STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petitions of **HAROLD RASHBAUM, AS OFFICER OF U.S. GENERAL SUPPLY CORP.** for Revision of Determinations or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the Period September 1, 1985 through November 30, 1988.	:	DECISION DTA Nos. 810446, 810447, 810448 and 810449
In the Matter of the Petitions of **MURRAY HARROW, AS OFFICER OF U.S. GENERAL SUPPLY CORP.** for Revision of Determinations or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the Period September 1, 1985 through November 30, 1988.	:	

Petitioners Harold Rashbaum, as officer of U.S. General Supply Corp., 70-25 Yellowstone Boulevard, Forest Hills, New York 11375, and Murray Harrow (deceased), as officer of U.S. General Supply Corp., c/o Howard Harrow, Esq., 2 Charlton Street, Suite 16B, New York, New York 10014, filed an exception to the determination of the Administrative Law Judge issued on February 3, 1994. Petitioners appeared by DeGraff, Foy, Holt-Harris & Mealey, Esqs. (James H. Tully, Jr., Esq., of counsel). The Division of Taxation appeared by William F. Collins, Esq. (James P. Connolly, Esq., of counsel).

Petitioners submitted a brief in support of their exception received on April 20, 1994. The Division of Taxation submitted a brief in opposition to petitioners' exception received on May 27, 1994. Petitioners submitted a reply brief received on June 20, 1994, which date began

the six-month period for the issuance of this decision. Petitioners' request for oral argument was denied.

The Tax Appeals Tribunal renders the following decision per curiam.

ISSUE

Whether the Division of Taxation can be estopped from asserting sales and use taxes against two corporate officers when it failed to assert a claim for taxes against the corporation during the course of bankruptcy proceedings.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge except for finding of fact "5" which has been modified, in part, as proposed by petitioners. The Administrative Law Judge's findings of fact and the modified finding of fact are set forth below.

Petitioners, Murray Harrow and Harold Rashbaum, were chairman and vice-chairman, respectively, of U.S. General Supply Corp. ("U.S. General"). U.S. General was a retail supplier of tools and hardware. It operated stores in 10 states and conducted a large mail order business. The Division of Taxation ("Division") began an audit of U.S. General in July 1988 for the period September 1, 1985 through May 31, 1988. The auditor assigned to the case contacted U.S. General's chief finance officer on August 15, 1988 and was told that the corporation was planning to file a petition in bankruptcy under Chapter 11 of the Bankruptcy Code within the next week. The auditor was asked to hold the audit in abeyance until the corporation made a final decision regarding the bankruptcy proceeding.

Between August 15, 1988 and September 23, 1988, the auditor made several phone calls to employees of U.S. General, including Charlotte Burns, the office manager, and Joseph Septimus, the new chief finance officer. He was informed that U.S. General filed a voluntary petition in bankruptcy on September 23, 1988 and that the claims bar date (the date set by the bankruptcy judge for the filing by creditors of claims against the debtor) was December 23, 1988. The auditor scheduled audit appointments on October 13 and October 14, 1988. On

those dates, he began reviewing U.S. General's records and transcribing information. On October 21, 1988, he informed the Division's Bankruptcy Unit that a petition in bankruptcy had been filed by U.S. General.

U.S. General was a large operation with voluminous sales and purchase transactions. From the first audit appointments in October 1988 through the beginning of February 1989, the auditor spent approximately two weeks of actual audit time reviewing available books and records and establishing an audit plan. The audit was further complicated by the reorganization of U.S. General being undertaken under the bankruptcy plan. For instance, U.S. General's mail order business was no longer in operation, and employees knowledgeable about this area were no longer employed by U.S. General. The Division decided to use a computer-assisted statistical sampling method to estimate tax due in the area of expense purchases, and a great deal of time was devoted to setting up the electronic data processing programs necessary for this type of audit. During this time period, the auditor was in contact with Charlotte Burns, U.S. General's office manager; Philip Mendolia, U.S. General's comptroller for a time; and Jerry Dresel, Mr. Mendolia's replacement. U.S. General rehired on a part-time basis Donna Lindberg, a former employee familiar with U.S. General's computer systems, to assist in the electronic data processing audit.

