STATE BOARD OF EQUALIZATION
SALES AND USE TAX APPEAL

# CALIFORNIA STATE BOARD OF EQUALIZATION

## APPEALS DIVISION SUMMARY FOR BOARD HEARING

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| In the Matter of the Petition for Redetermination Under the Sales and Use Tax Law of: | ) | |
| JAMES FISHMAN | ) | Account Number: SR CH 53-002472 |
| | ) | Case ID 355538 |
| Petitioner | ) | Pleasanton, Alameda County |

Type of Liability: Responsible person liability

Liability Period: 01/01/96 – 12/31/98

| Item | Amount |
|---|---|
| Responsible person liability | $9,183 |

| | Tax | Penalty |
|---|---|---|
| As determined | $55,268.52 | $5,636.49 |
| Adjustment: Sales and Use Tax Department | -47,019.88 | -4,701.99 |
| Proposed redetermination, protested | $8,248.64 | $ 934.50[1] |

| | |
|---|---|
| Proposed tax redetermination | $8,248.64 |
| Interest through 11/30/09 | 9,448.42 |
| Finality penalty | 934.50 |
| Total tax, interest, and penalty | $18,631.56 |
| Monthly interest beginning 12/1/09 | $54.99 |

This matter was scheduled for Board hearing on April 15, 2009, but was postponed so that the Sales and Use Tax Department (Department) could assess the amnesty interest penalty it had not previously assessed to the corporation because of the Department's policy of not billing an amnesty interest penalty during the time a taxpayer has a pending bankruptcy (here, the corporation). However, upon further consideration, the Department decided not to bill the amnesty interest penalty.

[1] This penalty was imposed on the corporation for its failure to timely petition or pay the determination issued to it based on 10 percent of the tax liability determined against the corporation (i.e., the tax remaining due when that determination became final). After that time, but before the determination was issued to petitioner, payments were made that were applied to the corporation's tax liability.

## UNRESOLVED ISSUES

**Issue 1:** Whether petitioner is personally liable as a responsible person pursuant to Revenue and Taxation Code section 6829 for a portion of the unpaid liabilities of Unmanned Solutions, Inc. (USI), seller's permit SR CH 26-736854, for the period January 1, 1996, through December 31, 1998. We find that petitioner is a responsible person for a portion of USI's unpaid liabilities.

USI, a California corporation, built custom equipment for processing hard disks and other semi-conductor equipment. USI held a seller's permit from June 1, 1982, through April 30, 2001, the date USI closed its business operation. A Notice of Determination (NOD) was issued to USI on August 19, 1999, as a result of an audit for the period January 1, 1996, through December 31, 1998, asserting tax of $78,476.90, plus applicable interest, and a negligence penalty of $7,847.71. The determination became final on September 19, 1999, when USI failed to petition or fully pay the determination within 30 days of issuance of the NOD. After the NOD became final, a finality penalty of $7,842.46 was added to USI's liability. USI filed a late petition which the Department accepted as an administrative protest. The Department subsequently conducted a reaudit which reduced USI's liability to tax of $56,419.18, interest, and finality penalty of $5,636.49. The Department also removed the negligence penalty. USI had made a previous payment prior to the issuance to it of the NOD and made subsequent payments totaling $1,150.36. At the time that USI closed its business, it had unpaid liabilities consisting of tax of $55,268.82, interest, and finality penalty of $5,636.49.

The Department considered petitioner a responsible person pursuant to section 6829 and on May 12, 2006, issued a NOD to petitioner for the unpaid liabilities of USI, which petitioner timely petitioned. On September 26, 2006, the Department determined that petitioner could not be held personally responsible for USI's tax liability resulting from disallowed claimed sales for resale because USI did not charge sales tax reimbursement on such resales. Therefore, the Department reduced petitioner's personal tax liability from $55,268.82 to $8,248.64, and reduced the finality penalty to $934.50 to reflect the reduction in tax.

Petitioner does not dispute that USI's business has been terminated, which is one requirement for imposing section 6829 liability. With respect to the requirement for section 6829 liability that USI included or added sales tax reimbursement on its sales of tangible personal property in California, or

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consumed tangible personal property in California and did not pay the use tax, the Department indicated that petitioner was only held personally responsible for the portion of USI's audit liability relating to unreported use tax on purchases from out-of-state vendors, measured by $2,192, and the amount by which recorded taxable sales exceeded reported taxable sales, measured by $123,436.

