

ST 05-15

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
IBT #: 0000-0000
NPL # 0000**

**Charles E. McClellan
Administrative Law Judge**

RECOMMENDATION FOR DECISION

Appearances: Marc Muchin, Special Assistant Attorney General, for the Illinois Department of Revenue (the “Department”); Lawrence Serlin for John Doe (“Taxpayer”).

Synopsis:

This matter arose from a protest filed by Taxpayer to a Notice of Penalty Liability issued to him by the Department on July 7, 2003. The NPL, in the amount of \$72,039.34 was issued to Taxpayer as a responsible officer or employee of ABC Enterprises, Inc. The underlying corporate liability for Retailers’ Occupation Tax and Use Tax (“sales tax”) was incurred by ABC Enterprises, Inc. d/b/a XYZ Liquors (“ABC”) for the months of July 1995 through February of the year 2000. The issue is whether Taxpayer is liable,

as a responsible person, for the penalty assessed him under § 735/3-7 of the Uniform Penalty and Interest Act¹.

I recommend that the Notice of Penalty Liability be made final.

Findings of Fact:

1. The Department issued a Notice of Penalty Liability to Taxpayer on July 7, 2003. Dept. Ex. No. 1.
2. The NPL, in the amount of \$72,039.34, was issued to Taxpayer as a responsible officer or employee of ABC Enterprises, Inc. d/b/a XYZ Liquors for the months of July 1995 through February of the year 2000. *Id.*
3. ABC, an Illinois corporation, filed annual reports signed by Taxpayer with the Illinois Secretary of State for each year from July 1995 through 2000 listing Taxpayer as president, secretary, and treasurer. Tr. pp. 43-45, Dept. Ex. No. 3.
4. In December 1982 Taxpayer signed an *Illinois Business Taxpayer Application for Registration* form by which ABC registered with the Department to operate a business called *XYZ Liquors*. Tr. p. 41, Dept. Ex. No. 2.
5. The XYZ Liquors store sold beer, wine, liquor, and sundry food items at retail. Tr. p. 49.
6. The store was open seven days each week for at least 12 hours per day. Tr. p. 50.
7. Taxpayer hired the manager of the store but let the manager hire the other store employees. Tr. p. 51.
8. The store occupied a leased property site. Tr. p. 51.

¹ Unless otherwise noted, all statutory references are to 35 ILCS 735/1, *et seq.*, the Uniform Penalty and Interest Act. (“UPIA”), or to the Retailers’ Occupation Tax Act (ROTA), 35 ILCS 120/1 *et seq.*, sometimes referred to as *sales tax*.

9. The business closed in February 2000 when ABC sold the business. Tr. pp. 50, 12.
10. On January 7, 2000, ABC's counsel submitted a Nuc-542-A *Notice of Sale or Purchase of Business Assets* to the Department which issued a bulk sales stop order to the purchaser requiring him to withhold \$15,000 to be held in escrow until all sales and withholding taxes are paid through the date of sale. Tr. pp. 13-15, Taxpayer Ex. Nos. 1, 2.
11. On February 23, 2000, the Department issued a letter demanding payment of ROT of \$1,282.52, withholding tax of \$345.54, and individual income tax of \$47.06 from the escrow funds. Tr. p. 17, Taxpayer Ex. No. 3.
12. The February 23, 2000 letter stated on its face that, "The seller's account is subject to an audit or hearing which may result in additional liabilities." *Id.*
13. On May 15, 2000, the Department issued a bulk sale stop order release. Tr. p. 19, Taxpayer Ex. No 4.
14. The May 15, 2000 stop order release stated on its face that, "This release does not mean that the seller is not liable for any liabilities that are due now or in the future." *Id.*
15. Taxpayer prepared all of ABC's sales tax returns and signed the checks to pay the taxes owed. Tr. p. 57.
16. Some of ABC's books and records were kept in the store, and some were kept at Taxpayer's home. Tr. p. 52.
17. ABC kept cash register tapes recording sales at the store and Taxpayer would call the store from home to obtain sales figures which he would record on the

back of a cigarette carton to add up and report on ABC's sales tax returns. Tr. pp. 53-54.

18. Taxpayer either prepared and signed ABC's checks to pay creditors and suppliers, or he pre-signed blank checks so his employees could do so. Tr. pp. 62-64.
19. The Department audited ABC's sales tax account for the periods July 1995 through February 2000 at the conclusion of which it issued a Notice of Tax Liability dated October 11, 2002. Tr. pp. 74-75, Dept. Ex. No. 4.
20. The Notice of Tax Liability was sent to Taxpayer at his last known residence address by U.S. Certified Mail and the Certified Mail Receipt was signed by Jane Doe at that address on October 15, 2002. *Id.*
21. When the dates approached beyond which the Department would have been barred by statute from issuing a Notice of Tax Liability to ABC, the Department obtained waivers from the Taxpayer, except for the period January through June 1999. Tr. pp. 77-79, Dept. Ex. No. 4.
22. The Notice of Tax Liability issued to ABC was never protested. Tr. p.74.