In February 1989, U.S. General appointed three individuals to represent it in connection with the sales and use tax audit for the period September 1, 1985 through November 30, 1988, Stanley Chrein, Ralph Steinman and Roberta A. Strasberg. The power of attorney filed with the Division was signed by Harold Rashbaum, as president of U.S. General, on February 17, 1989.

We modify the Administrative Law Judge's finding of fact "5" to read as follows:

> The audit proceeded from October 1988 through April 1990. The auditor's written log documents an ongoing stream of communication between the Division's auditor and representatives of U.S. General, primarily Ms. Strasberg and Mr. Dresel. On February 17, 1989, the auditor reviewed the expense accounts with Mr. Dresel, in preparation for setting up a statistical sampling audit. The auditor spent some time in March 1989 reviewing the records provided and discussing the audit plan with the Division's Electronic Data Processing Unit. He sent Ms. Strasberg various reconciliations and workpapers on March 13, 1989. He spoke to Ms. Strasberg at least once in April and met with her, Ms. Lindberg and Mr.

Dresel in May 1989. In June and July 1989, the auditor performed various reconciliations and calculations having to do with the statistical sampling audit. He met with Ms. Strasberg again in September 1989 to review the audit findings. Apparently, it was at this point that Ms. Strasberg questioned the use of a test period computer-assisted audit. The auditor's log shows that he spoke with Ms. Strasberg by telephone twice in October 1989. He received additional information from U.S. General by mail on October 31, 1989. In November 1989, the Division issued a Statement of Proposed Audit Adjustment to U.S. General. The Division also requested that a written agreement to a test period audit be signed and was refused. The auditor spoke to Ms. Strasberg again in December 1989. Most of the communication with representatives of U.S. General involved various requests by the Division, including its request that U.S. General execute a written consent to a test period audit and requests for additional books and records. In a letter to Ms. Strasberg dated January 9, 1990, the Division stated in part:

"PURSUANT TO OUR TELEPHONE CONVERSATION THIS MORNING, SINCE U.S. GENERAL SUPPLY CORP. HAS RESCINDED ITS VERBAL AGREEMENT TO A TEST PERIOD AUDIT, AND WILL NOT SIGN AN EXTENTION [sic] WAIVER, IT IS NECESSARY THAT ALL INVOICES FOR THE AUDIT PERIOD 9/1/85-9/23/88 FOR THE FOLLOWING EXPENSE ACCOUNTS BE MADE AVAILABLE (SEE ATTACHED SCHEDULES). ON 1/16/, 17, 18 & 19, 1990 I WILL BE AT U.S. GENERAL SUPPLY CORP.'S CORPORATE OFFICE TO EXAMINE THESE INVOICES AND TO CONCLUDE THE AUDIT."[1]

By letter dated January 16, 1990, Mr. Dresel informed the auditor that Ms. Strasberg would be unavailable on January 16, 1990 and further stated:

> "We deem your appearance to be highly irregular knowing that she is unavailable at this point in time and as previously discussed, our records have been filed away and not immediately accessible and a substantial amount of time would be necessary to reassemble these files."

On January 17, 1990, the auditor received a letter from attorneys representing U.S. General stating that the Division was barred from assessing sales and use taxes for any period prior to April 25 1989, the date of the bankruptcy court's order confirming the plan of reorganization. According to his log, the auditor then spoke to a Mr. Divinski in the Division's Bankruptcy Unit who confirmed this information. The auditor then attempted to determine whether assessments could be issued against the corporate officers. He contacted various individuals in the Bankruptcy Unit and the Division's Law Bureau and received contradictory

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[1] We modify finding of fact "5" of the Administrative Law Judge's determination by changing the first sentence which read "[t]he audit proceeded from February 1989 through April 1990" to more accurately reflect the record.

information. Finally, the auditor and his supervisor determined that it would be appropriate to issue assessments against the corporate officers, although no assessments could be issued against U.S. General.