Petitioner asserts that USI recorded a sale to Seagate Technology and accrued sales tax in its sales tax accrual account where the equipment to be sold was intended for Seagate's use in Singapore, but Seagate did not accept the equipment, did not cancel the order, and delayed the shipment. Petitioner argues that similar scenarios were repeated with several customers. He argues that no sale was consummated, so no bad debt occurred; instead, recording the sale and accruing the tax liability was an accounting error. In the case of Seagate, petitioner asserts that the equipment sat on USI's shelves for years after the time that USI accrued the sales and tax. Petitioner asserted that the bankruptcy trustee has all of the documentation supporting these accounting errors, and petitioner is unable to obtain the documents.

Without adequate documentation establishing that the recorded sales were never consummated, we believe that the evidence that tax was accrued supports the finding that tax or tax reimbursement was collected, which is consistent with the statement in the Department's audit report that sales tax was added to the retail selling price. Accordingly, we find that USI sold tangible personal property and its customary practice was to collect sales tax reimbursement on its taxable sales (which it did not remit to the Board as sales tax) and USI also purchased tangible personal property without paying sales tax reimbursement or use tax to its vendor or self-report use tax.

Section 6829 liability can be imposed only on a responsible person. Petitioner has submitted no argument or information to support that he was not a responsible person for USI's taxes, but he does assert that Mr. Mark Finkle, another corporate officer, is *also* a responsible person. Petitioner was president and CEO of USI, and as such had a duty to act for the corporation in complying with the Sales and Use Tax Law, and the evidence shows that petitioner actually acted on behalf of USI for sales and use tax matters. Whether Mr. Finkle was *also* a responsible person is irrelevant to petitioner's potential liability (though if more than one person were liable under section 6829 for unpaid taxes, the Board might choose to pursue collection from one of the persons before attempting to

collect against the other if the facts warranted).[2]

The final element required to impose liability under section 6829 is that the responsible person must have willfully failed to pay or to cause to be paid the taxes due from the corporation. This means that the failure must have been the result of an intentional, conscious, and voluntary course of action (Rev. & Tax. Code, § 6829, subd. (d)), but does not require a bad purpose or evil motive. (Cal. Code Regs., tit. 18, § 1702.5, subd. (b)(2).) A person is willful for these purposes if he or she knew that tax was not being properly paid (or lacked knowledge in reckless disregard of his or her duty to know) and had the authority to pay taxes or cause them to be paid, but failed to do so. The determination of willfulness is a finding of fact.

Petitioner contends that he did not act willfully because the proposed plan of reorganization and the disclosure statement USI filed during its bankruptcy clearly indicate that USI intended to pay the sales and use tax that the audit indicated was due and owing. He maintains that only after the U.S. Trustee took over USI's affairs did it fail to pay the alleged tax liability. However, petitioner's bankruptcy contention relates to the time period after the NOD was issued to USI and had become final, which is after the time relevant to petitioner's willfulness or lack thereof. The relevant time for ascertaining whether petitioner willfully failed to pay the tax or cause it to be paid is when the tax became due, that is, when USI filed its quarterly returns.

The evidence shows that USI continued in business, making retail sales and receiving payments for those sales, and paying wages during the relevant period, and it is reasonable to conclude that USI was also paying the other necessary operating expenses of the business during the entire liability period. That is, the evidence shows that USI had the money available to pay the Board when the use tax became due, and when it collected sales tax reimbursement for sales tax due, yet USI used the money to pay other creditors and expenses. Accordingly, we find that petitioner willfully failed to pay, or to cause to be paid, the tax due. Since all requirements for imposing section 6829 liability on

[2] The Department issued an NOD to Mr. Finkle, who paid the assessment and filed a timely claim for refund. We issued a separate D&R in that appeal, and have recommend that the claim be granted because Mr. Finkle was not a responsible person for sales and use taxes, and thus was not liable for the debts of USI. Accordingly, we recommended that the claim be granted, but that recommendation is being held in abeyance pending the Board's decision in the present matter.



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petitioner are satisfied with respect to the liability asserted by the Department, as adjusted, we conclude that petitioner is personally responsible for such liability.

**Issue 2:** Whether petitioner has established that USI should be granted relief from the finality penalty that has been passed through to petitioner as a responsible person. We conclude that petitioner has failed to establish that relief is warranted.

