

IN THE SUPREME COURT OF THE STATE OF DELAWARE

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DEPT. OF JUSTICE
Wilmington

DIRECTOR OF REVENUE,

§

§

Appellant Below,
Appellant,

§

§

No. 561, 1992

§

v.

§

Court Below: Superior Court

§

of the State of Delaware in

J. E. RHOADS & SONS, INC.,

§

and for New Castle County

§

C.A. No. 92A-01-003

Appellee Below,
Appellee.

§

§

Submitted: June 3, 1993

Decided: August 17, 1993

Before VEASEY, Chief Justice, MOORE and WALSH, Justices.

Appeal from Superior Court. Reversed and Remanded.

Joseph Patrick Hurley, Jr., Esquire, Deputy Attorney General,
Department of Justice, Wilmington, Delaware, for appellant.

J. E. Rhoads & Sons, Inc.

WALSH, Justice:

This is an appeal by the Director of Revenue of the State of Delaware ("Director") from a decision of the Superior Court which affirmed a ruling of the Delaware Tax Appeal Board ("Board") abating certain tax penalties assessed against the appellant, J. E. Rhoads & Sons, Inc. ("Rhoads"). The Director contends that the Superior Court and the Board erred in the application of the legal standard required to find reasonable cause to abate a penalty under 30 Del. C. § 1194(a) for late filing of a withholding tax return. Rhoads did not file a brief in this Court but relies upon the record presented in the Superior Court.

This controversy began with the Director's assessment of penalties against Rhoads for late payment of state withholding taxes for the period from January, 1988 through August, 1989. Initially, the Director abated the penalty for the month of January, 1988 but refused abatement with respect to the balance of the penalties. On appeal, the Board concluded that "reasonable cause" existed for abatement of all penalties.

The factual basis for the Board's finding of reasonable cause is set forth in the following stipulation of fact submitted by the parties incident to the Superior Court appeal:

STATEMENT OF FACTS

The factual hearing below which resulted in the appealed decision, produced a 46 page transcript, which is contained in the Board's record. Rhoads contended that the conduct of an employee constituted reasonable cause to file withholding tax returns late. The Director contended that no reasonable cause existed.

At the hearing Kevin Wooters, President and Chief Executive Officer ("Wooters") testified that several persons had been employed to perform bookkeeping duties, including payment of State and Federal withholding taxes, for the corporation. Wooters testified that because of Rhoads' poor economic condition it had difficulty attracting, hiring, and keeping competent persons to perform bookkeeping duties. (Transcript at 21) For the short period of May 1987 to November 1987 Brian Maloney ("Maloney") was employed to perform these duties. (Transcript at 24) Maloney quit his employment in November 1987 and sometime between November 1987 and January 1988 Rhoads discovered that Maloney had failed to perform all his duties. (Transcript at 26 and 31) At no time during the hearing was it alleged, however, that Maloney failed to file or pay state withholding taxes for any period.

In February, 1988, Wooters, then Vice President of the corporation, assumed responsibility for filing and payment of the State withholding taxes. (Transcript at 28) In July 1988 Rhoads filed late State withholding tax returns due for January 1988 and the State of Delaware, Division of Revenue ("Division of Revenue") subsequently assessed interest and late file penalties. In September 1988 Rhoads paid the assessed interest and protested the late file penalty citing the incompetence of its accountant Maloney as grounds for abatement. The penalty assessment was abated by the Division of Revenue in December 1988. (Transcript 14, 15, 18; Board Exhibit 1-A). The monthly returns required to be filed during

the period of February 1988 to August 1989 were filed late at various times between January 1989 to October 1989 with payments of the tax. The late filing came about as a conscious decision to use income taxes withheld from employees to meet other business obligations. (Transcript at 41 and 42). On each occasion the Division of Revenue assessed interest, a failure to file penalty and a negligence penalty. Rhoads paid the interest and protested the penalties to the Director of Revenue. The basis for the protests was that incompetence of its accountant, "Maloney" constituted reasonable cause for the failure to file the tax returns. The protests were denied by the Division of Revenue. (Transcript 14, 15, 18; Board Exhibits 1-A through 1F).

