STATE OF ALABAMA DEPARTMENT OF REVENUE,	§	STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION
v.	§	DOCKET NO. S. 89-202
THE FROZEN YOGURT SHOP, INC. As successor to Mulkey Enterprises d/b/a TCBY Circle West Shopping Center Dothan, AL 36303, Taxpayer.	§ § § § §	

FINAL ORDER

The Revenue Department assessed State, Houston County, Coffee County, City of Dothan and City of Enterprise sales tax against The Frozen Yogurt Shop, Inc., As Successor to Mulkey Enterprises, Inc., d/b/a TCBY concerning the period February 1,1988 through October 31, 1988. The Frozen Yogurt Shop, Inc. appealed to the Administrative Law Division and a hearing was conducted on March 7, 1990. Jeff Kohn, Esq. and Will Sellers, Esq. appeared for The Frozen Yogurt Shop, Inc. Assistant counsel Duncan Crow represented the Department. This Final Order is entered based on the evidence and arguments presented by both parties.

FINDINGS OF FACT

Mulkey Enterprises, Inc. (Mulkey) owned and operated two TCBY Yogurt stores in Alabama, one each in Enterprise and Dothan. Mulkey and The Frozen Yogurt Shop, Inc. (Taxpayer) entered into an Agreement For Purchase And Sale on March 1, 1988 by which the Taxpayer agreed to purchase the assets of the two yogurt stores. In return, the Taxpayer agreed to pay Mulkey $10.00 cash and assume the

following debts owed by Mulkey relating to the stores:

> (a) To TCBY Systems, Inc. in the approximate amount of $16,000.00 representing the Seller's Royalty and Advertising Co-op obligations.
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> (b) To Sowega Foods, Inc. in the approximate amount of $70,500.00 representing the Seller's obligations for purchase of equipment, etc. at the Dothan Store.
>
> (c) To TCBY Systems, Inc. in the approximate amount of $61,500.00 representing the Seller's obligations for the purchase of the equipment, etc., at the Enterprise Store.
>
> (d) To Aronov Realty Company, Inc. in the approximate amount of $4,044.00 representing the amount of rent past due under the lease described in Paragraph 3(a) hereof.

The sale was closed on November 1, 1988, at which time the Taxpayer took over and began operating the two stores. However, in the meantime Mulkey had continued to operate the two stores from March through October, 1988 and had failed to pay its sales tax liability to the State, Coffee County, Houston County and the Cities of Dothan and Enterprise.

The Department subsequently assessed the delinquent liability against the Taxpayer, as successor to Mulkey, pursuant to the sale tax "successor in business" statute, Code of Ala. 1975, §40-23-25. The issue in dispute is whether the Taxpayer is a successor in business under §40-23-25 and thus liable for Mulkey's unpaid sales taxes for the period February through October, 1988.

CONCLUSIONS OF LAW

Code of Ala. 1975, §40-23-25 provides as follows:

> Any person subject to the provisions hereof who shall sell out his business or stock of goods, or shall quit

> business, shall be required to make out the return provided for under §40-23-7 within 30 days after the date he sold out his business or stock of goods, or quit business and his successor in business shall be required to withhold sufficient of the purchase money to cover the amount of said taxes due and unpaid until such time as the former owner shall produce a receipt from the department of revenue showing that the taxes have been paid, or a certificate that no taxes are due. If the purchaser of a business or stock of goods shall fail to withhold purchase money as above provided the taxes shall be due and unpaid after the 30 day period allowed, he shall be personally liable for the payment of the taxes accrued and unpaid on account of the operation of the business by the former owner. If in such cases the department deems it necessary in order to collect the taxes due the state, it may make a jeopardy assessment as herein provided. (emphasis added)

The Taxpayer argues that it should not be liable for Mulkey's delinquent sales taxes because no "purchase money" was paid to Mulkey from which the delinquent taxes could have been withheld and paid over to the State.

Conversely, the Department contends that the statute should be broadly interpreted and that a successor business must be held strictly liable for payment of its predecessor's tax liability. The Department argues that the actual passage of "purchase money" directly from the purchaser to the seller is not necessary for the successor to be liable under the statute.

Section 40-23-25 has not been interpreted by any circuit or appellate court in Alabama. However, courts in other states have ruled that the purpose of a successor liability statute is to ensure the collection of taxes by imposing strict liability on the successor. The clear intent of such statutes is for the tax debt to

follow the business and its assets when sold. Further, the direct payment of "purchase money" from the purchaser to the seller is not necessary for the successor to be liable for any delinquent sales tax owed by its predecessor, see Bank of Commerce v. Woods, 585 S.W.2d 577; A. Copeland Enterprises v. Commissioner of Revenue, 703 S.W.2d 624.

In Bank of Commerce v. Woods, supra, a Tennessee bank loaned money for the operation of a convenience food store. The food store owners fell behind an the note payments to the bank, and to avoid default, subsequently transferred their interest in the store assets to the bank in consideration for settlement of the loan balance.

