

CALIFORNIA STATE BOARD OF EQUALIZATION

APPEALS DIVISION SUMMARY FOR BOARD HEARING

In the Matter of the Petition for Redetermination)
 Under the Sales and Use Tax Law of:)
 ERICK FRANCISCO CATALAN) Account Number: SR GH 53-003179
) Case ID 420368
)
 Petitioner) Hayward, Alameda County
)

Type of Liability: Responsible person liability

Liability Period: 2/2/01 – 12/31/02

<u>Item</u>	<u>Disputed Amount</u>		
Responsible person liability	\$70,036		
		<u>Tax</u>	<u>Penalties</u>
As determined, protested		\$82,768.39	\$29,261.62
Adjustments: Sales and Use Tax Department		-2,568.87	-1,151.84
Appeals Division		<u>-29,306.72</u>	<u>-8,966.34</u>
Proposed redetermination		<u>\$50,892.80</u>	<u>\$19,143.44</u>
Proposed tax redetermination		\$50,892.80	
Interest through 10/31/10		41,633.05	
Negligence penalty		3,624.78	
Penalty for failure to file returns		2,423.86	
Penalty for failure to timely pay determination		6,048.64	
Amnesty interest penalty		<u>7,046.16</u>	
Total tax, interest, and penalties		<u>\$111,669.29</u>	
Monthly interest beginning 11/1/10		<u>\$296.87</u>	

Petitioner did not respond to the Notice of Hearing, and the Board Proceedings Division the informed petitioner that this matter would be presented to the Board for decision without oral hearing. Subsequently, petitioner contacted the Board Proceedings Division to request an oral hearing.

UNRESOLVED ISSUES

Issue 1: Whether petitioner is personally liable as a responsible person under Revenue and Taxation Code section 6829 for the unpaid liabilities of Fancy Gold, Inc. (Fancy Gold), seller’s permit SR GH 97-814447, for the period February 2, 2001, through December 31, 2002. We conclude he is.

1 Fancy Gold was a retail and wholesale jewelry store that was incorporated in October 2000 by
2 petitioner and three others: Miguel Chavez, Juan J. Chavez, and Victor Salazar.¹ The articles of
3 incorporation appoint all four to act as initial directors. On February 1, 2001, Mr. Salazar (as president
4 and chief executive officer) and petitioner (as vice-president), signed the application for a seller's
5 permit. Fancy Gold's corporate status was suspended by the Secretary of State on December 23, 2002,
6 and the Franchise Tax Board suspended Fancy Gold on September 1, 2004.

7 Notices of Determination (NOD) were issued to Fancy Gold on September 25, 2002, based on
8 its failure to file returns for the period January 1, 2002, through June 30, 2002, and on August 15,
9 2003, based on an audit for the period February 2, 2001, through December 31, 2002. Fancy Gold did
10 not appeal or pay the NOD's, and thus finality penalties were added to the determinations, and an
11 amnesty interest penalty was added to the audit liability. Subsequently, the Sales and Use Tax
12 Department (Department) concluded petitioner had responsibility for Fancy Gold's sales and use tax
13 matters as a director of Fancy Gold because he signed the application for the seller's permit, an
14 application for credit with Citizen Watch Company, and sales and use tax returns (SUTR's) for the
15 second quarter of 2001 (2Q01), 3Q01, and 4Q01. The Department also found that petitioner spoke
16 with the Board's collection staff on July 7, 2003, indicating his accountant was working on the
17 SUTR's that were then past due for 3Q02 and 4Q02. On July 22, 2003, the accountant faxed unsigned
18 returns for 3Q02 and 4Q02, which the Department indicates contain deductions for sales tax included,
19 which is evidence that sales tax reimbursement was added to the retail sales of tangible personal
20 property.

21 By letter dated September 13, 2005, the Department notified petitioner that he might be held
22 personally responsible for the unpaid liability of Fancy Gold. As a result, petitioner negotiated an
23 installment payment agreement, but only to pay the liability established by the September 25, 2002,
24 NOD. Petitioner and Mr. Salazar made numerous payments that paid the September 25, 2002, NOD in
25 full. Thus, only the final liability of the August 15, 2003 NOD remained unpaid.

