

1 CALIFORNIA STATE BOARD OF EQUALIZATION

2 APPEALS DIVISION SUMMARY FOR BOARD HEARING

3 In the Matter of the Petition for Redetermination)
4 Under the Sales and Use Tax Law of:)
5 MICHAEL D. MIDGETT, SR.) Account Number: SR KH 53-001847
6) Case ID 314453
7)
8) Placerville, El Dorado County

7 Type of Liability: Responsible person liability

8 Liability Period: 4/1/02 – 3/31/03

9	<u>Items</u>	<u>Disputed Amounts</u>
10	Responsible person liability	\$64,536 ¹
11	Tax and penalties assessed for 1Q03	\$40,175 ² (included in amount above)

12		<u>Tax</u>	<u>Penalties</u>
13	As determined and protested:	<u>\$51,314.00</u>	<u>\$13,222.31</u>
14	Proposed redetermination	\$51,314.00	
15	Interest to 2/28/09	28,945.61	
16	Penalties for late payment of returns	3,783.50	
17	Penalty for late filing of return	805.00	
18	Penalties for late prepayments	133.26	
19	Penalty for failing to file return	3,347.90	
20	Penalty for failing to timely pay determination	3,347.90	
21	Amnesty interest penalties	<u>1,804.75</u>	
22	Total tax, interest, and penalties	<u>\$93,481.92</u>	
23	Monthly interest beginning 3/1/09	<u>\$342.09</u>	

21 UNRESOLVED ISSUES

22 **Issue 1:** Whether petitioner is personally liable as a responsible person for the unpaid
23 liabilities of The Sofa Factory, Inc. (The Sofa Factory). We find that petitioner is liable.

25 ¹ Comprised of \$51,314.00 tax, penalties of \$3,783.50 for the late payment of returns, a penalty of \$805.00 for the late
26 filing of a return, penalties of \$133.26 for the late filing of prepayment forms, a penalty of \$3,347.90 for failing to file a
27 return, a penalty of \$3,347.90 for failing to timely pay a determination, and amnesty interest penalties of \$1,804.75.

28 ² Comprised of \$33,479.00 tax, a penalty of \$3,347.90 for failing to file a return, and a penalty of \$3,347.90 for failing to
pay a determination timely. Petitioner has not specified how much of this tax (and associated penalties) he disputes, only
that he believes the liability assessed against the corporation for the period January 1, 2003, through March 31, 2003,
should be reduced.

1 The Sofa Factory (SR KH 97-221773) ceased business operations in April 2003 and its seller's
2 permit was closed out effective June 30, 2003. At the time, The Sofa Factory had unpaid liabilities
3 resulting from returns filed with partial or no remittance for the second quarter of 2002 (2Q02) and
4 4Q02 and a failure to file a return for 1Q03, as well as associated penalties and other penalties incurred
5 during the liability period. The Sales and Use Tax Department (Department) concluded that petitioner
6 was responsible for The Sofa Factory's compliance with the Sales and Use Tax (SUT) Law and is
7 personally liable for its unpaid liabilities for the liability period pursuant to Revenue and Taxation
8 Code section 6829. At the appeals conference, petitioner clarified that he disputes his liability as a
9 responsible person and the Department's assessment against The Sofa Factory for 1Q03, but does not
10 otherwise dispute the corporate liabilities attributable to the partial and nonremittance returns or any of
11 the penalties passed through from The Sofa Factory.

12 Four conditions must be satisfied to uphold this liability, two of which are not disputed: The
13 Sofa Factory must have ceased its selling business; The Sofa Factory must have added or included
14 sales tax reimbursement to its sales of tangible personal property in California; petitioner must have
15 been under a duty to act for The Sofa Factory to comply with the SUT Law; and petitioner must have
16 willfully failed to pay, or to cause to be paid, the taxes due from The Sofa Factory. Petitioner does not
17 dispute that The Sofa Factory has ceased its selling business, and that it added or included sales tax
18 reimbursement in the selling price of tangible personal property.

