

STATE OF NEW YORK
DIVISION OF TAX APPEALS

In the Matter of the Petition :
of :
GEORGE N. STAMAS : DETERMINATION
for Redetermination of a Deficiency or for : DTA NO. 809954
Refund of Personal Income Tax under Article 22 :
of the Tax Law for the Years 1985 and 1986. :

Petitioner, George N. Stamas, 1623 Third Avenue, Apt. 34J, New York, New York 10128, filed a petition for redetermination of a deficiency or for refund of personal income tax under Article 22 of the Tax Law for the years 1985 and 1986.

A hearing was held before Joseph W. Pinto, Jr., Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on November 3, 1992 at 1:15 P.M., with all briefs filed by January 8, 1993. Petitioner appeared pro se. The Division of Taxation appeared by William F. Collins, Esq. (Gary Palmer, Esq., of counsel).

ISSUE

Whether petitioner is liable for penalties under Tax Law § 685(g) for the unpaid withholding taxes of Advanced Care Systems, Inc.

FINDINGS OF FACT

On August 24, 1990, the Division of Taxation ("Division") issued to George Stamas a Statement of Deficiency which set forth penalty due under Tax Law § 685(g) in the sum of \$10,646.00 for the withholding tax period July 1, 1985 through December 31, 1985. Said statement also provided the definition of the term "person" as defined in Tax Law § 685(n) and the provisions of Tax Law § 685(g) which provide that any person required to collect, truthfully account for, and pay over the tax imposed by the income tax law who willfully fails to do so shall be liable to a penalty equal to the total amount of the tax due. The Statement of Deficiency indicated that available information indicated that Mr. Stamas was a person liable

for this penalty.

Along with the issuance of said Statement of Deficiency, on August 24, 1990, a Notice of Deficiency was issued to George Stamas which set forth a total penalty due of \$10,646.00.

On August 24, 1990, the Division issued to George Stamas a second Statement of Deficiency which set forth penalty due under Tax Law § 685(g) in the sum of \$359.00, for the withholding tax period January 1, 1986 through December 31, 1986. On the same date, the Division issued to George Stamas a Notice of Deficiency which set forth penalty due for the year 1986 in the sum of \$359.00.

Once again, the Statement of Deficiency for the year 1986, dated August 24, 1990, indicated that available information indicated that Mr. Stamas was the person liable for the penalty under section 685(g).

On or about June 25, 1982, two individuals, Dr. Leonard Primes and Thomas Young, assigned all of their right, title and interest to a composition for detoxification, "Miratox", to Sypco Research and Development Corporation, a Delaware corporation having a principal place of business in Massapequa, New York. The compound "Miratox" allegedly had the potential for providing major breakthroughs in the detoxification of alcoholics and drug abusers.

Sypco Research and Development Corporation was incorporated on May 14, 1982 in the State of Delaware, and was authorized to do business in the State of New York on August 4, 1983. Subsequently, on January 8, 1985, Sypco filed a Notice of Change of Name with the New York State Department of State, indicating that its new name was Advanced Care Systems, Inc.

Pursuant to an employment agreement between Sypco and petitioner, dated July 26, 1984, petitioner was hired as the president, chief operating officer and chief financial officer of Sypco Research and Development Corporation for a period of 24 months.

Pursuant to paragraph "4" of said employment agreement, petitioner's specific duties were defined as follows:

"4. Employee's duties. During the period of employment Employee shall devote his full business time and energies to the business and affairs of Employer and shall

perform his duties on a full time basis utilizing his best efforts, skills and abilities to promote Employer's interests. Employee's primary area of responsibility shall be the management operations, and financial affairs of the Employer subject to direction and control of the Chief Executive Officer and the Board of Directors."

Petitioner agreed to accept a salary of \$60,000.00 per annum with at least an annual review and adjustment. The agreement specifically provided in paragraph "5(d)" that all compensation was to be subject to the customary withholding tax and other employment tax.

The employment agreement also provided in paragraph "12" that the employee would receive, in consideration of accepting the position of president and chief operating officer, 5,000 shares of Sypco common stock at the price of \$.01 per share.

The employment agreement also provided in paragraph "14" that the employee:

"warrants and represents that he has had full and complete access to the books and records of the company, has had the opportunity to review a preliminary draft of a Form S-18 registration statement the Corporation plans to file with the Securities and Exchange Commission (the 'Commission') and that he is aware that the Corporation is totally dependent upon the receipt of the proceeds of the shares to be sold pursuant to said registration statement for its future activities and that there can be no assurance that any of such shares will in fact be sold."

