

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:)
FS HEALTH SYSTEMS, LLC) OTA Case No. 21098581
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OPINION

Representing the Parties:

For Appellant: Ben Murphy, CEO

For Respondent: Alisa L. Pinarbasi, Attorney

For Office of Tax Appeals: Lisa Burke, Business Taxes Specialist III

M. GEARY, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, FS Health Systems, LLC (appellant) appeals an action by the Franchise Tax Board (respondent) proposing additional tax of \$800, a late filing penalty of \$432, a notice and demand (demand) penalty of \$200, a filing enforcement fee of \$97, and applicable interest, for the 2018 tax year.

Appellant waived its right to a hearing. Therefore, the Office of Tax Appeals (OTA) decides this matter on the basis of the written record.

ISSUE¹

Was appellant required to file a California Limited Liability Company (LLC) Return of Income return and pay the annual \$800 LLC tax for the 2018 tax year?

¹ Appellant’s sole argument in this appeal is that it had no nexus with California in 2018 and, therefore, it was not required to file a 2018 California income tax return, and it owes no tax, penalties, fee, or interest for that year. It makes no other argument and provides no evidence related to the imposition or amounts of the penalties, fee, and interest. Consequently, this Opinion will address the one issue raised by appellant, and OTA’s decision regarding that issue will determine whether respondent’s action should be sustained.

FACTUAL FINDINGS

1. Appellant is a Minnesota-based LLC that makes online sales of kinesiology tape and other related products through Amazon. During the year in question, appellant participated in Amazon's "Fulfillment by Amazon" (FBA) program, which, as relevant here, means that during 2018, appellant owned a stock of goods (i.e., inventory) at Amazon warehouses (fulfillment centers) in California and contracted with Amazon to ship its products from those fulfillment centers to customers in California.
2. By letter dated December 13, 2018, the California Department of Tax and Fee Administration (CDTFA) informed appellant that because appellant owned an inventory stored in fulfillment centers in California, it met the definition of a retailer engaged in business in California and was, therefore, required to register with CDTFA, file sales and use tax returns here, and pay tax on sales made to California consumers.
3. Appellant filed one or more sales and use tax returns reporting taxable sales of goods in California totaling \$161,930 (rounded) during 2018.
4. On October 20, 2020, respondent issued a Demand for Tax Return (Demand) to appellant. The Demand instructed appellant to reply on or before November 25, 2020, by filing its 2018 return, providing a copy of its 2018 return if it had already been filed, or explaining why it was not required to file a 2018 return.
5. On December 28, 2020, after appellant failed to timely respond to the Demand, respondent issued a Notice of Proposed Assessment (NPA), proposing the annual \$800 LLC tax, the various penalties and the fee identified above, plus applicable interest.
6. Appellant timely protested the NPA.
7. Respondent issued a Notice of Action affirming the NPA on June 14, 2021.
8. This timely appeal followed.
9. On March 15, 2023, OTA sent appellant an additional briefing request, which invited appellant to provide evidence relevant to, among other things, the value of tangible personal property it owned and kept in Amazon's California fulfillment centers during 2018. Appellant did not respond to the request.

DISCUSSION

Certain LLCs must pay the annual \$800 LLC tax for the privilege of “doing business” in California, as defined in R&TC section 23101. (R&TC, §§ 17941(a), 23153(d).) A taxpayer is “doing business” in California if it is “actively engaging in any transaction for the purpose of financial or pecuniary gain or profit.” (R&TC, § 23101(a).) Since 2011, R&TC section 23101(b) also provides that a taxpayer is “doing business” in California if any of the following conditions are met: (1) the taxpayer is organized or commercially domiciled in California; (2) the taxpayer’s sales in California (including sales by an agent or independent contractor of the taxpayer) exceed the lesser of \$500,000 or 25 percent of the taxpayer’s total sales ; (3) the real property and tangible personal property of the taxpayer in California exceed the lesser of \$50,000 or 25 percent of the taxpayer’s total real property and tangible property ; or (4) the amount paid in California by the taxpayer for compensation exceeds the lesser of \$50,000 or 25 percent of the total compensation paid by the taxpayer.² (R&TC, § 23101(b)(2)–(4).) OTA has determined that R&TC section 23101(a) and (b) contain alternative tests for doing business, and that the satisfaction of either test leads to a finding that the taxpayer is doing business in California. (*Appeal of Aroya Investment I, LLC*, 2020-OTA-255P.)

