

CALIFORNIA STATE BOARD OF EQUALIZATION
APPEALS DIVISION BOARD HEARING SUMMARY

In the Matter of the Petition for Redetermination)
Under the Sales and Use Tax Law of:)
RICHARD CLARK FARRELL) Account Number SR EA 53-007717
Petitioner) Case ID 600710
Costa Mesa, Orange County

Type of Liability: Responsible person liability
Liability period: 01/01/05 – 03/31/05

<u>Item</u>	<u>Disputed Amount</u>
Responsible person liability	\$585,612
Tax as determined and protested	\$ 468,489.52
Interest through 04/30/16	468,146.82
Fraud penalty	<u>117,122.82</u>
Total tax, interest, and penalty	<u>\$1,053,759.16</u>
Monthly interest beginning 05/01/16	<u>\$ 2,342.45</u>

This matter was scheduled for Board hearing in August 2015, but petitioner did not respond to the Notice of Hearing timely, and the matter was scheduled for decision on the nonappearance calendar. Subsequently, petitioner contacted the Board Proceedings Division, and the matter was rescheduled for hearing. The matter was rescheduled for Board hearing in November 2015, but was postponed at petitioner’s request, in order to allow additional time to prepare. It was again scheduled for Board hearing in February 2016, but petitioner did not respond to the Notice of Hearing, and the matter was scheduled on the nonappearance calendar for March 2016. Petitioner then filed a late response to the Notice of hearing.

This appeal involves an amount in controversy that is \$500,000 or more and thus is covered by Revenue and Taxation Code section 40. Please see below for details.

UNRESOLVED ISSUE

Issue: Whether petitioner is personally liable as a responsible person for the unpaid liabilities of Irvine Photo Graphics, Inc., pursuant to Revenue and Taxation Code section 6829. We conclude petitioner is personally liable.

1 Irvine Photo Graphics, Inc. (IPG) (SR EA 99-574726) sold printed matter.¹ At the time its
2 business terminated, IPG had an unpaid liability related to a Notice of Determination (NOD) issued to
3 IPG because it had received a refund of excess tax reimbursement on sales made to The Gap, Inc.
4 (Gap), and it had not refunded the excess tax reimbursement to Gap. The Business Tax and Fee
5 Department, formerly the Sales and Use Tax Department (Department) concluded that petitioner was
6 personally responsible for IPG's sales and use tax compliance pursuant to section 6829.²

7 The facts in this case are somewhat atypical. Briefly stated, IPG filed a claim for refund of
8 excess tax reimbursement paid on sales to Gap with respect to exempt sales in interstate commerce.
9 According to petitioner, the excess tax reimbursement was discovered by KPMG, and Mark Stefan of
10 KPMG contacted IPG to ask that it file a claim for refund of the overpayments. Petitioner (on behalf
11 of IPG) was reluctant to take on the task of filing the claim for refund, asserting that it would take
12 numerous hours of the staff's time. Petitioner states that he told Mr. Stefan multiple times that the
13 compiling of information would be a time-consuming process. Petitioner further states that Mr. Stefan
14 told him to offset any expenses against the amount refunded to Gap.

15 Petitioner asserts that IPG filed the claim for refund with the understanding that IPG would be
16 reimbursed for any and all expenses related to filing the claim, and that he fully expected those
17 expenses to be in the hundreds of thousands of dollars. He also asserts Mr. Stefan was fully aware of
18 that expectation and fully aware that the refund to Gap would be dramatically reduced from the amount
19 of refund IPG received from the Board.

20 The excess tax reimbursement was refunded to IPG in early February 2005. IPG did not refund
21 any portion of the amount to Gap, and Gap eventually contacted the Department for assistance in
22 encouraging IPG to make the refund. IPG failed to do so, and the Department issued an NOD to IPG
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26 ¹ Although there is no dispute that IPG's business operations have been terminated, the date of business termination is not
entirely clear. However that specific date is not relevant to the matter at issue.

27 ² The Department also considered whether Betty Farrell (petitioner's former wife and the vice-president of IPG) was
28 responsible for IPG's sales and use tax matters, but it concluded that she did not have the requisite knowledge of the
liability at issue to sustain personal liability under section 6829. The Department did not identify any other individuals who
were responsible for IPG's sales and use tax compliance.

1 for tax of \$468,491.28, a fraud penalty of \$117,122.82, and accrued interest. This is the liability for
2 which the Department seeks to hold petitioner personally responsible under section 6829.

3 There are four elements required to impose liability under section 6829, and each is clearly
4 established in this appeal. First, there is no dispute that IPG's business operations terminated by the
5 end of December 2009. Second, since the entire amount at issue represents excess sales tax
6 reimbursement that IPG has not refunded to Gap, it is clear that IPG collected sales tax reimbursement
7 with respect to its taxable sales.

8 Third, at all relevant times, petitioner was the president of IPG, and he was actively involved in
9 all its dealings with the Department both during the period in which the claim for refund of excess tax
10 reimbursement was filed and granted, and during the period in which the NOD was issued to IPG
11 because it had not made the refund to its customer, Gap. Thus, there is ample evidence that petitioner
12 was a person responsible for IPG's sales and use tax matters and for this specific liability.

