

Omnibus Tax Equity and Enforcement Act

On April 17, 1985, the Omnibus Tax Equity and Enforcement Act of 1985 was signed into law (Chapter 65) in an effort to attack the problem of tax evasion in New York State. Many of the provisions of this Act are aimed at strengthening and rendering more effective the criminal and civil penalties imposed on personal income tax evaders and delinquents. This TSB-M contains descriptions of the Act's new or amended personal income tax provisions.

I. Criminal Penalties

Criminal penalties applicable to the Personal Income Tax Law (many of which were previously contained in section 695 of the Tax Law, repealed by the Omnibus Act) have been codified in a new Article 37 of the Law (section references below are to sections of the Tax Law).

Article 37

Section 1800 - Defines these terms relating to personal income tax

Person - Includes but is not limited to an individual, partnership, corporation (including a dissolved corporation), association, trust or estate. It shall also include an officer, employee or agent of a corporation; a member, employee or agent of a partnership or association; an employee or agent of an individual proprietorship; an employee or agent of an estate or trust; or a fiduciary. (Section takes effect April 17, 1985.)

Felony and Misdemeanor - These terms have the same meaning as in the Penal Law. The disposition and the sentences imposed for these offenses are the same as under Penal Law except that the court may impose a fine not to exceed \$50,000 for a felony and \$10,000 for a misdemeanor. (Section takes effect April 17, 1985.)

Section 1801 - Any person who, with intent to evade payment of any tax imposed under Article 22 or any related income or earnings tax statute, fails to make, render, sign, certify or file any return or who fails to supply information within the required time, or who, with like intent, supplies false or fraudulent information shall be guilty of a misdemeanor. (Section takes effect November 1, 1985.)

Section 1802 - Any person who fails to file a return for three consecutive years with the intent to evade payment of tax shall be guilty of a class E felony. The person must have had an unpaid tax liability for each of these three taxable years. The term return shall not include a partnership return, information return, employer return or any declaration of estimated tax required under law. (Section takes effect November 1, 1985.)

Section 1804 - Any person who makes, renders, signs, certifies or files any false or fraudulent return, declaration or statement with the intent to evade tax shall be guilty of a misdemeanor.

Any person who files a false or fraudulent return and substantially understates his tax liability with the intent to evade tax shall be guilty of a class E felony. A substantial understatement is made when the tax required to be shown on the return exceeds the tax shown on the return by more than \$1,500 and the taxpayer intended to evade at least this amount of tax.

The term return shall not include a partnership return, information return, employer return or any declaration of estimated tax required under law. (Section takes effect November 1, 1985.)

Section 1806 - Any person who willfully fails to collect any withholding tax as required under law shall be guilty of a misdemeanor, in addition to any other penalties provided by law.

A person who has been required to withhold, and has withheld tax shall be considered to have acted in a fiduciary character, and the tax withheld is considered to have been entrusted to such person by the state or political subdivision of the state. Whenever a person willfully fails to pay over any withholding tax to the state or political subdivision, such person may be prosecuted under the Penal Law (e.g., under larceny provisions) in addition to being subject to any other penalties imposed under the law.

Whenever an employer fails to collect, truthfully account for, or pay withholding tax, or fails to file tax returns as required, the Tax Commission may serve a notice requiring the employer to collect the tax as required and deposit such tax in a bank approved by the Tax Commission, in a separate account, in trust for and payable to the Tax Commission, and to keep the tax in such account until it is paid to the Tax Commission. Failure to adhere to these rules shall make such person guilty of a misdemeanor. (Section takes effect November 1, 1985.)

Section 1807 - Any person who, with the intent that any tax or requirement of Article 22 (Personal Income Tax) or any related income or earnings tax statute be evaded, shall, for a fee or other compensation, aid or assist in, or procure, counsel, or advise the preparation or presentation of any income or earnings tax return, report, statement, declaration or other document which is fraudulent or false, or supplies any false or fraudulent information in connection with an income or earnings tax matter, shall be guilty of a misdemeanor. It is immaterial that the person required to file the return, report, etc. may have had knowledge of or consented to the falsity or fraud.

If such person under the above circumstances causes an understatement of tax liability on a return by more than \$1,500 by means of a scheme or plan, he shall be guilty of a class E felony. The term return shall not include a partnership return, information return, employer return or any declaration of estimated tax required under law. (Section takes effect November 1, 1985.)