The employment agreement also provided that petitioner would be elected to Sypco's board of directors following execution of the employment agreement.

Petitioner explained that he was hired by Sypco in order to develop a business plan for the corporation and to guide the corporation through the Food and Drug Administration's application process for the corporation's chief asset, the compound "Miratox". It is noted that the Food and Drug Administration's testing process involves three separate phases. The first phase, only achieved after significant testing, is one in which the compound is proved safe. The second phase requires a demonstration of the compound's efficacy. The third phase is the time period in which the compound must be demonstrated to be safe and efficacious on human beings.

There were four original partners in the corporate entity Sypco: Dr. Leonard Primes, Murray Corn, Thomas Young and John Sullivan. In 1983 they were joined by an entrepreneur by the name of Donald McShane who was granted 15% of the stock for his \$500,000.00 investment contribution. The original four partners retained 15% each, and granted 25% of the

stock to a group of 45 to 50 investors.

In 1983, petitioner purchased 1,000 additional shares of Sypco stock for \$3,000.00 as part of a group led by Donald McShane, bringing his total investment to 6,000 shares. Petitioner actually worked for Sypco and its successor, Advanced Care Systems, Inc., between March of 1984 and September of 1986, receiving compensation for only about half of that period.

During the term of his employment, petitioner appeared to carry out his duties as president and chief operating officer of the corporation. He was a signatory on the corporation's only operating bank account, a checking account at the Chase Manhattan Bank on East 42nd Street in New York City. Petitioner was authorized to issue checks with a maximum value of \$500.00 to \$1,000.00. The secretary-treasurer of the company, Mr. Alfred Welsome, was also a signatory on the same account.¹ Petitioner signed various filings with the New York State Department of Taxation and Finance, including two applications for three-month extension for filing tax reports on July 17, 1985 and September 19, 1985, as president of Advanced Care Systems, Inc.; two metropolitan transportation business tax surcharge reports for the periods ended April 30, 1985 and April 30, 1986, signed as president of Advanced Care Systems, Inc.; and the corporation franchise tax reports filed for the fiscal years ended April 30, 1985 and April 30, 1986.

On the Schedule "F" attached to the New York Corporation Franchise Tax Report for the fiscal year ended April 30, 1985, Mr. Stamas was listed as an officer of the corporation receiving a salary or other compensation in the sum of \$35,000.00. On the New York Corporation Franchise Tax Report for the fiscal year ended April 30, 1986, Schedule "F" listed Mr. Stamas as an officer receiving salary or compensation in the sum of \$65,000.00.

With regard to the withholding tax at issue herein for the year 1985 and 1986, Advanced Care Systems, Inc. filed reconciliation statements indicating total New York State and New York City taxes withheld and the balance due for each year. The reconciliation statement

¹Petitioner speculated that Dr. Primes also was a signatory on the checking account.

submitted for the year 1985 indicated a balance due of \$10,646.00 and was signed on "2/15" by Alfred W. Welsome. The 1985 statement indicated a tax due in June of that

year in the sum of \$582.98. The reconciliation statement for the year 1986 was filed on February 2, 1987 and was signed by George N. Stamas, as president. The latter statement indicated total New York State and New York City taxes withheld in the sum of \$359.00.

Throughout the time petitioner was employed by the company, there were never more than four or five employees.

Emphasizing petitioner's stature with the company, and his position as president and chief operating officer, was his July 31, 1984 letter to Mr. John Sullivan, accepting Mr. Sullivan's resignation as secretary-treasurer and director of Sypco. Mr. Stamas signed the letter as president of Sypco Research and Development Corp. and accepted the resignation on behalf of himself and "Lenny" (Dr. Leonard Primes, chairman of the board of directors and chief executive officer of Sypco).

The initial capital contributions to the corporation were quickly consumed by the cost of testing, salaries and administration. Over the period October 1, 1984 through October 27, 1986, Donald McShane made additional contributions in the sum of \$67,510.00. Whenever additional contributions were made to the corporation, their specific use was authorized and directed by Mr. McShane and Dr. Primes. Petitioner had no authority to make any payments without the specific authority and direction of Dr. Primes or Mr. McShane.

Petitioner believed that the flow of funds ended approximately the same time his salary ended in the fall of 1985. From that point on, all funds flowing to the corporation were used for administrative costs such as rent, telephone, electricity and laboratory costs. Neither taxes nor salaries were paid from investment funds directed to the corporation after the fall of 1985.

