

STATE OF CALIFORNIA  
BOARD OF EQUALIZATION

535.0003

In the Matter of the Claim for )  
Refund of State and Local Sales ) DECISION AND RECOMMENDATION  
Tax; )  
)  
U--- S--- CORPORATION )  
OF AMERICA, dba P--- ) No. SR -- XX XXXXXX  
M--- H---, )  
)  
Claimant )

The above-entitled matter came on regularly for hearing on Monday, November 29, 1976 in San Diego, California. Robert H. Anderson, Hearing Officer.

Appearing for Claimant:

Mr. V--- E. R---, Attorney at Law  
--- & ---

Mr. E. R--- T---, Attorney at Law  
--- & ---

Mr. A--- E. W---, former president  
U--- S--- Corporation of America

Mr. F--- H. G---, President  
U--- S--- Corporation of America

Appearing for the Board:

Mr. John E. Johnson, Audit Supervisor  
San Diego District

Mr. Ray C. Sanborn, Collections  
San Diego District

Protest

Pursuant to an audit covering the period from 10-01-71 through 202-28-74, and a determination issued on December 3, 1974 against G--- D---, J---. doing business as G--- D--- & Associates (SR -- XX XXXXXX) claimant protests the assessment of tax, interest and penalty as successor to G--- D--- & Associates business.

Tax, interest and penalty in the amount of \$7,830.77 was paid with a \$5,000 surety bond and \$2,830.77 cash. Claimant claims a refund of \$7,836.77.

Contentions

Claimant contends it is not a successor to the G--- D--- business because it did not purchase the business.

Summary

G--- D--- & Associates commenced business under a permit issued to Mr. D--- as an individual proprietor to sell mobile homes. The permit was issued on 11-20-70. In late 1974 an audit was made of the business using only Mr. D---' income tax returns for 1971 and 1972 as no records were available to audit, and Mr. D--- could not be located. Mr. D---' account was secured by a \$5,000 surety bond with the American Bonding Company.

The original audit was dated October 7, 1974, and a determination was issued against Mr. D--- on December 3, 1974 for the following:

<u>Tax</u>	<u>Interest</u>	<u>Penalty</u>	<u>Total</u>
\$13,281.34	\$1,017.71	\$1,382.14	\$16,221.19

No payment on the assessment was made, and no petition was timely filed so an additional penalty of 10 percent for failure to pay the assessment was added to the penalty for negligence.

Mr. D--- was ultimately located through collection proceedings and records were produced in May or June 1975. A reaudit was made using those records and some Department of Motor Vehicle records which resulted in an adjustment to the measure of tax from \$274,981 down to \$186,919.

The original audited tax was reduced by \$4,337.83. There was a payment of \$100 on 5-14-75 and a payment by the American Bonding Company on 1-15-76 (G--- D--- Bond No. XXXX) that also reduced the tax that was assessed on the December 3, 1974 determination.

The reaudited tax liability was \$9,483.51; this automatically reduced the penalty for negligence to \$948.36 and the penalty for failure to make a timely payment or petition to \$948.36. Thus, the penalty was adjusted to \$1,896.72.

Interest was recomputed in accordance with the adjusted tax liability, and when claimant came into the picture as a successor, the total amount of tax, interest and penalty remaining was \$7,836.77. As noted, a bond put up by Mr. W--- as security for U--- S--- Corporation's permit was used to cover part of the assessment against claimant, and with the cash payment of \$2,830.77, the balance was reduced to \$6.00. Since the claim for refund was for the amount due and not the amount actually paid, the claim is for \$6.00 more than has been paid.

On June 5, 1973 U--- S--- Corporation of America obtained a seller's permit to sell mobile homes in the City of ---. Mr. D--- was operating his business in nearby --- --- out of a retail sales lot at XXX --- --- Road which he was renting.

Shortly after commencing business in ---, U--- S--- Corporation decided to expand its operations and open a second location in another city. They heard about G--- D--- and learned that he was contemplating closing his business so they contacted him about it with the idea that they might take over his location in lieu of opening a new one in --- ---.

On January 22, 1974 they entered into a "purchase and sales agreement" with Mr. D--- to purchase his (1) supplies, (2) inventory, (3) furniture, (4) office equipment, and (5) miscellaneous items. Exhibit A is a copy of the agreement with a detail schedule of the items purchased.

The consideration recited in the agreement consisted of the following:

1. Assumption of Mr. D---' liability to K--- M--- A--- Co. not to exceed \$6,270.20 which was what D--- owed K--- M---.
2. Assumption of Mr. D---' liability on his purchase of an office unit in the amount of \$2,203.28 financed at the Bank of America.
3. Miscellaneous bills not to exceed \$1,290.25 for phone, lights and carpet were also assumed.
4. The assumption of flooring on five mobile homes and two furniture packs (see schedule B of Exhibit A).

The lease on the property occupied by Mr. D--- was allegedly expired or was about to expire so U--- S--- principals allegedly contacted the owner of the property and negotiated a new lease under which they occupied the retail sales lot formerly operated by Mr. D---.

