

CALIFORNIA STATE BOARD OF EQUALIZATION

APPEALS DIVISION FINAL ACTION SUMMARY

In the Matter of the Administrative Protest)
 Under the Sales and Use Tax Law of:)
 ON SPORTS, INC.) Account Number: SR KH 97-659210
) Case ID 334978
)
 Taxpayer) Stockton, San Joaquin County

Type of Business: Manufacturer and Distributor of Sports apparel

Audit Period: 7/1/00 to 9/30/03

<u>Item</u>	<u>Measure in Dispute</u>	<u>Tax</u>	<u>Penalty</u>
Disallowed claimed sales for resale	\$681,680		
As established in the audit		\$61,028.79	
Credit for tax reported on Amnesty returns As determined		<u>-42,477.00</u> \$18,551.79	
Finality penalty			\$1,678.94
Adjustment: Appeals Division		-3,354.74	-1,678.94
Sales and Use Tax Department		-1,505.00 ¹	
Post hearing adjustment		<u>-500.59</u>	<u> </u>
Proposed tax liability		\$13,191.46	<u>\$0.00</u>
Concurred in amount		-3,858.87	
Add back tax reported on amnesty returns		+43,982.00	
Protested		<u>\$53,314.59</u>	
Audited tax less reaudit adjustments		\$57,173.46 ²	
Interest to 1/31/10		<u>1,994.37</u>	
Total tax and interest		\$59,167.83	
Tax reported on amnesty returns		-43,982.00	
Payments against determination		<u>-12,502.48³</u>	
Balance		<u>\$2,683.35</u>	
Monthly interest beginning 2/1/10		<u>\$4.02</u>	

¹ Taxpayer filed an amnesty return for the fourth quarter 2000 (4Q00) showing a tax credit of \$1,505. Since an amnesty return cannot show a credit, the 4Q00 amnesty return was adjusted to zero. Thus an adjustment has been made to reflect that tax of \$43,982 was reported on amnesty returns rather than the original \$42,477.

² \$61,028.79 - (\$3,354.74 + \$500.59) = \$57,173.46.

³ In the original Board hearing summary, we erroneously showed that payments were \$13,506.48 (which actually should have been \$1 more, \$13,507.48, based on our understanding at that time). However, we have now determined that actual payments made against the audit liability at the time of the Board hearing summary were \$12,002.48. The error of \$1,505 represents the credit reported on the 4Q00 amnesty tax return, that the Department disallowed, thereby increasing the tax reported on amnesty returns from \$42,477 to \$43,982, because amnesty returns cannot show a credit amount.

1 The Board heard this matter on July 21, 2009, and granted taxpayer 30 days to provide
2 additional documentation to support its contentions and 30 days for the Sales and Use Tax Department
3 (Department) to respond. The Department reviewed the documentation provided by taxpayer and
4 prepared adjustment schedules dated October 1, 2009, and by memorandum dated October 5, 2009, the
5 Department concludes that the measure of tax should be reduced by an additional \$6,358. We agree.
6 We note that the adjustments represented disallowed sales for resale to a customer which were not
7 related to the protested items in Issues 1 and 2 below.

8 UNRESOLVED ISSUES

9 **Issue 1:** Whether taxpayer has established that sales made to Knotty Team Sports were sales
10 for resale. We conclude that taxpayer has not.

11 The Department examined taxpayer's claimed sales for resale on an actual basis and accepted
12 as nontaxable those sales which were supported by resale certificates, as well as those sales for which
13 XYZ responses indicated that the sales were for resale. In instances where no XYZ response was
14 received, the Department examined the Board's computerized records and allowed the claimed sales
15 when the records indicated that the customer was in the business of selling apparel. In instances where
16 the Department was unable to establish whether the taxpayer's customers held a seller's permit or
17 resold the merchandise purchased from taxpayer, or where no XYZ response was received from
18 taxpayer's customers, the Department disallowed the taxpayer's claimed sales for resale. In our
19 Decision and Recommendation (D&R) and Supplemental D&R (SD&R), we recommended several
20 reductions to the disallowed claimed sales for resale.

21 The only remaining protested transactions for this item are taxpayer's sales to Knotty Team
22 Sports, which taxpayer contends were sales for resale even though Knotty Team Sports did not issue a
23 resale certificate to taxpayer or respond to the XYZ letter. Taxpayer provided the purchase history for
24 Knotty Team Sports as well as a few copies of invoices which taxpayer believes show that these sales
25 were for resale. Taxpayer maintained that Knotty Team Sports was a retailer of sports apparel and that
26 its sales to Knotty Team Sports were of such a high volume and frequency that it is clear that the
27 merchandise was resold despite the fact that the Department could not locate a seller's permit for this
28 customer. Taxpayer believes that numerous adjustments made by the Department were for sales for

1 resale to other similar retailers and that these disallowed claimed resales should be allowed as well.

