

Howard v. United States: Who Should Be Responsible for the 100 Percent Penalty?

I. INTRODUCTION

Every bookkeeper who has check signing authority for a corporation of any size is potentially liable for a penalty of 100 percent of the corporation's unpaid withholding tax liability. A great many bookkeepers are probably not aware of that possibility.

A number of courts have relied upon dicta in *Howard v. United States*¹ to extend liability for the 100 percent penalty of Internal Revenue Code (I.R.C.) section 6672² to corporate employees who were not even responsible for paying the corporation's withholding taxes.³ The problem with this result is that it penalizes employees responsible for paying other creditors of the corporation, rather than employees responsible for paying the taxes owed by the corporation.

The 100 percent penalty provision of I.R.C. section 6672 imposes a penalty that can far exceed the maximum criminal penalties for fraud or tax evasion. For this reason, the Internal Revenue Service (I.R.S.) should only assess the 100 percent penalty against persons who are clearly liable for the penalty. The maximum criminal penalty for tax fraud or evasion is generally 100,000 dollars,⁴ whereas liability under the 100 percent

1. *Howard v. United States*, 711 F.2d 729 (5th Cir. 1983). See *infra* text accompanying notes 53-54.

2. I.R.C. § 6672 (West 1988). See *infra* note 7 and accompanying text.

3. See *infra* notes 61-67 and accompanying text. Since a corporation is an entity that is responsible for paying its own taxes, in the context of the 100% penalty, the issue is actually which persons are responsible for seeing that the corporation pays its withholding taxes. This Note will use a shorthand description for this fact by simply referring to such people as persons responsible for paying the corporation's taxes. The *Howard* dicta allows a court to find such a person responsible on proof that the person was responsible for paying other creditors of the corporation, without ever reaching the issue of whether that person was responsible for paying the taxes. *Howard*, 711 F.2d at 734. The problem with the dicta is that in some cases those two responsibilities may not be equivalent.

4. I.R.C. § 7201-7203 (West 1988). The maximum criminal penalties for tax fraud or tax evasion for an individual are \$100,000 in fines, five years imprisonment, or both, together with costs of prosecution. Establishing criminal liability requires proof beyond a reasonable doubt of a specific intent to defraud the government. In contrast, as interpreted by courts such as the *Howard* court, the 100% penalty requires only a preponderance of the evidence establishing that the "responsible" person knew of the

penalty provision is unlimited and has been imposed in excess of 989,000 dollars.⁵ As Justice Rehnquist said in his dissent in *United States v. Sotelo*, the 100 percent penalty provision "imposes a potentially crushing liability on corporate officials—a liability that is nondischargeable (in bankruptcy) in its entirety and virtually in perpetuity."⁶

This Note will discuss section 6672, including its purpose, history, and specific requirements. This Note will then discuss the *Howard* case and analyze it in terms of the problems associated with section 6672. In conclusion, this Note will suggest solutions to these problems, including a new test for determining who should be responsible for the 100 percent penalty.

II. SECTION 6672

I.R.C. section 6672, the 100 percent penalty provision, provides in part:

(a) Any person required to collect, truthfully account for, and pay over any tax imposed by this title who willfully fails to collect such tax, or truthfully account for and pay over such tax, or willfully attempts in any manner to evade or defeat such tax or the payment thereof, shall, in addition to other penalties provided by law, be liable to a penalty equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over.⁷

This penalty is most frequently assessed when federal taxes withheld from employees' wages have not been paid to

unpaid corporate taxes and paid a creditor in preference to the government. See Moran, *Willfulness: The Inner Sanctum or Unnecessary Element of Section 6672*, 11 U. TOL. L. REV. 709, 714-15, 753-54 n.151 (1980) [hereinafter Moran].

5. *Simpson v. United States*, 664 F. Supp. 43, 45 (E.D.N.Y. 1987).

6. *United States v. Sotelo*, 436 U.S. 268, 290 (1978) (Rehnquist, J., dissenting). The *Sotelo* majority held that the 100% penalty was not dischargeable in bankruptcy. *Id.* at 282. Justice Rehnquist went on to say:

While the lifelong liability which the Court imposes today falls on the shoulders of one who was the chief executive officer of a small family business, there is unfortunately nothing in the Court's reasoning which would prevent the same liability from surviving bankruptcy in the case of a comptroller, accountant, or bookkeeper who reaped none of the fruits of entrepreneurial success other than continued employment in the corporation and in some cases possibly not even that.

Id. at 290-91.

7. Section 6672(a) states further that "[n]o penalty shall be imposed under § 6653 for any offense to which this section is applicable." Section 6672(b) provides rules for the posting of a bond to extend the period of collection of the penalty in order for the taxpayer to bring a suit to challenge the assessment of the penalty.

the I.R.S. by the employer. "Person," as used in section 6672, is defined by section 6671 of the I.R.C. to include "an officer or employee of a corporation, or a member or employee of a partnership, who as such officer, employee, or member is under a duty to perform the act in respect of which the violation occurs."⁸ Courts have generally held that two separate requirements must be met for a person to be held subject to the 100 percent penalty.⁹ First, the person must be a "responsible person," that is, the person must be under a duty to collect, truthfully account for, and pay over the taxes.¹⁰ Second, the person must have willfully failed "to collect, truthfully account for, and pay over the tax."¹¹

