

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition :
of :
KWANG YOUNG CHO : DETERMINATION
for Redetermination of Deficiencies or for Refund : DTA NO. 826088
of Personal Income Tax under Article 22 of the
Tax Law and the New York City Administrative
Code for the Period January 1, 2006 through :
December 31, 2008. :
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Petitioner, Kwang Young Cho, filed a petition for redetermination of deficiencies or for refund of personal income tax under Article 22 of the Tax Law and the New York City Administrative Code for the period January 1, 2006 through December 31, 2008.

A hearing was held before Joseph W. Pinto, Jr., Administrative Law Judge, at the offices of the Division of Tax Appeals in New York, New York, on February 9, 2015 at 10:30 A.M., with all briefs to be submitted by August 7, 2015, which date commenced the six-month period for issuance of this determination. Petitioner appeared by Edmund J. Mendrala, Esq. The Division of Taxation appeared by Amanda Hiller, Esq. (Peter B. Ostwald, Esq., of counsel).

ISSUE

Whether Kwang Young Cho was a person responsible for the collection and payment of employee withholding taxes on behalf of Fine Carpenters Group, Inc., for the period January 1, 2006 through December 31, 2008.

FINDINGS OF FACT

1. During the period January 1, 2006 through December 31, 2008 (audit period), Fine Carpenters Group, Inc. (FCG) was a company engaged in interior design, construction and renovation located at 15 East 32nd Street, in New York City.

2. Petitioner was the company's president and 90 percent shareholder. He was a highly skilled carpenter whose day-to-day responsibilities included managing job sites and over 20 employees.

3. Petitioner was authorized to sign checks on behalf FCG. He and FCG secretary, Joongoo Kang, signed the application for the business checking account with Shinhan Bank America in April 2006. Only petitioner signed the corporate authorization resolution, which represented that FCG's board of directors authorized him and Mr. Kang to open corporate accounts, endorse checks, withdraw funds, borrow money, execute promissory notes, and pledge security on behalf of FCG.

4. Petitioner was the sole incorporator for FCG and his signature appears on the certificate of incorporation, which was filed in the office of the New York State Department of State on May 3, 2005. Petitioner signed the certificate of assumed name on behalf of FCG, which also was filed with the New York State Department of State, on April 25, 2006.

5. Petitioner was listed as the principal officer of FCG on its application for a federal employer identification number. He signed the tax form NYS-100, New York State Employer Registration for Unemployment Insurance, Withholding, and Wage Reporting, dated September 1, 2006, indicating his official position with FCG as president. Petitioner signed New York corporation franchise tax returns for 2006 and 2007. No New York franchise tax return was filed

for 2008. In addition, he signed forms NYS-45-MN, quarterly combined withholding, wage reporting and unemployment insurance returns; and forms NYS-1, returns of tax withheld.

6. Petitioner received compensation from FCG during the audit period.

7. The Internal Revenue Service (IRS) conducted an examination of the payroll tax returns of FCG and determined that additional tax was due. The IRS discovered that FCG cashed the checks it received from clients and, in turn, paid its employees in cash, failing to withhold any taxes or issue any W-2s or 1099s. The federal changes were reported to New York State and withholding tax adjustments were made for the years 2006, 2007 and 2008. The IRS assessed FCG and Hyo Sung Kim, the 10 percent owner, for the taxes determined to be due to the IRS.

8. Mr. Kim, on behalf of FCG, and the IRS executed an agreement on or about October 27, 2010, accepting liability for the assessment and collection of the additional tax due. The agreement bound FCG to pay additional withholding taxes to the IRS in the sum of \$834,393.62. There was no explanation why only Mr. Kim and FCG were bound by the agreement or why Mr. Kim represented himself as president of FCG.

9. Acting on a referral of this information from the IRS, the Division issued a withholding tax field audit adjustment for the audit period, which asserted additional tax of \$353,440.00 plus penalty of \$186,555.00 and interest of \$161,256.00 for a total due of \$701,251.00. Mr. Kim, acting as an authorized person for the corporation, executed a consent to the assessment and collection of the amounts stated, dated February 5, 2012.

