

IN THE OREGON TAX COURT
MAGISTRATE DIVISION
Withholding Tax

JAMES GARDNER,)	
)	
Plaintiff,)	TC-MD 011051C (Control)
)	
v.)	
)	
DEPARTMENT OF REVENUE,)	
State of Oregon,)	
)	
Defendant.)	
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)	
ALICE RANDALL,)	
)	
Plaintiff,)	TC-MD 011052C
)	
v.)	
)	
DEPARTMENT OF REVENUE,)	
State of Oregon,)	
)	
Defendant.)	DECISION

Plaintiffs appeal from Defendant’s (the department) conference decision finding them personally liable for unpaid withholding taxes. Trial in the matter was held January 13, 2004, in the courtroom of the Oregon Tax Court. Dale H. Schofield, attorney at law, appeared on behalf of Plaintiffs. Jerry Bronner, Assistant Attorney General, appeared on behalf of the department.

I. STATEMENT OF FACTS

Plaintiffs are James Gardner (Gardner), owner and president, and Alice Randall (Randall), controller/comptroller, of Electro Mech Technology, Inc. (EMT). Gardner and Randall were at one time married to each other and, although the marriage lasted only a few years, they remained close after the divorce. Randall is a real estate broker and was the listing agent for the sale of EMT, a circuit board company originally located in Beaverton, Oregon.

Randall made Gardner aware of the business opportunity that EMT presented. Gardner resides on Lopez Island, outside Seattle, Washington. Gardner and a corporation with which he is affiliated, J. Gardner and J. Gardner, purchased EMT in mid-1994. Randall helped Gardner obtain financing for the purchase. Payroll began in July 1994. EMT continued to manufacture circuit boards after the acquisition, but operations were moved from Beaverton to Wilsonville.

An organizational meeting was held May 7, 1994. Gardner testified that he and Randall were the only individuals at that meeting. His testimony is supported by minutes from the meeting, which show that Gardner was appointed secretary and, following nominations by the "chairman," the directors voted Gardner as president/chairman and secretary, and Randall as agent and comptroller. Randall's written job description, discussed below, identifies her as the controller/comptroller. Gardner was registered with the Oregon Secretary of State's office as the "agent," "president," and "secretary." (Def's Ex BB.) James Kuehn (Kuehn) was nominated vice-president/CEO.

Kuehn was hired because of his technical industry knowledge. Randall recruited Kuehn and held an initial interview, or at least met with him, before Kuehn was introduced to Gardner. Gardner hired Kuehn after meeting with him on two separate occasions. It appears that Kuehn was the only employee hired by Gardner. Kuehn oversaw the day-to-day operations at the plant, and worked at EMT from July 1994 to April 1996. Kuehn and another employee were primarily responsible for plant management and production and Kuehn also handled sales.

Gardner and Randall were rarely at the plant. Gardner was nearly 300 miles away on Lopez Island, and Randall worked as a real estate broker from an office in Portland roughly 30 miles from the plant.¹ Randall's Portland office was established as the official corporate address.

¹ Based on information from an Internet mapping program called MapQuest.

Two signatures were required on every check written by EMT. Gardner, Randall, and Kuehn were the only individuals with authority to sign checks. Gardner signed many checks, including those to vendors, employees, and state and federal tax authorities. Plaintiffs' Exhibit 14 is a collection of approximately 80 payroll checks issued between April 1995 and April 1996. Gardner's signature is on every check. Kuehn was the second signatory on the majority, with Randall signing approximately one in five checks. Plaintiffs' Exhibit 15 contains photocopies of approximately 75 checks to vendors for accounts payable written between February 1995 and March 1996. Gardner's signature appears on every check and Randall provided the second signature on four out of five checks. Gardner signed checks to the State of Oregon and the federal government for payment of the withholding taxes for the first quarter 1995. Gardner also signed the Employer's Quarterly Federal Tax Return for the second quarter of 1995.

