

ST 10-05

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)	No.
)	NPL:
)	Letter ID:
v.)	Account ID:
)	
JOHN DOE,)	
as responsible officer of)	
THE ABC MARKET,)	Administrative Law Judge
TAXPAYER)	Kenneth J. Galvin

RECOMMENDATION FOR DISPOSITION

Appearances: Mr. John Doe, appearing *pro se*; Mr. George Foster, Special Assistant Attorney General, on behalf of the Department of Revenue of the State of Illinois.

Synopsis:

This matter comes on for hearing pursuant to Mr. John Doe’s protest of Notice of Penalty Liability No. (hereinafter “NPL”) as responsible officer of The ABC Market (hereinafter “ABC”). The NPL represents a penalty liability for retailers’ occupation tax of ABC due to the Department for August, 2005 and January through April of 2006. An evidentiary hearing was held in this matter on February 18, 2010 with Mr. and Mrs. Doe testifying. Following submission of all evidence and a review of the record, it is recommended that the NPL be finalized as issued. In support thereof, the following “Findings of Fact” and “Conclusions of Law” are made.

Findings of Fact:

1. The Department's *prima facie* case, inclusive of all jurisdictional elements, is established by the admission into evidence of NPL No. dated June 4, 2008, which shows a penalty for sales tax liability of The ABC Market of \$17,071.74 for August, 2005, and January through April, 2006. Tr. pp. 4-5; Dept. Ex. No. 1.
2. Mr. Doe owned 50% of the shares of ABC and was corporate secretary of the corporation. Mr. Doe was at ABC on a daily basis, oversaw the physical operation of the store, and was an authorized check signer for the business. Mr. Doe managed 30 employees. Tr. pp. 9-11.
3. During the period covered by the NPL, Mr. Doe paid vendors and he was aware that ABC had cash flow problems. Mr. Doe made decisions as to which vendors would be paid first and which vendors would have to wait. He was aware that ABC bounced checks to vendors during the period covered by the NPL and he was aware that there was unpaid liability to the Department of Revenue. Tr. pp. 11-14.

Conclusions of Law:

The sole issue to be decided in this case is whether Mr. Doe should be held personally liable for the unpaid retailers' occupation tax of ABC. 35 ILCS 120 *et seq.* The statutory basis upon which any personal liability is premised is Section 3-7 of the Uniform Penalty and Interest Act, which provides as follows:

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 to 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. The Department shall determine a penalty due under this Section according to its best judgment and information, and that determination shall be prima facie correct and shall be prima facie evidence of a penalty due under this Section.

35 ILCS 735/3-7.

It is clear under the statute that personal liability will be imposed only upon a person who: (1) is responsible for filing corporate tax returns and/or making the tax payments; and (2) “willfully” fails to file returns or make payments.

In determining whether an individual is a responsible person, the courts have indicated that the focus should be on whether that person has significant control over the business affairs of a corporation and whether he or she participates in decisions regarding the payment of creditors and disbursement of funds. Liability attaches to those with the power and responsibility within the corporate structure for seeing that the taxes are remitted to the government. Monday v. United States, 421 F. 2d 1210 (7th Cir. 1970), *cert. denied*, 400 U.S. 821 (1970). Additionally, the ability to sign corporate checks is a significant factor in determining whether a person is a responsible party because it generally comes with the ability to choose which creditors are paid. Gold v. United States, 506 F. Supp. 473, (E.D.N.Y 1981), *aff’d*, 671 F.2d 492 (2d Cir. 1982). Individuals who hold corporate office and who have authority to make disbursements are presumptively responsible persons for purposes of 26 USC § 6672, the federal responsible officer statute. Hildebrand v. United States, 563 F. Supp. 1259 (D.C. N.J. 1983).

The NPL at issue in this case covers the months of August, 2005, and January through April, 2006. Tr. pp. 4-5; Dept. Ex. No. 1. Mr. Doe testified that during the period covered by the NPL, he owned 50% of the shares of ABC and was corporate secretary of the corporation. Mr. Doe was at ABC on a daily basis, oversaw the physical operation of the store, and was an authorized check signer for the business. Mr. Doe managed 30 employees at ABC. Tr. pp. 9-11. As corporate secretary, with the ability to sign corporate checks, Mr. Doe could have written a check to the State of Illinois for unpaid taxes. Mr. Doe stated that he “never contested that the company and myself as an officer owed the outstanding taxes.” Tr. p. 6. Mr. Doe testified that he owned the business with Mr. Smith. Tr. p. 6. “The outstanding debt is there. I mean, we realized that, and I realize that as an officer of the company, I was responsible for it.” Tr. p. 8.

