

JURISDICTION: OKLAHOMA TAX COMMISSION
CITE: 89-07-25-04 / NON-PRECEDENTIAL
ID: P-88-310-P
DATE: JULY 25, 1989
DISPOSITION: DENIED
TAX TYPE: SALES / WITHHOLDING
APPEAL: AFFIRMED / S.CT. 73,855
CITE: NOT A PUBLISHED DECISION

FINDINGS OF FACT AND CONCLUSIONS OF LAW

A hearing was had, at which hearing, the Protestant was represented by ATTORNEY, and the Business Tax Division was represented by OTC ATTORNEY, Assistant General Counsel. The Protestant testified on his own behalf. Exhibits not herein itemized, were received in to evidence, and this case was submitted for a decision.

STATEMENT OF FACTS

COMPANY was doing business under the name RESTAURANT at ADDRESS for approximately one year before Protestant associated with the enterprise. During this period of time, OWNER operated the enterprise. Protestant testified that he believed that OWNER was part owner of the enterprise. Protestant, a trial lawyer, became involved in this enterprise after he was approached by ACQUAINTANCE, also an attorney, who asked Protestant to make an investment in COMPANY. Protestant agreed to make a \$15,000.00 investment in the enterprise, which he testified was in the form of a loan. He sought the advice of a lawyer, who advised him to become president and director of the enterprise in order to assure repayment. To protect his investment, Protestant acquired all of the outstanding stock of RESTAURANT, which owned 100% of the outstanding stock of COMPANY.

PROTESTANT testified that he believed that OWNER owned twenty-five percent of the stock. He testified that it was his and OWNER'S intent that he acquire the remaining seventy-five percent of the stock. He later discovered that OWNER did not in fact own any stock and that he had therefore acquired all of the corporation's stock. Although it was PROTESTANT'S intention to become the majority stockholder, it was not his intention to become the sole stockholder.

Also to assure repayment, Protestant became the president and a director of the enterprise as he had been advised to do, and OWNER continued as the secretary, treasurer and a director of the enterprise. OWNER continued to operate the enterprise as she had before Protestant became associated with the enterprise.

Protestant was an authorized signatory on company bank accounts, although he did not write any checks on these accounts. It was his uncontroverted testimony that he did not participate in the operations of the enterprise. He did not collect funds, deposit funds, disburse funds, nor did he give directions as to how funds should be collected, deposited or disbursed.

Protestant testified that OWNER approached him at another point in time and asked for an additional loan of \$2,500.00. Protestant was informed that the loan was for the purpose of repayment by the enterprise of a loan from a third party. Protestant gave OWNER the additional money requested. Protestant has not received repayment of either the \$15,000.00 loan or the \$2,500.00 loan. Protestant did not receive any money from the enterprise while it was in operation.

The enterprise ceased doing business on January 6, 1988. On that same date, Protestant received notice that the landlord of RESTAURANT had issued a notice to pay up or quit. Protestant testified that this was the first time he became aware that the enterprise was having financial difficulties. He also testified that it was not until he received notice of a proposed assessment that he became aware of unpaid tax liabilities. Protestant received such proposed assessments on May 10, 1988.

On June 8, 1988, Protestant timely protested the assessments. Protestant confessed his liability for unpaid mixed beverage tax in an amount not to exceed \$6,000.00, such concession being solely by reason of Protestant's personal surety bond in favor of the State of Oklahoma.

The parties have stipulated to the following facts:

1. The tax liabilities, for the months of September through December of 1987, exclusive of penalties and interest are as follows:

Sales tax	\$5,515.23
Employee withholding tax	\$ 615.42
Mixed beverage tax	\$4,183.82

2. The tax liabilities for the six days of January 1988 during which the corporation did business is to be calculated on a daily rate basis using the four month liability amounts in the preceding stipulation;

3. Protestant has no personal liability for the proposed assessment of franchise tax;

4. Protestant has no personal liability for the proposed assessment of mixed beverage tax except under the terms of his bond to the State of Oklahoma;

5. The corporation was in good standing with the Oklahoma Secretary of State during the period in question in this proceeding;

6. The taxes in question were collected or withheld as required by law and all necessary and required reports were made to the appropriate authorities;

7. The only questions to be determined are whether Protestant is a person responsible for paying over withholding taxes which were withheld, sales taxes which were collected.

