

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petition :  
of :  
**TERRENCE P. O'REILLY** : DETERMINATION  
for Redetermination of a Deficiency or for Refund of : DTA NO. 818564  
New York State Personal Income Tax under Article 22 :  
of the Tax Law and New York City Personal Income Tax :  
under the Administrative Code of the City of New York :  
for the Years 1992 through 1998. :

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Petitioner, Terrence P. O'Reilly, 92 New Chalet Drive, Mohegan Lake, New York 10547, filed a petition for redetermination of a deficiency or for refund of New York State personal income tax under Article 22 of the Tax Law and New York City personal income tax under the Administrative Code of the City of New York for the years 1992 through 1998.

A hearing was held before Dennis M. Galliher, Administrative Law Judge, at the offices of the Division of Tax Appeals, 641 Lexington Avenue, New York, New York, on February 28, 2002 at 10:45 A.M., with all briefs to be submitted by July 29, 2002, which date commenced the six-month period for the issuance of this determination. Petitioner appeared *pro se*. The Division of Taxation appeared by Barbara G. Billet, Esq. (Margaret T. Neri, Esq., of counsel).

***ISSUE***

Whether petitioner was a person required to collect, truthfully account for and pay over withholding tax with respect to a law firm with which he was affiliated, who willfully failed to do so thus becoming liable for a penalty equal to such unpaid tax under section 685(g) of the Tax Law.

***FINDINGS OF FACT***

1. Petitioner, Terrence P. O'Reilly, was admitted to practice law in the State of New York in 1967. From 1967 to 1973, petitioner was an assistant district attorney in the New York County District Attorney's Office. In 1973, petitioner joined the law firm of Foley, Hickey, Gilbert and Power. John Power and Richard Hickey were the active partners in the firm at such time, with Mr. Foley having died shortly before petitioner's association with the firm, and Jacob Gilbert, a retired Congressman, having little active involvement in the firm. The firm, which at that time consisted of approximately six attorneys, carried on a general practice of law, including corporate and commercial work, trusts and estates, and related litigation. Petitioner was hired as the firm's litigator to replace Mr. Foley.

2. In 1979, after six years with the firm, petitioner approached the two partners, John Power and Richard Hickey, and demanded to be made a partner in the firm. In turn, at some point in 1980, petitioner was advised that he had been made a full partner in the firm, and that his compensation would be a draw of \$500.00 per week against five percent of the firm's annual gross income.

3. During the same time period, the formerly amicable relationship between Richard Hickey and John Power was deteriorating. The dispute between the two individuals continued to worsen, and ultimately, petitioner sided with Richard Hickey such that, at the end of 1981, the matter came to a head and John Power was voted out of the firm. Petitioner noted that his vote was driven by his belief that the majority of the firm's clients would remain with Richard Hickey (and petitioner) as opposed to John Power. In 1981, the name of the firm was changed to Foley,

Hickey, Gilbert and O'Reilly,<sup>1</sup> and petitioner was made an authorized signatory on the firm's two bank accounts (a regular checking account and a special account).

4. Petitioner stated that there was no written partnership agreement for the firm at any time, and that he simply relied on Richard Hickey's word that he was a full (i.e., 50%) partner in the firm and that he was receiving 50 percent of the firm's income, gain, loss and deductions. The firm employed an accountant, and for the years 1979 through 1985, petitioner received copies of the firm's partnership tax return (Form 1065) and his own accompanying Schedule K-1 (Partner's Share of Income, Credits, Deductions, Etc.) for such years. Petitioner was listed as a 50 percent partner on these forms. Petitioner did not involve himself in meetings with the firm's accountant and Richard Hickey.

5. In 1985, Richard Hickey terminated the firm's accountant upon the stated reason that the firm could no longer afford his services. Mr. Hickey handled the firm's finances and books from such time forward. When checks for disbursements, court fees and the like were needed, petitioner would ask Richard Hickey for the necessary amounts, and Mr. Hickey would, in turn, cut the required checks.

6. Petitioner did not receive or see a copy of either Form 1065 for the firm, or Schedule K-1 for himself, for any of the years 1986 through the mid-1990s, notwithstanding his demands that Richard Hickey provide the same. Instead, petitioner was furnished, annually, with a half-sheet of paper showing his income amount from the firm. Petitioner, in turn, filed his own tax returns using the amount shown on this half-sheet of paper as partnership income, allegedly doing so because he did not know how else to file.

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<sup>1</sup> Jacob Gilbert died in the mid-1970s.

7. During the years in issue, the firm had several employees. Both petitioner and Richard Hickey had secretaries, and there was also a receptionist. From time to time, the firm would also hire associate attorneys. Petitioner drafted and placed advertisements for such associates, and conducted the initial interviews of such prospective firm employees, making hiring recommendations thereafter to Richard Hickey.

8. During the period 1977 through 1994 the firm, and most directly petitioner, was involved in litigating a complicated partnership accounting case in Supreme Court, Kings County, on a 50-percent contingency fee basis. Petitioner anticipated a substantial payment under this arrangement and the trial court initially awarded the firm's client over four million dollars, of which petitioner anticipated the firm would receive 50 percent. However, the matter was remanded on appeal and, after a new trial, the firm's client received only approximately \$35,000.00. Despite having time records representing fees in excess of one million dollars for the case, the firm's contingency agreement with its client resulted in very small legal fees for the firm.

