

## 1 CALIFORNIA STATE BOARD OF EQUALIZATION

## 2 APPEALS DIVISION BOARD HEARING SUMMARY

3 In the Matter of the Administrative Protest )  
 4 Under the Sales and Use Tax Law of: )  
 5 GORDON W. KELLEY ) Account Number SR AC 53-004070  
 6 Taxpayer ) Case ID 475764  
 )  
 ) Stuart, Florida

7 Type of Liability: Responsible person liability

8 Liability period: 07/01/00 – 06/30/03<sup>1</sup>9 Item Disputed Amount

10 Responsible person liability \$376,665

11 TaxPenalty12 As determined \$354,192.86 \$85,988.6013 Post-D&R adjustment - 35,419.2914 Adjusted liability \$354,192.86 \$50,569.3115 Less payments by others - 28,097.0016 Balance, protested \$326,095.86 \$50,569.31

17 Tax, as determined \$354,192.86

18 Interest through 10/31/12 349,567.36

19 Negligence penalty 50,569.3120 Total tax, interest, and penalty \$754,329.5321 Payments - 35,940.0022 Balance Due \$718,389.5323 Monthly interest beginning 11/01/12 \$ 1,591.2624 **UNRESOLVED ISSUES**

25 **Issue 1:** Whether taxpayer is personally liable as a responsible person for the unpaid liabilities  
 26 of Southland Fireplaces, Inc. pursuant to Revenue and Taxation Code section 6829. We conclude  
 27 taxpayer is personally liable.

28 Southland Fireplaces, Inc. (Southland) (SR AC 97-525550) operated as a construction  
 contractor furnishing and installing garage doors and fireplace units from July 1999 through September

<sup>1</sup> Although a portion of this period was covered by the Board's Tax Amnesty Program, no amnesty interest penalty was imposed against Southland Fireplaces, Inc. because it filed a timely amnesty application and entered into a qualifying installment payment agreement.

1 2005. At the time its business terminated, Southland had unpaid liabilities related to an audit. During  
2 the audit period, Southland billed its contracts on a lump sum basis, purchased materials without  
3 payment of tax by providing resale certificates to vendors, and reported no tax liability. The Sales and  
4 Use Tax Department (Department) concluded that taxpayer was personally liable for Southland's sales  
5 and use tax debts pursuant to section 6829.<sup>2</sup>

6 Taxpayer concedes that Southland ceased business operations on September 30, 2005, and that  
7 he was a person responsible for Southland's sales and use tax compliance. Taxpayer asserts, however,  
8 that the two remaining conditions for imposing personal liability on him have not been satisfied, that  
9 Southland collected sales tax reimbursement with respect to retail sales and that the failure to pay the  
10 taxes was willful. Regarding sales tax reimbursement, taxpayer misunderstands this requirement.  
11 While it is true that personal liability under section 6829 can be imposed with respect to *sales tax*  
12 liability only to the extent that the corporation had collected sales tax reimbursement, this element is  
13 also satisfied where the applicable tax is use tax owed on the primary taxpayer's consumption of  
14 tangible personal property. Here, Southland was the consumer of materials it used in the completion of  
15 lump sum construction contracts, but failed to report and pay that use tax. Since that use tax is the tax  
16 at issue here, we conclude that this element of section 6829 liability has been satisfied.

17 With respect to willfulness, taxpayer contends that his failure to pay Southland's tax was not  
18 willful because he relied on the advice of Norman Keef, whom taxpayer believed to be a Certified  
19 Public Accountant (CPA) and who stated that no sales or use taxes were required to be paid in light of  
20 the nature of Southland's business. In support, taxpayer has provided a declaration describing such  
21 reliance, as well as a business card and other evidence that indicate Mr. Keef led taxpayer to believe he  
22 was a CPA. Also, taxpayer cites various court cases which hold that reliance on the advice of tax  
23 professionals negates the willfulness element under Internal Revenue Code section 6672.

