

Cite as Det. No. 94-090, 14 WTD 244 (1995).

BEFORE THE INTERPRETATION AND APPEALS DIVISION  
DEPARTMENT OF REVENUE  
STATE OF WASHINGTON

In the Matter of the Petition	)	<u>D E T E R M I N A T I O N</u>
For Correction of Assessment of	)	
	)	No. 94-090
	)	
. . .	)	Unregistered
	)	

- [1] RULE 217; RCW 82.32.145: SALES TAX -- CORPORATION -- LIABILITY OF INDIVIDUAL. A former corporate officer or other person who fails to pay collected sales tax to the Department may be held individually liable notwithstanding the fact that (s)he is no longer associated with the company at the time of its termination.
  
- [2] RULE 217; RCW 82.32.145: SALES TAX -- CORPORATION -- LIABILITY OF INDIVIDUAL -- TERMINATION OF BUSINESS -- WHAT CONSTITUTES -- BANKRUPTCY. A filing under Chapter 11 of the bankruptcy code does not constitute the termination, dissolution, or abandonment of a corporate business for the purpose of invoking individual sales tax liability.
  
- [4] RULE 217; RCW 82.32.145: SALES TAX -- CORPORATION -- LIABILITY OF INDIVIDUAL -- INTENT. The fact that a former corporate officer or other person responsible for remitting sales tax to the state intended that such delinquent taxes would be paid eventually does not relieve that person of individual liability.
  
- [5] RULE 217; RCW 82.32.145: SALES TAX -- CORPORATION -- LIABILITY OF INDIVIDUAL -- CIRCUMSTANCE BEYOND CONTROL. The fact that one party failed to perform an agreement to pay sales taxes on behalf of a second party is not a circumstance beyond the control of the second party so as to relieve the second party of individual liability for failure to pay sales taxes for a corporate taxpayer.
  
- [6] RULE 217; RCW 82.32.145: SALES TAX -- CORPORATION -- LIABILITY OF INDIVIDUAL -- CONTRACT TO PAY. A

contract, to which the Department is not a party, that one party shall pay sales tax to the Department in place of another, shall not affect the Department's ability to pursue whichever party it is otherwise authorized by law to pursue.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

#### NATURE OF ACTION:

Protest by former corporate officer of personal assessment for sales tax collected by his former company.<sup>1</sup>

#### FACTS:

Dressel, A.L.J. -- The taxpayer<sup>2</sup> is a former officer of a rental and sales company (the company). The Department of Revenue (Department) levied a tax assessment against taxpayer individually. The taxpayer appeals.

The assessment was made as a "Notice of Individual Corporate Liability" pursuant to RCW 82.32.145. It is alleged by the Department that while he was active as an owner and operator of the company, taxpayer collected retail sales tax from customers which he failed to pay over to the Department of Revenue. Per RCW 82.32.145, under certain prescribed circumstances, a company officer or employee may be accountable personally for sales tax not reported or paid to the Department.

While the taxpayer does not deny that sales tax was collected and not forwarded to the Department, he asserts that another person is the proper target for individual liability. The taxpayer explains that during the period for which tax was assessed against him, October 1987 through January 1988,<sup>3</sup> his business was

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<sup>1</sup>Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

<sup>2</sup> The assessment in this case was made against taxpayer-husband and taxpayer-wife as a marital community. While that is the technical entity that may or may not be liable for the appealed assessment, depending on the outcome of this determination, hereafter when we refer to "the taxpayer", we mean taxpayer-husband, as he appears to have been the community member who was active in the company.

<sup>3</sup> The four year statute of limitations for the assessment of taxes does not apply in a situation where retail sales tax was

in serious financial difficulty. As a consequence in February of 1988, he filed a Chapter 11 action with the United States Bankruptcy Court for the purpose of reorganizing the business. While this action was pending, he sold all of the stock in the corporation to a buyer (hereafter referred to as the "the purchaser"). The sale agreement was signed July 22, 1988, after which time the purchaser operated the business. In the contract, the purchaser agreed to pay any delinquent taxes of the corporation. The purchaser encountered financial difficulties as well, and, in the fall of 1990, filed for dissolution of the corporation under Chapter 7 of the bankruptcy code.

The taxpayer argues that the only party with individual corporate liability for sales tax is the purchaser of the company's stock. He was the person in control of the business at the time it was dissolved. He was also the person charged with filing tax returns and paying sales tax for the two year period from July 1988 to the fall of 1990. Moreover, he specifically agreed in the contract of sale to pay all delinquent taxes.