2 Over a two-year period, taxpayer made 94 sales to Knotty Team Sports for a total of
3 \$19,569.20 for multiple quantities and sizes of similar items. This pattern of sales is consistent with
4 sales for resale *but* is also consistent with purchases by a customer for its own use. Approximately 60
5 percent of the invoices for sales to this customer were for sales under \$250, approximately 20 percent
6 of the invoices were for sales from \$251 to \$500, and 20 percent were for sales from \$501 to \$1,273.
7 In its January 14, 2008 correspondence, taxpayer indicated that the products sold to Knotty Team
8 Sports were resold through Knotty's retail location.⁴ However, our search for a business at the noted
9 address was unsuccessful, and based on an aerial view of the location, it appears to be a residence in a
10 residential area. Based on this and the lack of the purchaser's registration as a seller, the failure of
11 taxpayer to have taken and retained a resale certificate, and the failure of the purchaser to respond to
12 the XYZ letter, we conclude that taxpayer has failed to establish that Knotty Team Sports actually
13 resold the merchandise purchased from taxpayer, and recommend no further adjustments.

14 **Issue 2:** Whether taxpayer's sales to nonprofit youth sport organizations (YSO) were sales for
15 resale. We find that taxpayer has not established that the sales were for resale.

16 Taxpayer sold athletic apparel to YSO which claim to be non-taxable youth organizations as
17 defined by Internal Revenue Code section 501, subdivision (c). Taxpayer did not collect sales tax
18 reimbursement or remit sales tax in connection with these sales. The Department determined that the
19 YSO were not retailers because the YSO failed to satisfy the four conditions provided in California
20 Code of Regulations, title 18, section (Regulation) 1597, subdivision (h), to be considered a retailer.
21 Since the YSO were not retailers of the merchandise, that meant that taxpayer's sales were at retail
22 (either to the YSO as consumers or to the ultimate purchasers through taxpayer's agents, the YSO).
23 The Department thus disallowed all taxpayer's claimed sales for resale to the YSO.

24 Taxpayer contends that the YSO were retailers making retail sales of uniforms. Taxpayer
25 further contends that the purchase history of these leagues support the fact that the YSO sold the
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27 ⁴ Taxpayer makes this statement on page 2 of the summary in the correspondence binder dated January 14, 2008. In its
28 RFR dated July 11, 2008, taxpayer denies that this statement was made.

1 uniforms because they had to purchase new uniforms each season. Taxpayer supplied purchase history
2 for thirty YSO, website information showing merchandise for sale by some YSO, and signup forms
3 from some YSO showing the cost of the uniform was included in the registration fee.

4 In our D&R, we concluded that the YSO were not statutory consumers under Regulation 1597,
5 subdivision (e), because they did not produce the property they sold, so resolution of the issue of
6 whether taxpayer's sales to the YSO were for resale depended on whether the YSO were retailers or
7 were acting as agents of taxpayer. We found that the YSO were acting as taxpayer's agent in making
8 sales to consumers under Regulation 1597, subdivision (h), so that taxpayer was the retailer. In our
9 SD&R issued in response to taxpayer's Request for Reconsideration, we reversed both of these
10 findings. We found that taxpayer's sales to the YSO were direct sales to those persons, and that after
11 the sales to the YSO were complete, taxpayer had no further involvement, and the YSO's sales were
12 not made on taxpayer's behalf. Thus, we found that the YSO did not sell the merchandise as the agent
13 of taxpayer.

14 Since the YSO purchased the merchandise from taxpayer on their own behalf, they did so either
15 as consumers or as retailers. Contrary to the statement in the D&R, we found in the SD&R that the
16 property at issue did qualify as property produced by the members of the YSO, based on Business
17 Taxes Law Guide annotation 390.0130 (3/17/89).⁵ We also found that the YSO sold the merchandise
18 they purchased from taxpayer on an intermittent basis, and that the YSO were thus the consumers of
19 such property as provided in Regulation 1597, subdivision (e). Thus, taxpayer's sales to the YSO were
20 retail sales for which taxpayer is liable for sales tax.

21 AMNESTY

22 The amnesty interest penalty does not apply because taxpayer filed an application for amnesty
23 and entered into a qualifying installment payment plan.

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28 ⁵ Annotations are intended to provide guidance regarding the interpretation of the Sales and Use Tax Law with respect to
specific factual situations; they do not have the force and effect of law. (Cal. Code Regs., tit.18, § 5700, subds. (a)(1),
(c)(2).

RESOLVED ISSUES

In its October 5, 2009 memorandum, the Department found that five sales listed in the audit as sales to Darren Matsubara were actually sales made to Adidas America, for delivery to Darren Matsubara, which should be accepted as sales for resale. We agree, and we therefore recommend that the audited amount of disallowed claimed sales for resale be reduced by \$6,358, the total of the five sales to Adidas for delivery to Darren Matsubara.

We also recommend that relief from the penalty for failure to timely pay the determination be granted if taxpayer pays the remaining unpaid tax liability within 30 days of the mailing of the notice of the Board's final decision.

OTHER DEVELOPMENTS

None.

Summary prepared by Rey Obligacion, Business Taxes Specialist III, Retired