The Division then issued to each petitioner a Notice of Determination and Demand for Payment of Sales and Use Taxes Due, dated January 22, 1990, assessing tax due for the period September 1, 1985 through May 31, 1987 in the amount of $252,608.74, plus penalty and interest.

The Division received a power of attorney appointing James H. Tully, Jr. and Stewart Buxbaum to represent U.S. General in connection with the audit. The power of attorney is signed by Harold Rashbaum, as president of U.S. General, and dated February 1, 1990. The Division remained in contact with Ms. Strasberg and began communications with Mr. Buxbaum and Mr. Tully.

Apparently, the Division made further requests for books and records, and, in response, U.S. General took the position that it would no longer supply such records. The Division then issued to each petitioner a Notice of Determination and Demand for Payment of Sales and Use Taxes Due, dated April 4, 1990, assessing tax due for the period June 1, 1987 through November 30, 1988 in the amount of $192,115.68 plus penalty and interest.

During the course of the audit, two consents were executed extending the period of limitation for assessment of sales and use taxes. The last consent was signed by Mr. Chrein, acting under the power of attorney signed by Mr. Rashbaum appointing him to represent U.S. General. It states:

> "PURSUANT TO SECTION 1147c* of ARTICLE 28 and of SECTION 1250 of ARTICLE 29 OF THE TAX LAW, THE COMMISSIONER OF TAXATION AND FINANCE and
>
> U.S. General Supply Corp.
>
> * * *
>
> AGREE AS FOLLOWS:
>
> "THAT THE AMOUNT OF SALES AND USE TAXES DUE FROM THE ABOVE NAMED VENDOR, FOR THE TAXABLE PERIOD(S) 9-1-85

THROUGH 8-31-86, UNDER THE TAX LAW MAY BE DETERMINED AT ANY TIME ON OR BEFORE 1-20-90."

The first consent contains identical language and extended the period of limitation for assessment of taxes against U.S. General for the period September 1, 1985 through August 31, 1986 to December 20, 1989. This consent is signed by Harold Rashbaum as president of U.S. General and dated November 21, 1988. At the time the first notice of determination was issued, on or about January 22, 1990, Mr. Chrein did not hold a power of attorney from either Mr. Rashbaum or Mr. Harrow.

The Division filed no claims for taxes in U.S. General's bankruptcy proceeding based on the sales tax audit then being conducted. It did file a proof of claim dated November 22, 1988 for $16,723.04. The form filed by the Division shows that $15,508.81 of the the total amount claimed was for taxes due for the period March 1, 1988 through May 31, 1988 and was based on an actual return filed.

The Division filed a ballot with the bankruptcy court dated March 24, 1989, voting for rejection of the plan for reorganization for reasons having nothing to do with the then ongoing audit. The ballot showed post-petition tax due in the amount of $6,374.58 and pre-petition interest due of $722.29. The plan of reorganization was adopted by the bankruptcy court on April 25, 1989. The judge specifically added in writing that "[a]nything to [t]he contrary notwithstanding, the [d]ebtor shall escrow $110,000 in total with regard to disputed claims." All claims filed by the Division were paid.

After filing a petition in bankruptcy, U.S. General continued operating as a debtor in possession. Eventually, all creditors were paid under the bankruptcy plan. U.S. General obtained the money to pay off its debts by selling off portions of its business and from an infusion of cash provided by its owners. Mr. Rashbaum testified that he contributed $125,000.00 of his own money and that approximately $800,000.00 was received in the form of loans and gifts from family and friends.

U.S. General was represented in the bankruptcy proceeding by Abraham Backenroth, an attorney with extensive experience in bankruptcy law. He testified regarding his general

experience in bankruptcy proceedings and specifically about the U.S. General bankruptcy proceeding. He stated that in his experience the bankruptcy attorney is informed by the State of any ongoing audits so that a proof of claim can be filed by the State based on the results of the audit. He also stated that he has known the taxing authorities to file a proof of claim which states that the tax liability is undetermined or which shows a very large estimated sum.

