

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
William O. Allen : AFFIDAVIT OF MAILING

for Redetermination of a Deficiency or Revision :
of a Determination or Refund of Personal Income :
Taxes under Article 22 of the Tax Law for the Years:
1974 - 1976 and Article 30 of the Tax Law for the
Year 1976.

State of New York :

ss.:

County of Albany :

David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 1st day of March, 1985, he served the within notice of Decision by certified mail upon William O. Allen, the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

William O. Allen
99-30 59th Ave.
Rego Park, NY 11368

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the petitioner herein and that the address set forth on said wrapper is the last known address of the petitioner.

Sworn to before me this
1st day of March, 1985.

David Parchuck

James A. Haglund
Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK

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Michael I. Saltzman
Saltzman, Garbis & Schwait
One Rockefeller Plaza
New York, NY 10020

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the representative of the petitioner herein and that the address set forth on said wrapper is the last known address of the representative of the petitioner.

Sworn to before me this
1st day of March, 1985.

David Parchuck

James A. Haglund
Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK
STATE TAX COMMISSION
ALBANY, NEW YORK 12227

March 1, 1985

William O. Allen
99-30 59th Ave.
Rego Park, NY 11368

Dear Mr. Allen:

Please take notice of the Decision of the State Tax Commission enclosed herewith.

You have now exhausted your right of review at the administrative level. Pursuant to section(s) 690 & 1312 of the Tax Law, a proceeding in court to review an adverse decision by the State Tax Commission may be instituted only under Article 78 of the Civil Practice Law and Rules, and must be commenced in the Supreme Court of the State of New York, Albany County, within 4 months from the date of this notice.

Inquiries concerning the computation of tax due or refund allowed in accordance with this decision may be addressed to:

NYS Dept. Taxation and Finance
Law Bureau - Litigation Unit
Building #9, State Campus
Albany, New York 12227
Phone # (518) 457-2070

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative
Michael I. Saltzman
Saltzman, Garbis & Schwait
One Rockefeller Plaza
New York, NY 10020
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition :
of :
George E. Pugh : AFFIDAVIT OF MAILING
for Redetermination of a Deficiency or Revision :
of a Determination or Refund of Personal Income :
Taxes under Article 22 of the Tax Law for the Years:
1974 - 1976 and Article 30 of the Tax Law for the
Year 1976. :

State of New York :

ss.:

County of Albany :

David Parchuck, being duly sworn, deposes and says that he is an employee of the State Tax Commission, that he is over 18 years of age, and that on the 1st day of March, 1985, he served the within notice of Decision by certified mail upon George E. Pugh, the petitioner in the within proceeding, by enclosing a true copy thereof in a securely sealed postpaid wrapper addressed as follows:

George E. Pugh
620 E. 20th St., Suite 6-C
New York, NY 10009

and by depositing same enclosed in a postpaid properly addressed wrapper in a post office under the exclusive care and custody of the United States Postal Service within the State of New York.

That deponent further says that the said addressee is the petitioner herein and that the address set forth on said wrapper is the last known address of the petitioner.

Sworn to before me this
1st day of March, 1985.

David Parchuck

Conrad A. Hagelund

Authorized to administer oaths
pursuant to Tax Law section 174

STATE OF NEW YORK

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In the Matter of the Petition :
of :
George E. Pugh : AFFIDAVIT OF MAILING

for Redetermination of a Deficiency or Revision :
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Taxes under Article 22 of the Tax Law for the Years:
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Michael I. Saltzman
Saltzman, Garbis & Schwait
One Rockefeller Plaza
New York, NY 10020

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Sworn to before me this
1st day of March, 1985.

David Parchuck

James A. Haglund
Authorized to administer oaths
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STATE OF NEW YORK
STATE TAX COMMISSION
ALBANY, NEW YORK 12227

March 1, 1985

George E. Pugh
620 E. 20th St., Suite 6-C
New York, NY 10009

Dear Mr. Pugh:

Please take notice of the Decision of the State Tax Commission enclosed herewith.

You have now exhausted your right of review at the administrative level. Pursuant to section(s) 690 & 1312 of the Tax Law, a proceeding in court to review an adverse decision by the State Tax Commission may be instituted only under Article 78 of the Civil Practice Law and Rules, and must be commenced in the Supreme Court of the State of New York, Albany County, within 4 months from the date of this notice.

Inquiries concerning the computation of tax due or refund allowed in accordance with this decision may be addressed to:

NYS Dept. Taxation and Finance
Law Bureau - Litigation Unit
Building #9, State Campus
Albany, New York 12227
Phone # (518) 457-2070

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative
Michael I. Saltzman
Saltzman, Garbis & Schwait
One Rockefeller Plaza
New York, NY 10020
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition	:	
	:	
of	:	
	:	
GEORGE E. PUGH	:	
	:	
for Redetermination of a Deficiency or for	:	
Refund of Personal Income Taxes under Article	:	
22 of the Tax Law for the Years 1974 through	:	
1976 and Article 30 of the Tax Law for the Year	:	
1976.	:	

DECISION

In the Matter of the Petition	:	
	:	
of	:	
	:	
WILLIAM O. ALLEN	:	
	:	
for Redetermination of a Deficiency or for	:	
Refund of Personal Income Taxes under Article	:	
22 of the Tax Law for the Years 1974 through	:	
1976 and Article 30 of the Tax Law for the Year	:	
1976.	:	

Petitioner, George E. Pugh, 620 East 20th Street, Suite 6-C, New York, New York 10009, filed a petition for redetermination of a deficiency or for refund of personal income taxes under Article 22 of the Tax Law for the years 1974 through 1976 and Article 30 of the Tax Law for the year 1976 (File No. 17912).

Petitioner, William O. Allen, 99-30 59th Avenue, Rego Park, New York 11368, filed a petition for redetermination of a deficiency or for refund of personal income taxes under Article 22 of the Tax Law for the years 1974 through 1976 and Article 30 of the Tax Law for the year 1976 (File No. 17908).

A consolidated formal hearing was commenced before Frank W. Barrie, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on December 7, 1983 at 1:15 P.M. and continued to

conclusion at the same offices on February 6, 1984 at 1:00 P.M., with all briefs to be submitted by May 14, 1984. Both petitioners appeared by Michael I. Saltzman, Esq. at the hearing held on December 7, 1983. At the continuation of the hearing on February 6, 1984, petitioners appeared by Michael I. Saltzman, Esq. and Paul Green, Esq. The Audit Division appeared by John P. Dugan, Esq. (Anna Colello, Esq., of counsel) on both dates.

ISSUES

I. Whether petitioners were persons responsible for collecting and paying over taxes withheld from the wages of employees of the Arthur C. Logan Memorial Hospital (formerly known as Knickerbocker Hospital), who willfully failed to do so, and are therefore liable for the penalties imposed under Tax Law §685(g).

II. Whether New York State and/or New York City should have collected withholding taxes due and owing from Arthur C. Logan Memorial Hospital as an offset against the hospital's Medicaid reimbursement funds and, if so, whether petitioners are thereby relieved from any personal liability for such taxes.

III. Whether the penalties asserted against petitioners should be cancelled on the basis that the Audit Division discriminated against petitioners by not asserting penalties against all members of the hospital's board of trustees.

IV. Whether the State Tax Commission should utilize its discretion under Tax Law §685(g) (as amended by L. 1976, c. 10, §1) to waive the penalty asserted against petitioners.

FINDINGS OF FACT

Petitioners, by their representative, Michael I. Saltzman, Esq., and the Audit Division by its representative, John P. Dugan, Esq. (Anna Colello, Esq.,

of counsel) entered into a stipulation of facts¹ and a supplemental stipulation of facts which are incorporated into this decision.

1. On February 15, 1977, the Audit Division issued a Notice of Deficiency and two statements of deficiency against petitioner William O. Allen asserting penalties equal to the New York State withholding tax of Arthur C. Logan Memorial Hospital² (hereinafter "the hospital") which was due and unpaid for the years 1974, 1975 and 1976 of \$237,231.97, \$430,788.78 and \$352,313.33, respectively, plus the due and unpaid New York City withholding tax for the hospital for the year 1976 of \$99,796.01.

