

ST 19- 07

Tax Type: Sales Tax

Tax Issue: Responsible Corporate Officer – Failure to File or Pay Tax

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
SPRINGFIELD, ILLINOIS**

**THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS**

v.

JOHN SMITH

Taxpayer

Docket #

Letter ID:

Letter ID:

NPL ID:

1002D:

RECOMMENDATION FOR DISPOSITION

Appearances: Matthew Crain, Special Assistant Attorney General, for the Department of Revenue of the State of Illinois; John Smith, *pro se*

Synopsis:

The Department of Revenue (“Department”) issued two Collection Actions, Assessments and Notices of Intent (“Notices”) to John Smith (“taxpayer”) pursuant to section 1002(d) of the Income Tax Act (35 ILCS 5/1002(d)) and section 3-7 of the Uniform Penalty and Interest Act (“UPIA”) (35 ILCS 735/3-7). The Notices allege that the taxpayer was an officer or employee of ABC Management Group, Ltd. d/b/a XYZ Bar (“corporation”) who was responsible for willfully failing to pay the corporation's retailers' occupation taxes (“ROT”) and withholding taxes. The taxpayer requested a late discretionary hearing on the Notice, which was granted by the Chief Administrative Law

Judge. An evidentiary hearing was held during which the taxpayer argued that he was not responsible for filing the tax returns and did not participate in any of the financial decisions for the corporation. After reviewing the record, it is recommended that this matter be resolved in favor of the taxpayer and the Notices be dismissed.

Findings of Fact:

1. The corporation was in the business of operating a [REDACTED] bar in Anywhere, Illinois. (Taxpayer Ex. #1, p. 3; Recording)
2. According to the records of the Illinois Secretary of State, the corporation was organized on June 12, 2009 and involuntarily dissolved on November 12, 2010. [REDACTED] was the registered agent. The Secretary of State records do not indicate who is the president or other officers of the corporation. (Dept. Ex. #1, p. 14)
3. The taxpayer worked with [REDACTED] to open the bar on December 31, 2009. The taxpayer had previously worked with [REDACTED] at another [REDACTED] bar. The taxpayer kept “the front of the house” clean and made sure everything was in place. He helped with scheduling staff and took care of customer service issues. He worked like a “host.” He also helped with marketing and promotions such as happy hours. (Taxpayer Ex. #1, p. 3; Recording)
4. The taxpayer worked at the bar from the end of 2009 through the middle of 2010 when [REDACTED] told him his services were no longer needed. The taxpayer did not receive any compensation for his services. (Recording)
5. The taxpayer did not intend to work for free. He did not invest any money in the business, but he worked with the expectation of becoming a part owner in the future. If the business was successful, he expected to receive a profit from it. (Recording)

6. The taxpayer was not responsible for filing the corporation's tax returns and was not involved in any of the financial decisions for the corporation. The taxpayer did not have signature authority to sign checks, was not involved in the payment of creditors, and did not have control over the corporation's bank accounts. (Taxpayer Ex. #1, p. 3; Recording)
7. On April 27, 2011, the Department issued a Collection Action, Assessment and Notice of Intent to the taxpayer that proposed a total penalty liability of \$ [REDACTED], including tax, interest, and penalty, for the willful failure to pay the corporation's ROT for the following months: January 2010 through July 2010. The Notice was admitted into evidence under the certificate of the Director of the Department. (Dept. Ex. #1, pp. 2-3)
8. On April 27, 2011, the Department issued a Collection Action, Assessment and Notice of Intent to the taxpayer that proposed a total penalty liability of \$ [REDACTED], including tax, interest, and penalty, for the willful failure to pay the corporation's withholding taxes for the following quarters: March 2010 and June 2010. The Notice was admitted into evidence under the certificate of the Director of the Department. (Dept. Ex. #1, pp. 4-5)

Conclusions of Law:

Section 1002(d) of the Income Tax Act provides as follows:

Willful failure to collect and pay over tax. Any person required to collect, truthfully account for, and pay over the tax imposed by this Act who willfully fails to collect such tax or truthfully account for and pay over such tax or willfully attempts in any manner to evade or defeat the tax or the payment thereof, shall, in addition to other penalties provided by law, be liable for the penalty imposed by Section 3-7 of the Uniform Penalty and Interest Act. 35 ILCS 5/1002(d).

Section 3-7 of the Uniform Penalty and Interest Act provides in part as follows:

Any officer or employee of any taxpayer subject to the provisions of a tax Act administered by the Department who has the control, supervision or responsibility of filing returns and making payment of the amount of any

trust tax imposed in accordance with that Act and who wilfully fails to file the return or make the payment to the Department or wilfully attempts in any other manner to evade or defeat the tax shall be personally liable for a penalty equal to the total amount of tax unpaid by the taxpayer including interest and penalties thereon; 35 ILCS 735/3-7(a).

An officer or employee of a corporation may therefore be personally liable for the corporation's taxes if (1) the individual had the control, supervision or responsibility of filing the returns and paying the taxes, and (2) the individual willfully failed to perform these duties.