Gardner received regular reports of EMT's operation from both Kuehn and Randall. Gardner testified that Kuehn was required to keep him informed of production on a daily basis. Gardner elaborated by explaining that Kuehn was to apprise him daily of product output (sales) and actual cash receipts.² Kuehn testified he sent similar information to Randall each day. According to Gardner, Randall gave him a "daily heads up." At another point, Gardner testified that he spoke with Randall once a week to keep informed about company operations. Gardner testified that he relied on Randall as a "conduit of information." In addition, Randall looked to Gardner for approval of any large expenditures. Gardner and Kuehn both testified that Gardner reviewed all major purchases and repairs and had authority to approve or deny such expenditures.

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² At one point, Gardner testified that the information was usually sent to Randall, who would forward it to Gardner. However, when Gardner was later recalled to the stand, he testified that Kuehn sent him that information "daily."

According to Donald W. Gathwright (Gathwright), the outside CPA, quarterly financial statements (profit and loss) were prepared at Randall's office by an employee named Gerri Davis. Gathwright testified the reports were typically inaccurate, necessitating a meeting with Kuehn at the plant to reconcile those statements with the accounts payable and receivable. Kuehn testified he did not have that information; that Randall prepared the receivable/payable reports. Randall denies preparing those reports. The court finds it unnecessary to resolve the conflicting testimony.

Randall had possession of the corporate seal and the company checkbook. She kept an eye on company operations from her real estate office in Portland. Randall paid the bills and, according to her own testimony, made sure that money was not misappropriated. Gardner testified that he had a great deal of trust in Randall and the checkbook was kept at Randall's office so that "we" (Gardner and Randall) had control over which checks were written. Gardner described Randall as his watchdog, who kept an eye on things because he lived so far away. In some instances, Gardner's signature was affixed to a check by means of a signature stamp Randall kept at her office. Gardner trusted Randall to pay "legitimate expenses" based on her "common sense." Randall would pay "urgent" bills first. As indicated above, she signed many checks for EMT, including payroll, accounts payable, and state and federal withholding tax payments. Randall also prepared, signed, and submitted all the state withholding tax reports beginning with the first quarter 1995 until the company ceased operations in mid-1996. She also signed and submitted some federal withholding returns.

EMT developed financial problems and began delaying payments to vendors. It also failed to remit payroll withholding taxes for five quarters from April 1, 1995 through June 30, 1996. Both Gardner and Randall were aware that the state withholding taxes were not being paid. A meeting was held in May 1995 to address the emerging financial problem. Gardner,

Randall, Kuehn, and Gathwright were in attendance. Everyone was aware the taxes were not being paid and that the failure to pay the taxes was one reason for the meeting. A decision was made at that meeting to obtain a line of credit from Key Bank. EMT secured the financing using the company's receivables as collateral. Randall arranged for the financing and Kuehn completed at least some of the paperwork required by the bank. Gardner instructed Kuehn to pay the taxes from the proceeds of the line of credit. On cross-examination, Gathwright testified that Gardner approved payment of the taxes with the line of credit and "told" Kuehn to pay the taxes when the money was available. The taxes were never paid.

Randall and Kuehn did not get along. Randall became frustrated with Kuehn and submitted a letter to Gardner, dated September 26, 1995, resigning from the Board. The Board accepted that resignation by resolution signed by Gardner. Randall remained involved in company operations and, in an effort to minimize friction and clearly delineate responsibilities, Gardner wrote job descriptions in October 1995 outlining the duties of Randall and Kuehn. Gardner testified that he was trying to give Randall certain control of the company that Kuehn wanted and that he wrote the descriptions to "establish boundaries." According to Randall's job description, she was "the key financial executive who controls, analyzes, and directs the financial results * * *." (Def's Ex F.) Her described duties included "the preparation of budgets, internal auditing of company operations and records, control of company funds, tax policies and procedures with the CPA and preparation of reports to government agencies." (*Id.*) She was also responsible for "determin[ing] method of procurement * * * [and] prepar[ing] purchase orders," and prioritizing payment of accounts payable, "with the assistance of [Kuehn] * * *." (*Id.*) The testimony shows that Randall functioned in a manner consistent with that description. Kuehn and two other witnesses, Julia Johnson and Roxanne Eaton, both of whom worked at the EMT plant, described Randall as the person "in charge" of finances and all testified that vendors

looking for payment were referred to Randall. Randall generally did not take the call, leaving Kuehn to function as the intermediary.