On February 15, 1977, the Audit Division issued a Notice of Deficiency and two statements of deficiency against petitioner George E. Pugh asserting penalties equal to the New York State withholding tax of the hospital which was due and unpaid for the years 1974, 1975 and 1976 of \$237,231.97, \$430,788.78 and \$352,313.33, respectively, plus the due and unpaid New York City withholding tax for the Hospital for the year 1976 of \$99,796.01.

2. The periods and amount of the penalty were delineated by the Audit Division as follows:

<u>WITHHOLDING TAX PERIOD</u>	<u>NEW YORK STATE AMOUNT</u>
January 1, 1974 - June 30, 1974	\$ 172,299.04
September 1, 1974 - September 15, 1974	15,990.53
September 16, 1974 - September 30, 1974	16,667.70
December 1, 1974 - December 15, 1974	16,402.52
December 16, 1974 - December 31, 1974	15,872.18
February 16, 1975 - February 28, 1975	18,189.24
March 1, 1975 - March 15, 1975	17,879.90
March 16, 1975 - March 31, 1975	17,128.38
April 1, 1975 - April 15, 1975	17,620.61

¹ The stipulation of facts which petitioners prepared for purposes of this hearing included thirty-eight separately numbered paragraphs. The Audit Division agreed to all of such paragraphs except for paragraphs one, two, three, the fifth sentence of four, ten, fifteen, seventeen, the last sentence of nineteen, twenty, twenty-one, twenty-two, twenty-three and twenty-seven.

² The Hospital was formerly known as the Knickerbocker Hospital. In February of 1974, it became the Arthur C. Logan Memorial Hospital.

<u>WITHHOLDING TAX PERIOD</u>	<u>NEW YORK STATE AMOUNT</u>
May 1, 1975 - May 15, 1975	24,826.24
May 16, 1975 - May 31, 1975	18,470.95
June 1, 1975 - June 15, 1975	18,905.45
June 16, 1975 - June 30, 1975	18,978.44
July 1, 1975 - July 15, 1975	18,564.91
July 16, 1975 - July 31, 1975	20,880.17
August 1, 1975 - August 15, 1975	32,239.59
August 16, 1975 - August 31, 1975	21,010.70
September 1, 1975 - September 15, 1975	21,410.26
September 16, 1975 - September 30, 1975	20,546.09
October 1, 1975 - October 15, 1975	20,357.30
October 16, 1975 - October 31, 1975	28,051.00
November 1, 1975 - November 15, 1975	18,810.12
November 16, 1975 - November 30, 1975	17,882.75
December 1, 1975 - December 15, 1975	19,675.99
December 16, 1975 - December 31, 1975	20,560.29
October 1, 1975 - December 31, 1975 ³	18,300.40
January 1, 1976 - January 15, 1976	19,857.58
January 16, 1976 - January 31, 1976	32,775.06
February 1, 1976 - February 15, 1976	20,647.06
February 16, 1976 - February 29, 1976	20,508.44
March 1, 1976 - March 15, 1976	20,419.91
March 16, 1976 - March 31, 1976	19,998.85
April 1, 1976 - April 15, 1976	19,429.27
April 16, 1976 - April 30, 1976	27,517.77
May 16, 1976 - May 31, 1976	19,104.97
June 1, 1976 - June 15, 1976	20,481.09
June 16, 1976 - June 30, 1976	19,988.60
July 16, 1976 - July 31, 1976	29,449.78
August 1, 1976 - August 15, 1976	19,396.63
August 16, 1976 - August 31, 1976	19,070.36
September 16, 1976 - September 30, 1976	24,756.24
October 1, 1976 - October 15, 1976	18,911.72
	<u>\$1,020,334.08</u>
	<u>NEW YORK CITY AMOUNT</u>
February 1, 1976 - February 29, 1976	\$ 12,972.79
March 1, 1976 - March 31, 1976	13,818.48
April 1, 1976 - April 30, 1976	16,436.14
May 1, 1976 - May 31, 1976	13,159.32
June 1, 1976 - June 30, 1976	13,892.15
July 1, 1976 - July 31, 1976	16,398.14
August 1, 1976 - August 31, 1976	10,108.01
September 1, 1976 - September 30, 1976	3,010.98
	<u>\$ 99,796.01</u>

³ There is no explanation in the record concerning the separate delineation of this three month period.

3. The hospital was a non-profit voluntary hospital located at 130th Street and Convent Avenue in Harlem, New York City. The hospital, which was over one hundred years old, during the years at issue served a poor black community. It had 214 beds and operated at a patient occupancy level of approximately eighty-five to ninety percent of capacity. Approximately fifty percent of the hospital's revenue consisted of Medicaid (the program of public medical aid for the poor) payments. Thirty-five percent of the revenues consisted of Medicare (the program of public medical aid for the elderly and disabled) payments. The remainder of its revenue was from a variety of sources including Blue Cross, private insurance carriers, worker's compensation, and a contract with New York City to provide mental health services.

4. Petitioner William O. Allen served as the hospital's executive director from the end of 1972 until his resignation in February, 1978. He was the assistant director of the hospital for support services prior to his tenure as executive director. He testified that during the years at issue, his salary was approximately forty-five to fifty thousand dollars. However, at the time of his resignation in 1978, his salary was approximately sixty thousand dollars. As executive director, William O. Allen was responsible for carrying out policies established by the board of trustees. He testified that from February, 1976 to the end of the period at issue, the chairman of the board of trustees, Reverend M. L. Wilson, required him to provide the hospital's bank balance and a listing of outstanding bills on a daily basis. (Prior to February, 1976, such information was provided on a weekly basis.) Reverend Wilson reviewed this information and determined which parties should be paid.

William O. Allen had authority to sign checks up to three thousand dollars and he signed payroll checks. However, checks in excess of three

thousand dollars required the co-signature of one of the following three members of the board of trustees: Reverend M. L. Wilson, William R. Hudgins or Dr. Alfred Gellhorn. Mr. Allen testified that a check for \$400,000 to the Internal Revenue Service for previously unpaid federal withholding taxes was signed by Reverend Wilson and William Hudgins.

5. Article XI of the hospital's by-laws, which were in effect until April, 1974, detailed the duties and authority of the executive director. Pursuant to the by-laws, the executive director had the power to hire and fire all hospital employees, was responsible for the purchase of all hospital supplies, was required to keep accurate accounts of all moneys and was required to ensure "that the regulations of the Health Department and other public authorities, affecting the operation and management of this Institution, are immediately complied with." The hospital's by-laws, which were in effect on and after April, 1974, note the authority and responsibility of the executive director in much greater detail and also appear to expand his authority and responsibility. Pursuant to such by-laws, the executive director's additional responsibility and authority included the requirement that he advise the board of trustees on the formation of policies and also serve on the board of trustees with voting power.⁴ In addition, the new by-laws note that the executive director is the duly authorized representative of the hospital "in all matters which the Board has not formally

⁴ Petitioner Allen testified that he did not have voting power. In the minutes of board of trustees meetings, he is listed (with petitioner George Pugh) under a heading "Administration." He is not listed under the heading "For the Board of Trustees." However, the minutes for a meeting of the executive committee of the board of trustees on June 26, 1973 show that he seconded a motion concerning hospital house staff appointments and seconded a motion approving the resignation of Dr. Howard S. Dunbar. In addition, the minutes for the board of trustees meeting on April 22, 1975 show that Allen was elected an officer of the board as assistant secretary.

delegated to other persons." Furthermore, the by-laws provide that the executive director's decision as to the interpretation of the hospital's by-laws or his decision in cases of disputed authority "shall govern unless the Board shall determine otherwise."