9. The impact of the foregoing litigation put a severe cash flow strain on the firm. Petitioner never saw the firm's bank statements or payroll tax returns during the years in issue, never asked to see such tax returns, and never inquired as to whether withholding taxes were being paid. Petitioner stated that since Richard Hickey had not shown him any partnership tax returns, he never expected that Mr. Hickey would show him any payroll tax returns. Nonetheless, petitioner stated, in testimony, that "I assumed he [Richard Hickey] was doing the right thing." Petitioner remained with the firm throughout the period in question and until the present time. He remained initially in anticipation of the ultimately unrealized substantial

payment from the accounting action and thereafter because he believed his options to go elsewhere were limited.

10. The Division of Taxation (“Division”) determined that withholding tax returns had not been filed and withholding taxes had not been remitted by the firm for any of the years 1992 through 1998. As a result, on May 15, 2000, the Division issued to petitioner a total of 14 notices of deficiency asserting penalties equal to the unpaid New York State and New York City withholding tax owed by the firm: <sup>2</sup>

<u>YEAR</u>	<u>NYS TAX</u>	<u>NYC TAX</u>
1992	\$6,499.56	\$1,046.28
1993	\$6,724.44	\$1,492.12
1994	\$8,450.64	\$2,221.56
1995	\$5,409.72	\$1,761.00
1996	\$6,521.76	\$1,997.64
1997	\$7,041.84	\$1,848.24
1998	\$6,352.32	\$2,426.52

11. Only limited records, in addition to the firm’s checkbook, were available upon audit. The record does include wage and tax statements (Forms W-2) for the firm’s employees for each year, listing specific wages and deductions for each employee, together with Forms W-4 (Employee’s Withholding Tax Allowance Certificate) for some of the listed employees. These records reveal that the number of firm employees for the years in issue were as follows:

<u>YEAR</u>	<u>NUMBER OF EMPLOYEES</u>
1992	4
1993	6
1994	4
1995	4
1996	3
1997	7
1998	7

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<sup>2</sup> The amount columns list the penalty equal to the amount of unpaid New York State and New York City withholding tax for the years 1992 through 1998. They do not include interest asserted due.

The respective wage amounts listed on these records bear out that some, though not all, of the firm's employees were short-term or part-time employees. Neither Richard Hickey nor petitioner were listed as employees on these forms.

12. The Division also presented Records of Employment and Earning for some of the firm's employees for the years 1996, 1997 and 1998, listing specific amounts of weekly wages and deductions. No such records were presented for the earlier years in issue (1992 through 1995).

### ***SUMMARY OF PETITIONER'S POSITION***

13. Petitioner maintains that he was not a partner in the firm, but rather that the firm was in fact run by Richard Hickey, who controlled all of the financial aspects of the firm's operations. Petitioner claims that he never inquired as to the status of withholding or other tax filings and payments, but rather assumed that Mr. Hickey was properly discharging the duty to see that such filings and payments were timely made. Petitioner asserts further that because of the fact and manner in which Richard Hickey handled the firm's books, records and finances, petitioner was unable to be involved in such matters and thus should not be held responsible for the amounts asserted as due.

### ***CONCLUSIONS OF LAW***

A. With regard to the withholding tax penalty asserted against petitioner, Tax Law § 685(g) provides:

Willful failure to collect or 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 payments 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.

B. Tax Law § 685(n), in turn, furnishes the following definition of “persons” subject to the section 685(g) penalty:

The term person includes an individual, corporation or partnership or an officer or 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.

C. The question of whether someone is a “person” under a duty to collect and pay over withholding taxes is a factual one, and has been litigated many times. Factors to consider include whether the particular individual had the authority to sign tax returns and did so, derived a substantial part of his income from the business, or had the right to hire and fire employees (*Matter of Malkin v. Tully*, 65 AD2d 228, 412 NYS2d 492, 494, *affd* 49 NY2d 920, 428 NYS2d 675). Other pertinent areas of inquiry include the person’s official duties, his authority to pay obligations of the business, and his financial interest in the business (*Matter of Amengual v. State Tax Commn.*, 95 AD2d 949, 464 NYS2d 272,273; *see, Matter of McHugh v. State Tax Commn.*, 70 AD2d 987, 417 NYS2d 799, 801; *Matter of Shah*, Tax Appeals Tribunal, February 25, 1999). Summarized in terms of a general proposition, the issue to be resolved is whether petitioner had, or could have had, sufficient authority and control over the affairs of the business to be considered a person under a duty to collect and remit the unpaid taxes in question (*Matter of Constantino*, Tax Appeals Tribunal, September 27, 1990; *Matter of Chin*, Tax Appeals Tribunal, December 20, 1990).

