

**HONORARY BOARD MEMBERSHIP, REAL TAX  
LIABILITY: LIMITS TO TAX-EXEMPT ORGANIZATION  
HONORARY BOARD MEMBER IMMUNITY UNDER  
INTERNAL REVENUE CODE § 6672**

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“Speak to me of honour, and of duty, and of nobility; and tell me what they require of you.”<sup>1</sup>

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1. ANTHONY TROLLOPE, THE DUKE’S CHILDREN 485 (Hermione Lee ed., Oxford Univ. Press 1991) (1880).

## I. INTRODUCTION

Well over half of the Internal Revenue Service's (IRS's) total revenue collections are taxes withheld from by employers from their employees' wages and salaries.<sup>2</sup> To ensure actual collection by the government of the withheld taxes, the Internal Revenue Code<sup>3</sup> imposes personal liability upon the individuals responsible for withholding and paying over the taxes.<sup>4</sup> The withheld monies are commonly known as "trust funds."<sup>5</sup> In 1996, as part of the Taxpayer Bill of Rights 2 (hereinafter referred to as "TBOR2"), Congress provided a safe harbor to protect honorary board members of charitable organizations<sup>6</sup> from liability for trust funds.<sup>7</sup>

2. See INTERNAL REVENUE SERVICE, INTERNAL REVENUE SERVICE DATA BOOK 11 tbl. 5 (2007), <http://www.irs.gov/pub/irs-soi/07databk.pdf>.

3. Unless otherwise indicated, all section references in this Article are to the Internal Revenue Code (I.R.C.) of 1986, as amended. The Tax Reform Act of 1986, Pub. L. 99-514, 100 Stat. 2085 (1986), redesignated the Internal Revenue Code of 1954 as the Internal Revenue Code of 1986 and provided that, except where inappropriate, official reference to one shall entail reference to the other.

The Internal Revenue Code is codified at Title 26 of the United States Code. The widely used and accepted convention among tax practitioners and courts to cite the Internal Revenue Code as "I.R.C." instead of "26 U.S.C." will be utilized in this article. See also Terry S. Jones, *Estate of Bonner v. United States: QTIPS and Fractional Interest Discounts: Whipsaw Wonderland*, 33 IDAHO L. REV. 595, 595 n.1 (1997). Similarly, regulations issued by the Treasury Department pursuant to the Internal Revenue Code will be cited as "Treas. Reg." instead of "26 C.F.R."

4. See *infra* notes 45-48 and accompanying text.

5. *Slodov v. United States*, 436 U.S. 238, 243 (1978); see also *Fran Corp. v. United States*, 164 F.3d 814, 817 (2d Cir. 1999) ("[T]he taxes an employer withholds from and pays on behalf of its employees are often called 'trust fund taxes.'").

6. For the sake of clarity and brevity, the discussion in this article will use the terms "charitable" and "tax exempt" interchangeably, and the legal distinctions between charitable, religious, educational, and other tax-exempt purposes will be largely ignored, unless specifically indicated otherwise. See, e.g., *Taxation with Representation v. Regan*, 676 F.2d 715, 719 (D.C. Cir. 1982), *rev'd on other grounds sub nom.*, 461 U.S. 540 (1983) ("Section 501(c)(3) organizations-sometimes simply called 'charitable' organizations . . ."). See I.R.C. § 501 for classifications of various types of tax-exempt entities. See also *Taxation with Representation*, 676 F.2d at 718-21.

7. Taxpayer Bill of Rights 2, Pub. L. No. 104-168, § 904(a), 110 Stat. 1452, 1467 (1996) (codified at I.R.C. § 6672(e)).

The new subsection reads:

(e) Exception for voluntary board members of tax-exempt organizations

No penalty shall be imposed by subsection (a) on any unpaid, volunteer member of any board of trustees or directors of an organization exempt from tax under subtitle A if such member-

(1) is solely serving in an honorary capacity,

(2) does not participate in the day-to-day or financial operations of the organization, and

(3) does not have actual knowledge of the failure on which such penalty is imposed.

The preceding sentence shall not apply if it results in no person being liable for the penalty imposed by subsection (a).

Over the past few years, Congress and the Internal Revenue Service (and, for that matter, the state taxation, legislative and law enforcement authorities) have increased their scrutiny over the charities and other tax-exempt entities.<sup>8</sup> The resulting climate change in the charitable sector presents challenges and issues for those who actively involve themselves in charitable works.

This article will discuss the implications of the various governmental trends and initiatives upon the potential trust fund liability of tax-exempt organizations' honorary board members.

## II. BACKGROUND & STATUS OF CHARITABLE ORGANIZATIONS

It has long been the policy of the state and Federal governments to foster and encourage eleemosynary organizations.<sup>9</sup> Indeed, those who fail to voluntarily contribute what is popularly viewed as their fair share to charitable causes are sometimes viewed with suspicion.<sup>10</sup>

Consistent with the law's favored view of charitable and religious causes, policy dictates that donations to organizations having such purposes be facilitated and encouraged through favorable treatment in tax law<sup>11</sup> and other legal areas.<sup>12</sup>

In light of the overall benefits given to society by the charitable and religious organizations, abuses by such organizations of their tax-exempt status were, for a long time, largely tolerated and condoned by the authorities and the public. More recently, however, as abuses of the system have garnered public notoriety, the regulations affecting charitable organizations have multiplied. Over the years, the laws have responded to various public concerns ranging from unfair competition

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*Id.*

8. See *infra* notes 14-38 and accompanying text.

9. See, e.g., *Matter of Kimberly*, 27 A.D. 470, 473 (N.Y. App. Div. 1898); *Bond v. Pittsburgh*, 84 A.2d 328, 330 (Pa. 1951) ("There is no class of institutions more favored and encouraged by our people as a whole than those devoted to religious or charitable causes.").

10. See, e.g., *United States v. Pape*, 253 F. 270 (S.D. Ill. 1918); see also *President's News Conference on Foreign and Domestic Matters*, N.Y. TIMES, Jan. 20, 1982, at A20 (Unofficial transcript of President Ronald Reagan's news conference on January 19, 1982, reporting a question implicitly critical of the President's relatively low levels of charitable giving as shown on his tax return.).

11. See, e.g., *Gardiner v. Hassett*, 63 F. Supp. 853, 856 (D. Mass. 1945); see also Treas. Reg. § 1.170-1(b) (1972) (providing that unconditional mailing of a charitable contribution constitutes completion of the gift, notwithstanding the subsequent postal and payment clearance processes).

12. See, e.g., 11 U.S.C. § 548(a)(2) (2005) (providing exception to bankruptcy trustee's transfer avoidance powers with respect to certain transfers to charitable organizations).

with legitimate taxpaying businesses,<sup>13</sup> to the use of tax-exempt organizations to support subversive political activity.<sup>14</sup> The implication of tax-exempt organizations in insurance and Medicaid fraud schemes has been a problem,<sup>15</sup> as has the complicity of tax-exempt organizations in promoting questionable tax shelter arrangements.<sup>16</sup>

The issue of officials of charitable organizations abusing their trust came to the fore when William Aramony, the CEO of the United Way of America, used United Way monies for his personal chauffeur, and to finance a personal intimate relationship with his paramour.<sup>17</sup> Other high profile incidents involving alleged mismanagement or worse, by nonprofit entities have included Adelphi University's lavish salary and perquisites for its president at a time when the University was cutting back on programs<sup>18</sup> and the compensation and perquisites paid to the trustees of the Bishop Estate in Hawaii.<sup>19</sup> Such incidents by charitable and tax-exempt organizations have attracted the attention of Congress, the IRS, and other regulatory authorities.

In the spring of 2004, the IRS definitively signaled its intention to intensify scrutiny over the affairs of tax-exempt organizations. On April 1, 2004, the IRS issued Notice 2004-30<sup>20</sup> regarding certain types of transactions. According to an accompanying press release, Notice 2004-

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13. See, e.g., H.R. Rep. No. 2319, at 36-37 (1950), reprinted in 1950-2 C.B. 380, 409; S. Rep. No. 2375 (1950), reprinted in 1950 U.S.C.C.A.N. 3053, 3081; *C. F. Mueller Co. v. Comm'r*, 190 F.2d 120 (3d Cir. 1951), rev'g 14 T.C. 922 (1950).

14. See, e.g., *A New Red Inquiry Approved by House: Will Study if Tax-Free Groups Use Their Wealth to Promote Subversion – Protests Fail*, N.Y. TIMES, April 5, 1952, at 5.