A. Purpose of Section 6672

The Supreme Court has stated that the purpose of section 6672 is to assure compliance by the employer with its duty to pay such taxes by subjecting the employer's officials responsible for the employer's decisions regarding withholding and payment to a severe penalty.¹² The I.R.C. requires employers to withhold social security and income taxes from employees' wages.¹³ Once these taxes are withheld, the I.R.S. credits the amounts withheld as paid by the employees whether or not the taxes are ever paid to the I.R.S. by the employer.¹⁴ The I.R.S. may have to refund some of these taxes to individual employee taxpayers, even though the taxes have never been paid to the I.R.S. by the employer. Although the penalty applies to any tax collected by a third party for the government, most actions under section 6672 are for failure by the employer to pay over employee taxes that have been withheld.¹⁵

8. I.R.C. § 6671(b) (West 1988).

9. See, e.g., *Godfrey v. United States*, 748 F.2d 1568, 1574 (Fed. Cir. 1984).

10. *Id.* In *Slodov v. United States*, 436 U.S. 238, 250 (1978), the Court held that the phrase "'[a]ny person required to collect, truthfully account for, and pay over any tax imposed by this title' was meant to limit § 6672 to persons responsible for collection of third-party taxes, [such as withholding taxes,] and was not meant to limit it to those persons in a position to perform all three of the enumerated duties, that is, collection, accounting for, and paying the taxes." This Note will use phrases such as "person responsible to pay the taxes" as a shorthand for a person who is responsible for any one of the three enumerated duties.

11. I.R.C. § 6672(a) (West 1988); *Godfrey*, 748 F.2d at 1574.

12. *Slodov*, 436 U.S. at 247.

13. I.R.C. § § 3102(a), 3402(a) (West 1988).

14. *Slodov*, 436 U.S. at 243.

15. See, e.g., *id.* at 240-41; *Godfrey*, 748 F.2d at 1572-73; *Howard v. United States*, 711 F.2d 729, 731-33 (5th Cir. 1983).

The legislative history of section 6672 does not shed a great deal of light on the congressional intent behind the statute, however, the fact that the statute first appeared as part of a criminal statute is significant. That criminal statute was section 1308 of the Revenue Act of 1918, which imposed a 100 percent penalty on any "person who willfully refuses to pay, collect or truly account for and pay over" any excise tax.¹⁶ Section 1308 also provided for criminal penalties and the 100 percent penalty could be imposed in addition to the criminal penalties.¹⁷

Subsequent acts made changes in numbering and minor changes in wording.¹⁸ The Social Security Act of 1935 incorporated all of the penalties for excise taxes and made them applicable to social security taxes.¹⁹ The Current Tax Payment Act of 1943, which provided for withholding of income taxes, incorporated the social security penalties, and thus, by double incorporation, the 100 percent penalty had become applicable to withholding of social security and income taxes.²⁰ Up to this point in the evolution of section 6672, the 100 percent penalty remained a part of the criminal provisions.²¹

In 1954, Congress attempted to reorganize the I.R.C. to provide a more logical arrangement.²² In this rearrangement, Congress severed the 100 percent penalty from the other crimi-

16. Revenue Act of 1918, ch. 18, § 1308, 40 Stat. 1057, 1143, which provides in part: Any person who willfully refuses to pay, collect, or truly account for and pay over any such tax shall in addition to other penalties provided by law be liable to a penalty of the amount of the tax evaded, or not paid, collected, or accounted for and paid over.

17. *Id.*

18. For example, Revenue Act of 1924, ch. 234, § 1017(d), 43 Stat. 253, changed "refuses" to "fails" and extended the 100% penalty to a willful attempt to evade or defeat the tax or its payment, and Revenue Act of 1926, ch. 27, 44 Stat. 9, 116-17, changed the numbering of the 100% penalty statute to § 1114(d).

19. Act of Aug. 14, 1935, ch. 531, § 807(c), 49 Stat. 620, 638.

20. Current Tax Payment Act of 1943, Pub. L. No. 68, ch. 120 § 1627, 57 Stat. 126. Since the 100% penalty was made applicable to the collection of withholding taxes by incorporation from previous statutes, the congressional committee reports do not comment on the purpose of the penalty. See COMMENT BY COMMITTEE OF CONFERENCE, H.R. REP. NO. 510, 78th Cong., 1st Sess., *reprinted in* U.S. CODE CONG. SERVICE 2-56 (1943).

21. See Moran, *supra* note 4, at 748-50.

22. H.R. REP. NO. 1337, 83rd Cong., 2d Sess., *reprinted in* U.S. CODE CONG. & ADMIN. NEWS 4025-26 (1954); S. REP. NO. 1622, 83rd Cong., 2d Sess. *reprinted in* U.S. CONG. & ADMIN. NEWS 4629, 4629-30 (1954). Although both the House and Senate reports described the 100% penalty, neither report commented on the purpose of the penalty. HOUSE REPORT, *supra*, at 4568; SENATE REPORT, *supra*, at 5245.

nal provisions because it did not provide for imprisonment.²³ It was at this time that the 100 percent penalty was numbered as section 6672 and placed in the code along with other sections imposing civil penalties.

