

STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
JOSEPH P. SANTO	:	DECISION
	:	DTA NO. 821797
for Revision of a Determination or for Refund of Sales	:	
and Use Taxes under Articles 28 and 29 of the Tax Law	:	
for the Period March 1, 2005 through November 30,	:	
2005.	:	

The Division of Taxation filed an exception to the determination of the Administrative Law Judge issued on March 12, 2009. Petitioner appeared *pro se*. The Division of Taxation appeared by Daniel Smirlock, Esq. (Osborne K. Jack, Esq., of counsel).

The Division of Taxation filed a brief in support of its exception and petitioner filed a letter brief in opposition. Petitioner's request for oral argument was denied.

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

ISSUES

I. Whether petitioner was personally liable for the sales and use taxes due on behalf of New Road One, LLC, as a person required to collect and pay such taxes under Tax Law §§ 1131(1) and 1133(a).

II. Whether penalties assessed against petitioner should be abated.

FINDINGS OF FACT

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

On April 2, 2004, petitioner and Joseph M. Scotti and Thomas Smario entered into an Operating Agreement (the Agreement) for the formation of a limited liability company known as New Road One, LLC (the LLC), in order to own and operate a Red Robin Restaurant. The restaurant operated under the trade name Red Robin Gourmet Burgers & Spirits, and the address of the restaurant was 14 Crystal Run Crossing, Middletown, New York 10941.

The Agreement provided that Messrs. Scotti and Smario and petitioner were to be the “Managing Members” but stated more particularly that Joseph M. Scotti “is the Financial and Administrative Managing Member in charge of all the financial operations of the company, as well as the administrative matters;” that Thomas Smario “is the Managing Member designated as the construction manager, who will oversee the building and the improvements and general repairs and maintenance of the operation;” and that petitioner “is the Managing Member in charge of the daily operations of the company, which include the operation of the actual restaurant which includes directing, managing the staff available for food and beverage, consultants, systems, cleaning and maintenance.”

Pursuant to the Agreement, each Managing Member was to contribute \$1,000.00 to the capital of the LLC and each Managing Member was to own a 33 1/3% interest. However, a Summary of Receipts as of November 1, 2004 indicated that Joseph M. Scotti had contributed \$184,300.00, Thomas Smario had contributed \$62,000.00 and petitioner had contributed nothing to the LLC.

Mr. Scotti indicated to the other Managing Members that he had adequate funds to begin construction of the restaurant, which ended up costing nearly \$4,000,000.00, but that proved not to be the case. Therefore, other investors had to be found. The November 1, 2004 Summary of Receipts indicated that a number of other persons had become investors in the LLC. As a result thereof, as of November 1, 2004, the interest of petitioner and the other principals (Joseph M. Scotti and Thomas Smario) had been reduced to 24.17% each.

The Agreement provided that the Financial Managing Member (Mr. Scotti) would, among other things, “prepare or cause to be prepared all Federal, State and local income tax and information returns for the Limited Liability Company, and shall cause such tax and information returns to be filed timely with the appropriate governmental authorities.”

The Agreement stated that all books and records and tax and information returns were to be maintained at the principal place of business of the LLC which was 322 President Street, Brooklyn, New York, the home address of Joseph M. Scotti.

Petitioner joined with Messrs. Scotti and Smario on the condition that he would not be involved in raising funds and that he would not be responsible for financial duties on behalf of the LLC. While petitioner did not initially make any monetary investment in the LLC, he later loaned the LLC the sum of \$15,000.00 (which was the extent of his savings) to cover payroll. This loan was to be repaid within two weeks after its advance; however, it was never repaid. In addition to petitioner’s savings, his family and friends invested more than \$900,000.00, which was lost in the LLC venture.

Because of his previous experience in the restaurant business, petitioner’s function was to oversee the restaurant’s managers, who were to operate the restaurant in Middletown. Petitioner

hired the managers who then hired the other employees. In his position as supervisor of the restaurant managers, petitioner visited the restaurant once or twice weekly.

The managers made direct deposits into the bank twice daily and all bank statements and information went to Mr. Scotti, who had the LLC's checkbooks in his possession.

The restaurant opened in March 2005. However, the LLC had difficulty paying construction creditors, and investors were not getting the profit and loss reports as required by the Agreement. As a result, it became exceedingly difficult to raise money.