The late filing penalty is authorized under 30 Del. C. § 1194(a) which provides in pertinent part:

In case of failure to file any return required under this chapter on the date prescribed therefor . . . unless it can be shown that such failure is due to reasonable cause and not due to wilful neglect, there shall be added to the amount required to be shown as tax on such return . . . an additional 5% for each additional month . . . during which such failure continues, not exceeding 50% in the aggregate.

Subsection (b) of § 1194 imposes a separate penalty for non-payment of taxes, a matter not at issue here since Rhoads was not assessed a penalty for failure to pay the taxes due.

Although the terms "reasonable cause" and "willful neglect" are not specifically defined by statute, 30 Del. C. § 1101 provides that "[a]ny term used in this chapter shall have the same meaning as when used in a

comparable context in the laws of the United States referring to federal income taxes, unless a different meaning is clearly required." Accordingly, we look to federal law for interpretive guidance.

In United States v. Boyle, 469 U.S. 241 (1985), the Supreme Court considered the question whether an executor's agent's negligence amounted to reasonable cause sufficient to permit abatement of a late filing fee. The Court noted that, while determining the elements that constitute reasonable cause is a question of fact, the determination of what elements must be proven is a question of law. Id. at 249 n.8. The Court defined "reasonable cause" as that degree of care that requires "the taxpayer to demonstrate that he exercised 'ordinary business care and prudence' but nevertheless was unable to file the return within the prescribed time." Id. at 246 (quoting 26 C.F.R. § 301.6651(c)(1)(1984)) (emphasis added). The Supreme Court defined "willful neglect" to mean "a conscious, intentional failure or reckless indifference." Id. at 245. In applying these definitions to the facts before it, the Court established a "bright line rule" that reliance on an agent to timely file a tax return is not reasonable cause as a matter of law. Id. at 252.

Boyle's bright line standard was applied in another case involving a negligent employee. In Universal Concrete Products Corp. v. United States, E.D. Pa., 90-2 USTC (CCH) 50,440 (1990), aff'd., 3d Cir., 941 F.2d 1204 (1991), a taxpayer sought abatement of late filing penalties on the basis that the company controller misled the company into believing that its tax deadlines were being met. Although, as here, the taxpayer adequately supervised the controller and an independent accounting firm discerned no improper financial conduct on his part, the controller nonetheless failed to file the taxpayer's return in a timely manner. Citing Boyle, the court rejected the claim of reliance even though the corporation had not filed returns or made deposits during the employment of the controller. By contrast, in this case the non-filings occurred after the negligent employee had departed and his shortcomings discovered. Thereafter, Wooters decided not to make further filings.

Other federal decisions support the Director's contention that reasonable cause is limited to circumstances beyond the taxpayer's control. Daum Industries Inc. v. United States, D. Ida., 71-2 USTC (CCH) 9609 (1971) (corporate treasurer's decision to fund payroll rather than file employment tax return was imputed to corporate president and precluded

finding of reasonable cause despite president's claim that he was unaware of the non-filing); Leo Sanders v. Commissioner, 21 T.C. 1012 (1954), aff'd, 10th Cir., 225 F.2d 629, cert. den. 350 U.S. 976 (1956) (lack of funds to employ staff does not, as a matter of law, constitute reasonable cause for non-filing); Weiland v. Commissioner, 44 T.C.M. (CCH) 139 (1982) (taxpayer's claim that he was too busy trying to save a bankrupt company not sufficient cause to abate penalty for non-filing); Darrell Harris, Inc. v. United States, W.D. Okla., 770 F. Supp. 1492 (1991) (cash flow difficulties do not constitute reasonable cause not to file).

