

ST 14-29

Tax Type: Sales Tax

Tax Issue: Responsible Corporate Officer – Failure To File Or Pay Tax

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

THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS

v.

JOHN DOE,
Taxpayer

No. XXXX
Account ID XXXX
NPL Penalty ID XXXX
Period 6/09

Ted Sherrod
Administrative Law Judge

RECOMMENDATION FOR DISPOSITION

Appearances: Special Assistant Attorney General George Foster on behalf of the Illinois Department of Revenue; Timothy Edmier and Terrance Benshoof of Lawrence Kamin Saunders & Uhlenhop on behalf of John Doe.

Synopsis:

This matter is before this administrative tribunal pursuant to John Doe's protest of Notice of Penalty Liability ("NPL") number XXXX, as responsible officer of ABC Business Inc. The NPL represents a penalty liability for Retailers' Occupation and related taxes for the tax period ending June 30, 2009. A hearing was held on this matter on September 26, 2014, with the taxpayer providing oral testimony. The Department also submitted documentary evidence at the hearing. Following the submission of all evidence and a review of the record, it is recommended that the NPL at issue in this case be finalized as issued. In support of this recommendation, the following "findings of fact" and "conclusions of law" are made.

Findings of Fact:

1. The Department issued a Notice of Penalty Liability (“NPL”) to John Doe (the “taxpayer”) on June 26, 2012. Department Exhibit (“Ex.”) 1.
2. The NPL, in the amount of \$XXXX, was issued to the taxpayer as a responsible officer of ABC Business Inc., an Illinois domiciled corporation engaged in the operation of a gasoline service station selling gasoline, gasohol, sundry items and lottery tickets, located in Anywhere, Illinois. *Id.*
3. During the tax period in controversy, the taxpayer was the secretary of ABC Business and the manager of the company, and was responsible for running its day to day operations. Transcript (“Tr.”) pp. 28, 39, 45. In his capacity as ABC Business manager, the taxpayer’s duties included hiring and firing employees and purchasing inventory supplies. Tr. pp. 13, 14. The taxpayer was an authorized signer on ABC Business’s bank account and prepared and signed checks to pay the company’s creditors and suppliers. Tr. pp. 19, 20, 38, 39.
4. The stock of ABC Business was owned by the taxpayer, his brother Jack Black and Gene Green, the company’s President. Tr. pp. 11, 44; Department Ex. 1. All of these stockholders were also officers of the company. Tr. p. 45.
5. The taxpayer was responsible for filing the company’s sales tax returns which the taxpayer signed. Tr. pp. 20, 21, 39. The taxpayer also issued and signed checks to pay the taxes that were owed. Tr. pp. 20, 21.
6. ABC Business recorded daily gasoline sales on its computer at its service station location. Tr. p. 16. Gasoline sales information entered into the computer was based on gasoline pump meter readings showing the amount of gasoline sales each day. Tr. pp. 15, 16.

When the taxpayer was not at the gasoline service station, these meter readings were taken by the company's employees. Tr. p. 16.

7. The taxpayer entered purchase and sales information into the computer at the end of each business day. Tr. p. 29. All of the company's purchase and sales records in its computer were given to the company's accountant by the taxpayer at the end of each month, along with invoices and receipts, and then deleted. Tr./ pp. 18, 29-34. The taxpayer did not retain copies of any of the company's accounting information given to its accountant and maintained no permanent record of the company's purchases and sales. Tr. pp. 18, 19, 24, 25, 37, 38.
8. ABC Business ceased business operations on June 30, 2009. Department Ex. 1. Subsequent to the cessation of its business operations, ABC Business was acquired by Gene Green, its President. Tr. p. 23.
9. On July 17, 2009, the Department issued a bulk sales stop order to Gene Green, the purchaser of ABC Business, requiring him to withhold \$XXXX to be held in escrow until all sales and withholding taxes were paid through the date of sale. Department Ex. 1.
10. The Department audited ABC Business's sales tax returns for the period 1/1/07 through 6/30/09. *Id.* At the conclusion of its audit, the Department issued a Final Notice of Tax Due for Form ST-1, Sales and Use Tax Return assessing tax due in the amount of \$XXXX for the period ended 6/30/09. *Id.* The record contains no evidence that this assessment was ever contested or protested.

Conclusions of Law:

The issue in this case is whether John Doe was a responsible person who willfully failed to file and pay retailers' occupation tax due from ABC Business, a gasoline station located in

Anywhere, Illinois, as required by section 3-7 of the Uniform Penalty and Interest Act, 35 ILCS 735/3-7 imposing liability upon “responsible” officers who “willfully” fail to file returns and pay taxes. The admission into evidence of Notice of Penalty Liability (“NPL”) number XXXX issued Jack Black on June 26, 2012 establishes the Department's *prima facie* case with regard to both the fact that Jack Black was a "responsible" officer and the fact that he "willfully" failed to file and/or pay taxes that were due. Branson v. Department of Revenue, 168 Ill. 2d 247, 261-62 (1995). When the Department establishes its *prima facie* case, the burden shifts to the taxpayer to overcome the Department's finding. Masini v. Department of Revenue, 60 Ill. App. 3d 11 (1st District 1978). To overcome the Department's *prima facie* case, the taxpayer must present consistent, probable evidence, closely identified with books and records. Copilevitz v. Department of Revenue, 41 Ill. 2d 154 (1968); Central Furniture Mart v. Johnson, 157 Ill. App. 3d 907 (1st District 1987); Vitale v. Department of Revenue, 118 Ill. App. 3d 210 (3d District 1983). Oral testimony without corroborating books and records is insufficient to overcome the Department's *prima facie* case. Mel-Park Drugs v. Department of Revenue, 218 Ill. App. 3d 203 (1st Dist. 1991).

