since the Department calculated this deficiency by adding a
18 markup to petitioner's cost of the satellite dishes, the Board ordered that the amount of the markup
19 related to satellite dishes attached to become real property be removed from the measure of deficiency,
20 while retaining the amount of the markup in the measure of deficiency with respect to any satellite
21 dishes that were not attached to become real property. The Department concluded it was unlikely that
22 there were significant numbers of free-standing satellite dishes sold and thus deleted from the measure
23 of deficiency the markup with respect to *all* satellite dishes. The effect of that adjustment is a
24 reduction in the understated measure of tax reported of \$11,578, from \$1,281,747 to \$1,207,169. We
25 recommend no further adjustment.

26 The Board also directed the Department to further review the September 14, 2007,
27 memorandum regarding another taxpayer (mentioned in the prior summary), which reached a different
28 conclusion regarding the application of tax. Petitioner had argued that its circumstances were similar

1 to the other taxpayer's and that the conclusions in the memorandum should be applied here. We find
2 that petitioner's circumstances are readily distinguishable from those described regarding the other
3 taxpayer in the September 14, 2007, memorandum. Most significantly, in the other taxpayer's
4 transactions, DirectTV *leased* the equipment to its subscribers. In contrast, subscribers contracting
5 with petitioner were *purchasing* the equipment. We note that DirectTV did not begin leasing
6 equipment until March 1, 2006, more than a year after the end of the audit period in this matter,
7 December 31, 2004. Under the new lease program, DirectTV buys the equipment from the dealer
8 upon activation of the equipment, for lease to subscribers. However, under the previous dealer
9 contract, which was in effect during this audit of petitioner, the dealers sold the equipment directly to
10 subscribers, not as an agent for DirectTV. Thus, there is no similarity between the contracting
11 methods addressed in the September 14, 2007 memorandum and those in effect during this audit of
12 petitioner, and the conclusions in that memorandum regarding the application of tax are not applicable
13 here.

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15 Summary prepared by Deborah A. Cumins, Business Taxes Specialist III
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MARKUP TABLE

Percentage of taxable vs. nontaxable purchases	100%
Mark-up percentage developed (tangible personal property sold, excluding materials used by petitioner to install the equipment)	19.03%
Self-consumption allowed in dollars	None
Pilferage allowed in dollars	None