Conclusions of Law:

A pre-trial order was entered into the record for this case on January 13, 2005, in which the parties specified the issues to be resolved at the hearing as follows:

1. Whether Taxpayer is a responsible officer or employee.
2. Whether Taxpayer willfully failed to file returns or pay taxes to the Department.

The statute that imposes personal liability for paying to the state unpaid corporate Retailers' Occupation Tax and Use Tax obligations 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 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(a).

This section of the statute sets forth two tests for determining whether a person has personal liability for unpaid sales tax incurred by a corporation. First, 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 his closing argument, Taxpayer challenged the validity of the Notice of Tax Liability issued to ABC which gave rise to the Notice of Penalty Liability at issue in this matter. Specifically, he challenged the Department's audit procedures and whether the bulk sale stop order release precluded any further assessments of sales tax. He also asserted that there is no evidence that Taxpayer acted willfully in failing to pay sales tax due the Department and he challenged the Department's issuance of the Notice of Tax Liability to ABC.

With regard to the validity of the Notice of Tax Liability issued to ABC, the statute provides that a Notice of Tax Liability becomes final unless the taxpayer files a protest within 60 days after it is issued. 35 ILCS 120/4. Once the Notice of Tax Liability becomes final, the taxpayer has 35 days within which to file an administrative appeal in the circuit court. 735 ILCS 5/3-103. In this case ABC did not file a protest to the Notice

of Tax Liability nor did he file an administrative appeal to the circuit court, so it became final and conclusive as to all questions concerning its merits. *Dept. of Revenue v. Roman S. Dombrowski Enterprises*, 202 Ill. App. 3d 1050, 560 N.E.2d 881 (1st Dist. 1990).

Taxpayer's assertion that the bulk sale stop order release is without merit. The bulk sale stop order and the bulk sale stop order release both stated on their face that the seller, ABC, could be subject to audit and additional sales tax assessments. Therefore, both documents were conditioned upon the possibility of additional sales tax assessments.

As to the Taxpayer's liability for the penalty assessment, the record shows that Taxpayer was a responsible party. Taxpayer was the president, treasurer and secretary of ABC during the entire audit period. He prepared the sales tax returns and he signed the checks to pay creditors including the Department. These factors establish that he was a responsible officer.

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 Code² which contains language similar to the Illinois statute. *Branson v. Dept. of Revenue*, 168 Ill.2d 247, 254, 659 N.E.2d 961, 965, *Dept of Revenue v. Joseph Bublick & Sons*, 68 Ill.2d 568 (1977). The key to liability under IRC § 6672 is control of finances within the employer corporation including the power to control the allocation of funds to other creditors in preference to the withholding tax obligations. *Haffa v. U.S.*, 516 F.2d 931 (7th Cir. 1975). The issue of willfulness is concerned with the state of the responsible person's state of mind. *Sawyer v. U.S.*, 831 F.2d 755 (7th Cir. 1987) "Willful failure to pay taxes has generally been defined as involving intentional, knowing and voluntary acts

² 26 U.S.C. § 6672.

or, alternatively, reckless disregard for obvious or known risks.” *Branson, supra*, 168 Ill.2d at 255.

The record establishes that Taxpayer satisfied the requirements as set forth in *Branson, supra*. He testified that the cash register in the store produced tapes that recorded sales. However, he obtained the sales figures that he reported by telephone from his employees when he called them from home. There is no evidence that he ever made an attempt or instituted any controls to make sure that the numbers were being accurately recorded. He controlled the allocation of funds because he either signed the checks at bill paying time or he pre-signed blank checks so that his store employees could pay them. At best this shows a reckless disregard for the obvious risk that the numbers would not be correct and that the taxes might not be paid accurately or timely. There is nothing in the record to demonstrate that Taxpayer took any steps to make sure that the gross receipts numbers reported on ABC’s sales tax returns were accurate. By his own testimony, he was totally responsible for properly reporting and paying over the sales taxes due. He failed in this responsibility. The record clearly establishes willfulness under the law.

In this case, once the Department introduced into evidence the Notice of Deficiency 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 at 260. 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.* Taxpayer has failed to introduce any evidence to overcome the Department’s *prima facie* case.

Therefore, I recommend that the Notice of Penalty Liability be made final.

ENTER: June 24, 2005

**Charles E. McClellan
Administrative Law Judge**