Although the legislative history of section 6672 says little about the congressional intent with regard to its interpretation, it is at least clear from the history of the statute that it was originally intended as a criminal sanction.²⁴ In this regard, the construction of specific terms within the statute such as "willfully" should be similar to the construction of such terms in other criminal statutes.²⁵ As will be discussed below, this has not always been the way such terms have been construed by the courts. In fact, most courts that have addressed the purpose behind section 6672 have assumed that the purpose is as stated in the Internal Revenue Manual:

To encourage prompt payment of withheld and other collected taxes as provided by law, and to insure ultimate collection of such taxes from a secondary source in any event, Congress enacted IRC 6672.²⁶

The original nature of section 6672 as a criminal sanction has been lost, and the courts have instead described the statute as an alternate collection device.²⁷ As stated in *Newsome v. United States*: "[s]ection 6672's 'basic purpose is the protection of government revenue.'"²⁸ However, in light of the original nature of section 6672 as a criminal sanction, the Supreme Court was more accurate in its statement that the purpose of

23. See Moran, *supra* note 4, at 748-50. Professor Moran notes that since neither the House nor the Senate Reports expressed an intent to change the meaning of the 100% penalty, the separation of the penalty from the criminal provisions was in substance an unconscious separation, effected through a procedural rearrangement of the tax code. Prior to the 1954 rearrangement, 100% penalty provisions were found at § 1718(c) (regarding admissions and dues), § 1921(a)(3) (regarding taxes on documents, other instruments, and playing cards), § 2557(b)(4) (regarding taxes on narcotics), and 2707(a) (regarding taxes on pistols and revolvers). All of these 100% penalty provisions were subsections of provisions that generally provided criminal penalties for fraud and tax evasion. See Internal Revenue Code of 1939, PUB. L. NO. 1, ch. 2 § § 1718, 1921, 2557, 2707, 53 Stat. 1, 193, 202, 274-76, 290.

24. See Moran, *supra* note 4, at 723-54.

25. *Id.* at 751-54.

26. INTERNAL REVENUE MANUAL, pt. V, § 711(1) (1987).

27. See *supra* text accompanying notes 24-26. Section 6672 is a civil penalty, not a criminal penalty. INTERNAL REVENUE MANUAL, pt. V, § 711(1) (1987).

28. *Newsome v. United States*, 431 F.2d 742, 745 (5th Cir. 1970) (quoting *Monday v. United States*, 421 F.2d 1210, 1216 (7th Cir.), *cert. denied*, 400 U.S. 821 (1970)).

section 6672 is to assure that the duty to pay taxes is fulfilled.²⁹

B. *The Requirements for Section 6672 Liability*

1. "Responsible Person"

The first requirement for liability under section 6672 is that the taxpayer must be a "responsible person." A responsible person,³⁰ as defined by section 6671, includes an officer or an employee of a corporation, among other persons.³¹ The use of the term "includes" in section 6671 has generally been found to be significant in that the persons listed under the statute are not construed to exclude all others.³² On the other hand, holding a corporate office does not necessarily make the officeholder a responsible person.³³ The overwhelming weight of authority indicates that a responsible person must have the power to control the decision-making process by which funds are allocated to other creditors in preference to paying taxes that are due.³⁴

The courts generally look to factors like check signing authority, day-to-day management of the company, and control of voting stock as indicators of who has the power to control the allocation of funds.³⁵ For example, in *Godfrey v. United States*, the Federal Circuit Court found that a chairman of the board of directors did not have the power to control the allocation of funds because he was an outside director with no signif-

29. *Slodov v. United States*, 436 U.S. 238, 247 (1978).

30. The shorthand phrase "responsible person" has been used in cases decided under § 6672 to refer to a "person required to collect, truthfully account for, and pay over any tax imposed by this title." See *Slodov*, 436 U.S. at 246 n.7.

31. I.R.C. § 6671(b) (West 1988), which provides:

The term "person," as used in this subchapter, includes an officer or employee of a corporation, or a member or employee of a partnership, who as such officer, employee, or member is under a duty to perform the act in respect of which the violation occurs.

32. See *Commonwealth Nat'l Bank of Dallas v. United States*, 665 F.2d, 743, 750-51 (5th Cir. 1982). In that case, the court held that a corporate employer's lending bank or an officer of that bank may be responsible persons if either "could effectively determine how [the corporation's] funds were to be spent and which bills would or would not be paid and when." *Id.* at 755.

33. *Dudley v. United States*, 428 F.2d 1196, 1201 (9th Cir. 1970). Although *Dudley* held the office of president of a corporation that failed to pay its withholding taxes, he was not liable for the penalty because he had no knowledge of the failure to pay the taxes until after he no longer had significant control over the corporation.

34. *Godfrey v. United States*, 748 F.2d 1568, 1575 (Fed. Cir. 1984). See, e.g., *Calderone v. United States*, 799 F.2d 254, 261 (6th Cir. 1986); *Haffa v. United States*, 516 F.2d 931, 936 (7th Cir. 1975); *White v. United States*, 372 F.2d 513, 516 (Ct. Cl. 1967).

