

STATE OF NEW YORK
TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
GEORGE E. BAILEY	:	DECISION
for Redetermination of a Deficiency or for	:	DTA No. 806321
Refund of Personal Income Tax under Article 22	:	
of the Tax Law for the Year 1976.	:	

Petitioner George E. Bailey, 1016 Glenwood Boulevard, Schenectady, New York 12308, filed an exception to the determination of the Administrative Law Judge issued on January 7, 1993. Petitioner appeared pro se. The Division of Taxation appeared by William F. Collins, Esq. (Arnold M. Glass, Esq., of counsel).

Petitioner filed a brief on exception. The Division of Taxation filed a letter brief. Petitioner submitted a reply which was received June 9, 1993 and began the six-month period for the issuance of this decision. Oral argument, requested by petitioner, was denied.

Commissioner Koenig delivered the decision of the Tax Appeals Tribunal. Commissioner Dugan concurs.

ISSUES

I. Whether petitioner is subject to a penalty imposed pursuant to Tax Law § 685(g) as a person who willfully failed to collect, truthfully account for and pay over withholding taxes due.

II. If so, whether petitioner is liable for the entire penalty or whether the Division of Taxation should attempt to collect a proportionate share thereof from the other corporate officer and shareholder.

III. Whether Article 3-A of the Lien Law precludes the Division of Taxation from proceeding against petitioner.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge. These facts are set forth below.

Bailey Construction Company, Inc. ("Bailey Construction"), incorporated in 1969, is a construction company operating primarily as a general contractor performing public improvement contracts for governmental entities. Petitioner, George E. Bailey, president of the corporation, and his wife, Constance Bailey, secretary-treasurer, were sole owners of Bailey Construction, each holding a 50 percent share of the corporation's stock. Petitioner drew a salary from Bailey Construction and was responsible for designing and bidding projects, and providing oversight for purchasing and project completion. Petitioner hired most of the employees with the exception of tradesmen, who were typically hired by the foreman or field superintendent of a particular project. All of the financial aspects of the corporation such as banking and payroll were controlled by petitioner and his wife. Additionally, both had check-signing authority. Petitioner signed payroll checks and tax returns. It was also petitioner's decision not to remit the withholding taxes at issue, and he admitted the taxes have remained unsatisfied.

During the hearing when petitioner was asked by the Administrative Law Judge whether he would concede that "without any argument, that pursuant to the New York State Tax Law that [he] would fall under the category of an officer who is responsible for the management and general operations of the corporation?", he responded in the affirmative.

Bailey Construction, on January 6, 1977, submitted Forms IT-2101, Employer's Return - Personal Income Tax Withheld, to the New York State Income Tax Bureau for the following periods:

10/16/76 - 10/31/76
11/1/76 - 11/15/76
11/6/76 - 11/30/76
12/1/76 - 12/15/76
2/16/76 - 12/31/76

The Division of Taxation ("Division") was referred to Peerless Insurance Company ("Peerless") for payment. Payment bonds were in effect for the projects performed which resulted in

withholding taxes due. Petitioner asserts all monies owed for labor expended were payable under the bonds. The projects under construction were public projects performed for New York State as follows:

Gore Mountain Ski Center
Phase I - Pompously
North Creek, New York
General Construction Contract (a) Bond #P663762

Coxsackie Correctional Facility
Construction Work for Alterations and Improvements at
Laundry Building #52
Bond #P667892

The Division contacted Peerless but was unsuccessful in collecting payment. Petitioner believed this was because the statute of limitations period of one year on payment bonds ran before the State sought collection. In a letter dated August 4, 1978, the Division notified Bailey Construction that since Peerless did not satisfy the claim for withholding taxes due, Bailey Construction would be "totally liable for any and all tax liabilities."

A warrant was issued by the State Tax Commission against Bailey Construction, on November 20, 1980 and filed by the County Clerk's Office in Schenectady, New York on November 21, 1980 for the periods of October 16, 1976 through October 31, 1976, November 1, 1976 through November 15, 1976, and December 1, 1976 through December 15, 1976. The warrant referenced assessment numbers W7703296294, W7708012820 and W7703296297 for taxes in the total amount of \$1,313.10, plus penalty and interest in the amount of \$985.49.