ISSUES AND CONTENTIONS

The sole issue herein is whether Protestant as an officer of COMPANY is personally liable for the sales and withholding taxes of the corporation under the provisions of 68 O.S. Supp. 1988, §1361 and 68 O.S. Supp. 1988, §2385.3.

Protestant asserts that 68 O.S. Supp. 1988, §2385.1 and 2385.3 set forth the criteria for determining personal liability for withholding tax. Protestant contends that to be liable for withholding tax under 68 O.S. Supp. 1988, §2385.1 an officer must have control of the payment of the taxes. Protestant contends that Section 2385.1 is similar to Section 6672 of the Internal Revenue Code which speaks to the failure to collect, truthfully account for and pay over withholding tax on the federal level.

Protestant stated that he recognized that control can be exercised by giving directions or orders, as opposed to the physical act of disbursing funds, but asserts that he did not exercise any control over the company. To support the contention that because of his lack of control of the company he is not personally liable for withholding tax, Protestant relies on Brennan v. U.S., 85-1 USTC, 9113, which stands for the proposition that absent some active participation in corporate affairs, the mere ownership of shares of a corporation does not make a shareholder liable for corporate taxes. Protestant also relies on Pototzky v. U.S., 8 Ct.Cl. 308 (1985), which held that merely holding a corporate office, without exercising any authority is insufficient to make the officer a person responsible for corporate taxes.

Protestant further relies on 68 O.S. 1981, §253, which allows assessments to be made “against the principal officers of a corporation, if such officers are liable under the laws of Oklahoma.” Protestant asserts that Section 253 imposes liability only against officers who are liable. Protestant asserts that simply being an officer does not make one liable for a corporation’s failure to withhold or collect or truthfully account for and pay over taxes to taxing authorities.

Protestant contends that 68 O.S. Supp. 1988, §1361(E) makes it clear that collected taxes are held in trust and that a willful or intentional failure to remit those taxes coupled with an appropriation of the funds to one’s own use, constitutes embezzlement. Protestant concedes that the collected taxes have been used for a wrong purpose. Protestant, however, asserts that it was not Protestant who caused the funds to be wrongfully used. Protestant further contends that if in fact he is liable for collected but unremitted taxes, under the provisions of 68 O.S. Supp. 1988, §1361(E), he is guilty of embezzling funds he never touched or exercised control over. He asserts that this is an impossible result.

The Business Tax Division contends that 68 O.S. 1981, §1361 imposes liability on each principal officer of a corporation, and that PROTESTANT, as an officer of COMPANY, is personally liable for the sales tax collected by COMPANY. The Business Tax Division further asserts that Protestant is liable for withholding taxes not remitted by COMPANY under the provisions of 68 O.S. Supp. 1988, §2358.3(d), which provides that officers or employees of a corporation under a duty to act for the corporation to withhold and remit withholding taxes are personally liable for such taxes.

To support these contentions the Business Tax Division relies on Preston-Thomas Construction, Inc. v. Central Leasing Corp., 518 P.2d 1125 (Okl. 1974), a conversion case in which the Oklahoma Supreme Court held that the officers of a corporation were personally liable for use of funds entrusted to it if they received any of the money, if they participated in a wrongful asset distribution or if being ignorant of the wrong doing they were negligent in failing to learn of it and prevent it. The Business Tax Division asserts that Protestant knew or should have known that the taxes were being collected and withheld and that all the taxes were not being paid to the Tax Commission.

APPLICABLE LAW

Title 68 O.S. Supp. 1988, §1361(A) provides in pertinent part that each principal officer of a corporation shall be personally liable for sales taxes:

(A) The tax levied by this article shall be paid by the consumer or user to the vendor as trustee for and on account of this State. Each and every vendor in this State shall collect from the consumer or user the full amount of the tax levied by this article, or an amount equal as nearly as possible or practical to the average equivalent thereof. Every person required to collect any tax imposed by this article, and in the case of a corporation, each principal officer thereof, shall be personally liable for said tax. [Emphasis added].

