STATE OF CALIFORNIA
BOARD OF EQUALIZATION
BUSINESS TAXES APPEALS REVIEW SECTION

In the Matter of the Claim	)	
for Refund Under the Sales	)	
and Use Tax Law of:	)	
	)	DECISION AND RECOMMENDATION
	)	No. S- --- XX-XXX
Claimant	)	

The Appeals conference in the above-referenced matter was held by Elizabeth Abreu, Staff Counsel on February 4, 1994 in Sacramento, California.

Appearing for Claimant: Name---
                                      Tax Attorney

Appearing for the
Sales and Use Tax Department: E. Wayne Hopkins
                                      Supervising Tax Auditor

                                      Michael P. Kitchen
                                      Staff Tax Auditor

<u>Subject of Claim</u>

Claimant seeks a refund of credit interest on the overpayment of tax of $1,117,769.74 and a refund of tax in the amount of $23,277.90 for the period of January I, 1988 through December 31, 1989.

<u>Claimant's Contention</u>

Claimant is entitled to credit interest because its overpayment of tax was caused by a corporate reorganization, not by carelessness.

<u>Summary</u>

Claimant is a major --- company which makes sales of petroleum products, including sales of jet fuel at California airports and sales of marine bunker fuels at ports in San Diego and Los Angeles. Claimant is part of a group of related corporations which underwent a reorganization in 19XX. In June 19XX, a merger occurred between [company 1] and [company 2], claimant's parent corporation. The surviving corporation, which was claimant's new parent corporation, was

named [company 3]. [Company 4], which made the sales in issue in this case, was a division of claimant.

Prior to the merger in 19XX, claimant's parent corporation had a tax department located in [out of state] which prepared and filed claimant's California sales and use tax returns. For a short time after the merger, claimant's [out-of-state 2] office prepared and filed the returns. In 19XY, the responsibility for preparing and filing the returns was transferred to [out-of-state 3], the former home office of [company 1]. The sales and marketing department in the [out-of-state 2] office provided the [out-of-state 3] office with a summary worksheet containing the information needed to prepare the returns. During the audit period, the [out-of-state 2] office maintained all bills of lading, exemption certificates, resale certificates, and other documentation for transactions exempt or excluded from sales tax.

Claimant contends that the [out-of-state 3] office misunderstood the information contained in the summary worksheet and therefore did not claim exemptions and exclusions to which claimant was entitled. During an internal audit which began in 19XY, the reporting errors were discovered. It appears that claimant had not collected tax reimbursement or use tax on the nontaxable sales.

After the internal audit, a report dated August 3, 1990 was prepared which noted that [company 4] had recently begun a new system to calculate, invoice, and accrue sales and excise taxes. The old system operated on the basis that all transactions were tax exempt unless the customers' records indicated that they were taxable. The new system treated all transactions as taxable unless the customer was flagged exempt.

Claimant filed a claim for refund which the Board received on April 2, 1991. The claim requested a refund in the amount of $1,543,849.74 for the period January 1, 1988 through December 31, 1989. Claimant asserted in the claim that it had paid tax on sales for resale, exempt sales to air common carriers under Revenue and Taxation Code sections 6357.5 and 6385, and exempt sales of bonded fuel under Revenue and Taxation Code section 6352.

Because of the large amount of the claim, the Board performed an audit. Item A of the audit is the difference between taxable sales reported by claimant on its returns for the audit period and taxable sales calculated from the information on claimant's worksheets. In other words, Item A accepts at face value the deductions shown on claimant's worksheets. The Board, however, audited the deductions shown on claimant's worksheets and disallowed a small percentage of those deductions in Items C through E. After netting all of the items in the audit, the auditor determined that claimant was entitled to a refund of tax in the amount of $1,221,841.36, which consisted of $1,117,769.74 in tax overpaymanets, $21.69 in section 6406 credits, and $127,301.00 in excess payments, less interest in the amount of $23,277.90. At the Appeals conference, the Sales and Use Tax Department stated that debit interest should not have been accrued because there were net overpayments in each of the quarterly periods. Thus, the Department recommended that the claimant be refunded $23,277.90 that was previously deducted from the original refund amount.

Analysis and Conclusion

The provisions of Revenue and Taxation Code section 6908(a) authorize the denial of credit interest on overpayments of tax as follows:

"**Disallowance of interest; waiver**. If the Board determines that any overpayment has been made intentionally or by reason of carelessness, it shall not allow any interest thereon."

There is no evidence that claimant intentionally overpaid its taxes. Therefore, the decisive issue is whether claimant's overpayment was the result of carelessness. The term "carelessness" is not defined in the sales and use tax law. It must therefore be consider in light of the commonly understood meaning of the term. Webster's Third New International Dictionary defines carelessness to mean "not taking ordinary or proper care."

In the present case, claimant is a large company with accounting and tax personnel to maintain records and prepare and file returns. The exemptions and exclusions in issue require extensive documentation, all of which claimant's [out-of-state 2] office maintained. After taking into account audit adjustments, the amount of sales which were nontaxable was large, totaling approximately $16,000,000. The average unclaimed deductions for the audit period was approximately 31.9 percent of total amounts reported.

On the other hand, claimant's errors were due in part to the reorganization and a misunderstanding by its [out-of-state 3] office, and claimant would not receive a windfall from the interest since it had not collect tax reimbursement or use tax.[1]

In recognition of problems caused by the corporate reorganization, it is recommended that credit interest be allowed for the overpayments made for the first two quarters of 1988. Claimant, however, had a duty to inquire and to prepare its returns correctly. Six months should have been ample time for claimant to discover and correct its reporting errors. Instead, the reporting errors occurred over two years. Therefore, credit interest is not recommended for the remaining six quarters of the audit.

In addition, it is recommended that claimant be refunded an additional $23,277.90 for interest improperly computed and applied against claimant's refund of taxes.

Claimant notes that it did not receive the refund for more than two years after it filed its claim for refund because of the length of time of the audit. Claimant contends that it should be entitled to interest accruing during all or part of that period. There were no allegations that the auditor unduly delayed the audit or that claimant was not cooperative.

Claimant's point is well-taken. The statute, however, states that the Board "shall not allow any interest thereon." Therefore, no interest which accrued during the period between the time the claim for refund was filed and the refund was paid may be allowed on the overpayments for the last six quarters of the audit period.

---

[1]A taxpayer can earn interest on someone else's money if the taxpayer collects tax reimbursement from its customers on nontaxable transactions, pays the reimbursement to the state, files a claim for refund, returns the reimbursement to the customers, and keeps the interest on the overpayment.

<u>Recommendation</u>

It is recommended that credit interest be allowed for the tax overpayments made during the period January 1, 1988 through June 30, 1988. No credit or debit interest should be calculated for the periods July 1, 1988 through December 31, 1989. It is also recommended that claimant be refunded an additional $23,277.90 for interest improperly computed and deducted from claimant's refund of taxes.

_____   _____

Elizabeth Abreu, Staff Counsel   Date