6. In practice, petitioner Allen did not have exclusive authority to hire and fire hospital personnel. Appointments of hospital staff doctors were overseen by the hospital's medical board. The president of the medical board, who was a member of the board of trustees, would present to the board of trustees for final review the names of all of the doctors who satisfied the credentials committee of the medical board. (The hospital had difficulty attracting graduates of American medical schools and most of their staff doctors were foreign born and educated.) Other hospital employees including nurses were interviewed by the various department heads who, in conjunction with the hospital's director of personnel, reviewed the job application and made a determination to hire. In order to be placed on the payroll, petitioner Allen was required to sign a "personnel action" which he testified was merely perfunctory. In matters of firing, petitioner Allen also did not have exclusive authority to fire employees because, pursuant to a grievance procedure required by an agreement with the union representing the hospital's employees (other than doctors), the board of trustees made the final decision to dismiss an employee. It also appears that the board of trustees had the last word on the firing of doctors.

In addition, in practice, William O. Allen obtained approval or authority from the board of trustees to act on its behalf in matters of consequence. For example, the minutes of the executive committee of the board of trustees shows that Mr. Allen requested that the board of trustees "re-affirm his authority

to act independently without further confirmation (to close the hospital if the union representing hospital employees rejected the hospital's last proposal concerning a retroactive pay increase)...." His negotiations with the Internal Revenue Service concerning the payment of past-due withholding taxes were conducted pursuant to a resolution adopted by the board of trustees authorizing him to conduct such negotiations.

7. Petitioner George E. Pugh was employed by the hospital from December 11, 1973 through April 7, 1978. Mr. Pugh is a certified public accountant, has an M.B.A. and is a member of the New York State bar. He initially served as comptroller of the hospital until early 1975 when he became the assistant director of finance. He described his duties as encompassing "the general record keeping functions, billing, checks, securing of the revenues, filing of the various reports required by the various governmental agencies...." When he was comptroller, he oversaw the preparation of financial statements. In his capacity as assistant director of finance, he spent time trying to maximize reimbursements from Medicaid and Medicare and to develop sources of new revenue. He had no authority to sign checks. Petitioner George E. Pugh was not an officer or member of the hospital's board of trustees in any capacity.

8. Neither petitioner Allen nor petitioner Pugh signed tax returns, including withholding tax returns. New York withholding tax returns were signed by Ewan Dawes and Solomon Hoff, hospital staff accountants. However, William O. Allen signed a waiver extending the period of limitations to assess unpaid federal withholding taxes. According to the minutes of a special meeting of the board of trustees on May 29, 1974, "Mr. Allen asked for advice from the Board as to whether or not he should sign the IRS waiver or whether

someone else should sign. This matter was resolved in the affirmative in 'Executive Session'."

9. The hospital's board of trustees, which met monthly, consisted of ten to twelve members during the period at issue. Under the hospital's charter and by-laws, it managed the operations, affairs and property of the hospital. Some of the board members were prominent politicians and leaders including Robert F. Wagner, Bayard Rustin and Ramsey Clark. However, a review of the minutes of board meetings which are part of the record herein shows that only five to nine board members attended board meetings. In addition, the meetings were usually dominated by the chairman of the board, Rev. M. L. Wilson.

It appears that immediately prior⁵ to the period at issue, the executive committee of the board of trustees (which included Rev. M. L. Wilson, Dr. Michael A. Diana, Mr. William R. Hudgins and Dr. Robert E. Marshak) and not the entire board of trustees met to consider appointments and resignations of medical personnel and to discuss the hospital's finances in detail. The minutes for a meeting of the board of trustees on January 22, 1974 show that the former functions of the executive committee were apparently assumed by the entire board. In addition, at the meetings of the entire board of trustees, the acts and proceedings of officers and committees were ratified and approved.

10. Petitioners argue that the members of the board of trustees were the persons responsible for the payment of withholding taxes. William O. Allen's position is that he was merely an employee of the board carrying out their policy to keep the hospital in operation. However, see Finding of Fact "5", supra, where it was found that petitioner William O. Allen was an officer and member of the board of trustees.

⁵ For example, the minutes for meetings of the executive committee of the board of trustees for May 22, 1973 and June 26, 1973 show detailed discussions of hospital finances and the approval of medical staff appointments.

At a meeting of the finance committee of the board of trustees on June 18, 1974, Dr. Michael A. Diana noted that if the Internal Revenue Service did not forbear on the collection of unpaid withholding taxes, the hospital would close and the trustees would "seriously face the prospect of personal liability for unpaid withholding taxes." At the same meeting, Rev. M. L. Wilson noted that "(T)he corporate by-laws clearly spelled out the responsibility and non-delegability of the Board of Trustees' responsibility in fiscal matters...." In addition, the minutes of a "Special Regular Board of Trustees Meeting" on March 30, 1978, attended by members of the board, Rev. M. L. Wilson, Dr. Wyatt Tee Walker, Ramsey Clark, William Hudgins, Rose Morgan and Bayard Rustin, note that "It was agreed that all members of the Board past and present should be equally and collectively responsible (for unpaid federal withholding taxes)."

William O. Allen testified that the chairman of the board of trustees, Rev. M. L. Wilson, told him on several occasions that he could not be personally liable for unpaid withholding taxes because he was the board's employee. However, Rev. M. L. Wilson did not testify at the hearing held herein.

11. At the April 16, 1974 meeting of the board of trustees, Eliot H. Lumbard, a member of the board, criticized the payment of \$400,000 (which represented retroactive Medicare funds received by the Hospital) to the Internal Revenue Service for previously unpaid federal withholding taxes. According to the minutes of this meeting, "In his (Lumbard's) opinion, he stated the proper course would have been to take the money, invest it at interest, and 'negotiate' with creditors...." The minutes describe Mr. Allen's response as follows:

"Mr. Allen responded that this (the payment of the \$400,000) was done under his authority as Executive Director who was charged with the duty by the full Board of administering the affairs, including

fiscal, of the hospital. Mr. Allen further referred to the resolution⁶ of the full Board authorizing him to take whatever action he deemed necessary while the fiscal crisis continued in existence."

Mr. Allen also described his authority in broad terms in a letter dated February 11, 1976, Exhibit "N" herein, to George Pugh:

"I have relieved you of the day to day operations of the Accounting Department... Effective this date I assume responsibility for determining the allocations of cash to be disbursed. Do not in any way interfere with decisions that I have made and conveyed to Mr. Bridgett, Controller."

12. At the board of trustees meeting on March 26, 1974, Rev. M. L. Wilson appointed a special study committee on hospital financial matters. Members of the board of trustees serving on this committee were Eliot Lumbard, Mrs. Louise Gimbel (of the Gimbel's department store family), Dr. Edgar Draper and Dr. Robert Polk. At the first meeting of the study committee, Mr. Lumbard, who emerged as the spokesman for the study committee, asked petitioner Pugh why the hospital was continuing to operate with an increasing deficit. Mr. Pugh's response was to analyze the hospital's liabilities. He also pointed out that the hospital had "been operating on the government's money (withholding taxes that were not paid over to the Internal Revenue Service and New York State/City)." Mr. Lumbard asked about "the status of the liability insurance covering Trustees and officers of the hospital⁷." Mr. Pugh then pointed out that "(I)n his opinion, under the present reimbursement policies, limitations imposed by our outmoded physical facility, our patient clientel (sic), and with a notable lack in

⁶ It appears, based upon a review of the minutes for the meeting of the finance committee of the board of trustees on June 18, 1974, that the board of trustees adopted a resolution directing William O. Allen, as Executive Director, "to give first priority to payment of taxes and payroll related matters...."

⁷ It appears that Eliot Lumbard resigned from the board of trustees upon his realization that he might be potentially liable for unpaid withholding taxes if he remained on the board.

referral of private patients, he could see no way that a non-deficit operation was possible except through additional funds received through governmental subsidies, private contributions or both." The committee then discussed the proposal to construct a new facility which would combine the hospital and Sydenham Hospital into a five hundred bed facility (the Manhattanville Health Project). Mr. Pugh suggested that the hospital's deficit could be rolled over into the total mortgage loan on the new facility. "Mr. Lumbard expressed doubt as to the correctness of this Statement and conveyed a request to see this in writing." Mr. Pugh noted that the committee's concerns and suggestions "would be transmitted to the Executive Director for any action and follow-up be deemed appropriate."