Section 1809 - Any person who, in connection with any matter arising under Article 22, fails to obey a subpoena to attend as a witness or to produce books, accounts, records, memoranda, documents or other papers and fails or refuses to be sworn, refuses to answer any material and proper question or refuses after reasonable notice to produce books, accounts, etc., in his possession or under his control which constitute material and proper evidence, shall be guilty of a misdemeanor. (Section takes effect November 1, 1985.)

Section 1810 - Any person who fails to pay the tax under the Personal Income Tax Law with the intent to evade the tax or to evade any requirement under the Tax Law shall be guilty of a misdemeanor. (Section takes effect November 1, 1985.)

Section 1825 - Any person who violates the secrecy provisions of the Tax Law shall be guilty of a misdemeanor. (Section takes effect November 1, 1985.)

## II. Civil Penalties

The civil penalty sections and administrative sections of the Personal Income Tax Law, Article 22, have been amended as follows:

Section 651(b)(5) - Amends the innocent spouse provisions of the Tax Law by changing the basic criteria for application of these provisions from "a 25% omission of New York adjusted gross income" to "a substantial understatement of tax" provision.

A "substantial understatement" is defined as the excess of the tax required to be shown on the return for the taxable year over the amount of tax which is shown on the return (reduced by any rebate), which exceeds \$100. A rebate means so much of an abatement, credit, refund or other repayment (whether or not erroneous) made on the ground that amounts entering into the definition of a deficiency showed a balance in favor of the taxpayer.

The substantial understatement of tax must be attributable to grossly erroneous items of one spouse. The term "grossly erroneous" takes into account any item omitted from New York adjusted gross income and any claim of a New York deduction, exemption, credit or basis by the noninnocent spouse in any amount for which there is no basis in fact or law.

After taking into account all the facts and circumstances, it is found to be inequitable to hold the innocent spouse liable for the deficiency due to grossly erroneous items, the innocent spouse shall be relieved of liability for the tax, interest, penalties and other amounts attributable to the substantial understatement.

Where a substantial understatement is attributable to a New York deduction, exemption, credit, or basis for which there is no basis in fact or law, the following additional requirements must be met in order that the innocent spouse is afforded the protection of the innocent spouse provisions:

1) If the innocent spouse's New York adjusted gross income for the most recent taxable year ending before the date the deficiency notice is mailed is \$20,000 or less, the liability from the grossly erroneous items must be greater than 10% of adjusted gross income.

2) if the spouse's New York adjusted gross income for that year is more than \$20,000, then such liability must be greater than 25% of the adjusted gross income.

If the spouse is married to another spouse at the close of such year, the spouse's New York adjusted gross income shall include the New York adjusted gross income of the new spouse, whether or not they file a joint return. (Section takes effect April 17, 1985 and applies to notices of deficiency issued on or after April 17, 1985 and pending hearings and determinations or decisions of the Tax Commission which have not become final.)

Section 652 - Amended to eliminate the reference to "declaration" of estimated tax due to the repeal of sections 655 and 656 of the Tax Law. (Section takes effect April 17, 1985 and applies to taxable years beginning after December 31, 1985.)

Sections 653(a) and (c) - Amended to eliminate the reference to "declaration" of estimated tax due to the repeal of sections 655 and 656 of the Tax Law. (Sections take effect April 17, 1985 and apply to taxable years beginning after December 31, 1985.)

Sections 655 and 656 - These sections, which deal with "declarations of estimated tax" and "payments of estimated tax" respectively, have been repealed. (Sections take effect April 17, 1985 and apply to taxable years beginning after December 31, 1985.)

Section 657(a) - Amended to eliminate the reference to "declaration" of estimated tax due to the repeal of sections 655 and 656 of the Tax Law. (Section takes effect April 17, 1985 and applies to taxable years beginning after December 31, 1985.)

Section 682(c) - Amended to eliminate the reference to "under section 656" as section 656 has been repealed. (Section takes effect April 17, 1985 and applies to taxable years beginning after December 31, 1985.)

Section 684(b) - Amended to eliminate the reference to "under section 656" as section 656 has been repealed. (Section takes effect April 17, 1985 and applies to taxable years beginning after December 31, 1985.)

Section 685(a)(1) and (4) - These subsections have been amended to add a minimum penalty for failure to file a return within 60 days (including extensions) of the time prescribed for filing an income tax return. The penalty for failure to file a return remains at 5% a month not to exceed 25%.