15. *United States v. Hendricks*, 69 Fed. App'x 592 (4th Cir. 2003); *Easton v. Public Citizens, Inc.*, 1991 U.S. Dist. LEXIS 18690 (E.D.N.Y. Dec. 23, 1991); *Congregation B'nai Jonah v. Kuriansky*, 172 A.D.2d 35 (N.Y. App. Div. 1991), appeal dismissed, 590 N.E.2d 244 (N.Y. 1992); *Matter of Fuhrer*, 419 N.Y.S.2d 426 (N.Y. 1979), enforced, 72 A.D.2d 813 (N.Y. App. Div. 1979); *St. Francis Home, Inc., v. Ohio Dept. of Job and Family Services*, No. 06AP-287, 2006 Ohio App. LEXIS 6095 (Ohio Ct. App. Nov. 21, 2006), appeal denied, 864 N.E.2d 653 (Ohio 2007).

16. See, e.g., Darryll K. Jones, *When Charity Aids Tax Shelters*, 4 FLA. TAX REV. 769 (2001).

17. See *United States v. Aramony*, 88 F.3d 1369, 1373-74 (4th Cir. 1996), cert. denied, 520 U.S. 1239 (1997); see also *Vacco v. Aramony*, N.Y.L.J., Aug. 7, 1998, at 21 (N.Y. Sup. Ct. 1998).

18. See Bruce Lambert, *New York Regents Oust 18 Trustees from Adelphi U.*, N.Y. TIMES, Feb. 11, 1997, at A1; see also *Vacco v. Diamandopoulos*, 715 N.Y.S.2d 269 (N.Y. Sup. Ct. 1998).

19. See David A. Brennen, *Charities and the Constitution: Evaluating the Role of Constitutional Principles in Determining the Scope of Tax Law's Public Policy Limitation for Charities*, 5 FLA. TAX REV. 779, 796-803 (2002); Todd S. Purdum, *For \$6 Billion Hawaii Legacy, a New Day*, N.Y. TIMES, May 15, 1999, at A1; Lee Gomes, *IRS is Threatening to Revoke Status of Hawaii Estate if Trustees Don't Quit*, WALL ST. J., Apr. 30, 1999, at A16.

20. Notice 2004-30, though actually issued on April 1, 2004, was published in the Internal Revenue Bulletin nearly four weeks later. I.R.S. Notice 2004-30, 2004-1 C.B. 828. The delay was no doubt attributable, at least in part, to the hectic activity at IRS Headquarters in connection with the well-known personal income tax filing deadline of April 15th.

30 was “the first time the IRS has exercised its authority under the tax shelter regulations to specifically designate a tax-exempt party as a ‘participant’ in a tax avoidance transaction.”<sup>21</sup>

On April 7, 2004, IRS Commissioner Mark W. Everson testified before a Senate subcommittee that the IRS “will... discourage and deter non-compliance within tax-exempt and government entities, and the misuse of such entities by third parties for tax avoidance or other unintended purposes.”<sup>22</sup>

Three weeks later, IRS Exempt Organizations Division Director Steven T. Miller indicated that the IRS planned to give increased scrutiny to tax-exempt organizations when he spoke at a Georgetown University Law Center conference on April 29, 2004,<sup>23</sup> a conference at which staff members from the Senate Finance Committee also indicated growing Congressional interest in controlling abuses in connection with the tax-exempt organizations.<sup>24</sup> Miller made similar remarks at a Washington College of Law conference on May 20, 2004.<sup>25</sup> Less than one week later, the IRS announced that Miller would be elevated to Division Commissioner for Tax Exempt and Government Entities, effective June 1, 2004,<sup>26</sup> hardly a repudiation by Mr. Miller’s employer of the statements Mr. Miller uttered.<sup>27</sup>

All of these events within a two-month period proved to be the start of an IRS initiative, which has continued unabated.<sup>28</sup>

Congress has likewise taken an increasingly broad interest in tax-exempt organizations.<sup>29</sup> Specific Congressional attention has spotlighted

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21. I.R.S. News Release IR-2004-44 (Apr. 1, 2004), <http://www.irs.gov/newsroom/article/0,,id=122440,00.html>

22. *Transportation, Treasury and General Government Subcommittee Hearing on Tax Law Enforcement and Information Technology Challenges at the Internal Revenue Service*, 108th Cong. (2004) (written statement of Mark W. Everson, Commissioner, Internal Revenue Serv.), available at <http://web.archive.org/web/20060922223713/http://appropriations.senate.gov/hearings/record.cfm?id=220270>.

23. Fred Stokeld, *Miller Announces Initiative on EO Compensation, Other Compliance Projects*, 84 TAX NOTES TODAY 6 (Apr. 29, 2004).

24. Fred Stokeld, *Senate Finance Staffers Describe Lawmakers’ EO Abuse Concerns*, 84 TAX NOTES TODAY 7 (Apr. 29, 2004).

25. Fred Stokeld, *IRS’s Miller Briefs Church Reps on Service’s Policies On Churches, Religious Orgs.*, 99 TAX NOTES TODAY 6 (May 21, 2004).

26. Press Release, Internal Revenue Serv., Miller, Morgante Named to Leadership Posts (May 25, 2004), <http://www.irs.gov/newsroom/article/0,,id=123466,00.html>.

27. Public and special audience speeches by high-ranking IRS officials can not only indicate positions the IRS is likely to take regarding the various tax issues, but are also given weight by the courts. See *Vinson & Elkins v. Comm’r*, 99 T.C. 9, 58-59 (1992), *aff’d*, 7 F.3d 1235 (5th Cir. 1993).

28. See, e.g., Steven Toscher & Chad Nardiello, *IRS Scrutiny of Tax-Exempt Organizations*, 28 LOS ANGELES LAWYER 18 (Oct. 2005).

many areas of tax exemption privilege, including but not limited to charitable hospitals,<sup>30</sup> colleges and universities,<sup>31</sup> churches and religious organizations,<sup>32</sup> the Smithsonian Institution<sup>33</sup> and the American Red Cross.<sup>34</sup>

One telling example of how issues relating to tax-exempt organizations have come to pervade Congressional attitudes is the Pension Protection Act of 2006.<sup>35</sup> As its name implies, the primary purpose and thrust of the Act was to ensure the security of Americans' retirement pension funds.<sup>36</sup> But the Act also contains provisions of tenuous if not obscure connections to the Act's primary stated objectives, including Title XII, which imposes new requirements upon tax-exempt organizations and their contributors.<sup>37</sup> These new

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29. See, e.g., STAFF OF JOINT COMM. ON TAXATION, 109TH CONG., REPORT ON HISTORICAL DEVELOPMENT AND PRESENT LAW OF THE FEDERAL TAX EXEMPTION FOR CHARITIES AND OTHER TAX-EXEMPT ORGANIZATIONS 1(2005), available at <http://www.house.gov/jct/x-29-05.pdf>; Dana Brakman Reiser & Evelyn Brody, *Who Guards the Guardians?: Monitoring and Enforcement of Charity Governance*, 80 CHI.-KENT. L. REV. 543 (2005).

30. See, e.g., STAFF OF JOINT COMM. ON TAXATION, 109TH CONG., REPORT ON PRESENT LAW AND BACKGROUND RELATING TO THE TAX-EXEMPT STATUS OF CHARITABLE HOSPITALS 1 (2006), available at <http://www.house.gov/jct/x-40-06.pdf>.

31. See, e.g., Staff of Joint Comm. on Taxation, 109th Cong., Report on Present Law and Background Relating to Tax Exemptions and Incentives for Higher Education 1 (2006), available at <http://www.house.gov/jct/x-49-06.pdf>.

32. See, e.g., Press Release, Sen. Comm. on Finance, Grassley Seeks Information from Six Media-Based Ministries (Nov. 6, 2007), available at <http://finance.senate.gov/press/Gpress/2007/prg110607.pdf>.

33. See, e.g., Letter from Chuck Grassley, Minority Member, Sen. Finance Comm., to Roger Sant, Chair Exec. Comm., Smithsonian Board of Regents (Jan. 3, 2008), available at <http://finance.senate.gov/press/Gpress/2007/prg051707a.pdf>. GENERAL ACCOUNTING OFFICE, REPORT ON SMITHSONIAN INST.: BOARD OF REGENTS HAS IMPLEMENTED MANY GOVERNANCE REFORMS, BUT ENSURING ACCOUNTABILITY AND OVERSIGHT WILL REQUIRE ONGOING ACTION 1 (2008), available at <http://www.gao.gov/new.items/d08632.pdf>.