13. The Hospital's financial difficulties date back to the early 1970's when it was faced with the disallowance of substantial expenses which it incurred in the late 1960's in providing medical services to Medicaid and Medicare patients. According to the testimony of petitioner William O. Allen, "the retroactive cost reimbursement principle" forced the Hospital into the position where it could never meet its bills:

"The (Medicaid and Medicare) revenues would show hundreds of dollars came in but the State would grab off fifty dollars of that hundred dollars before we ever saw it. We may have a revenue on the books of the hundred dollars, but we would only get fifty dollars, and that's the way it went until the date it closed."

14. The State of New York Department of Health determined, pursuant to a reimbursement formula, the amount of Medicaid and Medicare payments payable to the hospital. The formula consisted of a base of two year old data which was adjusted for inflation, pursuant to a trend factor, much like a cost-of-living index. It was further subjected to peer group ceilings and to various penalties. The hospital's "allowable costs" (which were reimbursed by Medicaid and Medicare

payments) were always substantially lower than its actual costs for a number of reasons. First, the hospital was compared with other similarly sized hospitals, its "peer group." The most that the hospital could receive in reimbursement was 110 percent of the peer group average. According to the testimony of William O. Allen, none of the other hospitals in the hospital's peer group were inner-city hospitals serving a poor black community. The hospital was further penalized by a reduction in its reimbursement amounts for the following reasons: (1) its patients were staying longer than their statistical averages and (2) patients were not being discharged to other types of facilities such as skilled nursing homes or acute care hospitals. The hospital treated many homeless or ill-housed people who had no suitable place to go after treatment and, according to William O. Allen, the hospital was "obligated to keep them until there was a place... We kept one woman for six years because the State of New York did not obtain placement for her." In addition, the hospital was legally required to provide emergency medical services regardless of the ability of a patient to pay for such services. Approximately fifteen percent of the hospital's patient load consisted of the working poor who did not qualify for Medicaid and were unable to pay for medical services. To compound the difficulty of a reimbursement rate which did not meet its actual costs of providing services to Medicaid and Medicare patients, in 1974 and 1975, New York State imposed a freeze on raising reimbursement rates.

15. The hospital's dire financial condition was tempered by hopes that some means would be found to pay off or cancel the unpaid withholding taxes. The board thought that it might be possible to obtain a political decision from the office of Governor Nelson Rockefeller to forgive unpaid payroll taxes or that, in the alternative, the Division of Hospital Financing of the New York

State Department of Health might approve reimbursement rates high enough to pay off back taxes. The board's main hope for the survival of the hospital rested upon the approval of its Manhattanville Health Project. In addition to the possibility that the hospital's deficit might be rolled over into the mortgage loan which would finance the construction of the new hospital, the board hoped that a new facility would attract doctors with private practices. In petitioner Pugh's words, "We could not afford not to build the new hospital."

16. On October 26, 1976, the Hospital filed a petition under Chapter XI of the Bankruptcy Act seeking a plan for rehabilitation. It continued in operation until 1978 when it finally closed its doors. The record is unclear when it was finally adjudicated bankrupt and its assets liquidated. A review of the minutes for the meetings of the board of trustees reveals the following deficits⁸ for the Hospital:

<u>Date</u>	<u>Accumulated Deficit</u>	<u>Total Deficit</u>	<u>Total Accumulated Deficit</u>	<u>Aggregate Deficit</u>
April 30, 1973		\$5,329,118		
May 31, 1973		5,507,987		
December 31, 1973	\$6,428,338			
March 31, 1974	6,824,571			
May 31, 1974			\$6,022,767	
August 31, 1974	6,476,118			
October 31, 1974	6,707,782			
August 31, 1975			5,750,240	
August 31, 1976				\$7,701,326

17. The Internal Revenue Service assessed penalties for unpaid withholding taxes of the hospital against each of the petitioners in the approximate amount of \$3 million. The Internal Revenue Service commenced an action against petitioners and others in the United States District Court for the Southern District of New York. The action was dismissed without prejudice after it was determined

⁸ The deficits as noted in the chart, infra, were described in various ways in the minutes. The record is unclear on how such terms vary from one to the other.

that there was no prospect of collection from the petitioners. However, tax liens for three million dollars against petitioners remain outstanding until the statute of limitations on collection expires.

18. Included in petitioners' brief are proposed findings of fact, numbered one through thirty-seven. All are incorporated into and made a part of this decision except for the following:

(1) The last sentence of proposed finding of fact "3" (because the record does not establish that William Allen's authority was limited);

(2) Proposed finding of fact "5" (because William Allen was granted very broad powers and much discretion to act as he determined was necessary);

(3) Proposed finding of fact "6" to the extent that it says that petitioner Allen provided the chairman of the board of trustees, Rev. M. L. Wilson with a report of the hospital's bank statements and a request for disbursements on a daily basis (see Finding of Fact "4", supra);

(4) The last sentence of proposed finding of fact "7" (because, as a member of the board of trustees, petitioner Allen participated in hiring decisions);

(5) The last sentence of proposed finding of fact "8" (because as a member of the board of trustees, petitioner Allen would have participated in such decisions);

(6) Proposed finding of fact "11" (because petitioner Pugh was comptroller of the hospital from April, 1973 until early 1975);

(7) The last sentence of proposed finding of fact "22" (because the record does not establish such fact); and

(8) Proposed finding of fact "28" to the extent that it says "members" of the board of trustees criticized Allen and Pugh (because the record shows that only trustee Eliot Lumbard was critical with regard to the payment of \$400,000 to the Internal Revenue Service).

CONCLUSIONS OF LAW

A. That, pursuant to Tax Law §685(g),⁹ any "person" required to collect, truthfully account for and pay over withholding taxes, who willfully fails to do so, can be subjected to a penalty equaling the amount of the tax. "Person" for purposes of this section includes "any officer or employee of any corporation ...who as such officer, employee...is under a duty to perform the act in respect of which the violation occurs." Tax Law §685(n).

B. That petitioner George E. Pugh was not a member of the hospital's board of trustees, the governing body of the hospital. In addition, as noted in Finding of Fact "7", supra, his authority and responsibilities were circumscribed. Therefore, it is concluded that petitioner George E. Pugh was not a person responsible for the collection and payment over of withholding taxes due from the hospital.

C. That petitioner William O. Allen was a voting member of the hospital's board of trustees. In addition, as noted in Findings of Fact "5" and "11", the board of trustees delegated significant authority and discretion to petitioner William O. Allen concerning the operation of the hospital. Although petitioner William O. Allen did not have exclusive authority concerning the operation of the hospital and also obtained approval or ratification of his actions from the board of trustees, he was influential in the affairs of the hospital, both in

⁹ Tax Law §1312 provides that any tax imposed pursuant to Article 30 "shall be administered and collected by the State Tax Commission in the same manner as the tax imposed by article twenty-two...."

the capacity as a board member and as executive director, and was a responsible person for purposes of Tax Law §685(g). See Cooper v. United States, 539 F. Supp. 117.

D. That in order to conclude that petitioner William O. Allen may be saddled with personal liability under Tax Law §685(g) for unpaid withholding taxes, we must also determine that he willfully failed to collect and pay over withholding taxes of the hospital.

E. That the failure to collect and pay over withholding taxes is willful if such failure 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. Matter of Levin v. Gallman, 42 N.Y.2d 32.

Petitioner George E. Pugh was correct, when he noted at the first meeting of the hospital's special study committee on hospital financial matters, that the hospital had "been operating on the government's money (withholding taxes that were not paid over to the Internal Revenue Service and New York State/City)." Although such money was used for the worthy purpose of keeping the doors of a hospital in a poor, black community open, nonetheless the trust funds belonged to the government and should have been paid over to the government. Therefore, petitioner William O. Allen, as an active member of the board of trustees and executive director of the hospital, participated in the decision to keep the hospital open and therefore he "willfully" failed to collect and pay over the withholding taxes at issue.

F. That there is no basis in law or regulations to relieve petitioner William O. Allen of personal liability for the unpaid withholding taxes because New York State/City did not offset the taxes due and owing against the hospital's Medicaid reimbursement funds. Furthermore, the Audit Division was not required

to attempt to collect the taxes from the corporation before asserting potential liability against a responsible officer.

