

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 R-TEK COMMUNICATIONS, INC.) Account Number: SR KH 100-966218
) Case ID 461499
 6 Petitioner) Stockton, San Joaquin County

7 Type of Business: Construction Contractor

8 Liability Period: 02/05/04 – 06/30/06

9 Item Amount in Dispute

10 Unreported cost of materials consumed \$602,976
 11 Penalty for failure to file returns \$1,037

	<u>Tax</u>	<u>Penalty</u>
12 As determined, protested	\$51,661.51	\$1,037.06
13 Proposed tax redetermination	\$51,661.51	
14 Interest through 5/31/11	26,096.94	
15 Failure-to-file penalty	<u>1,037.06</u>	
16 Total tax, interest, and penalty	<u>\$78,795.51</u>	
17 Monthly interest beginning 6/1/11	<u>\$301.36</u>	

17 This matter was previously scheduled for Board hearing on November 18, 2010, but was
 18 postponed at petitioner's request due to a medical emergency. It was rescheduled for Board hearing on
 19 February 22, 2011, but was again postponed because petitioner recently retained new representation.
 20 This matter was then rescheduled for Board hearing on May 25, 2011. Petitioner has now waived its
 21 right to appear at a Board hearing. Accordingly, the Board Proceedings Division informed petitioner
 22 that this matter will be presented to the Board for decision without oral hearing.

23 UNRESOLVED ISSUES

24 **Issue 1:** Whether petitioner is entitled to an offset against its tax liability for tax allegedly paid
 25 by another. We conclude that petitioner is not entitled to any offset.

26 During the audit of a vendor of construction materials, the Sales and Use Tax Department
 27 (Department) noted that the vendor had accepted a resale certificate from petitioner. The Department
 28 thereafter conducted an audit of petitioner, a construction subcontractor who furnished and installed

1 materials (coaxial and other communications wire and cable) under lump sum construction contracts
2 with prime contractors who sold new homes to the public. During the audit, the Department found that
3 petitioner had originally been operated as a sole proprietor, owned by Mr. Rodney Place, and that the
4 business had been incorporated on February 5, 2004, as R-Tek Communications, Inc. (petitioner), with
5 Mr. Place as the president. Thus, while the audit period commences July 1, 2003, the period covered
6 by the Notice of Determination under review here begins February 5, 2004, when petitioner
7 commenced as a corporation.

8 Petitioner did not obtain a seller's permit, instead using the seller's permit issued to the
9 predecessor sole proprietor to file annual sales and use tax returns and to purchase construction
10 materials for resale. The Department also found that petitioner's business had been terminated on June
11 30, 2006, and its corporate status has been suspended since July 2, 2007. The Department assigned an
12 arbitrary account number (SR KH 100-966218) to petitioner for the purpose of issuing a Notice of
13 Determination. The Department closed the seller's permit issued to the sole proprietor and transferred
14 to the arbitrary account number all sales and use tax information related to petitioner's post-
15 incorporation business.

16 The Department's audit disclosed \$551,444 in purchases of materials made without payment of
17 tax or tax reimbursement to the vendors for the period July 1, 2003, through September 30, 2005.
18 Since petitioner and the sole proprietor had reported taxable consumption of \$52,773 for the fiscal year
19 ending June 30, 2004, the Department established that petitioner and the sole proprietor understated
20 their reported taxable purchases by \$498,671. Of this amount, the Department calculated that
21 \$422,082 was petitioner's portion for the period February 5, 2004, through September 30, 2005. Based
22 on this amount, the Department estimated unreported taxable purchases of \$180,894 for the period
23 October 1, 2005, through June 30, 2006, resulting in a Notice of Determination issued to petitioner for
24 unreported taxable purchases of construction materials for use of \$602,976, plus a penalty of \$1,037.06
25 for failure to file a return for the period January 1, 2006, through June 30, 2006.

26 Petitioner filed a timely petition for redetermination arguing that, although it does not dispute
27 the taxable measure established by the Department, it is not responsible for the liabilities assessed in
28 the determination because, upon the sale of the newly constructed homes, the prime contractors

1 collected, reported, and paid all taxes associated with petitioner's consumption of the materials. At the
2 appeals conference, petitioner also contended that the business had been purchased on April 1, 2004,
3 by another corporation known only as "Comm360," which absorbed petitioner and took over
4 petitioner's business. Petitioner argues that Comm360's purchase of petitioner's business absolves
5 petitioner from the liability asserted in the determination. Petitioner also argues that Mr. Place's
6 signature was forged on the resale certificates bearing the seller's permit number of the sole proprietor
7 in order to purchase materials without payment of tax or tax reimbursement in the name of petitioner.
8 Petitioner submitted several documents which allegedly evidence the forged signature.

9 We find that the signatures on the allegedly forged documents appear to be very similar to the
10 signatures on other documents signed by Mr. Place, such as the application for his seller's permit and
11 the Waiver of Limitations. Additionally, petitioner has not reported such alleged forgery to any law
12 enforcement agencies or creditors. Thus, we reject petitioner's contention that it is the victim of
13 forgery.

14 Since petitioner acquired materials from vendors under resale certificates, it owes use tax on its
15 use of such materials.¹ The evidence is that petitioner consumed all such materials. Accordingly, it
16 owes use tax on its purchase price of all such materials. We note that under very limited
17 circumstances, a construction contractor acting as a subcontractor may obtain an offset against the
18 taxes it owes for the taxes paid by the general contractor. (Cal. Code Regs., tit. 18, § 1700, subd.
19 (b)(5)(B).) However, petitioner has the burden of proving that the prime contractor did in fact pay tax
20 to the state. (Cal. Code Regs., tit. 18, § 1700, subd. (b)(4).) Not only has petitioner not done so, based
21 on the facts as we understand them, it appears clear that the circumstances could not come within the
22 offset provisions. Petitioner states that it performed the construction contracts for prime contractors
23 who sold the new homes. Based on our experience, we find it virtually inconceivable that prime
24 contractors who sell homes as part of real estate transactions would collect an amount as sales tax from
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26 ¹ Since petitioner was not in the business of selling materials, it was not entitled to purchase them under resale certificates.
27 However, for the dispute here, the only issue in this context is whether petitioner did purchase property under resale
28 certificates, not whether it issued the resale certificates improperly. Since we find petitioner did make the purchases
pursuant to resale certificates, it owes use tax on its use of such property.

1 the new home purchasers and remit such amounts to the Board. In any event, there is no evidence to
2 support an offset, and we thus conclude no offset is warranted.

3 Similarly, petitioner has not submitted any evidence, other than Mr. Place's statements, to
4 support its second argument, that Comm360 acquired its operations and took over its business on
5 April 1, 2004, and thus, Comm360 became liable for the tax at issue. The evidence shows that the
6 business was operated by petitioner through the end of the liability period, and we therefore conclude
7 that no adjustments are warranted for this argument.

8 **Issue 2:** Whether the penalty for failure to file returns for the period January 1, 2006, through
9 June 30, 2006, should be relieved. We find relief is not warranted.

10 We explained to petitioner that it could request relief of the penalty and provided a form it
11 could use to do so. Petitioner failed to respond. Thus, we have no basis to consider recommending
12 relief of the penalty.

13 **OTHER DEVELOPMENTS**

14 None.

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16 Summary prepared by Pete Lee, Business Taxes Specialist II
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