

ST 05-7

Tax Type: Sales 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. 04-ST-0000
IBN: 0000-0000
NOD # 0000
NPL # 0000
Tax pds.: 09/02-02/03**

**Charles E. McClellan
Administrative Law Judge**

RECOMMENDATION FOR DECISION

Appearances: George Foster, Special Assistant Attorney General, for the Illinois Department of Revenue (the “Department”); Stuart T. Edelstein for John Doe (“Taxpayer”)

Synopsis:

This matter involves a Notice of Deficiency issued to Taxpayer, as responsible party, on March 31, 2004 for a penalty under Section 1002(d) of the Illinois Income Tax Act in the amount of tax withheld from employees of ABC Group, Inc. (the “Corporation”) for the fourth quarter of 2002 and not paid over to the State of Illinois. It also involves a Notice of Penalty Liability issued to Taxpayer, as responsible party, on March 30, 2004 for a penalty under Section 735/3-7 of the Uniform Penalty and Interest Act, 35 ILCS 735/-7, for the failure of the Corporation to pay sales tax to the State of Illinois. An evidentiary hearing was held on February 9, 2005.

I recommend that the Notice of Deficiency and the Notice of Penalty Liability be canceled.

Findings of Fact:

1. The Corporation was incorporated in October of 2001. Tr. p. 8, Dept. Ex. No. 2.
2. The original shareholders were Joe Blow, Taxpayer's cousin ("Blow), Taxpayer and Ron Doe ("Ron Doe") each of whom owned one-third of the corporate shares. *Id.*
3. Taxpayer did not invest any money in the Corporation. Tr. pp. 9, 20.
4. Taxpayer was president of the Corporation, but not a director. Tr. p. 10, Dept. Ex. No.2.
5. Initially, the Corporation was going to engage in the real estate business, but after that plan failed to develop, Blow decided that the Corporation would open a clothing store. Tr. pp. 8-11.
6. The store opened at 79th & Anywhere in Anywhere. *Id.*
7. After being open for about one year, the business closed sometime in the 2003-year. Tr. p. 27.
8. The Corporation maintained a bank account at the Bank for which Taxpayer was one of the signatories, and during the existence of the business he signed between 10 and 12 checks. Tr. pp. 12, 14-15, Tp. Exs. No. 1, 2.
9. None of the checks written against this account were made payable to Taxpayer. Tp. Ex. No. 1.
10. Taxpayer signed a document dated April 30, 2003 in which he resigned as "Director and Secretary" of the Corporation, effective as of that date. Tr. p. 18, Tp. Ex. No. 3.
11. The Corporation filed a Department of Revenue Form NUC-1 Illinois Business Registration on December 6, 2001. Line 14 in Section 2 and Section 7 on page four of

that form have the signature of John Doe subscribed as president and the person accepting “personal responsibility for the filing of returns and the payment of taxes due.”

Tr. pp. 21-22, Dept. Ex. 2.

12. The Department sent Taxpayer a Notice of Penalty Liability pursuant to 35 ILCS 735/3-7¹ on March 30, 2004 assessing penalties for the months of September 2002 through February 2003. Tr. p. 5, Dept Ex. No. 1.
13. The Department sent Taxpayer a Notice of Deficiency on March 31, 2004. assessing the penalty provided by IITA Section 1002(d)² for the 4th quarter of 2002. *Id.*

Conclusions of Law:

The Department issued the Notice of Penalty Liability and the Notice of Deficiency assessing the penalties involved in this case to Taxpayer as a person responsible for filing tax returns and paying the sales tax³ and withholding tax owed by the Corporation. The sales tax liabilities underlying the penalty assessed in the Notice of Penalty at issue are for the periods beginning with September of 2002 through February 2003 owed but not paid by the Corporation. The taxes underlying the penalty assessed in the Notice of Deficiency at issue are the taxes withheld from employees of the Corporation for the fourth quarter of 2002.

In the case of the sales tax liability, UPIA Section 735/3-7 assesses a penalty equal to the amount of tax due against any officer, partner or employee of a corporation who is responsible for paying the corporation’s sales tax liability. Specifically, the applicable section provides as follows:

¹ The Uniform Penalty and Interest Act. (“UPIA”) 35 ILCS 735/1, *et seq.*

² The Illinois Income Tax Act (“IITA” or the “Act”), 35 ILCS 5/101, *et seq.*

³ The Retailers’ Occupation Tax Act (ROTA), 35 ILCS 120/1 *et seq.*, sometimes referred to as *sales tax*.

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 wilfully fails to file the return or make the payment to the Department or wilfully 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. 735 ILCS 735/3-7.

In the case of the withholding tax, the applicable statute provides as follows:

Any person required to collect, truthfully account for, and pay over the tax imposed by this 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 the payment thereof, shall, in addition to other penalties provided by law, be liable for the penalty imposed by Section 3-7 of the Uniform Penalty and Interest Act.
35 ILCS 5/1002(d).

These sections, taken together, prescribe two tests to determine if an individual is personally liable for unpaid tax. First, under both provisions, the person must be responsible for accounting for and paying the tax due. Second, the individual must willfully fail to file or pay the tax shown to be due on the payroll tax returns.