G. That the Audit Division was not required to take steps against all persons who might have personal liability for unpaid withholding taxes. See Burack v. U.S., 72-2 USTC ¶9490.

H. That an amendment to Tax Law §685(g) was added effective February 25, 1976 authorizing the State Tax Commission "in its discretion, to waive, reduce or compromise any penalty under this subsection." An examination of the legislative bill jacket for the Laws of 1976, Chapter 6, which codified this amendment, reveals that the intent behind the legislation was to provide the State Tax Commission with statutory authority to abate the withholding tax penalty against responsible officers if the full tax due and owing has been collected once (which previously had been administrative policy). Therefore, this discretionary authority is not applicable herein.


I. That the petition of George E. Pugh is granted.

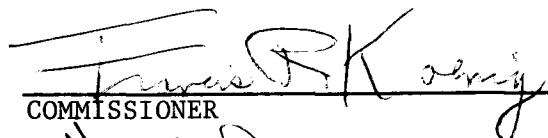
J. That the petition of William O. Allen is denied.

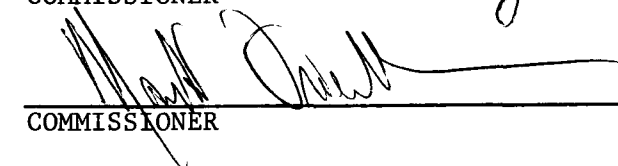
DATED: Albany, New York

STATE TAX COMMISSION

MAR 01 1985


PRESIDENT


COMMISSIONER


COMMISSIONER

TA 26 (9-79)

STATE OF NEW YORK
State Tax Commission
TAX APPEALS BUREAU
STATE CAMPUS
ALBANY, N. Y. 12227

8691

☐ CHECK

☐ HOLD

DATE 3-48

1ST NOTICE 3/9

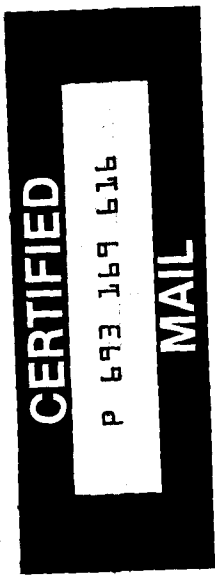
2ND NOTICE 3/19

RETURN

Detached from
PS Form 3049-A
Oct. 1980



William O. Allen
99-30 59th Ave.
Reno Park, NY 11368



STATE OF NEW YORK
STATE TAX COMMISSION
ALBANY, NEW YORK 12227

March 1, 1985

William O. Allen
99-30 59th Ave.
Rego Park, NY 11368

Dear Mr. Allen:

Please take notice of the Decision of the State Tax Commission enclosed herewith.

You have now exhausted your right of review at the administrative level. Pursuant to section(s) 690 & 1312 of the Tax Law, a proceeding in court to review an adverse decision by the State Tax Commission may be instituted only under Article 78 of the Civil Practice Law and Rules, and must be commenced in the Supreme Court of the State of New York, Albany County, within 4 months from the date of this notice.

Inquiries concerning the computation of tax due or refund allowed in accordance with this decision may be addressed to:

NYS Dept. Taxation and Finance
Law Bureau - Litigation Unit
Building #9, State Campus
Albany, New York 12227
Phone # (518) 457-2070

Very truly yours,

STATE TAX COMMISSION

cc: Petitioner's Representative
Michael I. Saltzman
Saltzman, Garbis & Schwait
One Rockefeller Plaza
New York, NY 10020
Taxing Bureau's Representative

STATE OF NEW YORK

STATE TAX COMMISSION

In the Matter of the Petition	:	
	:	
of	:	
	:	
GEORGE E. PUGH	:	
	:	
for Redetermination of a Deficiency or for	:	
Refund of Personal Income Taxes under Article	:	
22 of the Tax Law for the Years 1974 through	:	
1976 and Article 30 of the Tax Law for the Year	:	
1976.	:	

DECISION

In the Matter of the Petition	:
	:
of	:
	:
WILLIAM O. ALLEN	:
	:
for Redetermination of a Deficiency or for	:
Refund of Personal Income Taxes under Article	:
22 of the Tax Law for the Years 1974 through	:
1976 and Article 30 of the Tax Law for the Year	:
1976.	:

Petitioner, George E. Pugh, 620 East 20th Street, Suite 6-C, New York, New York 10009, filed a petition for redetermination of a deficiency or for refund of personal income taxes under Article 22 of the Tax Law for the years 1974 through 1976 and Article 30 of the Tax Law for the year 1976 (File No. 17912).

Petitioner, William O. Allen, 99-30 59th Avenue, Rego Park, New York 11368, filed a petition for redetermination of a deficiency or for refund of personal income taxes under Article 22 of the Tax Law for the years 1974 through 1976 and Article 30 of the Tax Law for the year 1976 (File No. 17908).

A consolidated formal hearing was commenced before Frank W. Barrie, Hearing Officer, at the offices of the State Tax Commission, Two World Trade Center, New York, New York, on December 7, 1983 at 1:15 P.M. and continued to

conclusion at the same offices on February 6, 1984 at 1:00 P.M., with all briefs to be submitted by May 14, 1984. Both petitioners appeared by Michael I. Saltzman, Esq. at the hearing held on December 7, 1983. At the continuation of the hearing on February 6, 1984, petitioners appeared by Michael I. Saltzman, Esq. and Paul Green, Esq. The Audit Division appeared by John P. Dugan, Esq. (Anna Colello, Esq., of counsel) on both dates.

ISSUES

I. Whether petitioners were persons responsible for collecting and paying over taxes withheld from the wages of employees of the Arthur C. Logan Memorial Hospital (formerly known as Knickerbocker Hospital), who willfully failed to do so, and are therefore liable for the penalties imposed under Tax Law §685(g).

II. Whether New York State and/or New York City should have collected withholding taxes due and owing from Arthur C. Logan Memorial Hospital as an offset against the hospital's Medicaid reimbursement funds and, if so, whether petitioners are thereby relieved from any personal liability for such taxes.

III. Whether the penalties asserted against petitioners should be cancelled on the basis that the Audit Division discriminated against petitioners by not asserting penalties against all members of the hospital's board of trustees.

IV. Whether the State Tax Commission should utilize its discretion under Tax Law §685(g) (as amended by L. 1976, c. 10, §1) to waive the penalty asserted against petitioners.

FINDINGS OF FACT

Petitioners, by their representative, Michael I. Saltzman, Esq., and the Audit Division by its representative, John P. Dugan, Esq. (Anna Colello, Esq.,

of counsel) entered into a stipulation of facts¹ and a supplemental stipulation of facts which are incorporated into this decision.

1. On February 15, 1977, the Audit Division issued a Notice of Deficiency and two statements of deficiency against petitioner William O. Allen asserting penalties equal to the New York State withholding tax of Arthur C. Logan Memorial Hospital² (hereinafter "the hospital") which was due and unpaid for the years 1974, 1975 and 1976 of \$237,231.97, \$430,788.78 and \$352,313.33, respectively, plus the due and unpaid New York City withholding tax for the hospital for the year 1976 of \$99,796.01.

On February 15, 1977, the Audit Division issued a Notice of Deficiency and two statements of deficiency against petitioner George E. Pugh asserting penalties equal to the New York State withholding tax of the hospital which was due and unpaid for the years 1974, 1975 and 1976 of \$237,231.97, \$430,788.78 and \$352,313.33, respectively, plus the due and unpaid New York City withholding tax for the Hospital for the year 1976 of \$99,796.01.