When the restaurant opened, petitioner, because of his previous experiences, reminded Mr. Scotti that it was imperative to file timely tax returns and pay the LLC's tax liabilities since the failure to do so would result in the imposition of interest and penalties. On several occasions, petitioner asked Mr. Scotti for copies of the sales tax returns, but he did not receive the copies as requested. In addition, petitioner asked for bank reconciliation statements because "I was getting a little nervous and we didn't get those for a long time and when we got them, they were not legible."

Petitioner had no role in the preparation of the LLC's sales tax returns. Each of the sales tax returns for the period at issue was signed by Joseph Scotti, Member.

For the sales tax quarter ended May 31, 2005, the LLC reported sales tax due in the amount of \$70,012.31, but paid only \$4,862.31, thereby leaving a balance due of \$65,150.00.

For the sales tax quarter ended August 31, 2005, the LLC reported sales tax due in the amount of \$65,111.00, but had total tax credits and advance payments totaling \$44,908.00, thereby leaving a balance due of \$20,203.00. Attached to the return were copies of eight checks, all of which were dated September 15, 2005, totaling \$20,053.00. These checks bore what appears to be the signature of Joseph Scotti, who signed the sales tax return.

For the sales tax quarter ended November 30, 2005, the LLC reported sales tax due of \$50,683.00, but had total tax credits and advance payments totaling \$33,872.00, thereby leaving a balance due of \$16,661.00. Attached to the return were copies of two checks, dated December 15, 2005, totaling \$5,661.00. The checks bore what appears to be the signature of Joseph Scotti, who signed the sales tax return.

On May 22, 2006, the Division issued three notices of determination to petitioner that advised him that he was being assessed as an officer or responsible person of New Road One, LLC.¹ The notices assessed as follows:

Period Ended	Tax	Interest	Penalty	Payments/Credits	Total
05-31-05	65,150.00	8,546.76	13,281.50	17,500.00	69,478.26
08-31-05	65,111.00	7,228.63	12,394.11	0.00	84,733.74
11-30-05	26,150.00	1,747.41	4,072.50	0.00	31,969.91

Petitioner had check signing authority on behalf of the LLC; however, he signed only six to ten checks in total, drawn on one of the business's checking accounts, and signed these checks only when Mr. Scotti was on vacation.

In 2004, petitioner began undergoing radiation implantology for prostate cancer. On July 21, 2006, petitioner went into cardiac arrest and was taken to the hospital where he was resuscitated and implanted with a pacemaker. After approximately two weeks in the hospital, petitioner notified Messrs. Scotti and Smario that he could no longer tolerate the extreme stress of the business and he, therefore, separated himself from the operation.

¹ Based upon the sales tax returns filed, the credits claimed and the copies of the checks attached to the returns, it is unclear how the amounts of tax assessed by the notices of determination were calculated.

In the fall of 2006, bankruptcy proceedings on behalf of the LLC were commenced and the restaurant closed.

THE DETERMINATION OF THE ADMINISTRATIVE LAW JUDGE

The Administrative Law Judge observed that the Tax Law imposes personal liability upon any person who is found responsible for the collection of the tax imposed by Article 28 of Tax Law § 1133(a). A person required to collect tax is defined to include, among others, corporate officers and employees who are under a duty to act for such corporation in complying with the requirements of Article 28 (*see*, Tax Law § 1131[1]).

The Administrative Law Judge pointed out that the mere holding of corporate office does not, per se, impose tax liability upon an office holder. Rather, whether a person is an officer or employee liable for tax must be determined upon the particular facts of each case.

The Administrative Law Judge noted that in *Matter of Constantino* (Tax Appeals Tribunal, September 27, 1990), we held that a corporate officer and shareholder was not a person responsible for the collection and payment of sales tax pursuant to Tax Law §§ 1131 and 1133, where:

petitioner's role was essentially that of a minority investor and supervising employee who was precluded from taking actions with regard to the financial and management activities of the corporation.

* * *

The significance of petitioner's officer and shareholder status in the determination of responsibility is offset by the circumstances relating to control of the corporation which are present here. Petitioner lacked the power to exercise the tax collection responsibilities on behalf of the corporation. The evidence does not support a conclusion that petitioner could have acted but chose not to.

