

STATE OF NEW YORK
DIVISION OF TAX APPEALS

In the Matter of the Petition :
of :
LEOPOLD GALLO : DETERMINATION
for Redetermination of a Deficiency or for :
Refund of Personal Income Tax under Article 22 :
of the Tax Law for the Years 1971, 1972 and :
1973. :

Petitioner, Leopold Gallo, 1859 Como Park Boulevard, Lancaster, New York 14086, 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 1971, 1972 and 1973 (File No. 800007).

A hearing was commenced before Timothy J. Alston, Hearing Officer, at the offices of the State Tax Commission, 65 Court Street, Buffalo, New York, on March 11, 1987, at 1:15 P.M. and was continued to conclusion at the same location on March 12, 1987 at 1:00 P.M., with all briefs to be submitted by April 30, 1987. Petitioner appeared by Salvatore M. Latona, Esq. The Audit Division appeared by John P. Dugan, Esq. (Deborah J. Dwyer, Esq., of counsel).

ISSUES

- I. Whether petitioner is liable for the penalty asserted against him pursuant to Tax Law § 685(g) with respect to withholding taxes due from Deplan Contracting, Inc.
- II. Whether the Audit Division should be precluded from proceeding against petitioner in light of its failure to timely proceed against the bankruptestate of Deplan Contracting, Inc.

FINDINGS OF FACT

1. On October 28, 1974, the Audit Division issued a Notice of Deficiency along with a Statement of Deficiency to petitioner, Leopold Gallo, asserting a penalty equal to the amount of unpaid withholding taxes which the Audit Division determined to be due from Deplan Contracting, Inc. ("the corporation"). The notice asserted deficiencies as follows:

<u>Period</u>	<u>Amount</u>
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1971	\$ 5,465.97
1972	28,184.81
1973	<u>1,732.40</u>
	\$35,383.18

2. Deplan Contracting, Inc. was incorporated and began doing business in 1955. It was engaged in the business of contracting. Petitioner and three of his brothers each owned twenty-five percent of the shares of the corporation.

3. During the period at issue petitioner was president of the corporation. He, along with his brothers, had authority to sign checks on behalf of the corporation. In connection with his office he signed corporate tax returns, including withholding tax returns. He was not involved in the payment of creditors of the corporation.

4. Petitioner and his brothers jointly hired an individual named Darwin Martin as office manager for the corporation. Mr. Martin had been employed as office manager for approximately 14 years prior to the period at issue. This individual was assigned the responsibility of the day-to-day management of the corporation's financial affairs during the period at issue. Included among Mr. Martin's responsibilities were maintenance of corporate books and records and providing information to the corporation's certified public accountants. He was also responsible for the corporation's accounts payable and accounts receivable. Mr. Martin prepared and signed withholding tax returns on the corporation's behalf.

5. Petitioner was primarily involved in Deplan Contracting, Inc. as a field supervisor. In that capacity, he worked on site managing various construction projects.

6. Petitioner's annual salary from the corporation was \$46,000.00 during the period at issue.

7. The corporation also retained the services of an independent certified public accounting firm. This firm conducted a full audit of the corporation's operations on an annual basis during the period at issue and prepared corporate tax returns during this time.

8. During the period at issue, petitioner and his brothers, as shareholders of the

corporation, met two or three times per year with Mr. Martin and the corporation's accountants. At no time prior to early February 1973 did either Mr. Martin or the accountants advise petitioner that the corporation was in financial difficulty or that taxes were not being paid.

9. In early February 1973, petitioner was advised by a member of the accounting firm that the corporation was in serious financial difficulty. Petitioner subsequently undertook, along with the accountants, to determine the extent of the difficulty. It was determined that, for several years, Mr. Martin had failed to pay an overwhelming amount of the corporation's accounts payable and its withholding taxes. Mr. Martin was subsequently fired from the corporation. The accounting firm had, in its audit of the corporation, failed to discover Mr. Martin's activities.

10. Upon learning of the extent of the corporation's financial difficulties, it was decided among the shareholders, upon the advice of counsel, to file a petition on behalf of the corporation under Chapter XI of the Bankruptcy Code. Said filing occurred on March 20, 1973. The petition was subsequently transferred to Chapter VII of the Bankruptcy Code and the corporation was duly adjudged bankrupt on May 8, 1973. The final day for filing claims by creditors against the bankrupt's estate was fixed by the bankruptcy court as December 4, 1973. The Department of Taxation and Finance, which had a claim against the bankrupt's estate, i.e., the unpaid withholding tax asserted against petitioner herein, failed to timely file its claim pursuant to the order of the bankruptcy court. The Department's claim was, therefore, rejected. It is undisputed that had the Department timely filed its claim it would have received approximately 78 percent of said claim from the proceeds of the bankrupt estate.