2. The periods and amount of the penalty were delineated by the Audit Division as follows:

<u>WITHHOLDING TAX PERIOD</u>	<u>NEW YORK STATE AMOUNT</u>
January 1, 1974 - June 30, 1974	\$ 172,299.04
September 1, 1974 - September 15, 1974	15,990.53
September 16, 1974 - September 30, 1974	16,667.70
December 1, 1974 - December 15, 1974	16,402.52
December 16, 1974 - December 31, 1974	15,872.18
February 16, 1975 - February 28, 1975	18,189.24
March 1, 1975 - March 15, 1975	17,879.90
March 16, 1975 - March 31, 1975	17,128.38
April 1, 1975 - April 15, 1975	17,620.61

¹ The stipulation of facts which petitioners prepared for purposes of this hearing included thirty-eight separately numbered paragraphs. The Audit Division agreed to all of such paragraphs except for paragraphs one, two, three, the fifth sentence of four, ten, fifteen, seventeen, the last sentence of nineteen, twenty, twenty-one, twenty-two, twenty-three and twenty-seven.

² The Hospital was formerly known as the Knickerbocker Hospital. In February of 1974, it became the Arthur C. Logan Memorial Hospital.

<u>WITHHOLDING TAX PERIOD</u>	<u>NEW YORK STATE AMOUNT</u>
May 1, 1975 - May 15, 1975	24,826.24
May 16, 1975 - May 31, 1975	18,470.95
June 1, 1975 - June 15, 1975	18,905.45
June 16, 1975 - June 30, 1975	18,978.44
July 1, 1975 - July 15, 1975	18,564.91
July 16, 1975 - July 31, 1975	20,880.17
August 1, 1975 - August 15, 1975	32,239.59
August 16, 1975 - August 31, 1975	21,010.70
September 1, 1975 - September 15, 1975	21,410.26
September 16, 1975 - September 30, 1975	20,546.09
October 1, 1975 - October 15, 1975	20,357.30
October 16, 1975 - October 31, 1975	28,051.00
November 1, 1975 - November 15, 1975	18,810.12
November 16, 1975 - November 30, 1975	17,882.75
December 1, 1975 - December 15, 1975	19,675.99
December 16, 1975 - December 31, 1975	20,560.29
October 1, 1975 - December 31, 1975 ³	18,300.40
January 1, 1976 - January 15, 1976	19,857.58
January 16, 1976 - January 31, 1976	32,775.06
February 1, 1976 - February 15, 1976	20,647.06
February 16, 1976 - February 29, 1976	20,508.44
March 1, 1976 - March 15, 1976	20,419.91
March 16, 1976 - March 31, 1976	19,998.85
April 1, 1976 - April 15, 1976	19,429.27
April 16, 1976 - April 30, 1976	27,517.77
May 16, 1976 - May 31, 1976	19,104.97
June 1, 1976 - June 15, 1976	20,481.09
June 16, 1976 - June 30, 1976	19,988.60
July 16, 1976 - July 31, 1976	29,449.78
August 1, 1976 - August 15, 1976	19,396.63
August 16, 1976 - August 31, 1976	19,070.36
September 16, 1976 - September 30, 1976	24,756.24
October 1, 1976 - October 15, 1976	18,911.72
	<u>\$1,020,334.08</u>
	<u>NEW YORK CITY AMOUNT</u>
February 1, 1976 - February 29, 1976	\$ 12,972.79
March 1, 1976 - March 31, 1976	13,818.48
April 1, 1976 - April 30, 1976	16,436.14
May 1, 1976 - May 31, 1976	13,159.32
June 1, 1976 - June 30, 1976	13,892.15
July 1, 1976 - July 31, 1976	16,398.14
August 1, 1976 - August 31, 1976	10,108.01
September 1, 1976 - September 30, 1976	3,010.98
	<u>\$ 99,796.01</u>

³ There is no explanation in the record concerning the separate delineation of this three month period.

3. The hospital was a non-profit voluntary hospital located at 130th Street and Convent Avenue in Harlem, New York City. The hospital, which was over one hundred years old, during the years at issue served a poor black community. It had 214 beds and operated at a patient occupancy level of approximately eighty-five to ninety percent of capacity. Approximately fifty percent of the hospital's revenue consisted of Medicaid (the program of public medical aid for the poor) payments. Thirty-five percent of the revenues consisted of Medicare (the program of public medical aid for the elderly and disabled) payments. The remainder of its revenue was from a variety of sources including Blue Cross, private insurance carriers, worker's compensation, and a contract with New York City to provide mental health services.

4. Petitioner William O. Allen served as the hospital's executive director from the end of 1972 until his resignation in February, 1978. He was the assistant director of the hospital for support services prior to his tenure as executive director. He testified that during the years at issue, his salary was approximately forty-five to fifty thousand dollars. However, at the time of his resignation in 1978, his salary was approximately sixty thousand dollars. As executive director, William O. Allen was responsible for carrying out policies established by the board of trustees. He testified that from February, 1976 to the end of the period at issue, the chairman of the board of trustees, Reverend M. L. Wilson, required him to provide the hospital's bank balance and a listing of outstanding bills on a daily basis. (Prior to February, 1976, such information was provided on a weekly basis.) Reverend Wilson reviewed this information and determined which parties should be paid.

William O. Allen had authority to sign checks up to three thousand dollars and he signed payroll checks. However, checks in excess of three

thousand dollars required the co-signature of one of the following three members of the board of trustees: Reverend M. L. Wilson, William R. Hudgins or Dr. Alfred Gellhorn. Mr. Allen testified that a check for \$400,000 to the Internal Revenue Service for previously unpaid federal withholding taxes was signed by Reverend Wilson and William Hudgins.

5. Article XI of the hospital's by-laws, which were in effect until April, 1974, detailed the duties and authority of the executive director. Pursuant to the by-laws, the executive director had the power to hire and fire all hospital employees, was responsible for the purchase of all hospital supplies, was required to keep accurate accounts of all moneys and was required to ensure "that the regulations of the Health Department and other public authorities, affecting the operation and management of this Institution, are immediately complied with." The hospital's by-laws, which were in effect on and after April, 1974, note the authority and responsibility of the executive director in much greater detail and also appear to expand his authority and responsibility. Pursuant to such by-laws, the executive director's additional responsibility and authority included the requirement that he advise the board of trustees on the formation of policies and also serve on the board of trustees with voting power.⁴ In addition, the new by-laws note that the executive director is the duly authorized representative of the hospital "in all matters which the Board has not formally

⁴ Petitioner Allen testified that he did not have voting power. In the minutes of board of trustees meetings, he is listed (with petitioner George Pugh) under a heading "Administration." He is not listed under the heading "For the Board of Trustees." However, the minutes for a meeting of the executive committee of the board of trustees on June 26, 1973 show that he seconded a motion concerning hospital house staff appointments and seconded a motion approving the resignation of Dr. Howard S. Dunbar. In addition, the minutes for the board of trustees meeting on April 22, 1975 show that Allen was elected an officer of the board as assistant secretary.

delegated to other persons." Furthermore, the by-laws provide that the executive director's decision as to the interpretation of the hospital's by-laws or his decision in cases of disputed authority "shall govern unless the Board shall determine otherwise."

6. In practice, petitioner Allen did not have exclusive authority to hire and fire hospital personnel. Appointments of hospital staff doctors were overseen by the hospital's medical board. The president of the medical board, who was a member of the board of trustees, would present to the board of trustees for final review the names of all of the doctors who satisfied the credentials committee of the medical board. (The hospital had difficulty attracting graduates of American medical schools and most of their staff doctors were foreign born and educated.) Other hospital employees including nurses were interviewed by the various department heads who, in conjunction with the hospital's director of personnel, reviewed the job application and made a determination to hire. In order to be placed on the payroll, petitioner Allen was required to sign a "personnel action" which he testified was merely perfunctory. In matters of firing, petitioner Allen also did not have exclusive authority to fire employees because, pursuant to a grievance procedure required by an agreement with the union representing the hospital's employees (other than doctors), the board of trustees made the final decision to dismiss an employee. It also appears that the board of trustees had the last word on the firing of doctors.

In addition, in practice, William O. Allen obtained approval or authority from the board of trustees to act on its behalf in matters of consequence. For example, the minutes of the executive committee of the board of trustees shows that Mr. Allen requested that the board of trustees "re-affirm his authority

to act independently without further confirmation (to close the hospital if the union representing hospital employees rejected the hospital's last proposal concerning a retroactive pay increase)...." His negotiations with the Internal Revenue Service concerning the payment of past-due withholding taxes were conducted pursuant to a resolution adopted by the board of trustees authorizing him to conduct such negotiations.