Petitioner testified that he notified both Dr. Primes and Mr. McShane of the Federal and New York State tax liabilities and was successful in resolving all taxes due with the Federal government. However, he was never successful in acquiring the funds from Dr. Primes or

Mr. McShane to pay the New York State withholding taxes due.

During the years in issue, the board of directors of Advanced Care Systems, Inc. was composed of Dr. Primes, Mr. Stamas, Dr. Bernard Bihari and a fourth individual whose identity was not disclosed in the record. Board of directors meetings were held approximately every six months at Donald McShane's residence in New York City and it was at these meetings that the company's business agenda was set.

Petitioner testified that the corporation utilized the services of an accounting firm by the name of Bernard Wind and Company. The accounting firm prepared all filings made to the New York State Department of Taxation and Finance on behalf of the corporation, including the withholding tax reconciliation statements and returns. Either petitioner or Mr. Welsome prepared the checks for payment of the taxes due to both the Federal and New York State authorities.

Mr. Stamas submitted into evidence two letters to Dr. Primes written by himself on July 2, 1992 and August 17, 1992 pleading with Dr. Primes to resolve the instant matter by paying the outstanding taxes due. Allegedly, neither of these letters was responded to by Dr. Primes.

Petitioner testified that he received a salary until approximately November of 1985. He was also aware that withholding taxes were not being paid sometime earlier in the year 1985. However, petitioner testified that he was confident at that time that the company would be able to meet its tax obligations. As the incoming funds were directed to the payment of rent, telephone and electric bills and laboratory costs, it became apparent that there were insufficient funds to meet the tax obligations.

The conciliation conference was held on May 22, 1991 and, as a result, the statutory notices of deficiency at issue herein were sustained in full by order dated June 21, 1991.

SUMMARY OF PETITIONER'S POSITION

Essentially, petitioner argues that the liability rests with the ongoing concern, i.e., Advanced Care Systems, Inc. and its principals, Dr. Leonard Primes and Donald McShane.

Petitioner contends that he is not a responsible person because of the clear language in his employment contract which indicates that his responsibility for the management operations and financial affairs of the company would be subject to the direction and control of the chief executive officer and the board of directors.

Petitioner believes that he did not have meaningful control over the corporation and therefore could not direct payment of the withholding taxes in issue at the time they were due and that Dr. Primes and Mr. McShane held this ultimate authority.

CONCLUSIONS OF LAW

A. Tax Law § 685(g) penalizes those persons responsible for the withholding and paying over of such funds for willfully failing to do so. This section provides, in pertinent part, as follows:

"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."

Tax Law § 685(n) defines "person" subject to the section 685(g) penalty as follows:

"Person defined.--For purposes of subsections (g), (i), (o), (q), and (r), the term person includes an individual, corporation or partnership or an officer and employee of any corporation (including a dissolved corporation), or a member or employee of any partnership, who as such officer, employee, or member is under a duty to perform the act in respect of which the violation occurs."

It is determined that petitioner has not established that he was not a person required to pay over withholding tax and that he did not prove that his failure was not willful.

The question of whether an individual is a person within the meaning of Tax Law § 685(n) is a factual one (see, Matter of Ragonesi v. New York State Tax Commn., 88 AD2d 707, 451 NYS2d 301), "resolution of which turns on such factors as whether the taxpayer owned stock, signed the tax returns, exercised authority over employees and assets of the corporation, derived substantial income from the corporation, or served as an officer or employee thereof" (Matter of Capoccia v. State Tax Commn., 105 AD2d 528, 481 NYS2d 476).

Petitioner's argument that Advanced Care Systems, Inc. remains a going concern and

therefore should be liable for the withholding tax in issue does not recognize his personal liability as a person subject to section 685(g) penalty. The fact that the corporate entity or other individuals might also be "persons" required to collect, truthfully account for, and pay over the tax imposed herein is not relevant to petitioner's liability.

Petitioner's argument that he is not liable for the collection and paying over of the withholding tax herein because he was subject to the direction and control of Dr. Primes and the board of directors, as specifically set forth in the fourth paragraph of the employment agreement, requires more analysis.

