OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of:	) OTA Case No. 18083582) CDTFA Case No. 571358
DISPLAYIT INCORPORATED	)
	)
	)
	)

OPINION

Representing the Parties:

For Appellant:	Javier Ramirez, Accountant Michael Cataldo, Representative
For Respondent:	Mariflor Jimenez, Hearing Representative Christopher Brooks, Tax Counsel IV Jason Parker, Chief of Headquarters Operations
For Office of Tax Appeals:	Lisa Burke, Business Taxes Specialist III

A. KWEE, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 6561, Displayit Incorporated (appellant) appeals a decision, as amended by two supplemental decisions, issued by respondent California Department of Tax and Fee Administration (CDTFA)[1] on appellant's petition for redetermination of a Notice of Determination (NOD) dated April 1, 2011 (collectively, CDTFA's decision). The NOD is for $978,154.54 in tax (representing a deficiency measure of $12,650,470), plus applicable interest, for the period July 1, 2005, through June 30, 2008 (audit period).[2] CDTFA's decision reduces the understated measure of tax from $12,650,470 to $10,898,367, but otherwise denies the petition. CDTFA performed a fourth reaudit during the pendency of this appeal before the

[1] Sales taxes were formerly administered by the Board of Equalization (board). Effective July 1, 2017, certain functions of the board relevant to this case were transferred to CDTFA. (Gov. Code, § 15570.22.) When this opinion refers to acts or events that occurred before July 1, 2017, "CDTFA" shall refer to its predecessor, the board, to the extent those acts or events would have been performed by CDTFA on and after July 1, 2017.

[2] The NOD includes a payment of $1,730, which reduces the tax to $976,424.54.

Office of Tax Appeals (OTA). As provided in the fourth reaudit, CDTFA concedes that the understated taxable measure be reduced to $7,585,963 (representing tax of $589,548).[3]

OTA Administrative Law Judges Andrew J. Kwee, Josh Aldrich, and Keith T. Long held an oral hearing for this matter on August 20, 2020.[4] At the conclusion of the hearing, the record was held open for additional briefing. Thereafter, this matter was submitted for a decision on October 26, 2020.

ISSUES

1. Whether appellant established that additional adjustments are warranted to the tax liability as determined by CDTFA.
2. Whether appellant established a basis for interest relief.

FACTUAL FINDINGS

1. Appellant manufactures, stores, ships, and installs tradeshow exhibit fixtures and store displays.
2. On its sales and use tax returns for the audit period, appellant reported total sales of $33,484,660. Appellant reduced reported total sales by claimed deductions of $2,454,224 for nontaxable sales for resale, $3,035,855 for nontaxable labor, $17,600,096 for exempt sales in interstate commerce, and $1,590,519 for tax-paid purchases resold. Appellant reported taxable sales of $8,803,966.
3. For audit, appellant provided its federal income tax returns, general ledger, sales journals, disbursements journal, sales invoices, purchase invoices, contracts, and resale certificates for some transactions.
4. CDTFA examined appellant's sales journals and compiled recorded nontaxable sales of $23,259,375.[5] Appellant's recorded nontaxable sales included 165 sales totaling $19,720,199. Each of these sales were in an amount exceeding $25,000. CDTFA

[3] CDTFA notified appellant of the proposed change in the liability by letter dated June 7, 2019. CDTFA also discussed the matter with appellant. CDTFA summarized the discussion in the June 7, 2019 letter.

[4] The oral hearing was noticed for Cerritos, California, and conducted electronically due to COVID-19.

[5] Recorded nontaxable sales exceed appellant's claimed nontaxable sales for resale, nontaxable labor, and exempt sales in interstate commerce, which total $23,090,175 for the audit period. This discrepancy has not been explained.

examined each sale exceeding $25,000 on an actual basis and disallowed deductions of sales for which appellant collected and retained sales tax reimbursement; unsupported claimed nontaxable sales for resale; unsupported claimed exempt sales in interstate commerce; and costs of tangible personal property used by appellant in the performance of construction contracts.[6] A substantial portion of appellant's claimed nontaxable sales of $25,000 or more were sales to Nextel of California, Inc., Nextel Systems Corporation, and Sprint Nextel (Sprint and related companies). CDTFA segregated its findings between sales over $25,000 to Sprint and related companies, and separated them out from sales over $25,000 to all other customers. For sales over $25,000 to Sprint and related companies, CDTFA disallowed claimed nontaxable sales of $6,347,090 (Audit Item 2). CDTFA also disallowed claimed nontaxable sales of $3,510,831 to all other customers (Audit Item 1).

