

**CALIFORNIA STATE BOARD OF EQUALIZATION**

**APPEALS DIVISION SUMMARY FOR BOARD HEARING**

In the Matter of the Administrative Protest )  
 Under the Sales and Use Tax Law of: )  
 LISA MARIE BAGOT ) Account Number: SR FH 53-003453  
 ) Case ID 435016  
 Taxpayer ) San Diego, San Diego County

Type of Liability: Responsible person liability

Liability Period: 1/1/96 – 6/30/02

<u>Item</u>	<u>Disputed Amount</u>	<u>Tax</u>	<u>Penalty</u>
Responsible person liability	\$23,487.88		
As determined, protested		<u>\$18,986.42</u>	<u>\$4,501.46</u>
Proposed tax redetermination		\$18,986.42	
Interest to 3/31/11		25,202.17	
Negligence penalty		1,122.60	
Late prepayment penalty		14.00	
Late payment penalty		33.20	
Penalty for failure to timely pay determination		<u>3,331.66</u>	
Total tax, interest, and penalties		\$48,690.05	
Payments		<u>-677.61</u>	
Balance due		<u>\$48,012.44</u>	
Monthly interest beginning 4/1/11		<u>\$106.80</u>	

**UNRESOLVED ISSUES**

**Issue 1:** Whether taxpayer is personally liable as a responsible person for the unpaid liabilities of Blue Cape International, Inc. (Blue Cape) (SR FH 25-901826) for the period January 1, 1996, through June 30, 2002. We find that taxpayer is personally liable.

Blue Cape was incorporated on April 26, 1991 under the name of Creative Integration, Inc. (Creative). Creative obtained a seller’s permit effective May 1, 1991. On May 19, 2000, Creative filed a Certificate of Amendment with the Secretary of State, and changed its corporate name to Blue Cape International, Inc. Blue Cape terminated its business on June 30, 2002, and on September 26,

1 2002, the Sales and Use Tax Department (Department) closed out Blue Cape's seller's permit effective  
2 June 30, 2002. At the time of its termination, Blue Cape had unpaid liabilities, mostly established by a  
3 Notice of Determination (NOD) issued for each of two audits covering the period January 1, 1996,  
4 through June 30, 2002, consisting of: tax of \$18,986.42; negligence penalty of \$1,122.60; finality  
5 penalty of \$3,331.66; amnesty interest penalty of \$4,671.71; late payment penalty of \$33.20 for the  
6 third quarter 2001 (3Q01); and late prepayment penalty of \$14.00 for August 2000.

7 The Department determined that taxpayer is personally liable for Blue Cape's unpaid liabilities  
8 pursuant to Revenue and Taxation Code section 6829, based on the following facts: (1) several sales  
9 and use tax returns and prepayment forms were signed by taxpayer on behalf of Blue Cape; (2) several  
10 documents identified taxpayer as an officer of Blue Cape; (3) a document that showed taxpayer had a  
11 49 percent stock ownership of Blue Cape; (4) taxpayer communicated with the Board on several  
12 occasions regarding Blue Cape's sales and use tax matters; and (5) taxpayer participated in the  
13 discussion of the audit results. The Department also found that Blue Cape added sales tax  
14 reimbursement to the selling price of taxable sales based on the two audit reports and that taxpayer had  
15 been willful in her failure to pay the outstanding liabilities of Blue Cape because, although Blue Cape  
16 had funds available, they were used instead to pay wages and to pay vendors and other creditors. Since  
17 the Department found all four conditions to imposing liability on taxpayer pursuant to section 6829  
18 were satisfied, it issued an NOD to taxpayer as a responsible person for the unpaid liabilities of Blue  
19 Cape. Taxpayer filed an untimely appeal, which the Department accepted as an administrative protest.

20 Taxpayer conceded that Blue Cape terminated its business operations on June 30, 2002, and  
21 added sales tax reimbursement to the selling price of tangible personal property, two of the four  
22 conditions for imposing personal liability pursuant to section 6829. However, with respect to the other  
23 two conditions for imposing liability under section 6829, taxpayer contends that she was not  
24 responsible for reporting or paying Blue Cape's sales and use tax liabilities and that she did not  
25 willfully fail to pay the liabilities at issue, although she did not provide any specific supporting  
26 arguments for these contentions.

27 A responsible person for purposes of section 6829 is a person who had a duty to act for the  
28 corporation in complying with any provision of the Sales and Use Tax Law when the subject taxes

1 became due, including responsibility for the filing of returns or the payment of tax. As president of  
2 Blue Cape, taxpayer was the general manager and executive officer of Blue Cape, unless otherwise  
3 provided in the articles or bylaws of the corporation. Taxpayer has not shown that there was any  
4 limitation on her authority, and thus we find that taxpayer had broad implied and actual authority to do  
5 all the acts connected with the operation of Blue Cape, including ensuring that Blue Cape complied  
6 with the Sales and Use Tax Law. Furthermore, taxpayer signed Blue Cape's sales and use tax returns  
7 from at least 3Q95 through 2Q02, and she has not shown any diminution in her responsibilities with  
8 respect to Blue Cape's sales and use tax compliance during the liability period. Thus, we find that  
9 taxpayer was a responsible person under section 6829 for the period in issue.

