

ST 06-7

Tax Type: Sales 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)	
)	Docket # 00-ST-0000
v.)	IBT # 0000-0000
)	NPL # 0000, 0000
JANE DOE and MARY DOE)	
)	
Respondents)	

RECOMMENDATION FOR DISPOSITION

Appearances: Kent Steinkamp, Special Assistant Attorney General, for the Department of Revenue of the State of Illinois; Jonathon C. Fox of Califf & Harper, P.C. for Jane Doe and Mary Doe.

Synopsis:

The Department of Revenue (“Department”) issued Notices of Penalty Liability (“NPLs”) to Jane Doe and Mary Doe (“respondents”) pursuant to section 3-7 of the Uniform Penalty and Interest Act (“UPIA”) (35 ILCS 735/3-7). The NPLs allege that the respondents were officers or employees of ABC International Pipeline Services, Inc. (“corporation”) who were responsible for wilfully failing to pay the corporation’s retailers’ occupation taxes (“ROT”). Jane Doe timely protested the NPL issued to her; Mary Doe did not timely protest her NPL, but her request for a discretionary hearing was

granted. The cases were consolidated for an evidentiary hearing. After reviewing the record, it is recommended that both NPLs be upheld.

Findings of Fact:

1. The corporation was organized in October 1994 and was a company that supplied pipeline materials to contractors. (Dept. Ex. #3; Tr. pp. 28-29)

2. The corporation's facility was located at in Anywhere, Illinois. (Dept. Ex. #1-3; Tr. p. 9)

3. The respondents are the daughters of John and Joe Doe, who are brothers who operate a business known as Doe Brothers, which is a pipeline construction company located in Anywhere, Illinois. (Tr. pp. 10, 23-24, 39)

4. The corporation sold products to Doe Brothers. (Tr. p. 43)

5. Mary Doe was formerly known as Mary Jones, and Jane Doe was formerly known as Jane Smith. (Tr. pp. 12, 21)

6. The Domestic Corporation Annual Report filed in September 2000 shows that the corporation's president was Joe Blow. Mary Jones was both the secretary and treasurer of the corporation. The directors of the corporation were Joe Blow, Mary Jones, and Jane Smith. (Dept. Ex. #3)

7. On March 19, 1997, Mary Jones signed a "Certificate" that stated as follows:

The undersigned, Secretary of ABC International Pipeline Services, Inc., does hereby certify that seventy percent (70%) of the issued and outstanding shares of the corporation are owned by Jane Smith and Mary Jones, both of whom are women, making this Illinois corporation "minority owned" under prevailing understanding of this term. This ratio of ownership has been effective since the incorporation of the company and continues to this date and forward." (Dept. Ex. #3)

8. On July 2, 2000, Jane Doe signed a Corporate Resolution to Borrow indicating that she was the vice president of the corporation. The resolution also states that the three officers are authorized and empowered to, among other things, borrow money, execute

notes, grant security, and execute security documents. The document was certified to and attested by Mary Jones. (Dept. Ex. #3)

9. On September 26, 2000, the three directors of the corporation signed a “Memorandum of Action by Directors of ABC International Pipeline Services, Inc.” which stated as follows:

We, the undersigned, being all the Directors of ABC International Pipeline Services, Inc. an Illinois corporation, take the following actions by consent and without a meeting, as if by unanimous vote, pursuant to Section 8.45 of the Illinois Business Corporation Act, and waive all notice of a meeting, pursuant to Section 7.20 of that Act:

RESOLVED, that Mary Jones, Secretary/Treasurer of the Corporation, is hereby authorized to sign the extension of the Corporation’s line of credit with First Midwest Bank, N.A.” (Dept. Ex. #3)

10. During 2001, Ms. Mary Doe was employed part-time at Doe Brothers. The corporation has never employed either respondent. (Tr. pp. 8-9, 18)

11. Ms. Jane Doe has been employed full-time by XYZ Intrastate Pipeline Company since 1994. This company transports natural gas. (Tr. pp. 18, 23)

12. During the time period in question, the vice president and risk manager for Doe Brothers would tell the respondents when they needed to sign papers for the corporation, and they would go to the Doe Brothers office and sign them. (Tr. pp. 14, 35, 40)