34. See American National Red Cross Governance Modernization Act of 2007, P.L. 110-26, 1221 Stat. 103 (2007); H.R. Rep. No. 110-87 (2007). Though the popular name under which it operates is the "American Red Cross," the organization's official name is the "American National Red Cross." 36 U.S.C. § 300101(b) (2009). The American National Red Cross has mixed legal attributes of both a charitable organization and an agency of the United States Government. See Wesley A. Sturges, *The Legal Status of the Red Cross*, 56 MICH. L. REV. 1 (1957).

35. Pension Protection Act of 2006, Pub. L. 109-280, 120 Stat. 780 (2006) [hereinafter "PPA"].

36. See President's Remarks on Signing the Pension Protection Act of 2006, 42 WEEKLY COMP. PRES. DOC. 1469 (Aug. 21, 2006). President's Statement on Signing the Pension Protection Act of 2006, 42 WEEKLY COMP. PRES. DOC. 1470 (Aug. 21, 2006).

37. PPA, *supra* note 35, at §§ 1201 - 44.

requirements affected, and continue to affect, virtually every charity and its donors.<sup>38</sup>

The current atmosphere of active and intrusive official scrutiny, oversight, and inquiry into the tax-exempt organization has been quite pervasive, and will likely continue indefinitely.

### III. TRUST FUND PENALTIES

#### A. General Background

It has long been universally recognized among diverse governing regimes that those who perform the taxation function must be personally accountable for the taxes they collect and handle.<sup>39</sup>

The Revenue Act of 1918 imposed a personal monetary penalty separate and apart from, but equal to, unremitted third-party tax collections.<sup>40</sup> This imposition of responsibility upon third-party tax

38. *E.g., id.* at § 1217 (requiring that donors obtain and retain “a bank record or a written communication from the donee” to substantiate their charitable contributions). Prior to PPA, donors of relatively small cash amounts could, under certain circumstances, estimate their cash contributions, and the taxpayer’s bare unsubstantiated word, when credible, was accepted by the taxation authorities and the courts. *See, e.g., Calderazzo v. Comm’r*, 26 T.C.M. (CCH) 140, 142 n.3 and accompanying text (T.C. Memo 1967-25) (reciting that IRS New York District had a written internal policy which gave auditors discretion to allow up to \$1.50 per week in unsubstantiated charitable contributions when the auditor believed the taxpayer’s oral statements to be credible); *Robertson v. Dep’t of the Treasury*, 2005 MSPB LEXIS 560 (Feb. 2, 2005), *aff’d*, 180 Fed. Appx. 963 (Fed. Cir. 2006), *cert. denied*, 549 U.S. 1021 (2006); *Bagby v. Comm’r*, 102 T.C. 596, 611 (1994); *Robinette v. Comm’r*, No. 16875-04S, 2006 WL 1330886 (2006) (T.C. Summary Op. 2006-69); *Fontanilla v. Comm’r*, 77 T.C.M. (CCH) 1977 (1999) (T.C. Memo 1999-156); *Jackson v. Comm’r*, 77 T.C.M. (CCH) 2203 (U.S. Tax Ct. Apr. 26, 1999) (T.C. Memo 1999-203).

39. *See, e.g.,* CODE OF HAMMURABI KING OF BABYLON ABOUT 2250 B.C. 25 (R. F. Harper trans., U. of Chicago Press 2d ed. 1904):

§38 An officer, constable or tax-gatherer shall not deed to his wife or daughter the field, garden or house, which is his business (i.e., which is his by virtue of his office), nor shall he assign them for debt.

§39 He may deed to his wife or daughter the field, garden or house which he has purchased and (hence) possesses, or he may assign them for a debt.

*Id.*; MAIMONIDES MISHNEH TORAH (YAD HAZAKAH) 95 (Philip Bimbaum trans., Hebrew Publ. Co. 1967) (Describing procedure for counting the shekels collected for the Temple: “Besides, conversation was maintained with him from the moment he entered the chamber until he left it, to prevent him from putting coins in his mouth.”); THE CIVIL LAW, THE CODE OF JUSTINIAN, 319 (S. P. Scott trans., AMS Press Inc. 1973) (1932) (“Whenever a collector is accused and convicted of depredations, he must suffer the penalty prescribed by law, without appealing to Our clemency.”); *Order per Collectors the penny per pound*, (7 October 1675), in MINUTES OF THE COUNCIL AND GENERAL COURT OF COLONIAL VIRGINIA 424 (H. R. McIlwaine ed., 1st ed. 1979) (requiring tax collectors to give bond for their performances).

40. Revenue Act of 1918, § 1308(c), 40 Stat. 1143.

collectors became salient in 1943 with the Current Tax Payment Act,<sup>41</sup> which, amidst the personal financial chaos that afflicted many taxpayers in the wartime economy, gave the United States Treasury a steady and reliable stream of income by mandating that employers withhold income taxes from their employees' paychecks, instead of having to rely upon the individual taxpayers' making their tax payments in full following the close of the tax year.<sup>42</sup>

America's return to the peacetime economy following World War II, and the accompanying and consequent changes in the American demographics and economy, definitively began the shift in the primary base of the Treasury's revenue from excise tax receipts to income tax receipts.<sup>43</sup>

Following the lessons and precedents from history, the current Internal Revenue Code of 1954/1986<sup>44</sup> continues the anciently-rooted scheme of holding accountable those individuals whose duty it is to collect and remit the taxes withheld from employees' paychecks. Specifically, the Code provides that all withheld monies be considered held in "a special fund in trust for the United States,"<sup>45</sup> and also provides that the willful failure to collect, account for, or remit any tax is a felony offense<sup>46</sup> (though the government has been criticized for its hesitancy to invoke such criminal sanctions<sup>47</sup>). More commonly invoked than any criminal sanctions, however, is the purely civil Code Section 6672,

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41. Current Tax Payment Act of 1943, Pub. L. No. 78-68, ch. 120, 57 Stat. 126 (1943).

42. See SHELLEY L. DAVIS, UNBRIDLED POWER: INSIDE THE SECRET CULTURE OF THE IRS 196 (HarperBusiness 1997); see also *Donelan Phelps & Co., Inc. v. United States*, 876 F.2d 1373, 1374-75 (8th Cir. 1989).

The parallels between the "pay as you go" tax collection system and the practice of purchasing goods on credit are more than mere coincidence; the Current Tax Payment Act was the suggestion of Beardsley Ruml, who, in addition to being a Director of the New York Federal Reserve Bank, was also the Chairman of the R. H. Macy Co., the well-known department store retailer. DAVIS, *supra* at 196.

43. See *id.* at 196-97.

44. See *supra* note 3.

45. I.R.C. § 7501(a). There is no specific requirement that the monies be placed in a separate bank account or otherwise segregated from the employer's other funds pending remittance to the IRS. *Slodov v. United States*, 436 U.S. 238, 243 (1978). However, such would be the safer and more advisable practice. See, e.g., *In re Lyle*, 83 B.R. 57, 60 (Bankr. N.D. Ala. 1988).

46. I.R.C. § 7202; see also *United States v. Easterday*, 539 F.3d 1176 (9th Cir. 2008); *United States v. Scharf*, 558 F.2d 498 (8th Cir. 1977).

47. See, e.g., Leonard R. Rosenblatt, *Payroll Tax Fraud: No Excuses, No Exemptions*, 155 N.J.L.J. 756 (1999).



which jointly and severally imposes an assessable penalty, equal to the amount of the taxes not remitted to the IRS.<sup>48</sup>

The funds withheld are commonly known as “trust funds.”<sup>49</sup> Those individuals who are responsible for collecting and remitting the payroll taxes are commonly referred to as “responsible persons” or the like.<sup>50</sup> Many states have similar if not substantially verbatim statutes which impose personal liability upon responsible persons,<sup>51</sup> and the constructions by the respective state courts of such statutes tend to follow the Federal courts’ construction of I.R.C. § 6672.<sup>52</sup>

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48. I.R.C. § 6672. *Cf.* TA TSING LEU LEE, THE FUNDAMENTAL LAWS AND A SELECTION FROM THE SUPPLEMENTARY STATUTES OF THE PENAL CODE OF CHINA 132 (George Thomas Staunton trans., photo reprint Ch’eng-wen Pub. 1966) (1810). Civil Code Section 125 states :

If any superintending officer of government, having charge of a part of the produce of the revenue . . . borrows for his own use, or lends the same to others, . . . such superintendent *shall be punished for every offence in proportion to the amount and value*, according to the law concerning the embezzlement of the property of government.

If any other person borrows for his own use, or lends the produce of the revenues as aforesaid, he *shall be punished in proportion to the amount and value*, according to the law for punishing *thefts* committed upon the property of the state.

*Id.* (first emphasis added).