Title 68 O.S. Supp. 1988, §2385.3(d) also imposes personal liability on those with a duty to act on behalf of a corporation for withholding tax purposes as follows:

(d) Every employer who fails to withhold or pay to the Tax Commission any sums herein required to be withheld or paid shall be personally and individually liable therefor to the State of Oklahoma. The term “employer” as used in this paragraph and in Section 2385.6 includes an officer or employee of a corporation, or a member or employee of a partnership, who as such officer or employee of a corporation, or a member is under a duty to act for a corporation or partnership to withhold and remit withholding taxes in accordance with this section and Section 2385.2. Any sum or sums withheld in accordance with the provisions of Section 2385.2 shall be deemed to be held in trust for the State of Oklahoma, ... [Emphasis added].

Neither statute imposes personal liability on all officers of a corporation. Section 1361(A) of the Oklahoma Sales Tax Code imposes personal liability on principal officers, but no definition of principal officer is provided by statute. Section 2385.3(d) of the Oklahoma Income Tax Act imposes personal liability on the officers and employees of a corporation who are under a duty to act for the corporation to withhold and remit withholding taxes. The Oklahoma Supreme Court has not addressed the question of whether an individual was a principal officer for sales tax purposes or was under a duty to act for withholding tax purposes. A similar federal withholding tax provision in the Internal Revenue Code has been interpreted, however. See Godfrey v. United States, 748 F.2d 1568 (Fed.Cir. 1984); Spang v. United States, 533 F.Supp. 220 (W.D.Okl. 1982); Pototzky v. United States, 8 Ct.Cl. 308 (1985).

For federal withholding tax purposes, there are two separate statutory requirements for individual liability. First, the person must be under a duty to perform the act and second, the “responsible person” must have willfully failed to perform the act. For state withholding taxes, Oklahoma Statute requires only that the individual be under a duty to act.

In Godfrey v. United States, 748 F.2d 1568 (Fed.Cir. 1984), the circuit court discussed at length the requirement that the individual be under a duty to perform the act. This court reasoned as follows:

The overwhelming weight of case precedent requires the factfinder to look through the “mechanical functions of the various corporate officers”, White v. United States, 372 F.2d at 516, to determine the persons having “the power to control the decision-making process by which the employer corporation allocates funds to other creditors in preference to its withholding tax obligations.” Haffa v. United States, 516 F.2d 931, 936 (7th Cir.1975). The inquiry required by the statute is “a search for a person with ultimate authority over expenditure of funds since such a person can fairly be said to be responsible for the corporation’s failure to pay over its taxes.” White v. United States, 372 F.2d at 517.

The court went on to state:

As the case law makes abundantly clear, a person’s “duty” under § 6672 must be viewed in light of his power to compel or prohibit the allocation of corporate funds. It is a test of substance, not form. Thus, where a person has authority to sign the checks of the corporation, . . . or to prevent their issuance by denying a necessary signature, . . . or where that person controls the disbursement of the payroll, . . . or controls the voting stock of the corporation, . . . he will generally be held “responsible”. [Citations omitted].

In an earlier federal case the federal district court held that a taxpayer was not personally liable for withholding taxes since the taxpayer had no managerial responsibilities and had no control over the issuing of checks or over payroll or general checking accounts and made no decisions regarding the order in which creditors would be paid. Spang v. United States, 533 F.Supp. 220 (W.D.Okl. 1982).

At 225 the court stated as follows:

Liability may attach to each of those persons responsible for seeing that trust fund taxes deducted from employees’ wages are paid over to the government, i.e., those persons who have significant control over the business affairs of the corporation or who participate in decisions regarding what bills should be or should not be paid and when. Leushchner v. United States, 336 F.2d 246 (9th cir. 1964); Bloom v. United States, 272 F.2d 215 (9th Cir. 1959), cert. denied, 363 U.S. 803, 80 S.Ct. 1236, 4 L.Ed.2d 1146 (1960). Control necessary to support liability under Section 6672 is simply the ability to direct or control

the payment of corporate funds. *Bolding v. United States*, 215 Ct.Cl. 148, 565 F.2d 663, 671 (1977). [Emphasis added].