5. CDTFA examined appellant's recorded nontaxable sales under $25,000 in a test of the third quarter of 2007 (3Q07). Of the recorded nontaxable sales totaling $546,296 for the test period, CDTFA disallowed sales totaling $103,695, which represented an error rate of 18.98 percent. CDTFA applied the error rate to appellant's recorded nontaxable sales of less than $25,000 for the audit period to establish a deficiency measure of $671,736 for disallowed claimed nontaxable sales of less than $25,000 (Audit Item 3).

6. Appellant deducted all of its credit card purchases as tax-paid purchases resold on its sales and use tax returns, after reducing credit card charges by an estimated amount for sales tax.[7] Based on CDTFA's examination of the available purchase invoices for a one-year test period, CDTFA found that many of the purchases paid by credit card were of services rather than of tangible personal property. Additionally, CDTFA found that appellant had issued resale certificates to most of its local vendors and thus, those transactions did not qualify for the deduction. CDTFA allowed appellant's deductions for tax-paid purchases from Home Depot and other large retailers but disallowed the remaining deductions. Based on its analysis of merchandise purchases paid by credit card for 2007, which totaled $611,756, CDTFA determined that appellant paid tax on

[6] For lump-sum construction contracts, CDTFA estimated that costs of materials and fixtures represented 33 percent of the invoiced price.

[7] Appellant estimated the amount of sales tax paid by dividing total merchandise purchases by 1.0775.

purchases totaling $49,137. CDTFA compared purchases of $562,619 for which appellant did not pay tax to its vendors ($611,756 - $49,137) with appellant's claimed tax-paid purchases resold deduction of $594,374 for 2007, and computed an error rate of 94.66 percent. CDTFA then applied the error rate to appellant's claimed tax-paid purchases resold deduction of $1,590,519 for the audit period to establish disallowed claimed deductions for tax-paid purchases resold of $1,505,586 (Audit Item 7).

7. CDTFA established a deficiency of $12,650,470, consisting of the following seven audit items: (1) disallowed claimed nontaxable sales of $25,000 or more to customers other than Sprint and related companies of $3,306,043; (2) disallowed claimed nontaxable sales of $25,000 or more to Sprint and related companies of $6,347,090; (3) disallowed claimed nontaxable sales under $25,000 of $671,736; (4) purchases of supplies subject to use tax of $48,298; (5) purchases of fixed assets subject to use tax of $70,602; (6) unreported taxable sales of $701,115 based on an analysis of the sales journal and sales tax accrual account; and (7) disallowed tax-paid purchases resold deductions of $1,505,586.[8]

8. On April 1, 2011, CDTFA issued a NOD for the liability disclosed by audit.

9. On or about April 26, 2011, appellant filed a timely petition for redetermination and provided additional documents, which CDTFA reviewed in a first reaudit.

10. On or about August 16, 2012, CDTFA completed the first reaudit. Results of the first reaudit showed a reduction of $264,458 to Audit Item 2, disallowed claimed nontaxable sales over $25,000 to Sprint and related companies.

11. On May 12, 2014, CDTFA issued a Decision and Recommendation (D&R) in which it recommended that Audit Items 1 and 2, disallowed claimed nontaxable sales over $25,000, be reduced by $24,986 and by $363,522, respectively, and that Audit Item 3, disallowed claimed nontaxable sales under $25,000, be reduced by $304,723. Otherwise, the D&R recommended that the petition be denied.

12. On or about July 15, 2014, during the second reaudit (to make the adjustments recommended in the D&R), CDTFA determined that it had reduced Audit Item 3, disallowed claimed nontaxable sales under $25,000, in error.

[8] Audit Items 3 through 6 are not at issue in this appeal.

13. In a Supplemental D&R dated November 10, 2014, CDTFA reversed its recommendation that Audit Item 3 be reduced. Thereafter, CDTFA completed the second reaudit on or about July 16, 2015.

14. On June 21, 2017, appellant filed an untimely request for reconsideration of the Supplemental D&R, contending that reductions to disallowed claimed nontaxable sales to Sprint and related companies were warranted in both Audit Items 2 and 3. In support of its position, appellant submitted documentation from Nextel of California, Inc. (Nextel), including detail of Nextel's use tax accrual for the third quarter of 2006 (3Q06) and 4Q06, purporting to show that Nextel accrued and reported use tax on disallowed claimed nontaxable sales to Sprint and related companies. Based on the new information, CDTFA began a third reaudit.

15. CDTFA completed the third reaudit on or about September 19, 2017. In the third reaudit, CDTFA allowed transactions over $25,000 supported by Nextel's use tax accrual detail on an actual basis, which resulted in an additional reduction of $1,363,595 to Audit Item 2.