There is no statutory or regulatory authority for relieving this penalty in section 6829 determinations, but if petitioner could show that the penalty should be relieved as to the corporation under Revenue and Taxation Code section 6592, the relief would also inure to petitioner's benefit. On November 21, 2008, petitioner submitted the required declaration signed under penalty of perjury in which he claims that USI should have filed amended returns to reduce the reported sales which were accrued but not consummated. Petitioner also contends that after the returns were filed it became apparent that certain customers were not going to pay for machinery USI shipped because the customers had become insolvent. Also, according to petitioner, USI entered bankruptcy proceedings and a federal trustee controlled USI's payments and the trustee never amended returns or otherwise paid the tax due.

We conclude that petitioner's arguments relating to the actions of the bankruptcy trustee are not relevant to USI's failure to pay the final liability or file a timely petition on or before September 19, 1999, because USI filed its bankruptcy petition on November 17, 1999, which is after USI's NOD became final. With respect to petitioner's argument that USI should have filed amended returns, we note that upon receiving an NOD, a reasonable and prudent business in circumstances similar to that of USI, which received an NOD while believing it actually had overpaid its sales taxes, would have filed a timely petition for redetermination or paid the tax and filed a claim for refund. A reasonable business would not simply have ignored the NOD under such circumstance, which is what USI did. We conclude that petitioner failed to establish a basis for relief to the penalty.

**Issue 3:** Whether the NOD was timely issued to petitioner. We find that he NOD was timely.

As relevant here, section 6487, subdivision (a), provides that, except for certain circumstances such as fraud, every notice of a deficiency determination must be mailed within three years after the last day of the calendar month following the quarterly period for which the amount is proposed to be

determined, except that the period is extended to eight years where the person against whom the determination is issued did not file a sales and use tax return.[3]

A person liable for the tax debts of a corporation under section 6829 is a separate person from the corporation (Rev. & Tax. Code, § 6005), and the responsible person's liability under section 6829 is a separate liability from that of the corporation, although derivative. Liability attaches under section 6829 upon the termination of the selling business of the corporation, and payment is due from a person liable under section 6829 by the end of the month following the quarter during which the selling business of the corporation terminates. Thus, for these purposes, a return filed by the corporation is *not* equivalent to a return having been filed by the responsible person in his or her own name. A person liable under section 6829 is regarded as having filed a return covering his or her liability under section 6829, such that the three-year limitations period is applicable, only if the person filed a return in his or her own name, such as a return filed under a seller's permit he or she held as a sole proprietor, for the period during which the selling business of the corporation terminates. (Memorandum Opinion in *Hosmer Chandler McKoon* (5/31/07).)

Here, there is no evidence that petitioner filed sales and use tax returns in his name, and therefore the eight-year statute applies. (Rev. & Tax. Code, § 6487, subd. (a).) Accordingly, since USI's business operations ceased on April 30, 2001, and the NOD was issued on May 12, 2006, the NOD was timely issued well within the eight-year statute, which began to run on April 30, 2001.

**AMNESTY**

USI had a final liability at the time of the amnesty program. Although USI did not participate in the amnesty program, at the end of the amnesty period, USI was in bankruptcy, and thus the amnesty interest penalty was not applied at that time. The NOD issued to petitioner as a responsible person for USI's tax liability was issued on May 12, 2006, at which time the amnesty interest penalty had still not been imposed on USI. Later, on October 18, 2006, after USI's bankruptcy proceeding was

[3] Section 6829 has been amended, effective January 1, 2009, to provide a different statute of limitations than as discussed here. Since the NOD at issue here was issued prior to January 1, 2009, the new rule effective January 1, 2009, is inapplicable.



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over, an amnesty interest penalty of $18,883.14 was imposed on USI.[4] The Department requested a postponement of the Board hearing so that it could assess the amnesty interest penalty. Subsequently, the Department decided not to impose the amnesty interest penalty because too much time has elapsed since this matter was originally determined and it was the Department's own oversight that caused the amnesty interest penalty not to be billed in the first place.

**OTHER DEVELOPMENTS**

None.

Summary prepared by Rey Obligacion, Business Taxes Specialist III

[4] The $18,883.14 penalty relates to the tax of $55,268.82 owed by USI. Since the Department has reduced the liability asserted to petitioner by over 85 percent (from tax of $55,268.82 to tax of $8,248.64) for the disallowed claimed resales for which no tax reimbursement was collected, the portion of the amnesty interest penalty related to the liability asserted to petitioner would be correspondingly reduced, to about $2,467.



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