The Department seeks to impose personal liability for failure to remit Retailers' Occupation and related taxes (“ROT”) to the Department for the period ending June 30, 2009. The personal liability penalty for the ROT violation determined by the Department is imposed by section 3-7 of the Uniform Penalty and Interest Act (“section 3-7”), which provides as follows:

(a) Any officer or employee of any taxpayer subject to the provisions of a tax Act administered by the Department who has the control, supervision or responsibility of filing returns and making payment of the amount of any trust tax imposed in accordance with that Act and who willfully fails to file the return or make the payment to the Department or willfully attempts in any other manner to evade or defeat the tax shall be personally liable for a penalty equal to the total amount of tax unpaid by the taxpayer including interest and penalties thereon.

35 ILCS 735/3-7.

An officer or employee of a corporation may therefore be personally liable for the corporation's taxes if: (1) the individual had the control, supervision or responsibility of filing the sales tax returns and paying the taxes; and (2) the individual willfully failed to perform these duties.

Under section 3-7, the Department's certified record relating to the penalty liability constitutes *prima facie* proof of the correctness of the penalty due. 35 ILCS 735/3-7(a); Branson, *supra* at 260. Once the Department presents its *prima facie* case, the burden shifts to the taxpayer to establish that one or more of the elements of the penalty are lacking, that is, that the person charged was not a responsible corporate officer, or that the person's actions were not willful. *Id.* at 261.

For guidance in determining whether a person is responsible under section 3-7, the Illinois Supreme Court has referred to cases interpreting section 6672 of the Internal Revenue Code, 26 U.S.C.A. section 6672.¹ Branson at 254-56; Department of Revenue v. Heartland Investments Incorporated, 106 Ill. 2d 19, 29-30 (1985). These Federal cases state that the critical factor in determining responsibility is whether the person had "significant" control over the corporation's finances. Purdy Co. of Illinois v. United States, 814 F. 2d 1183, 1188 (7th Circuit 1987). A key indicia of such control is participation in decisions regarding the payment of creditors and disbursement of funds. Monday v. United States, 421 F. 2d 1210 (7th Circuit 1970), cert. denied, 400 U.S. 821 (1970). Significant control does not mean exclusive or absolute control over the dispersal of funds. Thomas v. U.S., 41 F. 3d 1109, 1113 (7th Cir. 1994). All that is required is that the person could have impeded the misapplication of revenues to pay

¹ Section 6672 of the Internal Revenue Code imposes penalty liability on corporate officers who willfully fail to collect, account for, or pay over employee Social Security and federal income withholding taxes.

expenses other than delinquent tax liabilities by preventing the corporation from squandering the taxes that it should have paid to the taxing authority. *Id.*

In the present case, the taxpayer has failed to present sufficient documentary evidence to show that he did not have significant control over the corporation's finances. The record indicates that the taxpayer was one of only three officers of ABC Business. Tr. p. 45. This corporation's by-laws are not in evidence, and the record does not show what duties and responsibilities were vested in the company's officers. However, the officers of a corporation are usually charged with the financial management of the corporation and, in the absence of any documentary evidence to the contrary, there is no reason to assume that this was not the case with ABC Business.

In fact, the testimony presented in this case shows that Jack Black was in charge of important aspects of ABC Business's financial management. Specifically, Jack Black testified that his duties included control over the day-to-day operations of this company. Tr. p. 28. This function entailed preparing and signing checks to cover the company's expenses. Tr. pp. 19, 20, 38, 39. The record further indicates that Jack Black was also responsible for overseeing the preparation and filing of the company's tax returns which he executed in his capacity as an officer of the company. Tr. pp. 20, 21, 39..

Jack Black has failed to rebut indicia of significant control over ABC Business's financial affairs apparent from his status a company officer, his authority to sign checks and his execution of ABC Business's tax returns. Throughout his testimony, Jack Black attempted to underplay his authority over ABC Business's financial and tax affairs during the tax period in controversy by testifying that he delegated complete authority over these functions to Fred Red, the company's outside accountant. Tr. pp. 12, 17-22, 37, 38. However, his testimony as to his

lack of responsibility concerning the company's financial affairs and tax compliance is self-serving and therefore unpersuasive.