However, when there is a failure to file within 60 days (including extensions) of the time prescribed for filing an income tax return, this penalty when computed may not be less than the lesser of \$100 or 100% of the amount required to be shown as tax on the return. The amount required to be shown on the return must be reduced by any tax paid on or before the date prescribed for payment and by any credit against tax which may be claimed on the return. It should be noted that there is no minimum penalty to be applied if there is no tax liability. (Sections take effect July 16, 1985 and apply to returns required to be filed, determined with regard to extensions, on or after such date.)

Section 685(b) - This section has been amended to include, in addition to the 5% negligence penalty, an additional penalty of 50% of the interest payable under section 684 (relating to an underpayment of tax) if a deficiency is due to negligence or an intentional disregard of the Personal Income Tax Law. The interest, figuring this new penalty, is computed from the due date for the payment of the tax, determined without regard to any extensions, to date of the assessment of the tax or the date of the payment of tax, whichever is earlier.

If any portion of the underpayment of tax is due to a failure to report dividends, patronage dividends or interest on the personal income tax return, the amount of that underpayment will be treated as due to negligence in the absence of clear and convincing evidence to the contrary. (Section takes effect July 16, 1985 and applies to taxes required to be paid, determined with regard to extensions, on or after such date.)

Section 685(c) - This subsection has been amended to eliminate the "specific" requirements to pay estimated tax, and since sections 655 and 656 were repealed, there is no longer a requirement to file a declaration of estimated tax. In their place is an addition to tax for not paying the required amount of estimated tax for each installment date - April 15, June 15, September 15 and January 15 of the succeeding tax year.

The penalty is based upon the difference between the required installment and the installment paid on or before the due date for such installment.

The required installment is the lesser of:

- A) 25% of the lesser of
    - 1) 80% of the tax shown on the return for the taxable year (or if no return is filed, 80% of the tax for such year) or
    - 2) 100% of the tax shown on the return for the preceding taxable year, provided the individual filed a return for such year and such year was a taxable year of 12 months;
- or

B) Annualized income installment - which is the placing of taxable income and minimum taxable income on an annualized basis for the months in the taxable year ending before the due date of the required installment. Compute the tax on that amount and multiply the tax by the applicable percentage as - 20% for the 1st installment, 40% for the 2nd installment, 60% for the 3rd installment and 80% for the 4th installment. The next step would then be to subtract any prior installment payments made for that taxable year from the "tax multiplied by the applicable percentage."

When the above computation yields the annualized income installment as the required amount for any one installment due date, the next installment payment must be increased by the difference between the installment amount using the current or prior year's tax and the payment made using the annualized income method.

As under the old law, withholding tax paid during the year is still deemed as four equal amounts applied as payments against each of the four required installments of estimated tax, unless the taxpayer proves otherwise.

Also, if the taxpayer files a return and pays the tax in full on or before January 31 of the subsequent taxable year, the fourth installment of estimated tax need not be paid.

In the case of farmers and fishermen (including oyster farmers), there is only one required installment of estimated tax, due on January 15 of the succeeding taxable year. However, if a farmer or fisherman files his return and pays the tax in full on or before March 1 of the succeeding taxable year, the required installment of estimated tax need not be paid. The required annual installment for a farmer or fisherman is computed by substituting 66 2/3% for 80% in section 685(c)(3). An individual is deemed to be a farmer or fisherman if the individual's New York adjusted gross income from farming or fishing for the taxable year is at least 2/3 of the total New York adjusted gross income from all sources for the taxable year or if such individual's New York adjusted gross income from farming or fishing shown on the return of the individual for the preceding taxable year is at least 2/3 of the total New York adjusted gross income from all sources shown on such return.

The laws regarding husband and wife joint estimated tax, fiscal year filers and short taxable years which were previously found under repealed sections 655 and 656 have remained the same and can now be found under section 685(c). (Section takes effect April 17, 1985 and applies to taxable years beginning after December 31, 1985.)

Section 685(d) - This subsection has been amended to create the following new exceptions to the addition to tax required for failure to pay estimated income tax. The four exceptions are:

- 1) if the tax shown on the return for the taxable year or, if no return is filed, the tax, reduced by credits including the credit for tax withheld, is less than \$100, no penalty will be imposed for that year.
- 2) if the preceding taxable year was a taxable year of twelve months, and no tax liability was incurred for such year, and throughout that year the individual was a resident of New York State or a nonresident who had New York adjusted gross income, no penalty will be imposed for that year.
- 3) if there is an installment due on or after an individual's death, no penalty will be imposed with respect to such installment.
- 4) waivers in certain cases -
  - a) if the Tax Commission determines that due to a casualty, disaster or other unusual circumstances, the penalty would be against equity and good conscience, no penalty will be imposed with respect to any related underpayment.
  - b) if the Tax Commission determines that in the taxable year that estimated tax payments were required to be made or in the tax year preceding such taxable year, the taxpayer retired after becoming 62 years old or became disabled and that such underpayment of estimated tax was due to reasonable cause and not to willful neglect, no penalty will be imposed with respect to any related underpayment. (Section takes effect April 17, 1985 and applies to taxable years beginning after December 31, 1985. However, exception 4 above applies to underpayments for taxable years beginning in 1984.)