Kuehn's job description states he was to "oversee sales, production, purchasing, personnel & training * * * quality control * * * inventory control and all day to day supervisory duties." (Def's Ex E.) That document further reads that "management determines what and how much will be produced." (*Id.*)

Finally, Randall is identified on EMT's employer registration form filed with the department as the individual authorized to discuss payroll taxes. (Def's Ex U.) That document was signed by Gardner October 21, 1994. (*Id.*)

On July 14, 1998, the department issued liability notices against Plaintiffs and Kuehn for the unpaid withholding taxes. The parties requested, and the department held, a conference hearing. After the conference, the department issued a ruling finding Gardner, Randall, and Kuehn liable for the unpaid withholding taxes. All three timely appealed to this court. At Kuehn's trial, the department advised the court that, based on Kuehn's testimony and other information in its possession, it believed Kuehn was not liable for the taxes. Accordingly, a judgment was issued finding Kuehn not liable. Plaintiffs are attempting to avoid liability by arguing that Kuehn is the liable officer. That issue, however, is not before the court. Rather, the court must determine whether Gardner and Randall were liable.

II. ANALYSIS

ORS 316.167³ requires employers to "deduct and retain" withholding taxes from employee wages. The money deducted by the employer is held in trust for the State of Oregon. ORS 316.207(1). Employers are required to prepare and file quarterly tax reports with the

³ Unless otherwise noted, all references to the Oregon Revised Statutes (ORS) are to 1993.

department. ORS 316.168(1), (2).⁴ “The report shall be accompanied by payment of any tax due * * *.” ORS 316.168(2)(a). ORS 316.197(1)(a) reiterates (with somewhat more detail) the requirement that the employer pay over to the department the taxes required to be withheld. “The amounts deducted from the wages of an employee * * * shall be considered to be in part payment of the tax on such employee’s income for the taxable year * * *.” ORS 316.187. Delinquent payments to the department by the employer accrue interest at the statutory rate prescribed under ORS 305.220. ORS 316.197(3). When, as in this case, the employer fails to remit any amount withheld, “the department may issue a notice of liability to any officer, employee or member described in ORS 316.162(3)(b) * * *.” ORS 316.207(3)(a).

The determination of whether Gardner and Randall are liable for the unpaid withholding taxes of EMT hinges on whether Plaintiffs were “employers” during the time in question.

ORS 316.162(3) defines an employer as:

“(a) A person who is in such relation to another person that the person may control the work of that other person and direct the manner in which it is to be done; or

“(b) An officer or employee of the corporation, or a member or employee of a partnership, who as such officer, employee or member is under a duty to perform the acts required of employers by ORS 316.167, 316.182, 316.197, 316.202 and 316.207.”

The department has promulgated an administrative rule that sets forth a list of factors for determining whether a person should be considered an “employer.” The rule, in relevant part, provides that an employer includes:

“an officer or employe of a corporation or other business entity if, among other duties, that individual has:

“(a) the power or authority to see that the withholding taxes are paid when due;

“(b) power or authority to prefer one creditor over another[;]

⁴ The relevant statutory language is substantially the same in the 1995 edition, except that the later version requires the employer to “make and file a combined quarterly tax **and assessment** report * * *.” ORS 316.168(1) (1995) (emphasis added).

“(c) authority to hire and fire employees;
“(d) authority to set working conditions and schedules;
“(e) authority to sign or co-sign checks;
“(f) authority to compute and sign payroll tax reports;
“(g) authority to make fiscal decisions of the corporation;
“(h) authority to incur debt on behalf of the corporation;
“(I) knowledge of the nonpayment of the withholding taxes;
“(j) exercised authority on behalf of the corporation at or after the time the duty arose to collect and hold the taxes;
“(k) exercised authority on behalf of the corporation at or after the time the duty arose to pay over the taxes required to be withheld.”

