

STATE OF NEW YORK
TAX APPEALS TRIBUNAL

In the Matter of the Petition :
of :
EUGENE BOSHES : DECISION
for Redetermination of a Deficiency or for :
Refund of Personal Income Tax under Article 22 :
of the Tax Law for the Period April 1, 1980 :
through December 31, 1983 :

Petitioner Eugene Boshes, 230 Park Avenue, Suite 610, New York, New York 10169, filed an exception to the determination of the Administrative Law Judge issued on April 5, 1990 with respect to his petition for redetermination of a deficiency or for refund of personal income tax under Article 22 of the Tax Law for the period April 1, 1980 through December 31, 1983 (File No. 803296). Petitioner appeared by Richard H. Wynn, Esq. The Division of Taxation appeared by William F. Collins, Esq. (Herbert Kamrass, Esq., of counsel).

Neither party filed a brief on exception. Oral argument was requested by petitioner but was denied.

After reviewing the entire record in this matter the Tax Appeals Tribunal renders the following decision.

ISSUE

Whether petitioner, as a person required to collect, truthfully account for, and pay over withholding taxes with respect to Environmental Research and Development, Inc., is liable for the penalty pursuant to Tax Law § 685(g) for willfully failing to do so.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for finding of fact "7" which has been modified. The Administrative Law Judge's findings and the modified finding of fact are set forth below.

On January 14, 1986, the Division of Taxation issued a Notice of Deficiency and a Statement of Deficiency to petitioner, Eugene Boshes. The Statement of Deficiency stated that he was liable for a penalty under Tax Law § 685(g) which was computed as follows:

<u>Withholding Tax Period</u>	<u>Amount</u>
04/01/80 - 12/31/80	\$ 38,509.04
08/16/81 - 11/30/81	17,113.88
01/01/83 - 01/15/83	684.32
01/16/83 - 01/31/83	514.77
02/01/83 - 02/15/83	514.77
02/16/83 - 02/23/83	1,114.77
03/01/83 - 03/15/83	655.25
03/16/83 - 03/31/83	870.07
12/23/82 - 12/31/82	70,596.40
12/16/83 - 12/31/83	<u>66,054.24</u>
TOTAL	<u>\$196,627.51</u>

Subsequent to the issuance of the Notice of Deficiency and Statement of Deficiency, the Division modified the amount of penalty asserted against Eugene Boshes as follows:

<u>Withholding Tax Period</u>	<u>Amount</u>
02/16/83 - 02/28/83	\$ 514.77
12/23/82 - 12/31/82	17,657.36
12/16/83 - 12/31/83	-0-

The adjusted tax due for the periods between December 23, 1982 and December 31, 1983, therefore became \$21,411.31. Petitioner concedes his liability for this amount of penalty pursuant to Tax Law § 685(g).

Therefore, the only penalty asserted against petitioner pursuant to Tax Law § 685(g) remaining in issue is that for the period April 1, 1980 through December 31, 1980 in the amount

of \$38,509.04 and for the period August 16, 1981 through November 30, 1981 in the amount of \$17,113.88. Hence, the total amount left in dispute is \$55,622.92.

During the period left in issue, petitioner was the president of Environmental Research and Development, Inc. ("ERD"), a New York corporation which began operations in 1964. Additionally, petitioner owned one-third of the outstanding stock of said corporation.

The remainder of the stock was owned by petitioner's two partners, Stanley Morris, who was chairman and chief executive officer, and Richard Lehrer, who was executive vice president and chief operating officer. Mr. Lehrer was also treasurer and responsible for the day-to-day operations of the business, including the filing of tax returns and payment of bills.

During the period in issue, petitioner's duties primarily involved making sales of services provided by ERD, including real estate consulting, interior design and construction management. Petitioner estimated that he spent almost 85% of his time outside of the office.

ERD employed between 50 and 70 employees in the years 1980 and 1981, mostly draftsmen, engineers, field supervisors and other support staff.

