IN THE

ARIZONA COURT OF APPEALS

DIVISION ONE

STATE OF ARIZONA, ex rel.,
ARIZONA DEPARTMENT OF REVENUE,
Plaintiff/Appellee,

v.

KARL TUNBERG, et al.,
Defendants/Appellants.

No. 1 CA-TX 18-0008
FILED 4-21-2020

Appeal from the Arizona Tax Court
No. TX2016-000324
The Honorable Christopher T. Whitten, Judge

AFFIRMED

COUNSEL

Arizona Attorney General's Office, Phoenix
By Penny Taylor Moore
Counsel for Plaintiff/Appellee

Quarles & Brady, LLP, Phoenix
By Dawn R. Gabel, Lauren Elliott Stine, Hannah R. Torres
Counsel for Defendants/Appellants

OPINION

Judge Diane M. Johnsen delivered the opinion of the Court, in which Presiding Judge Kenton D. Jones joined. Judge James B. Morse Jr. specially concurred.[1]

J O H N S E N, Judge:

¶1 Under the Arizona tax code, an officer of a company that must pay transaction privilege tax may be personally liable for failing to remit tax payments the company has charged and collected from its customers. In this appeal, we affirm the tax court's judgment against a member-manager and chief executive officer of a limited liability company for those payments. We also affirm the tax court's denial of the officer's request for attorney's fees.

FACTS AND PROCEDURAL BACKGROUND

¶2 After an audit, the Arizona Department of Revenue determined that Sanctuary Design, L.L.C. had failed to pay $353,652 in transaction privilege tax. Sanctuary did not protest the audit, and it became final. The Department then sued to recover the taxes, naming Sanctuary and its member-manager and CEO, Karl Tunberg, as defendants. After the Department obtained a default judgment against Sanctuary, the parties filed cross-motions for summary judgment on the claim against Tunberg, which alleged he was personally liable under Arizona Revised Statutes

---

[1] Judge Johnsen was a sitting member of this court when the matter was assigned to this panel of the court. She retired effective February 29, 2020. In accordance with the authority granted by Article 6, Section 3, of the Arizona Constitution and pursuant to A.R.S. § 12-145, the Chief Justice of the Arizona Supreme Court has designated Judge Johnsen as a judge *pro tempore* in the Court of Appeals, Division One, for the purpose of participating in the resolution of cases assigned to this panel during her term in office.

("A.R.S.") section 42-5028 (2020) for failing to remit tax payments Sanctuary had collected from its customers.[2]

¶3 The tax court concluded that "uncontested evidence" established that Tunberg was responsible for the taxes Sanctuary had collected and therefore was personally liable under the statute. After a trial to establish the amount due, the court ruled Tunberg and his spouse were liable for $49,769.65 in taxes Sanctuary collected between May 2008 and September 2009 but failed to remit.[3] The court later denied Tunberg's motion for attorney's fees and entered final judgment. Tunberg filed a timely appeal. We have jurisdiction pursuant to Article 6, Section 9, of the Arizona Constitution, and A.R.S. §§ 12-120.21(A)(1) (2020) and -2101(A)(1) (2020).

DISCUSSION

A. The Tax Court Did Not Err by Finding Tunberg Liable.

¶4 "The court shall grant summary judgment if the moving party shows that there is no genuine dispute as to any material fact and the moving party is entitled to judgment as a matter of law." Ariz. R. Civ. P. 56(a). Summary judgment is appropriate when "the facts produced in support of the claim or defense have so little probative value, given the quantum of evidence required, that reasonable people could not agree with the conclusion advanced by the proponent." *Orme School v. Reeves*, 166 Ariz. 301, 309 (1990). We review the tax court's summary-judgment ruling *de novo*. *Sw. Airlines Co. v. Ariz. Dep't of Revenue*, 217 Ariz. 451, 452, ¶¶ 5-6 (App. 2008). We likewise review the interpretation of statutes *de novo*. *Id.* at ¶ 6.