OAR 150-316.162 (3) (1) (January 1996).⁵

The Tax Court previously stated that:

“The intent of the statutory scheme is to impose liability on those individuals who have the ability to control or the authority to direct payment of withheld taxes. There may be several officers or employees in a single business which fall within the scope of the statute, making them jointly and severally liable.”

Sayles v. Dept. of Rev., 13 OTR 324, 326 (1995).

Based on the evidence provided, the court is persuaded that both Gardner and Randall had the ability and authority to see that the withholding taxes were paid.

Gardner clearly had the corporate authority to direct payment of the withholding taxes. No one had more authority at EMT than Gardner. He was the owner, the president, the secretary, and the registered agent of the company. Although he hired Kuehn to run the plant, Gardner kept a watchful eye on his investment. He required both Randall and Kuehn to send him daily reports and information. Gardner approved all large expenditures. He was authorized to sign checks and did so regularly, including checks remitting withholding taxes. Gardner signed some employer withholding reports. He met jointly with Randall and Kuehn when they were not getting along and then wrote job descriptions to establish boundaries. Most importantly, Gardner was aware

⁵ According to the rules effective January 1996, the rule was effective December 31, 1985, and no amendments were made prior to January 1996. Accordingly, the same provisions are found in the rules governing in 1995.

the taxes were not being paid and he was in a position to do something about it. Gardner did not have possession of the checkbook but could have directed Randall to write the check and he had the authority to sign it.

Randall wielded nearly as much power as Gardner. It appears Randall was second-in-command in terms of overall decision-making authority, but more involved than Gardner in day-to-day operations. She helped Gardner locate financing to purchase EMT and obtain a line of credit to keep it operating. She kept the checkbook and paid the bills, including prioritizing payments. Kuehn was required to send Randall information about production and cash receipts. Randall signed withholding reports and cosigned the checks remitting the taxes, until EMT quit making payments. Randall acknowledged that she watched over the checkbook to ensure money was not misappropriated. Randall's written job description gave her authority over budget preparation, tax policies, internal auditing, purchasing, and prioritization of bill payments. Kuehn was in charge of production, sales, and day-to-day supervision of employees. The scope of the authority Randall had as against Kuehn refutes Randall's assertion that she took orders from Kuehn. Randall also knew the taxes were not being paid. In fact, she was the one not writing the checks. Randall claims Kuehn told her not to pay the taxes. Randall did not follow that instruction, but instead checked with Gardner, who allegedly told her to do as Kuehn said.

It appears neither Gardner nor Randall viewed payment of the taxes as a priority. If they were concerned about the problem, as the testimony regarding the meeting in May 1995 suggests, Gardner and Randall could have ensured that the taxes were paid without Kuehn's involvement or approval. Randall could have written and signed the checks and then either forwarded them to Gardner to sign or affixed Gardner's signature, thereby supplying the two signatures necessary for the valid issuance of the checks. It is difficult to understand why Gardner would instruct Kuehn to pay the taxes with the proceeds from the line of credit, given that Kuehn did not have

possession of the checkbook and could provide only one of the two necessary signatures on the checks. Randall's assertion that Gardner told her to follow Kuehn's advice and pay other bills instead of the taxes is more difficult to square with Gardner's earlier concern, expressed at the May financial meeting, that the taxes be paid with the borrowed funds.