The Board's conclusion that the taxpayer's reliance on its errant accountant constitutes "reasonable cause" to permit abatement of the late filing penalties not only misapplies the legal test but lacks a factual predicate as well. No delinquent filings occurred while the accountant was employed at Rhoads from May to November 1987. In February, 1988, when Wooters assumed responsibility for the tax filings only the monthly filing for January 1988 was delinquent and the Director abated the late filing penalty attributed to that month when Rhoads requested an abatement. From February 1988 onward, Wooters was clearly on notice that current filings were delinquent but he apparently made a conscious decision to turn his attention elsewhere

in an effort to straighten out the Company's mishandled financial affairs. Wooters never claimed, and the Board did not find, that he lacked the ability to file a return, an independent step which could have been accomplished even without payment of the tax. Under the Boyle standard, in the absence of such inability, reasonable cause cannot be established. The Superior Court's ruling that the Board's decision was supported by substantial evidence merely compounded the error.

In failing to apply the correct standard for determining taxpayer excusal, the Board committed fundamental error. Since the stipulated evidence clearly shows that the taxpayer's explanation for failing to file in this case is not attributable to the requisite inability to comply with the filing obligation, reasonable cause within the meaning of 30 Del. C. § 1194(a) has not been demonstrated as a matter of law. Accordingly, the Superior Court's affirmance of the Board must be reversed.

The judgment of the Superior Court is REVERSED and this matter is REMANDED to the Superior Court with direction for FURTHER REMAND to the Board for the entry of a decision in favor of the Director.

State of Delaware

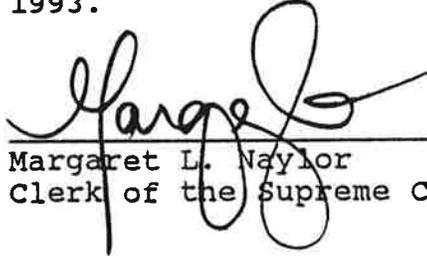
Kent County

}
} ss.
}

I, Margaret L. Naylor, Clerk of the Supreme Court of the State of Delaware, do hereby certify that the foregoing is a true and correct copy of the Opinion issued August 17, 1993, in Director of Revenue v. J.E. Rhoads & Sons, Inc., No. 561, 1992 as the same remains on file and of record in said Court.

IN TESTIMONY WHEREOF,

I have hereunto set my hand and affixed the seal of said Court at Dover this 2nd day of September A.D. 1993.



Margaret L. Naylor
Clerk of the Supreme Court

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Hearing
9/17/92

THE HEARING OFFICER: Off the record.
(Discussion off the record.)

THE HEARING OFFICER: The next matter before the Board is J.E. Rhoads, R-h-o-a-d-s, and Sons, Inc., Petitioners versus Director of Revenue. This is Docket Number 982.

This Board some time ago entered an order ruling in favor of the petitioner on this matter. That decision was appealed to the Superior Court and the Superior Court affirmed this Board's decision.

Subsequently that decision was appealed to the Supreme Court and the Supreme Court in Docket Number 561, 1992, rendered a decision reversing and remanding the case to the Superior Court who by order dated September 8, 1993 remanded

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ordered.
(Discussion off the record.)

MANDATE

THE SUPREME COURT OF THE STATE OF DELAWARE

To: Superior Court of the State of Delaware in and for New
Castle County:

GREETINGS:

WHEREAS, in the case of:

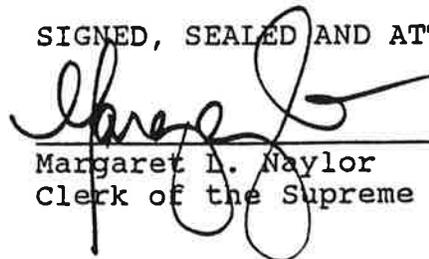
DIRECTOR OF REVENUE V. J.E. RHOADS & SONS, INC.
C.A. No. 92A-01-003

a certain judgment or order was entered on the 10th day of
November, 1992, to which reference is hereby made; and

WHEREAS, by appropriate proceedings the judgment or order
was duly appealed to this Court, and after consideration has
been finally determined, as appears from the opinion or order
of this Court filed on August 17, 1993, a certified copy of
which is attached hereto;

ON CONSIDERATION WHEREOF IT IS ORDERED AND ADJUDGED that
the judgment or order be and it is hereby reversed, with
costs, hereby taxed in the sum of ----- Dollars (\$000.00) to
be recovered by appellant against appellee with right of
execution; and the case is hereby remanded with instructions
to take such further proceedings therein as may be necessary
in conformity with the opinion or oder of this Court.

