

**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: )  
 )  
 ) Account Number: SR AP 53-001918  
 ELIZABETH WARDLEY KWONG ) Case ID 316054  
 )  
 RAYMOND WAH KWONG ) Account Number: SR AP 53-001917  
 ) Case ID 316055  
 )  
 Petitioners ) Altadena, Los Angeles County

Type of Liability: Responsible Person Liability

Audit Period: 1/1/00 – 3/28/01

<u>Item</u>	<u>Amount in Dispute</u>	<u>Tax</u>	<u>Penalties</u>
Determined responsible person liability	\$101,371 <sup>1</sup>		
Alleged allowable bad debt deduction	\$ 84,708		
As determined		\$99,166.00	\$35,621.96
Adjustment - Sales and Use Tax Department		- 10,011.00	- 3,766.62
- Appeals Division		<u>00.00</u>	<u>- 19,639.84</u>
Proposed redetermination, protested		<u>\$89,155.00</u>	<u>\$12,215.50</u>
Proposed tax redetermination		\$ 89,155.00	
Interest to 2/28/10		80,463.97	
Penalties		<u>12,215.50</u>	
Total tax, interest, and penalties		<u>\$181,834.47</u>	
Monthly interest beginning 3/1/10		<u>\$520.07</u>	

At the appeals conference, petitioners stated that they no longer contest their liability as responsible persons for the liability of The Permanent Wiseguys, Inc. (Wiseguys) (SR AP 17-806560), and thus, in our Decision and Recommendation (D&R), we recommended that the matter be redetermined without adjustment. After we issued our D&R, petitioners filed a settlement proposal, but the settlement negotiations were not successful. Petitioners thereafter requested a Board hearing,

<sup>1</sup> Consisting of tax of \$89,155.00 and penalties of \$12,215.50 for late payment of taxes reported on the quarterly returns for the year 2000 (interest continues to accrue).

1 and that hearing was scheduled for October 2, 2007. However, since our D&R did not identify any  
2 remaining disputes, the original hearing date was postponed so that we could contact petitioners to  
3 determine the issues that remained for decision by the Board. After petitioners identified those  
4 remaining issues, we issued a Supplemental D&R to address them.

### 5 UNRESOLVED ISSUES

6 **Issue 1:** Whether petitioners' liability as responsible persons has been discharged as a result of  
7 the bankruptcy of Wiseguys or as a result of petitioners' personal bankruptcy. We conclude that the  
8 liabilities have not been discharged.

9 There is no dispute that petitioners are personally liable under Revenue and Taxation Code  
10 section 6829 for the portion of the unpaid liabilities of Wiseguys that the Department continues to  
11 assert they owe (see discussion under "Resolves Issues"). Wiseguys filed for Chapter 11 bankruptcy  
12 on September 15, 2000 (Case No. LA 00-36186-VZ). On April 2, 2001, the case was converted to a  
13 Chapter 7 bankruptcy, and it was closed on September 22, 2004. Petitioners filed for Chapter 7  
14 bankruptcy on March 22, 2002 (Case No. LA 02-18641-VZ), and were granted a discharge on  
15 September 9, 2002.

16 Taxes are generally not dischargeable in bankruptcy. (11 U.S.C. §§ 523(a)(1)(A), 507(a)(8).)  
17 Section 523(a)(1)(A) of title 11 of the U.S. Code provides that taxes "of the kind and for the periods"  
18 specified in section 507(a)(8) of the U.S. Bankruptcy Code are non-dischargeable in bankruptcy. (See  
19 also 11 U.S.C. § 727(b).) A bankruptcy court discharge does not discharge taxes measured by gross  
20 receipts, such as the sales tax at issue here, that are not assessed before the bankruptcy petition is filed  
21 but remain assessable thereafter. (11 U.S.C. § 523(a)(1)(A), 507(a)(8)(A) (iii), see also *George v.*  
22 *California State Bd. of Equalization* (9<sup>th</sup> Cir. BAP 1989) 95 B.R. 718, 721 (holding that responsible  
23 person liability is a tax for determining dischargeability in bankruptcy).)

24 Petitioners assert that the Board was listed as a creditor in these bankruptcy cases but did not  
25 file any claims. Ms. Kwong also asserts, "Our bankruptcy attorney and Trustee advised us that both  
26 cases have been released, the court approved the Trustees [sic] request for final payment to creditors  
27 and these have all been made. We met all the requirements of our bankruptcies and we are no longer  
28 under any monetary obligation."

1           The Sales and Use Tax Department (Department) states that, contrary to petitioners' assertion,  
2 it filed a claim in the bankruptcy of Wiseguys on July 25, 2001, which was prior to the claims deadline  
3 of August 21, 2001.<sup>2</sup> The Department states that the Board did not receive any payment on its claim in  
4 the bankruptcy of Wiseguys. As for petitioners, the Department notes that it issued the Notices of  
5 Determination to petitioners for responsible person liability on June 9, 2005, more than two years after  
6 they filed for bankruptcy. Therefore, the Department contends that the liabilities were not discharged  
7 in bankruptcy because the liabilities of petitioners as responsible persons were assessed after their  
8 bankruptcy case closed and therefore their personal liabilities were not discharged in bankruptcy.