Shortly after the business began in 1964, the three partners divided up the duties of the corporation, whereby Mr. Boshes took on the sales responsibilities, Mr. Morris supervised the work of the engineers and draftsmen and, as stated above, Mr. Lehrer administered the day-to-day business operations. Each of the men received equivalent salaries, had equal stock ownership, and were signatories on the corporation's checking account. Two signatories were required to sign each check.

We modify finding of fact "7" to read as follows:

During the late summer/early fall of 1981, ERD sold 20% of its stock to a group of investors for approximately \$900,040.00. The purpose of this sale was to be for the payment of outstanding bills including New York State and City Withholding taxes.¹

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The original finding of fact "7" of the Administrative Law Judge's determination read as follows:

"Sometime in 1980, ERD sold 20% of its stock to a group of investors for approximately \$900,040.00. The purpose of this sale was purported to be for the payment of outstanding bills including New York State and City withholding taxes."

Although Mr. Boshes and the firm's accountant at the time, Mr. John Herde, testified that a check payable to the proper taxing authority in the sum of approximately \$66,000.00 was drawn in late 1981 and signed by Mr. Boshes, said payment was never received by the Division of Taxation.

In January of 1982, Mr. Lehrer and Mr. Morris left ERD and formed a new corporation called Research Dynamics. Although Mr. Boshes had an oral agreement with his partners that the proceeds of the stock sale would be used to pay unpaid taxes, Mr. Boshes testified that he believed his partners diverted the funds to their new corporation.

During the period in issue, Mr. Boshes had the authority to sign checks and tax returns and to hire and fire employees. He also acknowledged that he delegated all of the day-to-day operations and management of the business to his partner including the preparation and payment of withholding taxes.

OPINION

The Administrative Law Judge determined that petitioner was a person required to collect, truthfully account for and pay over withholding taxes (a "responsible officer") and that petitioner's actions were "willful" within the meaning of Tax Law § 685(g) and that the penalty prescribed by that section, i.e., a penalty equal to 100 percent of the tax due, should be imposed on petitioner. The Administrative Law Judge found petitioner liable for the penalty for the period April 1, 1980 through December 31, 1980, and for the period August 16, 1981 through November 30, 1981.

On exception, petitioner does not challenge his status as a responsible officer for the purpose of Tax Law § 685(g). Petitioner, however, argues that his actions do not fall within the meaning of "willful" as used in § 685(g).

We affirm the determination of the Administrative Law Judge.

Tax Law § 671 requires an employer to deduct from wages paid to employees:

This fact was changed to more accurately reflect the record.

"tax computed in such a manner as to result, so far as practicable, in withholding from the employee's wages during each calendar year an amount substantially equivalent to the tax reasonably estimated to be due under this article [22] resulting from the inclusion in the employee's New York adjusted gross income or New York source income of his wages received during such calendar year."

Tax Law § 673 provides that any amount of tax actually deducted and withheld shall be deemed to have been paid to the Division of Taxation on behalf of the person from whom withheld, and such person shall be credited with having paid that amount of tax for the tax year. In effect, the section provides a credit to an employee regardless of whether the employer turns the amounts withheld over to the State.

Tax Law § 674 requires that employers must file a withholding return and pay to the Commissioner of Taxation or a depository designated by the Commissioner, the taxes required to be deducted and withheld. The section prescribes various filing periods, depending on the amount required to be deducted.

Tax Law § 675 makes the employer liable for the withheld tax and provides that any amount of tax actually deducted and withheld shall be held to be a special fund in trust for the State.

Tax Law § 676 provides that where an employer fails to deduct and withhold tax and thereafter the tax against which such tax may be credited is paid, the tax to be deducted and withheld shall not be collected from the employer, but the employer remains liable for any penalties, interest, or additions to the tax otherwise applicable for failure to deduct and withhold.

