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:

FAMILY LEISURE PRODUCTS, INC.

Petitioner

Account Number: SR S OH 97-199866
Case ID 491614

Coeur D'Alene, Idaho

Type of Business: Retailer of spas and hot tubs

Audit period: 07/01/08 – 3/31/09

Item	Disputed Amount
Unreported taxable sales	$334,275

	Tax	Penalty
As determined:	$11,365.00	$1,136.50
Adjustment - Sales and Use Tax Department	+15,118.00	1,511.80
Proposed redetermination, protested	$26,483.00	$2,648.30

Proposed tax redetermination	$26,483.00
Interest through 9/30/11	5,416.83
Penalty for failure-to-file returns	2,648.30
Total tax, interest, and penalty	$34,548.13
Payments	-318.88
Balance Due	$34,229.25
Monthly interest beginning 10/1/11	$130.82

A Notice of Appeals Conference was mailed to petitioner's address of record, and the notice was not returned by the Post Office. Petitioner did not respond to the notice or appear at the appeals conference, which was held as scheduled. We thereafter sent petitioner a letter offering it the opportunity to provide any additional arguments and evidence in writing it wished us to consider, but it did not respond. This matter was scheduled for Board hearing on July 26, 2011, but was postponed at petitioner's request to allow additional time to prepare for hearing.

UNRESOLVED ISSUE

Issue: Whether adjustments are warranted to the asserted liability. We find no adjustments are warranted.

Petitioner, headquartered in Coeur D'Alene, Idaho with a Sacramento warehouse, sold spas and hot tubs. Petitioner obtained a seller's permit with an effective start date of March 1, 1998. In May 2009, it requested that its seller's permit be closed effective March 31, 2009, because it was no longer engaged in business in California.

Since petitioner did not file sales and use tax returns for the period July 1, 2008, through March 31, 2009, the Department computed audited taxable sales of $143,466 for this nine-month audit period based on the average taxable sales petitioner had reported for the preceding 12 months, plus 10 percent. Shortly after the Department issued the Notice of Determination for the audited deficiency, petitioner filed non-remittance returns for the audit period reporting total sales of $149,620 and claiming deductions for nontaxable labor of $13,343, exempt sales in interstate commerce of $85,929, sales tax reimbursement included in total sales of $6,285, returned merchandise of $7,060, and cash discounts of $2,293. The taxable sales petitioner reported on these late returns, $34,710, was $108,756 less than the audited taxable sales established by the Department. Although the Department requested additional information, petitioner provided no records or documentation to support its late returns.

The Department contacted petitioner's only supplier of hot tubs and spas, Softub's Inc., and obtained information indicating that, for the period July 1, 2008, through June 24, 2009, it made the following sales to petitioner: 1) sales of $287,151 shipped to "Family Leisure" through December 2008; 2) sales of $158,521 shipped to "Estes Express Freight in Sacramento" through October 2008; and 3) sales of $32,375 shipped to various individuals in the Sacramento area who appear to have been the consumers of the products, $14,950 of which occurred during the audit period. The Department regarded only the products shipped to "Family Leisure" as resold by petitioner in taxable sales. Although petitioner did not provide any documentation in support of exemption, the Department regarded the products shipped to "Express Freight" and to the individuals in California as having been resold by petitioner in exempt sales in interstate commerce. Nor did the Department add a markup to petitioner's cost of goods regarded as sold in taxable sales because the Department was unable to conduct a shelf test. Rather, it regarded petitioner's $287,151 cost of such property during the third and fourth quarters 2008 as its taxable gross receipts during those quarters. For the first quarter 2009,

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the Department retained the $47,124 measure of tax asserted in the Notice of Determination (the Department regarded this amount as accounting for the sale of merchandise in inventory at the start of the audit period). Thus, the Department computed audited taxable gross receipts for the audit period of $334,275, which is an increase in the measure of tax assessed by the Notice of Determination of $190,809. The Department asserted tax on the amount of the increased measure pursuant to Revenue and Taxation Code section 6563.

Petitioner did not appear at the conference or respond to our post-conference letter inviting further submissions, and has not otherwise provided any documentation to support its late-filed returns. In fact, based on the information available, it appears that even with its asserted increase, the Department has assessed less tax than is due. Products purchased for $14,950 were delivered by Softub's on petitioner's behalf to individuals in California during the audit period. Although these appear to have been drop shipped directly to petitioner's retail purchasers, the Department accepted these all as nontaxable sales. The Department also accepted that products purchased for $158,521 and delivered to Estes Express Freight during the audit period were resold in exempt sales in interstate commerce. Estes Express Freight is a common carrier and could well have shipped these products to points outside California pursuant to petitioner's retail sales that required such out-of-state delivery. Estes Express might also have shipped some or all of these products to locations within California so that tax was properly applicable. The Department was certainly generous in regarding all such transactions as qualifying for the exemption. Finally, we note that the Department based its assessment solely on petitioner's cost of goods, even though it appears certain that petitioner made the sales at a price above cost. In sum, we find that the asserted liability is not overstated, and we thus recommend no adjustment.

OTHER DEVELOPMENTS

We advised petitioner by letter that it could submit a request for relief of the failure-to-file penalties imposed as a result of its failure to file timely returns for the audit period. Petitioner has not done so, and we thus have no basis on which to consider recommending relief of any penalties.

Summary prepared by Thea Etheridge, Business Taxes Specialist II

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