

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition :
of :
RICHARD KLEIN :
for Revision of a Determination or Refund of Sales and : DETERMINATION
Use Taxes under Articles 28 and 29 of the Tax Law for : DTA NO. 819560
the period September 1, 2000 through November 30, 2001. :

Petitioner, Richard Klein, 551 Fifth Avenue, Suite 1700, New York, New York 10176, filed a petition 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 September 1, 2000 through November 30, 2001.

A hearing was held before Joseph W. Pinto, Jr., Administrative Law Judge, at the offices of the Division of Tax Appeals, 641 Lexington Avenue, New York, New York, on March 11, 2004 at 10:30 A.M., with all briefs submitted by July 28, 2004, which date began the six-month period for the issuance of this determination. Petitioner appeared by William Klein, CPA. The Division of Taxation appeared by Christopher C. O'Brien, Esq. (Cynthia E. McDonough, Esq. and Susan Hutchinson, Esq., of counsel).

ISSUES

I. Whether petitioner was a person responsible for the collection and payment of sales and use taxes on behalf of Sunset Landing LLC for the period September 1, 2000 through November 30, 2001.

II. If petitioner is liable for sales and use taxes, whether he has established that his failure to pay said taxes was due to reasonable cause and not willful neglect.

FINDINGS OF FACT

1. Petitioner, Richard Klein, and his partners opened a restaurant on the Canarsie Pier in Brooklyn, New York which began business on April 6, 2000.¹ The restaurant was known by the name Sunset Landing and provided dining and catering service to the public.

2. The restaurant was operated pursuant to a concession contract from the United States Department of the Interior (“National Parks Service”) which owned the premises, until operations ended on or about June 21, 2002.

3. According to the 2000 New York State Partnership Return, the three members of the limited liability company who owned Sunset Landing LLC and their respective shares were as follows:

<u>Members</u>	<u>Capital Contribution</u> (2000)	<u>Percentage of Ownership</u>
Richard Klein	\$497,832.00	75.4463
William Klein	\$75,000.00	12.2767
Robert Greene	\$75,000.00	12.2769

Petitioner’s percentage of profit and loss sharing in the limited liability company was stated on the 2001 partnership return to be 80%. Petitioner consistently represented himself as the managing member of the company as witnessed by the application for registration as a sales tax vendor and the Quarterly Combined Withholding, Wage Reporting and Unemployment Insurance Return for the period January 1 through March 31, 2001.

4. William Klein, petitioner’s representative herein, is petitioner’s father and Robert Greene’s father-in-law. Mr. Greene took no part in the business other than his initial capital

¹The company did not receive approval of the assignment of the concession contract for the restaurant location from the National Parks Service until August 9, 2000. April 6, 2000 was the date listed on the partnership return and the date of the application for registration as a sales tax vendor.

contribution while William Klein performed the accounting functions. Petitioner hired a restaurant manager to operate the business on a day-to-day basis. This individual had worked at the business location for the previous owner for about 15 years.

5. Although the restaurant operated between April 2000 and June 2002 it was never profitable and all contributions to capital were lost.

6. After receiving several no-remit sales and use tax returns from the company, including the ones for the quarters ended May 31, 2001, August 31, 2001 and November 30, 2001, the Tax Compliance Division began an investigation which included several field visits to the Canarsie Pier location, the first of which took place on March 22, 2002. During that visit, the Division observed operations but was unable to locate the owner, identified by an employee as Richard Klein. The investigator's report noted that there was a restaurant on the Canarsie Pier with a river boat parked behind it. The restaurant was open and stated its hours of operation as Monday to Sunday, 11:30 A.M. to 11:00 P.M. Although the Division left several messages, both verbal and written, for petitioner to contact it, it received no response from petitioner.

7. A second visit took place on July 29, 2002, at which time it was discovered the business had closed. Discussions with the National Parks Service revealed that the company's lease had been canceled due to nonpayment of rent and that business operations had ceased on June 21, 2002.

8. Having established that the business had been closed for nonpayment of rent since June 21, 2002 and with little information forthcoming, on July 11, 2002, the Division issued five notices of determination to Richard Klein as a person responsible for the collection and payment

of sales and use tax on behalf of Sunset Landing LLC. The parties stipulated at hearing that only three of the notices remain at issue,² as more fully delineated in the chart below.

Notice	Period Ended	Tax	Penalty	Interest	Total
L-021304563-9	11/30/01	\$27,578.68	\$4,708.29	\$2,204.01	\$34,490.98
L-021304564-8	8/31/01	\$46,447.73	\$9,289.44	\$5,221.65	\$60,958.82
L-021304565-7	5/31/01	\$31,699.63	\$7,225.82	\$4,563.78	\$43,489.23

Sales tax returns were filed for each of the periods above, but the tax stated as due thereon was not paid. Petitioner conceded that he was responsible for the tax and interest due from the company for all periods up to December 31, 2000, but not thereafter.

