STATE OF CALIFORNIA

460.0025

BOARD OF EQUALIZATION

LEGAL DIVISION, APPEALS SECTION

In the Matter of the Petition for Redetermination Under the Sales and Use Tax Law of:	)	SUPPLEMENTAL DECISION AND RECOMMENDATION
[E]	)	No. S- -- XX XXXXXX-010
Petitioner	)	

Our original Decision and Recommendation dated June 21, 1996, is incorporated herein by this reference. The Sales and Use Tax Department (the "Department") filed a timely Request for Reconsideration by memo dated August 13, 1996. Petitioner filed a timely Request for Reconsideration on September 20, 1996.

Introduction

Petitioner billed its customers for tax reimbursement measured by the total charge for the property it sold. It claimed inflated deductions on its sales and use tax returns, so the amount of tax paid to the Board was significantly less than the amount of tax reimbursement collected from customers. Petitioner intentionally and knowingly retained the excess as additional profit on its sales. We originally concluded that the understatements were due to fraud.

Petitioner's Request for Reconsideration

Petitioner's Contentions

1. The understatements were not due to fraud and the fraud penalty should be eliminated.

2. Periods prior to January 1, 1991, are barred by the statute of limitations.

Summary, Analysis and Conclusions

1. Petitioner claims that it charged tax reimbursement on design charges which it believed in good faith were not subject to tax. It collected and retained the tax reimbursement only as a way to obtain extra payment for services without causing customer complaints. Therefore, petitioner concludes, its failure to pay tax on these charges was not due to an intent to evade tax. In sum, petitioner contends that it intended to defraud its customers, not the state, and the fraud penalty thus cannot be sustained.

Petitioner relies on the following statement by the Court in Marchica v. State Board of Equalization, 107 Cal.App.2d 501 (1951), at 509: "The fraud meant by the statute is actual,

intentional wrongdoing, and the intent required is the specific purpose to evade a tax believed to be owed." As authority for this statement, the Court cited a federal income tax case, Guaranty Trust Co. v. United States, 44 F.Supp. 417 (1942).

In our original Decision and Recommendation, we concluded that similar language in federal income tax cases is not controlling. This is because the sales tax, unlike the income tax, can be passed on to customers as a separately stated charge. Despite the federal decisions, we found that a fraud penalty is proper in sales tax cases when a taxpayer knowingly and intentionally collects money from customers under a false representation that it is "sales tax" which will be paid to the state, then retains the money as its own profit.

We do not believe Marchica is to the contrary. There is nothing in the Court's opinion to indicate that the taxpayer had charged tax reimbursement to customers. The only question before the Court was whether a mere understatement of tax, without more, was sufficient to sustain a fraud penalty. The Court was not asked to decide, and in fact did not decide, whether the penalty is proper when a person knowingly collects and retains tax reimbursement.

In People v. Superior Court (Williams), 8 Cal.App.4th 688 (1992), the Court said:

> "However, '[i]t is axiomatic ... that a decision does not stand for a proposition not considered by the court.' (People v. Harris (1989) 47 Cal.3d 1047, 1071 [255 Cal.Rptr. 352, 767 P.2d 619], citing People v. Myers (1987) 43 Cal.3d 250, 265, fn. 5 [233 Cal.Rptr. 264, 729 P.2d 698]; Ginns v. Savage (1964) 61 Cal.2d 520, 524, fn. 2 [39 Cal.Rptr. 377, 393 P.2d 689].) '[I]t is only the ratio decidendi of a Supreme Court opinion that is fully binding as a precedent on the lower courts of this state. [Citations.]' (Bunch v. Coachella Valley Water Dist. (1989) 214 Cal.App.3d 203, 212 [262 Cal.Rptr. 513].) 'The ratio decidendi is the principle or rule which constitutes the ground of the decision, and it is this principle or rule which has the effect of a precedent. It is therefore necessary to read the language of an opinion in light of its facts and the issues raised, to determine ... which statements of law are necessary to the decision, and therefore binding precedents ....' (9 Witkin, Cal. Procedure (3d ed. 1985) Appeal, § 783, p. 753, quoted in Bunch v. Coachella Valley Water Dist., supra, 214 Cal.App.3d at p. 212; Santa Monica Hospital Medical Center v. Superior Court (1988) 203 Cal.App.3d 1026, 1033 [250 Cal.Rptr. 384].) '"It is the general rule that the language of an opinion must be construed with reference to the facts presented by the case, and the positive authority of a decision is coextensive only with such facts." [Citations.]' (Brown v. Kelly Broadcasting Co. (1989) 48 Cal.3d 711, 734-735 [257 Cal.Rptr. 708, 771 P.2d 406], quoted in Harris v. Capital Growth Investors XIV (1991) 52 Cal.3d 1142, 1157 [278 Cal.Rptr. 614, 805 P.2d 873].)"

The statement in Marchica upon which petitioner relies was dicta, unnecessary to the decision, and is therefore not binding as precedent. We remain of the opinion that petitioner is liable for the fraud penalty.

2. Revenue and Taxation Code Section 6487 imposes a three year statute of limitations for issuing deficiency determinations against persons who have filed returns, except in the case of fraud. For any period in which the understatements were due to fraud, the determination is not barred by the statute of limitations.

The Department's Request for Reconsideration

The Department's Contentions

1. Periods for which petitioner's returns are not available should remain in the audit liability.

2. The determination should be increased.

Summary, Analysis and Conclusions

1. We originally recommended that the fraud penalty be deleted for periods where the Board no longer has copies of petitioner's returns. We said: "[A]pparently the Board has no record of the gross receipts reported and deductions claimed. Without that information, it cannot be shown that petitioner claimed deductions for amounts on which it collected tax reimbursement from customers."

The Department has now located computer records showing the amounts of tax paid by petitioner for the relevant periods. These Board records, considered together with petitioner's own records, show that petitioner collected tax reimbursement from customers and claimed inflated deductions during the questioned periods. We therefore conclude that the fraud penalty was properly imposed for all periods covered by the Notice of Determination.

2. Because returns were not available, the original audit had estimated the underpayments for the questioned periods by using a percent-of-error calculated for later periods. Since records are now available to show the actual tax reported, the Department has prepared a schedule using that information to recalculate the tax measure. The recalculation results in a $10,301 increase in the understated measure. Petitioner does not object to the calculations. If the Department wishes to increase the determination, however, it must follow the procedures required by Revenue and Taxation Code Section 6563.

Recommendation

Redetermine without adjustment to the tax or penalty, unless the Department claims an increase in accordance with the requirements of Revenue and Taxation Code Section 6563.

James E. Mahler, Tax Counsel — October 1, 1996 Date