In the present matter, the Administrative Law Judge found the credible testimony of petitioner established that, like Mr. Constantino, petitioner's role was as a minority investor who was precluded from taking action with regard to the financial and management activities of the LLC. The Administrative Law Judge noted that the Agreement provided that Joseph M. Scotti was in charge of all of the financial operations and administrative matters pertaining to the LLC and that petitioner was to manage the staff involved in the operation of the restaurant. The Agreement further stated that the Financial Managing Member (Mr. Scotti) would prepare or cause to be prepared all tax returns for the LLC and would cause the returns to be filed timely with the appropriate governmental authorities.

The Administrative Law Judge found that while a Managing Member, petitioner was not an investor, was not involved in the day-to-day operation of the restaurant and was not responsible for the financial management of the business. The Administrative Law Judge, relying on our decision in *Constantino*, found that petitioner lacked the power to exercise the tax collection responsibilities on behalf of the LLC and, therefore, cannot be held as a person responsible for the collection and payment of sales tax on behalf of the LLC.

By virtue of his holding on the issue of liability, the Administrative Law Judge found that the issue of whether penalties imposed should be abated, was rendered moot.

ARGUMENTS ON EXCEPTION

On exception, the Division has not taken exception to any of the findings of fact of the Administrative Law Judge. However, the Division argues that the Administrative Law Judge erred in treating this member of a limited liability company as if he were not a responsible officer or employee of the corporation. The Division urges that we determine that Tax Law § 1131(1) imposes per se liability on any member of a Limited Liability Company.

Petitioner requests that we affirm the determination of the Administrative Law Judge in all respects.

OPINION

In section 2(5) of the Tax Law, a limited liability company is defined as a “domestic limited liability company or a foreign limited liability company, as defined in section one hundred two of the limited liability company law, a limited liability investment company formed pursuant to . . . the banking law, or a limited liability trust company formed pursuant to . . . of the banking law.” Section 2(6) of the Tax Law provides that for purposes of the Tax Law, a partnership includes, but shall not be limited to, a limited liability company. Thus, when a company is formed as a limited liability company in accordance with the Limited Liability Company Law or the Banking Law, it is treated as a partnership for purposes of the Tax Law.

Tax Law § 1131(1) defines “persons required to collect [sales] tax,” to include every vendor of tangible personal property or services, and:

[s]hall also include any officer, director or employee of a corporation . . . , any employee of a partnership, any employee or manager of a limited liability company . . . who as such officer, director, employee or manager is under a duty to act for such corporation, partnership, limited liability company . . . in complying with any requirement of this article; ***and any member of a partnership or limited liability company.***

Thus, we reverse the determination of the Administrative Law Judge. We find that it was an error for the Administrative Law Judge to treat petitioner as if he were an officer or employee of a corporation, and that his reliance on ***Matter of Constantino (supra)*** was misplaced.

Petitioner was a member of a limited liability company and, as with members of a partnership, such members are subject to per se liability for the taxes due from the limited liability

company (*see*, Tax Law § 1131[1]; *see also*, *Matter of Bartolomei*, Tax Appeals Tribunal, April 3, 1997).

Where petitioner is an employee or manager of a partnership or limited liability company, the Division would be required to show, as a condition precedent to finding personal liability, evidence not just of petitioner's status as a employee or manager, but that he had a duty to act for the company in the collection and payment of sales tax to the State of New York (*see*, Tax Law §§ 1131[1]; 1133[a]). Since Tax Law § 1131(1) imposes strict liability upon members of a partnership or limited liability company, all that is required to be shown by the Division for liability to obtain is the person's status as a member.

We remand this matter to the Administrative Law Judge for a determination on the issue of penalties based on the existing record.

ACCORDINGLY, it is ORDERED, ADJUDGED and DECREED that this case be remanded so that the Administrative Law Judge can address the findings of fact and conclusions of law with respect to penalties. Upon issuance of such determination, the full record shall be returned to the Tax Appeals Tribunal for a decision on the remaining issue.

DATED: Troy, New York
December 23, 2009

/s/ Charles H. Nesbitt
Charles H. Nesbitt
President

/s/ Carroll R. Jenkins
Carroll R. Jenkins
Commissioner