9. Among the reasons the Division issued the notices to petitioner were his title of “managing member” stated on Sunset Landing’s application for registration as a sales tax vendor, dated June 2, 2000; his signature on the NYS-45, Quarterly Combined Withholding, Wage Reporting and Unemployment Insurance Return for the period January 1 through March 31, 2001, dated April 25, 2001, identifying petitioner as “managing member”; a copy of a letter the Division received from Chase Manhattan Bank, dated November 15, 2001, in which petitioner informed the bank that he was no longer a member of Sunset Landing LLC and requesting that he be removed as a signatory on the business’s operating account; and the aforementioned 2000 New York State Partnership Return for the period April 6, 2000 through December 31, 2000, which set forth each of the members, their capital contributions and percentages of ownership.

10. There were indications that petitioner had attempted to separate himself from the company. On December 13, 2000, Sunset Landing LLC, William Klein and petitioner executed a

²Notice numbers L-021304566-6 and L-021304567-5 were paid in full and are no longer in issue pursuant to the parties’ stipulation at the formal hearing.

“Membership Purchase Agreement” which provided for petitioner’s share to be transferred to William Klein on January 1, 2001 for the stated price of \$2,000.00. However, the agreement recited that petitioner was the “sole member” of Sunset Landing LLC, in direct conflict with the 2000 New York State Partnership Return, which listed three members through at least July 15, 2001. In addition, the agreement was not acknowledged.

11. By letter dated January 3, 2001, petitioner informed the National Parks Service that he had transferred all his interest in the company to William Klein pursuant to the aforementioned agreement.

12. Despite the documentary evidence suggesting petitioner’s departure from the company as of January 1, 2001, he continued to sign checks on behalf of the company, including payroll, as a matter of convenience for William Klein, who had serious health issues and was unable to discharge the duties associated with managing the business. In addition, as mentioned above, petitioner also signed a Quarterly Combined Withholding, Wage Reporting and Unemployment Insurance Return on April 25, 2001.

13. William Klein resumed control of the business as of the end of June 2001, including signing checks. He utilized a second checking account at Banco Popular on which he was the only signatory. However, petitioner remained a signatory on the Chase Manhattan checking account until November 2001, and checks were issued on this account until that month. Based solely on the checks produced at hearing, it appeared that petitioner signed his last check on that account in June 2001, but account statements and canceled checks produced at hearing by William Klein were incomplete. Two of thirty-two checks were missing from the October 2001 statement and three of five checks for November 2001 were not accounted for. All the checks presented for those months were signed by William Klein.

14. William Klein prepared the tax returns for the company, including the New York partnership return for 2000. However, no subsequent partnership returns were filed for the company despite the fact that the business remained in operation until June of 2002.

15. Petitioner, an attorney, opened the restaurant in order to create an outlet for the culinary talents of his spouse. However, after a very brief period, his wife left the business. Their marital situation deteriorated quickly and a divorce proceeding soon consumed much of petitioner's time and efforts. As a result, his level of participation in the operation of the business declined, but by how much is uncertain.

CONCLUSIONS OF LAW

A. Petitioner conceded that the taxes set forth on the notices of determination in issue are due and owing. The issues presented for resolution are whether petitioner was a person responsible for the collection of the taxes for the quarters in issue and, if so, whether he has demonstrated a basis for abating the penalty imposed.

B. Tax Law § 1133(a) imposes personal liability for taxes required to be collected under Articles 28 and 29 of the Tax Law upon a person required to collect such tax. A person required to collect such tax is defined as "any employee or manager of a limited liability company, . . . who as such . . . employee or manager . . . is under a duty to act for such . . . limited liability company . . . in complying with any requirement of [article 28]; and any member of a partnership or limited liability company." (Tax Law § 1131[1].) The evidence indicated that petitioner was a member of the company and the managing member at the inception of the business in June 2000. When he departed the business is less clear, an ambiguity of his own creation.

C. The resolution of whether a person is responsible for collecting and remitting sales tax on behalf of a company such that the person would have personal liability for the taxes not

collected or paid depends on the facts of each case (*Matter of Cohen v. State Tax Commn.*, 128 AD2d 1022, 513 NYS2d 564; *Matter of Stacy v. State Tax Commn.*, 82 Misc 2d 181, 183, 368 NYS2d 448).

D. Based on the facts presented in this matter, it is determined that petitioner was a person responsible for the collection and payment of sales and use taxes by Sunset Landing LLC for the quarters in issue. He was a substantial capital contributor, pouring almost half a million dollars into the venture, earning him an ownership percentage of 75.4463 and 80% of the profits and losses. The business was his idea and creation. He was the managing member of the limited liability company, signed payroll checks and checks to suppliers/vendors during the audit period, hired a manager to whom he delegated the daily operations of the business, signed at least one tax return and the application for sales tax registration, and negotiated for the assignment of the lease from the prior owner to Sunset Landing LLC.