The store owners owed delinquent sales tax to the State, and the Tennessee Revenue Department assessed the delinquent taxes against the bank as successor under Tennessee's successor statute, T.C.A. Section 67-3025. The Tennessee statute is almost identical to §40-23-25 in that it requires that any successor "shall withhold sufficient of the purchase money to cover the amount of such taxes, interest and penalties due and unpaid . . . if the purchaser of a business or stock of goods shall fail to withhold the purchase money as above provided, he shall be personally liable for the payment of the taxes, interest, and penalties" owed by the former owner. The bank denied liability based an its assertion that no "purchase money" had changed hands from which the delinquent taxes could have been withheld and paid over to the State.

The Tennessee Supreme Court ruled that the statute should be broadly construed and held for the Department. The Court specifically ruled that the actual exchange of purchase money from the bank to the store owners was not necessary for the successor bank to be liable. The Court stated as follows, at page 581:

> Our successor liability statute broadly imposes a duty on a "successor, successors, or assigns" of a taxpayer who sells out or quits his business. The use of the words "purchase money" cannot be construed as a limitation on this duty, but is merely a descriptive term of the action to be taken by the person or business entity on whom the duty has been imposed.

In A. Copeland Enterprises, Inc. v. Commissioner of Revenue, supra, Copeland was the owner and franchiser of six fried chicken outlets in Memphis, Tennessee. Copeland leased the locations and sold the equipment to Coyote Properties, Inc. (Coyote). The equipment was sold for $115,000.00, payable in monthly installments secured by a mortgage on the equipment.

Coyote successfully operated the outlets for a time, but then became delinquent on the lease and equipment payments. Copeland subsequently forgave the delinquent payments owed by Coyote in return for Coyote transferring the equipment back to Copeland and cancelling the leases. No money changed hands in the transaction.

The Tennessee Revenue Department assessed Copeland as successor for delinquent taxes owed by Coyote, citing Bank of Commerce v. Woods. Copeland's defense, like the bank's in Bank of Commerce v. Woods, was that no "purchase money" was paid from which the taxes could have been withheld and paid over to the Department. The

Tennessee Supreme Court rejected Copeland's argument and affirmed its decision in Bank of Commerce v. Woods as follows:

> We have heretofore held that the legislative purpose in enacting the successor statute, T.C.A. §67-6-513, was to provide that the tax debt follow the business, its assets or any portion thereof to ensure the collectibility of sales tax due the State. Bank of Commerce v. Woods, supra at 580. It is not incumbent upon the commissioner to show that purchase money or an equity in excess of a cancelled indebtedness, passed to the successor as a pre-requisite of imposing successor liability under the statute.

For similar holdings in other states, see Knudsen Dairy Products Company v. State Board of Equalization, 12 Cal. App. 3rd 47, 90 Cal. Rpt. 533; State v. Sloan, 164 Ohio St. 579, 132 N.E.2d 460; Tri-Financial Corporation v. Department of Revenue, 6 Wa. App. 637, 495 P.2d 690; and generally 65 A.L.R.3d 1181.

The Taxpayer correctly points out that this Administrative Law Judge ruled in a previous case that a successor should be liable for a predecessor's delinquent sales or use tax liability only if "purchase money" actually changes hands from which the delinquent tax can be withheld and paid over to the State, see Docket No. U.84-149. However, after reviewing the above cited cases, I must conclude that my prior decision is incorrect and that the better reasoned view is that taken by the Tennessee Supreme Court in the above cases.

The purpose for enacting a successor statute is to ensure that all sales tax owed the State is paid when a taxpayer sells out or

quits business. The seller is required to "produce a receipt from the department of revenue showing that the taxes have been paid, or a certificate that no taxes are due." The purchaser is thus under a duty to know if delinquent taxes are owed, and is liable if any taxes are left unpaid by the seller, see State v. Sloan, supra, at p. 464, and Bank of Commerce v. Woods, supra, at p. 581.

Also, as noted above, the use of the words "purchase money" in the statute should not limit a successor's liability to only those instances where money is actually paid directly by the purchaser to the seller. If the successor's liability was so limited, then a successor could avoid liability by structuring the purchase so that no money flowed directly to the seller. As stated in Knudsen Dairy Products Company v. State Board of Equalization, supra:

> In a purchase and sale, the purchase price need not necessarily flow directly to the seller. The fact that the purchase price here went to a third party, to wit, Creamery (Mulkey's creditors), does not militate against the finding that Dairy (Taxpayer) was a "purchaser". To hold otherwise would permit a taxpayer to avoid liability by the simple device of having the purchase price paid through an intermediary.

In the present case, the Taxpayer was undeniably the successor to Mulkey in the operation of the two yogurt stores. The fact that consideration for the stores' assets was paid to Mulkey's creditors and not directly to Mulkey cannot relieve the Taxpayer of liability.

The above considered, the Department is directed to make the assessments in issue final, with applicable interest.

Entered this the 18th day of April, 1990.

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BILL THOMPSON
Chief Administrative Law Judge