19 The third requirement is that petitioner must have had a duty to act for The Sofa Factory in
20 complying with the provisions of the SUT Law. Petitioner was the vice president, secretary, and
21 treasurer of The Sofa Factory. As noted in the Supplemental D&R, in which we reconsidered whether
22 petitioner was a responsible person, although the holding of the office of vice president or secretary
23 does not, in and of itself, indicate that a person is responsible for a corporation's financial or tax
24 affairs, we believe that the holding of the position as corporate treasurer does. Corporations Code
25 section 2305 provides that the treasurer of a corporation is deemed to be its chief financial officer
26 (CFO). A corporation's CFO is normally charged with the responsibility for the corporation's
27 financial affairs. We recognize that in close corporations, such as here, the duties assigned to
28 corporate officers may vary but, in lieu of convincing evidence to the contrary, we conclude that

1 petitioner's role as treasurer for The Sofa Factory (its CFO) means that he had a duty to act for The
2 Sofa Factory in its financial affairs, including ensuring compliance with the SUT Law. This finding is
3 consistent with the responses from former employees on questionnaires and evidence showing that
4 petitioner signed checks on The Sofa Factory's behalf. We thus conclude that petitioner came within
5 the broad definition of "responsible person" under section 6829.

6 The final requirement is that petitioner must have willfully failed to pay or cause to be paid
7 taxes due from The Sofa Factory. For purposes of section 6829, willfulness does not imply bad
8 purpose or evil motive. A person is willful for these purposes if he or she knew that tax was not being
9 properly paid and had authority to pay them or cause them to be paid, but did not do so.

10 Here, the Department provided statements by former employees that are consistent with each
11 other, which we conclude are credible evidence of petitioner's involvement in the financial affairs of
12 The Sofa Factory. These statements support our finding that petitioner signed checks, including
13 paychecks, issued by The Sofa Factory and made arrangements with The Sofa Factory's creditors for
14 payment of its debts during periods relevant here. Further, while petitioner claims that the president,
15 not petitioner, ran the day-to-day operations of The Sofa Factory, the evidence shows that petitioner
16 was paid the same amount of wages as The Sofa Factory's president from January 2002 through April
17 2002 and in January 2003, which are the only periods for which we have wage information for
18 petitioner.³ Considering that the evidence otherwise indicates that petitioner was acting in accordance
19 with his position as treasurer and that he was paid the same amount of wages as the corporate president
20 who was allegedly running the day-to-day business operations, we conclude that petitioner did in fact
21 act as treasurer and exercised his authority to issue and sign checks during the relevant periods.

22 Additionally, records from The Sofa Factory's landlord's management company show that The Sofa
23 Factory paid its rent and related fees between April 5, 2002, through March 5, 2003, and records from
24 a supplier shows that The Sofa Factory made numerous payments to that supplier from June 3, 2002,
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27 ³ The Sofa Factory's president was petitioner's son, Michael D. Midgett (SR KH 53-001846), to whom the Department also
28 issued a responsible person determination for the same unpaid liabilities at issue herein and who has filed a separate appeal
(Case ID 314399).

1 through July 30, 2002. Taken together, this documentation indicates that The Sofa Factory had funds
2 available to pay the taxes to the Board as they became due, but chose to pay other creditors instead.

3 The evidence here is not as clear as we would like. For example, during the same general
4 period during when petitioner signed checks to vendors, The Sofa Factory's president signed checks to
5 the IRS and the Board for \$5,000 and \$10,000, respectively. This could be consistent with petitioner's
6 check-signing authority having been limited (e.g., for amounts up to \$1,000, or for payments only to
7 vendors), or that payment of taxes was handled by the president. Also, we note that the president
8 signed The Sofa Factory's 4Q01, 2Q02, 3Q02, and 4Q02 sales and use tax returns, as well as its
9 October 2001, November 2001, and January 2002 prepayment forms. Nevertheless, that petitioner's
10 authority may have been limited is merely a possibility for which petitioner has not provided any
11 supporting documentation. Based on the documentation the Department has provided, we find that it
12 has made its prima facie case that petitioner was a responsible person who willfully failed to pay, or to
13 cause to be paid, the tax liabilities of The Sofa Factory from available corporate funds. Since
14 petitioner has provided no documentation to overcome the Department's case, we find that petitioner is
15 liable for The Sofa Factory's unpaid tax debts pursuant to section 6829.

