

1 CALIFORNIA STATE BOARD OF EQUALIZATION

2 APPEALS DIVISION SUMMARY FOR BOARD HEARING

3 In the Matter of the Administrative Protest)
 4 Under the Sales and Use Tax Law of:)
 5 JOHN DOUGLAS BAILEY) Account Number: SR CH 53-002398
) Case ID 382279
 6 Taxpayer) Dallas, Texas

7 Type of Liability: Responsible person liability

8 Liability period: 07/01/98 – 06/28/01

9 Item Disputed Amount

10 Responsible person liability \$49,567

	<u>Tax</u>	<u>Penalties</u>
11 As determined:	\$70,718.30	\$17,409.27
12 Adjustment - Sales and Use Tax Department	-31,167.00	-6,233.40
13 - Appeals Division	<u>-1,054.52</u>	<u>-105.45</u>
14 Protested tax and penalties	<u>\$38,496.78</u> ¹	<u>\$11,070.42</u>
15 Proposed tax, after adjustments	\$38,496.78	
16 Interest through 11/30/10	30,451.64	
17 Penalties for late payment of returns	11,024.12 ²	
Finality penalty for 3Q00	<u>46.30</u>	
18 Total tax, interest, and penalties	\$80,018.84	
Payments	<u>-38,109.18</u> ³	
19 Balance Due	<u>\$41,909.66</u>	
Monthly interest beginning 12/1/10	<u>\$54.77</u>	

20 This matter was previously scheduled for Board hearing on December 15, 2009, but was
 21 postponed at the request of the Sales and Use Tax Department (Department) for further consideration.
 22 It was rescheduled for Board hearing on March 24, 2010, and then July 14, 2010, but was postponed
 23 because taxpayer could not appear on those dates due to medical issues.

24
25 ¹ Consisting of \$9,389.78 for the fourth quarter 2000 (4Q00) and \$29,107.00 tax for the 1Q01.26 ² \$955.62 for 2Q00, \$2,132.30 for 3Q00, \$5,025.50 for 4Q00, and \$2,910.70 for 1Q01.27 ³ All payments have been made by another responsible party, Katherine Kruss. With the exception of \$1,244.73 applied to
 28 3Q00, all payments have been applied to the 1Q01. For 1Q01, the tax of \$29,107.00 has been fully paid as well as
 \$7,757.45 of the interest, leaving interest of \$11,786.00 and penalty of \$2,910.70, for a total due for that quarter of
 \$14,696.70. If taxpayer were to prevail on his contention that the tax due for 1Q01 should be reduced to \$3,248.00
 (addressed under Issue 2), his maximum benefit would be the \$14,696.70 of interest and penalty that remain due. Any
 reduction for 1Q01 in excess of \$13,447.64 would represent an overpayment by Ms. Kruss.

UNRESOLVED ISSUES

1
2 **Issue 1:** Whether taxpayer is personally liable as a responsible person for the unpaid liabilities
3 of Sable Technologies, Inc. (Sable) (SR CH 19-747408) pursuant to Revenue and Taxation Code
4 section 6829. We conclude taxpayer is personally liable.

5 Sable developed and sold point-of-sale systems and other computer systems from May 1, 1988,
6 through June 28, 2001. At all times, Sable was a wholly owned subsidiary of ST Systems Corporation
7 (ST). At the time its business terminated, Sable had unpaid liabilities related to non-remittance returns
8 and late payment of returns, as well as an unpaid audit liability.

9 The Department issued a Notice of Determination for Sable's liability to Ms. Katherine Kruss
10 pursuant to section 6829. We issued a Decision and Recommendation (D&R) recommending that the
11 petition filed by Ms. Kruss be denied, and after a hearing on November 15, 2005, the Board agreed,
12 upholding the liability, and also directing that the Department to consider pursuing other persons who
13 might be responsible for Sable's liability (the appeal of Ms. Kruss is now closed). After considering
14 other persons who might be responsible for Sable's liability, in March 2006 the Department issued the
15 instant determination and a determination to Mr. Larry O'Connor. In our D&R in Mr. O'Connor's
16 appeal, we recommended that his petition be granted (that recommendation has been held in abeyance
17 pending the outcome of this matter).

18 After the Notice of Determination had been issued to taxpayer, the Department concluded that
19 he was not liable for the period after March 31, 2001, because he had resigned as CEO, president, and
20 chairman of the board of ST and its subsidiaries effective May 23, 2001. We concluded that taxpayer
21 is not responsible for the liability resulting from the determination issued pursuant to audit because that
22 determination was not issued until July 26, 2001, after taxpayer had resigned. The liability that
23 remains in dispute is \$38,496.78 in tax reported, but not paid, on returns filed for the second quarter
24 2000 (2Q00) through the 1Q01, applicable interest, and \$11,070.42 in penalties assessed with respect
25 to the late payment of those returns.