Tax Law § 681 requires the Commissioner of Taxation and Finance to examine returns and determine the proper amount of tax due; and where no return has been filed, to estimate the tax due.

Since employees are entitled to a credit (or refund) based on the taxes deducted from their wages, the State may be out-of-pocket for taxes it has never received. Alternatively, the State may not receive the tax it is entitled to if the employer fails to properly withhold tax from its

employees. Accordingly, to insure collection of the tax, the Legislature has made the tax the tax of the employer and has prescribed stringent protective measures.

One such protective measure is Tax Law § 685(g) which penalizes those persons responsible for the withholding and paying over of such funds for willfully failing to so withhold or pay over. This section provides:

"Willful failure to collect and pay over tax. - Any person required to collect, truthfully account for, and pay over the tax imposed by this article who willfully fails to collect such tax or truthfully account for and pay over such tax or willfully attempts in any manner to evade or defeat the tax or the payment thereof, shall, in addition to other penalties provided by law, be liable to a penalty equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over. No addition to tax under subsections (b) or (e) shall be imposed for any offense to which this subsection applies. The tax commission shall have the power, in its discretion, to waive, reduce or compromise any penalty under this subsection." (Emphasis added.)

The determination that petitioner is subject to the § 685(g) penalty is a two step process. First, petitioner must be a responsible officer, and second, his actions must be willful. However, merely because one is determined to be a responsible officer, it does not automatically follow that a failure to withhold and pay over income taxes is "willful" within the meaning of that term as used in § 685(g). The Court of Appeals held in Matter of Levin that the test is:

"whether the act, default, or conduct is consciously and voluntarily done with knowledge that as a result, trust funds belonging to the Government will not be paid over but will be used for other purposes No showing of intent to deprive the Government of its money is necessary but only something more than accidental nonpayment is required" (Matter of Levin v. Gallman, 42 NY2d 32, 396 NYS2d 623, 625 [emphasis added]).

The essence of the willfulness standard is that the person must voluntarily and consciously direct the trust fund monies from the State to another purpose. There need not be any particular motive for doing so, only the result that the State has not received the monies held in trust for it. Mere negligence is not enough. The fact that a penalty is imposed by § 685(g) only when the failure is willful is strong evidence that it was not intended to be imposed without personal fault (see, e.g., Slodov v. United States, 436 US 238; Brown v.

United States, 591 F2d 1136, 79-1 USTC ¶ 9285 [5th Cir 1979]; White v. United States, 372 F2d 513 [Ct Cl 1967]; Braden v. United States, 442 F2d 342, 71-1 USTC ¶ 9428 [6th Cir 1971] [interpreting analogous language in § 6672 of the Internal Revenue Code], cert denied 404 US 912).

Proof of this conscious and voluntary action is by necessity dependent on the facts and circumstances of each case. The lack of actual knowledge negates a finding that the act was voluntarily and consciously done (cf., Matter of Levin v. Gallman, *supra*, at 625 and Matter of MacLean v. State Tax Commn., 69 AD2d 951, 415 NYS2d 492, 494, affd 49 NY2d 920, 428 NYS2d 675 [where actual knowledge supported a finding of willful]). However, a responsible officer's failure can be willful, notwithstanding his lack of actual knowledge, if it is determined that the officer recklessly disregarded his corporate responsibilities including the responsibility to see that taxes were paid (Matter of Capoccia v. State Tax Commn., 105 AD2d 528, 481 NYS2d 476, 477; Matter of Ragonesi v. State Tax Commn., 88 AD2d 707, 451 NYS2d 301, 303; Matter of Flax, Tax Appeals Tribunal, September 9, 1988; cf., Reyers v. State Tax Commn., 116 AD2d 880, 498 NYS2d 199; Matter of Lyon, Tax Appeals Tribunal, June 3, 1988). This is appropriate because a responsible officer should not be able to insulate himself from liability by abandoning his responsibilities. However, we have previously held that a responsible officer can make a reasonable delegation of authority (Matter of Lyon, *supra*).