16. On December 29, 2017, CDTFA issued its Second Supplemental D&R, in which it found that no other adjustments were warranted (beyond what was allowed in the third reaudit).

17. This timely appeal followed.

18. During appeal before OTA, appellant provided additional documentation with its opening brief filed on March 8, 2019. Upon review of the additional documentation, CDTFA performed a fourth reaudit.

19. CDTFA completed its fourth reaudit on or about June 6, 2019. CDTFA summarized the results of its fourth reaudit in a letter dated July 8, 2019. The fourth reaudit resulted in a reduction of $2,875,685 to Audit Item 2, disallowed claimed nontaxable sales of $25,000 or more to Sprint and related companies, and a reduction of $436,719 to Audit Item 3, disallowed claimed nontaxable sales under $25,000.

20. On appeal, CDTFA contends that no further adjustments are warranted, and the liability should be redetermined as set forth in CDTFA's fourth reaudit.[9]

[9] CDTFA submitted two different versions of its fourth reaudit workpapers to OTA. In an order dated December 13, 2019, OTA requested clarification. In a subsequent order dated February 3, 2020, and without objection from either party, OTA struck the incorrect version of CDTFA's fourth reaudit workpapers from the record.

21. During a pre-hearing conference held on July 30, 2020, appellant clarified that the remaining items at issue in this appeal are: (1) disallowed claimed nontaxable sales over $25,000 (excluding sales to Sprint and related companies) of $3,281,057 (Audit Item 1); (2) disallowed claimed nontaxable sales over $25,000 to Sprint and related companies of $1,744,288 (Audit Item 2); and (3) a disallowed tax-paid purchases resold deduction of $1,505,586 (Audit Item 7). In summary, the disputed taxable measure at issue in this appeal is $6,530,931.
22. On August 5, 2020, appellant filed a statement, signed under penalty of perjury, requesting interest relief on the basis that it took CDTFA over 10 years, three decisions, and five audits, to process appellant's appeal.
23. During the oral hearing appellant changed its position and indicated that it was also disputing Audit Item 3, disallowed claimed nontaxable sales under $25,000, of $235,017.
24. Following the oral hearing, the record was held open until October 26, 2020, to allow for additional briefing from the parties.

DISCUSSION

Issue 1: Whether appellant has established that additional adjustments are warranted to the tax liability as determined by CDTFA.

California imposes sales tax on a retailer's retail sales in this state of tangible personal property, measured by the retailer's gross receipts, unless the sale is specifically exempt or excluded from taxation by statute. (R&TC, §§ 6012, 6051.) For the purpose of the proper administration of the Sales and Use Tax Law and to prevent the evasion of the sales tax, the law presumes that all gross receipts are subject to tax until the contrary is established. (R&TC, § 6091.)

When CDTFA is not satisfied with the amount of tax reported by the taxpayer, or in the case of a failure to file a return, CDTFA may determine the amount required to be paid on the basis of any information which is in its possession or may come into its possession. (R&TC, §§ 6481, 6511.) In the case of an appeal, CDTFA has a minimal, initial burden of showing that its determination was reasonable and rational. (*Appeal of Talavera*, 2020-OTA-022P.) Once CDTFA has met its initial 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.) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (See *ibid*.; see also *Appeal of Magidow* (82-SBE-274) 1982 WL 11930.) It is the taxpayer's responsibility to maintain and make available for examination on request all records necessary to determine the correct tax liability, including bills, receipts, invoices, or other documents of original entry supporting the entries in the books of account. (R&TC, §§ 7053, 7054; Cal. Code Regs., tit. 18, § 1698(b)(1).)

The burden of proving that a sale of tangible personal property is not at retail is upon the seller unless the seller timely takes in good faith a certificate from the purchaser that the property is purchased for resale. (R&TC, § 6091.) If the seller does not timely obtain a valid and complete resale certificate, the seller will be relieved of liability for the tax only where the seller shows that the property: (1) was in fact resold by the purchaser prior to an intervening use;[10] (2) is being held for purposes of resale by the purchaser and there has been no intervening use; or (3) was consumed by the purchaser and tax was reported by the purchaser directly to CDTFA on the purchaser's returns or in an audit of the purchaser. (Cal. Code Regs., tit. 18, § 1668(e).) One method CDTFA authorizes to assist a seller to show that the sale was for resale or the tax was paid is obtaining "XYZ" letters signed by its customers.[11] (Cal. Code Regs., tit. 18, § 1668(f).) CDTFA is not required to relieve a seller from liability for tax based on a customer's response to an XYZ letter. (Cal. Code. Regs., tit. 18, § 1668(f)(3).) CDTFA may contact the purchaser or any other person to verify the responses in the XYZ letter. (Cal. Code Regs., tit. 18, § 1668(f)(3).)