At some point in 2001, petitioner terminated his relationship with Sunset Landing. Unfortunately, petitioner failed to establish with clarity when this occurred and thus has failed to meet his burden of proof. (20 NYCRR 3000.15[d][5]; *Matter of Allied New York New York Services, Inc. v. Tully*, 83 AD2d 727, 442 NYS2d 624.) This conclusion flows directly from the conflicting evidence submitted by petitioner in support of his claim that he had left the company prior to November of 2001.

The Membership Purchase Agreement can be accorded little weight given its flaws. The agreement, dated December 31, 2000, recited that petitioner was the sole member of the company, contradicting the 2000 partnership return and William Klein's testimony at the formal hearing, both of which disclosed three members of the limited liability company and their respective ownership shares. In fact, the ownership shares of William Klein and Robert Greene

accounted for more than 24.5%, yet there was no mention of them in the agreement. Further, the acknowledgments at the end of the agreement were not executed, casting doubt on the authenticity of the agreement and whether the document was even signed by petitioner or that he made the representations contained therein. (*See*, 1 NY Jur 2d, Acknowledgments, § 1.) There was no evidence that the agreement had been disseminated to Chase Manhattan Bank or to creditors of the company, leading a prudent observer to conclude that petitioner, for unknown reasons and motives, did not want any entity other than the National Parks Service to rely on the agreement. For purposes of this determination, the agreement does not demonstrate when petitioner left the company.

The letter of January 3, 2001 from petitioner to the National Parks Service is of little value also, since it offered the same flawed Membership Purchase Agreement as an inducement for the Parks Service to release him from liability incurred by Sunset Landing LLC as a party to the concession contract between Sunset and the Parks Service. This self-serving document did nothing to rectify the problems with the Membership Purchase Agreement noted above, was not authenticated and was not probative of the issue of whether petitioner was a person responsible for the collection and payment of sales and use taxes on behalf of Sunset Landing LLC.

E. On or about April 25, 2001, almost four months after sending the letter to the Parks Service indicating that he had transferred his interest in the company to William Klein, petitioner filed the Quarterly Combined Withholding, Wage Reporting and Unemployment Insurance Return for the period January 1 through March 31, 2001, and signed the return as the “managing member” of the company.

Although petitioner argued that his participation in the management of the company after January 1, 2001 was only temporary and as a convenience to the company while William Klein

was ill, his behavior as managing member did not change. He had already delegated the daily operations of the business to a manager he hired, he continued to issue payroll checks and made payments to vendors, at least until June 2001, and was unable to establish that he did not issue checks through November 2001, due to the fact that checks were missing from the statements produced at hearing.

Finally, his letter to Chase Manhattan Bank, dated November 15, 2001, obtained by the Division in its investigation and not produced or challenged by petitioner, stated that petitioner resigned as a member of the company on November 15, 2001 and requested that his name be removed from the Sunset Landing LLC account. Therefore, as late as November 15, 2001, petitioner continued to hold himself out to the public as a member of the company. Again, inexplicably, petitioner did not disclose the existence of the Membership Purchase Agreement to the bank, creating more confusion over when he terminated his role and membership in the company.

Petitioner's failure to demonstrate when he terminated his relationship with the company results in a failure to meet his burden of proof and, ultimately, liability for taxes due from the company until November 2001.

F. Petitioner contends that penalty should be abated due to the extenuating circumstances presented. Specifically, he believes his divorce proceeding prevented him from participating fully in the operation, thus causing the business to founder and preventing him from paying the tax due.

Tax Law § 1145(a)(1)(i) provides that any person failing to file a return or pay any tax within the time required shall be subject to a penalty equal to ten percent of the tax due, with an additional one percent due for each additional month or fraction thereof while the failure

continues. Tax Law § 1145(a)(1)(iii) provides that the commissioner of tax and finance may remit all of such penalty upon a finding that the failure to pay was due to reasonable cause and not willful neglect. The regulation at 20 NYCRR 2392.1(d) sets forth various grounds for a finding of reasonable cause, none of which presents itself herein. Indeed, Sunset Landing LLC filed its returns indicating a business operation with taxable sales for each of the months reported, but with no payment of the stated tax due. No reason was given why none of the tax was paid for any of the three quarters in issue. Since the business was a going concern which operated until June of 2002, it obviously made purchases of supplies and paid expenses such as payroll, but chose to totally ignore its responsibility for the taxes it knew were due and dutifully reported to the Division on a quarterly basis. Since petitioner has offered no reason for the abatement of penalty, the Division's imposition of penalty is sustained.

G. The petition of Richard Klein is denied and the three notices of determination dated July 11, 2002 are sustained.

DATED: Troy, New York
November 24, 2004

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