In addition, the Division made a request for records from both the company and petitioner, but was told by their accountant, Bryan Ban, that the company had gone out of business and destroyed its records. The Division continued its efforts to get information about the persons responsible for the payment of the withholding taxes, subpoenaing records from Shinhan Bank

America and examining returns and applications filed by FCG. Based on all the information it received, it determined that petitioner was a person responsible for the tax on behalf of FCG

10. During the Division's audit of FCG, it discovered that petitioner had been one of two signatories on FCG's bank account, held the office of president, and performed other duties consistent with a person who was responsible for the collection and payment of taxes on behalf of the company, discussed in detail above. As a result, it issued to petitioner six notices of deficiency, dated March 13, 2013, for the following:

Period Ended	Jurisdiction	Notice Number	Penalty	Total
12/31/2006	State	L-039131145	\$99,496.00	
12/31/2006	City	L-039131142	\$54,157.00	
12/31/2007	State	L-039131144	\$58,222.00	
12/31/2007	City	L-039131146	\$31,695.00	
12/31/2008	State	L-039131143	\$71,143.00	
12/31/2008	City	L-039131147	\$38,727.00	
				<u>\$353,440.00</u>

11. Mr. Kim had operated in real estate prior to his involvement with FCG, and had experience in developing properties. He was presented with an opportunity to build storefronts and showrooms for the design industry. He was keenly aware of the value of skilled craftsmen, and, based on his observation of petitioner's work, he believed that he would need to make certain promises to petitioner to ensure a lasting relationship for this new business endeavor. This was partly due to a cultural custom that would bolster petitioner's self worth and value to the company.

12. Mr. Kim proposed that a new corporation be formed in which petitioner would be the majority shareholder and hold the office of president. The agreement between the two was not

memorialized in writing, but based on good faith. In fact, petitioner held a 90 percent ownership interest in the company and Mr. Kim 10 percent. As mentioned, petitioner incorporated the company in June 2005 and became one of two signatories on FCG's bank account. Mr. Kim was not a signatory on that account. It was Mr. Kang, the office administrator and secretary of the corporation, who was the second signatory on that account.

13. Mr. Kang operated FCG's office at 15 East 32nd Street, performing accounting and bookkeeping functions, procuring merchandise and supervising other employees. He saw petitioner at the office on occasion, when petitioner would stop in to pick up architectural drawings. Although Mr. Kang was a signatory on FCG's bank account, he would only issue checks with Mr. Kim's authorization. Mr. Kim would tell Mr. Kang what to pay and whose name he wanted as the signatory, sometimes telling him to write Mr. Kang's name, sometimes petitioner's name. Mr. Kim directed Mr. Kang whose name he wanted on tax returns as well, particularly the form NYS-45-MN, quarterly combined withholding, wage reporting and unemployment insurance returns, where he directed Mr. Kang to sign his name, petitioner's name and even Mr. Kim's own name. Mr. Kang also observed petitioner signing checks and tax returns as well.

14. Mr. Kim and petitioner had a professional relationship that spanned over 20 years. Petitioner's skilled craftsmanship made him a very desirable employee to a company that was well known in the design and fashion industry. Both Mr. Kim and petitioner were known for their ability to deliver a high-end, quality product.

15. Petitioner made no cash contribution to capitalize FCG, while Mr. Kim estimated he contributed approximately \$100,000.00.

SUMMARY OF THE PARTIES' POSITIONS

16. Petitioner contends that the holding of corporate office alone does not automatically impose liability on an officer. Petitioner believes he did not have authority and control over the financial affairs of FCG and that all financial decisions were made by Mr. Kim. Petitioner argues that he was directed by Mr. Kim to sign tax returns and checks.

17. Petitioner points out that he managed laborers at construction sites and had no administrative duties or authority.

18. Petitioner noted that Mr. Kim, and not he, was held responsible for the federal withholding taxes, only Mr. Kim. He also noted that Mr. Kim paid personal expenses through the company accounts, indicating that he was the true owner of the company.

19. The Division contends that petitioner has not met his burden of proving that he was not a person responsible for the payment of the withholding taxes for FCG. It argues that petitioner is in error when he argues that the Division is bound by the federal determination. The Division notes that it is free to reexamine the evidence and make an independent determination of tax liability. In this matter, the Division requested records but was told that FCG had gone out of business and destroyed its records, forcing the Division to subpoena bank records and review other documentation and public filings.

20. The Division notes all of petitioner's powers with respect to FCG and his exercise of those powers, including check signing authority, signing tax returns, supervising workers on site and performance of all the tasks necessary to set up the corporation. Further, the Division argues that petitioner was not precluded from taking action in furtherance of his fiduciary duties to FCG.

21. The Division believes that petitioner has failed to meet his burden of showing that he did not willfully fail to collect and pay the withholding taxes due.

