

BEFORE THE
CALIFORNIA UNEMPLOYMENT INSURANCE APPEALS BOARD

In the Matter of:

PACIFIC AVENUE LOUNGE, INC.
(Petitioner)

STOCKTON HICKORY PIT
C. J. CROZIER, DBA
(Respondent)

PRECEDENT
TAX DECISION
No. P-T-142
Case No. T-71-31

DEPARTMENT OF HUMAN
RESOURCES DEVELOPMENT

The petitioner appealed from Referee's Decision No. S-T-4057 which denied its petition for reassessment and held that it was liable for unemployment insurance taxes in the amount of \$1,349.85 contributions and \$263.29 penalty, plus interest. The petitioner was found to be a successor in interest to a limited partnership. We have considered the written argument submitted by the Department and the petitioner.

STATEMENT OF FACTS

The petitioner owns at one location a bowling alley, cocktail lounge and coffee shop. Prior to April 1, 1969 the petitioner operated all three businesses. Effective April 1, 1969 the petitioner leased the restaurant portion of the operation to a limited partnership. The partnership did business as the Stockton Hickory Pit. The partnership became delinquent in paying taxes to the Internal Revenue Service. On January 26, 1970 the Internal Revenue Service padlocked the premises and took over the partnership property.

The petitioner cancelled the partnership lease and informed the Internal Revenue Service that it should remove the partnership property as soon as possible. The petitioner was expecting to host a bowling tournament in the near future and wished to make arrangements to have the restaurant reopened. Shortly thereafter the Internal Revenue Service conducted a public sale of the partnership's property. The petitioner submitted the high bid of \$848.16 and purchased all of the partnership assets. The assets consisted primarily of an equity in some booths and a small amount of perishable food.

The booths had been purchased on a conditional sales contract. The contract and note had been discounted to the Bank of Stockton. The petitioner subsequently paid off the balance on the conditional sales contract in the amount of \$801.84 to the Bank of Stockton.

At the time the payments were made to the Internal Revenue Service and the Bank of Stockton, the petitioner had not inquired of the Department as to any tax deficiencies. The petitioner did not request a tax certificate pursuant to section 1732 of the code. The assessment against the petitioner was made after the partnership property had been acquired.

REASONS FOR DECISION

Section 1731 of the California unemployment Insurance Code provides:

"Any person or employing unit that acquires the organization, trade or business, or substantially all the assets thereof, of an employer shall withhold in trust money or other property sufficient in amount or value to cover the amount of any contributions, interest and penalties due or unpaid from such employer until such employer produces a certificate from the department stating that no contributions, interest or penalties are due. If such employer does not produce such certificate, the acquiring person or employing unit shall pay the amount or the value of the property so withheld to the department at the time of such acquisition."

Section 1732 of the code further provides:

"(a) Upon request of either of the parties to an acquisition as described in Section 1731, the department shall within 30 days issue a certificate, or a statement showing the amount of any contributions, interest and penalties claimed to be due. The failure to issue a certificate or a statement within the period of 30 days shall be deemed equivalent to the issuance of a certificate stating that no contributions, interest or penalties are due.

"(b) If the department issues a statement showing the amount of contributions, interest and penalties claimed to be due, the amount stated therein shall be withheld and paid to the department such amount, however, not to exceed the purchase price. The issuance of any certificate stating that no

contributions, interest and penalties are due, or the failure to issue such certificate or statement within the period of 30 days shall not release the employer from liability on account of any contributions, interest and penalties then or thereafter determined to be due from him, but shall release the acquiring person or employing unit from any further liability on account of any such contributions, interest and penalties."

Section 1733 of the code provides:

"Any person or employing unit that fails to withhold money or other property or fails to pay the amount or value of the property withheld as provided in Sections 1731 and 1732 shall be personally liable for the payment of the contributions, interest and penalties due from the employer up to but not exceeding the purchase price. The director shall assess such amount to the acquiring person or employing unit and shall give a written notice of the assessment in accordance with the provisions of Section 1140. Sections 1133 through 1140 apply to assessments under this section."

The above quoted provisions of the California Unemployment Insurance Code set forth a system for collecting unpaid unemployment insurance and disability insurance taxes from a successor in interest. The petitioner did acquire substantially all of the assets of the partnership and did not obtain prior tax clearance. Therefore the assessment for taxes by the Department is proper and the petitioner must pay unless the action of the federal tax authorities served to break the chain and cut off liability.

Pertinent provisions of Title 26, United States Code, are as follows:

Section 6331(a):

"If any person liable to pay any tax neglects or refuses to pay the same within 10 days after notice and demand, it shall be lawful for the secretary or his delegate to collect such tax . . . by levy upon all property and rights to property . . . belonging to such person. . . ."

Section 6331(b):

"Seizure and sale of property. The term 'levy' as used in this title includes the power of distraint and seizure by any means. . . . In any case in which the secretary or his delegate may levy upon property or rights to property, he may seize and sell such property or rights to property. . . ."

Section 6339(c):

"A certificate of sale of personal property given or a deed to real property executed pursuant to section 6338 shall discharge such property from all liens, encumbrances and titles over which the lien of the United States with respect to which the levy was made had priority."

The Internal Revenue Service had authority, under section 6331(a) of the United States Code quoted above, to levy upon all of the property of the partnership. This levy established a valid tax lien in favor of the United States. The United States then had authority to sell the property at public sale. The sale passed the interest of the delinquent debtor in the property to the petitioner. Mansfield v. Excelsio Refining Company (135 U.S. 326) The certificate of sale issued pursuant to section 6039(c), United States Code, extinguished all debts or liens subsequent to that of the United States. The federal tax sale did not affect the interest of the Bank of Stockton in the booths. The Bank of Stockton held title to that part of the property as assignee of a conditional sales contract. The bank's interest was prior to the tax levy. The petitioner subsequently purchased the bank's interest. Under all of the circumstances, we conclude that the petitioner took title to all the property free and clear of any Department lien for taxes.

The last issue we must consider is whether or not a Department lien came into existence after the sale under the provisions of section 1731 of the Unemployment Insurance Code. In Fried v. New York Life Insurance (354 U.S. 922) the Supreme Court held that a state may not interfere with the power of Congress to levy and collect federal taxes on income. In our opinion it would be a definite interference with federal authority for us to hold that a state lien for unemployment insurance and disability insurance taxes attaches to property after its sale to satisfy federal taxes. Such a holding would be in direct defiance of section 6339(c), Title 26, United States Code. Accordingly, we must hold that section 1731 of the Unemployment Insurance Code is not applicable to this case and the petitioner cannot be held liable for the tax.

DECISION

The decision of the referee is reversed. The petition for reassessment is granted. The petitioner is not liable for the assessed tax.

Sacramento, California, July 11, 1972

CALIFORNIA UNEMPLOYMENT INSURANCE APPEALS BOARD

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