When proofs of claim were filed by the Division against U.S. General, Mr. Beckenroth believed, based on his past experience, that no other tax claims would be filed for periods prior to the filing of the bankruptcy petition. He stated that he has never heard of an insufficient claim being filed during the course of an ongoing audit. In his estimation, U.S. General's plan for reorganization would not have been approved if the judge and parties had known that there was an outstanding tax liability in an unknown sum. In that case, Mr. Beckenroth believes that U.S. General would have liquidated.

Following a conciliation conference, the Division issued conciliation orders reducing the amount of tax assessed against petitioners for the period September 1, 1985 through May 31, 1987 to $58,507.05 and for the period June 1, 1987 through November 30, 1988 to $84,087.59. All penalties were cancelled as well.

OPINION

The Administrative Law Judge rejected petitioners' contention that by filing notices of claim in the bankruptcy proceeding for the period March 1, 1988 through May 31, 1988 based on a return filed by the corporation without remittance of the tax due, the Division was barred from issuing any other assessments of sales and use tax for any period prior to the filing of the bankruptcy petition. Relying on Matter of Harry's Exxon Serv. Sta. (Tax Appeals Tribunal, December 6, 1988), the Administrative Law Judge determined that petitioner failed to offer proof that the Division made an actual misrepresentation or committed some other wrongdoing on which petitioner reasonably relied.

The Administrative Law Judge found that petitioners failed to establish that the Division had a duty to inform the bankruptcy court of the audit. The Administrative Law Judge also concluded that given Mr. Rashbaum's execution in February 1989 of three powers of attorney for individuals to represent the corporation in the audit, Mr. Rashbaum was aware of the ongoing audit. Further, the Administrative Law Judge concluded that considering the subsequent contacts between the corporation's representatives and the Division, the review of audit findings between the auditor and Ms. Strasberg and the Division's issuance of a statement of proposed audit adjustment, the Division never implied through its actions that the audit was being discontinued. Because petitioners failed to prove that the Division made an actual misrepresentation, the Administrative Law Judge concluded that petitioners had failed to lay a foundation for the application of the doctrine of estoppel.

The Administrative Law Judge also determined that the Division was barred by Tax Law § 1147(b) from assessing tax against petitioners for the quarters ending November 30, 1985, February 28, 1986, May 31, 1986, August 31, 1986 and November 30, 1986. The Administrative Law Judge based her determination on the principle that the three-year period of limitation of section § 1147(b) may be raised separately by the corporate officer, whether or not the defense is available to the corporation. The Administrative Law Judge found that Tax Law § 1447(c) provides that a consent to extend the limitations period must be in writing by the taxpayer. Given the statute's writing requirement, the Administrative Law Judge determined that the provision is a limitation on the general principle that waiver may be inferred. As a result, the Administrative Law Judge further found that the corporation's consent to extend the period of limitations did not cover the corporate officers and, consequently, petitioners did not waive the period of limitation for assessment of tax against them.

On exception, petitioners argue the Division is barred from seeking to collect the taxes at issue because these claims could have been raised in the bankruptcy proceeding in which the Division participated. Citing Federal case law, petitioners argue that claims by creditors which could have been raised in objection to confirmation of a Chapter 11 plan are afterwards barred

under the doctrine of claim preclusion against the corporation or those in privity with the corporation.

Petitioners also renew their equitable estoppel argument, contending that the Division misrepresented the amount owed and the taxpayers had a right to rely on that misrepresentation. Petitioners also argue the audit had lasted approximately eight months and an estimated claim could have, but was not filed. Petitioners further contend that the Division's tax records indicate that petitioners had no knowledge that more taxes were going to be claimed.