27 ¹ The Department found insufficient evidence to issue a dual determination to Juan J. Chavez and Miguel Chavez, but did
28 issue one to Mr. Salazar on September 22, 2006. Mr. Salazar did not file a petition for redetermination, and thus, his
liability is final.

1 The Department issued a NOD to petitioner for the unpaid liability of Fancy Gold because it
2 concluded that each of the four conditions for imposing section 6829 liability on petitioner were
3 satisfied: Fancy Gold's business was terminated on December 31, 2002; sales tax reimbursement was
4 collected on retail sales of tangible personal property; petitioner was responsible for Fancy Gold's
5 compliance with the Sales and Use Tax Law; and petitioner willfully failed to pay or cause to be paid
6 taxes due from Fancy Gold.

7 Petitioner agrees that Fancy Gold's business was terminated. However, petitioner contends that
8 Fancy Gold did not collect sales tax reimbursement on its retail sales of jewelry, and instead absorbed
9 the sales tax burden by backing the tax due out of the selling price on retail sales, which it then
10 reported on its SUTR's. Petitioner also argues that he was not a responsible person with respect to
11 3Q02 and 4Q02 because he was not associated with Fancy Gold, and had no control or supervision of,
12 or responsibility for, its sales and use tax matters when taxes became due for those periods. Finally,
13 petitioner contends that he did not willfully fail to pay taxes because he was not aware of the liability
14 until after the Department billed the audit liability on August 15, 2003.

15 We reject petitioner's argument with respect to sales tax reimbursement. According to the
16 audit comments, some invoices in customer files showed retail sales with sales tax added to or
17 included in the price. Petitioner's assertion that Fancy Gold "backed out" the tax is entirely consistent
18 with this conclusion because it would not have been entitled to reduce its gross receipts by the amount
19 of tax included in the selling price before calculating the tax due (that is, "backing out" the tax) unless
20 it had actually included an amount as sales tax in the selling price to the purchaser (Cal. Code Regs.,
21 tit. 18, § 1700). As stated by petitioner, Fancy Gold did claim deductions for sales tax included on its
22 SUTR's, which we find shows that it did include or add sales tax reimbursement on its retail sales.

23 Petitioner did not have specific arguments or evidence to counter the Department's findings
24 that he was responsible for Fancy Gold's sales and use tax compliance other than his claim that he was
25 not employed by Fancy Gold during the time that the 3Q02 and 4Q02 returns were due and thereafter.
26 Petitioner was Fancy Gold's incorporator, he was the vice president who was responsible for sales and
27 use tax matters when he signed the application for Fancy Gold's seller's permit, he paid Fancy Gold's
28 assessments when it did not file SUTR's for 1Q02 and 2Q02, and he directed his accountant to file

1 Fancy Gold's (unsigned) returns for 3Q02 and 4Q02. Based on the evidence, we find that petitioner
2 was responsible for Fancy Gold's sales and use tax compliance during the relevant periods.

3 With respect to willfulness, personal liability can be imposed on a responsible person only if
4 that person willfully failed to pay or to cause to be paid taxes due from Fancy Gold, which means that
5 the failure was the result of an intentional, conscious, and voluntary course of action but does not mean
6 that the failure had to have been done with a bad purpose or evil motive. A person is regarded as
7 having willfully failed to pay taxes, or cause them to be paid, where he or she had knowledge that the
8 taxes were not being paid (or lacked knowledge in reckless disregard of his or her duty to know) and
9 had the authority to pay taxes or cause them to be paid, but failed to do so.

10 Petitioner prepared and signed Fancy Gold's tax returns in 2001, which shows he had access to
11 sales and use tax information and understood his responsibility to report to the Board. We have no
12 evidence that petitioner's duties changed in 2002, other than petitioner's statement, which we conclude
13 conflicts with the fact that he and Mr. Salazar paid the assessment for the unreported liability for the
14 1Q02 and 2Q02. His statement also conflicts with his continuing control as evidenced by the
15 accountant's filing of the unsigned 3Q02 and 4Q02 returns at petitioner's direction. Thus, we
16 conclude he knew that taxes were due for each of the four quarters of 2002 and he failed to pay them.