A. Disallowed claimed nontaxable sales of $25,000 or more excluding sales to Sprint and related companies (Audit Item 1)

On appeal, for Audit Item 1, appellant only disputes disallowed sales to two customers: ES3, Inc. (ES3) and Art Impressions Licensing (AIL). First, the item appellant sold to AIL is described as a "Tradeshow Magic Booth for Magic 2007," and appellant sold it for $25,662. Appellant's records indicate that AIL is in Calabasas, California. Appellant shipped the property

[10] We use the term "intervening use" to mean a use for any purpose other than retention, demonstration, or display while holding it for sale in the regular course of business. (Cal. Code Regs., tit. 18, §§ 1668(e), 1669(a).)

[11] XYZ letters are letters in a form approved by CDTFA that are sent to some of or all the seller's purchasers inquiring as to the disposition of the property purchased from the seller.

to a trade show in Las Vegas, Nevada. The law creates a presumption that tangible personal property delivered outside this state to a person known by the retailer to be a California purchaser was purchased for storage, use, or consumption in this state. (R&TC, § 6247.) The retailer may rebut this presumption by timely taking a statement signed by the purchaser that the property was purchased for use at a designated point outside this state. (R&TC, § 6247.)

The use tax is imposed on the purchaser. (R&TC, § 6202.) A retailer engaged in business in this state must collect the use tax from the purchaser and remit it to the state. (R&TC, § 6203(a).) Here, appellant did not obtain a statement or any other supporting documentation from the purchaser. Therefore, we find that appellant failed to rebut the presumption that tax applies because it sold property outside this state to a known-California purchaser.

Second, appellant disputes four sales to ES3, which CDTFA disallowed based on a review of sales invoices from appellant to ES3. Three of the sales are for $185,295 each. This property is described as "Scion Backstage Tour Structures." The fourth sale to ES3 is for "Scion Backstage Tour Additions Graphics" for $34,220. The four sales to ES3 total $590,105. Appellant contends that ES3 resold the property to Toyota Motor Company (Toyota), a vehicle manufacturer. In support, appellant submitted a September 12, 2010 XYZ letter, signed by ES3's Treasurer, stating that ES3 is a service-based communications company and was hired to train Toyota and Scion dealers on new product offerings from Toyota, and the property at issue was a deliverable element of the training project. ES3's Treasurer further states "from what I understand [Toyota] 'self-assesses'" its tax liability to the state. Additionally, ES3 provided a multijurisdictional sales and use tax certificate from Toyota Motor Sales, USA (TMS), with the "issued to" field left blank. The certificate states that TMS held a California seller's permit and was engaged in the business of selling Toyota and Lexus vehicles, parts, and accessories. CDTFA contends that it disallowed the sales to ES3 because ES3 did not hold a seller's permit and did not provide any documentation to show it resold the property to Toyota.

There is no dispute that appellant sold tangible personal property to ES3, not to Toyota. In its letter dated September 12, 2010, ES3 states that it was engaged by Toyota "to do a national training program for the new Scion Xa and Xd." The facts indicate that Toyota hired ES3 to

perform training services.[12] Persons engaged in the business of rendering service are consumers, not retailers, of the tangible personal property which they use incidentally in rendering the service. Tax, accordingly, applies to the sale of property to service providers. (Cal. Code Regs., tit. 18, § 1501.) Thus, since the burden is on appellant, absent evidence to the contrary we must conclude that ES3 used the tangible personal property purchased from appellant incidentally in providing training services for Toyota.

Here, the XYZ letter is insufficient to establish a nontaxable resale in fact. The XYZ letter provided by ES3 does not state that ES3 resold the property described in the four sales invoices to Toyota. ES3 claims that it relied on TMS's (a different entity from Toyota)[13] exemption certificate and, as such, ES3 did not charge sales tax when it sold property to Toyota. However, the exemption certificate in question is not specific, and merely states that as a retailer of Toyota and Lexus vehicles, parts, and accessories, TMS's purchase of property specified on any purchase orders provided at the time of purchase is for resale. No such TMS or Toyota purchase orders for the property at issue were provided in connection with this appeal.

In addition, appellant provided no contemporaneous evidence to establish that ES3 resold tangible personal property purchased from appellant to Toyota (or TMS). Pertinent records might have included billing invoices from ES3 to Toyota for the sale of the property at issue, or purchase orders issued by Toyota to ES3 for the tangible personal property at issue. Furthermore, Toyota is not in the business of selling display structures, graphics, or other training materials to its dealers or other personnel. As such, we find that, in the absence of any contemporaneous evidence to support that appellant's sales to ES3 qualify as nontaxable sales for resale in fact, any claimed resale deductions would be disallowed for lack of support. In summary, we find that appellant failed to establish that ES3 resold the tangible personal property it purchased from appellant to either Toyota or TMS.