In *Pototzky v. United States*, 8 Ct.Cl. 308 (1985), another federal withholding tax case, a taxpayer had been an active participant in the management of the corporation. During the audit period, however, taxpayer was an officer in name only. The Court focused on substance rather than form, and stated that the mere fact that an individual is a corporate officer does not impose individual liability for corporate taxes. The reasoning employed by the federal courts in determining individual liability for federal withholding taxes is persuasive in determining liability for state withholding taxes in light of the similar “duty” requirement.

Although Protestant did not actively participate in the management of the corporation on a day-to-day basis, as President, 100% stockholder, Director, and chief financier of the corporation, he most certainly had the ultimate authority over the expenditure of funds and can be said to be responsible for the corporation’s failure to remit the taxes. Protestant possessed the power to compel or prohibit the allocation of corporate funds. The fact that he chose not to concern himself with corporate affairs or exert his power does not relieve him of that duty.

For purposes of establishing individual liability for sales taxes that were collected but not remitted, Protestant is a principal officer of the corporation. 68 O.S. Supp. 1988, §1361. Protestant argues that under 68 O.S. Supp. 1988, §253, simply being an officer of a corporation does not make him liable for the sales taxes. Section 253 directs the Tax Commission to file proposed assessments for unpaid sales taxes and withholding taxes as follows:

§ 253. Corporations--Filing assessment for certain unpaid taxes

When the Oklahoma Tax Commission files a proposed assessment against corporations for unpaid sales taxes and withheld income taxes, the Commission shall file such proposed assessments against the principal officers of such corporations, if such officers are liable under the laws of Oklahoma.

Protestant correctly maintains that liability does not attach by his simply being an officer of COMPANY but that he must be a principal officer of the corporation. A determination that an officer is a principal officer must be made on the specific facts and circumstances of each case.

When the Tax Commission has previously considered the issue of individual liability for sales taxes for officers, the Commission has looked to such factors as the officer’s involvement in the management and day-to-day operations of the business, the percentage of stock ownership, the degree of control or authority over the business, the check signing authority, and the purpose of the individual in accepting the officer position. Each case must be analyzed on its own set of facts and no one specific factor is determinative.

It is inconceivable that the Protestant, who was the President and sole stockholder of the corporation, and consequently had ultimate responsibility for and control of the company, could be anything less than a principal officer of the corporation. These particular circumstances far

outweigh the fact that he was not involved in the day-to-day operations of the business. Under Section 1361 of the Sales Tax Code, Protestant must be held individually liable for the collected yet unremitted sales taxes.

The conclusion that Protestant is a principal officer does not require a finding of embezzlement as Protestant contends. Civil liability is not determined by the same standards as criminal culpability, which requires willfulness, intent and wrongful appropriation. See Title 68 O.S. Supp. 1988, §1361(E). This is a civil proceeding.

CONCLUSIONS OF LAW

In view of the above and foregoing findings of fact and law applicable thereto, the undersigned Administrative Law Judge concludes as follows:

1. The Oklahoma Tax Commission has jurisdiction in this matter.
2. Title 68 O.S. Supp. 1988, §1361(A) imposes personal liability on each principal officer of a corporation for sales tax.
3. Title 68 O.S. Supp. 1988, §2385.3(d) imposes personal liability on any officer who is under a duty to act for the corporation to withhold and remit withholding taxes.
4. Protestant was a principal officer of COMPANY and was under a duty to act for the corporation to withhold and remit withholding taxes.
5. Protestant confessed his liability to the State for mixed beverage tax up to the amount of his surety bond, that being \$6,000.00.
6. The parties stipulated that the Protestant has no personal liability for the proposed assessment of franchise tax.

DISPOSITION

It is the ORDER of the OKLAHOMA TAX COMMISSION, based upon the specific facts and circumstances of this case, that the sales and withholding tax protest of PROTESTANT be denied.

OKLAHOMA TAX COMMISSION

CAVEAT: This decision was NOT deemed precedential by the Commission. This means that the legal conclusions are generally applicable or are limited in time and/or effect. Non-precedential decisions are not considered binding upon the Commission. Thus, similar issues may be determined on a case-by-case basis.