2020 – OTA – 069P
Precedential

OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of: **PASATIEMPO INVESTMENTS, LTD PTN,[1] dba Back Nine Grill & Bar[2]**	) OTA Case No. 18103908) CDTFA Case No. 909789) CDTFA Acct. No. 52-056809))) Date Issued: November 20, 2019

OPINION

Representing the Parties:

For Appellant: Richard Gregersen, CEO

For Respondent: Jarrett Noble, Tax Counsel III

J. LAMBERT, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 6561, Pasatiempo Investments, LTD PTN (appellant) appeals a decision issued by respondent California Department of Tax and Fee Administration (CDTFA)[3] denying appellant's timely petition for redetermination of CDTFA's Notice of Determination (NOD), which assessed $67,983.48 additional tax, plus accrued interest, for the period April 1, 2011, through September 30, 2013 (liability period).

Appellant waived its right to an oral hearing and therefore the matter is being decided based on the written record.

ISSUE

Whether appellant is liable for unreported taxable sales.

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[1] Appellant identified itself to respondent as "Pasatiempo Investments, LTD PTN." However, the name listed with the California Secretary of State is "Pasatiempo Investments, A California Limited Partnership."

[2] The dba of "Peachwood's" was changed to "Back Nine Grill & Bar" on April 20, 2015, after the liability period.

[3] Sales taxes were formerly administered by the State Board of Equalization (board). Effective July 1, 2017, functions of the board relevant to this case were transferred to CDTFA. (Gov. Code, § 15570.22.) When referring to acts or events that occurred before July 1, 2017, "CDTFA" shall refer to its predecessor, the board.

FACTUAL FINDINGS

1. Appellant, a California limited partnership, owned the Inn at Pasatiempo, a 54-room hotel, with an onsite restaurant and bar known as Peachwood's Grill & Bar (Peachwood's), located in Santa Cruz, California.[4]
2. During the liability period, appellant held a seller's permit to operate the restaurant and bar under the dba Peachwood's.
3. Appellant operated Peachwood's and filed its sales and use tax returns (SUTRs) prior to, and throughout, the liability period. On February 15, 1992, appellant and Peachwood's Management, Inc. (PMI) entered into a lease agreement, under which PMI agreed to operate the restaurant and bar using the same business name, location, furniture, equipment, glassware, silverware, etc. previously used by appellant.
4. The lease agreement states that appellant will transfer its liquor license to PMI, dictates the days and hours PMI operates the restaurant and bar, and requires that PMI continue to provide a European breakfast and room service consistent with that previously provided by appellant. The lease agreement requires appellant's approval regarding menu offerings, restaurant decor, quality of service, portion size, average food cost, and food quality.
6. By letter dated March 4, 1992, appellant's general partner informed CDTFA that appellant leased the restaurant and bar to PMI, and that PMI's president and owner would obtain a new seller's permit upon securing a temporary liquor license.
7. However, appellant held the liquor license throughout the liability period, and PMI did not obtain a liquor license or a seller's permit to operate Peachwood's.
8. Appellant and PMI signed a First Lease Amendment (FLA) in October 2010, which required PMI to remit all sales tax payments directly to appellant, which would then file all SUTRs and pay CDTFA the taxes due. In the FLA, PMI agreed not to contact or communicate with CDTFA.
9. After executing the lease agreement, appellant continued to report restaurant sales in SUTRs filed under its own seller's permit, reporting taxable sales of $996,065 for the liability period.

[4] There is evidence that indicates the name of the restaurant may have been Peachwood's Bar & Grill and Peachwood's Steakhouse at various times.

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10. PMI vacated the leased premises at appellant's request near the end of October 2012.
11. CDTFA commenced an audit of appellant for the liability period. To verify reported amounts, CDTFA examined PMI's bank statements for July 2010 through December 2012. In addition, CDTFA obtained copies of federal Forms 1099-K[5] issued by credit card processors to "Peachwood's Grill and Bar," "Pasatiempo Investments," and "Peachwood's Steakhouse" indicating gross receipts generated from restaurant sales during 2011 and 2012.
12. CDTFA issued a Field Billing Order to appellant dated July 3, 2015, which found one deficiency item, unreported taxable sales of $782,221, based on the difference between reported taxable sales and bank deposits for the liability period.
13. CDTFA issued an NOD to appellant on July 10, 2015, for the liability period for $67,983.48 tax, plus accrued interest.
14. Appellant filed a timely petition for redetermination.
15. CDTFA issued a Decision on September 18, 2018, reducing unreported taxable sales by $18,014, from $782,221 to $764,207, based on a calculation error. The decision otherwise denied the petition. This timely appeal followed.