Petitioners also request, if it is determined that the Division is not estopped, that credit be given for the taxes paid by the corporation pursuant to the confirmed plan in bankruptcy. Further, petitioners argue that the Conciliation Order removed certain periods from the assessment and this matter should be remanded to the Administrative Law Judge for a determination as to what taxes shall be attributable to the periods remaining open. By letter dated April 20, 1994, petitioners also request, pursuant to Tax Law § 3008, that additional tax and penalty be waived as of August 7, 1992, the effective date of section 3008. Petitioners make this request on "the basis that errors and delays in the performance of ministerial functions by the New York State Department of Taxation and Finance . . . resulted in that no assessments were issued at the time that the Audit Division states it was enabled to issue such assessments and, further, allegedly complete claims were not made in the bankruptcy proceedings . . ." (Petitioner's letter dated April 20, 1994).

The Division, on exception, urges the affirmation of the Administrative Law Judge's conclusion that the Division was not estopped from claiming petitioners were liable for taxes owed by the corporation. The Division argues that the Division was not in a position to assert a claim based on the audit at the time the proof of claim was required. Further, the Division argues Bankruptcy Code § 507(a)(7) does not require a creditor to file a claim. The Division also argues that it is irrelevant what duties the Division had in corporate bankruptcy given that petitioners were not parties to the bankruptcy.

The Division also rejects petitioners' argument that the doctrine of claim preclusion bars this proceeding. The Division points out that petitioners were not involved in the bankruptcy, only the corporation. The Division further argues it was not in a position to file a claim based on the audit as of the claims bar date. The Division also argues that the proceeding before the Bankruptcy Court involved a different claim (a return filed with no remittance) than that involved here (an alleged underreporting of tax based on a field audit).

The Division also argues that petitioners, in relying on Tax Law § 3008, failed to show any error or delay on the part of the Division in performing a ministerial act that would have have led to any of the interest assessed against them. The Division points out that if the Division erred in not issuing an assessment against the corporation, it is not a ministerial one.

The Division rejects as untimely petitioners' argument that the Division did not give them credit for monies paid by U.S. General pursuant to the bankruptcy plan. The Division further contends that petitioners have not established the amount of the credit, if any, they are entitled to. As a final matter, the Division rejects petitioners' request that the Tax Appeals Tribunal remand this matter if it is decided that some periods remain open.

The Division has not excepted to the Administrative Law Judge's conclusion that the consents executed for the corporation did not extend the statute of limitations for petitioners.

We affirm the determination of the Administrative Law Judge.

We begin by addressing petitioners' claim that the Division is barred by the doctrine of claim preclusion from raising in this administrative forum a matter which could have been raised in the Chapter 11 proceeding where the corporation was the debtor.

In determining whether the Division's claim is barred by its participation in the earlier bankruptcy proceeding, we look to the four factors required for claim preclusion to apply to a judgment. They are that: the judgment was entered by a court of competent jurisdiction; the judgment was found on the merits; there is identity of both parties or their privities (Gramatan Home Investors Corp. v. Lopez, 46 NY2d 481, 485, 414 NYS2d 308; Ott v. Barash, 109 AD2d

254, 491 NYS2d 661); and the claim must involve the same cause of action as involved in the earlier proceeding (O'Brien v. City of Syracuse, 54 NY2d 353, 445 NYS2d 687).

Although the case relied on by petitioners, Matter of Justice Oaks II, Ltd. (898 F2d 1544, cert denied 498 US 959), does suggest that petitioners have satisfied the first three requirements, we find petitioners have not satisfied the last requirement of claim preclusion.

The claim brought by the Division in this administrative proceeding fails to satisfy the test employed by Federal and New York courts to determine whether the same cause of action is being brought (Matter of Justice Oaks II, Ltd., supra; O'Brien v. City of Syracuse, supra). In deciding this issue, both State and Federal courts employ a "transactional" analysis (O'Brien v. City of Syracuse, supra; Smith v. Russell Sage College, 54 NY2d 185, 445 NYS2d 68). The Court of Appeals in O'Brien stated:

> "once a claim is brought to a final conclusion, all other claims arising out of the same transaction or series of transactions are barred, even if based upon different theories or seeking different remedies (O'Brien v. City of Syracuse, supra, 445 NYS2d 687, 688).