¶5 "The transaction privilege tax is an excise tax on the privilege or right to engage in an occupation or business in the State of Arizona." *Ariz. Dep't of Revenue v. Action Marine, Inc.*, 218 Ariz. 141, 142, ¶ 6 (2008) (citation omitted). Although it "is a tax on the gross receipts of a person or entity engaged in business activities," liability for the tax "falls on the taxpayer, not on the taxpayer's customers." *Id.* at ¶¶ 6-7; *see* A.R.S. §§ 42-

---

[2] Absent material revision after the relevant date, we cite the current version of a statute or rule.

[3] The complaint alleged no act by which Tunberg's spouse would be liable under § 42-5028. She was named only for community-property purposes because she and Tunberg were married at all relevant times.

5008 (2020), -5024 (2020). The default judgment the Department obtained against Sanctuary for $340,644 in tax owing on its sales receipts is not at issue in this appeal.

¶6 A taxpayer that makes a sale to a customer may choose to bill the customer for the transaction privilege tax the taxpayer will owe on the proceeds of that sale. When the taxpayer does so, it must remit to the Department whatever tax it collects from the customer, "even if it collects more than the taxpayer owes." *Action Marine*, 218 Ariz. at 142, ¶ 7; *see also* A.R.S. § 42-5002(A)(1) (2020). The logic is that tax payments the taxpayer collects from customers "do not belong to and are not for the use of the taxpayer." *Action Marine*, 218 Ariz. at 142, ¶ 8.

¶7 Here, the Department sued Tunberg pursuant to § 42-5028, under which an officer or director of a taxpayer may be "personally liable" for transaction privilege taxes the taxpayer bills and collects from its customers. *See Action Marine*, 218 Ariz. at 145, ¶ 21. *Action Marine* held that when a business collects the tax from a customer, § 42-5028 imposes personal liability upon any officer or director of that business who has "assumed a duty to remit" to the government what the customer has paid. *Id.* Officers and directors assume that duty when they "hold[], maintain[] control over, or [have] responsibility for the money collected separately" for the tax. *Id.*

¶8 The supreme court directed the tax court in *Action Marine* to decide on remand whether the individual defendants were liable under § 42-5028. *Id.* at 147, ¶ 28. The court observed that facts relevant to that inquiry may include whether an individual "had control over, responsibility for, or supervision of the money collected to pay the tax" and whether, for example, the individual "had the final word as to what bills should or should not be paid" because he "had the authority required to exercise significant control over the corporation's financial affairs, regardless of whether he exercised such control in fact." *Id.* at ¶ 29 (citation omitted).

¶9 At issue in the Department's claim against Tunberg were taxes Sanctuary collected from customers between May 2008 and September 2009. Tunberg was CEO and managing member of the limited liability company throughout that period. He signed some of the customer contracts at issue as "owner" of Sanctuary. He also participated in the audit on behalf of the company.

¶10 On summary judgment, Tunberg offered evidence that, until 2008, Sanctuary's outside certified public accountant had prepared the company's tax returns. According to Tunberg, Sanctuary then hired a chief financial officer, who "was responsible for all financial operations and took over the transaction privilege tax reporting at the beginning of 2008." Tunberg asserted that as CEO, his own duties were limited to "overall strategic vision," negotiating loans and "dealing with large customers to either help land the business or smooth over any concerns that arose." He argued that although he signed proposals or letters of engagement with customers, he was not involved with any "sales tax, employee tax or other accounting functions." He contended he did not decide whether Sanctuary would separately bill customers for transaction privilege tax, did not know whether Sanctuary did bill the tax separately, was not responsible for any customer payments of taxes and never maintained control over monies customers paid in taxes. According to Tunberg, all these duties belonged to the CFO. That CFO, however, decided at some point to stop making the company's tax payments. Tunberg asserted he did not know Sanctuary had not been reporting and paying transaction privilege taxes until he learned the Department was auditing the company.

¶11 The Department offered evidence showing that Tunberg telephoned the Department about the company's tax returns on December 16, 2008. During that call, the Department informed Tunberg that Sanctuary had not filed transaction privilege tax returns since May 2008; according to the Department, Tunberg responded that he would make sure they were filed. The Department also offered evidence that, contrary to Tunberg's assertion that he did not know Sanctuary billed customers for transaction privilege tax, he had signed seven contracts containing line entries for tax to be paid by the customers.