13. The corporation filed Form NUC-1, Illinois Business Registration Application, with the Department on July 13, 1995. The NUC-1 shows that Laurence Blow personally accepted responsibility for the filing of returns and the payment of taxes due. (Dept. Ex. #3)

14. XXX, who was the corporation’s controller, signed all of the corporation’s ROT returns for the months of January through July 2001. The returns for January through March 2001 were dated May 8, 2001. The April return was dated May 21, 2001,

the May return was dated June 20, 2001, the June return was not dated, and the July return was dated August 27, 2001. (Dept. Ex. #3; Tr. p. 34)

15. On February 23, 2004, the Department issued NPL number 0000 to Mary Doe and NPL number 0000 to Jane Doe. Each NPL proposed a total penalty liability of \$82,802.44, including tax, interest, and penalty, for failure to pay ROT for the months of January through July 2001. The NPLs were admitted into evidence under the certificate of the Director of the Department. (Dept. Ex. #1).

Conclusions of Law:

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 ROT returns and paying the taxes, and (2) the individual wilfully failed to perform these duties.

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

¹ This section imposes personal liability on corporate officers who willfully fail to collect, account for, or pay over employees' social security and Federal income withholding taxes.

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.

In addition, these cases define "wilfull" as involving intentional, knowing and voluntary acts or, alternatively, reckless disregard for obvious known risks. See Branson at 254-56; Heartland at 29-30. Wilfull 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 wilfully 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 wilfull 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 respondent to establish 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

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).

person's actions were not wilfull. Id. at 261. In order to overcome 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 books and records to support the claim. Id.

The Department believes that the respondents were responsible for filing the returns and paying the taxes and that they wilfully failed to do so. The Department argues that even if the respondents had no knowledge of their responsibilities related to their positions with the corporation, they had a duty to know what their responsibilities were.

The respondents contend that they were not responsible for filing the returns or paying the taxes, and that the facts in this case are similar to those in McLean v. Department of Revenue, 326 Ill. App. 3d 667 (1st Dist. 2001). In that case, the court found that for a certain time period the plaintiff was not a “responsible” person because he was not involved in the day-to-day operations of the business, signed only two checks, seldom visited the corporate site, and never prepared, signed, or filed the tax returns. The respondents state that in the instant case they were not involved in the day-to-day operations of the corporation, they never signed checks for the corporation and never visited the corporate site, which was in Anywhere. The respondents argue that during the time period in question, Ms. Jane Doe was living in Minnesota and Ms. Mary Doe was residing in Moline. They also claim that they never prepared, signed, or filed the tax returns, and they were not involved in the selection of the individuals or entities who provided the corporation with tax and/or accounting services. The respondents state that the corporation had controllers or outside accounting firms who were responsible for preparing the returns and paying the taxes.

In addition, the respondents maintain that even if it is assumed that they were responsible for filing the returns, they did not wilfully fail to do so. They state that in People ex rel. Department of Revenue v. National Liquors Empire, Inc., 157 Ill. App. 3d 434 (4th Dist. 1987), the wilfull failure to pay requirement was not met when the corporation's president and sole officer stated that the corporation had an accountant and bookkeeper who prepared the tax reports, and he had no personal knowledge that the sales tax had been unreported. The respondents claim that in the present case, they were not involved in preparing sales tax reports and had no personal knowledge that the sales tax had been unreported or not paid.

The Department's *prima facie* case was established in this case when the Department's certified record relating to the penalty liability was admitted into evidence. As previously noted, the respondents have the burden of establishing that one or more of the elements of the penalty are lacking. In order to overcome the Department's *prima facie* case, the respondents must present more than their testimony denying the accuracy of the Department's assessment. Sprague v. Johnson, 195 Ill. App. 3d 798, 804 (4th Dist. 1990); Barnes & Co., 173 Ill. App. 3d at 833-34. They must present evidence that is consistent, probable, and identified with the books and records to support the claim. Id. The reason why the respondents bear the burden of disproving the Department's determination is because it is the respondents, not the Department, who have access to the information regarding why the returns were not filed and the taxes were not paid. Branson, 168 Ill. 2d at 262.