U--- S--- operated the sales lot until November of 1974 when they sold out to a J--- W--- and M--- D---, thereby ceasing all their operations out of --- ---.

It is contended that U--- S--- did not purchase Mr. D---' business, and they point out that the purchase and sales agreement expressly provides that "this is not a purchase of a business, but consists entirely of a purchase between buyer and seller of merchandise, parts, inventory, for proper consideration."

Mr. W--- and Mr. G--- contend that they had no intention of buying Mr. D---' business; they say that they could have occupied another location in --- ---, but decided to take over D---' place because he was closing and his assets were available. Further, at the time they thought it would be less expensive than moving on to a lot that had not been a mobile home sales location. They point out the following as evidence that the transaction was not the purchase of a business:

1. They did not assume or take over the lease under which D--- operated.
2. They did not retain or use D---' business name, phone number or permits and licenses under which he operated, and did not acquire any goodwill.
3. They opened new accounts for utilities and a telephone.
4. They moved the office building they purchased and replaced it with another one.
5. They did not acquire any accounts receivable and did not assume any liabilities relating to warranties on mobile homes that D--- had previously sold. On this point, it is alleged that a few customers called at the --- --- sales lot looking for Mr. D--- in respect to warranties and service on homes they had purchased from D---. The customers were allegedly told that their problems were D---' responsibility and were advised where they could reach him.
6. They contended that the five mobile homes they acquired for resale was not the entire inventory of Mr. D--- as he retained a few which he delivered after U--- S--- took over the lot because he, D---, had taken deposits on them and therefore completed the sales on his own after U--- S--- moved on to the lot.
7. They did not receive any assignment of Mr. D---' dealer reserve account with the Bank of America or any other bank.
8. They used their own Department of Motor Vehicles license to operate in --- ---.
9. They did not utilize any signs, marks, marques, logos, etc., that would identify them with Mr. D---' business operations. However, it is noted that there was a sign on the premises that read "Mobile Homes" which remained where it had been when D--- operated the lot.
10. Mr. D--- did not agree to any covenant not to compete and could have opened up another sales lot immediately and as close as possible to the --- --- address if he had wanted to and U--- S--- could not have done anything about it.

Mr. Ramirez contends that the total consideration paid was \$6,267.20 notwithstanding the consideration recited in the agreement. He referred to a copy of the promissory note (Exhibit B) relating to the assumption of the K--- M--- A--- liability as evidence of this. Payments to K--- M--- were made directly to that firm pursuant to the note.

Accordingly, it is contended that, assuming it is concluded that U--- S--- is a successor, the maximum liability as a successor would be no more than \$6,267.20.

In addition, Mr. G--- believes that D--- may have already gone out of business when he was contacted about the sale since he was rarely open when they tried to talk to him about the purchase.

However, the point was made, to emphasize that they did not purchase Mr. D---' business, that D--- made some sales after U--- S--- took over. These were allegedly to customers who had made deposits on mobile homes prior to U--- S--- coming into the picture.

The record discloses that Mr. D--- was reporting his sales on a monthly basis and was filing returns monthly. The last return he filed was for the month of February, and with it, he reported no sales. He reported no sales in January either. The State Board of Equalization was notified by American Bonding Company on January 29, 1974 that Mr. D---' bond was canceled effective thirty days after receipt of the notice. The Board's records disclose the bond was canceled effective March 2, 1974.

Mr. R--- also contends that Mr. D--- still has assets that can be reached and that the State should have gone after them first. He contended that Mr. D--- has a dealer reserve account with the Bank of America, --- --- branch, that should contain more than enough to cover the \$7,836.77 that he is primarily liable for. In addition, he mentioned other assets believed to be owned by Mr. D---.

The bank was contacted regarding Mr. D---' dealer reserve account and a notice to withhold was sent to them; they responded on December 2 as follows:

The bank has the right to charge the Dealer Participation account for any past due indebtedness of the seller to the bank.

There are four unpaid contracts yet to be paid out by the buyers, plus the balance owed our bank on a direct basis by the seller, G--- D---, Jr. The total involved will more than absorb all of the funds available in the Dealer Participation account, therefore there is no surplus available for assignment.

It is to be noted that collection efforts against Mr. D--- were made at the outset and over \$5,000 was obtained as a result.

Mr. R--- cites Knudsen Dairy Products Company v. State Board of Equalization (1970) 12 Cal. App. 3d 47, as authority for establishing the successorship or nonsuccessorship of a business. He points out that the court indicated:

1. Tax laws are to be strictly construed in favor of the taxpayer, especially where statutes seeks to impose tax liability of one person on another in order to facilitate its collection.

2. Where a debtor transferred all of its operating assets to taxpayer at creditor's direction, and where taxpayer, in turn, issues a promissory note...so that creditor then credited debtor in the amount of value of assets transferred, taxpayer was a "successor" of debtor's business within the statute requiring a successor to withhold amount of seller's sales and use tax liability from the purchase price.
3. "Where seller of business does not receive a purchase price, from which purchaser can withhold amount of seller's sales and use tax liability, purchaser cannot protect State's interests, and, therefore, cannot be held liable for amount of tax by his failure to withhold same."