10 With respect to willfulness, personal liability can be imposed on a responsible person under  
11 section 6829 only if that person willfully failed to pay or to cause to be paid taxes due from the  
12 corporation, which means that the failure was the result of an intentional, conscious, and voluntary  
13 course of action (even if without a bad purpose or evil motive). A person is regarded as having  
14 willfully failed to pay taxes, or cause them to be paid, where he or she had knowledge that the taxes  
15 were not being paid (or lacked knowledge in reckless disregard of his or her duty to know) and had the  
16 authority to pay taxes or cause them to be paid, but failed to do so.

17 Taxpayer was clearly aware of the liabilities established by the two audits of Blue Cape since  
18 she participated in the discussion regarding the results of the two audits. As president, taxpayer clearly  
19 had the authority to pay or cause to be paid the amounts due, and evidence shows that Blue Cape had  
20 sufficient funds available to pay each of the liabilities when they became due. However, rather than  
21 paying the taxes due, the available funds were instead were used to pay other creditors and debts. We  
22 find that, by causing or allowing such payments to other creditors rather than to pay the taxes due,  
23 taxpayer willfully failed to pay or to cause to be paid the taxes due.

24 Accordingly, we conclude that all four conditions for imposition of personal liability on  
25 taxpayer pursuant to section 6829 for the tax debts incurred by Blue Cape have been satisfied.

26 **Issue 2:** Whether taxpayer has established that the liabilities established in the audit for the  
27 period October 1, 1999 through June 30, 2002, were overstated. We conclude that she has not.  
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1           During the audit, the Department found that sales invoices were incomplete and did not match  
2 the sales journal provided. Blue Cape also was unable to provide all the records requested. Thus, the  
3 Department compared recorded sales with gross receipts reported on Blue Cape's 2000 and 2002  
4 federal income tax returns and found differences which the Department concluded were unreported  
5 taxable sales. The Department also compared recorded taxable sales with taxable sales reported on  
6 sales and use tax returns and found differences which the Department also concluded were unreported  
7 taxable sales. The Department accepted Blue Cape's claimed nontaxable sales for resale, sales to the  
8 U.S. Government, sales in interstate commerce, and charges for service and installation labor.

9           Taxpayer contends that the audit deficiency was overstated but could not provide any  
10 documentary evidence to support her contention. Taxpayer explains that she could not provide any  
11 documentation because, after Blue Cape's business was terminated, all records were stored in her  
12 garage, and after the audit was completed, her residence and all of Blue Cape's records were destroyed  
13 in the Cedar wildfire on October 26, 2003.

14           We note that the Department utilized recognized and standard audit methodology to obtain a  
15 valid audited taxable measure and that the audit report was completed on April 16, 2003. Taxpayer  
16 had six months prior to the wildfire to submit any additional records in her possession but she did not  
17 do so. While taxpayer's loss of her residence and Blue Cape's records was unfortunate, the burden is  
18 upon her to explain the disparity between the Board's audit and Blue Cape's books and records. Thus,  
19 without additional records to support her contention, we find that any adjustment to the audit  
20 deficiency is not warranted.

21           **Issue 3:** Whether Blue Cape was negligent. We conclude that it was.

22           The Department imposed the negligence penalty for the audit period October 1, 1999, through  
23 June 30, 2002, because Blue Cape understated its taxable sales by 40 percent and failed to maintain  
24 adequate records to support total and taxable sales reported on its returns, including incomplete sales  
25 invoices which did not match the sales journal provided. Taxpayer argues that the negligence penalty  
26 should not apply in the second audit because Blue Cape provided the same records and utilized the  
27 same accounting software as in the prior audit, and a negligence penalty was not imposed in the prior  
28 audit.

1 We find that Blue Cape was negligent because it failed to maintain complete books and  
2 summary records or complete source documents, such as sales invoices, to support the amounts  
3 reported in its returns. We also find that an understatement of 40 percent compared to reported taxable  
4 sales is significant and constitutes strong evidence of negligence. Nor is taxpayer's contention  
5 persuasive. The error ratio of 8 percent and understatement of \$50,811 in the prior audit are much  
6 smaller than the error ratio of 40 percent and understatement of \$146,701 in the second audit, which  
7 alone supports the imposition of a negligence penalty in the second audit while no penalty was  
8 imposed in the prior audit. Furthermore, the prior audit did not indicate that Blue Cape failed to  
9 maintain adequate records while the second audit did find a failure to maintain adequate records. We  
10 find that the negligence penalty was properly imposed for the second audit period.