CONCLUSIONS OF LAW

A. Where a person is required to collect, truthfully account for and pay over withholding taxes and willfully fails to collect and pay over such taxes, Tax Law § 685(g) imposes on such person "a penalty equal to the total amount of tax evaded, or not collected, or not accounted for and paid over."

B. Tax Law § 685(n) defines "person", for purposes of Tax Law § 685(g), to include:

"an individual, corporation or partnership or an officer or employee of any corporation...who as such officer, employee, or member is under a duty to perform the act in respect of which the violation occurs."

C. Whether petitioner was a person required to collect, truthfully account for and pay over withholding taxes during the period in issue is a question of fact

(Matter of McHugh v. State Tax Commission, 70 AD2d 987, 988;

(Matter of MacLean v. State Tax Commission, 69 AD2d 951, affd 49 NY2d 920). Factors which are relevant to this determination include whether the individual signed the corporation's tax returns, derived a substantial part of his income from the corporation and possessed the right to hire and fire employees (Matter of Amengual v. State Tax Commission, 95 AD2d 949, 950; Matter of Malkin v. Tully, 65 AD2d 228, 231). Other factors considered are the amount of stock owned, the authority to pay corporate obligations and the individual's official duties

(Matter of Amengual v. State Tax Commission, supra).

D. Petitioner was a person required to collect, truthfully account for and pay over the withholding taxes of Deplan Contracting, Inc. during the period at issue. Petitioner was president of the corporation, received a substantial salary, owned 25 percent of its stock, and had authority to sign checks on its behalf. He also signed withholding and other corporate tax returns on its behalf. He was, therefore, under "a duty to act" on the corporation's behalf within the meaning of Tax Law § 685(n) and was thus a "person" under Tax Law § 685(g).

E. Inasmuch as petitioner was a "person" for purposes of Tax Law § 685(g), his liability for the penalty at issue herein rests upon a determination as to whether he willfully failed to collect and pay over the withholding taxes of Deplan Contracting, Inc. The test of willfulness is as follows:

"[W]hether 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, 34.)

F. Petitioner's failure to collect and pay over withholding taxes was willful under Tax Law

§ 685(g). Persons responsible for payment of withholding tax pursuant to Tax Law § 685(g) may not "absolve themselves merely by disregarding their duty and leaving it to someone else to discharge (Matter of Gardiner v. State Tax Commn., 78 AD2d 928, 929)."

(Matter of Ragonesi v. State Tax Commn., 88 AD2d 707, 708). The record indicates that petitioner, in discharging his duty to see that withholding taxes were filed and paid, merely relied on the competence and good faith of the corporation's office manager and accountants. The record indicates that petitioner received reports on the corporation's financial status from its office manager and accountants two or three times per year (Finding of Fact "8", supra). The record does not disclose any supervision of the office manager by petitioner during the years at issue, nor does the record disclose any inquiries made by petitioner of the office manager or accountants with respect to the filing and payment of withholding taxes. Although the record indicates that petitioner and the corporation were the victims of apparent fraudulent conduct by an employee of 14 years and possible professional misfeasance by an accounting firm, petitioner has failed to show herein that he exercised a degree of care sufficient to discharge the duty imposed pursuant to Tax Law § 685(g). It is thus determined that petitioner disregarded his duty (see ___ Matter of Ragonesi v. State Tax Commn., supra), and this disregard results in a finding that such failure to act was "willful" within the meaning of Tax Law § 685(g) (see ___ Matter of Levin v. Gallman, supra).

G. It is of no consequence to the result reached herein that the Department of Taxation and Finance failed to timely file its claim against the bankrupt corporation's estate, and that had the Department timely filed its claim, it would have received approximately 78 percent of said claim (Finding of Fact "10", supra). The penalty imposed by Tax Law § 685(g) creates joint and several liability (Hartman v. United States, 538 F2d 1336, 1340 [8th Cir 1976]).¹ "A taxpayer

¹It should be noted that Tax Law § 685(g) is modeled after section 6672 of the Internal Revenue Code and, as a result, Federal cases may be used for guidance (Yellin v. New York State Tax Commission, 81 AD2d 196).

who is equally liable with another for the payment of accrued but unpaid tax, cannot avoid collection against himself on the ground that the Government should first collect it from the other party" (Kelly v. Lethert, 362 F2d 629, 635 [8th Cir 1966]). Therefore, petitioner may not use as a defense to the section 685(g) penalty the fact that the Department of Taxation and Finance failed to timely proceed against another entity which was equally liable.

H. The petition of Leopold Gallo is in all respects denied and the Notice of Deficiency, dated October 28, 1974, is sustained.

DATED: Albany, New York
December 10, 1987

ADMINISTRATIVE LAW JUDGE