CONCLUSIONS OF LAW

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

“Willful failure to collect and pay over tax.--Any person required to collect, truthfully account for, and pay over the tax imposed by this article who willfully fails to collect such tax or truthfully account for and pay over such tax or willfully attempts in any manner to evade or defeat the tax or the payment thereof, shall, in addition to other penalties provided by law, be liable to a penalty equal to the sum of [i] the total amount of the tax evaded, or not collected, or not accounted for and paid over”

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

“For purposes of subsections [g], [i], [o], [q] and [r], the term person includes an individual, corporation or partnership or limited liability company or an officer or employee of any corporation [including a dissolved corporation], or a member or employee of any partnership, or a member, manager or employee of a limited liability company, who as such officer, employee, manager or member is under a duty to perform the act in respect of which the violation occurs.”

C. The question of whether someone is a “person” under a duty to collect and pay over withholding taxes is a factual one. Factors to be considered include whether the individual had the authority to sign tax returns and did so, derived a substantial part of his income from the business, or had the right to hire and fire employees (*Matter of Malkin v. Tully*, 65 AD2d 228 [3d Dept 1978]). Other pertinent areas of inquiry include the person’s official duties, his authority to pay obligations of the business, and his financial interest in the business (*Matter of Amengual v. State Tax Commn.*, 95 AD2d 949 [3d Dept 1983]; *Matter of McHugh v. State Tax Commn.*, 70 AD2d 987 [3d Dept 1979]; *Matter of Shah*, Tax Appeals Tribunal, February 25, 1999). The issue to be resolved is whether petitioner had, or could have had, sufficient authority and control over the affairs of the business to be considered a person under a duty to

collect and remit the unpaid taxes in question (*Matter of Constantino*, Tax Appeals Tribunal, September 27, 1990; *Matter of Chin*, Tax Appeals Tribunal, December 20, 1990).

D. In addition, if petitioner is held to be a person under a duty as described, it must then be decided whether his failure to withhold and pay over such taxes was willful. The question of willfulness is related directly to the question of whether petitioner was a person under a duty, since clearly a person under a duty to collect and pay over the taxes is the one who can consciously and voluntarily decide not to do so. However, merely because one is determined to be a person under a duty, it does not automatically follow that a failure to withhold and pay over income taxes is “willful” within the meaning of that term as used in Tax Law § 685(g). As the Court of Appeals indicated in *Matter of Levin v. Gallman* (42 NY2d 32 [1977]), the test is:

“whether the act, default, or conduct is consciously and voluntarily done with knowledge that as a result, trust funds belonging to the Government will not be paid over but will be used for other purposes No showing of intent to deprive the Government of its money is necessary but only something more than accidental non-payment is required” (*id.*, 396 NYS2d at 624-625; *see, Matter of Lyon*, Tax Appeals Tribunal, June 3, 1988).

The failure to pay over taxes can be willful notwithstanding the lack of actual knowledge, if the person recklessly disregarded his responsibilities, including the responsibility to see that employment taxes are paid (*Matter of Capoccia v. State Tax Commn.*, 105 AD2d 528 [3d Dept 1984]). Finally, “corporate officials responsible as fiduciaries for tax revenues cannot absolve themselves merely by disregarding their duty and leaving it to someone else to discharge” (*Matter of Risoli v. Commr.*, 237 AD2d 675 [3d Dept 1997]).

E. Upon review of the entire record, it is clear that petitioner was properly held responsible for the withholding tax obligations of FCG for the period in issue. In order to prevail in this case, petitioner was required to establish by clear and convincing evidence that he was not

under a duty to act on behalf of FCG, i.e., that he lacked the necessary authority, or he had the necessary authority but he was thwarted by others in carrying out his duties (*Matter of Goodfriend*, Tax Appeals Tribunal, January 15, 1998). Neither of these circumstances accurately describes the facts of this case.

Petitioner was the president and 90 percent owner of the corporation - - a corporation he formed as the incorporator, signed the certificate of incorporation and certificate of assumed name on behalf of FCG and filed them with the New York State Department of State. As president of the corporation, petitioner was listed as the principal officer of FCG on its application for a federal employer identification number, signed tax form NYS-100, signed the New York State employer registration for unemployment insurance, withholding, and wage reporting, signed New York corporation franchise tax returns for 2006 and 2007, signed forms NYS-45-MN, quarterly combined withholding, wage reporting and unemployment insurance returns and signed a form NYS-1, return of tax withheld.

In addition, petitioner worked long days for FCG, managed 20 or more laborers at his work sites and received compensation from the corporation.

Petitioner and Mr. Kim developed the idea of creating FCG to meet the high end construction needs of the fashion industry. Mr. Kim was well known in the industry as a businessman with the ability to undertake and complete construction projects with high quality results. Petitioner, also well known in the industry, was a craftsman with the skills necessary to guarantee the quality of the projects and see them to completion. Given their long relationship and knowledge of each other's skills and abilities, joining together in this new venture was a natural progression.