Section 685(e) - This subsection has been amended to include, in addition to the 50% fraud penalty, an additional penalty of 50% of the interest payable under section 684 (relating to an underpayment of tax) when an understatement of tax is due to fraud. The interest, in figuring this new penalty, is computed from the due date for the payment of the tax, determined without regard to any extensions, to the date of the assessment of the tax or the date of the payment of tax, whichever is earlier. (Section takes effect July 16, 1985 and applies to taxes required to be paid, determined with regard to extensions, on or after such date.)

Section 685(h) - This subsection has been amended to increase the penalty, for failure to file information returns, from \$1 to \$50 for each statement not filed. The total amount to be imposed on the delinquent person for all such failures during any calendar year is increased from \$1,000 to \$10,000.

Also, the penalty under this section, for failing to file a partnership or an S corporation return or failure to show required information on such returns, has been increased from \$20 to \$50 per partner or shareholder per month (up to a maximum of 5 months).

In addition, this section now includes a new penalty regarding professional corporations. If a professional corporation, which is organized under Article 15 of the Business Corporation Law, or authorized to do business in New York State under Article 15-a of such Law, fails to file a return, as prescribed, determined with regard to extensions of time to file, under section 658(f) of the Personal Income Tax Law, a penalty will be due. The penalty, due from the professional corporation, is computed by multiplying the number of information returns not filed by \$100 for every month (or fraction thereof) during which the failure to file the returns continues (up to a maximum of 5 months).

The penalties under this section are not applicable where it can be shown that a failure was due to reasonable cause and not due to willful neglect. (Section takes effect July 16, 1985 and applies to returns required to be filed, determined with regard to extensions, on or after such date.

Section 685(i) - This subsection has been amended to eliminate the reference to "declaration of estimated tax" due to the repeal of sections 655 and 656 of the Tax Law. (Section takes effect April 17, 1985 and applies to taxable years beginning after December 31, 1985.)

Section 685(k) - This subsection has been amended to raise the penalty from \$5 to \$50 for each failure to:

- 1) furnish identifying number to another person, or
- 2) include in any return, statement or other document made with respect to another person the identifying number of such other person.

The penalty for failure to include one's own identifying number in any return, statement or other document remains at \$5.

The total amount of penalty imposed on any person in any calendar year may not exceed \$10,000 for the above mentioned failures. Also, the penalty will not be imposed where a failure is due to reasonable cause and not due to willful neglect. (Section takes effect July 16, 1985 and applies to failures occurring on or after such date.)

Section 685(1) - This subsection has been amended to add new sections 685(q), (r) and (s) to that list of sections which do not come under the notice of deficiency provisions (section 681) of the Tax Law. (Section takes effect July 16, 1985.)

Section 685(n) - This subsection, which defines the word "person" under the Personal Income Tax Law, was amended to add new sections 685(q) and (r) to the list of sections which refer to the word "person" for Tax Law purposes. (Section takes effect July 16, 1985.)

Section 685(p) - This new subsection imposes a penalty at the rate of 10% of the amount of an underpayment which is attributable to a substantial understatement of income tax. There is a substantial understatement when the amount of understatement for the taxable year exceeds the greater of 10% of the tax required to be shown on the return for the taxable year or \$2,000.

The term "understatement" is defined as the excess of the tax required to be shown on the return for the taxable year over the amount of tax which is shown on the return (reduced by any rebate). A rebate means so much of an abatement, credit, refund or other repayment (whether or not erroneous) made on the ground that amounts entering into the definition of a deficiency showed a balance in favor of the taxpayer. This understatement, however, may be reduced by that portion of the understatement which is attributable to:

- a) the tax treatment of any item by the taxpayer if there is or was substantial authority for such treatment.
- b) any item with respect to which the relevant facts affecting the item's tax treatment are adequately disclosed in the return or in a statement attached to the return.

If the taxpayer can show that there was reasonable cause for the understatement (or a portion thereof) and that he acted in good faith, the Tax Commission may waive all or part of the penalty. (Section takes effect July 16, 1985 and applies to returns required to be filed, determined with regard to extensions, on or after such date.)