We conclude that no additional adjustments are warranted to the amount of disallowed claimed nontaxable sales of more than $25,000 to customers other than Sprint and related companies.

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[12] Appellant and ES3 state that ES3 is a service-based business. It is undisputed that ES3 does not hold a California seller's permit.

[13] The XYZ letter states that ES3's customer is Toyota; however, the resale certificate identifies the seller's permit number for TMS.

B. Disallowed claimed nontaxable sales of $25,000 or more to Sprint and related companies (Audit Item 2)

CDTFA disallowed $3,489,887 in claimed nontaxable sales to Sprint and related companies. This amount consists of $1,549,781 in disallowed sales to Nextel; plus $1,776,205 in disallowed sales to Sprint Nextel (Sprint); and $163,901 in disallowed sales to Nextel Systems Corporation (NSC). On appeal, CDTFA made an allowance of $1,745,599 for tax paid by Nextel during a separate audit of Nextel. As a result, the remaining amount at issue consists of $1,744,288 in disallowed transactions for Sprint and related companies (i.e., $3,489,887 - $1,745,599 = $1,744,288).

Sales to Nextel

First, appellant disputes the disallowed sales to Nextel of California, Inc. (Nextel) on the basis that Nextel paid the tax to the state. In a separate matter, CDTFA audited Nextel for the period January 1, 2007, through June 30, 2008, and determined a use tax liability of $1,745,599 for purchases from appellant, which Nextel paid to the state. Although CDTFA made an allowance of $1,745,599, to account for use tax assessed on and paid by Nextel pursuant to an audit of Nextel, the total amount of disallowed sales to Nextel in the audit of appellant was only $1,549,781.[14] This is because CDTFA had, in one of the re-audits of appellant, accepted some previously disallowed sales to Nextel based on additional documentation submitted by appellant.[15] In any event, the end result is that the total allowance for disallowed sales to Nextel exceeds the total amount of disallowed sales to Nextel by $195,818. In other words, CDTFA made an allowance of $195,818 to which appellant is not legally entitled. Therefore, we have no basis to conclude that any additional adjustments are warranted because the amount already allowed exceeds the amount disallowed, resulting in a net credit to appellant for these transactions.

[14] This amount consists of the following 11 transactions: $918,750 (invoice #2270); $200,246 (invoice #2255), $91,491 (invoice #2828), $59,900 (invoice #2964), $55,540 (invoice 2810), $51,822 (invoice #2596), $44,550 (invoice #2269), $38,500 (invoice #2415), $35,250 (invoice #2597), $27,884 (invoice #2909), and $25,848 (invoice #2615).

[15] Appellant had provided copies of use tax accrual work sheets obtained from Nextel for the months of August 2005, October 2005, November 2005, and December 2005.

Sales to Sprint

Second, the disallowed sales to Sprint consist of 14 transactions totaling $1,776,205, which CDTFA examined on an actual basis. CDTFA disallowed these transactions because appellant did not timely obtain a resale certificate from Sprint, and was unable to provide documentation, such as an XYZ letter, to support that Sprint resold the property. The law provides that the burden of proving a sale of tangible personal property is not at retail is upon the retailer unless the retailer timely obtains a resale certificate from the purchaser. (R&TC, § 6091.) As such, appellant's sales to Sprint are presumed taxable. In absence of any documentation to the contrary, we have no legal basis to make an adjustment.

Sales to NSC

Finally, the remaining transactions consist of four transactions with NSC totaling $163,901, which appellant claimed as nontaxable. All four transactions represent charges for construction contracts for store buildouts performed by appellant on a time-and-material or lump-sum basis. A construction contractor is regarded as a consumer of materials, and retailer of fixtures, that they furnish and install in the performance of a construction contract. (Cal. Code Regs., tit. 18, § 1521(b)(2)(A)1., (B)1.) Unless the construction contractor includes a separately stated charge for fixtures, the measure of tax is their cost price for the fixtures. (Cal. Code Regs., tit. 18, § 1521(b)(2)(B)2.a.) A contractor cannot avoid liability for sales tax or use tax on materials or fixtures furnished and installed by him or her by taking a resale certificate from the customer. (Cal. Code Regs., tit. 18, § 1521(b)(6)(A).) For the lump-sum contracts, CDTFA estimated the costs of the materials and fixtures to be 33 percent of the contract price. We find that it was appropriate for CDTFA to disallow claimed nontaxable sales of materials and fixtures furnished and installed in the performance of construction contracts because, as the construction contractor, appellant was regarded as the consumer of the materials, and the retailer of the fixtures. For the lump-sum contracts, appellant owed tax on its cost because appellant did not separately charge for the fixtures. Appellant has provided no documentation or other evidence to show that its costs of materials and fixtures were less than 33 percent of its contract price. Thus, we conclude that appellant failed to establish that an adjustment is warranted for the disallowed construction contracts.