35. *Godfrey*, 748 F.2d at 1576.

icant voting stock, no check signing authority, and no involvement in the day-to-day management of the corporation.³⁶ He was therefore not liable for the 100 percent penalty.³⁷

2. "Willfulness"

The second requirement for liability under section 6672 is that the responsible person acted "willfully." The test for willfulness was established by the Ninth Circuit Court of Appeals in *Bloom v. United States*.³⁸ For a person to be found to have acted willfully within the meaning of the statute, that person must have performed a "voluntary, conscious and intentional act to prefer other creditors . . . over the United States."³⁹ In *Bloom*, the court found that payments on a bank loan and payments of net wages to employees made while taxes were owing amounted to a willful failure to pay over the taxes.⁴⁰

A willful act can certainly be described as a voluntary, conscious, and intentional act. However, as pointed out by Professor Moran of the University of Toledo College of Law in his article on section 6672 willfulness, the test should be applied to the obligation of paying the taxes, not to the interim question

36. *Id.* Godfrey was an attorney with tax expertise who was elected as chairman of the board of Career Academics, Inc. He accepted the chair to provide consultation and advice concerning Career's financial and personnel problems. Godfrey was essentially an outside director with no power to control the allocation of funds, no check signing authority, and no involvement in the day-to-day management of the corporation. *Id.* at 1571. The court found that he was not a responsible person because he had no control over the allocation of funds. *Id.* at 1576. There was no evidence to show that Godfrey knew of the failure to pay taxes that led to the imposition of the 100% penalty, and therefore the court also found that the failure to pay the taxes was not willful on his part. *Id.* at 1577-78.

37. *Id.* at 1579.

38. *Bloom v. United States*, 272 F.2d 215, 233 (9th Cir. 1959), *cert. denied*, 363 U.S. 803 (1960).

39. This Note will hereinafter refer to this test as the "*Bloom* test," i.e., an act to prefer other creditors over the government with knowledge that taxes are due establishes willfulness. *Id.*

40. *Id.* at 218, 223. Bloom was the president and chief executive officer of Idaho Smelting, Inc., and virtually its sole stockholder. Bloom argued that he was prevented from paying the taxes by the corporation's financing bank, but the court found that the evidence did not support that argument. Instead, the court held that Bloom's voluntary, conscious, and intentional acts to prefer other creditors over the government established that he had acted willfully in not paying the taxes.

Bloom concerned taxes from 1947-48, prior to the 1954 Code, which placed the 100% penalty provision at § 6672. See *supra* notes 22-23 and accompanying text. Bloom's penalty was therefore assessed under § 2707(a), a 100% penalty provision that was applicable to social security taxes and income tax withholding through § § 1400 and 1627. *Bloom*, 272 F.2d at 217.

of whether payment to other creditors was voluntary, conscious, and intentional.⁴¹ It does not necessarily follow that a taxpayer who pays another creditor intends not to pay taxes. Nevertheless, the *Bloom* test is currently applied by most courts. In recent cases, courts have held that the *Bloom* test allows for a finding of willfulness as a matter of law.⁴²

However, a question definitely has arisen about whether the *Bloom* test has any validity after the decision of the Supreme Court in *Slodov v. United States*, in which Justice Brennan's majority opinion stated that "[t]he fact that the provision imposes a 'penalty' and is violated only by a 'willful failure' is itself strong evidence that it was not intended to impose liability without personal fault."⁴³ *Slodov* involved a taxpayer who assumed control of a financially troubled corporation that had no funds to pay past due taxes. The Court held that *Slodov* did not willfully fail to pay the taxes that had accrued prior to his assumption of control by using after-acquired funds to pay other creditors.⁴⁴ *Slodov* had paid other creditors while taxes were due, which would have been enough to establish liability under the *Bloom* test. However, he had no personal fault in the failure to pay the taxes when they were originally due.

The possibility that *Slodov* may have invalidated the *Bloom* test was first considered by the court in *In re Osborn*.⁴⁵

41. Moran, *supra* note 4, at 770. Professor Moran points out that although the payment of other creditors while taxes are due is evidence of an intentional failure to pay the taxes, it is far from being conclusive evidence of such an intent. See *infra* notes 84-87 and accompanying text for examples of instances in which other creditors might be paid without an intentional failure to pay the taxes.

42. See, e.g., *Howard v. United States*, 711 F.2d 729, 735 (5th Cir. 1983); *Mazo v. United States*, 591 F.2d 1151, 1157 (5th Cir. 1979), *cert. denied*, 444 U.S. 842 (1979).

43. *Slodov v. United States*, 436 U.S. 238, 254 (1978). Mr. *Slodov*, an orthodontist, purchased the stock of three corporations engaged in food vending. At the time of the purchase, the corporations owed about \$250,000 in taxes withheld from employee wages, and the corporations had no funds with which to pay the taxes. *Slodov* did not use any of the funds that the corporations acquired after the purchase to pay these taxes, and within six months of the purchase, the corporations filed for bankruptcy. The Court held that *Slodov* was not liable for the 100% penalty for the taxes that accrued before his purchase of the corporations because he had no personal fault in not paying the taxes when they were originally due.

44. *Id.* at 259-260.