Plaintiffs argue that Gardner was an uninvolved investor with "no ability to govern the day to day operations or management of the company" and that Randall "functioned purely as a subordinate, who was required to follow Mr. Kuehn's instructions regarding all financial matters." (Ptf's Closing Br at 11, 12, and 13.) Plaintiffs argue that Gardner's check signing authority is the "only factor that could possibly make [him] liable." (*Id.* at 11.) Plaintiffs gloss over the fact that it was Gardner and Randall, the two incorporators, adopting bylaws written by Randall, who established the two-signature requirement. Plaintiffs further argue that Randall, like Gardner, lacked the ability or opportunity to control EMT's operations. (*Id.* at 6.) The facts clearly refute that claim. Finally, Plaintiffs argue that Randall was unable to complete the quarterly returns without the withholding information Kuehn generated at the plant and delivered to Randall and that Randall had no ability to control or even be aware of the financial picture of EMT without the information provided by Kuehn. (*Id.* at 4 and 6.) However, there is no evidence to suggest that the information Kuehn may have generated at the plant was inaccurate. It appears that Kuehn was acting in a subordinate role to Randall, merely forwarding basic payroll information (hours worked, etc.) to Randall so that Randall could draft the payroll checks and prepare necessary official paperwork, including the quarterly withholding reports. As for Randall's awareness of EMT's financial picture, Randall regularly received information and reports from Kuehn precisely because she and Gardner felt the need for Randall to be aware of EMT's operations.

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Plaintiffs assert that the focus of controlling case law is on “**who has control over and runs the day to day operations of the company.**” (*Id.* at 8; emphasis in original.) The court agrees that supervision and control of day-to-day operations was a factor in *Frutiger v. Department of Revenue*, 270 Or 821, 529 P2d 910 (1974) and *Briggs v. Commissioner*, 2 OTR 162 (1965). However, that inquiry is relevant because it tends to show who has the “requisite authority and control in form and substance within the corporate structure to order the payment of or pay the corporate tax.” *Bellotti v. Dept. of Rev.*, 12 OTR 543, 546 (1993), citing *McCormick v. Dept. of Rev.*, 10 OTR 380, 385 (1987).

Frutiger was decided some 30 years ago and involved a company owned by Mr. Frutiger, who was the president, director, and sole stockholder of the corporation. The court found that the husband, who was the managing officer, had the “legal and actual responsibility for the direction and control of the corporation” in spite of some managerial involvement by an outside factoring company. *Frutiger*, 270 Or at 825. The court found the wife was not an employer within the meaning of the statute although she held the offices of secretary and treasurer and was a member of the Board. The wife in *Frutiger* was authorized to sign corporate payroll checks but did not do so, although she did compute and sign the monthly and quarterly tax reports. *Id.* at 826. The court concluded that “she was, in fact, a corporate officer in name only.” *Id.* Here, both Gardner and Randall signed numerous corporate checks, including payroll and withholding checks. And, unlike the wife in *Frutiger*, they both exercised day-to-day supervision and control over the corporation, albeit from afar. The October job clarification meeting shows Gardner’s authority. And, he approved large expenditures. Randall held the checkbook and received regular operational information from the plant.

Briggs is distinguishable because there is no evidence that the plaintiff in that case, who was in another state managing another business, had **any** involvement in the operation of the

Oregon logging company. Gardner, like Briggs, was also physically located in another state; however, unlike Briggs, Gardner was closely watching over the company he owned and was actively involved in important decisions. Gardner was not only the titular head of the company, with check signing authority, but he also had knowledge that the taxes were not paid, instructed the company manager (Kuehn) to pay the taxes from the proceeds of a loan he approved, and intervened in the personal conflict between Randall and Kuehn related to the operation of EMT. In an effort to calm the storm, Gardner wrote job descriptions seeking to clarify Randall's corporate authority and limit Kuehn's role to production and sales.

Plaintiffs cite *Olson v. Dept. of Rev.*, 304 Or 241, 744 P2d 240 (1987) (en banc), in support of their claim that they should not be found to be employers because they had no control over the day-to-day operations of EMT. In *Olson*, the court held that a vice-president, who was also secretary and half-owner of a closely held corporation, and who exercised authority to sign checks and other documents in the absence of the other officer and owner, was personally responsible for the withholding taxes. It is true that the plaintiff in *Olson* managed operations on the production floor. However, the plaintiff's operational role did not factor into the court's reasoning. *Id.* at 247. Instead, the court discounted the plaintiff's argument that his purely operational role was evidence of his lack of control. The *Olson* court based its finding of liability on the plaintiff's corporate titles, the lack of evidence in the bylaws or minutes controverting his responsibilities as an officer, and the fact that the plaintiff had previously exercised his authority to pay corporate bills. *Id.* at 245. That reasoning applies with at least equal force to Gardner and Randall, who were regularly involved in the overall operation of EMT. Whereas Olson signed checks and other documents only in the absence of the other owner, Gardner and Randall routinely engaged in such activities.