¶12 We hold the tax court did not err by concluding that Tunberg assumed a duty under § 42-5028 to remit taxes Sanctuary had collected from its customers. As CEO of the company, Tunberg "had the final word as to what bills should or should not be paid." 218 Ariz. at 147, ¶ 29. In *Action Marine*, the supreme court observed that imposing personal liability under the statute on "corporate officers or directors assuages concerns that such persons might abuse the privilege of limited liability protection by collecting money from customers under the guise of a state-imposed tax, using such monies for other purposes, forcing the taxpayer into bankruptcy, and later claiming limited liability protection." 218 Ariz. at 144, ¶ 17. The supreme court's concern may be particularly apt in the context of an owner-managed company whose owner stands to benefit when the company collects tax monies from customers but fails to pay them over to

the Department. Here, Tunberg was Sanctuary's managing member. He was the CEO and signed contracts as its "owner." And although the company had grown to some 20 employees heading into 2008, it went out of business in Arizona in late 2009, during the audit period.

¶13 We need not consider here whether officers and directors of owner-managed companies generally are liable under § 42-5028 and *Action Marine*. Tunberg argues he had delegated to the company's newly hired CFO the responsibility for processing and remitting customers' tax payments in 2008. The evidence, however, was that, as of December 2008, Tunberg knew the CFO had not been forwarding customers' tax payments to the Department. The tax court found Tunberg liable for payments made by customers on two contracts Sanctuary entered into and performed during the latter half of 2008 and on four contracts executed in 2009. As Sanctuary's managing member and CEO, after learning the CFO was not remitting taxes paid by customers during that time period, Tunberg had the power and the obligation to delegate that responsibility to someone else, but there is no evidence in the record showing he did so.

¶14 Under these circumstances, as the tax court reasoned, "a corporate entity cannot evade taxes simply by failing to delegat[e] a person responsible for their payment. In the absence of someone who has been given that responsibility, it must be the person with ultimate responsibility for the entity." Having failed to delegate that responsibility to another corporate officer, Tunberg assumed the duty himself, and so became personally liable under § 42-5028.

B. Substantial Evidence Supports the Tax Court's Finding that Sanctuary Collected $49,769.65 in Tax for Which Tunberg Is Liable.

¶15 We will affirm the tax court's findings of fact as to the amount of tax Sanctuary collected from its customers if it is supported by substantial evidence and not clearly erroneous. *Kocher v. Dep't of Revenue*, 206 Ariz. 480, 482, ¶¶ 8-9 (App. 2003).

¶16 At trial, the Department offered eight contracts it argued showed Sanctuary charged and collected from its customers a total of $93,334.04 in transaction privilege tax. After hearing the evidence, the tax court found the Department had proved only that the company collected $49,769.65 in tax from six of the eight customers. The court's finding is not clearly erroneous and is supported by substantial evidence.

¶17 Each of the six contracts the tax court cited specified a line item for tax. After tracing the payments Sanctuary received from each of

the six customers, the Department's auditor testified he found that on one of the contracts, the customer paid Sanctuary the full contract amount for the project and that on the other five contracts, the customers paid Sanctuary more than the full contract amounts.

¶18 Tunberg argues the Department failed to show that Sanctuary billed the six customers separately for taxes and could not prove the company received the customers' payments. Even absent invoices or other documentation, however, substantial evidence supported the tax court's finding. Each of the six customers signed a contract that specified a line item for tax, then paid Sanctuary the full amount of the contract or more. The court's ruling reflects a careful review of the evidence: It declined to find that customers had paid tax on two contracts on which the Department's auditor testified he could not confirm that Sanctuary had collected the full contract amounts.

¶19 Tunberg argues that change orders or other documents not in the record might reflect changes in the work Sanctuary wound up doing for the six customers, with corresponding changes in taxes ultimately due and paid on the projects. The tax court, however, did not err by finding the Department proved by a preponderance that Sanctuary collected the stated amounts in taxes from the six customers.