17 Additionally, evidence shows that, despite his knowledge that taxes were due, petitioner
18 allowed or caused Fancy Gold to pay ongoing expenses, including payments to suppliers, rather than
19 paying or causing to be paid the taxes due. Accordingly, we find that petitioner willfully failed to pay
20 the liability to the Board, which satisfies the final requirement for personal liability.

21 **Issue 2:** Whether Fancy Gold was negligent. We conclude that it was.

22 Petitioner did not offer any arguments or evidence on the question of negligence. We find that
23 the penalty for negligence was properly applied in this case because Fancy Gold provided few records
24 to the Department with respect to the audit for 2001 and provided only a single bank statement for
25 2002. Such lack of adequate records constitutes negligence in record keeping. (Cal. Code Regs., tit.
26 18, § 1698, subd. (b).) Additionally, the rate of understatement of reported taxable sales during the
27 audit period after the reaudit performed to make the adjustments we recommended was 510 percent
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1 (\$1,200,881 understatement ÷ \$235,493 reported). Such large error rate and lack of adequate records
2 establish that the Department correctly imposed the negligence penalty.

3 **Issue 3:** Whether petitioner has established reasonable cause to relieve the failure-to-file
4 penalty, the penalty for failure to timely pay the determination (finality penalty), and amnesty interest
5 penalty, assessed against Fancy Gold, which were also included in the determination issued to
6 petitioner under section 6829. We conclude that he has not.

7 Petitioner filed a request for relief of the failure-to-file penalty asserting that he was not
8 employed by Fancy Gold at the time the returns were due for 3Q02 and 4Q02. As explained above, we
9 reject that explanation in connection with the issue for which it is relevant (that is, whether petitioner is
10 liable under section 6829). This allegation is not relevant to the issue here, which is whether Fancy
11 Gold had a reasonable basis for failing to file a return. We find that petitioner has not provided a
12 reasonable basis for *Fancy Gold's* failure to file returns, and that relief of the penalty is not warranted.

13 With respect to the finality penalty, petitioner argues that Mr. Salazar had all the records,
14 petitioner was already separated from the company when the liability was assessed, and he had no
15 knowledge of the deficiency and no authority or ability to timely appeal or pay the liability. Again,
16 petitioner has not provided a reasonable explanation for *Fancy Gold's* failure to timely pay the
17 determination, which resulted in imposition of the penalty. Accordingly, we recommend that relief of
18 the finality penalty be denied.

19 With respect to the amnesty interest penalty, petitioner argues that relief should be granted
20 because Fancy Gold ceased to exist years before the amnesty program began. He also asserts that the
21 audit covered the entire time that Fancy Gold conducted its business, and the audit work papers should
22 function as amnesty returns. He also argues that he personally filed for amnesty on February 18, 2005,
23 and that he therefore should not be subject to the penalty.

24 Relief from the amnesty interest penalty would be appropriate if Fancy Gold ceased to exist
25 before the amnesty program, and no person or entity continued to act on its behalf with the authority
26 and funds to participate in the amnesty program. However, the evidence shows that, even though
27 Fancy Gold's business ceased before the amnesty program, it filed a timely application for amnesty;
28 thus, Fancy Gold continued to exist and was capable of at least applying for amnesty. Additionally,

1 Fancy Gold or persons acting on its behalf paid the NOD issued on September 25, 2002 (based on the
2 compliance assessment) *after* the amnesty interest penalty was assessed on June 30, 2005, which
3 shows that there were funds available to participate in the amnesty program. However, Fancy Gold did
4 not either pay the amnesty-eligible tax or enter into a qualified installment agreement. As a result, the
5 penalty was imposed. We find that petitioner has not established a reasonable basis for Fancy Gold's
6 failure to complete the requirements of the amnesty program, and thus recommend that relief of the
7 penalty be denied.

8 **OTHER DEVELOPMENTS**

9 None.

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11 Summary prepared by Rey Obligacion, Retired Annuitant
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