In addition, the taxpayer disagrees with a statement made by the Department's revenue officers that the Chapter 11 filing constitutes "abandonment" such that corporate officer liability is triggered under RCW 82.32.145. He asserts that the business operated continuously until the Chapter 7 filing in 1990. The taxpayer also argues that to be liable under RCW 82.32.145, the party charged with individual liability must have acted intentionally in not paying sales taxes to the state. He claims the fact the sale agreement provided that the purchaser would pay delinquent taxes evidences the former's intent that taxes would be paid. Finally, the taxpayer states that he should be excused from this liability because the fact that the buyer of his company did not pay the sales tax is a circumstance beyond his control.

#### ISSUE:

The issue is whether tax liability may be assessed against a former corporation principal for failure to pay collected sales tax to the Department, if that person had, subsequently, sold his stock in the corporation to another person and the sales contract provided the purchaser would pay all delinquent taxes.

#### DISCUSSION:

A special fiduciary duty is statutorily imposed on those businesses which collect retail sales tax from their customers. According to RCW 82.08.050, ". . . the [retail sales] tax required by this chapter, to be collected by the seller, shall be deemed to be held in trust by the seller until paid to the

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collected but not remitted to the Department. WAC 458-20-230, subsection (6).

department . . ." (Bracketed inclusion ours.) In those situations where a seller does not pay collected sales tax to the Department, certain individuals associated with that seller may be held personally liable for payment of the collected sales tax. In this regard, RCW 82.32.145 reads, in part:

Termination, dissolution, or abandonment of corporate business--Personal liability of person in control of collected sales tax funds.(1) Upon termination, dissolution, or abandonment of a corporate business, any officer or other person having control or supervision of retail sales tax funds collected and held in trust under RCW 82.08.050, or who is charged with the responsibility for the filing of returns or the payment of retail sales tax funds collected and held in trust under RCW 82.08.050, shall be personally liable for any unpaid taxes and interest and penalties on those taxes, if such officer or other person wilfully fails to pay or to cause to be paid any taxes due from the corporation pursuant to chapter 82.08 RCW . . .

For purposes of this subsection "wilfully fails to pay or to cause to be paid" means that the failure was the result of an intentional, conscious, and voluntary course of action.

(2) The officer or other person shall be liable only for taxes collected which became due during the period he or she had the control, supervision, responsibility, or duty to act for the corporation described in subsection (1) of this section, plus interest and penalties on those taxes.

(3) Persons liable under subsection (1) of this section are exempt from liability in situations where nonpayment of the retail sales tax funds held in trust is due to reasons beyond their control as determined by the department by rule.

[1] An examination of the first subsection is illuminating for the purpose of determining whether a former corporate officer may be held liable for sales taxes collected. Liability may be imposed against "any officer or other person." This language does not specify a current officer. The taxpayer, thus, is not specifically excluded on that basis. Liability may be imposed against "another person." Certainly, the taxpayer qualifies as "another person," whether or not he qualifies as an "officer."

The second subsection also sheds some light on the same issue. It states that an "officer or other person shall be liable only for taxes collected which became due during the period he or she had the control, supervision, responsibility, or duty to act for the corporation . . ." For the period at issue, the taxpayer was the only such person. Although the corporation had a manager for some time prior to that, the taxpayer acknowledges that the

taxpayer was the person in control and the one responsible for filing state tax returns from October 1987 through January 1988. The purchaser, on the other hand, had no connection with the company until July 22, 1988, well after the period in question. The subject taxes became due before the purchaser assumed control of the business.

There is a practical reason as well why the taxpayer is as culpable as the purchaser. The sales tax was collected during the time the former controlled the business. As indicated in RCW 82.08.050, it was to be held in trust until it was paid over to the Department. A trust deposit is "Where money or property is deposited to be kept intact and not commingled with other funds or property . . ." Black's Law Dictionary 1683 (revised 4th ed. 1968). There is no evidence that this was done. Certainly, if the tax was collected by the taxpayer's company, kept in a separate fund for payment to the Department, and was available to the purchaser for that purpose when he assumed control, the taxpayer would have advised us to that effect. He did not. We conclude that those funds were not available to the purchaser when he took over and that the taxpayer and/or his company had already spent the collected sales taxes for purposes other than payment to the state. The taxpayer violated his duty to hold the sales taxes collected in trust for the Department.