Moreover, even though the record shows that the taxpayer routinely forwarded all of the company's books and records to the company's accountant to prepare the company's tax returns, and exercised absolutely no oversight over the accountant's tax return preparation, such proof is not a dispositive defense to liability in this case. As pointed out in Howard v. United States, 82-2 USTC P 9567 (N.D. Texas 1982), affirmed 711 F. 2d 729 (5th Circuit 1983), in determining whether a taxpayer is a responsible officer, "the question is not whether" the taxpayer "exercised the power he possessed, but rather what power he possessed." Howard, *supra* at 2. Since ABC Business's accountant was an independent contractor retained by ABC Business to prepare the company's tax returns, Jack Black, as an officer of ABC Business, clearly had the authority to supervise and control the accountant's compliance functions. Accordingly, it is clear that Jack Black possessed the authority to control and direct the manner in which the company's tax returns were prepared and to refuse to sign the company's returns or sign checks paying the company's taxes until after reviewing the returns to make sure that they were accurate and complete.

In the instant case, the taxpayer presented no documentary evidence of any kind to support his claim that he was not a responsible officer. Indeed, the only evidence that he was not a responsible officer is the taxpayer's own testimony. However, in order to overcome the Department's *prima facie* case, it was incumbent upon the taxpayer to present more than his own testimony indicating that he was not a responsible person. Mel-Park Drugs, *supra* at 217. Since the taxpayer failed to provide corroborating documentary proof that he lacked the apparent significant control over the corporation's finances that his status as an officer, his check signing

authority and tax compliance authority indicates, the Department's determination that he was a responsible officer has not been rebutted by the evidence the taxpayer has submitted.

Pursuant to section 3-7, a second element, willful failure to pay taxes, must be shown in order to impose personal liability in this case. The Department presented a *prima facie* case for willfulness with the introduction of the NPL into evidence. Branson, *supra*. The burden then was on the presumptive responsible party to rebut the presumption of willfulness. *Id.*

As stated in Newsome v. United States, 431 F. 2d 742 (5th Cir. 1970), willfulness does not require a criminal or other bad motive on the part of the responsible person. All that must be shown is a voluntary, conscious and intentional failure to collect, truthfully account for, or pay over the taxes that are held in trust for the Government. *Id.* at 745. Accordingly, the subjective state of mind of the responsible officer is not determinative. Rather, as noted in Branson, *supra*, "willful failure to pay taxes has generally been defined as involving intentional, knowing and voluntary acts or, alternatively, reckless disregard for obvious or known risks." *Id.* at 255.

During the hearing in this case, the taxpayer testified that he did not keep any of the company's books and records for more than 30 days, and that after 30 days all of the company's books and records were destroyed. Tr. pp. 18, 19, 24, 25, 29-34, 37, 38. Accordingly, the taxpayer, by his own admission, failed to retain any of the company's records of purchases and sales recorded in the company's computer during each business day. The taxpayer testified that these records were deliberately destroyed at the end of each month. By virtue of this testimony, the taxpayer admitted during the hearing that he deliberately failed to comply with section 7 of the Retailers' Occupation Tax Act which provides, in relevant part, as follows:

Every person engaged in the business of selling tangible personal property at retail in this State shall keep records and books of sales of tangible personal property, together with invoices, bills of lading, sales records, copies of bills of sale, inventories prepared as of December 31 or each year or otherwise

annually as has been the custom of the specific trade and other pertinent papers and documents.
35 ILCS 120/7.

Moreover, the taxpayer testified that he turned over all of the company's records of purchases and sales to the taxpayer's accountant for use in preparing the company's sales tax returns before destroying his records of them, and retained no copies of these documents for his own use. As a consequence of the taxpayer's failure to meet his obligations under section 7 of the Retailers' Occupation Tax Act, 35 ILCS 120/7, and his failure to maintain any books and records detailing the company's sales information, it was impossible for him to ever check any of the numbers reported as sales on the company's tax returns for accuracy and completeness, even though the taxpayer was charged with the responsibility for doing so by virtue of his control over the company's tax preparation and filing. At best, this failure shows a reckless disregard for the obvious risk that these numbers might not be correct and that the company's taxes might not be accurately reported and paid. Indeed, there is absolutely nothing in the record to demonstrate that the taxpayer took any steps to make sure that the gross receipts numbers on the company's sales tax returns were accurate. The destruction of all of the company's books and records before the company's tax returns were executed and filed made this impossible. Tr. p. 22 ("Did you have any paperwork at the station that you would have been able to pull documents and compare to the report of total revenue or anything of that nature? A. No, I did not.").

By his own testimony, the taxpayer was responsible for properly reporting and paying over the company's sales taxes due. He failed in this responsibility. The record clearly shows the taxpayer's complete disregard for the obvious risk that the company's sales might be incorrectly reported on the company's sales tax returns due to the taxpayer's lack of oversight.

This “reckless disregard for obvious or known risks” clearly establishes willfulness under the law. Branson, *supra* at 255.

WHEREFORE, for the reasons stated above, it is my recommendation that the Department’s Notice of Penalty Liability number XXXX be affirmed in its entirety.

Ted Sherrod
Administrative Law Judge

Date: November 14, 2014