

M e m o r a n d u m**170.2200**

To: Mr. Paul Nelson
Petition Unit

Date: May 22, 1986

From: Donald J. Hennessy
Tax Counsel

Subject: Personal Liability of Corporate Officers Pursuant to Section 6829
Liability of Corporate Officers of Suspended Corporation

This is in response to your memorandum of March 24, 1986 regarding our discussion of a determination issued to a corporate officer pursuant to section 6829. The corporate liability was based on an audit in which claimed sales for resale or sales in interstate commerce were disallowed. You assumed that the corporation had not collected sales tax reimbursement on these disallowed sales.

Section 6829(c) reads as follows:

“Personal liability may be imposed pursuant to this section, only if the board can establish that the corporation had included tax reimbursement in the selling price of, or added tax reimbursement to the selling price of, tangible personal property sold in the conduct of its business, or when it can be established that the corporation consumed tangible personal property and failed to pay the tax to the seller or to report and pay use tax.”

Given the above facts, I gave you my opinion that the requirements of Section 6829(c) were not satisfied and, therefore, the corporate officers were not liable. You later discussed my conclusion with Supervisor of Collections, Rick Slater, who provided you with a copy of my memorandum opinion of January 16, 1986 which has been interpreted by our staff as reaching a contrary result. In order to clarify our interpretation of Section 6829(c), you ask whether corporate officers would be liable under the following ten factual situations. Situations five through nine raise the additional question of whether Section 6829 includes liability for use tax collection. In all of the following situations, we assume that the requirements of Section 6829, other than collection of reimbursement, e.g., willfully, responsibility, have been satisfied.

“1. Sales tax liability of the corporation exists on sales made by the corporation. Tax reimbursement was included in or added to the selling price. The corporation receives payment for the selling price plus tax reimbursement.”

Yes, the corporate officers would be liable. The requirements of Section 6829(c) are satisfied.

“2. Same as #1 above, except the corporation receives payment for the selling price but not for the tax reimbursement.”

No, the corporate officers would not be liable because sales tax reimbursement was not collected.

“3. Sales tax liability of the corporation exists on sales made by the corporation. Tax reimbursement was not included in or added to the selling price. The corporation receives payment for the selling price only.”

No, the corporate officers would not be liable because sales tax reimbursement was not collected.

“4. Same as #3 above, except the corporation receives payment for the selling price plus reimbursement for tax.”

Yes, the corporate officers would be liable. The requirements of Section 6829(c) are satisfied.

“5. Use tax liability of the corporation exists on tangible personal property consumed by the corporation.”

Yes, the corporate officers would be liable. Section 6829 specifically so provides.

“6. Use tax liability of the corporation exists on sales made by the corporation. Tax was added to the sales price of the property sold. The corporation received payment for the sales price and the tax.”

No, the corporate officers would not be liable because Section 6829 does not include the use tax collection duty.

“7. Same as six above, except the corporation received payment for the sales price but not for the tax.”

No, the corporate officers would not be liable because Section 6829 does not include the use tax collection duty.

“8. Use tax liability of the corporation exists on sales made by the corporation. Tax was not added to the sales price of the property sold. The corporation received payment for the sales price only.”

No, the corporate officers would not be liable because Section 6829 does not include the use tax collection duty.

“9. Same as #8 above, except the corporation received payment for the sales price and the tax.”

No, the corporate officers would not be liable because Section 6829 does not include the use tax collection duty.

“10. The corporation has certain transactions which fit into one or more of the above nine categories. Can the corporate officers be liable for some transactions and not others?”

Yes.

In response to the unnumbered question at the end of your memo, the above answers are the same whether the corporate liability was self-reported tax or determined tax.

Operations memo 719 of November 10, 1981, on page 2 at 4, in construing the above quoted Section 6829(c) states:

“It must be established that sales tax reimbursement was collected from the customers or the corporation consumed tangible personal property and failed to pay the use tax.

The evidence required to establish personal liability must be ample to show that tax reimbursement was the normal operating procedure of the business. This evidence may include sales records, tax returns, audit reports, invoices, etc., showing that tax reimbursement was either included in or added to the selling price of the merchandise.”

On January 16, 1986, I wrote to Chief Compliance Supervisor P. K. Taylor regarding Section 6829(c) and the question of whether investigations must prove that tax reimbursement was collected on specific transactions, and only those transactions included in determinations against corporate officers, or may investigations simply establish that it was the custom and practice of the corporation to collect tax reimbursement in the normal course of business. After stating the above quoted material from Operations Memo 719, I concluded that “investigations need not show that reimbursement was collected on specific transactions, but must show that it was the custom and practice of the corporation to collect tax reimbursement.”

