

STATE OF ALABAMA  
DEPARTMENT OF REVENUE,

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STATE OF ALABAMA  
DEPARTMENT OF REVENUE  
ADMINISTRATIVE LAW DIVISION

§

v.

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DOCKET NO. INC. 87-203

KAUFMAN, ROTHFEDER & BLITZ  
P.O. Drawer 4540  
Montgomery, AL 36103,

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§

Taxpayer.

§

ORDER

The Revenue Department assessed withholding tax against Kaufman, Rothfeder & Blitz, P.C. ("Taxpayer") for the period June 1, 1984 through December 31, 1986. The Taxpayer appealed to the Administrative Law Division and a hearing was conducted on December 14, 1988. Jo Karen Parr, Esq. appeared for the Taxpayer. Assistant counsel Mark Griffin represented the Department. Based on the evidence presented by the parties, the following findings of fact and conclusions of law are hereby entered.

FINDINGS OF FACT

The relevant facts are undisputed.

The Taxpayer is a professional corporation located in Montgomery, Alabama and employs numerous attorneys and support personnel.

The Department audited the Taxpayer and determined that the Taxpayer had failed to properly withhold tax from the wages of a number of employees during the period June 1, 1984 through December 31, 1986, as required by Code of Ala. 1975, §40-18-71, et. seq. The deficiencies varied with each employee and for each year

involved. Based thereon, the Department assessed a 25% penalty and interest computed from the due date of each quarterly withholding report. No tax was assessed because all tax due was paid individually by the various employees.

The Taxpayer employed a full-time bookkeeper who was delegated the responsibility of properly withholding from each employee's wages. Three different bookkeepers were employed during the years in issue. Each of the bookkeepers had prior bookkeeping experience and thus were not given any special training, instructions or directions by the Taxpayer concerning how and in what amounts to withhold. Further, the Taxpayer had no internal control or review system whereby the bookkeepers' work product was routinely checked for accuracy. That is, the Taxpayer failed to monitor the bookkeepers and was unaware that tax was not being properly withheld from employee wages.

The firm's managing partner, Mr. Alan Rothfeder, testified that he had instructed the bookkeepers not to withhold from his wages because he had overpaid his Alabama income tax and had a credit on his estimated tax account with the Department. Mr. Rothfeder further anticipated that he would owe no Alabama tax for 1984 and 1985 and in fact had no Alabama liability for those years. None of the other attorneys gave any special withholding instructions to the bookkeepers.

The Taxpayer argues that no penalty or interest should be charged on the deficiencies relating to Rothfeder's wages because

Rothfeder had a credit with the Department and owed no tax during the periods in question. Concerning the other employees, the Taxpayer contends that it had no knowledge that tax was being improperly withheld and consequently that it should not be penalized for its bookkeepers' unauthorized failure to properly withhold.

#### CONCLUSIONS OF LAW

Code of Ala. 1975, §§40-18-71 through 80 require than an employer must withhold tax from an employee's wages and pay over said tax to the Department. The employer is specifically liable for the tax required to be withheld, see §40-18-76.

The tax must be withheld in the amount as set out in §40-18-71, and any overpayment resulting therefrom can only be refunded subsequent to the tax year as provided by §40-18-79. That is, the employer is required to withhold even if the employee in good faith believes that no tax will be due and in fact no tax is due by the employee for the subject year.<sup>1</sup>

Code of Ala. 1975, §40-18-80(b) levies "a civil penalty equal to 25% of the amount of taxes that should have been properly withheld and paid over to the Department . . .11 Despite the use of

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<sup>1</sup>Federal law allows an employee to reduce the amount withheld based on estimated itemized deductions (26 U.S.C. §3402(m)), or claim a total exemption based on the expectation that no tax will be due for the subject year (26 U.S.C. §3402(n)). Alabama has no similar provisions.

the imperative "shall", Alabama's courts have held that a "mandatory" penalty may be waived for reasonable cause if the taxpayer's failure to comply was caused or aided by the Department or the failure did not constitute a breach of duty by the taxpayer. State v. Mark, 411 So.2d 797; Morgan v. State, 194 So.2d 820.

However, in the present case the Department in no way contributed to the Taxpayer's clear breach of duty in failing to properly withhold. Accordingly, the penalty is clearly applicable.

The Taxpayer cannot avoid its responsibility to properly withhold by delegating that duty to an employee. United States v. Boyle, 105 S. Ct. 687.

In Boyle, an estate was assessed a penalty under 26 U.S.C. §6651 for failing to timely file an estate tax return. The estate had relied on an attorney to file the return. The issue was whether reliance on the attorney constituted "reasonable cause" which would relieve the estate from the penalty, see 26 U.S.C. §6651(a)(1). The Court applied the "ordinary business care and prudence" test and held that reliance on the attorney did not relieve the estate from liability.

In deciding the case, the Supreme Court recognized that reasonable cause may exist if the taxpayer has reasonably relied on the advice of an accountant or an attorney concerning a matter of law, i.e., whether a return should have been filed at all, see cases at Boyle, p. 692. However, if the taxpayer's duty is clear,

then reliance on an agent to complete the duty cannot relieve the taxpayer of any penalty due to the agent's failure to comply. As stated in Boyle, at p. 692, "[T]hat the attorney, as the executor's agent, was expected to attend to the matter does not relieve the principal of his duty to comply with the statute."

The Taxpayer's reliance on its bookkeeper in the present case is analogous to the estate's reliance on the attorney in Boyle. The Taxpayer was aware of its duty to properly withhold and cannot avoid liability by its reliance on an employee.

The Taxpayer argues that penalty and interest should not be assessed on that amount which Rothfeder had previously overpaid and carried as a credit with the Department on his individual account.

However, the penalty levied by §40-18-80(b) is to encourage and enforce strict compliance with the withholding provisions. An employer cannot avoid withholding by allowing an employee to pay through estimated payments or through application of a previous overpayment. The penalty must apply based on the employer's violation of the withholding statute.

Interest accrues on any deficiency from the due date of the tax, see §40-18-80(g). But interest should run only on the net amount due and unpaid to the State. Thus, interest should not be charged on the money overpaid by Rothfeder and held by the State. The fact that the overpayment was credited to Rothfeder's personal account and not to the Taxpayer's withholding account is irrelevant for

purposes of computing interest. While the penalty must be assessed based on the Taxpayer's failure to comply with the withholding tables, the State should not collect interest on a technical withholding deficiency if the money has already been paid to the State, even though credited to a different account.

The Department is hereby directed to recompute the assessment in issue as set out above. The assessment as recomputed should then be made final, with interest as required by statute.

Entered this the 18th day of January, 1989.

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BILL THOMPSON  
Chief Administrative Law Judge