11 **Issue 4:** Whether taxpayer has established reasonable cause to relieve the late-prepayment,  
12 late-payment of return, and finality penalties assessed against Blue Cape. We conclude that taxpayer  
13 has not done so.

14 There is no statutory or regulatory authority for relieving penalties in section 6829  
15 determinations, but if Blue Cape were relieved of a penalty under Revenue and Taxation Code section  
16 6592, that relief will also inure to the benefit of taxpayer. Taxpayer submitted a declaration signed  
17 under penalty of perjury requesting relief from the penalties at issue. With respect to the finality  
18 penalties, taxpayer asserted that Blue Cape believed that a security bond in that amount of \$10,000 was  
19 in place and could be used to pay the outstanding liability for the first audit for the period January 1,  
20 1996, through December 31, 1998, but learned in 2006 that the bonding company that issued Blue  
21 Cape's sales tax bond had closed without paying Blue Cape's liability. For the second audit, taxpayer  
22 asserts that Blue Cape disputed the liability but did not have the resources to establish that it did not  
23 owe the tax.

24 We find taxpayer's contention that Blue Cape thought the audit liability would be paid through  
25 its security bond unpersuasive. We also find unpersuasive taxpayer's assertion that Blue Cape was not  
26 aware of the cancellation of its bond until sometime in 2006. First, taxpayer has not provided any  
27 records indicating that the Board was applying the security bond to the first audit liability. Second the  
28 first bondholder, Amwest Surety Insurance Co. notified the Board, all policy holders, principals,

1 obliges, and agents that all of its policies were to be canceled by July 6, 2001, pursuant to court order  
2 and that on September 5, 2001, American Contractors Indemnity Company issued a security bond,  
3 effective on August 2, 2001, to Blue Cape. Thus, Blue Cape knew about the cancellation of the bond  
4 in 2001, almost two years after its liability from the September 24, 1999 NOD became due, as  
5 evidenced by the action it took to obtain another bond from American Contractors Indemnity Company  
6 to replace the canceled bond.

7 With respect to the second audit liability, we find that taxpayer's explanation that Blue Cape  
8 intended to appeal the determination but could not do so because the records were lost in the Cedar  
9 Wildfire does not constitute reasonable cause and circumstances beyond Blue Cape's control  
10 warranting relief of the finality penalty. The NOD for the second audit liability was issued on June 2,  
11 2003, and became final on July 2, 2003, prior to the occurrence of the wildfire on October 26, 2003.  
12 Thus, the wildfire clearly was not the reason Blue Cape failed to timely file a petition for  
13 redetermination or pay the amount determined due prior to the finality date of July 2, 2003.

14 Taxpayer did not address Blue Cape's failure to make a prepayment of tax liability for the  
15 period August 1, 2000, through August 31, 2000, or its failure to timely pay its return for 3Q01. We  
16 conclude that relief from the late-prepayment, late-payment, and finality penalties is not warranted.

#### 17 **Amnesty**

18 Blue Cape did not participate in the amnesty program although the Tax Amnesty Application  
19 and Notice of Tax Amnesty Opportunity were mailed to her and to Blue Cape at their addresses of  
20 record on January 10, 2005. Accordingly, amnesty interest penalties were imposed totaling \$4,671.71,  
21 which were included in the NOD issued to taxpayer. Taxpayer has submitted a declaration signed  
22 under penalty of perjury on behalf of Blue Cape explaining that Blue Cape was not able to participate  
23 in the amnesty program because she did not receive notice of the Board's Tax Amnesty Program and  
24 first learned of it when she consulted with her attorney in 2009. Taxpayer declared that, after the  
25 October 2003 wildfire destroyed her home, she moved in with her friends until she rented a house in  
26 December 2003 and stayed there until May 2005. Taxpayer claims that during that time, she  
27 experienced difficulty in having her mail forwarded to the rental house address.  
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1 We believe it is possible that taxpayer and Blue Cape did not receive the Tax Amnesty  
2 Application mailed on January 10, 2005, and thus conclude that they should be given the benefit of  
3 doubt. Accordingly, we recommend that the amnesty interest penalty be relieved provided that  
4 taxpayer pays in full the tax and interest due within 30 days from the notice of final decision, or within  
5 that same period, enters into an installment payment agreement not exceeding 13 months and  
6 successfully completes that payment agreement.

7 **OTHER DEVELOPMENTS**

8 None.

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10 Summary prepared by Rey Obligacion, Retired Annuitant

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STATE BOARD OF EQUALIZATION  
SALES AND USE TAX APPEAL