C. Disallowed claimed nontaxable sales under $25,000 (Audit Item 3)

Appellant only disputes three sales to Bellus, LLC (Bellus). The three transactions are disallowed sales in the amount of $12,089, $3,741, and $1,100, during the test period (3Q07). CDTFA's audit working papers indicate that these transactions were disallowed because, although the purchaser signed an XYZ letter, the purchaser did not have a valid seller's permit. The XYZ letter is undated and states that the property at issue is "office equipment," "office equipment," and "outlets, logo sign & curtain rod," respectively. The XYZ letter also states that Bellus is engaged in the business of selling cosmetics. At the oral hearing, appellant contended that the purchaser fully intended to resell the property subject to the XYZ letter.

Here, appellant had the burden of proof because it failed to timely obtain a resale certificate. (R&TC, § 6091.) Unlike a timely resale certificate, an XYZ letter is insufficient to shift the burden of proof and, as such, CDTFA is not required to relieve a seller from liability for tax based on an XYZ letter. (R&TC, § 1668(f)(3).) In determining the weight to give the Bellus XYZ letter, we consider that it was signed by *appellant's* Chief Executive Officer, and there is no supporting documentation, such as a purchaser order, to establish that Bellus ultimately resold the property. To the contrary, Bellus is engaged in the business of selling cosmetics, and the nature of the property purchased was office equipment and related supplies, which we would expect to be consumed by a retailer of cosmetics (Bellus). Based on the above, we find that appellant failed to establish that it made nontaxable sales of office equipment and related supplies to Bellus for purposes of resale in the regular course of its business: selling cosmetics.[16]

D. Disallowed tax-paid purchases resold deduction (Audit Item 7)

A retailer who resells tangible personal property before making any use thereof (other than retention, demonstration or display while holding it for sale in the regular course of business) may take a deduction of the purchase price of the property if, with respect to its purchase, the retailer has reimbursed his vendor for the sales tax or has paid the use tax. (Cal. Code Regs., tit. 18, § 1701(a).)

[16] Appellant contends that Bellus' failure to obtain a seller's permit should not preclude the transactions from qualifying as nontaxable sales for resale. In reaching our conclusion that appellant failed to meet its burden, we give no weight to whether Bellus held a California seller's permit. Our conclusion would be the same if Bellus held a seller's permit because there is no supporting documentation to establish that the property was resold, and Bellus is not engaged in the business of selling office equipment.

Appellant claimed a deduction of $1,590,519 for tax paid purchases resold during the audit period. CDTFA disallowed $1,505,586 of this amount. For purposes of reporting, appellant had deducted all credit card purchases charged to cost of goods sold on its sales and use tax returns. Upon audit, appellant provided a small number of purchase invoices to support its contention that the credit card charges were tax paid. Upon review, CDTFA determined that most of the purchases pertained to services or out of state events. Furthermore, appellant had issued a resale certificate to local vendors and purchased the property without payment of tax. Appellant made several large one-time purchases from chain-retailers, including Home Depot, which CDTFA allowed. Appellant claims it should be allowed a deduction closer to 60 percent, instead of the 5.34 percent allowed. Nevertheless, the burden is on appellant and appellant failed to provide documentation, such as receipts or purchase invoices, to document that it paid tax on a greater amount than allowed during audit. Therefore, we conclude that no reduction to the amount of disallowed deductions for tax-paid purchases resold is warranted.

Issue 2: Whether appellant is entitled to relief of interest due to unreasonable delays.

The imposition of interest is mandatory. (R&TC, § 6482.) It accrues at the modified adjusted rate per month, or fraction thereof, from the last day of the month following the quarterly period for which the amount or any portion thereof should have been returned until the date of payment. (*Ibid*.) There is no statutory right to interest relief. The law allows the board,[17] in its discretion, to grant relief of all or any part of the interest imposed on a person under the Sales and Use Tax Law where the failure to pay the tax is due in whole or in part to an unreasonable error or delay by an employee of the board acting in his or her official capacity. (R&TC, §§ 20, 6593.5(a)(1).) Thus, in reviewing a denial of a request for interest relief, we generally examine the record to determine whether there was an abuse of discretion by CDTFA. (*Micelle Laboratories, Inc.*, 2020-OTA-290P.) An unreasonable error or delay shall be deemed to have occurred only if no significant aspect of the error or delay is attributable to an act of, or failure to act by, the taxpayer. (R&TC, § 6593.5(b).) Any person requesting interest relief must

[17] R&TC section 6593.5 states "board"; however, on and after July 1, 2017, the term "board" generally means CDTFA. As an exception, on and after January 1, 2018, the term "board," with respect to an appeal, means OTA. (R&TC, § 20(a), (b).)

include a statement under penalty of perjury setting forth the facts on which the request is based.[18] (R&TC, § 6593.5(c).)