Respondent relies entirely on R&TC section 23101(a) to support its proposed assessment in this matter. It contends that appellant’s participation in Amazon’s FBA program during 2018, including appellant’s maintenance of a stock of goods at Amazon fulfillment centers in California, establishes sufficient physical presence in the state to allow the proposed assessment of the annual \$800 LLC tax, regardless of the factors referred to in R&TC section 23101(b). Citing *Appeal of GEF Operating, Inc.*, 2020-OTA-057P, respondent asserts that its determination in this regard is presumed to be correct and the taxpayer has the burden of proving error.

Appellant argues that it is not subject to California tax for the 2018 tax year because: it is a Minnesota-based LLC that had no physical presence in California during that year; its California sales of \$160,900.43 in 2018 represented only 7.4 percent of its total revenue for that year; all of its sales in California occurred through Amazon’s marketplace; and that its sales to

² The dollar amounts are adjusted for inflation. (R&TC, § 23101(c).) For example, for the tax year at issue, the dollar amounts used for R&TC section 23101(b)(2), (3), and (4) were \$583,867, \$58,387, and \$58,387, respectively.

California customers were only subject to sales tax “due to Amazon’s [fulfillment centers] creating nexus” However, appellant has submitted no evidence to support its arguments.

OTA interprets appellant’s argument that its California sales in 2018 constituted only 7.4 percent of its total revenue for that year to be in opposition to any claim by respondent that its authority to assess the tax is based on the sales threshold set forth in R&TC section 23101(b)(2). However, respondent does not rely on any of the factors set forth in R&TC section 23101(b)(2)-(4). Rather, it argues that its proposed assessment is authorized by R&TC section 23101(a). Thus, even if appellant’s sales were below the threshold established by R&TC section 23101(b)(2), which its unsubstantiated statement does not prove, such evidence would not prove that respondent’s reliance on R&TC section 23101(a) is misplaced. (See *Appeal of Aroya Investment I, LLC, supra.*)

The evidence shows that during 2018, appellant owned inventory at one or more of Amazon’s California fulfillment centers and that appellant made over \$160,000 in sales to California customers that year. Based on these facts, respondent’s determination that appellant was doing business in California during 2018 is reasonable. Therefore, it is presumed to be correct; appellant thus has the burden of proving error. (*Appeal of GEF Operating, Inc., supra.*) Unsupported assertions are not sufficient to satisfy a taxpayer’s burden of proof. (*Ibid.*) Appellant has had ample opportunity to show that the presence of its inventory in California during 2018 was insufficient to support a finding that it was doing business in California during 2018 under R&TC section 23101(a). Indeed, not only did appellant not argue that point directly – it appears to solely argue the sales threshold was not exceeded under R&TC section 23101(b)(2) – it failed to accept OTA’s invitation to provide evidence relevant to the inventory issue. Accordingly, OTA finds that appellant has failed to overcome the presumption in favor of respondent’s proposed assessment, and that appellant actively engaged in transactions in California for the purpose of financial or pecuniary gain or profit, thus satisfying the “doing business” standard under R&TC section 23101(a).

HOLDING

Appellant was doing business in California during 2018, and therefore was subject to the annual \$800 LLC tax.

DISPOSITION

Respondent’s action is sustained in full.

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Michael Geary
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Michael F. Geary
Administrative Law Judge

We concur:

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Huy "Mike" Le
Administrative Law Judge

DocuSigned by:
Kenneth Gast
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Kenneth Gast
Administrative Law Judge

Date Issued: 3/18/2024