26 The Department determined that Sable's business was terminated on or about June 28, 2001,
27 and that the business had added or included sales tax reimbursement in its retail sales. These are two
28 of the four conditions for imposing personal liability on taxpayer for the tax debts incurred by Sable,

1 and they are undisputed. The other two conditions, which taxpayer does dispute, are that taxpayer
2 must have been responsible for sales tax compliance by Sable, and taxpayer must have willfully failed
3 to pay or to cause to be paid taxes due from Sable.

4 Taxpayer was elected to ST's board of directors in December 1997 and became chairman of the
5 board in July 1998. On July 2, 1998, taxpayer entered into a consulting agreement with ST. In
6 November 1999, taxpayer was appointed chief executive officer (CEO) of ST and its subsidiaries. In
7 March 2000, taxpayer also became the president of ST and its subsidiaries. Taxpayer resigned as
8 CEO, president, and chairman of the board of ST and its subsidiaries effective May 23, 2001.

9 The Department concluded that taxpayer is liable under section 6829 based on: (1)
10 questionnaires signed by employees and corporate officers; (2) records from an outside consultant
11 indicating that taxpayer was involved in payments to vendors; (3) bankruptcy documents that show
12 taxpayer as Sable's president; (4) California Secretary of State documents showing taxpayer was a
13 director and CEO of Sable as of March 30, 2000; and (5) a circular from ST indicating taxpayer was
14 named CEO in November 1999 and president in March 2000. The Department also determined that
15 taxpayer willfully failed to pay, or to cause to be paid, Sable's tax liabilities because Sable had funds
16 available at the time the taxes became due and chose to pay other creditors. In reaching this
17 conclusion, the Department noted that records from vendors and suppliers showed that they received
18 payments from Sable through July 2001.

19 Taxpayer contends that he is not personally liable for Sable's unpaid tax liabilities because he
20 was merely a consultant whose duties consisted primarily of developing strategic plans and budgets
21 and reporting to ST's board of directors. Although taxpayer was chairman of the board and then
22 president and CEO, he contends that he never had the powers or responsibilities that traditionally
23 accompany those titles, and since he lived in Texas, he had little involvement in the day-to-day
24 operations. Taxpayer maintains that the payment of Sable's bills, including tax liabilities, could be
25 authorized only by ST's board of directors. Although he concedes that he regularly reported to the
26 board, taxpayer contends that he was only a "conduit," passing information from Sable to the board
27 and relaying instructions from the board to Sable's management. Taxpayer asserts that he was not
28 even aware of Sable's unpaid tax liabilities until October 2000, and, once he became aware of the tax

1 liabilities, he used what authority he had to try to get the taxes paid. Moreover, taxpayer contends that
2 he left his position at Sable and ST on April 1, 2001, and thus he should not be held responsible for
3 any taxes that became due after that date.

4 Regarding taxpayer's contention that his titles with Sable and its parent, ST, were merely
5 tokens and that his duties did not change from when he was a consultant, we note that taxpayer's duties
6 under the consulting agreement included preparation of annual budgets and strategic plans,
7 participation in company management, and assisting in the operation of the company as required. We
8 find that, even if taxpayer's duties did not change from when he was hired as a consultant, those duties
9 were very broad and could be viewed as including supervision of Sable's sales and use tax compliance.
10 While it is undisputed that taxpayer lived in Texas, taxpayer has stated that he had regular contact with
11 company management and the board. Thus, the fact that taxpayer resided in Texas did not prevent him
12 from having continual involvement in the overall management of either ST or Sable.

13 Taxpayer's primary contention is that the board of directors had sole authority relating to sales
14 and use tax compliance and he was only a conduit who passed information to the board. However,
15 taxpayer has submitted copies of "Officer's Certificates" in which taxpayer, in his capacity as CEO,
16 certified that Sable was in arrears on certain tax returns, including sales tax. The Officer's Certificates
17 do not seek the board's *authorization* to pay certain taxes. According to the minutes of meetings of the
18 board of directors signed by taxpayer as chairman of the board, taxpayer advised the board on a wide
19 range of issues. Thus, the minutes do not support taxpayer's contention that all decisions regarding
20 sales and use tax compliance rested with the board of directors. We find that the available evidence
21 shows that taxpayer, as CEO, had the ultimate authority to determine what bills were paid, including
22 sales and use taxes.