49. *Slodov v. United States*, 436 U.S. 238, 243 (1978); *see also* *Fran Corp. v. United States*, 164 F.3d 814, 817 (2d Cir. 1999) (“The taxes an employer withholds from and pays on behalf of its employees are often called “trust fund taxes.””).

50. *Slodov*, 436 U.S. at 246; *see also* *United States v. Energy Resources Co., Inc.*, 495 U.S. 545, 547 (1990) (citing *Slodov* and using term “responsible individuals”); *Lubetzky v. United States*, 393 F.3d 76, 81 (1st Cir. 2004) (using term “responsible party”); *Bell v. United States*, 355 F.3d 387, 393-94 (6th Cir. 2004) (using, at various places, “responsible person,” “responsible party” and “responsible individual”).

Terms such as “responsible person,” “responsible party” and “responsible individual” are of administrative and judicial origin; I.R.C. § 6672 does not utilize the word “responsible” at all. *Cf.*, *e.g.*, 42 U.S.C. § 9604(a) (2005) (referring to “potentially responsible parties” in connection with toxic waste clean-up statutes).

51. *E.g.*, ARIZ. REV. STAT. § 42-5028 (LexisNexis 1999); CONN. GEN. STAT. § 12-736 (1997); NY TAX LAW § 685(g) (McKinney 2005); OHIO REV. CODE § 5739.33 (West 2003). Some local municipalities, including New York City, have their own trust fund statutes. *See, e.g.*, NEW YORK CITY, N.Y., ADMIN. CODE tit. 11, §§ 11-1775 and 11-1913 (2007); PHILADELPHIA, PA., INCOME TAX REG. § 407 (2001). The state and local statutes can apply to taxes other than payroll taxes. *See, e.g.*, *Rock v. Department of Taxes*, 742 A.2d 1211 (Vt. 1999) (imposing Vermont trust fund liability for withholding payroll taxes, rooms and meals taxes, and sales and use taxes).

52. *See, e.g.*, *Rock*, *supra* note 51, at 1215-17; *Breck v. State*, 862 P.2d 854 (Alaska 1993); *State v. Cook*, No. CR93-441268s, 1993 WL 343688 (Conn. Super. Ct. 1993); *Brumby v. Brooks*, 216 S.E.2d 288, 292 (Ga. 1975); *Branson v. Dept. of Revenue*, 659 N.E.2d 961 (Ill. 1995); *Dep’t of Revenue v. Safayan*, 654 N.E.2d 270, 274-75 (Ind. 1995); *Yellin v. New York State Tax Comm.*, 81 A.D.2d 196 (N.Y. App. Div. 1981).

### B. *The Sweep of the Statute*

The courts have interpreted and applied I.R.C. § 6672 very broadly.<sup>53</sup> Individual responsibility is determined according to the particular facts and circumstances of the case, with no single factor being determinative.<sup>54</sup> Factors weighed by the courts and the IRS include whether and to what extent the individual

(1) is an officer or member of the board of directors, (2) owns shares or possesses an entrepreneurial stake in the company, (3) is active in the management of day-to-day affairs of the company, (4) has the ability to hire and fire employees, (5) makes decisions regarding which, when, and in what order outstanding debts or taxes will be paid, (6) exercises control over daily bank accounts and disbursement records, and (7) has check-signing authority.<sup>55</sup>

Other factors may also be considered,<sup>56</sup> including whether the individual actually signed the tax returns.<sup>57</sup>

I.R.C. § 6672 is, of necessity, a harsh statute.<sup>58</sup> In administering the statute as a tool to collect the revenue, the IRS has the prerogative to

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53. See, e.g., *Williams v. United States*, 931 F.2d 805, 810 (11th Cir. 1991); *Mazo v. United States*, 1977 U.S. Dist. LEXIS 16783 (S.D. Ga. Mar. 22, 1977), *aff'd*, 591 F.2d 1151 (5th Cir. 1979), *cert. denied*, 444 U.S. 842 (1979); Mary A. Bedikian, *The Pernicious Reach of 26 U.S.C. § 6672*, 13 VA. TAX REV. 225 (1993); Corrie Lynn Lyle, *The Wrath of I.R.C. § 6672: The Renewed Call for Change – Is Anyone Listening? If You Are a Corporate Official, You Had Better Be*, 74 S. CAL. L. REV. 1133, 1140-43 (2001).

54. *Fiataruolo v. United States*, 8 F.3d 930 (2d Cir. 1993).

55. *Id.* at 939; *cf.* *Benoit v. Comm’r of Rev.*, 453 N.W.2d 336, 344 (Minn. 1990). The court states:

The courts have looked at the following factors in determining who is a responsible person:

- (1) The identity of the officers, directors and stockholders of the corporation and their duties;
- (2) The ability to sign checks on behalf of the corporation;
- (3) The identity of the individuals who hired and fired employees;
- (4) The identity of the individuals who were in control of the financial affairs of the corporation; and
- (5) The identity of those who had an entrepreneurial stake in the corporation.

*Id.*

56. *Bedford v. United States*, 1977 U.S. Dist. LEXIS 16728, at \*13 (E.D. Wis. March 25, 1977).

57. See Internal Revenue Manual § 5.7.3.3.1.4 (April 13, 2006); *Winter v. United States*, 196 F.3d 339, 347 (2d Cir. 1999); *Bergman v. United States*, 2007 U.S. Dist. LEXIS 51305, at \*24 (E.D.N.Y. July 16, 2007); see also N.Y. COMP. CODES R. & REGS. tit. 20, § 526.11(b)(2) (2008) (New York State Dept. of Taxation & Finance guidance: “Generally, a person who is authorized to sign a corporation’s tax returns or who is responsible for maintaining the corporate books, or who is responsible for the corporation’s management, is under a duty to act.”).

pursue the responsible parties of its choice,<sup>59</sup> and broad discretion to settle with any responsible person on whatever terms it deems appropriate or convenient,<sup>60</sup> without regard to any considerations of fairness or equity as among multiple responsible parties.<sup>61</sup> Moreover, those who wish to dodge Section 6672's statutory sting are often placed in the unhappy position of having to abdicate their authority and/or resign their positions in order to avoid liability.<sup>62</sup> Additionally, a Section 6672 obligation is a nondischargeable debt in a bankruptcy situation.<sup>63</sup>

### *C. The Safe Harbor for Volunteer Board Members of Tax-Exempt Organizations*

Various entities, including tax-exempt organizations, often designate particular individuals as honorary board members. This is done for various reasons, which may entail the recognition of the individual's past contributions to the organization,<sup>64</sup> trading on the celebrity of the individual to give the organization public visibility,<sup>65</sup> effectuating the organization's special relationship with government<sup>66</sup> or

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58. *See, e.g.*, *Wright v. United States*, 809 F.2d 425, 428 (7th Cir. 1987) ("The statute is harsh, but the danger against which it is directed - that of failing to pay over money withheld from employees until it is too late, because the company has gone broke - is an acute one against which, perhaps, only harsh measures are availing.").

59. *See, e.g.*, *Mussato v. United States*, No. 80-W-1550, 1982 U.S. Dist. LEXIS 14336 at \*7-8 (D. Colo.); *see also* H.R. Rep. No. 104-506, at 40 (1996).

60. *See, e.g.*, *Wollman v. United States*, 571 F. Supp. 824 (S.D. Fla. 1983).

61. *Fowler v. United States*, 820 F. Supp. 1390, 1394 (D.Wyo. 1993) ("The IRS apparently makes no effort to administrate the penalty against potentially liable officers and directors in an equitable or fair manner. The IRS collects money as it is paid, without reference to who pays or what amount is paid.").

62. *See, e.g.*, *United States v. Running*, 7 F.3d 1293, 1299 (7th Cir. 1993) ("Running maintains that he knew of Bethel's financial problems early on, but 'rather than subject himself to the obvious risk that the employment taxes may go unpaid, he resigned.'" ); *see also* *Lyle, supra* note 53, at 115-54 ("The officer should also terminate his or her check-signing authority immediately, since the IRS often uses check-signing authority as prima facie evidence of being a responsible person. Furthermore, the officer should resign from the company after finding out that the taxes have not been paid.").

63. *United States v. Sotelo*, 436 U.S. 268, 274 (1978).

64. *See, e.g.*, *Ingalls v. Mount Oak Methodist Church Cemetery*, 223 A.2d 778 (Md. 1966).

65. *See, e.g.*, *Rogers v. Dallas Morning News, Inc.*, 889 S.W.2d 467, 469 (Tex. App. 1994).