The indicia of responsibility is virtually identical for both sales and use taxes and withholding tax. In the Matter of Constantino (Tax Appeals Tribunal, September 27, 1990), which specifically dealt with an individual's liability for sales and use taxes, several indicia were established for use in determining officer liability. The Tribunal stated:

"The question to be resolved in any particular case is whether the individual had or could have had sufficient authority and control over the affairs of the corporation to be considered a responsible officer or employee. The case law and the decisions of this Tribunal have identified a variety of factors as indicia of responsibility: the individual's status as an officer, director, or shareholder; authorization to write checks on behalf of the corporation; the individual's knowledge of and control over the financial affairs of the corporation; authorization to hire and fire employees; whether the individual signed tax returns for the corporation; the individual's economic interests in the corporation [citations omitted]" (Matter of Constantino, Tax Appeals Tribunal, supra).

These are some of the factors which are typically weighed in determining responsibility (see, Matter of Ragonesi v. New York State Tax Commn., supra; Matter of Capoccia v. New York State Tax Commn., supra). The record in the instant matter clearly indicates that petitioner fits squarely within the classic definition of a responsible person. Mr. Stamas was the president and chief operating officer of Advanced Care Systems, Inc. during the years in issue, he was a member of the board of directors, he received the highest compensation of any officer during the years in issue, he was one of two or possibly three signatories on the company's checking account, he is one of two persons who had the authority to issue payroll checks, checks for taxes and dealt directly with the corporation's accounting firm. He signed numerous tax forms and reports including the withholding tax reconciliation statement for 1986; he was totally involved

in the day-to-day operations of the corporation; he was a shareholder and investor in the corporation, and he spent all of his time in the business of the corporation.

However, the ultimate issue raised by the Constantino case is the issue of "sufficient authority and control over the affairs of the corporation" and "control over the financial affairs of the corporation." The instant record indicated that petitioner had the duty to see that withholding tax returns were prepared and that the taxes were paid. In fact, he or Mr. Welsome, the secretary of the corporation, would sign said checks. When the corporation began encountering difficult financial times in 1985, petitioner was aware that debts needed to be prioritized.

The Division raised a critical point in its brief when it noted that Mr. Stamas drew the single largest salary of any corporate employee during the audit period until November of 1985 when petitioner ceased drawing a salary. However, the Division accurately noted that petitioner was aware sometime earlier in 1985, as money was continuing to flow into the corporation, that taxes were not being paid but that petitioner was confident the corporation would be able to meet its tax obligations. As it turned out, petitioner's confidence was misplaced. The corporation chose to pay rent, telephone and electric bills and laboratory costs until its funds were entirely depleted and the withholding tax remained unpaid. Such economic difficulties did not relieve petitioner of his authority to act on behalf of the corporation in respect of its withholding tax obligations while there were available funds (see, Allen v. State Tax Commn., 126 AD2d 51, 512 NYS2d 916; Matter of Dworkin Const. Co., Tax Appeals Tribunal, August 4, 1988). In Dworkin, the Tribunal succinctly stated that, "mere economic difficulties are not an excuse for the failure to pay taxes . . . [and] [t]o allow the payment of taxes to be postponed on account of financial difficulties would seriously impede the ability of the State to raise revenue through taxes" (Matter of Dworkin Construction Co., Tax Appeals Tribunal, supra).

Therefore, petitioner is determined to have been a person required to collect, truthfully account for and pay the withholding tax herein. His assertion that he was subject to the control

and direction of Dr. Primes and the board of directors is unconvincing since he was one of the four board members and also had the knowledge of the taxes due and the ability and authority to pay them in 1985, but chose not to in reliance upon his confidence that the corporation would be able to pay later in the year. This same rationale holds true for 1986 as well.

B. Merely because one is determined to be a person so required does not mean that a failure to withhold and pay over income taxes was "willful" within the meaning of that term as used in Tax Law § 685(g) (see, Matter of Davison, Tax Appeals Tribunal, November 23, 1988).

The courts have held that more is required and 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 non-payment is required" (Matter of Levin v. Gallman, 42 NY2d 32, 34, 396 NYS2d 623).

As stated in the Davison case:

"The essence of the willfulness standard is that the person must voluntarily and consciously direct the trust fund monies from the State to someone else. 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" (Matter of Davison, supra).

It is found herein that petitioner consciously directed the withholding taxes in question for the payment of administrative costs (including his own salary until November 1985) and lab fees while simultaneously misjudging the future flow of income or capital contributions to the corporation, thus bringing his conduct within the "willful" standard articulated in Davison (supra).

C. The petition of George N. Stamas is denied, and the two notices of deficiency dated August 24, 1990 are sustained.

DATED: Troy, New York
July 1, 1993

/s/ Joseph W. Pinto, Jr.
ADMINISTRATIVE LAW JUDGE