23 Thus, we find that taxpayer was a responsible person as defined by section 6829. With respect
24 to taxpayer's assertion that he resigned on April 1, 2001, and that any possible responsibility ended on
25 that date, we note that the announcement from ST stating that taxpayer had resigned as ST's president,
26 CEO, and chairman of the board, was dated May 24, 2001. Also, a press release dated April 12, 2001,
27 an information circular from ST dated May 16, 2001, and a May 18, 2001 announcement from ST each
28 identify taxpayer as president and CEO. We find that the evidence supports a finding that taxpayer

1 resigned all positions with ST and Sable on May 23, 2001, but not before. Accordingly, taxpayer was
2 a responsible person at the time the 1Q01 taxes became due.

3 Willfulness for these purposes means that the failure was the result of an intentional, conscious,
4 and voluntary course of action, even if not done with a bad purpose or evil motive. A person is
5 regarded as having willfully failed to pay taxes, or cause them to be paid, where he or she had
6 knowledge that the taxes were not being paid (or lacked knowledge in reckless disregard of his or her
7 duty to know) and had the authority to pay taxes or cause them to be paid, but failed to do so.

8 Taxpayer contends he did not know that Sable had failed to pay its taxes until October 2000.
9 Although there is no direct evidence that taxpayer had specific knowledge of the tax deficits prior to
10 October 2000, taxpayer received daily reports from Sable's management and provided weekly and
11 monthly reports to the board of directors. We find it highly unlikely, given the management structure
12 and the constant flow of information to and from taxpayer that taxpayer would not have been aware
13 that the 2Q00 and 3Q00 returns were being filed without payment. This is especially true if, as
14 taxpayer contends, all decisions regarding payment of taxes went to the board, since taxpayer was the
15 conduit of that information. Consequently, we find that taxpayer knew that Sable's taxes for 2Q00
16 through 1Q01 were not paid timely.

17 Willfulness also requires that the responsible person must have been able to pay, or cause to be
18 paid, the taxes when due. We find for the same reasons noted above that taxpayer had authority to
19 cause the taxes due to be paid. Regarding whether Sable had sufficient funds to pay the taxes due, we
20 note that during the applicable periods, Sable was making substantial sales, as evidenced by its
21 reported gross receipts, and making payments to vendors and suppliers during the period at issue. We
22 find that funds were available to pay the sales tax liability, but Sable's management chose to pay other
23 creditors instead. In summary, we conclude that all conditions have been satisfied for imposing
24 personal liability on taxpayer under section 6829 for the outstanding tax liabilities of Sable.

25 **Issue 2:** Whether adjustments are warranted to the tax liability assessed against Sable for the
26 1Q01. We recommend no adjustment.

27 For the 1Q01, Sable reported \$601,922 in gross sales and \$385,246 in taxable sales. In its audit
28 of Sable for the period July 1, 1998, through March 31, 2001, the Department established an

1 understatement of tax of \$1,054.52 for the audit period. The Department is unable to locate the audit
2 workpapers. Our review of the Board's computerized records indicates that the audit difference
3 represented recorded sales tax liability that was not reported. The only difference for 1Q01 apparently
4 was an understatement of measure of \$1,827 subject to Alameda County Transit Authority taxes.

5 In August 2008, taxpayer submitted an amended return for 1Q01, showing tax due of
6 \$3,248.00. As support, taxpayer provided copies of Sable's monthly sales reports. Taxpayer indicates
7 that the difference relates primarily to sales reported for 1Q01 that did not actually occur until after
8 March 31, 2001. The Department did not accept the amended return because the 1Q01 was included in
9 the audit of Sable, and the audit found liability greater than the amount reported. The D&R
10 recommended a reaudit of Sable's sales for 1Q01. However, taxpayer was unable to provide
11 documentation to show that the amount of taxable sales reported for 1Q01 was overstated.
12 Accordingly, we recommend no adjustment.

13 **Issue 3:** Whether taxpayer has established reasonable cause sufficient for relieving the late-
14 payment and finality penalties originally assessed against Sable. We conclude that he has not.

15 Taxpayer submitted a request for relief, signed under penalty perjury. The grounds stated in
16 the request for relief do not address why *Sable* failed to timely pay the taxes and determination at issue
17 but instead reiterate taxpayer's contention that he should not be held personally liable. Accordingly,
18 taxpayer has not established reasonable cause for Sable's late payments of amounts due reported on
19 returns and its failure to timely pay the determination at issue. Consequently, we find no basis for
20 relief from the penalties.

21 AMNESTY

22 Although Sable incurred amnesty interest penalties of \$1,795.78 for 4Q00 and \$5,130.11 for
23 1Q01 because it did not participate in the amnesty program, those penalties were not included in the
24 determination issued to taxpayer. Thus, the amnesty interest penalties assessed against Sable are not at
25 issue here.

26 OTHER DEVELOPMENTS

27 None.

28 Summary prepared by Rey Obligacion, Retired Annuitant