7. Petitioner George E. Pugh was employed by the hospital from December 11, 1973 through April 7, 1978. Mr. Pugh is a certified public accountant, has an M.B.A. and is a member of the New York State bar. He initially served as comptroller of the hospital until early 1975 when he became the assistant director of finance. He described his duties as encompassing "the general record keeping functions, billing, checks, securing of the revenues, filing of the various reports required by the various governmental agencies...." When he was comptroller, he oversaw the preparation of financial statements. In his capacity as assistant director of finance, he spent time trying to maximize reimbursements from Medicaid and Medicare and to develop sources of new revenue. He had no authority to sign checks. Petitioner George E. Pugh was not an officer or member of the hospital's board of trustees in any capacity.

8. Neither petitioner Allen nor petitioner Pugh signed tax returns, including withholding tax returns. New York withholding tax returns were signed by Ewan Dawes and Solomon Hoff, hospital staff accountants. However, William O. Allen signed a waiver extending the period of limitations to assess unpaid federal withholding taxes. According to the minutes of a special meeting of the board of trustees on May 29, 1974, "Mr. Allen asked for advice from the Board as to whether or not he should sign the IRS waiver or whether

someone else should sign. This matter was resolved in the affirmative in 'Executive Session'."

9. The hospital's board of trustees, which met monthly, consisted of ten to twelve members during the period at issue. Under the hospital's charter and by-laws, it managed the operations, affairs and property of the hospital. Some of the board members were prominent politicians and leaders including Robert F. Wagner, Bayard Rustin and Ramsey Clark. However, a review of the minutes of board meetings which are part of the record herein shows that only five to nine board members attended board meetings. In addition, the meetings were usually dominated by the chairman of the board, Rev. M. L. Wilson.

It appears that immediately prior⁵ to the period at issue, the executive committee of the board of trustees (which included Rev. M. L. Wilson, Dr. Michael A. Diana, Mr. William R. Hudgins and Dr. Robert E. Marshak) and not the entire board of trustees met to consider appointments and resignations of medical personnel and to discuss the hospital's finances in detail. The minutes for a meeting of the board of trustees on January 22, 1974 show that the former functions of the executive committee were apparently assumed by the entire board. In addition, at the meetings of the entire board of trustees, the acts and proceedings of officers and committees were ratified and approved.

10. Petitioners argue that the members of the board of trustees were the persons responsible for the payment of withholding taxes. William O. Allen's position is that he was merely an employee of the board carrying out their policy to keep the hospital in operation. However, see Finding of Fact "5", supra, where it was found that petitioner William O. Allen was an officer and member of the board of trustees.

⁵ For example, the minutes for meetings of the executive committee of the board of trustees for May 22, 1973 and June 26, 1973 show detailed discussions of hospital finances and the approval of medical staff appointments.

At a meeting of the finance committee of the board of trustees on June 18, 1974, Dr. Michael A. Diana noted that if the Internal Revenue Service did not forbear on the collection of unpaid withholding taxes, the hospital would close and the trustees would "seriously face the prospect of personal liability for unpaid withholding taxes." At the same meeting, Rev. M. L. Wilson noted that "(T)he corporate by-laws clearly spelled out the responsibility and non-delegability of the Board of Trustees' responsibility in fiscal matters...." In addition, the minutes of a "Special Regular Board of Trustees Meeting" on March 30, 1978, attended by members of the board, Rev. M. L. Wilson, Dr. Wyatt Tee Walker, Ramsey Clark, William Hudgins, Rose Morgan and Bayard Rustin, note that "It was agreed that all members of the Board past and present should be equally and collectively responsible (for unpaid federal withholding taxes)."

William O. Allen testified that the chairman of the board of trustees, Rev. M. L. Wilson, told him on several occasions that he could not be personally liable for unpaid withholding taxes because he was the board's employee. However, Rev. M. L. Wilson did not testify at the hearing held herein.

11. At the April 16, 1974 meeting of the board of trustees, Eliot H. Lumbard, a member of the board, criticized the payment of \$400,000 (which represented retroactive Medicare funds received by the Hospital) to the Internal Revenue Service for previously unpaid federal withholding taxes. According to the minutes of this meeting, "In his (Lumbard's) opinion, he stated the proper course would have been to take the money, invest it at interest, and 'negotiate' with creditors...." The minutes describe Mr. Allen's response as follows:

"Mr. Allen responded that this (the payment of the \$400,000) was done under his authority as Executive Director who was charged with the duty by the full Board of administering the affairs, including

fiscal, of the hospital. Mr. Allen further referred to the resolution⁶ of the full Board authorizing him to take whatever action he deemed necessary while the fiscal crisis continued in existence."

Mr. Allen also described his authority in broad terms in a letter dated February 11, 1976, Exhibit "N" herein, to George Pugh:

"I have relieved you of the day to day operations of the Accounting Department... Effective this date I assume responsibility for determining the allocations of cash to be disbursed. Do not in any way interfere with decisions that I have made and conveyed to Mr. Bridgett, Controller."

12. At the board of trustees meeting on March 26, 1974, Rev. M. L. Wilson appointed a special study committee on hospital financial matters. Members of the board of trustees serving on this committee were Eliot Lumbard, Mrs. Louise Gimbel (of the Gimbel's department store family), Dr. Edgar Draper and Dr. Robert Polk. At the first meeting of the study committee, Mr. Lumbard, who emerged as the spokesman for the study committee, asked petitioner Pugh why the hospital was continuing to operate with an increasing deficit. Mr. Pugh's response was to analyze the hospital's liabilities. He also pointed out that the hospital had "been operating on the government's money (withholding taxes that were not paid over to the Internal Revenue Service and New York State/City)." Mr. Lumbard asked about "the status of the liability insurance covering Trustees and officers of the hospital⁷." Mr. Pugh then pointed out that "(I)n his opinion, under the present reimbursement policies, limitations imposed by our outmoded physical facility, our patient clientel (sic), and with a notable lack in

⁶ It appears, based upon a review of the minutes for the meeting of the finance committee of the board of trustees on June 18, 1974, that the board of trustees adopted a resolution directing William O. Allen, as Executive Director, "to give first priority to payment of taxes and payroll related matters...."

⁷ It appears that Eliot Lumbard resigned from the board of trustees upon his realization that he might be potentially liable for unpaid withholding taxes if he remained on the board.

referral of private patients, he could see no way that a non-deficit operation was possible except through additional funds received through governmental subsidies, private contributions or both." The committee then discussed the proposal to construct a new facility which would combine the hospital and Sydenham Hospital into a five hundred bed facility (the Manhattanville Health Project). Mr. Pugh suggested that the hospital's deficit could be rolled over into the total mortgage loan on the new facility. "Mr. Lumbard expressed doubt as to the correctness of this Statement and conveyed a request to see this in writing." Mr. Pugh noted that the committee's concerns and suggestions "would be transmitted to the Executive Director for any action and follow-up be deemed appropriate."

13. The Hospital's financial difficulties date back to the early 1970's when it was faced with the disallowance of substantial expenses which it incurred in the late 1960's in providing medical services to Medicaid and Medicare patients. According to the testimony of petitioner William O. Allen, "the retroactive cost reimbursement principle" forced the Hospital into the position where it could never meet its bills:

"The (Medicaid and Medicare) revenues would show hundreds of dollars came in but the State would grab off fifty dollars of that hundred dollars before we ever saw it. We may have a revenue on the books of the hundred dollars, but we would only get fifty dollars, and that's the way it went until the date it closed."