Although the testimony in this case presented facts similar to those in McLean, and the respondents did not sign the returns for the time period in question, the respondents have failed to present sufficient documentary evidence to support their claims. Ms. Jane Doe testified that she was living in Minnesota during 2001, but she did not present documentary evidence, such as her paycheck receipts or invoices, showing that she resided there. Ms. Mary Doe stated that she lived in Moline, which is

approximately 30 miles from Anywhere. (Tr. p. 38) This distance is short enough for her to have had frequent contact with the corporate office.

Both respondents testified that they were not involved in the daily operations of the business and did not sign checks, but they did not provide documentary support for their testimony, such as verification from the bank that they did not have signature authority for the corporation's account. The vice president for Doe Brothers, Joe Blow, testified that he would contact the respondents in order for them to go to the Doe Brothers office to sign papers for the corporation. (Tr. pp. 35, 40) Joe Blow apparently had regular contact with someone from the corporation, but he did not explain who gave him the papers, with whom he spoke at the corporation concerning the papers, or why he was the person who received the papers and contacted the respondents. He did not explain whether he attempted to locate corporate documents for the respondents or why he did not have access to corporate documents to support the respondents' claims.³

Ms. Mary Doe stated that she first learned about the tax liability when she heard that her name was in the newspaper for a tax lien. (Tr. pp. 16-17) Ms. Jane Doe testified that she became aware of the liability when she received the NPL in February or March of 2004. (Tr. p. 20) Joe Blow, however, testified that he had knowledge of the corporation's delinquent taxes in late 2001. (Tr. p. 31) Joe Blow had regular contact with both respondents and someone from the corporation, and it is difficult to believe that the respondents were not aware of the liabilities until 2004.

The evidence also suggests that the respondents' fathers may have been aware of the tax problems as well. Ms. Jane Doe testified that at the time of the hearing her father was still alive. (Tr. p. 24) Ms. Mary Doe did not indicate whether her father was still

³ The "Certificate" signed by Ms. Doe on March 19, 1997 indicates that the corporation is "minority owned." Section 2(A)(4) of the Business Enterprise for Minorities, Females, and Persons with Disabilities Act states in relevant part as follows: "'Female owned business' means, * * * in the case of a corporation, at least 51% of the stock in which is owned by one or more females; and the management and daily business operations of which are controlled by one or more of the females who own it." 35 ILCS 575/2(A)(4). Therefore, in order to qualify as a minority owned business for the State of Illinois, either Ms. Doe or Ms. Jane Doe must have had control of the business operations.

alive, and neither respondent indicated that they did not have regular contact with their fathers. Joe Blow explained that the Doe brothers helped Mr. Blow with financing for the corporation. The Doe brothers guaranteed a two million dollar line of credit for the corporation. (Tr. pp. 32, 40) Joe Blow testified that “sometime in the late summer of 2001 we learned from the bank that, that credit had been used up.” (Tr. p. 31) He later stated that Mr. Blow was in the hospital for an addiction problem, and “when he ended up in the hospital and the bank is saying we want our two million dollars, we knew nothing – we meaning the Does and myself – about the company. And we had to talk to people. And we hired XXX back. And, by that, I mean we just asked her can you come back because there is nobody there and we don’t know what’s going on.” (Tr. p. 34) Because the returns for January through March of 2001 were all signed by XXX on May 8, 2001, and the remaining returns were signed on days closer to their due dates, it appears as though Ms. XXX might have been “hired back” in May of 2001, and Joe Blow and the Doe brothers would have been aware of the tax problems during the time period in question. Although Joe Blow stated that they “knew nothing,” they were connected to the corporation enough to attempt to remedy the problems. It is reasonable to conclude that because of the contact that the respondents most likely had with their fathers and Joe Blow, the respondents were aware of the problems as well. The evidence suggests that the respondents ought to have known that there was a grave risk that the taxes were not being paid, and they were in a position to find out for certain very easily. See Wright, *supra*.

Recommendation

Because the respondents did not present sufficient evidence to overcome the Department's *prima facie* case, it is recommended that the Notices of Penalty Liability be upheld.

Linda Olivero
Administrative Law Judge

Enter: February 10, 2006