9           We agree. Petitioners filed their personal petition for bankruptcy in 2002, and the Department  
10 did not issue the Notices of Determination to petitioners at issue here until over three years later in  
11 2005. Since those determinations were timely, the determined liabilities remained assessable after the  
12 filing of the personal bankruptcy. (In fact, a tax is assessed for purposes of bankruptcy law when the  
13 determination becomes final, so the disputed liability has still not been "assessed" for bankruptcy  
14 purposes, but remains assessable.) Thus, the personal liability of petitioners for Wiseguys' unpaid  
15 liabilities to the Board was not discharged in their bankruptcy proceeding.

16           **Issue 2:** Whether petitioners have established that any adjustments are warranted to the  
17 underlying liability of Wiseguys due to bad debts. We recommend no adjustments.

18           Petitioners submitted two charts that purportedly show the bad debts deduction that Wiseguys  
19 was entitled to claim. After conversations with Mrs. Kwong and review of the charts, it appears  
20 petitioners seek a bad debt allowance of \$84,708.15.

21           Petitioners have not provided sufficient documentation to establish the following critical  
22 elements of an allowable bad debt deduction: (1) the date of the original sale; (2) the name and address  
23 of the purchaser; (3) the amount the purchaser contracted to pay; (4) the amount on which Wiseguys  
24 paid tax; (5) the jurisdiction(s) where the local taxes and, as applicable, district taxes were allocated;  
25 (6) all payments or other credits applied to the purchaser's account; (7) evidence that the uncollectible  
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27 <sup>2</sup> The Department also states that corporations are not eligible to receive a discharge in a Chapter 7 proceeding pursuant to  
28 11 U.S.C. section 727 (a).

1 portion of the gross receipts on which tax was paid actually has been legally charged off as a bad debt  
2 for income tax purposes in accordance with generally accepted accounting principles; and (8) the  
3 taxable percentage of the amount charged off as a bad debt properly allocable to the amount on which  
4 Wiseguys reported and paid tax. (Cal. Code Regs., tit. 18, 1642, subd. (e).)

5 Accordingly, absent such documentation, we conclude that petitioners have failed to establish  
6 that any adjustment to the underlying liability of Wiseguys is warranted for bad debts. Thus, we  
7 recommend that the responsible person liabilities be redetermined without adjustment.

### 8 **RESOLVED ISSUES**

9 By memorandum dated February 16, 2010, the Department has advised the Appeals Division  
10 that, upon further review of the facts in this case, it has concluded that petitioners did not willfully fail  
11 to pay the tax due for the first quarter 2001. The return for that period was due on April 30, 2001, at  
12 which time Wiseguys was in bankruptcy. The Department has concluded that on the due date of the  
13 tax for the first quarter 2001, the bankruptcy trustee had total control over the assets of Wiseguys and  
14 petitioners did not willfully fail to pay the tax due for that quarter. Accordingly, the Department  
15 recommends that the amounts owed by Wiseguys for the first quarter 2001 (tax of \$10,011, penalties  
16 of \$3,766,62, and applicable interest) be removed from the liability owed by petitioners.

17 An amnesty interest penalty was imposed on Wiseguys because of its failure to participate in  
18 the amnesty program, and those penalties were included in the determinations issued to petitioners.  
19 We had not explained to petitioners that they could request relief of that penalty on Wiseguys' behalf,  
20 nor had we considered whether relief would be warranted. After this omission was brought to our  
21 attention, we considered the circumstances and have concluded that relief of the amnesty penalty  
22 would be warranted, if a proper request were submitted, because Wiseguys had a reasonable basis for  
23 not participating in the amnesty program (that is, Wiseguys was closed out with its remaining assets  
24 distributed well before the amnesty program). The Department agrees, and contacted petitioners to  
25 obtain a request for relief signed under penalty of perjury. Ms. Kwong advised that she would submit  
26 such a request. As of the writing of this revised summary, we have not yet received the request.  
27 Conditioned on receiving a request for relief of the amnesty interest penalty, signed under penalty of  
28 perjury, we recommend that the amnesty interest penalty of \$19,639.84 be relieved if petitioners pay

1 the tax and interest they owe within 30 days of the Notice of Redetermination or if, within 30 days of  
2 the Notice of Redetermination, petitioners enter into an installment payment plan to pay that tax and  
3 interest within 13 months and they successfully complete that agreement.

4 **OTHER DEVELOPMENTS**

5 None.

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8 Summary prepared by Rey Obligacion, Business Taxes Specialist III, Retired  
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