14. The State of New York Department of Health determined, pursuant to a reimbursement formula, the amount of Medicaid and Medicare payments payable to the hospital. The formula consisted of a base of two year old data which was adjusted for inflation, pursuant to a trend factor, much like a cost-of-living index. It was further subjected to peer group ceilings and to various penalties. The hospital's "allowable costs" (which were reimbursed by Medicaid and Medicare

payments) were always substantially lower than its actual costs for a number of reasons. First, the hospital was compared with other similarly sized hospitals, its "peer group." The most that the hospital could receive in reimbursement was 110 percent of the peer group average. According to the testimony of William O. Allen, none of the other hospitals in the hospital's peer group were inner-city hospitals serving a poor black community. The hospital was further penalized by a reduction in its reimbursement amounts for the following reasons: (1) its patients were staying longer than their statistical averages and (2) patients were not being discharged to other types of facilities such as skilled nursing homes or acute care hospitals. The hospital treated many homeless or ill-housed people who had no suitable place to go after treatment and, according to William O. Allen, the hospital was "obligated to keep them until there was a place... We kept one woman for six years because the State of New York did not obtain placement for her." In addition, the hospital was legally required to provide emergency medical services regardless of the ability of a patient to pay for such services. Approximately fifteen percent of the hospital's patient load consisted of the working poor who did not qualify for Medicaid and were unable to pay for medical services. To compound the difficulty of a reimbursement rate which did not meet its actual costs of providing services to Medicaid and Medicare patients, in 1974 and 1975, New York State imposed a freeze on raising reimbursement rates.

15. The hospital's dire financial condition was tempered by hopes that some means would be found to pay off or cancel the unpaid withholding taxes. The board thought that it might be possible to obtain a political decision from the office of Governor Nelson Rockefeller to forgive unpaid payroll taxes or that, in the alternative, the Division of Hospital Financing of the New York

State Department of Health might approve reimbursement rates high enough to pay off back taxes. The board's main hope for the survival of the hospital rested upon the approval of its Manhattanville Health Project. In addition to the possibility that the hospital's deficit might be rolled over into the mortgage loan which would finance the construction of the new hospital, the board hoped that a new facility would attract doctors with private practices. In petitioner Pugh's words, "We could not afford not to build the new hospital."

16. On October 26, 1976, the Hospital filed a petition under Chapter XI of the Bankruptcy Act seeking a plan for rehabilitation. It continued in operation until 1978 when it finally closed its doors. The record is unclear when it was finally adjudicated bankrupt and its assets liquidated. A review of the minutes for the meetings of the board of trustees reveals the following deficits⁸ for the Hospital:

<u>Date</u>	<u>Accumulated Deficit</u>	<u>Total Deficit</u>	<u>Total Accumulated Deficit</u>	<u>Aggregate Deficit</u>
April 30, 1973		\$5,329,118		
May 31, 1973		5,507,987		
December 31, 1973	\$6,428,338			
March 31, 1974	6,824,571			
May 31, 1974			\$6,022,767	
August 31, 1974	6,476,118			
October 31, 1974	6,707,782			
August 31, 1975			5,750,240	
August 31, 1976				\$7,701,326

17. The Internal Revenue Service assessed penalties for unpaid withholding taxes of the hospital against each of the petitioners in the approximate amount of \$3 million. The Internal Revenue Service commenced an action against petitioners and others in the United States District Court for the Southern District of New York. The action was dismissed without prejudice after it was determined

⁸ The deficits as noted in the chart, infra, were described in various ways in the minutes. The record is unclear on how such terms vary from one to the other.

that there was no prospect of collection from the petitioners. However, tax liens for three million dollars against petitioners remain outstanding until the statute of limitations on collection expires.

18. Included in petitioners' brief are proposed findings of fact, numbered one through thirty-seven. All are incorporated into and made a part of this decision except for the following:

(1) The last sentence of proposed finding of fact "3" (because the record does not establish that William Allen's authority was limited);

(2) Proposed finding of fact "5" (because William Allen was granted very broad powers and much discretion to act as he determined was necessary);

(3) Proposed finding of fact "6" to the extent that it says that petitioner Allen provided the chairman of the board of trustees, Rev. M. L. Wilson with a report of the hospital's bank statements and a request for disbursements on a daily basis (see Finding of Fact "4", supra);

(4) The last sentence of proposed finding of fact "7" (because, as a member of the board of trustees, petitioner Allen participated in hiring decisions);

(5) The last sentence of proposed finding of fact "8" (because as a member of the board of trustees, petitioner Allen would have participated in such decisions);

(6) Proposed finding of fact "11" (because petitioner Pugh was comptroller of the hospital from April, 1973 until early 1975);

(7) The last sentence of proposed finding of fact "22" (because the record does not establish such fact); and

(8) Proposed finding of fact "28" to the extent that it says "members" of the board of trustees criticized Allen and Pugh (because the record shows that only trustee Eliot Lumbard was critical with regard to the payment of \$400,000 to the Internal Revenue Service).

CONCLUSIONS OF LAW

A. That, pursuant to Tax Law §685(g),⁹ any "person" required to collect, truthfully account for and pay over withholding taxes, who willfully fails to do so, can be subjected to a penalty equaling the amount of the tax. "Person" for purposes of this section includes "any officer or employee of any corporation ...who as such officer, employee...is under a duty to perform the act in respect of which the violation occurs." Tax Law §685(n).

B. That petitioner George E. Pugh was not a member of the hospital's board of trustees, the governing body of the hospital. In addition, as noted in Finding of Fact "7", supra, his authority and responsibilities were circumscribed. Therefore, it is concluded that petitioner George E. Pugh was not a person responsible for the collection and payment over of withholding taxes due from the hospital.

C. That petitioner William O. Allen was a voting member of the hospital's board of trustees. In addition, as noted in Findings of Fact "5" and "11", the board of trustees delegated significant authority and discretion to petitioner William O. Allen concerning the operation of the hospital. Although petitioner William O. Allen did not have exclusive authority concerning the operation of the hospital and also obtained approval or ratification of his actions from the board of trustees, he was influential in the affairs of the hospital, both in

⁹ Tax Law §1312 provides that any tax imposed pursuant to Article 30 "shall be administered and collected by the State Tax Commission in the same manner as the tax imposed by article twenty-two...."

the capacity as a board member and as executive director, and was a responsible person for purposes of Tax Law §685(g). See Cooper v. United States, 539 F. Supp. 117.

D. That in order to conclude that petitioner William O. Allen may be saddled with personal liability under Tax Law §685(g) for unpaid withholding taxes, we must also determine that he willfully failed to collect and pay over withholding taxes of the hospital.

E. That the failure to collect and pay over withholding taxes is willful if such failure 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. Matter of Levin v. Gallman, 42 N.Y.2d 32.

Petitioner George E. Pugh was correct, when he noted at the first meeting of the hospital's special study committee on hospital financial matters, that the hospital had "been operating on the government's money (withholding taxes that were not paid over to the Internal Revenue Service and New York State/City)." Although such money was used for the worthy purpose of keeping the doors of a hospital in a poor, black community open, nonetheless the trust funds belonged to the government and should have been paid over to the government. Therefore, petitioner William O. Allen, as an active member of the board of trustees and executive director of the hospital, participated in the decision to keep the hospital open and therefore he "willfully" failed to collect and pay over the withholding taxes at issue.

F. That there is no basis in law or regulations to relieve petitioner William O. Allen of personal liability for the unpaid withholding taxes because New York State/City did not offset the taxes due and owing against the hospital's Medicaid reimbursement funds. Furthermore, the Audit Division was not required

to attempt to collect the taxes from the corporation before asserting potential liability against a responsible officer.

G. That the Audit Division was not required to take steps against all persons who might have personal liability for unpaid withholding taxes. See Burack v. U.S., 72-2 USTC ¶9490.

H. That an amendment to Tax Law §685(g) was added effective February 25, 1976 authorizing the State Tax Commission "in its discretion, to waive, reduce or compromise any penalty under this subsection." An examination of the legislative bill jacket for the Laws of 1976, Chapter 6, which codified this amendment, reveals that the intent behind the legislation was to provide the State Tax Commission with statutory authority to abate the withholding tax penalty against responsible officers if the full tax due and owing has been collected once (which previously had been administrative policy). Therefore, this discretionary authority is not applicable herein.

I. That the petition of George E. Pugh is granted.

J. That the petition of William O. Allen is denied.

DATED: Albany, New York

STATE TAX COMMISSION

MAR 01 1985


PRESIDENT


COMMISSIONER


COMMISSIONER