However, what is evident is that neither petitioner nor Mr. Kim respected the legal existence of the corporation, FCG, and operated their business without regard for titles, bank authorizations or representations to the public that appear on numerous filings. Names were signed to tax returns and checks without any proper authority and petitioner, while imbued with authority to perform all financial functions of the corporation, including paying the withholding taxes, chose to rely on others to do so without ever checking to see that taxes were paid or returns filed. While glad to accept the 90 percent ownership in and presidency of the corporation, he then chose to ignore all responsibilities pertaining thereto.

Petitioner's argument that he did not exercise control over FCG's financial matters is without merit. Petitioner was able to control FCG through his ownership of 90% of the outstanding shares of the company. He was FCG's president, with the authority to hire and fire employees, regardless of whether he ever exercised that power. The fact that he held 90% of the stock meant he had control of the board of directors and the ability to appoint officers of the corporation. As indicated above, he signed many legal documents, tax returns and checks on behalf of the corporation. Petitioner had the ability to control the financial and business affairs of the company, but chose to delegate that responsibility, including his duty to collect, truthfully account for and pay over withholding taxes. The only question remaining is whether his failure to do so was willful. Petitioner's central argument is that he was a skilled carpenter who managed laborers at work sites and only held stock and an officer's title as an indicator of his value to the enterprise. He pleads ignorance of the business operations and claims he left all responsibility for the business operations, including the filing of corporate returns and payment of its tax liabilities, to Mr. Kim.

F. It is true, as petitioner argues, that the mere holding of a corporate office does not indicate a responsibility for the payment of tax and filing of returns (*Matter of Chevlowe v. Koerner*, 95 Misc2d 388 [Sup Ct Queens County 1978]). However, as a 90% shareholder of FCG and its president, he had a fiduciary responsibility to ensure that withholding taxes were paid, regardless of whether he chose to have a third party fulfill the obligation for him (*Matter of Risoli* [where the court stated that an officer with broad oversight authority with respect to the management of the corporation was a responsible person within the meaning of the Tax Law notwithstanding his failure to exercise that authority, and that delegation of the responsibility to pay the tax to other corporate shareholders cannot absolve a corporate fiduciary merely by disregarding their duty and leaving it to someone else to discharge]).

Petitioner and Mr. Kim created a corporation that employed 20 to 30 people during the audit period, yet as fiduciaries they recklessly disregarded their responsibility to pay withholding taxes, choosing instead to cash checks from clients and pay the employees in cash, off the books. They used the corporate structure when it was to their advantage to do so, but otherwise disregarded it. However, despite the confusion, the record demonstrates that petitioner was under a duty to act for the FCG within the meaning of Tax Law § 685(n) during the audit period.

It is also clear that petitioner's actions were willful as defined in Tax Law § 685(g). As a person charged with the duty to pay the tax, he was obligated to do more than just delegate that responsibility to someone else (*Matter of Risoli*). His acceptance of a 90% ownership share of the company and the title of president with authority over the checking account that he exercised, made his disregard for payment of withholding taxes reckless and resulted in "more than accidental nonpayment" (*Matter of Capoccia*).

G. The burden was upon petitioner to establish that he was not a responsible person pursuant to Tax Law § 685(n) who wilfully failed to collect and pay the withholding taxes on behalf of FCG. (Tax Law § 689[e]; *Matter of Goodman*, Tax Appeals Tribunal, November 15, 2007.)

The evidence indicates that petitioner never inquired into the state of the corporation's books and records during the audit period, and, instead, simply allowed Mr. Kim to manage the operation of the business as he pleased. Petitioner "assumed" the business was run properly. A responsible officer's failure can be willful, notwithstanding his lack of actual knowledge, where it is determined the officer recklessly disregarded his corporate responsibilities including the responsibility to see that taxes were paid (*Matter of Cappoccia; Matter of Ragonesi v. New York State Tax Commn.*, 88 AD2d 707 [3d Dept 1982]). Under these facts, petitioner's delegation of all management of the business to Mr. Kim without any involvement or oversight on his part as 90% owner of the company and its president, constitutes a reckless disregard of his corporate responsibility, and was willful within the meaning of Tax Law § 685(g) (*Matter of Oehler*, Tax Appeals Tribunal, July 10, 2003, *Matter of Flax*, Tax Appeals Tribunal, September 9, 1988). Petitioner has failed to carry his burden of proof pursuant to Tax Law § 685(e).

H. The petition of Kwang Young Cho is denied and the six notices of deficiency, dated March 13, 2013, are sustained.

DATED: Albany, New York
January 28, 2016

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