45. 4 Bankr. 431, 436 (Bankr. W.D. Mo. 1979). Mr. and Mrs. *Osborn* were sole stockholders and managing officers of two corporations that had declared bankruptcy while withholding taxes were still outstanding. Because of previous problems, Mr. *Osborn* had promised the I.R.S. that he would deposit gross payrolls in a separate bank account and then pay only the net wages out of that account, leaving the withholding taxes in trust for the government. He failed to keep that promise and paid operating

However, because the *Osborn* court held the taxpayer's conduct to have been willful under either the *Bloom* test or the *Slodov* test, the court did not reach a conclusion on the issue.⁴⁶ The court in *Feist v. United States* stated that under *Slodov*, the *Bloom* test could not be applied to the exclusion of other evidence bearing on the personal fault of the taxpayer.⁴⁷ That *Slodov* had made personal fault a necessary element of willfulness was fully recognized by the Federal Circuit Court in *Godfrey*.⁴⁸ Professor Vasek of the University of Kentucky, in his article on section 6672, points out that the dissent in *Slodov* interpreted the majority opinion as rejecting the *Bloom* test, which he describes as the "conscious act or omission" test.⁴⁹ According to Professor Vasek, *Slodov* replaced the *Bloom* test with the "personal fault" test.⁵⁰ Since the *Bloom* test focuses on payments to other creditors, the test does not require per-

expenses out of the account. His personal fault in failing to keep his promise, together with his payments to other creditors, made his actions willful under either test.

46. *Id.*

47. *Feist v. United States*, 607 F.2d 954, 962 (Ct. Cl. 1979). In *Feist*, the taxpayer owned a controlling interest in a corporation engaged in the retail department store business. He was also the corporate treasurer and chairman of the board of directors. Just prior to the completion of a sale of the stock in the corporation to another company, he was informed that the corporation was delinquent in withholding tax deposits. The buyer assured him that the taxes would be paid immediately, but the buyer failed to pay the taxes after a principal in the buyer's company embezzled a large amount of the money left in the corporation. The court held that, under *Slodov*, personal fault is a necessary element of willfulness. The court found that Feist had acted in good faith and could not be held at fault for the embezzlement of funds with which he had intended the taxes be paid.

48. *Godfrey v. United States*, 748 F.2d 1568, 1577 (Fed. Cir. 1984). After reciting the *Bloom* test, the *Godfrey* court said that "willfulness must also be viewed in light of the 'personal fault' of the plaintiff." *Id.* (citing *Slodov*, 436 U.S. at 254). The evidence failed to establish that Godfrey knew of the tax delinquency, and therefore the government failed to establish Godfrey's personal fault. *Id.*

49. Vasek, *The Hidden Tax Trap of I.R.C. Section 6672*, 67 KY. L.J. 43 (1978) [hereinafter Vasek].

50. *Id.* at 73. That the *Slodov* court replaced the *Bloom* test with the personal fault test may be seen by the fact that application of the *Bloom* test would have found *Slodov* liable for the 100% penalty for the taxes that were unpaid before he assumed control of the corporation. This is because *Slodov* paid other creditors of the corporation instead of paying the taxes that were due. In not finding *Slodov* liable for the penalty for those taxes, the court held that there must be personal fault in not paying the taxes, not merely personal fault in paying other creditors. The fact that many courts have overlooked the *Slodov* Court's replacement of the *Bloom* test is probably due to a tendency of some courts, and attorneys briefing those courts, to distinguish *Slodov* on its peculiar facts. See, e.g., *Wood v. United States*, 808 F.2d 411 (5th Cir. 1987), in which the court found the *Slodov* test inapplicable because Wood was "a responsible person both before and after the obligations at issue accrued," and therefore the court applied the *Bloom* test. This confusion results from the fact that the *Slodov* Court did not apply the personal fault test to tax obligations that accrued

sonal fault regarding nonpayment of taxes and is therefore inconsistent with the personal fault required by *Slodov*. After reading Justice Brennan's opinion in *Slodov* and Chief Justice Rehnquist's dissent in *Sotelo*, it is hard to imagine that a majority of the present Supreme Court would not agree that *Slodov* overruled the *Bloom* test.

In sum, the purpose of section 6672 is to insure compliance with an employer's duty to pay taxes by subjecting the persons responsible to a severe penalty. Liability under section 6672 has two prerequisites. First, the person must be responsible for collecting, truthfully accounting for, and paying over the tax. To determine who is a responsible person, the courts generally look to factors that indicate who has the power to control the decision-making process for the allocation of funds. Second, the responsible person must have willfully failed to collect, truthfully account for, and pay over the tax. Courts use one of two tests to determine willfulness. Many courts still use the *Bloom* test, which establishes willfulness by showing that the person paid creditors other than the government, knowing that taxes were due. However, many authorities argue that the Supreme Court replaced the *Bloom* test with the test in *Slodov* by requiring that personal fault for not paying the taxes must be shown.

III. THE *HOWARD* DECISION

A. *Facts*

Waymon Leon Howard, the appellant in *Howard*, was a director, minority shareholder, treasurer, and executive vice-president of Eden Marketing Corporation (Eden), a Texas corporation. Paul Jennings was Eden's chief executive officer and majority shareholder. Howard was responsible for Eden's day-to-day operations. For a substantial period of time he was the only authorized signatory on Eden's main checking account. For the remainder of his time with Eden, he shared check signing authority with Eden's comptroller; however, only one signature was required on checks drawn. Early in Howard's tenure with Eden, he had issued an 8,000 dollar check for back withholding taxes to the I.R.S. The I.R.S. credited the money to an outstanding liability of one of Jennings' previous partner-

while *Slodov* was in control of the corporation because *Slodov* conceded liability for the penalty for those taxes.

ships. On discovering Howard's action, Jennings relieved Howard of his duties for several weeks. Upon reinstating Howard, Jennings instructed him not to pay any bills without approval. Nonetheless, the Fifth Circuit Court found that Howard satisfied both prongs of the 100 percent penalty provision in that he was a "responsible person" and his failure to pay the withholding taxes of the corporation was "willful."⁵¹ He was therefore found liable for the 100 percent penalty in the amount of 22,671 dollars.⁵²