13 Fourth, regarding willfulness, there is no dispute that petitioner was fully aware that the refund
14 of excess tax reimbursement that IPG received in February 2005 was required to be paid to Gap (which
15 was the whole reason for the Board's refund), or returned to the Board, and therefore petitioner had
16 actual knowledge of the liability as early as February 2005. Additionally, the very premise of
17 petitioner's argument (i.e., that IPG had an alleged agreement with Gap allowing IPG to offset its costs
18 *against the refund owed to Gap*) establishes that petitioner had actual knowledge of the liability no
19 later than IPG's receipt of the refund. Furthermore, petitioner clearly had actual knowledge of the
20 liability no later than November 16, 2010, when the NOD was issued.

21 Next, there is no dispute that there were funds available to pay the liability (since IPG had
22 received a refund, and the Department had issued an NOD for repayment of that same amount). In
23 addition during the period 2005 through 2008, IPG reported approximately \$12 million in gross
24 receipts on its sales and use tax returns, and paid approximately \$6 million in wages. Finally, it is clear
25 that, at all relevant times, petitioner had the authority to pay the liability to either the Gap or the Board.
26 Thus, there really is no question that all four conditions have been met to hold petitioner personally
27 liable under section 6829 for the unpaid tax liability at issue.

28 On appeal, petitioner argues that he did not willfully fail to pay the tax liability at issue because
he contends that IPG was not liable for the amount due, raising the same arguments that he raised

1 when IPG's appeal was considered by the Appeals Division. We note that no one appeared at the
2 Board hearing regarding the appeal, and the Board upheld the Appeals Division's recommendation that
3 IPG's appeal be denied.

4 In brief, petitioner argues that IPG effectively refunded the entire amount (almost one-half
5 million dollars) to Gap by offsetting its expenses against the amount of excess tax reimbursement to be
6 refunded to Gap. Petitioner has offered various explanations of how the agreement regarding this
7 offset procedure was reached between IPG and KPMG, some of which are conflicting. The salient
8 point, however, is that neither IPG nor petitioner has provided any documentation showing that there
9 was any agreement. The fact is that IPG received a refund of about \$468,490 of excess tax
10 reimbursement that it had collected from Gap. IPG was required to refund the excess tax
11 reimbursement to Gap or return the entire amount to the Board. There is no dispute that IPG never
12 issued a check for any portion of that refund to Gap, and there is no evidence of any agreement
13 between the parties that IPG was authorized to retain funds to offset expenses that equaled the amount
14 of the refund. Petitioner has not shown that the refund has been effectively granted to Gap, and we
15 find IPG owes the unpaid liability, and petitioner is personally liable pursuant to section 6829.

16 Section 40 Matter

17 As noted above, this matter is subject to Revenue and Taxation Code section 40. Therefore,
18 within 120 days from the date the Board's vote to decide the appeal becomes final, a written opinion
19 (i.e., Summary Decision or Memorandum Opinion) must be published on the Board's website. (Cal.
20 Code Regs., tit. 18, § 5552, subs. (b), (f).) The Board's vote to decide the appeal will become final 30
21 days following the date on which notice of the Board's decision is mailed to the parties, except when a
22 petition for rehearing is filed within that period.³ (Cal. Code Regs., tit. 18, § BT: 5561, subd. (a).)

23 Following the conclusion of this hearing, if the Board votes to decide the appeal, but does not
24 specify whether a Summary Decision or a Memorandum Opinion should be prepared, staff will
25 expeditiously prepare a nonprecedential Summary Decision and submit it to the Board for
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27 ³ If a petition for rehearing is filed, the Board's decision will not become final, and no written opinion under Section 40 will
28 be considered until after the petition for rehearing is resolved.

1 consideration at a subsequent meeting. (Cal. Code Regs., tit. 18, § 5551, subd. (b)(2).) Unless the
2 Board directs otherwise, the proposed Summary Decision would not be confidential pending its
3 consideration by the Board (Cal. Code Regs., tit. 18 § 5551, subd. (b)(5)); accordingly, it would be
4 posted on the Public Agenda Notice for the meeting at which the Board will consider and vote on the
5 Summary Decision.

6 A taxpayer may request that the Board hold in abeyance its vote to decide the appeal so the
7 taxpayer may review the Board's written opinion prior to the expiration of the 30-day period for the
8 filing of a petition for rehearing. If the vote is held in abeyance, the proposed Summary Decision will
9 be confidential until it is adopted by the Board. (Cal. Code Regs., tit. 18, § 5551, subd. (b)(5).) Any
10 request that the Board's vote be held in abeyance should be made in writing to the Board Proceedings
11 Division prior to the hearing or as part of oral argument at the hearing. Any such request would then
12 be considered by the Board during its deliberations on the appeal.

13 **OTHER MATTERS**

14 None.

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16 Summary prepared by Deborah A. Cumins, Business Taxes Specialist III
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