16 **Issue 2:** Whether petitioner has established that the assessment against The Sofa Factory for
17 1Q03 (and therefore derivatively against petitioner) is overstated. We find that petitioner has not.

18 Since The Sofa Factory failed to file a return for 1Q03 and the Department had no corporate
19 records in its possession, the Department used The Sofa Factory's average daily sales as reported on its
20 sales and use tax returns for 2Q02 through 4Q02 to establish a tax liability of \$33,479 for 1Q03.

21 Petitioner contends that the Department's assessment for 1Q03 was made without any inquiry
22 into The Sofa Factory's records and, without a review of such records, the Department could not have
23 accurately calculated sales or the amount of sales tax reimbursement collected during 1Q03. Also,
24 petitioner contends the Department's use of average daily sales based on 2Q02 through 4Q02 returns
25 resulted in an overstated taxable measure for 1Q03, because The Sofa Factory was going out of
26 business during this quarter and made either minimal or no sales during this time. Following the
27 appeals conference, petitioner submitted various documents but did not provide The Sofa Factory's
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1 actual sales figures for 1Q03 or the amounts of sales tax reimbursement and use tax collected during
2 this time.

3 The Department responded that, although these various documents are relevant to 1Q03, they
4 are not sufficient to accurately determine if the assessment is overstated. The Department asserts that
5 it cannot determine if the bank closing statements reflect all monies collected and disbursed during
6 1Q03, and which bank deposits are attributable to sales and use tax. The Department also contends
7 that it cannot determine whether the documents submitted are all of the records that list or reflect all
8 taxable events that occurred during 1Q03. The Department states that, in order to determine if any
9 adjustments are warranted, petitioner should file sales and use tax returns for the Sofa Factory for
10 1Q03 and 2Q03, along with proper documentation. On July 25, 2006, we informed petitioner that he
11 could file The Sofa Factory's returns for 1Q03 and 2Q03, but petitioner has failed to do so.

12 We find that the Department employed an appropriate methodology under the circumstances to
13 determine The Sofa Factory's tax liability following its failure to file a return for 1Q03. Following the
14 appeals conference, petitioner failed to provide evidence sufficient to enable the Department to make a
15 more accurate determination and, without such records, we have no basis on which to verify
16 petitioner's allegation that The Sofa Factory's sales were declining or nonexistent during 1Q03.
17 Accordingly, there is no basis on which to recommend any reduction to the measure of tax.

18 AMNESTY

19 The D&R incorrectly states that no amnesty interest penalties have yet been imposed because
20 petitioner filed a timely petition. In fact, The Sofa Factory incurred 50-percent amnesty interest
21 penalties totaling \$1,804.75 when it failed to apply for amnesty or pay off the amnesty-eligible tax and
22 interest due for 2Q02 and 4Q02 by March 31, 2005, as required by the amnesty program, and these
23 penalties were included in the determination issued to petitioner as part of his responsible person
24 liability.⁴ There is no statutory or regulatory authority for relieving amnesty interest penalties in
25 section 6829 determinations, but section 6592 provides that amnesty interest penalties may be relieved

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27 ⁴ In accordance with Board policy, since the amnesty-interest penalties incurred by The Sofa Factory have been included in
28 the liabilities asserted against petitioner under section 6829, an additional penalty for petitioner's personal failure to
participate in the amnesty program will not be added to his liability.

1 if a person's failure to comply with amnesty was due to reasonable cause and circumstances beyond
2 the person's control and occurred notwithstanding the exercise of ordinary care and in the absence of
3 willful neglect. Thus, if petitioner can establish that The Sofa Factory should be relieved of the
4 amnesty interest penalties, then that would also inure to petitioner's benefit. At the appeals
5 conference, we explained that relief is available for the amnesty interest penalties (as well as the other
6 penalties passed through to petitioner) and that a statement under penalty of perjury is required for us
7 to consider such relief, but petitioner indicated that he does not dispute any of the penalties assessed
8 against The Sofa Factory, including the amnesty interest penalties.

9 **OTHER DEVELOPMENTS**

10 None.

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17 Summary prepared by Rey Obligacion, Business Taxes Specialist III
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