

PRESENTED AT
64th Annual Taxation Conference and
2016 Stanley Johanson Estate Planning Workshop

November 30 – December 1, 2016
Austin, Texas

Personal Liability for
Tax Assessments of a Business

Jimmy Martens

Author Contact Information:
Jimmy Martens and Katie Wolters
Martens, Todd, Leonard, Taylor & Ahlrich
Austin, Texas

jmartens@textaxlaw.com
512-542-9898

Jimmy Martens
Martens, Todd, Leonard, Taylor & Ahlrich
301 Congress Ave., Ste. 1950
Austin, TX 78701

(512) 542-9898
jmartens@textaxlaw.com

BACKGROUND, EDUCATION AND PRACTICE

Jimmy Martens, trial and appellate attorney, is the founding partner of Martens, Todd, Leonard, Taylor & Ahlrich, a boutique tax litigation law firm located in downtown Austin, Texas. Mr. Martens has handled the trial of tax cases and related appeals all the way through both the Texas Supreme Court and the U.S. Supreme Court.

His recent Texas Supreme Court cases include: *Combs v. Roark Amusement & Vending, L.P.*, 422 S.W.3d 632 (Tex. 2013); *In Re: AllCat Claim Service, L.P.*, 356 S.W.3d 455 (Tex. 2011); and *Titan Transportation, L.P. v. Combs*, 433 S.W.3d 625 (Tex. App. – Austin, 2014, pet. denied).

His recent appellate cases include: *Combs v. Newpark Resources, Inc.*, 422 S.W.3d 46 (Tex. App.—Austin 2013, no pet.); *Hegar v. CGG Veritas Services (U.S.), Inc.*, 2016 Tex. App. LEXIS 2439 (Tex. App.—Austin Mar. 9, 2016, no pet.); *Graphic Packaging Corp. v. Hegar*, 471 S.W.3d 138 (Tex. App.—Austin 2015, pet. filed); and *Gulf Copper & Mfg. Corp. v. Hegar*, No. D-1-GN-14-004620 (53rd Dist. Ct., Travis County, Tex. Feb. 22, 2016), pet. filed, No. 03-16-00250-CV.

He limits his law practice to Texas tax and multi-state tax controversies and litigation. He is board certified by the Texas Board of Legal Specialization in Tax Law.

Mr. Martens is a former council member of the Tax Section for the State Bar of Texas and the former chair of the CLE Committee. He is also a CPA and teaches for the Texas Society of CPA's statewide courses on Texas franchise and sales tax. Mr. Martens received his B.B.A. and J.D. from The University of Texas at Austin, both with honors.

Table of Contents

I.	Is Mr. Moore Personally Liable for the Corporation's Tax Assessment?	1
II.	Challenging the Underlying Assessment	2
III.	Franchise Tax Reporting and Payment Failures.....	2
IV.	Failing to Pay Over Collected Taxes.....	7
V.	Intentionally Failing to File a Report, Substantially Understating Tax & Records Misconduct	12
VI.	Contributing to Tax Evasion	13
VII.	Successor Liability	15
VIII.	Fraudulent Transfer of a Business.....	17
IX.	Bankruptcy Trustee Liability.....	19
X.	Criminal Penalties	19
XI.	Civil Penalties.....	20
XII.	Ethics: Representing a Corporate Entity.....	21

I. Is Mr. Moore Personally Liable for the Corporation's Tax Assessment?

Bill Moore walks into your office and hires you to defend a lawsuit. The State of Texas has sued him personally, seeking to recover over \$500,000 in sales taxes, penalties, and interest supposedly owed by Coastal Furnishings, Inc., a corporation for which he served as CFO. The now-defunct corporation sold specialty furniture until it closed its doors at the end of 2010 and filed for bankruptcy. You read the assessment certificate attached to the State's petition and learn that the sales tax liability period spanned 2011-2014, which is *after* the business closed its doors.

Further, you find a letter from the State dated July 1, 2011, notifying Coastal Furnishings of its failure to file its 2011 Texas franchise tax report. Upon further investigation, you learn that Coastal Furnishings failed to file its 2011 report when due on May 15, 2011. The bankruptcy trustee filed the report exactly one year later.