The claim asserted by the Division in bankruptcy was based on U.S. General's failure to include the proper remittance with its return for the quarter beginning March 1, 1988 and ending May 31, 1988. Thus, the transaction at issue in the bankruptcy claim was simply U.S. General's failure to pay the amount the corporation itself reported as due on the return for the quarter. The claim being asserted in the instant matter by the Division is based on a field audit of the corporation's books and records for the period September 1, 1985 to November 30, 1988. The transaction underlying this claim is the alleged failure of the corporation to properly report the amount of tax due for the entire period. Because the transactions are completely distinct, we conclude that the two claims are also entirely distinct "causes of action."

Our conclusion that the claim before the bankruptcy court and the claim before us involve distinct and separate transactions is consistent with our holding in Matter of Kadish (Tax Appeals Tribunal, November 15, 1990) where we concluded that the bankruptcy proceeding must negate the factual basis of the corporation's sales tax liability in order for it to effect the liability of the responsible officer. To negate the factual basis of the sales tax liability of the

corporation, obviously the bankruptcy proceeding must involve the same transaction as is the basis for liability against the responsible officer. Our decision in Kadish followed that of the Appellate Division in Matter of Trachtenberg v. New York State Tax Commn. (107 AD2d 57, 485 NYS2d 621) and Matter of Yellin v. New York State Tax Commn. (81 AD2d 196, 440 NYS2d 382) which dealt with a responsible officer's penalty under section 685(g) of the Tax Law for the withholding tax liability of the corporation.

Turning to petitioners' estoppel claim, we find the Administrative Law Judge adequately addressed this issue and we affirm for the reasons stated therein. We add to the Administrative Law Judge's analysis a single observation. In petitioners' notice of exception, they contend that after the ballot was filed on March 24, 1989, Mr. Rashbaum received notice that the audit was over. As stated in the facts, the record shows that in April the auditor contacted Ms. Strasberg, one of the individuals appointed by Mr. Rashbaum to represent the corporation in the audit, in order to schedule a meeting for May 1989 (Auditor's notes, Division's Exhibit "O"), which would be beyond the date the reorganization plan was confirmed, April 25, 1989. Petitioners' contention is inconsistent with this fact.[2]

With regard to petitioners' request that credit be given for amounts paid by the corporation pursuant to the plan of reorganization in bankruptcy, we decline to do so. We find that, given that the claim filed in bankruptcy was for petitioners' failure to pay the taxes the corporation's return indicated were owed, and that the claim in this proceeding was for taxes owed in excess of what the corporation claimed it owed, the amount paid in bankruptcy to satisfy the former claim is irrelevant to the matter before us.

With respect to the adjustments made at the conciliation conference, as the Division notes, these are explained in Exhibit "P." Therefore, we see no basis for petitioners' request for a remand "for a determination as to what taxes would be attributable to the periods remaining open" (Petitioners' brief on exception, p. 21).

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[2]It should be noted that as petitioners and the debtor corporation were aware of the ongoing audit they could have asserted a claim on the creditor's behalf within thirty days after the time prescribed for filing claims (Bankruptcy Code § 3004). This claim could later have been supplemented by one from the Division.

Addressing petitioners' claim regarding the waiver of penalty and interest pursuant to Tax Law § 3008, we find the record does not reflect the existence of any ministerial error committed by an employee of the Division. As a result, petitioners' request must be denied.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Harold Rashbaum, as officer of U.S. General Supply Corp., and Murray Harrow, as officer of U.S. General Supply Corp., is denied;

2. The determination of the Administrative Law Judge is affirmed;

3. The petitions of Harold Rashbaum, as officer of U.S. General Supply Corp., and Murray Harrow, as officer of U.S. General Supply Corp., are granted to the extent indicated in conclusion of law "B" of the Administrative Law Judge's determination, but are otherwise denied; and

4. The Division of Taxation is directed to modify the notices of determination dated January 22, 1990 (as modified by the conciliation orders issued on November 29, 1991) to the extent stated in the Administrative Law Judge's conclusion of law "B," but such notices are otherwise sustained.

DATED: Troy, New York
December 15, 1994

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

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