Any person who is required to collect, truthfully account for and pay over the tax is referred to as a "responsible person." McLean v. Department of Revenue, 326 Ill. App. 3d 667, 674 (1st Dist. 2001). For guidance in determining whether a person is responsible under section 3-7 the Illinois Supreme Court has referred to cases interpreting section 6672 of the Internal Revenue Code (26 U.S.C. §6672)¹. See Branson v. Department of Revenue, 168 Ill. 2d 247, 254-56 (1995); Department of Revenue v. Heartland Investments, Inc., 106 Ill. 2d 19, 29-30 (1985). These cases state that the critical factor in determining responsibility is whether the person had significant control over the corporation's finances. See Purdy Co. of Illinois v. United States, 814 F. 2d 1183, 1186 (7th Cir. 1987) Responsibility is generally found in high corporate officials who have control over the corporation's business affairs and who participate in decisions concerning the payment of creditors and the dispersal of funds. Monday v. United States, 421 F. 2d 1210, 1214-1215 (7th Cir. 1970), cert. den. 400 U.S. 821.

No single factor is dispositive in determining whether a person had significant control over the corporation's finances; the determination must be made by considering the totality of the circumstances. Winter v. United States, 196 F. 3d 339, 345 (2nd Cir. 1999). The relevant circumstances include whether the person (1) is an officer or member of the board of directors, (2) owns shares or possesses an entrepreneurial stake in the company,

¹ This section imposes personal liability on any person who is required to collect, account for, and pay employees' withholding taxes and who willfully fails to do so.

(3) is active in the management of day-to-day affairs of the company, (4) has the ability to hire and fire employees, (5) makes decisions regarding which, when and in what order outstanding debts or taxes will be paid, (6) exercises control over daily bank accounts and disbursement records, and (7) has check-signing authority. *Id.*

In addition, these cases define "willful" as involving intentional, knowing and voluntary acts or, alternatively, reckless disregard for obvious known risks. See Branson at 254-56; Heartland at 29-30. Willful conduct does not require bad purpose or intent to defraud the government. Branson at 255; Heartland at 30. Willfulness may be established by showing that the responsible person (1) clearly ought to have known that (2) there was a grave risk that the taxes were not being paid and (3) the person was in a position to find out for certain very easily. Wright v. United States, 809 F. 2d 425, 427 (7th Cir. 1987). Furthermore, whether the person in question willfully failed to pay the taxes is an issue of fact to be determined on the basis of the evidence in each particular case. Heartland at 30; Department of Revenue v. Joseph Bublick & Sons, Inc., 68 Ill. 2d 568, 577 (1977). Courts have found that giving preferential treatment to other creditors rather than paying the corporation's taxes constitutes willful behavior. See Heartland at 29-30.

Under section 3-7, the Department's certified record relating to the penalty liability constitutes *prima facie* proof of the correctness of the penalty due.² See Branson at 260. Once the Department presents its *prima facie* case, the burden shifts to the taxpayer to establish by a preponderance of the evidence that one or more of the elements of the penalty are lacking, *i.e.*, that the person charged was not a responsible corporate officer or employee, or that the person's actions were not willful. *Id.* at 261. In order to overcome

² The relevant portion of section 3-7 provides as follows: "The Department shall determine a penalty due under this Section according to its best judgment and information, and that determination shall be prima facie correct and shall be prima facie evidence of a penalty due under this Section. Proof of that determination by the Department shall be made at any hearing before it or in any legal proceeding by reproduced copy or computer printout of the Department's record relating thereto in the name of the Department under the certificate of the Director of Revenue. * * * That certified reproduced copy or certified computer print-out shall without further proof, be admitted into evidence before the Department or in any legal proceeding and shall be prima facie proof of the correctness of the amount of tax or penalty due." 35 ILCS 735/3-7(a).

the Department's *prima facie* case, the allegedly responsible person must present more than his or her testimony denying the accuracy of the Department's assessment. A. R. Barnes & Co. v. Department of Revenue, 173 Ill. App. 3d 826, 833-34 (1st Dist. 1988). The person must present evidence that is consistent, probable, and identified with the respondent's books and records to support the claim. *Id.*

In the present case, the Department's *prima facie* case was established when the Department's certified record relating to the penalty liability was admitted into evidence. In response, the taxpayer provided documents from the corporation's creditors that show collection efforts against [REDACTED]. The taxpayer also presented a statement from an employee of the corporation that verified the taxpayer's limited role in the business. The taxpayer was not responsible for filing the corporation's tax returns and was not involved in any of the financial decisions for the corporation. The taxpayer did not have signature authority to sign checks, was not involved in the payment of creditors, and did not have control over the corporation's bank accounts. The taxpayer has met his burden of proving by a preponderance of the evidence that he was not a responsible person under section 3-7 of the Uniform Penalty and Interest Act.

Recommendation

It is therefore recommended that the two Collection Actions, Assessments and Notices of Intent issued against the taxpayer, NPL Penalty ID [REDACTED] and 1002D Penalty ID [REDACTED], be dismissed.

Linda Olivero
Administrative Law Judge

Enter: June 28, 2019