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Another relevant but distinguishable case is *Bellotti*. The plaintiff in *Bellotti* was found not to be an employer liable for unpaid withholding taxes even though he had check signing authority and signed certain withholding tax reports. The plaintiff was the corporate secretary and the controller of an S corporation owned by a single shareholder who was also the only director and the president of the corporation. The court based its decision on the fact that the plaintiff lacked authority to prioritize payment of bills and, when the president of the corporation decided not to pay the withholding taxes, the plaintiff refused to sign the withholding tax returns. In the instant case, both Gardner and Randall had authority to prioritize the payment of bills. Randall continued to complete, sign, and submit state withholding tax reports after EMT ceased remitting the taxes, a fact (non-payment of taxes) known to both Randall and Gardner. Gardner signed the federal quarterly report for the second quarter of 1995 in December of that year, which distinguishes his situation from Bellotti's.

Neither Plaintiff claimed they were not aware of the unpaid taxes and the evidence refutes any claim that they lacked the ability to control the payment of the taxes or the authority to direct the payment. As the court explained above, Randall would have written a check and submitted the payment had Gardner instructed her to do so, and Randall could have taken care of the matter on her own, using Gardner's signature stamp to provide the necessary second signature. The court believes Gardner would not have objected if Randall had insisted on paying the taxes, an act consistent with Gardner's stated position at the October meeting, shortly before the borrowed funds became available.

Both Gardner and Randall have attempted to avoid their liability by pointing the finger at Kuehn. Gardner attempted to disassociate himself from the company by virtue of his distance from the plant and the fact that he was practically never there. Randall attempted to characterize herself as a bookkeeper operating under Kuehn's instructions. The court rejects those claims.

And, because liability is joint and several, the court's view of Kuehn's responsibility as an employer is irrelevant one way or the other, except as it enters into the overall view of the hierarchy of the corporate management.

III. CONCLUSION

On the evidence presented, the court concludes that Plaintiffs Gardner and Randall were "employers" for purposes of ORS 316.162. They were both corporate officers with the power and authority to see that the withholding taxes were paid when due, the power to prefer creditors, authority to sign checks, compute and sign payroll tax reports, to make fiscal decisions, and the ability to pay and prioritize bills, including withholding taxes. Moreover, they both had knowledge that the taxes were not paid and continued to exercise corporate authority during the period of nonpayment. Gardner also clearly had the complete authority to incur debt for the corporation. Now, therefore,

IT IS THE DECISION OF THIS COURT that the department's liability determination against Gardner and Randall is upheld, and Plaintiffs' appeals are denied.

Dated this ____ day of August 2004.

DAN ROBINSON
MAGISTRATE

IF YOU WANT TO APPEAL THIS DECISION, FILE A COMPLAINT IN THE REGULAR DIVISION OF THE OREGON TAX COURT, BY MAILING TO: 1163 STATE STREET, SALEM, OR 97301-2563; OR BY HAND DELIVERY TO: FOURTH FLOOR, 1241 STATE STREET, SALEM, OR. YOUR COMPLAINT MUST BE SUBMITTED WITHIN 60 DAYS AFTER THE DATE OF THE DECISION OR THIS DECISION BECOMES FINAL AND CANNOT BE CHANGED.

THIS DOCUMENT WAS SIGNED BY MAGISTRATE DAN ROBINSON AUGUST 2, 2004. THE COURT FILED THIS DOCUMENT AUGUST 2, 2004.