DISCUSSION

California imposes sales tax on a retailer's retail sales of tangible personal property in this state, measured by the retailer's gross receipts from such sales, unless the sale is specifically exempt or excluded from taxation by statute. (R&TC, § 6051.) A retailer is defined as "[e]very seller who makes a retail sale or sales of tangible personal property." (R&TC, § 6015, subd. (a)(l).) Every person desiring to engage in or conduct business as a seller within this state shall file with CDTFA an application for a seller's permit. (R&TC, § 6066, subd. (a).) A return shall be filed by every seller and by every person who is liable for the sales tax. (R&TC, § 6452, subd. (b).) Although gross receipts derived from the sale of "food products" are generally exempt from the sales tax, sales of food served in a restaurant and sales of hot prepared food are subject to tax. (R&TC, § 6359, subds.(a), (d)(2), (d)(7).)

[5] Federal Form 1099-K, "Payment Card and Third-Party Network Transactions," is a form used by credit card companies and third-party processors (payment settlement agencies) to report the gross amount of reportable payments made to the taxpayer by the payment settlement agency.

Under California Code of Regulations, title 18, section (Regulation) 1699, subdivision (d), a prime retailer may be held jointly and severally liable for any sales and use taxes imposed on unreported retail sales made by a retailer operating as a concessionaire on the prime retailer's retail business premises. For these purposes, a concessionaire is defined as an independent retailer who is authorized, through contract with, or permission of, the prime retailer to operate within the perimeter of the prime retailer's business premises, which to all intents and purposes appear to be wholly under the control of that prime retailer, and to make retail sales that to the general public might reasonably be believed to be the transactions of the prime retailer. (Cal. Code Regs., tit. 18, § 1699, subd. (d).)

A prime retailer is relieved of liability for sales and use tax incurred by its concessionaire for periods for which the concessionaire holds a seller's permit for the business location, or where the prime retailer retains a written statement taken in good faith in which the concessionaire affirms that he or she holds a seller's permit for that location. (Cal. Code Regs., tit. 18, § 1699, subd. (d).) Some factors indicating that a retailer is not operating as a concessionaire include: appearing to the public as a separate and autonomous business from the prime retailer (e.g., signs naming each business, separate cash registers, and receipts or invoices printed with retailer's own business name), maintaining separate business records (particularly with respect to sales), establishing its own selling prices, making independent business decisions (such as hiring and firing employees or purchasing inventory and supplies), registering as a separate business with regulatory agencies (such as CDTFA, the Employment Development Department, and the Secretary of State), and depositing funds into separate accounts. (*Ibid*.)

Except as explained in Regulation section 1699, subdivision (f)(3), a person holding a seller's permit will be held liable for any taxes, interest, and penalties incurred, through the date on which the CDTFA is notified to cancel the permit, by any other person who, with the permit holder's actual or constructive knowledge, uses the permit in any way. (Cal. Code Regs., tit. 18, § 1699, subd. (f)(2).) Regulation section 1699, subdivision (f)(3), states that, where the seller's permit holder does not establish that CDTFA received actual notice of a transfer of the business for which the permit was held and is thus liable for the taxes, interest, and penalties incurred by another person using that permit, that liability is limited to the quarter in which the business was transferred and the three subsequent quarters, and shall not include any penalties imposed on the other person for fraud or intent to evade the tax. (Cal. Code Regs., tit. 18, § 1699, subd. (f)(3).)

R&TC section 6071.1 states that a permitholder who fails to surrender a seller's permit upon transfer of a business shall be liable for any tax, interest, and penalty incurred by the transferee if the permitholder has actual or constructive knowledge that the transferee is using the permit in any manner. The predecessor's liability shall be limited to the quarter in which the business is transferred, and the three subsequent quarters. (R&TC, § 6071.1, subd. (a).)

CDTFA may determine a tax deficiency on the basis of any information which is in its possession or may come into its possession. (R&TC, §§ 6481, 6511.) When there is an appeal, CDTFA has a minimal, initial burden of showing that its determination is reasonable and rational. (See *Schuman Aviation Co. Ltd. v. U.S.* (D. Hawaii 2011) 816 F.Supp.2d 941, 950; *Todd v. McColgan* (1949) 89 Cal.App.2d 509, 514; *Appeal of Myers* (2001-SBE-001) 2001 WL 37126924.) If CDTFA carries that burden, the burden of proof shifts to the taxpayer to establish that a result differing from CDTFA's determination is warranted. (*Riley B's, Inc. v. State Bd. of Equalization* (1976) 61 Cal.App.3d 610, 616.) The applicable burden of proof is by a preponderance of the evidence, which means the taxpayer must establish that the circumstances it asserts are more likely than not to be correct. Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (See *id.*; see also *Appeal of Magidow* (82-SBE-274) 1982 WL 11930.)

