Corporate Officer Liability and Related Issues in Georgia

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Introduction

Georgia, like most other states, has a statutory provision in its sales tax law that creates a personal liability for business officers, owners, and employees when sales tax has not been remitted to the Georgia Department of Revenue. This is often referred to as a "responsible person" liability. As the economy continues to remain soft and as tax collections plummet, many small business owners are growing concerned about their own personal liability for any sales tax liability that may be found owing to the state of Georgia. In this article, I will outline the general provisions of Georgia's rules with respect to officer liability and successor liability. While these provisions are different, they are often closely related and one can often turn into the other, as I will detail below.

Officer Liability

Georgia Tax Code at Section 48-2-52 states:

> (a) Any officer or employee of any corporation, any member, manager, or employee of any limited liability company, or any partner or employee of any limited liability partnership who has control or supervision of **collecting from purchasers** or others amounts required under this title or of collecting from employees any taxes required under this title, and of accounting for and paying over the amounts or taxes to the commissioner, and who **willfully fails** to collect the amounts or taxes or truthfully to account for and pay over the amounts or taxes to the commissioner, or who **willfully attempts** to evade or defeat any obligation imposed under this title, shall be **personally liable** for an amount equal to the amount evaded, not collected, not accounted for, or not paid over. (Emphasis added)
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> (b) The liability imposed by this Code section shall be paid upon notice and demand by the commissioner or his delegate and shall be assessed and collected in the same manner as the tax in connection with which the act or failure to act under this Code section occurs or has occurred.

These provisions can and should strike terror in the hearts of any business owner, officer, or employee who has the responsibility for collecting and remitting sales tax in the state of Georgia. The statute above is relatively unchanged since it was first codified in 1960. The statute embraces several categories of employees and officers who can be personally liable for the tax. These categories include:

1. Those having control or supervision of collecting sales tax from purchasers, or

2. Those having control or supervision of collecting withholding tax from employees, AND
3. Willfully fails to collect the taxes due, or
4. Willfully fails to remit the taxes collected to the Department of Revenue, or
5. Willfully attempts to evade or defeat ANY obligation imposed under the sales tax title.

Several conclusions can be reached by a careful reading of this statute. First, personal liability only exists for sales tax and does not exist for consumer use tax. As such, if your business failed to pay tax on purchases it made from an out-of-state business, the state could only hold the business liable for the payment of the tax and could not look to the officers or other responsible parties for the tax. This is not to say that the DOR could not impose significant pressure (including asset forfeiture and sale) to get the money they are due. The other major conclusion to be reached is that the personal liability only exists if there is "willful" intent to not collect the tax or not to pay the tax collected. We will explore this concept in more detail below.

What does "Willfully" Mean?

There is not a great deal of Georgia law on this particular subject matter. The only significant court case dates back to 1971. In *Blackmon vs. Mazo and Friedman*, GA Ct. of Appl. No. 46178 (11-1-1971) the Court determined that the term 'willful" means more than just bad motives, fraud, or an intend to deprive the state its tax revenue. In the *Mazo* case, the two officers directed that over $24,000 of cash be transferred to another creditor after a sales tax liability had been determined and assessed against their organization. This payment was made with the full knowledge and approval of the officers involved. Based on this fact, the Court determined that the officers were personally liable for the $24,788 of sales tax liability that was owed at the time of the transfer to the other creditors. The preferential transfer was deemed by the Court to be a "willful" attempt to evade or defeat the tax obligation.

The mere holding of a corporate office does not, in and of itself, automatically make that officer potentially liable for unpaid or unremitted tax. That officer must first have control or supervision of the tax and the failure to pay the tax must be willful. If a person knows or should know that sales tax are due and makes a conscience decision to pay other creditors or to not attempt to collect the tax, then the actions could be deemed as willful. Further, in *Kalb v. United States*, 505 F. 2d 506 (2nd Cir. 1974) the Court held that "willful" conduct included the failure to investigate or correct mismanagement after having notice that taxes have not been remitted to the government. This case has not been adopted by any Georgia court, but the theory certainly exists and could be used by the state to impose this penalty.

In addition, many courts have concluded that the "willfulness" requirement will be found if the responsible officer or employee demonstrates a reckless disregard of a known or obvious risk that trust funds may not be remitted to the government (*Thibodeau v. United States*, 828 F. 2d at 1505).

The officer or employee liability outlined above is a "joint and several" tax liability. That is, each affected officer and each affected employee is equally responsible for the taxes due and the state can pursue the full liability against each party until the debt is satisfied. There is no such thing a "proportionate" or limited liability for this tax. However, it does appear that officers and employees can only be personally liable only for the tax liability created during their time as an officer or as an employee. As such, if problems arise before or following your employment with the company it is unlikely that any liability could be assigned to you. If problems were created during your employment and you had control or supervision of the sales tax while you were employed, it may still be possible for you to be personally liable if it can be shown that your behavior met the standards for willful intent.

Successor Liability

Another area of surprise for businesses is that of "successor" liability. This provision is outlined below and is found in Georgia Code Section 48-8-46.

> If any dealer liable for any tax, interest, or penalty imposed by this article sells out his business or **stock of goods or equipment** or quits the business, he shall make a final return and payment within 15 days after the date of selling or quitting the business. The dealer's successor or assigns, if any, shall withhold a sufficient amount of the purchase money to cover the amount of the taxes, interest, and penalties due and unpaid until the former owner produces either a receipt from the commissioner showing that the taxes, interest, and penalties have been paid or a certificate from the commissioner stating that no sales and use taxes, interest, or penalties are due. **If the purchaser of a business or stock of goods or equipment fails to withhold the purchase money as required by this Code section, he shall be personally liable for the payment of any sales and use taxes, interest, and penalties accruing and unpaid by any former owner or assignor.** The personal liability of the purchaser in such a case shall not exceed the amount of the total purchase money, but the property being transferred shall in all cases be subject to the full amount of the tax lien arising from the delinquencies of the former owner. (Emphasis added)

This provision may be the most widely ignored or misunderstood provision of Georgia sales tax. In fact, this provision exists in one fashion or another in almost every state that has a sales tax. For federal tax planning and corporate liability purposes, asset sales are preferred because the federal tax and other liabilities stay with the seller's legal organization. In a stock transaction, these liabilities will follow the

stock and become the liability of the new owner. For sales tax purposes, however, an asset transfer or sale is treated exactly the same way as a stock transaction with regard to the liability going to the purchaser. Unless the purchaser withholds an amount of the estimated sales tax and waits for the seller to provide some certificate of "no tax due", then the purchaser becomes liable for all of the sales tax owed by the seller. The liability is for the disclosed and the undisclosed sales and use tax due.

This provision, and others similar to it, has created significant problems for purchasers of assets from other businesses. It is a vital that sufficient due diligence be performed on any transaction where the seller is a retailer of property or has operations in multiple states. In many cases, the liability assumed by the purchaser has been larger than the purchase price of the business. The Georgia law limits the liability to the purchase price of the business. However, not every state has that provision. Most states have no limitation or allocation of liability. In some states, a purchaser who only buys 15 percent of the assets of a company could be held liable for 100 percent of the sales tax liability of the company at the time the assets were purchased. This is a very harsh penalty but not at all uncommon. If you are considering the purchase of any assets of a business make sure to conduct sufficient "due diligence" before that sale is completed. Make sure you know and follow the Georgia law.