SIGNED, SEALED AND ATTESTED BY:



Margaret L. Naylor
Clerk of the Supreme Court

Issued: September 2, 1993
Supreme Court No. 561, 1992

14.

IN THE SUPERIOR COURT OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

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DIRECTOR OF REVENUE)	
)	
Respondent Below,)	
Appellant,)	
)	
V.)	C.A. No. 92A-01-003
)	
J.E. RHOADS & SONS, INC.,)	
)	
Petitioner Below,)	
Appellee.)	

ORDER

NOW, THIS 8th day of September, 1993 upon receipt of the opinion and mandate of the Supreme Court in the matter (copy attached), it is

ORDERED, that this case be and is **REMANDED** to the Delaware Tax Appeal Board for entry of a decision in favor of the Director of Revenue and denying abatement of penalties.



The Honorable Richard S. Gebelein

orig: Prothonotary
cc: Donald E. Gregory, Esquire
Mr. Kevin Wooters, President
J.E. Rhoads & Sons, Inc.

CERTIFIED AS A TRUE COPY:
ATTEST: SHARON AGNEW
PROTHONOTARY
BY Sharon T. Cleekwood

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IN THE SUPERIOR COURT OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

DIRECTOR OF REVENUE)	
)	
Respondent Below,)	
Appellant,)	
)	
v.)	C.A. No. 92A-01-003
)	
J.E. RHOADS & SONS, INC.,)	
)	
Petitioner Below,)	
Appellee.)	

Date Submitted: August 26, 1992
Date Decided: November 10, 1992

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MEMORANDUM OPINION

Upon appeal of a decision of the Tax Appeal Board. **AFFIRMED.**

Donald E. Gregory, Esquire, Deputy Attorney General, Division of Revenue, Wilmington, Delaware for the appellant.

Mr. Kevin Wooters, *pro se*, President, J.E. Rhoads & Sons, Inc.

GEBELEIN, Judge

This is an appeal from the Tax Appeal Board under 29 *Del.C.* § 10142. The Board, in a decision dated December 13, 1991, abated penalties assessed to taxpayer J.E. Rhoads & Sons, Inc. ("Rhoads") by the Director of Revenue ("Director") for late filing of withholding information. Director now appeals this abatement, contending that there was not substantial evidence to support the Board decision. For the reasons stated herein, the Board decision is AFFIRMED.

The Tax Appeal Board (the "Board") is specifically included within the Delaware Administrative Procedures Act (the "Act"), 29 *Del.C.* ch. 101.¹ Thus, the review procedure for Board decisions is set forth in 29 *Del.C.* § 10142.² Under the Act, the standard and scope

¹ 29 *Del.C.* § 10161 provides in relevant part:

§ 10161. State agencies affected.

This chapter shall apply only to the following agencies:

* * *

(6) Tax Appeal Board[.]

² 29 *Del.C.* § 10142 provides:

(a) Any party against whom a case decision has been decided may appeal such decision to the Court.

(b) The appeal shall be filed within 30 days of the day the notice of the decision was mailed.

(c) The appeal shall be on the record without a trial *de novo*. If the Court determines that the record is insufficient for its review, it shall remand the case to the agency for further proceedings on the record.

(d) The Court, when factual determinations are at issue, shall take due account of the experience and specialized competence of the agency and of the purposes of the basic law under which the