Appellant contends that it is entitled to relief of all accrued interest pursuant to R&TC section 6593.5 based on its assertion that there were unreasonable delays in the audit and appeals process. Appellant argues that it has repeatedly asserted the same contentions throughout the process, and complains that CDTFA continued to re-audit, make small adjustments, and hold multiple district hearings, which only resulted in small adjustments throughout the process. According to appellant, CDTFA only made significant adjustments after the fourth reaudit. Therefore, appellant asserts that CDTFA's conduct constitutes unreasonable delay.

Delay while the appeal was with OTA

As a preliminary matter, appellant requests interest relief for the period in which the appeal was with OTA. In support, appellant submitted a statement, signed under penalty of perjury, stating that:

> Over about a ten-year period, [CDTFA] repeatedly audited and re-audited Appellant and held multiple district hearings, all resulting in minor adjustments throughout. Only after the fourth re-audit did [CDTFA] make significant adjustments.

Here, appellant contends that CDTFA's actions maintaining this appeal for a decade constituted an unreasonable delay. Appellant contends that it should be granted interest relief because CDTFA continued to maintain this appeal with OTA, despite the liability being overstated, as evidenced by the fourth reaudit adjustment while the appeal was pending before OTA. Here, appellant is confusing an allegedly unsubstantiated position on appeal with an unreasonable delay by CDTFA.

R&TC section 6593.5 authorizes interest relief for certain unreasonable errors or delays that prevented the taxpayer from timely paying the tax. Such a delay means, for example, an unreasonable failure to work on an appeal. On the other hand, interest relief does not extend to an allegedly "unreasonable" position taken on appeal, that is otherwise being actively maintained. Actively working on an appeal is, by definition, not a "delay" for purposes of

[18] California Code of Regulations, title 18, section 1703 restates, without adding further clarification to, the requirements for interest relief within the meaning of R&TC section 6593.5. (See Cal. Code Regs., tit. 18, § 1703(b)(1)(E).)

R&TC section 6593.5. Instead, the remedy for such a scenario as alleged by appellant is expressly contemplated by R&TC section 7091, which authorizes reimbursement of certain fees and expenses if the actions taken by CDTFA on appeal were unreasonable. (R&TC, § 7091.) Such a claim may be filed within one year after the date the decision on the appeal becomes final. (R&TC, § 7091(a)(1); Cal. Code Regs., tit. 18, § 30705.) The instant appeal is not yet final and such a reimbursement claim is not before OTA in this appeal. Furthermore, appellant does not contend that there was a delay by OTA.[19] In summary, we find that interest relief is inapplicable on this basis.

Delay by CDTFA

Appellant similarly requests interest relief for the period the appeal was being handled by CDTFA, on the basis that CDTFA acted unreasonably in maintaining this appeal through the audit and several re-audits and numerous district hearings. For the same reasons discussed above, interest relief is inapplicable on this basis. Appellant has not otherwise identified a specific error or delay, and our review does not identify one. At the beginning of the audit process, CDTFA conducted a thorough examination of appellant's available records. CDTFA completed an audit report and a revised audit report allowing appellant time to obtain XYZ letter responses from its customers as support for its claimed nontaxable sales, prior to issuing the NOD on April 1, 2011. On appeal, CDTFA performed a reaudit based on additional documents provided by appellant. The reaudit resulted in a reduction of $264,458 to the taxable measure. Following an appeals conference held on October 15, 2013, CDTFA issued a D&R on May 12, 2014, and a Supplemental D&R on November 10, 2014, which resulted in a reduction of $24,986 to the taxable measure in a second reaudit. By letter dated June 21, 2017, appellant filed an untimely request for reconsideration and submitted additional documentation. Based on CDTFA's examination of the additional documentation in a third reaudit, CDTFA reduced the taxable measure by $1,363,595. Appellant provided additional documentation with its opening brief filed with OTA on March 8, 2019. Upon review of the additional documentation, CDTFA performed a fourth reaudit, which resulted in a reduction of $3,312,404 to the taxable measure.