Under the first prong of the 100 percent penalty provision, the court found that Howard was a responsible person by looking to his status and duties within Eden. The court, in dicta, went on to say that although Howard might have been fired if he had disobeyed his superior by paying the taxes, Howard was not relieved of his responsibility to do so.⁵³ Although the facts indicate that Howard did have a high level of responsibility at Eden, other courts have used this dictum to unjustly extend liability to persons with less authority than Howard.⁵⁴

Under the second prong of the 100 percent penalty provision, the court applied the *Bloom* test and found willfulness as a matter of law because Howard made payments to creditors other than the I.R.S. with knowledge that taxes were due.⁵⁵ The court did not consider, however, that this test may no longer be good law in light of the Supreme Court's reasoning in *Slodov*.

B. Analysis by the Howard Court

1. New Responsible Person Test

In an apparent attempt to find guidelines as to whether Howard was a "responsible person," the first requirement for liability under section 6672, the *Howard* court fashioned a new three-part test: "[r]esponsibility in this context is a matter of

51. *Howard v. United States*, 711 F.2d 729, 733-36 (5th Cir. 1983). Citing *Newsome v. United States*, 431 F.2d 742, 747 (5th Cir. 1970), the *Howard* court suggested that a failure to pay the taxes was not willful if there was a "reasonable cause" for the failure. However, both the *Newsome* and *Howard* courts suggest that the reasonable cause exception is quite limited in scope, and neither opinion gave any examples of a "reasonable cause."

52. *Howard*, 711 F.2d at 733.

53. *Id.* at 734.

54. See, e.g., *Roth v. United States*, 779 F.2d 1567 (11th Cir. 1986); *Freeman v. United States*, 603 F. Supp. 272 (D. Ariz. 1985), *aff'd mem.*, 817 F.2d 106 (9th Cir. 1987).

55. *Howard*, 711 F.2d at 736.

status, duty and authority."⁵⁶ The court found that Howard had the requisite status because he was a director, shareholder, treasurer, and executive vice-president of Eden.⁵⁷ The court found that Howard had a duty to ensure that Eden's taxes were paid because he ran the day-to-day operations of the company and was a signatory on the corporation's main checking account.⁵⁸ The court defined "authority" as the "effective power to pay" and found that Howard had such authority because he issued small checks on several occasions without the approval of Paul Jennings, the chief executive officer and majority shareholder of Eden.⁵⁹ As used in *Howard*, status, duty, and authority are three factors for the court to consider and weigh in determining a corporate employee's responsibility for paying taxes; some indicia of each factor must be present in order to establish liability.⁶⁰

In finding that Howard had the requisite authority, the court stated that "[t]he fact that Jennings might well have fired Howard had he disobeyed Jennings' instructions and paid the taxes does not make Howard any less responsible for their payment."⁶¹ Having already decided that Howard had the authority to pay the taxes, the court reasoned that he would have only lost the authority after he had paid them.⁶²

The conclusion, in dicta, that Howard was responsible, notwithstanding that he would have been fired for paying the taxes, has been followed by several subsequent cases finding persons even less responsible than Howard liable for the 100 percent penalty. In *Roth v. United States*, the Eleventh Circuit Court cited *Howard* with approval while imposing section 6672 liability against a vice president who was neither a director nor a stockholder of the corporation and who was specifically instructed by the corporation's president not to pay the taxes.⁶³

56. *Id.* at 734. This test was suggested by *Mazo v. United States*, 591 F.2d 1151, 1156 (5th Cir. 1979), *cert. denied*, 444 U.S. 842 (1979) ("responsibility is a matter of status, duty and authority, not knowledge").

57. *Howard*, 711 F.2d at 734.

58. *Id.*

59. *Id.*

60. *See id.* at 733-35.

61. *Id.* at 734. *Howard* was an appeal of a summary judgment ruling. The court, therefore, had to consider the facts in the light most favorable to Howard and had to accept the possibility that Howard might have been fired for paying taxes as a fact. *Id.* at 733.

62. *Id.* at 734.

63. *Roth v. United States*, 779 F.2d 1567, 1571-72 (11th Cir. 1986).

In *Freeman v. United States*, the court relied on *Howard*⁶⁴ to impose section 6672 liability against Jerry Taylor, a treasurer, corporate director, and eight percent stockholder, who had been hired as a bookkeeper one year before the unpaid taxes accrued.⁶⁵ Taylor presented evidence that he would have been fired if he had paid the taxes.⁶⁶ Taylor was found liable for a penalty of 48,960 dollars, although he was hired at an annual salary of only 18,000 dollars. As the *Freeman* case illustrates, the application of the *Howard* dicta may result in a penalty that is completely disproportionate to salary. However, courts persist in following the dicta in *Howard* and continue to find that the threat of being fired is not enough to relieve someone of the responsibility to pay taxes.⁶⁷ Prior to *Howard*, the test for a responsible person focused on who had the power to determine which creditors will be paid. In the line of cases spawned by *Howard*, that focus has been lost.