On September 30, 1982, the Tax Compliance Division corresponded with petitioner and his wife informing them that both Mr. and Mrs. Bailey "[a]s individual officers, . . . are liable for paying withholding tax."

Levies were served by the Division at Schenectady Trust and Pioneer Savings Bank on August 4, 1988¹ in an attempt to satisfy the outstanding warrant. Both banks responded

¹Included in Exhibit "G" is a Tax Compliance Division contact sheet, which indicated that levies were served at Mohawk National, 1st National and Key Bank as well, but only copies of

separately by letters dated August 8, 1988, stating their records did not show any accounts under the name Bailey Construction, and they were, therefore, unable to remit payment.

On December 11, 1987, the Division issued a Notice of Deficiency to petitioner for a penalty in the amount of \$1,313.10 for willful failure to pay over withholding taxes due. A conciliation conference was conducted on July 26, 1988 and on August 19, 1988, a Conciliation Order was issued sustaining the notice. On November 21, 1988 and January 8, 1991, respectively, petitioner filed a petition and an amended petition for redetermination of the deficiency. In his petition, petitioner alleged:

- The Division failed to show the tax alleged due has not been paid nor has the Division established a ground for the imposition of any penalty.
- Since there are two officers of Bailey Construction Company, Constance Bailey, the other officer, should be ordered to appear in this proceeding as a party to share petitioner's liability.
- The liability at issue arose from the performance of a public contract; therefore, Article 3-A of the Lien Law operates in this instance instead of the Tax Law, thereby making the Notice of Deficiency unenforceable.

In this instance, the labor expenses and withholding tax liability arose from public improvement contracts between Bailey Construction and New York State. Petitioner explained that under Article 3-A of the Lien Law, monies owed to Bailey Construction for performing the project were paid directly by the governmental entity into a separate trust fund created especially for each project in order to finance that particular project. Bailey Construction did not receive money directly from the government. The purpose of Article 3-A is to prevent funds for one project from being used in financing another project, thereby preventing improper beneficiaries from collecting monies owed. The beneficiaries are the various creditors of the project, one of which was New York State Department of Taxation and Finance. Bailey Construction served as trustee to the trust ensuring proper distribution to the beneficiaries. Therefore, even though the

levies and responses to levies from Schenectady Trust and Pioneer Savings Bank were submitted into evidence.

contract was performed by Bailey Construction and its employees, petitioner contends that due to provisions in the Lien Law, the withholding tax would be improperly paid if its source was other than the trust fund established for the project. Petitioner maintains he is protected by the Lien Law and therefore cannot be held liable for taxes which must be paid from the trust.

Another complication arose from the performance of this project when New York State failed to pay money into the trust for distribution to the beneficiaries. Bailey Construction, as trustee, brought an action in the Court of Claims against New York State for recovery of funds owed to the trust. By order dated December 13, 1983, the court determined that the State of New York owed damages in the amount of \$43,000.00. However, petitioner contends that the \$43,000.00 less legal expenses of \$8,600.00 was not received by the trustee, but was diverted by an order of the Supreme Court of the State of New York, County of Schenectady, on November 8, 1984, and paid out to other improper beneficiaries. Therefore, pursuant to section 77 of the Lien Law, the Division's only recourse is to bring an action, along with Bailey Construction, as trustee, to enforce the trust in order to recover any outstanding taxes.

Conversely, the Division maintains that the corporation is liable for withholding tax arising from compensation paid to employees of Bailey Construction. Since satisfaction of the tax could not be obtained from the corporation, the notice was properly issued against petitioner, as a responsible officer of Bailey Construction under Tax Law § 685(g).