66. *See, e.g.*, *San Francisco Arts & Athletics, Inc. v. U. S. Olympic Comm.*, 483 U.S. 522, 552 n.6 (1987) (citing "President [Jimmy] Carter's letter to the USOC, written in his capacity as 'Honorary President of the United States Olympic Committee,' in which the President explains the 'deeper issues . . . at stake' in the USOC's decision [to not participate in the 1980 Moscow Summer Olympics]"); *United States v. D. C.*, 558 F. Supp. 213, 216-17 (D.C. Dist. 1982), *vacated on unrelated grounds*, 709 F.2d 1521 (D.C. Cir. 1983) ("[T]he [United States Capitol Historical Society] does have an Honorary Board of Trustees. The President and Vice President of the United

with an organized religious denomination,<sup>67</sup> a gracious face-saving exit for a board member whose removal is compelled for health, financial, or political reasons,<sup>68</sup> or some combination of these purposes.<sup>69</sup>

In 1996, as part of TBOR2, Congress enacted a statutory exclusion for voluntary board members of charitable and other tax-exempt organizations.<sup>70</sup> The amendment specifically provides:

- (e) Exception for voluntary board members of tax-exempt organizations. No penalty shall be imposed by subsection (a) on any unpaid, volunteer member of any board of trustees or directors of an organization exempt from tax under subtitle A if such member-
- (1) is solely serving in an honorary capacity,
- (2) does not participate in the day-to-day or financial operations of the organization, and
- (3) does not have actual knowledge of the failure on which such penalty is imposed.

The preceding sentence shall not apply if it results in no person being liable for the penalty imposed by subsection (a).<sup>71</sup>

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States and other distinguished government figures are members of the Board. This is an indication of the unusual relationship the USCHS has with the federal government.”)

67. See, e.g., *In re Kensington Hospital for Women*, 58 A.2d 154, 156 (Pa. 1948) (reciting that the Bishop of the Protestant Episcopal Diocese was the honorary president of the board of a hospital affiliated with the Protestant Episcopal Church).

68. See, e.g., *Wellman v. Dickinson*, 475 F. Supp. 783, 799 (S.D.N.Y. 1979), *aff'd*, 682 F.2d 355 (2d Cir. 1982), *cert. denied*, 460 U.S. 1069 (1983) (“Dickinson was deposed as chairman and nudged out the back door with the title of Honorary Chairman.”).

69. See, e.g., Texas Ranger Hall of Fame & Museum, In Memoriam: Clayton Moore (Dec. 28, 1999), <http://web.archive.org/web/20020623130322/http://www.texasranger.org/ClaytonMoore1.htm> (Obituary announcement for actor Clayton Moore, who played The Lone Ranger in the popular television series of that name which ran from 1949 – 1957. “Earlier this year, Mr. Moore accepted an honorary lifetime appointment to the Advisory Board of the Texas Ranger Hall of Fame and Museum. The honor was conveyed to him in recognition of his positive contributions to the image of the Texas Rangers . . . .” In addition to the motive of honoring Mr. Moore, the Hall of Fame and Museum obviously stood to enhance its own public image by co-opting such a celebrity as an honorary member of its board.).

70. See *supra* note 7. TBOR2 also codified a federal law right of contribution for those responsible parties who pay more than their proportionate share of the IRC § 6672 penalty when there is more than one responsible party. Taxpayer Bill of Rights 2, § 903, 110 Stat. 1452, 1466 (codified at I.R.C. § 6672(d) (1998)). This author has previously expounded upon the I.R.C. § 6672(d) right of contribution. Kenneth H. Ryesky, *In Employers We Trust: The Federal Right of Contribution under Internal Revenue Code § 6672*, 9 FORDHAM J. OF CORP. & FIN. L. 191 (2003).

71. I.R.C. § 6672(e). The amendment also requires the IRS to publicize the trust fund rights and responsibilities of honorary board members and others to the public and to the IRS’s own employees. Tax Payer Bill of Rights, § 904(b), 110 Stat. at 1467.

TBOR2 thus, on its face, provides a statutory safe harbor for voluntary board members of charitable organizations who meet its 3-prong test. The parameters of this safe harbor will presently be explored.

1. “Is solely serving in an honorary capacity”<sup>72</sup>

What is meant by service in an honorary capacity? Terms such as “honorary board member” or the like can be given whatever meaning the user might wish to give them.<sup>73</sup> Merely because someone’s board position is denoted as “honorary” would not fulfill the first prong of Subsection 6672(e). The mere use or non-use of “honorary” as an honorific is certainly not dispositive of one’s actual functions or duties with respect to the organization.<sup>74</sup> One can, for example, be designated as an “honorary” board member and still have the authority to sign contracts on behalf of the corporation or entity.<sup>75</sup> Being that the term “serving in an honorary capacity” is not otherwise defined by statute or regulation,<sup>76</sup> the statute must be construed by giving the term its plain meaning as used in common parlance.<sup>77</sup>

For such purposes, a dictionary is a very helpful tool in construing the term.<sup>78</sup> Several common dictionaries carry comparable definitions for the word “honorary” as it would be used in connection with a board member or officer. The Funk & Wagnalls Dictionary’s relevant definition of honorary is “[h]olding an office or title bestowed in sign of honor and exempt from the regular powers and duties or without the

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72. I.R.C. § 6672(e)(1).

73. See, e.g., *United Title Ins. Co. v. Comm’r*, 55 T.C.M. (CCH) 34, 37 n.6 (1988) (T.C. Memo 1988-38) (“Respondent on brief characterizes these independent outside directors as ‘honorary board members,’ a meaningless term which respondent seems to use in a pejorative sense.”).

74. See, e.g., *Locke Assocs. v. Found. for the Support of the UN*, 661 N.Y.S.2d 691, 693 (N.Y. 1997).

75. See, e.g., *Rubin v. United States*, No. 72-350, 1974 U.S. Dist. LEXIS 9656 (W.D. Pa. 1974).

76. *But cf.* 12 C.F.R. § 7.2004 (2004) (“A national bank may appoint honorary or advisory members of a board of directors to act in advisory capacities *without voting power or power of final decision in matters concerning the business of the bank.*” (emphasis added)).

77. *Foxgord v. Hischmoeller*, 820 F.2d 1030, 1032 (9th Cir. 1987), *cert. denied*, 484 U.S. 986 (1987) (construing term “honorary consul”).

78. See *id.*; *but cf.* Samuel A. Thumma & Jeffrey L. Kirchmeier, *The Lexicon has Become a Fortress: The United States Supreme Court’s Use of Dictionaries*, 47 BUFF. L. REV. 227, 296 (1999) (concluding that the wooden invocation of dictionary definitions, without regard to “context, underlying facts, legislative purpose, [and] prior decisions . . .,” is not a sound process for construing terms).

usual emoluments.”<sup>79</sup> Similarly, the relevant Merriam-Webster definition is “a. conferred or elected in recognition of achievement or service without the usual prerequisites or obligations <an [honorary] degree> <an [honorary] member>. b. unpaid, voluntary <an [honorary] chairman>.”<sup>80</sup>

Accordingly, the critical element of the first prong of I.R.C. § 6672(e) would be an appointment to the board with the intention that the honorary membership have no functional significance other than lending the honorary member’s name to the organization.<sup>81</sup> Also implicit in the definition of “honorary” is that the individual serve without pay<sup>82</sup> (though the argument can be made that reimbursement for mileage, meals and similar outlays would not be considered remuneration so as to defeat the honorary nature of the service<sup>83</sup>).

2. “Does not participate in the day-to-day or financial operations of the organization”<sup>84</sup>

At first glance, this prong would seem redundant to the first prong.<sup>85</sup> But, as previously mentioned, the meaning of “honorary” is subject to diverse variation from organization to organization,<sup>86</sup> and even unpaid board members or officers whose service might otherwise be characterized as “honorary” have been known to participate in the management and finances of their organizations.<sup>87</sup> Accordingly, this second prong limits the functions of the “honorary” board member who seeks the safe harbor of I.R.C. § 6672(e), regardless of how the term

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79. FUNK & WAGNALLS NEW STANDARD DICTIONARY OF THE ENGLISH LANGUAGE 1177 (1949).

80. MERRIAM-WEBSTER’S COLLEGIATE DICTIONARY 557 (10th ed. 1997).

81. If indeed the position is purely honorary, with no governance or financial authority or responsibility, then there would be no reason why a board could not have more than one such honorary member. *See, e.g.* N. J. Title Guarantee & Trust Co. v. Am. Nat’l Red Cross, 160 A. 842, 843 (N.J. Ch. 1932) (reciting that organization had two honorary chairmen in addition to its nominal chairman).

82. *See supra* notes 79-80 and accompanying text.

