

IT 95-84

Tax Type: INCOME TAX

Issue: Penalty Under 1002(d) - Failure To File/Pay Withholding

STATE OF ILLINOIS  
DEPARTMENT OF REVENUE  
OFFICE OF ADMINISTRATIVE HEARINGS  
CHICAGO, ILLINOIS

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DEPARTMENT OF REVENUE )  
STATE OF ILLINOIS )  
 ) Docket:  
 v. ) SSN#  
 )  
TAXPAYER, )  
Responsible Officer, )  
CORPORATION A )  
 ) Wendy S. Paul  
 ) Admin. Law Judge  
Taxpayer(s) )  
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RECOMMENDATION FOR DISPOSITION

APPEARANCES: XXXXX for TAXPAYER; Shepard Smith, Special Assistant Attorney General, for the Illinois Department of Revenue.

SYNOPSIS: This case involves taxpayer's potential liability under 35 ILCS 5/1002(d) for failure to pay over to the State of Illinois withheld Illinois income taxes from compensation paid to the employees of the CORPORATION A during the 2nd calendar quarter of 1992 . On June 28, 1994, the Department issued a Notice of Deficiency to the taxpayer. The Notice proposed a tax deficiency for the 2nd quarter of 1992 in the amount of \$1,952 exclusive of statutory interest.

In response thereto, on August 19, 1994, the taxpayer filed a timely Protest. The issue to be resolved is whether, for the calendar quarter at issue, the taxpayer was a responsible officer of CORPORATION A required to collect, truthfully account for and pay over the tax imposed by Article 7 of the Illinois Income Tax Act and, if so, whether the taxpayer willfully failed to do so.

A hearing was held on May 16, 1995. Following the submission of all evidence and a review of the record, it is recommended that this matter be

resolved in favor of the taxpayer.

FINDINGS OF FACT:

1. On June 28, 1994, the Department issued a Notice of Deficiency to the taxpayer proposing a tax deficiency for the 2nd quarter of 1992 in the amount of \$1,952 for failure to pay over to the State of Illinois income taxes withheld from employees of CORPORATION A. (Dept. Ex. No. 1)

2. On August 19, 1994 the taxpayer filed a timely Protest. (Dept. Ex. No. 2)

3. The sum of \$1,952 was withheld from compensation paid to the employees of CORPORATION A for the 2nd quarter of 1992 but the withheld funds were not paid over to the Department of Revenue. (Dept. Ex. No. 5; Tr. p. 15)

4. CORPORATION A was an Illinois limited partnership which operated a restaurant and nightclub known as "XXXXX". The partnership has since been dissolved. (Dept. Ex. No. 8; Tr. p. 9)

5. The General Partners of the partnership were CORPORATION B, a corporation owned and controlled by TAXPAYER (taxpayer) and TAXPAYER A; CORPORATION C, a corporation owned and controlled by TAXPAYER B; and CORPORATION C, a corporation owned and controlled by TAXPAYER C. (Dept. Ex. No. 6, 8)

6. Under the Private Placement Memorandum, the General Partners had the exclusive authority to manage the operations and affairs of the Partnership and to make all decisions regarding the business of the Partnership. (Dept. Ex. No. 8)

7. The General Partners retained CORPORATION D, a corporation owned by TAXPAYER D, to manage the restaurant and nightclub operations. (Dept. Ex. No. 8; Tr. p. 21)

8. Initially, TAXPAYER D and TAXPAYER B were in charge of daily operations. Toward the end, and during the calendar quarter at issue, TAXPAYER C took over the daily operation of the business, which included hiring and firing, and the payment of bills, payroll and taxes. (Tr. p.

21)

9. When TAXPAYER C took over the daily operation, Taxpayer was one of three persons with signature authority on the partnership's payroll account, for which two signatures were required. Taxpayer was one of either two or three persons with signature authority on the partnership's operating account, for which two signatures were required. Taxpayer's signature authority was in effect during the calendar quarter at issue. (Dept. Ex. No. 7; Tr. p. 15, 22, 23)

10. Taxpayer did not personally sign checks; however, he had authorized a stamp with his signature to be made, which stamp was used as his signature on partnership checks. (Tr. p. 23)

11. Taxpayer did not participate in the daily operation of the business. (Dept. Ex. No. 8; Tr. p. 21)

12. The Illinois withholding tax return (IL-941) for the quarter at issue contains the purported signature of XXXXX by TAXPAYER. (Dept. Ex. No. 5)

CONCLUSIONS OF LAW : I find that taxpayer was a "responsible person" within the meaning of the statute (35 ILCS 5/1002(d)), but that the second statutory element, willfulness, was not sufficiently established for imposition of personal liability.