C. The Tax Court Did Not Err in Declining to Award Fees to Tunberg.

¶20 After the tax court entered its post-trial ruling, Tunberg moved for his attorney's fees pursuant to A.R.S. § 12-348(B)(1) (2020), under which a court "may award fees and other expenses to [a] party . . . that prevails by an adjudication on the merits . . . in an action . . . to enforce the assessment or collection of taxes." The court denied Tunberg's request, noting that he was held personally liable for taxes, although "in an amount considerably lower than the Department had sought." On appeal, Tunberg argues the tax court erred because even though a judgment was entered against him, he "prevail[ed]" in that the $49,769 judgment was far less than the $340,644 the Department sought when it filed its complaint.

¶21 Neither party has cited, and we were unable to identify, a case addressing whether a defendant "prevails" in a tax-collection suit under § 12-348(B) when the result of an adjudication on the merits is that the defendant must pay taxes, but not as much as the government originally sought. In *4501 Northpoint LP v. Maricopa County*, 212 Ariz. 98, 99, ¶¶ 2, 6 (2006), judgment was entered in favor of a taxpayer that had challenged the

assessed full cash value of its property. The taxpayer accepted the county's offer of a judgment, and the issue on appeal was whether § 12-348(B) allowed the tax court to award the taxpayer its fees. *Id.* at 99-100, ¶¶ 6-9. The court reviewed the issue *de novo* as a matter of statutory construction and concluded the judgment constituted an "adjudication on the merits." *Id.* at 100, 102, ¶¶ 14, 20 (noting court already had "held that a party, in order to 'prevail' by an adjudication on the merits, must secure a final resolution of the case *in the party's favor*") (emphasis added) (citing *Scottsdale Healthcare, Inc. v. Ariz. Health Care Cost Containment Sys. Admin.*, 206 Ariz. 1, 8-9, ¶ 29 (2003)).

¶22 In arguing he "prevail[ed]" even though judgment was entered against him, Tunberg cites two decisions interpreting contractual fee provisions, *Ocean West Contractors, Inc. v. Halec Construction Co.*, 123 Ariz. 470 (1979) (in division), and *Murphy Farrell Development, LLLP v. Sourant*, 229 Ariz. 124 (App. 2012).

¶23 In *Ocean West*, the supreme court interpreted a contract provision authorizing fees to the "successful" party. 123 Ariz. at 472. The superior court had ruled both parties breached, then netted out the damages proved on the competing claims and entered a judgment awarding damages to the plaintiff. *See id.* In affirming an award of fees to the plaintiff, the supreme court explained:

> The party who is awarded a money judgment in a lawsuit is not always the successful or prevailing party. The award of money is, however, an important item to consider when deciding who, in fact, did prevail. The fact that a party did not recover the full measure of relief requested does not mean that he is not the successful party. Neither does the fact that the amount of the claim is set off or reduced by counterclaim mean that the plaintiff was not the successful party.

Id. at 473 (citation omitted); *see also Berry v. 352 E. Virginia, L.L.C.*, 228 Ariz. 9, 13-14, ¶ 22 (App. 2011) (in case presenting competing claims and counterclaims, "successful party" for purposes of A.R.S. § 12-341.01(A) (2020) is the "net winner" (citation omitted)).

¶24 At issue in *Murphy Farrell* was a contract requiring a fees award to "the prevailing party." 229 Ariz. at 132, ¶ 30 & n.8. The superior court found the plaintiff proved the defendant had breached but denied the plaintiff's request for a constructive trust and entered judgment for the defendant. *Id.* at 128, ¶ 11. On appeal, the defendant argued he had

prevailed and challenged the court's refusal to award him fees. *Id.* at 132, ¶ 30. Citing *Ocean West*, we noted that the defendant's breach "d[id] not necessarily preclude him from being the 'prevailing party'" under the contract. *Id.* at 133, ¶ 34. Applying a "'percentage of success' factor or a 'totality of the litigation' rubric to determine which party prevailed," we held the defendant was entitled to fees because he had prevailed when the court denied relief to the plaintiff. *Id.* at 134, ¶¶ 36-37 (citation omitted).[4]