D. In addition, if petitioner is held to be a person under a duty as described, it must then be decided whether his failure to withhold and pay over such taxes was willful. The question of willfulness is related directly to the question of whether petitioner was a person under a duty, since clearly a person under a duty to collect and pay over the taxes is the one who can consciously and voluntarily decide not to do so. However, merely because one is determined to

be a person under a duty, it does not automatically follow that a failure to withhold and pay over income taxes is “willful” within the meaning of that term as used in Tax Law § 685(g). As the Court of Appeals indicated in *Matter of Levin v. Gallman* (42 NY2d 32, 396 NYS2d 623), the test is:

[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 non-payment is required (*id.*, 396 NYS2d at 624-625; *see, Matter of Lyon*, Tax Appeals Tribunal, June 3, 1988).

The failure to pay over taxes can be willful notwithstanding the lack of actual knowledge, if the person recklessly disregarded his responsibilities, including the responsibility to see that employment taxes are paid (*Matter of Capoccia v. State Tax Commn.*, 105 AD2d 528, 481 NYS2d 476). Finally, “corporate officials responsible as fiduciaries for tax revenues cannot absolve themselves merely by disregarding their duty and leaving it for someone else to discharge” (*Matter of Risoli v. Commr.*, 237 AD2d 675, 654 NYS2d 218, quoting *Matter of Ragonese v. State Tax Commn.*, 88 AD2d 707, 451 NYS2d 301).

E. Upon review of the entire record, it becomes clear that petitioner was properly held responsible for the withholding tax obligations of the firm. In order to prevail in this case, petitioner was required to establish by clear and convincing evidence that he was not a member or employee of the partnership having a duty to act on its behalf, i.e., that he lacked the necessary authority, or he had the necessary authority but he was thwarted by others in carrying out his duties (*Matter of Goodfriend*, Tax Appeals Tribunal, January 15, 1998). Neither of these circumstances accurately describes petitioner’s situation.

F. Petitioner argues that he was not a partner in the firm. However, the evidence is unconvincing with respect to this assertion. Petitioner admits that he was told he was a partner,



he participated in fact in the “vote” by which John Power was forced out of the firm, he was one of the four “named” partners of the firm<sup>3</sup> after the ouster of John Power, he was a signatory on the firm’s bank accounts and he received partnership returns (Forms 1065) and accompanying Schedules K-1 listing him as a 50-percent partner for several years prior to those in issue. To conclude that his lack of receipt of such forms for other, later, years means that petitioner had somehow ceased to be a partner is simply not plausible.

G. Petitioner’s position and role in the firm clearly leaves him responsible for the unpaid tax in question. Petitioner apparently took little involvement in the firm’s ongoing business operations. Whether this lack of focus on firm business resulted from his involvement with the ongoing long-term litigation, or from simple benign indifference to such matters, or to outright avoidance of duty in order to avoid potential conflict with Richard Hickey, petitioner, as one of the two partners in the firm during the years in issue, clearly had the authority and responsibility to determine whether or not the firm’s withholding obligations were being met. Petitioner’s testimony with regard to his efforts to obtain fiscal information about the firm, and his blithe acceptance of the lack of such information, does not excuse him from the responsibility to assure the payment of the sums in issue. In fact, petitioner’s unmet “demands” for information from Richard Hickey, as well as the manner in which he received such limited personal information regarding his own compensation from the firm, should reasonably have given rise to suspicion and occasioned further inquiries including bank inquiries and, ultimately, action. At the least, this situation entirely undermines petitioner’s claim that he had no reason to believe the requirements of filing and payment were not being met.

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<sup>3</sup> Foley, Hickey, Gilbert & O’Reilly

H. Petitioner did not exercise the authority he had as a partner and as a signatory on the firm's bank accounts. While petitioner may not have undertaken direct involvement in the daily operational aspects of the firm's business, or may in fact have consciously avoided doing so, he had no less actual authority than Richard Hickey. Petitioner clearly expected to share in the anticipated large fee from the accounting action, and on a scale far in excess of that which would be accorded an uninvolved employee. The picture that emerges most clearly is that petitioner fervently hoped for the "big payday" potential of the accounting matter that was actively litigated and long pending, but which ultimately did not result in a successful conclusion.

Petitioner noted that he never signed checks, including payroll checks, or signed or filed tax returns, alleging Richard Hickey's manner of conducting business effectively precluded petitioner from writing checks, hiring and firing employees, or having access to the firm's financial information. This claim must be contrasted against petitioner's long-time membership in the firm, the fact that he had at least initial involvement and input in the hiring of associate attorneys, his partnership status and his daily presence at the firm. Simply put, the record does not support the conclusion that petitioner did not have or could not have exercised sufficient authority and control over the firm's affairs (*see, Matter of Shah*, Tax Appeals Tribunal, February 25, 1999), was misled by reasonable reliance upon the advice of Richard Hickey as to the conduct and status of firm matters, or was thwarted in his efforts to act. In sum, the Division properly determined that petitioner willfully failed to remit the withholding taxes due from the firm during the years in issue.

I. The petition of Terrence P. O'Reilly is hereby denied and the notices of deficiency dated May 15, 2000 are sustained.

DATED: Troy, New York  
January 9, 2003

/s/ Dennis M. Galliher  
ADMINISTRATIVE LAW JUDGE