In this case, once the Department introduced into evidence the Notice of Deficiency and the Notice of Penalty Liability under the Director's certificate, its *prima facie* case was made on the questions of responsibility and willfulness. *Branson v. Dept. of Revenue*, 168 Ill.2d 247, 261-262 (1995). The burden then shifted to the Taxpayer to overcome the Department's case. *Id.* To rebut the Department's *prima facie* case, Taxpayer had to come forward with sufficient evidence to disprove the Department's case. *Id.* at 262.

The statute does not define the concept of willful failure. However, in applying the penalty tax, the Illinois courts look to federal cases involving § 6672 of the Internal Revenue

Code⁴, which contains language similar to the Illinois statute. *Branson, supra* at 254 (1995), *Dept of Revenue v. Joseph Bublick & Sons*, 68 Ill.2d 568 (1977).

Taxpayer testified that he had nothing to do with the operation of the store. He testified that his cousin, Blow, ran the store. He testified that he never received compensation for working there. Taxpayer testified that he never prepared any tax returns and did not know that there was a tax problem until he received the notices from the Department. He testified that he had no responsibility for preparing or filing tax returns.

Jones-Smith testified that he was employed by the Corporation from the time the store opened until it closed in 2003, a period of about one year. He testified that he started out as a sales person, and later moved up to being a buyer and manager. He testified that he only knew Taxpayer as a relative of Blow and never saw him doing anything with respect to the operation or administration of the Corporation's business, and that he only saw Taxpayer in the store when he came in to shop.

Ron Doe, one of the original shareholders in the Corporation, testified that neither he nor Taxpayer invested any money in the Corporation; that he was an employee of the Corporation originally; that he resigned in December of 2001; and that Blow had complete control over the store operations and that he ran the store by himself. Ron Doe testified that he had been in the store 5 or 10 times. He testified that he heard Taxpayer resign from the Corporation at the same time he did in December 2001.

Taxpayer testified that he rarely visited the store. He testified that, "Maybe once or twice every other month or so I would probably stop by there. I mean it was my cousin; it's his clothing store. I would get discounts." Tr. p. 11. Later, in response to the question "And you never went there?" He responded, "No." In response to the next question, "Just on several

⁴ 26 U.S.C. § 6672.

occasions?” He responded, “Right.” Tr. p. 19. None of this testimony regarding Taxpayer’s infrequent visits to the store and Blow’s complete control over the operation of the store was rebutted.

Taxpayer testified that he tried to resign as president early on. This testimony is supported by the testimony of Ron Doe. It is also supported by the fact that, although Taxpayer had check signing authority over the Corporation’s checking account, and signed about ten checks during the period that the business was in operation, none of the checks he signed were dated after June 2, 2002. Tr. pp. 6, 12, 15, Tp. Exs. No. 1⁵ & 2. This also supports Taxpayer’s testimony that he had nothing to do with running the store or the Corporation.

The NUC-1 Business Registration Form filed by the Corporation has the signature of Taxpayer as the person accepting personal responsibility for the filing of returns and paying taxes on Line 14 of Section 2 of the form. Dept. Ex. No. 2. The same signature appears on the signature line of the affidavit in Section 7 of the form. However, Taxpayer testified that neither one of these signatures on the Business Registration form is his signature. This testimony is supported by the signatures on the checks that he admitted that he signed and on the subscription to the transcript of his deposition at taken at the request of the Department that he signed under oath. Dept. Ex. No. 3. A comparison of the signatures that purport to be those of Taxpayer on the NUC 1 form with those on the Corporation’s checks that he admitted that he signed and on the subscription to the transcript of his deposition make it clear that the signatures that purport to be his on the NUC 1 form were written by someone other than Taxpayer.

Being a corporate officer does not, *per se*, impose the duty to collect, account for and pay over the withheld taxes. *Monday v. U.S.*, 421 F.2d 1210, (7th Cir. 1970). However, an officer may

⁵ In addition, a perusal of the Corporation’s checking account for the period November 1, 2001 through January 31, 2004, establishes that no checks written during that period of time were made payable to Taxpayer.

have that duty even though he does not have the treasury function. *Id.* He has the duty if he has general control over corporate business affairs and participates in decisions concerning payment of creditors. *Id.*

The Corporation in this case had three equal shareholders. Taxpayer was one of them, although he had not invested any funds in the business. Although, he was the president of the corporation, his testimony and the unrefuted testimony of Jones-Smith and Ron Doe establish that Blow ran the business by himself and that Taxpayer had nothing to do with the operation other than signing a few checks during the first six months of 2002. The record in this case establishes that although Taxpayer may have been president until he submitted his written resignation, and by that fact may have been a responsible party, he did not willfully failed to file returns for and pay the corporate tax that led to the penalty assessments in this case.

I find that Taxpayer the evidence of record is sufficient to overcome the Department's *prima facie* case.

Therefore, I recommend that the Notice of Deficiency and the Notice of Penalty Liability be canceled.

ENTER: March 30, 2005

Charles E. McClellan