83. *Cf. In re Perry*, 239 B.R. 801, 807 (Bankr. W.D. Ark. 1999) (reciting that debtor had served as a member of the Arkansas State Board of Education “without pay, except for a small appearance fee” and travel expenses for attending Board meetings); *Nat’l Wooden Box Assn. v. United States*, 59 F. Supp. 118, 119 (Ct. Cl. 1945) (“In some instances, where the president [who served in an essentially honorary capacity] made a trip to preside over a meeting, exclusively for that purpose, he was reimbursed his actual traveling expenses by the Association, and no more.”).

84. I.R.C. § 6672(e)(2).

85. *See supra* notes 72-83 and accompanying text.

86. *See supra* notes 73-75 and accompanying text.

87. *See, e.g.*, *United States v. Bernstein*, 179 F.2d 105, 109 (4th Cir. 1949) (reciting that the individuals in question, though unpaid, did sign stock certificates and checks).

“honorary” might be understood in connection with his or her board membership.

But what constitutes participation in the “day-to-day or financial operations of the organization” does not necessarily lend itself to a bright line definition. To be sure, the phrase “day-to-day” is susceptible to various definitions, some of which connote one day at a time, and others which connote an ongoing course of conduct.<sup>88</sup> Given the ordinary recurring nature of payrolls and their consequent trust fund taxes, and the continuing, persistent obligation that such trust fund taxes be remitted to the government, the phrase “day-to-day” is obviously employed in Section 6672(e) in its expansive sense; it remains to be seen whether one or two isolated incidents of minor participation, without more, would disqualify the individual.

But what of the honorary board member who has been retained as the Board’s attorney or accountant, or the honorary board member who is the plaintiff in a lawsuit which the organization is financing or in which the organization is the real party with an interest?<sup>89</sup> If such actions do not constitute “day-to-day” participation, they would, in all likelihood, rise over and above the “solely serving in an honorary capacity” requirement of the first prong.<sup>90</sup> And, of course, there potentially exists the question of Section 6672 liability for the individual whose board membership status alternates from active to honorary and vice-versa.<sup>91</sup>

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88. See *Balasubramanian v. San Diego Cmty. Coll. Dist.*, 80 Cal. App. 4th 977 (Cal. Ct. App. 2000).

89. See *Wertheimer v. Fed. Election Comm’n*, 268 F.3d 1070, 1071 (D.C. Cir. 2001) (reciting that plaintiff Archibald Cox was Chairman Emeritus of Common Cause, an organization which had filed an administrative complaint with allegations similar to those asserted in the lawsuit at bar).

90. See *supra* notes 78-81 and accompanying text.

91. See *Martha Graham School & Dance Foundation, Inc. v. Martha Graham Center of Contemporary Dance, Inc.*, 224 F. Supp. 2d 567, 571 (S.D.N.Y. 2002), *aff’d in part & rev’d in part*, 2004 U.S. App. LEXIS 20904 (2d Cir. Aug. 18, 2004), *cert. denied sub nom. Martha Graham School & Dance Foundation, Inc. v. Spitzer*, 544 U.S. 1060 (2005), *decision on remand*, 374 F. Supp. 2d 355 (S.D.N.Y. 2005), *aff’d*, 466 F.3d 97 (2d Cir. 2006) (reciting that plaintiff’s witnesses included “Francis Mason, who, in 1973 or 1974, became a member and Chairman of the Center’s board of directors. After two or three years, he became Chairman Emeritus of the board. In 2001, Mason again became Chairman of the board . . .”).

3. “Does not have actual knowledge of the failure on which such penalty is imposed”<sup>92</sup>

The general rule for I.R.C. § 6672 trust fund liability is that “willfully”<sup>93</sup> failing to collect, remit, or account for the withholding taxes does not require actual knowledge of the failure; reckless disregard of whether the taxes were remitted is sufficient to bring one within the pale of the willfulness requirement.<sup>94</sup> In such regard, the Subsection 6672(e) safe harbor thus imposes a more exacting standard upon the IRS in order to find that an honorary board member is a responsible party, and commensurately provides a greater margin of safety for those whose tax-exempt organization board membership is truly honorary within the meaning of the Subsection.

But this small modicum of protection is nullified if the honorary board member learns, through whatever means, that the taxes are not being remitted as required. Accordingly, if the organization’s tax delinquency is mentioned at a board meeting attended by the honorary member,<sup>95</sup> then Subsection 6672(e) would no longer apply.

4. “Shall not apply if it results in no person being liable”<sup>96</sup>

The safe harbor of I.R.C. § 6672 has an “all bets are off” clause; the safe harbor does not apply if it would result in no person being liable to the government for the unpaid trust funds.

The “all bets are off” proviso is arguably superfluous. It is obvious and axiomatic that taxes do not pay themselves; the American system of voluntary compliance<sup>97</sup> requires proactive involvement of individuals. If

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92. I.R.C. § 6672(e)(3).

93. I.R.C. § 6672(a).

94. *Malloy v. United States*, 17 F.3d 329, 332 (11th Cir. 1994); *Hauf v. Internal Revenue Serv.*, 968 F. Supp. 78, 80 (N.D.N.Y. 1997).

95. *See, e.g., Jefferson v. United States*, 459 F. Supp. 2d 685, 688 (N.D. Ill. 2006), *aff’d*, 546 F.3d 477 (7th Cir. 2008) (“The Executive Director of the United Way attended New Zion’s February 1998 board meeting and informed Jefferson and the other directors that, *inter alia*, New Zion was delinquent in its tax payments and was in jeopardy of losing its United Way funding.”); *see also Schwinger v. United States*, 652 F. Supp. 464, 469 (S.D.N.Y. 1987).

It is not clear how someone outside the New Zion organization learned of the delinquency, inasmuch as tax information is supposed to be accorded a high degree of confidentiality by the IRS. *See* I.R.C. § 6103.

96. I.R.C. § 6672(e).

97. Voluntary compliance “means that taxpayers are expected to comply with the law without being compelled to do so by action of a federal agent; it does not mean that the taxpayer is free to decide whether or not to comply with the law.” INTERNAL REVENUE SERVICE, PUB. NO. 1273, GUIDE TO THE INTERNAL REVENUE SERVICE FOR CONGRESSIONAL STAFF 4 (1996).



indeed an individual is truly serving on an organization's board solely in an honorary capacity, then there would be other individuals who are effecting the organization's business transactions (and who should have been effecting the payment of the taxes). But novel and unintended circumstances have compelled absurd tax consequences in other matters,<sup>98</sup> accordingly, the "all bets are off" proviso ensures that there will always be at least one person who can be deemed a responsible party.

Given that the unabashed purpose of I.R.C. § 6672 is to collect the revenue,<sup>99</sup> the IRS, with its inherent bias towards maximizing the funds it collects,<sup>100</sup> may well be tempted to argue that the "all bets are off" proviso would kick in where the other responsible parties are impecunious, unlocatable, or otherwise unavailable as a source of funds, leaving the honorary board member holding the bag. But in other matters the IRS itself has specifically distinguished liability from collectibility in its regulations,<sup>101</sup> and so, bankruptcy issues notwithstanding, the success of such an argument, if made, remains to be seen.

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98. See, e.g., *Estate of Spiegel v. Comm'r*, 335 U.S. 701 (1949) (requiring inclusion in decedent's estate an approximately \$1 million trust having a retained interest with an actuarial value of approximately \$70, with consequent marginal tax of approximately \$450,000); *Exxon-Mobil Corp. v. United States*, 244 F.3d 1341, 1348 (Fed. Cir. 2001) ("Although these provisions arguably allow Exxon to claim an excessive deduction, it is not the province of this court to remedy anomalies in the tax laws that Congress and the Secretary have refrained from correcting."); *Hearing to Examine Tax Fraud Committed by Prison Inmates Before the Subcomm. on Oversight of the H. Comm. on Ways and Means*, 109th Cong. (2005), available at <http://waysandmeans.house.gov/hearings.asp?formmode=view&id=4523> (describing, by several witnesses and commentators, the statutory constraints that impede tax information sharing by the IRS with other law enforcement agencies to combat tax fraud by prison inmates).

99. See, e.g., *Slodov v. United States*, 436 U.S. 238, 247 (1978) ("[I.R.C. § 6672 was] designed to assure compliance by the employer with its obligation to withhold and pay the sums withheld.").

100. *Lykes v. United States*, 343 U.S. 118, 128-29 (1952) (Jackson, J., dissenting) ("The Treasury may feel that it is good public policy to discourage taxpayers from contesting its unjustified demands for taxes and thus justify penalizing resistance. It is hard to imagine any instance in which the Treasury could have a stronger self-interest in its regulation."); Kenneth H. Ryesky, *Analysis of the Split Authority on Proof of a Postmark under Internal Revenue Code § 7502*, 21 U. DAYTON L. REV. 379, 394-95 (1996).