The three-part test to determine a responsible person announced in *Howard*—status, duty, and authority—could be useful, but the focus of this test is wrong because it does not focus on what the court is trying to determine. It must be remembered that what a court is trying to determine is whether the taxpayer is a “person required to collect, truthfully account for, and pay over any tax.”⁶⁸

Status as a separate factor from duty tends to skew the focus of the inquiry. As stated in *Dudley v. United States*, corporate office (or any other indicator of status) does not of itself establish responsibility.⁶⁹ However, a person's status within a corporation may be relevant to the inquiry because it could be indicative of a duty, as for example when the bylaws of a corporation provide that the corporate treasurer is responsible for paying taxes. Status may also indicate a duty of oversight of

64. *Freeman v. United States*, 603 F. Supp. 272, 275 (D. Ariz. 1985), *aff'd mem.*, 817 F.2d 106 (9th Cir. 1987).

65. *Id.* at 273.

66. *Id.* at 274.

67. See, e.g., *Gephart v. United States*, 818 F.2d 469, 474-75 (6th Cir. 1987); *In re Green*, 89 Bankr. 466, 475-76 (Bankr. E.D. Pa. 1988); *In re Turner*, 35 Bankr. 811, 815 (Bankr. D.N.D. 1983), *aff'd*, 43 Bankr. 752 (Bankr. D.N.D. 1984), *remanded mem.*, 760 F.2d 273 (8th Cir. 1985). For other cases that have cited the *Howard* dicta with approval, see *Thibodeau v. United States*, 828 F.2d 1499, 1504-05 (11th Cir. 1987); *Simpson v. United States*, 664 F. Supp. 43, 48 (E.D.N.Y. 1987); *Johnson v. United States*, 583 F. Supp. 127, 130 (W.D. Ky. 1984); *In re Terrell*, 74 Bankr. 291, 297-99 (Bankr. N.D. Ala. 1987).

68. I.R.C. § 6672(a) (West 1988).

69. 428 F.2d 1196, 1201 (9th Cir. 1970).

the payment of taxes. The proper test should focus on duty and authority because these are the key indicators of responsibility, with status merely a factor to consider in determining whether a duty exists.

Duty is clearly an important element of responsibility in this context, but the inquiry should focus on whether the taxpayer had a duty within the corporate structure to pay the taxes or to see that the taxes were paid, rather than on whether the taxpayer had a duty to pay other creditors. The *Howard* court apparently found duty in the fact that Howard ran Eden's day-to-day operations and was a signatory on Eden's main checking account.⁷⁰ Although those facts could evince a possible duty to pay taxes in some cases, the *Howard* court's inquiry stopped short of the ultimate question of whether Howard had a duty to pay the taxes. In fact, the only evidence on this question discussed by the court indicates that paying taxes was specifically excluded from Howard's duties by Jennings.

The authority portion of the *Howard* test comes closest to the generally accepted test for a responsible person—determining who had the power to control the decision-making process by which funds are allocated to other creditors in preference to paying taxes that are due.⁷¹ The focus of even this generally accepted test is wrong. Although it obviously parallels the *Bloom* test for willfulness—preferring other creditors over the I.R.S.—the focus should be on whether the taxpayer had the authority to pay the taxes. It is unlikely that a different outcome would result from a shift in focus since, in most cases, one with the authority to pay other creditors would also have the authority to pay taxes. However, the *Howard* case itself is a good example of the problem created by an incorrect focus. The court found that Howard had authority to pay taxes by the fact that he issued several small checks to other creditors without Jennings' approval.⁷² This simply does not reach the question of whether Howard had authority to pay the taxes.

The most unfortunate part of the *Howard* decision is the court's statement that even though Jennings might have fired Howard, Howard was nevertheless a responsible person. As pointed out in the District Court decision in *Roth v. United*

70. 711 F.2d at 734.

71. *Godfrey v. United States*, 748 F.2d 1568, 1575 (Fed. Cir. 1984).

72. *Howard*, 711 F.2d at 734.

States, this statement expanded the existing view about who was a responsible person by reaching persons who have no discretion to ensure that taxes are paid.⁷³ In reaching its conclusion, the *Howard* court used circular reasoning. The court first found that Howard was a responsible person and then said that the fact that he could have been fired did not relieve him of that responsibility.⁷⁴ However, the court should have considered whether Howard could be fired for paying the taxes in determining whether Howard had the authority to pay the taxes in the first place. The court begged the question by using its own determination of Howard's responsibility as part of its analysis of his responsibility.

The District Court in *Roth* refused to follow *Howard*, stating that the *Howard* decision was a "totally surprising and unnecessary departure" from existing law.⁷⁵ The *Roth* District Court stated that the *Howard* decision "unjustifiably and harshly penalizes an individual who acted as would any reasonable man under those circumstances."⁷⁶ In reversing the *Roth* District Court, the Eleventh Circuit Court committed exactly the same error of begging the question as did the *Howard* court.⁷⁷ The court used its own determination of Roth's responsibility as part of its analysis of his responsibility.

It is interesting to note that the Eleventh Circuit stated and then rejected a suggestion purported to be from the trial court that "to follow the precept of *Howard* would be to condone the corporation's vice presidents using corporation money

73. *Roth v. United States*, 53 AFTR 2d 84-1153, 84-1155 (N.D. Ala. 1984), *rev'd*, 779 F.2d 1567 (11th Cir. 1986). In order to more easily distinguish these cases, the author will subsequently refer to them as *Roth I* and *Roth II*.