¶25 *Ocean West* involved a fee award to the net winner on competing claims and counterclaims, *see* 123 Ariz. at 472, a situation to which § 12-348(B) does not apply. Nor is this a case like *Murphy Farrell* in which judgment is entered in favor of the defendant on what arguably was a technicality. *See* 229 Ariz. at 128, ¶ 11. Even if the reasoning of those cases might support the conclusion that Tunberg "prevail[e]d" for purposes of § 12-348(B), however, he cites no authority for the proposition that the tax court lacked discretion under the circumstances here to decline his request for fees. *See* A.R.S. § 12-348(B) ("a court *may* award fees and other expenses to a party . . . that prevails by an adjudication on the merits") (emphasis added). This is particularly true given Tunberg does not assert he ever offered to settle the Department's claim, let alone offered to settle for an amount greater than the judgment ultimately entered against him. *See* A.R.S. § 12-348(C) (permitting court to reduce a fees award to a "prevailing party" that "refused an offer of civil settlement that was at least as favorable to the party as the relief ultimately granted").

¶26 Accordingly, we affirm the tax court's denial of Tunberg's fee request. *See Reyes v. Frank's Serv. & Trucking, LLC*, 235 Ariz. 605, 610, ¶ 16 (App. 2014) ("We will affirm the trial court's decision if it is correct for any reason."). Under these circumstances, the Department's failure to win as large a judgment against Tunberg as it originally sought did not require an award of fees in his favor under § 12-348(B).

CONCLUSION

¶27 For the reasons stated, we affirm the judgment of the tax court and deny Tunberg's request for fees pursuant to A.R.S. § 12-348(B). The

---

[4] We need not decide whether a "prevail[ing]" party under § 12-348(B) is the equivalent of a "successful party" under § 12-341.01(A), but we note that the cases use the terms interchangeably. *See, e.g.*, *Am. Power Prods., Inc. v. CSK Auto, Inc.*, 242 Ariz. 364, 367, ¶ 10 (2017); *Desert Mountain Props. Ltd. P'ship v. Liberty Mut. Fire Ins. Co.*, 225 Ariz. 194, 213, ¶ 81 (App. 2010).

Department is entitled to its costs on appeal subject to compliance with Arizona Rule of Civil Appellate Procedure 21.

M O R S E, J., specially concurring:

¶28 I fully join the opinion but write separately to address when a party may prevail "by an adjudication on the merits . . . in an action . . . to enforce the assessment or collection of taxes." *See* A.R.S. § 12-348(B)(1). As the opinion tacitly acknowledges, the tax court erred when it applied the "net winnings test." *See supra* ¶ 25-26. However, remand is not necessary because Tunberg failed to provide sufficient evidence upon which a court could conclude that he "prevailed" for the purposes of A.R.S. § 12-348. Tunberg argued that the Department refused to discuss settlement, but he disputed both personal liability *and* the amount owed. Moreover, as discussed *supra* ¶ 25, Tunberg presented no evidence to suggest he was willing to accept liability in an amount at or near the judgment ultimately entered against him. On this record, the tax court did not abuse its discretion in finding that the Department prevailed in the litigation. *See Wilderness World, Inc. v. Ariz. Dep't of Revenue*, 182 Ariz. 196, 202 (1995) (noting "the award of attorneys' fees in tax cases [is] discretionary" but "taxpayer should not be deterred from making a good faith challenge to the government's wrongful imposition of taxes"); *RenalWest L.C. v. Ariz. Dep't of Revenue*, 189 Ariz. 409, 415 (App. 1997) (award of fees under § 12-348(B) is within tax court's discretion); *cf. also* A.R.S. § 12-348(C)(3) (providing that an award of fees to a prevailing taxpayer may be reduced when the taxpayer "refused an offer of civil settlement that was at least as favorable to the party as the relief ultimately granted").