Justice Jackson's view of the tax collection process is especially poignant in light of his service, prior to ascending to the bench, as General Counsel of the Bureau of Internal Revenue (1934 - 1935), and as an Assistant Attorney General in the Justice Department Tax Division (1936 - 1938). See Federal Judges Biographical Database, Robert Houghwout Jackson, <http://www.fjc.gov/servlet/tGetInfo?jid=1160> (last visited Feb. 27, 2009).

101. Treas. Reg. § 301.7122-1(b) (2002) (setting forth "doubt as to liability" and "doubt as to collectibility" as two separate and distinct grounds for entering into compromises with taxpayers.). Tax regulations are promulgated through a complex process of collaboration between the IRS and the Treasury Department proper, and while the Treasury has ultimate veto power over the final

#### D. Nonliability outside the Safe Harbor

Board members who cannot find shelter in the safe harbor of I.R.C. § 6672(e) may nonetheless avoid responsibility for trust fund taxes which their organization has failed to remit to the IRS if, through application of the usual § 6672 factors, they are not a responsible person. A bankruptcy case, *Lartz*<sup>102</sup> exemplifies the possibilities for such avoidance. The debtor in *Lartz* served as an unpaid president of a social organization who was chosen on account of his perceived propensity to attract new members.<sup>103</sup> The minimal managerial tasks and functions exercised by Mr. Lartz, including his engagement of a consultant and his direction to the payroll contractor,<sup>104</sup> would certainly have disqualified him from the § 6672(e) safe harbor provisions, if for no other reason than his service went beyond being “solely in an honorary capacity.”<sup>105</sup> Nevertheless, weighing all of the factors, the Bankruptcy Court found that Lartz was not a responsible person within the meaning of § 6672, and accordingly sustained his objection to the IRS’s responsible person claim.<sup>106</sup>

Failure to qualify with the strict provisions of the § 6672(e) safe harbor, then, does not necessarily compel a board member’s liability as a responsible person for trust fund taxes (though it certainly is preferable, from the honorary board member’s perspective, to remain squarely within the safe harbor in the event of the organization’s tax delinquency).

#### IV. A SURVEY OF THE § 6672(E) CASES

A LEXIS search of the term “6672(e)” yielded a total of five published<sup>107</sup> judicial opinions, two of which were separate proceedings in the same case.<sup>108</sup> These cases are presently analyzed.

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regulation, the lion’s share of the work falls upon the shoulders of the cognizant IRS personnel. *See* Treas. Reg. § 601.601(1987).

102. *In re Lartz*, No. 1-00-01864, 2003 Bankr. LEXIS 246 (Bankr. M.D. Pa. 2003), *aff’d*, 301 B.R. 807 (M.D. Pa. 2003).

103. *Id.* at \*2.

104. *Id.* at \*2 -\*3.

105. I.R.C. § 6672(e)(1). Though the *Lartz* court did not specifically evaluate the debtor’s suitability for the I.R.C. § 6672(e) safe harbor protection, § 6672(e) is in fact set forth, *en passant*, in the opinion. *Lartz*, *supra* note 102, at \*10.

106. *Id.* at \*5 -\*12.

107. As used in this instance, the term “published” entails any form of publication, and is not necessarily limited to appearance of a case in an officially-designated court reporter.

The status of judicial opinions not published in official court reporters is a controversial issue in its own right. *See, e.g., Anastasoff v. United States*, 223 F.3d 898, *vacated en banc &*

*A. Lartz*<sup>109</sup>

*Lartz* was a bankruptcy case in which the debtor was exonerated of § 6672 liability.<sup>110</sup> As mentioned previously, the *Lartz* court applied and weighed the applicable factors to the particular circumstances.<sup>111</sup> Though the court did mention § 6672(e) *en passant*,<sup>112</sup> it made no finding that the § 6672(e) safe harbor provision was applicable; and could not, for *Lartz*, though serving without pay, was aware of the organization's tax deficiencies.

*B. Holmes*<sup>113</sup>

*Holmes* consists of two largely verbatim decisions handed down a little more than a week apart, respectively finding two officer-directors of a non-profit school jointly and severally liable for the § 6672 trust fund taxes.<sup>114</sup> The mere fact that the two officer-directors served without pay did not bring them into the safe harbor of I.R.C. § 6672(e), nor did the fact that the school's checks required two signatories serve to insulate any one check signatory from liability.<sup>115</sup> *Holmes* thus makes plain what should be the plain meaning of § 6672(e).

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*remanded*, 235 F.3d 1054 (8th Cir. 2000). Some courts have seen fit to admonish attorneys for citing unreported or "unpublished" opinions in briefs. *E.g.*, *Sorchini v. City of Covina*, 250 F.3d 706 (9th Cir. 2001); *see also* *Regency Pheasant Run, Ltd. v. Kareem*, 860 S.W.2d 755, 758 (Ky. 1993).

This article, focused as it is upon particular tax liability matters, shall restrain what might easily become an extended discourse bordering on polemic on the issue. Suffice it to say that fiats which restrict the universe of citable cases to those officially reported can easily transform a judicial opinion's publication status into a precious vendible in which corrupt judges and/or other courthouse functionaries might nefariously traffic. *Cf., e.g.*, Kevin Flynn & Andy Newman, *Inquiry Into Term-Limits Case Finds Judge's Actions Suspect*, N.Y. Times, June 14, 2003, at B1 (reporting that N.Y. Supreme Court Justice Gerard H. Rosenberg ordered a court attorney to delete a draft opinion from the court's computer database).

108. Author's LEXIS search for "6672(e)" in all state and federal cases (Aug. 25, 2008) (on file with author).

109. *See* *Lartz*, *supra* note 102.

110. *Id.*

111. *See supra* notes 103-107 and accompanying text.

112. *See* *Lartz*, *supra* note 102, at \*10 n.3.

113. *Holmes v. United States*, No. H-03-1493, 2004 U.S. Dist. LEXIS 7681 (S.D. Tex. Apr. 29, 2004), *later proceeding at* No. H-03-1493, 2004 U.S. Dist. LEXIS 9749 (S.D. Tex. May 7, 2004).

114. *Id.*

115. *Id.* In addition to the two director-officers who were party to the case, there was a third signatory, the school's administrator, who apparently made the decisions as to how the scarce funds would be distributed. *Id.* at \*2.

*C. Jefferson*<sup>116</sup>

Charles E. Jefferson had served, without pay, for nearly two decades as the President of the Board of Directors of the New Zion Day Care Center.<sup>117</sup> “Jefferson presided over the board’s monthly meetings, reviewed and approved New Zion’s financial statements and director’s statements, and acted as a co-signatory on New Zion’s bank accounts,”<sup>118</sup> and had specific knowledge of New Zion’s past tax delinquencies which, when combined with his knowledge of New Zion’s continuing financial deterioration, put him on notice that he should have ascertained that New Zion’s obligations to the IRS were current before drawing checks to other parties.<sup>119</sup> Accordingly, Jefferson not only failed miserably to qualify for the § 6672(e) safe harbor,<sup>120</sup> but was definitively liable under the general factors analysis application for § 6672.<sup>121</sup>

*D. Verret*<sup>122</sup>

As with the responsible party in *Jefferson*,<sup>123</sup> Stephen K. Verret was found liable for the trust fund taxes of a bankrupt nonprofit hospital under the § 6672 factors analysis, and specifically also found to not qualify for the § 6672(e) safe harbor for voluntary board members. Specifically,

Verret attended Board meetings, negotiated and personally guaranteed a \$500,000.00 working capital loan to acquire new equipment, reviewed financial information, actively engaged in recruiting physicians and developing a new source of revenue for Doctors Hospital, conversed with the Executive Director on an almost daily basis, signed the hospital’s IRS Form 990 for 1999 and 2000, and was a signatory on all of Doctors Hospital’s checking accounts. He also actively participated in the selection and retention of outside companies to assist in the management of Doctors Hospital. Thus,

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116. *Jefferson v. United States*, 459 F. Supp. 2d 685 (N.D. Ill. 2006), *aff’d*, 546 F.3d 477 (7th Cir. 2008).

117. *Id.*

118. *Id.* at 690.

119. *Id.* at 691.

120. *Id.* at 690.

121. *See supra* notes 54-57 and accompanying text.

122. *Verret v. United States*, 542 F. Supp. 2d 526 (E.D. Tex. 2008).

123. *See supra* notes 117-21 and accompanying text. The *Verret* decision specifically cites *Jefferson* and notes the numerous similarities between the two cases. *Verret*, 542 F. Supp. 2d at 543.