The testimony shows then that Mr. Doe was in a responsible position with ABC in which he knew or should have known whether returns were filed and taxes paid. In order to overcome the Department’s *prima facie* case, evidence must be presented which is consistent, probable and identified with the corporation’s books and records. Central Furniture Mart, Inc. v. Johnson, 157 Ill. App. 3d 907 (1st Dist. 1987). When the Department established its *prima facie* case, the burden shifted to Mr. Doe to overcome the presumption of responsibility through sufficient evidence. Branson v. Dept. of Revenue, 168 Ill. 2d 247 (1995). No evidence was offered by Mr. Doe at the hearing. Without any documentary evidence, I must conclude that Mr. Doe has failed to rebut the Department’s presumption that he was a responsible party of ABC during the period covered by the NPL.

The second and remaining element which must be met in order to impose personal liability is the willful failure to pay the taxes due. The Department presents a *prima facie* case for willfulness with the introduction of the NPL into evidence. Branson at 260. The burden, then, is on the responsible party to rebut the presumption of willfulness.

35 ILCS 735/3-7 fails to define what constitutes a willful failure to pay or file taxes. In attempting to clarify what constitutes a willful failure to file or pay taxes, the courts have adopted a broad interpretation of the words “willfully fails.” Department of Revenue ex rel. People v. Corrosion Systems, Inc., 185 Ill. App. 3d 580 (4th Dist. 1989). Under this broad interpretation, responsible officers are liable if they fail to inspect corporate records or otherwise fail to keep informed of the status of the retailers’ occupation tax returns and payments. Branson, supra. Willfulness also includes “failure to investigate or to correct mismanagement after having notice that withholding taxes have not been remitted to the Government.” Peterson v. United States, 758 F. Supp. 1209 (N.D. Ill. 1990). “Willfulness” as used in the statute may indicate a reckless disregard for obvious or known risks. Monday v. United States, 421 F. 2d 1210 (7th Cir. 1970) *cert. denied* 400 U.S. 821 (1970).

Mr. Doe’s conduct was willful under each of the above benchmarks. Mr. Doe testified that during the period covered by the NPL, he paid vendors. Mr. Doe was aware that ABC had cash flow problems. Mr. Doe made decisions as to which vendors would be paid first and which vendors would have to wait. He was aware that ABC bounced checks to vendors during the period covered by the NPL and he was aware that there was unpaid liability to the Department of Revenue. Tr. pp. 11-14. It is clear from Mr. Doe’s

own testimony that he failed to keep informed of the status of the retailer's occupation tax returns and payments and he failed to correct mismanagement when he was aware that taxes had not been remitted to the State, exhibiting willfulness.

Mr. Doe testified that, as ABC was being liquidated, Mr. Smith took \$100,000 from the business. He took this money "by agreement" with Mr. Doe. According to Mr. Doe's testimony, it was also "the agreement" that Mr. Smith would pay the taxes due to the Department of Revenue. "He agreed to pay the sales taxes and both of our personal bankruptcies, as well as the company's bankruptcy." Tr. pp. 7, 13-14. This agreement was "verbal." Tr. p. 7. By allowing Mr. Smith to take the \$100,000 without first paying the State for the delinquent sales taxes, Mr. Doe exhibited reckless disregard for obvious or known risks, further showing willfulness.

Mr. Doe's "agreement" with Mr. Smith does not relieve Mr. Doe from liability for the sales taxes. The statute does not confine liability to only one person or to the person most responsible. All responsible persons owe a fiduciary obligation to care properly for the funds that are entrusted to them. "A fiduciary cannot absolve himself merely by disregarding his duty and leaving it to someone else to discharge." Hornsby v. Internal Revenue Service, 558 F. 2d 952 (5th Cir. 1979). One does not cease to be a responsible person merely by delegating that responsibility to others. Gustin v. United States, 876 F.2d 485 (5th Cir. 1989). Mr. Doe could not absolve himself from responsibility for the taxes by simply delegating their payment to Mr. Smith.

WHEREFORE, for the reasons stated above, it is my recommendation that Notice of Penalty Liability No. be finalized as issued.

April 2, 2010

Kenneth J. Galvin
Administrative Law Judge