¶29 In other circumstances, however, a taxpayer could "prevail" under A.R.S. § 12-348(B)(1) by substantially reducing the tax liability sought by the Department. Entry of judgment is not dispositive in determining the prevailing party. *See Ocean West Contractors*, 123 Ariz. at 473 (noting that the "party who is awarded a money judgment in a lawsuit is not always the successful or prevailing party"). This principle is particularly applicable to tax cases, where the taxpayer's goal is often to reduce the amount of taxes owed. *See City of Phoenix v. Paper Distribs. of Ariz., Inc.*, 186 Ariz. 564, 565 (App. 1996) (taxpayer awarded attorney fees after successfully receiving abatement of $27,257.24 from an assessed tax deficiency of $81,994.55); *see also Ariz. Tax Research Ass'n v. Ariz. Dep't of Revenue*, 163 Ariz. 255, 258 (1989)

(holding that successful challenge to property tax valuation could give rise to fee award under § 12-348(B)).

¶30 "In enacting A.R.S. § 12-348, the legislature expressed its intent to reduce the economic deterrents individuals faced in contesting governmental actions, magnified by the disparity between the resources and expertise of the government and individuals." *Id.* (citing Laws 1981, Ch. 208, §§ 1 and 3); *see also 4501 Northpoint*, 212 Ariz. at 100, ¶ 13 (noting that "fees generally should be awarded under § 12-348(B) when taxpayers successfully challenge the government's wrongful imposition of taxes"). "A.R.S. § 12-348 was modeled after [the federal Equal Access to Justice Act, 28 U.S.C. § 2412]" and "[f]ederal interpretations are 'persuasive' when Arizona courts interpret our state counterparts to federal statutes." *Estate of Walton*, 164 Ariz. 498, 500 (1990) (citing *New Pueblo Constructors, Inc. v. State*, 144 Ariz. 95, 109 (1985)). In contrast to the Equal Access to Justice Act, however, Arizona courts have rejected a narrow construction of § 12-348 and found that our statute provides broader authority to grant attorney's fees. *Walton*, 164 Ariz. at 501 (citing *New Pueblo Constructors*, 144 Ariz. at 111); *4501 Northpoint*, 212 Ariz. at 101, ¶ 18.

¶31 Federal courts regularly look to the extent that a party's position has been vindicated in the litigation to determine the prevailing party. For example, in federal tax collection cases, 26 U.S.C. § 7430(c)(4)(A) provides that the "prevailing party" includes "any party . . . which--(I) has substantially prevailed with respect to the amount in controversy." *See also Oliver v. United States*, 921 F.2d 916, 922 (9th Cir. 1990) ("There is little dispositive difference between [26 U.S.C. §] 7430 and [the Equal Access to Justice Act]."). Thus, courts may consider the amount by which tax liability is reduced in determining whether a taxpayer has prevailed. *See Goettee v. C.I.R.*, 124 T.C. 286, 2005 WL 1277655 (2005), *aff'd*, 192 Fed. Appx. 212 (4th Cir. 2006) (finding taxpayers were not prevailing parties where they were awarded "not quite five percent" of what they claimed should be abated); *In re Yochum*, 156 B.R. 816 (D. Nev. 1993), *rev'd on other grounds*, 89 F.3d 661 (9th Cir. 1996) (finding debtors prevailed when an IRS assessment was reduced from $480,000 to $1,400); *Cassuto v. C.I.R.*, 93 T.C. 256 (1989), *aff'd in part, rev'd on other grounds*, 936 F.2d 736 (2nd Cir. 1991) (holding that petitioners prevailed when Commissioner issued deficiency for $49,084 and parties settled on $4,684); *see also Buckhannon Bd. & Care Home, Inc. v. W. Va. Dep't of Health & Human Res.*, 532 U.S. 598, 604 (2001) (defining "prevailing party" as one who obtains a "material alteration of the legal relationship of the parties").

¶32 Accordingly, in an appropriate case, a taxpayer could "prevail" and be entitled to an award of attorney's fees under § 12-348(B) based on a significant reduction in tax liability, despite a significant judgment in favor of the state.

AMY M. WOOD • Clerk of the Court
FILED: AA