I considered my conclusion as applying to situations in which we did not know whether or not sales tax reimbursement had been collected on specific sales. In such situations, we could rely on "normal operating procedures". In hindsight, if I had anticipated the problems in your March 24, 1986 memo, my January 16, 1986 memo to Mr. Taylor would have further stated that, in my opinion, if we in fact know or later discover that sales tax reimbursement was not collected on specific sales, we should not include those specific sales in the determination against corporate officers, or we should delete them if they were earlier included under the "normal operating procedure" rationale.

While preparing this reply to your inquiry, I have discovered that, prior to my January 16, 1986 memo to Mr. Taylor, the Audit Policy and Management Guidelines Manual, (APMG), as revised November 1984, in Section 2214.15 on Corporate Suspension states:

"When the evidence shows the above criteria are met and that tax reimbursement was the normal operating procedure of a particular corporation, a dual liability may be established against the suspended corporation and corporate officers for the entire audit assessment even though all or a portion of the audit assessment involves disallowed deductions or other taxable sales for which sales tax was neither added to nor included in the selling price of the merchandise."

In APMG Section 2214.45, on Section 6829 liability, it is stated that the above quoted comment from Section 2214.15 regarding disallowed deductions is applicable to Section 6829 audit assessments. The same requirements are at Sections 715.025 and 715.026 of the Compliance Policy and Procedures Manual (CPPM). The above quoted sections of both the APMG and CPPM were approved by Legal, but apparently without specific attention to their doing away with the need for the collection of sales tax reimbursement on specific sales before determinations were issued against corporate officers. We apologize for this oversight, and recommend that such section of the APMG and CPPM be amended.

In his April 3, 1980 memo to the Honorable Richard Nevins recommending that the Board revive the practice of issuing dual determinations against corporate officers for liability incurred during the period of corporate suspension, Assistant Chief Counsel Gary Jugum stated on page 7 that:

"However, we would strongly recommend that dual determinations be issued in only those cases where sales tax reimbursement has in fact been collected from customers."

We recommend that this same rule be applied to determinations issue to corporate officers pursuant to Section 6829. I believe the interpretation to be given Operations Memo 719, in order to comply with this rule is that, if we don not know whether or not sales tax reimbursement was collected, we may issued a determination against the corporate officers if we have evidence that the corporation's "normal operating procedure" was to include or add sales

tax reimbursement. But, if we know, or if in the case of claimed sales for resale or sales in interstate commerce, there is a strong presumption that sales tax reimbursement was not collected, we should not include such sales in the Section 6829 determination or, if they were earlier included under the "normal operating procedures" rationale, such sales would be deleted.

That this should be our position seems even more apparent after our recent experience with AB 3060 introduced by Assemblymen Hannigan and Davis on February 12, 1986. The concept of this bill as post-amnesty enforcement was originally approved in principal by our Board's legislative committee. As relevant herein, the original bill would have deleted Section 6829(c), thereby making the question of whether or not sales tax reimbursement was collected irrelevant to billings against corporate officers. Staff Counsel John Abbott tells me that, when AB 3060 specifically came before our entire Board, the vote was to oppose the deletion of Section 6829(c). When Mr. Abbott informed Assemblyman Hannigan's office of our Board's opposition, the bill was amended, March 17, 1986, so that subsection (c) remains in Section 6829. From this it is clear that our Board members do not want corporate officers to be personally liable for sales tax unless reimbursement was collected.

A further question raised in your memo is whether Section 6829(c) imposes liability on corporate officers for use tax which the corporation was required to collect. Such a corporation may have failed in its duty to collect the use tax, the usual case, or in the unusual case, it may have collected the use tax but not paid it over to us. Does the language of Section 6829(c) reach such corporate officers? The best reading of Section 6829(c) is that use tax collection duties, as distinguished from use tax imposed directly on the corporation, are not within such section. This is in line with our Board members restrictive reading of Section 6829.

The history of Section 6829 is, of course, well known. Since our Collection Unit believes corporate tax liability is a significant portion of our uncollectables, we attempted to get a much stronger statute than Section 6829. We failed. Section 6829 is full of restrictions, one of which is subsection (c), in which the Legislature makes clear that personal liability may be imposed on a corporate officer only if the Board can establish that the corporation had included or added tax reimbursement. The legislative intent was to limit personal liability to reimbursements collected from the buying public. This is a variation on the old "involuntary trust" theme from Decorative Carpets v. State Board of Equalization, 58 Cal.2d 252, 254. A taxpayer should not be allowed to collect monies from the public under the guise of taxes, and then not pay such taxes to the Board. That far the Legislature was willing to go, but no farther. That far our Board is willing to go, but no farther. Our staff must go no farther.

DJH:rar

cc: Mr. Glenn Bystrom
Mr. Rick Slater – I will write you soon on the "willfully" issue
Mr. R. L. Dick
Mr. E. L. Sorensen, Jr.