Section 685(q) - This new subsection imposes a penalty not exceeding \$500 for filing a frivolous tax return. A return is frivolous when:

- 1) it does not contain information on which the substantial correctness of the self-assessment may be judged, or
- 2) contains information that on its face indicates that the self-assessment is substantially incorrect,

and

such conduct is due to a position which is frivolous or an intent (which appears on the tax return) to delay or impede the administration of Article 22. This penalty is in addition to any other penalty provided by law. (Section takes effect July 16, 1985 and applies to returns required to be filed, determined with regard to extensions, on or after such date.

Section 685(r) - This new subsection imposes a penalty not exceeding \$1,000, on persons who intend tax to be evaded, and aid or assist in giving of fraudulent returns, reports, statements or other documents.

The penalty will be imposed upon any person who, for a fee or other compensation or as an incident to the performance of other services for which such person receives compensation, shall:

- 1) aid or assist in or procure, counsel or advise the preparation or presentation under or in connection with any matter arising under the Personal Income Tax Law of any return, report, declaration, statement or other document which is fraudulent or false as to any material matter, or
- 2) supply any false or fraudulent information.

It is immaterial whether the fraud is with the knowledge or consent of the person authorized or required to present such return, report, declaration, statement or other document. (Section takes effect July 16, 1985.)

Section 685(s) - This new subsection imposes a penalty of \$500 per statement when an individual makes a statement which decreases income tax withholding amounts where there was no reasonable basis for making such a statement. The penalty must be waived by the Tax Commission if the individual's personal income tax liability is equal to or less than his credits (including withholding tax and payments of estimated tax) allowed against such income tax liability. The penalty is in addition to any criminal penalty which may be imposed by law. (Section takes effect July 16, 1985.)

Section 686(e) - This subsection has been amended to eliminate the reference to "whether or not claimed as a credit in the declaration of estimated tax for such succeeding taxable year" due to the repeal of sections 655 and 656 of the Tax Law. (Section takes effect April 17, 1985 and applies to taxable years beginning after December 31, 1985.)

Section 689(e) - This subsection was amended to add new sections 685(q) and (r) to that list of instances where the "burden of proof" would be placed upon the Tax Commission rather than the taxpayer. (Section takes effect July 16, 1985.)

Section 691 - The heading of this section was changed to add the word "miscellaneous." (Section takes effect April 17, 1985.)

Section 691(a) - This subsection was amended to eliminate the reference to "declaration of estimated tax" due to the repeal of sections 655 and 656 of the Tax Law. (Section takes effect April 17, 1985 and applies to taxable years beginning after December 31, 1985.)

Section 691(d) - This new subsection provides that certification by the Tax Commission that personal income tax has not been paid, that a return has not been filed or that information has not been submitted, as required by or under the Personal Income Tax Law, will be prima facie evidence that such has not been done. (Section takes effect April 17, 1985.)

Section 691(e) - This new subsection allows the Attorney General concurrent jurisdiction with any district attorney in the prosecution of Article 37 offenses with respect to personal income taxes. (Section takes effect April 17, 1985.)

Sections 692(d) and 692(f) - These subsections have been amended to make technical changes regarding warrants and liens. To create a lien on real and personal property, warrants are required to be filed in the office of the County Clerk. This amendment requires warrants to be filed also in the Department of State in order to create a lien on personal property. (Sections take effect July 16, 1985.)

Section 695 - This section, which deals with criminal penalties, has been repealed. A new section 695 is now cross-referenced to Article 37 for criminal penalties. (Section takes effect November 1, 1985 and applies to all offenses committed on or after that date.)

Section 697(b)(2) - This new subsection gives the Tax Commission power to investigate any offense dealing with administration or enforcement of the Personal Income Tax Law for the purpose of ascertaining the correctness of any return or for the purpose of making an estimate of taxable income of any person. Investigations by the Tax Commission may not continue after the referral of a case to the Attorney General, a district attorney or any prosecutorial agency. (Section takes effect November 1, 1985 and applies to all offenses committed on or after that date.)

Section 697(i) - This subsection has been amended to eliminate the reference to "declaration and" of estimated tax, due to the repeal of sections 655 and 656 of the Tax Law. (Section takes effect April 17, 1985 and applies to taxable years beginning after December 31, 1985.)

Amendments, where required, have been similarly made to the Administrative Code of the City of New York, the General City Law and the Code and Ordinances of the City of Yonkers.