of this Court's review of Board decisions is limited to determining whether the Board's decision is supported by substantial evidence and whether the Board properly applied the relevant principles of law. *Talmo v. New Castle County*, Del. Super., 444 A.2d 298 (1972), *aff'd*, Del. Supr., 454 A.2d 758 (1972). In the absence of an error of law, the Court will not disturb a decision of the Board which is supported by substantial evidence. *Asplundh Tree Expert Co. v. Clark*, Del. Super., 369 A.2d 1084 (1975). Substantial evidence is more than a scintilla and less than a preponderance. *Olney v. Cooch*, Del. Supr., 425 A.2d 610, 614 (1981). It is the function of the Board, not of this Court, to resolve conflicts in testimony and issues of credibility, and to weigh the evidence presented. *Mooney v. Benson Management*, Del. Super., 451 A.2d 839 (1982). The Court may not substitute its own judgment for that of the Board on issues relating to the weight and credibility of the evidence. *Johnson v. Chrysler Corp.*, Del. Supr., 213 A.2d 64 (1965). In reviewing the record for substantial evidence, the Court will consider the record in the light most favorable to the party prevailing below. *GMC v. Guy*, Del. Super., C.A. No. 90A-JL-5, Gebelein, J. (August 16, 1991).

In the instant appeal, the Board clearly decided that the reasons given by Rhoads for its late payments were sufficient to meet the reasonable cause standard for abatement.³ The

agency has acted. The Court's review, in the absence of actual fraud, shall be limited to a determination of whether the agency's decision was supported by substantial evidence on the record before the agency.

³ 30 *Del.C.* § 1194 specifically provides that the penalties for failure to file and failure to pay taxes due would trigger specified penalties, "unless it is shown that such failure is due to reasonable cause and not due to willful neglect . . ."

determination that Rhoads had reasonable cause for its late filing is a finding of fact, which falls uniquely within the province of the Board.

The Director contends that the Board failed to set forth with sufficient specificity its reasons for reaching this conclusion. However, the Board decision clearly states the standard against which it measured Rhoads' conduct:

The Board feels that the taxpayers (sic) responsibilities are: 1) To attempt to hire competent people through interviewing techniques, researching personal references and looking at education and experience levels, 2) To request and receive regular feedback from the responsible individual and, (sic) 3) To employ outside experts where necessary to oversee the work of the employees. If a taxpayer takes these steps, that taxpayer is acting reasonably.

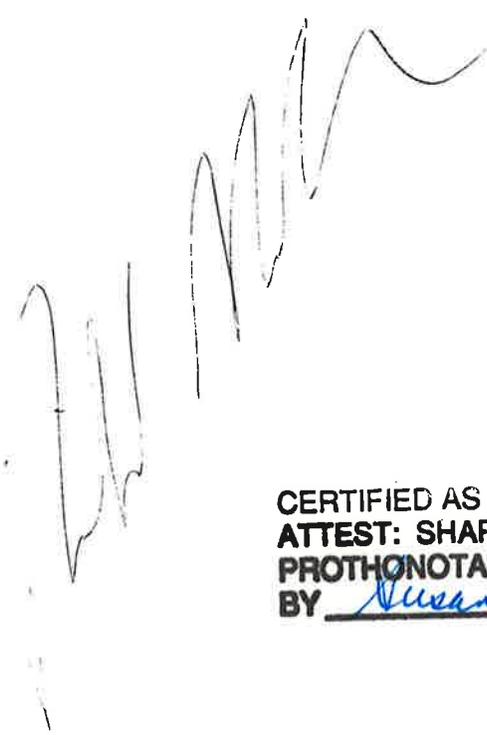
Board decision, at 2-3. The Board further states that Rhoads' conduct met this standard, and was therefore reasonable.

This Court believes that the Board applied the correct standard to the taxpayer's behavior in this instance. That being the case, the Court can look no further than the Board's determinations that Rhoads "regularly included the accountant in weekly staff meetings and discussed the state of the companies (sic) finances. . ." and that "the accountant deliberately withheld information or presented false or misleading information to the owners." Board decision at 3. These findings of fact were supported by the testimony before the Board of Kevin Wooters, President and Chief Executive Officer of Rhoads. As noted previously, the Court may not inquire into issues of credibility or weight of the evidence. The Board obviously found Mr.

Wooters' testimony credible, and this Court must accept that factual determination. For this reason, this Court must conclude that there was substantial evidence to support the Board's decision.

For these reasons, the decision of the Board is **AFFIRMED**.

IT IS SO ORDERED.



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ATTEST: SHARON AGNEW
PROTHONOTARY
BY Susan T. Fleewood