35 ILCS 5/1002(d) imposes a penalty on any person required to collect, truthfully account for, and pay over any tax imposed by the Illinois Income Tax Act who willfully fails to collect such tax or truthfully account for and pay over such tax or willfully attempts in any manner to evade or defeat the tax or payment thereof in an amount equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over.

35 ILCS 5/1002(d) is patterned after Section 6672 of the Internal Revenue Code and contains virtually identical language to both the federal statute and to Section 13.5 of the Retailers' Occupation Tax Act (35 ILCS 120/1 et seq., since repealed), so that cases interpreting both of these

statutes constitute authority here.

Section 1002(d) establishes a two-part test for imposing personal liability for failure to pay withholding taxes to the state. First, the individual must be a "responsible person." Second, there must have been a "willful failure" to have paid the taxes in question. *Wetzel v. United States*, DC Miss., 92-1 USTC, 50,217.

Courts have broadly construed the meaning of the term "responsible person." Responsibility for employment taxes is a matter of status, duty and authority, not merely a matter of knowledge concerning the existence of a corporate tax liability. *Mazo v. United States*, 591 F. 2d 1151 (5th Cir. 1979) "Authority" refers to effective authority. In other words, a court must determine whether taxpayer was a person who could have seen to it that the taxes were paid; i.e., a person with authority over which corporate obligations were paid who can fairly be considered responsible for the corporation's failure to pay its taxes. Here, taxpayer's corporation (CORPORATION B) was one of several general partners with complete and exclusive authority to manage all of the business operations, including financial decisions, of the partnership. Taxpayer was one of only two or three people with signature authority on both the payroll and the operating bank accounts of the partnership during the quarter in question. Even if taxpayer did not personally sign the Form IL-941, he was obviously authorized to do so or there would have been no reason for his signature, or purported signature, to have appeared thereon. Taxpayer testified, and it is so found, that he never actively participated in the daily operation of the business. The fact that taxpayer chose not to participate, however, does not mean that he was not in a position to do so, had he so chosen. Nor does the fact that someone else (TAXPAYER C) was actively managing the business during the quarter in question, and was, perhaps, more responsible than taxpayer for the collection and payment of taxes, in any way negate taxpayer's status as a responsible person. See, e.g. *Monday v. United States*, 421 F. 2d 1210, cert. denied, 400 U.S. 821 (7th Cir. 1970).

While it was established that taxpayer was a responsible person, there is insufficient evidence that his failure to collect or pay the taxes was willful. This element requires a showing of a voluntary, conscious, and intentional failure to make tax payments (Department of Revenue v. Joseph Bublick & Sons, Inc. 68 Ill. 2d 568 (1979)) or a reckless disregard of a known or obvious risk (Monday v. U.S., supra.; Kruse v. Sweet, 90 CH 12248 (Cook County Circuit Court, June 2, 1993)). The concept of notice, actual or constructive, is fundamental to a determination of liability through recklessness. Thus, willful conduct may be shown if the individual is aware that money held for the taxing entity is being used for other purposes. Kruse v. Sweet, supra., citing Hornsby v. IRS, 558 F. 2d 925 (5th Cir. 1979).

Here, the only evidence tending to show taxpayer's notice was his purported signature on the Form IL-941. (Dept. Ex. No. 5) Taxpayer, however, testified that the signature thereon was not his and that he had never signed a Form IL-941 for any of the quarters in which the business was operational. In support of such testimony, Taxpayer offered into evidence four samples of his actual signature. (Taxpayer Group Ex. No. 1) The administrative law judge, however, was not able to conclusively determine the authenticity of the signature on the IL-941 after comparing it to those contained on Taxpayer Group Exhibit No. 1 and to taxpayer's signature on the Power of Attorney (Dept. Ex. No. 4). Nevertheless, taxpayer's testimony that he never signed any IL-941 was neither contradicted nor impeached.

Further, although taxpayer had signature authority on the bank accounts, he never actually signed any of the checks. Nor did he ever sign any of the partnership tax returns. During the quarter in question, it was TAXPAYER C who was managing the operations. Taxpayer's testimony relating to his lack of involvement in the actual business operations and financial decisions, and relating to the use of his name as his principal

contribution to the partnership, was undisputed and was believable, in light of his fame as a well-known local sports figure and the fact that he lacked any type of business background. (Dept. Ex. No. 8)

In conclusion, taxpayer presented sufficient evidence on the issue of willfulness to overcome the Department's prima facie case. Accordingly, it is recommended that the Notice of Deficiency be withdrawn.

Administrative Law Judge