During the period April 1, 1980 through December 31, 1980, petitioner's delegation of authority for the timely filing of withholding tax returns and the payment of withholding taxes themselves may have been reasonable (see, Matter of Lyon, *supra*; Matter of Reyers v. State Tax Commn., *supra*; Matter of Gallo, Tax Appeals Tribunal, September 9, 1988 [where such facts negated a finding of willfulness]). However, we conclude that the continuation of this delegation during the second period, August 16, 1981 through November 30, 1981, was unreasonable.

During this second period, petitioner should be held to a higher level of care in discharging his fiduciary responsibility due to his awareness of the change in circumstances

within ERD. First, this was a transition period for the corporation. The corporation was in the process of selling 20% of its stock to a group of investors for approximately \$900,040.00, and petitioner, along with the other two shareholders, Messrs. Lehrer and Morris, had agreed to use the proceeds of this stock sale to pay off any outstanding obligations of ERD, including withholding taxes. Furthermore, at the beginning of the new year (1982), Lehrer and Morris were leaving ERD and spinning off ERD's computer division into a new and independent corporation leaving Boshes as the main principal of ERD. Secondly, during this period petitioner clearly had knowledge of taxes owing and due to the Division. This knowledge is evidenced both by petitioner's allegation that he signed a check for payment of the outstanding taxes and by the corporation's need to raise funds to pay past tax obligations.

Petitioner's actions during this second period should have reflected his knowledge of the past due withholding taxes and the fact that the individual on whom he relied was planning to leave the corporation (taking part of the corporation's assets with him) and had not in the past discharged the responsibility of paying over taxes which were due and owing. Instead, petitioner merely continued to delegate away his authority to file and pay withholding taxes until both of his co-officers and co-shareholders had left the corporation, and the corporation no longer had sufficient funds to pay past due withholding taxes. Since corporate officers responsible for withholding taxes cannot insulate themselves from a finding of "willfulness" by disregarding their duties and leaving them to someone else to discharge (see, Matter of Basch v. State Tax Commn., 134 AD2d 786, 521 NYS2d 840; Matter of Capoccia v. State Tax Commn., supra; Matter of Ragonesi v. State Tax Commn., supra; Matter of Davison, Tax Appeals Tribunal, November 23, 1988), we conclude that petitioner willfully failed to collect and pay over the tax due for the period August 16, 1981 through November 30, 1981.

We also conclude that petitioner's actions during the period ended November 30, 1981 make him liable for the taxes which accrued during the earlier period. Although aware that the corporation owed taxes, petitioner failed to ensure that the funds raised by the stock offering were in fact paid over to the Division. Since petitioner was a responsible person, both at the

time the tax liability accrued and thereafter, he had a duty to apply any available unencumbered funds to reduction of accrued withholding tax liability, whether or not those funds are deemed to be trust funds within the meaning of Tax Law § 675 (see, Mazo v. United States, 591 F2d 1151, 79-1 USTC ¶ 9284 at 86,622 [interpreting analogous language in § 7501 of the Internal Revenue Code]). As discussed above, reliance on Lehrer, who petitioner knew had failed to pay the taxes in the past, was a reckless disregard of this duty. Accordingly, petitioner is liable for taxes for both periods as determined by the Administrative Law Judge.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Eugene Boshes is denied;
2. The determination of the Administrative Law Judge is affirmed;
3. The petition of Eugene Boshes is denied; and
4. The Notice of Deficiency issued on January 14, 1986, as modified herein, is sustained.

DATED: Troy, New York
November 29, 1990

/s/John P. Dugan
John P. Dugan
President

/s/Francis R. Koenig
Francis R. Koenig
Commissioner

/s/Maria T. Jones
Maria T. Jones
Commissioner