Appellant contends that it is not liable for PMI's tax liability because PMI did not operate the restaurant as its concessionaire. Appellant also contends that it notified CDTFA of the transfer of its business to PMI and, therefore, its liability should be limited by Regulation section 1699, subdivision (f)(3), and R&TC section 6071.1.[6]

Here, appellant knowingly allowed (and in fact under the lease terms appellant required) PMI to operate under appellant's seller's permit. Therefore, appellant is liable for the tax applicable to PMI's sales made under appellant's seller's permit. Moreover, appellant did not transfer or sell its business to PMI, but instead appellant retained its business and required PMI to operate it. Regulation 1699, subdivision (f)(2), states that a permit holder is liable for taxes, interest, and penalties incurred "by any other person" who uses the permit "in any way," and

[6] Appellant also contends that the liability is barred by the 3-year statute of limitations for issuing a notice of a deficiency determination, pursuant to R&TC section 6452. However, appellant signed a Waiver of Limitation on April 3, 2015, agreeing to extend the statute of limitations to July 31, 2015, with regard to determinations mailed for the period from October 1, 2010, through March 31, 2012. The NOD was issued on July 10, 2015, within the extension period. Therefore, the liability is not barred by the statute of limitations.

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does not state that it applies only to circumstances involving a transferor and transferee. (See Cal. Code Regs., tit. 18, § 1699(f)(2).) Appellant's name was on the seller's permit and appellant had actual knowledge of PMI's use of the permit. (*Id.*; see also *In re Murgillo* (9th Cir. BAP 1995) 176 B.R. 524, 530 ["[T]he seller's permit is not transferable; thus, the taxing authority must rely on the named individual(s)."].) Accordingly, appellant is liable for the unreported taxable sales.[7]

Although the foregoing is dispositive of this appeal, appellant would also be liable for the tax because PMI operated as appellant's concessionaire, pursuant to Regulation 1699, subdivision (d). PMI continued to operate at the same location, under the same name, serving the same menu (with changes approved by appellant) and using the same equipment. Appellant dictated the days and hours PMI operated the restaurant and bar, required that PMI continue to provide a European breakfast and room service consistent with that previously provided, and required appellant's approval regarding menu offerings, restaurant decor, quality of service, portion size, average food cost, and food quality. Accordingly, we find that the general public would reasonably believe that PMI's retail sales were the transactions of appellant. Furthermore, appellant was solely responsible for the filing of SUTRs and making tax payments to CDTFA. In fact, PMI was not allowed to communicate with CDTFA. Additionally, 1099 forms show that income generated from PMI's restaurant sales were deposited directly into accounts in appellant's name. Thus, the evidence shows that PMI was authorized to operate the restaurant and bar, which was wholly under the control of appellant, and PMI made retail sales that might reasonably be believed to be the transactions of appellant. Accordingly, PMI operated as a concessionaire authorized by appellant, the prime retailer, thus making appellant jointly and severally liable for the taxes owed on the unreported retail sales attributed to PMI.

Based on the foregoing, we find that CDTFA's determination is reasonable and appellant has failed to establish that it is not liable for the tax owed for the liability period.

[7] We hold that the business was not transferred and, as a result, there is no limitation on appellant's liability. (See Cal. Code Regs., tit. 18, § 1699, subd. (f); Rev. & Tax Code, § 6071.1.)

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HOLDING

Appellant is liable for unreported taxable sales.

DISPOSITION

CDTFA's action in reducing the measure of unreported taxable sales by $18,014, from $782,221 to $764,207, but otherwise denying the petition, is sustained.

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Josh Lambert
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Josh Lambert
Administrative Law Judge

I concur:

DocuSigned by:
Tommy Leung
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Tommy Leung
Administrative Law Judge

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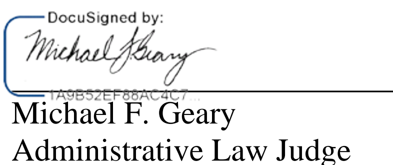
M. GEARY, concurring:

I concur in the majority's holding and disposition. However, given the parties contentions, I am not persuaded, that Regulation 1699, subdivision (f) applies in this case.



Michael F. Geary
Administrative Law Judge