You file an Open Records Act request and learn that in 2015, the Comptroller's auditor went to Coastal Furnishings' former location and saw that the business was gone. Following agency procedure, the auditor created an estimated assessment under which the auditor multiplied Coastal Furnishings' highest monthly sales by 120%. The highest monthly sales occurred in September of 2009, when business was booming. It was easy for the auditor to find this amount because it was shown on Coastal Furnishings' sales tax report that it filed for September of 2009.

The auditor then presumed that this level of sales had occurred each month of the three-year period spanning 2011-2014. The auditor further assumed that Coastal Furnishings had collected taxes at 8.25% on these estimated sales and failed to pay them over to the Comptroller. The auditor prepared an assessment notice for \$500,000: \$300,000 sales tax, \$150,000 penalty (for failing to pay the \$300,000 to the Comptroller) and another \$50,000 interest. The auditor then mailed the assessment notice to Coastal Furnishings' former location, as required by the rules.

Since no one was there to receive the assessment notice, the 30-day period for challenging it lapsed. The assessment became final against Coastal Furnishings. When the Comptroller realized that both Coastal Furnishings' assets and shareholders were gone, the State filed suit against Mr. Moore demanding that he personally pay the full \$500,000 plus attorney's fees.

Unfortunately, this fact pattern is all too common. The Comptroller has several grants of statutory authority to impose personal liability for Texas sales and use tax otherwise owed by a business. This paper addresses the most common statutory vehicles for personal state tax liability, including those relevant to Mr. Moore.

II. Challenging the Underlying Assessment

A taxpayer cannot directly lower a delinquent corporate tax assessment by presenting proof that taxes are not owed.¹ However, our firm has found that the state's attorneys will often consider the defendant's evidence on this point. In one recent case, we were able to show that the alleged tax liability had, in fact, been fully paid by another individual. As a result, the state's attorney agreed to remove the assessment.

Moreover, as we discuss below, challenges to the underlying assessment are available as a defense to some of the laws invoked to impose personal liability.

Statute of Limitations. In general, the Comptroller has four years from the date a tax becomes due and payable to assess a deficiency tax liability.²

However, the statute of limitations does not apply if:³

- The taxpayer files a false or fraudulent sales tax return with the intent to evade the tax;
- The taxpayer fails to file a sales tax return; or
- The taxpayer files a sales tax return that has gross error.

In these three circumstances, the Comptroller may assess and collect taxes, penalties, and interest against a taxpayer at *any time*- even if a business has ceased operations.

III. Franchise Tax Reporting and Payment Failures.

Corporate officers, directors, managing members of LLCs, and others may become personally liable for the debts of a corporation, including taxes, in several circumstances. The same is true for managing members of LLCs and other persons serving in similar capacities for other types of business entities.⁴

Types of Entities. The Texas Tax Code defines a "taxable entity" broadly, extending the list of entities that could forfeit privileges to include partnerships, limited liability partnerships, corporations, banking corporations, savings and loan associations, limited liability companies,

¹ Comptroller Hearing No. 105,174 (STAR No. 201308771H) (August 29, 2013) (Petitioner's redetermination hearing is limited to issues of personal liability).

² 34 Tex. Admin Code § 3.339(a)(1).

³ 34 Tex. Admin Code § 3.339(a)(2) ("Gross Error" exists when the amount of tax due and payable, after the correction of error, exceeds the amount of tax reported on the return by at least 25%).

⁴ Tex. Tax Code § 171.2515.

Find the full text of this and thousands of other resources from leading experts in dozens of legal practice areas in the [UT Law CLE eLibrary \(utcle.org/elibrary\)](http://utcle.org/elibrary)

Title search: Personal Liability for Tax Assessments of a Business

Also available as part of the eCourse

[2016 Hot Topics in Tax Law: 385 Regulations, Goodwill, Personal Liability, Cancellation of Debt, and Family Limited Partnerships](#)

First appeared as part of the conference materials for the
64th Annual Taxation Conference session
"Personal Liability for Corporate Tax Assessments"