[2] We do agree with the taxpayer's point that the Chapter 11 bankruptcy filing was not "termination, dissolution, or abandonment" so as to trigger the individual liability provisions of RCW 82.32.145. Based on the information with which we have been furnished, the corporation continued to conduct business operations during and after the Chapter 11 filing in February of 1988. In fact, it did so, to the best of our knowledge, until the Chapter 7 filing in the fall of 1990. Neither was the corporation dissolved. Its stock was simply sold to another individual who continued to carry on the business until the Chapter 7 filing. Indeed, Chapter 11 contemplates a "reorganization" rather than a "termination, dissolution, or abandonment." Moreover, Chapter 11 proceedings are inconsistent with the definitions of those three terms as they appear in the regulation which implements RCW 82.32.145, WAC 458-20-217 (Rule 217).<sup>4</sup> Collectively, those definitions contemplate a complete cessation of business operations and a winding up of corporate affairs.

[1] Chapter 7, however, is another matter. A filing of same is the precursor to complete liquidation of a business.<sup>5</sup> This is

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<sup>4</sup> See Rule 217(6)(c)(iii)-(v).

<sup>5</sup> See Rule 217(6)(c)(iii), regarding the definition of "termination."

the event that triggered RCW 82.32.145. As per the above discussion, though, its application is not limited to the officers or other persons in control at the time of "termination, dissolution, or abandonment." It is our holding that "individual corporate liability" may be asserted against whomever was in charge of filing and paying collected sales taxes to the Department from the time those taxes were collected until they were due and payable to the Department. As stated earlier, those funds are deemed to be held in trust. Any person who violates that trust may be held personally accountable under RCW 82.32.145 whether or not (s)he is still associated with the taxpayer at the time of "termination, dissolution, or abandonment."

A person does not cut off that liability by leaving the corporation. If (s)he could do that, (s)he could quit the day before the filing of a Chapter 7, for instance, and contend that (s)he was not the person responsible for sales tax at the time of termination and, therefore, no individual tax liability may be assessed against her or him. Or, that person could be reassigned to another job within the company the day before Chapter 7 and make the same legal argument. We doubt the legislature intended that the provisions of RCW 82.32.145 could be so easily avoided. Statutes are to be interpreted in such a way as to avoid an absurd result. Yakima First Baptist Homes v. Gray, 82 Wn.2d 295 (1973). Our construction of the RCW 82.32.145 here does just that.

[4] As an additional argument, the taxpayer contends that because the contract for the sale of the corporation required the buyer to pay all taxes for which the taxpayer was liable, the latter's failure to pay was not "intentional, conscious, and voluntary", as required by RCW 82.32.145. While it is laudable that the taxpayer had such a clause inserted into the sale agreement, that action does not vitiate his individual liability. The statute applies if there is an intentional failure to pay collected sales taxes timely. The taxpayer is not relieved of liability if he intended that the tax debt be paid eventually. In Determination 91-173, 11 WTD 215 (1991), a taxpayer contended that he did not intend to evade the payment of taxes because he hoped that, eventually, he would be in a financial position to pay them. We held that, for purposes of applying the evasion penalty, even if the taxpayer intended to evade on only a temporary basis, he intended to evade. Even though here we are construing a different statute, we perceive no good reason to deviate from that line of reasoning. The taxpayer intentionally, consciously, and voluntarily converted sales taxes, which should have been held in trust on the state's behalf, to his own

purposes or the purposes of his corporation.<sup>6</sup> The fact that he intended that the delinquent taxes eventually be paid by the buyer of the corporate stock does not relieve the taxpayer of his own individual liability under RCW 82.32.145.

[5] Lastly, the taxpayer asserts the fact that the buyer of his company did not pay the delinquent sales taxes in accordance with the sale agreement is a circumstance beyond the taxpayer's control such that he should be relieved of liability under RCW 82.32.145(3). Again, intent to pay timely is the key. The taxpayer did have complete control over timely payment and failed to make it. Furthermore, the taxpayer did not exercise good faith in collecting and holding the sales tax funds in trust. See Rule 217(6)(h). The buyer's non-payment did not affect timely payment. It is not a circumstance which relieves the taxpayer of his individual liability.

[6] While it is unfortunate that the buyer did not live up to his agreement to pay the delinquent tax, it is important to notice that the Department was not a party to that agreement. It is not bound by that agreement. It is free to pursue whichever party it is authorized by law to pursue. Based on RCW 82.32.145, the taxpayer is such a party. The fact that the buyer may have breached its contract with the taxpayer's company is a matter between those two parties. The Department is not required to suffer a loss as the result of the buyer's nonfeasance.

#### DECISION AND DISPOSITION:

The taxpayer's petition is denied. This matter is remanded to the Compliance Division for collection.

DATED this 31st day of May, 1994.

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<sup>6</sup> When asked at the hearing of this matter, what was done with the collected sales taxes, the taxpayer's representative said he didn't know.