More than twelve years have passed since the audit period ended on June 30, 2008. However, the mere passage of time does not establish error or delay. (See *Cosgriff v.*

[19] We need not, and do not, address the issue of whether R&TC section 6593.5 authorizes OTA to grant relief of interest for a delay by OTA.

Commissioner, T.C. Memo. 2000–241, citing *Lee v. Commissioner* (1999) 113 T.C. 145, 150.) While the audit and appeals process in this case has spanned a significant period of time, we are unable to identify any unreasonable delay attributed to CDTFA's failure to act. While appellant may have repeatedly asserted the same contentions throughout the process, as it claims it did, its unsupported assertions were not sufficient to satisfy its burden of proof. Each time that appellant provided additional documentation after the issuance of the NOD, it appears that CDTFA promptly examined the new documentation and made the warranted adjustments. Therefore, we find that the length of the audit and appeals process in this case can largely be attributed to appellant's failure to timely provide sufficient documentation to support its claimed nontaxable sales.

In post-hearing briefing, appellant further contends that delays which CDTFA attributed to appellant during the oral hearing are not as lengthy as CDTFA has asserted. For example, CDTFA attributed a delay from November 21, 2008, through June 30, 2009,[20] to appellant's representative. Appellant contends that the amount of delay attributable to appellant is limited to the following periods: March 10, 2009, through April 15, 2009, and one week in June 2009. Based on our review of CDTFA's Assignment Activity History,[21] there is a delay attributable to appellant from October 2, 2008, until June 30, 2009. During this period, CDTFA was waiting on documentation from appellant to complete the audit.[22] Appellant further identifies other such periods during which a delay that CDTFA attributed to appellant was allegedly shorter than as stated by CDTFA.

[20] Appellant's brief states "November 21, 2008, through June 30, 2008 [SIC]." Based on a review of the file, this is a typographical error and all references are to the period November 21, 2008, through June 30, 2009.

[21] The Form 414-Z, Assignment Activity History, is a history of taxpayer contacts, staff actions, taxpayer or representative responses, and significant events that occur during the course of an audit assignment. (CDTFA Audit Manual, section 0201.14. (See: https://www.cdtfa.ca.gov/taxes-and-fees/manuals/am-02.pdf.)

[22] CDTFA provided appellant a list of claimed exempt sales that CDTFA was questioning on October 2, 2008 and requested documentation to support the questioned transactions. Appellant signed a waiver of the statute of limitations on October 10, 2008, and CDTFA again requested the supporting documentation on October 28, 2008. On November 21, 2008, appellant stated it could not find all the documentation requested, and the representative stated he would check with appellant on how to proceed about scheduling an office visit. On March 9, 2009, CDTFA indicated it had not heard back from appellant, and requested a follow-up appointment. In response, appellant requested postponing until after April 15, 20009. There are a number of follow-up communications between the parties until June 30, 2009, when appellant provided a written description of what happened with each questioned transaction.

At this point, it is necessary to go back to the elements for interest relief. The first requirement for relief is that there must be an unreasonable error or delay by CDTFA. (R&TC, § 6593.5(a)(1).) The second requirement is that no significant aspect of the delay can be attributable to the taxpayer. (R&TC, § 6593.5(b).) In its post-hearing briefing, appellant did not allege or establish periods of unreasonable error or delay by CDTFA, aside from its general allegation that CDTFA delayed completion of the audit for years. Time alone is insufficient to establish an unreasonable error or delay by CDTFA. Here, the record indicates that CDTFA was working on the appeal during this period, and the record includes plausible explanations for why the appeal took a long time, such as the need for four reaudits. As such, we need not examine to what extent appellant was responsible for causing delays during the handling of the audit (i.e., the second element) because we do not find an unreasonable error or delay by CDTFA. In summary, we find that appellant failed to establish a basis for interest relief.

HOLDINGS

1. Appellant has not established that any additional adjustments are warranted to the tax liability as determined by CDTFA.
2. Appellant has not established that it is entitled to relief of interest.

DISPOSITION

Sustain CDTFA's decision to deny the petition for redetermination, subject to CDTFA's adjustments and concessions on appeal which are set forth in CDTFA's fourth re-audit report.[23]

DocuSigned by:
715CE19AD48041B...
Andrew J. Kwee
Administrative Law Judge

We concur:

DocuSigned by:
Josh Aldrich
48745BB806914B4...
Josh Aldrich
Administrative Law Judge

DocuSigned by:
DC88A60D8C3E442...
Keith T. Long
Administrative Law Judge

Date Issued: 12/2/2020

[23] CDTFA's fourth re-audit findings are summarized in a CDTFA letter to appellant dated June 7, 2019.