Verret clearly played an active role in the management of Doctors Hospital and was not serving solely in an honorary capacity.<sup>124</sup>

Indeed, in addition to his nominally uncompensated service on the board of the hospital, Verret, or business controlled, by Verret performed services to the hospital in other capacities, for which they were in fact compensated.<sup>125</sup>

#### IV. IMPLICATIONS OF § 6672 FOR HONORARY BOARD MEMBERS

The case law on I.R.C. § 6672(e), while quite sparse at this time, does give some rough indication as to what might be required if one is to benefit from its sheltering provisions. It must be remembered that statutory provisions, which grant relief from taxes are construed narrowly and strictly by the courts.<sup>126</sup> With such matters in mind, sound advice is possible for clients who contemplate accepting the honor of honorary membership on a tax-exempt organization's board. Indeed, the explicit interest of the Department of Justice in pursuing employment tax liabilities indicates that I.R.C. § 6672 issues are no longer the sole province of the IRS, that the IRS has already begun close cooperation with the Justice Department on employment tax issues, and that cognizance of the legal issues regarding employment taxes can be expected to grow increasingly more imperative for all who might be proximate to the employment tax collection processes.<sup>127</sup>

First of all, the honorary board member should be duly designated as such, preferably by a title such as "honorary" or "emeritus" or the like. Such designation should plainly appear in the minutes of a board meeting, and no official organization documents or stationery should indicate that such an individual serves in any capacity otherwise.

Once the honorary position is so designated, the honorary board member must take pains to in fact not actively participate in the operations of the organization. Actual or apparent signatory authority over bank accounts or other matters weighs decidedly against honorary status (and indeed, decidedly towards general liability under the general

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124. *Id.*

125. *Id.* at 529-30.

126. *Chrysler Corp. v. Comm'r*, 436 F.3d 644, 654 (6th Cir. 2006).

<sup>127</sup> See, e.g., Amy S. Elliott, *IRS will More Aggressively Pursue Employment Tax Liabilities*, *Hochman Says*, TAX NOTES TODAY, Jan. 14, 2009, at 8-8 (reporting Jan. 9, 2009 remarks by Assistant Attorney General Nathan Hochman, Chief of DOJ's Tax Division, at ABA Taxation Section Meeting). See *supra* note 27 regarding speeches by government officials.

factor analysis of § 6672).<sup>128</sup> And neither should the honorary board member exercise any say-so over payment of bills, hiring and firing of employees, or engagement of outside contractors. Much as a limited partner may lose his or her protections as such by engaging in managerial functions of the limited partnership entity,<sup>129</sup> an honorary board member can similarly lose the protection of the § 6672(e) safe harbor by participating in the financial or day-to-day operations of the non-profit entity. There should be no appearance of ambiguity in an honorary board member's honorary status.<sup>130</sup>

And, of course, the honorary service should be without any remuneration other than reasonable out-of-pocket expense reimbursement for activities necessitated by their honorary office.

Given that the I.R.C. § 6672(e) safe harbor also requires that the honorary board member have no knowledge of the tax-exempt entity's withholding tax delinquencies,<sup>131</sup> the honorary board member would be well advised to take pains to regularly absent himself or herself from any board meetings at which any organization financial or day-to-day operating business is discussed.

As expounded earlier, I.R.C. § 6672 is a broad brush statute with which the IRS has tarred many individuals whose complicity in the nonpayment of withholding taxes has been minor.<sup>132</sup> Accordingly, honorary board members, and those considering honorary board membership need to be mindful of the statute's tremendous downside potential.<sup>133</sup>

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128. See *supra* notes 54-57 and accompanying text. Even unexercised authority to sign checks weighs heavily towards trust fund liability. See, e.g., *Cohen v. State Tax Comm'n*, 128 A.D.2d 1022 (N.Y. App. Div. 1987). And the honorary officer or board member is well advised to not avail a facsimile signature rubberstamp to other organization personnel. See *Matter of Klein*, N.Y.S. Tax App. Tribunal, DTA Nos. 810209, 811722 & 811723 (Jan. 25, 1996).

129. E.g., *Gonzalez v. Chalpin*, 565 N.E.2d 1253, 1255 (N.Y. 1990); *Hommel v. Micco*, 602 N.E.2d 1259, 1263 (Ohio App. 1991).

130. See *DER Travel Serv., Inc. v. Dream Tours & Adventures, Inc.*, No. 99 Civ. 2231 (HBP), 2005 U.S. Dist. LEXIS 25861 (S.D.N.Y. Oct. 28, 2005) (piercing corporate veil and holding "honorary chairman" of entity liable for breach of contract where he failed to apprise those with whom he dealt of the "honorary" status of his title).

131. I.R.C. § 6672(e)(3).

132. See *supra* note 53 and accompanying text.

133. Downside potential may also include liability for state payroll and/or sales tax withholdings, pursuant to the analogous state trust fund statutes. Cf., e.g., *United States v. Landau*, 155 F.3d 93 (2d. Cir. 1998), *cert. denied*, 526 U.S. 1130 (1999) (reciting fact that IRS assessed trust fund penalties in 1987 against Nathan Unger and Robert Landau with respect to Federal withholding taxes owed by Robert Landau Associates ("RLA") for 1984 tax year), with *Matter of Unger*, No. 805351 and 806353 (N.Y. Tax App. Mar. 24, 1994), available at <http://www.nysdta.org/Determinations/805351.ORD.pdf> (reciting fact that New York State

Prior to accepting the honorary position in the first place, the prospective honorary board member should take into account the purposes behind the particular honorary position,<sup>134</sup> and, more importantly, ascertain what if any duties would be expected of him or her by the organization. Indemnification insurance policies for tax-exempt organizations often include emeritus board members as covered individuals;<sup>135</sup> the status and extent of such coverage should be ascertained by the prospective honorary board member.

If, for whatever reason, an individual finds himself or herself not squarely within the safe harbor of I.R.C. § 6672(e) (as, for example, would be the case if he or she were to serendipitously learn of the organization's tax delinquency<sup>136</sup>), behavior which does not constitute the possession or wielding of control over the organization's operations or finances might yet spare him or her of trust fund liability.<sup>137</sup>

## V. CONCLUSION

Pursuant to his wishes, following legal philosopher Jeremy Bentham's death, his body was preserved as an "auto-icon" and is now seated on display in a mobile glass and wood case at the University College of London, where, anecdotally, it is periodically wheeled into College Council meetings, and the minutes of such meetings reflect Bentham as "Present, but not voting."<sup>138</sup> Bentham's degree of involvement and participation with the College Council is an exemplar which pushes the limits of what an honorary board member of a charitable organization may do in order to drop anchor in the safe harbor of I.R.C. § 6672(e).<sup>139</sup>

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Department of Taxation & Finance issued Notices of Determination to Nathan Unger and Robert Landau with respect to sales taxes for periods ending August 31, 1984 owed by RLA).

134. See *supra* notes 64-69 and accompanying text.

135. See *Tr. of Princeton Univ. v. Nat'l Union Fire Ins. Co.*, 839 N.Y.S.2d 437 (N.Y. 2007).

136. See I.R.C. § 6672(e)(3).

137. See, e.g., *supra* notes 110-12 and accompanying text.

138. See, e.g., *Bent on Keeping His Head*, THE LAWYER, June 19, 2000, at 27; F. S. Schwarzbach, Letter to the Editor, CHRON. OF HIGHER EDUC. (Wash., D.C.), Apr. 10, 1998, at B13; see also Chemical History of UCL: The Autoicon, <http://www.chem.ucl.ac.uk/resources/history/chemhistucl/hist03.html> (last visited Feb. 27, 2009) (displaying photograph of auto-icon); NEGLEY HARTE, THE UNIVERSITY OF LONDON 1836 - 1986: AN ILLUSTRATED HISTORY 66 - 67 (Athlone Press 1986) (containing photograph of auto-icon).

139. Unlike the deceased Bentham, a living honorary board member who attends board meetings at which the organization's tax delinquencies are discussed has actual knowledge of such delinquencies and therefore cannot claim the shelter of the safe harbor. I.R.C. § 6672(e)(3).

But the best strategy by far, for all concerned, is to resist the temptation to tap withheld taxes to cover cash flow shortages<sup>140</sup> and to timely remit all withheld taxes to the government, so that personal trust fund liability is never even put into question.<sup>141</sup>

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140. See, e.g., P. Prestin Weidner, *The Misappropriation of Trust Fund Taxes Under the Guise of Reasonable Cause*, 57 VAND. L. REV. 287, 288-91 (2004).

141. See *United States v. Porth*, 426 F.2d 519, 522 (10th Cir. 1970).