24 The willfulness requirement for imposing liability under section 6829 is satisfied where the  
25 failure to pay or to cause to be paid the taxes due was the result of an intentional, conscious, and  
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27 <sup>2</sup> The Department also found that Terry Eaves and Greg Keeton were personally liable as responsible persons pursuant to  
28 section 6829. Terry Eaves has filed an administrative protest (case ID 475767), which is scheduled for Board hearing on  
the same calendar as this matter. Mr. Keeton has not protested the determination issued to him.

1 voluntary course of action (even if without a bad purpose or evil motive). A person is regarded as  
2 having willfully failed to pay taxes or to cause them to be paid where he or she had knowledge that the  
3 taxes were not being paid and had the authority and ability to pay the taxes or to cause them to be paid,  
4 but failed to do so.

5 When Southland applied for its seller's permit signed by taxpayer as manager, the Department  
6 provided Southland copies of several regulations and Board publications, including California Code of  
7 Regulations, title 18, section 1521 and Board Publication 9, "Tax Tips for Construction and Building  
8 Contractors." These publications clearly explain that construction contractors billing on a lump sum  
9 basis, such as Southland, are consumers of materials and owe use tax on cost if not paying tax or tax  
10 reimbursement to their vendors, as here. Taxpayer signed the seller's permit application, and we  
11 assume that taxpayer read the publications provided. We note in this regard that taxpayer did not  
12 attend the appeals conference, so we were unable to judge his credibility. We note also that taxpayer  
13 had been vice-president of Advanced Fireplaces, a construction contractor furnishing and installing  
14 prefabricated fireplaces from August 1983 through March 1992 (during an audit, the Department found  
15 that Advanced Fireplaces included the cost of materials in its reported taxable measure). We find that,  
16 based on the evidence presented, taxpayer was aware that Southland incurred use tax liability when it  
17 consumed materials it purchased for resale to perform construction contracts. Taxpayer's citations to  
18 cases interpreting federal law are not relevant here.

19 There is ample evidence that taxpayer had authority to cause the taxes due to be paid, and he  
20 does not dispute that finding. Regarding whether Southland had sufficient funds to pay the taxes due,  
21 we note that during the applicable periods, Southland was making substantial sales, as evidenced by its  
22 reported gross receipts, and it paid wages totaling \$3,352,855 during the years 2001 through 2005. We  
23 find Southland had funds available to pay its tax liability, but its management chose to pay other  
24 creditors instead. In summary, we conclude that all conditions have been satisfied for imposing  
25 personal liability on taxpayer under section 6829 for the outstanding tax liabilities of Southland.

26 **Issue 2:** Whether Southland was negligent. We conclude that it was.

27 The Department imposed the negligence penalty in the audit of Southland because the audit  
28 disclosed a taxable measure of \$6,181,239, and Southland had paid no tax liability for the audit period.

1 Taxpayer disputes the penalty on the basis that Southland's failure to report tax was the result of  
2 reliance on erroneous advice received from Mr. Keef.

3 We find that Southland's failure to report any of the tax it owed, measured by over \$6 million,  
4 is a particularly egregious understatement, which cannot be obviated by the alleged reliance on  
5 Mr. Keef's advice. We note also our finding that taxpayer did actually know that use tax had been  
6 incurred, but not paid. We find that there is ample evidence of negligence and that the penalty was  
7 properly applied.

8 **RESOLVED ISSUE**

9 Since Southland did not timely pay the determination or file a petition for redetermination, a  
10 finality penalty of \$35,491.29 was applied, which was included in the determinations issued to  
11 taxpayer. Taxpayer has filed a request for relief of the finality penalty. We find that Southland's  
12 failure to timely pay the determination was the result of reasonable cause because, by the time the  
13 determination became final, Southland had filed bankruptcy, no longer had control over its assets, and  
14 thus lacked the ability to pay the liability. Accordingly, we recommend relief of the finality penalty if  
15 the remaining tax liability is paid in full within 30 days of the mailing of the notice of final decision in  
16 this appeal.

17 **OTHER MATTERS**

18 None.

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