### Conclusions

The primary issue in this matter is whether, upon execution of the purchase and sales agreement, U--- S--- did become a successor to Mr. D---' business. The statutes (sections 6811 and 6812) do not expressly define "successor" nor do they spell out what constitutes the "sale of a business". There merely create the authority for holding a successor liable for tax owed by the predecessor if certain conditions are met.

Section 6811 must be read in conjunction with 6812. Section 6811 provides:

If any person liable for any amount under this part (Mr. D--- in this case) sells his business or stock of goods or quits the business, his successors or assigns shall withhold sufficient of the purchase price to cover such amount until the former owner produces a receipt from the board showing that it has been paid or a certificate showing that no amount is due.

Mr. D--- had a business and he sold everything relating to it to U--- S--- including his remaining stock of goods according to the schedule in Exhibit A.

The court, in People v. Gabriel (1943) 57 Cal. App. 2d 788, held that where a person closed his business and walked away in the fall of one year and came back and sold the business assets the spring of the following year, there was no successor to the business as there was no business since it had been closed for such a substantial period of time. This is not the case in the sale by Mr. D--- to U--- S---.

The statute does not require a successor to keep the same business name, the same phone number, operate on the same lot, assume the accounts receivable, use the predecessor's business licenses and permits, take over the predecessor's bank accounts, etc., in order to be a successor of a business.

In this case there may not have been any goodwill to acquire; nonetheless whatever there was U--- S--- acquired it by reason of its continued operation at the same location on which Mr. D--- had been operating for over three years. They acquired the business location and it makes no difference whether they were assigned D---' rights under his lease or negotiated a new lease.

A person could purchase another's business, close it down, dispose of all the assets and never operate it and still be a successor for purposes of sections 6811 and 6812.

When Mr. D--- completed his transaction with U--- S--- he had no business, no business assets and no stock of goods. Still there was a business at the same location and it included inventory that Mr. D--- had been holding for sale plus much of the capital assets needed to operate his business. U--- S--- purchased it and became the successor.

The statement on the purchase agreement that U--- S--- was not purchasing a business is nothing more than an opinion. It does not negate the fact that the business was purchased if, in fact, the business was sold.

U--- S--- no doubt tried to arrange the acquisition of the assets and the inventory in a way that it would not wind up with any of the responsibility for warranties on sales that were made by Mr. D---, and it probably did, but that fact does not negate the possibility that the business could still be sold. The assumption of warranties is not a prerequisite to the sale of a business.

The sale of a business can include many things such as accounts receivable, customer lists, goodwill trade names and secrets, operating assets, etc., but it does not have to include all or any of them to still be a sale of a business. However, it must include the sale of the inventory held for sale. Here, there was a sale of inventory plus other assets coupled with the seller no longer operating a business. U--- purchased the inventory, took over the location and continued operations, which makes it a successor.

The court in Knudsen Dairy Products (supra) said that it appears that while the Legislature in section 6811 speaks of successors and assigns they limit the definition of a successor or an assignee to a "purchaser" by the use of that phrase in section 6812.

The Board recognizes that where the seller did not receive a purchase price from which a withholding of sales or use tax could be made the purchaser cannot protect the State's interest and therefore cannot be held liable. This would include assignments for benefit of creditors, foreclosures of mortgages or sales by trustees in bankruptcy.

The Court interpreted sections 6811 and 6812 to require that for a successor or assign to become personally liable for the tax liability of another, such successor must also be a purchaser who, through the handling of the purchase price or the form thereof, was in a position to protect the State's interest in collecting taxes which were due and owing.

U--- S--- was a "purchaser". There was a purchase price, and it was the amounts of liability that were assumed. According to the purchase agreement schedule, the total of the amounts assumed was greater than the balance of tax due which was assessed against U--- as successor.

Regulation 1702 was adopted by the Board to implement the administration of sections 6811 and 6812. Subsection (a) contains the provisions relating to "when the duty to withhold a purchase price arises". It reads as follows:

The requirement that a successor or purchaser of a business or stock of goods withhold sufficient of the purchase price to cover the tax liability of the seller, arises only in the case of the purchase and sale of a business or stock of goods under a contract providing for the payment to the seller or person designated by him of a purchase price in money or property or providing for the assumption of liabilities and only to the extent thereof, and does not arise in connection with other transfers of a business such as assignments for the benefit of creditors, foreclosures of mortgages, or sales by trustees in bankruptcy.

U--- S--- could have assumed less liabilities than it did and used the difference to pay Mr. D---' tax liability. Thus, as a successor, U--- S--- was personally liable for the tax.

Recommendation

Redetermine without any adjustment. Claim for refund be denied

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Robert H. Anderson, Hearing Officer

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DEC 23, 1976

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Date