OPINION

In the determination below, the Administrative Law Judge held that under Tax Law § 685(n), petitioner is a person required to collect, truthfully account for and pay over withholding taxes for Bailey Construction Company, Inc. and, further, "[s]ufficient evidence exists to conclude petitioner willfully failed to pay the tax within the meaning of Tax Law § 685(g) in that he knowingly and voluntarily disregarded his obligation under the statute" (Determination, conclusion of law "B"). Therefore, the Administrative Law Judge concluded

that petitioner was "liable to a penalty equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over" (Tax Law § 685[g]).

The Administrative Law Judge also held that petitioner may not use as a defense to the penalty that the Division failed to proceed against another officer who may be equally liable.

In addition, the Administrative Law Judge rejected petitioner's contentions and claims relating to Article 3-A of the Lien Law. The Administrative Law Judge concluded that the Lien Law's directions as to how trust assets are to be applied by the contractor/trustee did not insulate petitioner in his personal capacity from liability for the tax. The Administrative Law Judge also rejected petitioner's assertion that the Supreme Court improperly diverted funds in First Natl. Bank of Scotia v. Bailey Constr. (Sup Ct, Schenectady County, Nov. 8, 1984, Mercure, J.).

Finally, the Administrative Law Judge held that petitioner never met his obligation to see that monies actually withheld from employees' income taxes were held in a special trust fund for the tax commission, thus, the penalty must stand and the Notice of Deficiency dated December 11, 1987 was sustained in its entirety.

On exception, petitioner argues that under Article 3-A of the Lien Law the Division's claim is against the trust fund and not the property of the company or petitioner. Petitioner further argues that: 1) Tax Law § 685(g) is inapplicable to the company and its officers; 2) since the State withheld trust funds from the Trust, Tax Law § 678 applies to the State itself; 3) the Court of Claims' award of damages were actually trust funds under Article 3-A of the Lien Law; 4) the Supreme Court action of November 8, 1984 did not comply with Lien Law § 77 and said action is prohibited by law as the Court had no authority to order a distribution of Trust assets; and 5) the Trust exists, it is funded and the Division remains a beneficiary and the company remains trustee.

Finally, petitioner argues that the Division must be ordered to proceed as the beneficiary of the Trust to collect the tax, the other corporate officer must be brought into this proceeding, and

the Administrative Law Judge erred in stating that one of the Public Improvement Contracts was for work at the Coxsackie Correctional Facility.

The Division argues that the Administrative Law Judge correctly determined that petitioner was liable for the penalty imposed, properly found that the statutory standard of willfulness was met and was also correct in deciding the Lien Law is irrelevant to petitioner's liability. In arguing that petitioner's exception should be denied and the determination sustained, the Division cited to Matter of Yellin v. New York State Tax Commn. (81 AD2d 196, 440 NYS2d 382) for the principle that the "penalty under section 685(g) against a corporate officer is independent of and not derivative from or secondary to the corporation employer's liability."

In reply to the Division's letter brief, petitioner argues:

"under contracts for public improvements in New York State the contractor does not make payment of wages, nor does it deduct anything from anyone's wages. Such payments, etc. are the obligation of the State. Contractor's officers then are not required to collect/deduct either. The contractor is the Trustee and acts as directed by Lien Law Article 3-A" (Petitioner's response letter).

We affirm the determination of the Administrative Law Judge. Petitioner raises on exception the same arguments raised at hearing.

The Administrative Law Judge completely and correctly addressed the issues before her, and we affirm her determination for the reasons stated therein.

We do, however, find it necessary to address petitioner's claim that the Administrative Law Judge erred in stating one of the Public Improvement Contracts was for work at the Coxsackie Correctional Facility.

We disagree with petitioner. In the record below, Division's Exhibit "H" is a letter dated January 6, 1977 on Bailey Construction Company stationery wherein IT-2101 returns were forwarded for the periods in question with a listing of the projects to which the returns applied, Project "C" being the Coxsackie Correctional Facility.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of petitioner George E. Bailey is denied;
2. The determination of the Administrative Law Judge is affirmed;
3. The petition of George E. Bailey is denied; and
4. The Notice of Deficiency dated December 11, 1987 is sustained.

DATED: Troy, New York
November 24, 1993

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

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