74. *Howard*, 711 F.2d at 734.

75. 53 AFTR at 84-1155. Roth was the vice president of Leewood Development Corporation in charge of acquisitions and completion of job projects. He was authorized to write checks on several accounts of the corporation and was the sole signatory on the payroll account. On a motion for summary judgment filed by the government, Roth produced evidence that the corporation's president, Dobbins, determined which creditors would be paid and that Roth was told by Dobbins not to pay the taxes. Roth's evidence showed that he had been assured by Dobbins that the taxes would be paid with funds from a pending sale of apartments that were owned by Dobbins. The District Court explicitly rejected the reasoning of *Howard* and found that Roth was not a responsible person. *Id.* On appeal, the Eleventh Circuit explicitly followed *Howard* and reversed the District Court, granting summary judgment to the government. *Roth II*, 779 F.2d at 1572.

76. 53 AFTR 2d at 84-1155.

77. *Roth II*, 779 F.2d at 1572. Chief Justice Godbold commented on the circularity of the majority's reasoning. *Id.* at 1575 (Godbold, C.J., concurring in part and dissenting in part.)

contrary to the instructions of the president and that this would be equated with embezzlement."⁷⁸ The *Howard* decision does in fact put a corporate employee instructed not to pay taxes in the position of having to choose between facing the 100 percent penalty or paying the taxes to prevent personal liability for the penalty. The unauthorized use of corporate funds for personal benefit in any other context would be considered embezzlement.

There are thus three problems with the court's analysis of the responsible person element. First, the court's use of status as an independent factor tends to skew the analysis since the status is merely an indicator of duty. Second, the focus of the duty and authority factors is incorrect since the focus is on the duty and authority to pay other creditors, rather than on the duty and authority to pay taxes. Third, the court engaged in circular reasoning by using its own determination of Howard's responsibility in analyzing his responsibility.

2. Willfulness

On the question of willfulness, the *Howard* court recited the *Bloom* test.⁷⁹ Howard made out thirty-six checks to creditors other than the I.R.S. after he knew that Eden owed taxes. According to the *Bloom* test, Howard willfully failed to pay the taxes as a matter of law.⁸⁰ In its discussion of willfulness, the court quoted a portion of the *Slodov* decision concerning personal fault,⁸¹ but dismissed any consideration of Howard's personal fault by saying that Howard had a choice because "[h]e could have paid the taxes, accepted the consequences (presumably being fired), and thus avoided the penalty."⁸²

Under *Slodov*, a different result would be almost certain. *Slodov* also had a choice of paying the taxes or other creditors and decided to pay the other creditors, but the *Slodov* court focused on his personal fault in not paying the taxes. The *Howard* court did not look beyond the fact that *Howard* made out checks to other creditors.

The *Howard* court is certainly not alone in continuing to apply the old *Bloom* test to the question of willfulness,⁸³ but

78. *Id.* at 1572.

79. *Howard*, 711 F.2d at 735.

80. *Id.*

81. See *supra* text accompanying note 43.

82. *Howard*, 711 F.2d at 735.

83. See, e.g., *Mulee v. United States*, 648 F. Supp. 1181, 1185 (N.D. Ill. 1986) (citing

this application is difficult to justify in light of *Slodov*. The *Bloom* test is certainly beneficial to the I.R.S. All that the government must do under *Bloom* is to introduce checks to other creditors into evidence and establish that the person knew that taxes were due and it has won its case. However, due to the potentially staggering penalties that can be imposed under section 6672, the *Slodov* personal fault test is necessary to insure that the taxpayer willfully failed to pay the taxes, not just that the taxpayer willfully paid some other bills. The *Bloom* test imposes absolute liability on a responsible person, in spite of the legislative history of section 6672. The legislative history shows that the use of the word "willfully" in the statute originally indicated the same level of culpability as where the word "willfully" is used in criminal statutes.

Although in most cases the use of the personal fault test will not produce a different outcome than the *Bloom* test, there are a few significant examples in which the outcome would be different. The Fifth Circuit in *Newsome* found willfulness when a taxpayer paid other creditors even before the taxes were due.⁸⁴ Probably because of that decision, the *Howard* court found it unnecessary to specify whether the checks that Howard issued to other creditors were issued before or after the taxes were due. However, it is extremely difficult, without more evidence, to translate a payment to another creditor before the taxes are due into a willful failure to pay the taxes. The courts should at least consider whether such a payment could reasonably have been expected to preclude payment of the taxes when they did become due.

Another example of a case in which the outcome would be different under a personal fault test was addressed by the

Howard v. United States, 711 F.2d 729, 735 (5th Cir. 1983)); *In re Flemister*, 48 Bankr. 427, 430 (Bankr. N.D. Ga. 1985) (the court cites *Howard* for the *Bloom* test and then goes on to say that signing blank checks with knowledge that taxes are not being paid constitutes willful failure).

84. *Newsome v. United States*, 431 F.2d 742, 745 (5th Cir. 1970). Under the *Newsome* facts, it was evident that *Newsome* used funds to pay other creditors when it was highly likely that the corporation would not have the funds to pay the taxes when they became due. Under those facts, the *Newsome* holding was correct. The difficulty would arise when this holding is coupled with the use of the *Bloom* test for a finding of willfulness as a matter of law, without examining the surrounding facts to determine the likelihood that the payment to another creditor would prevent payment of the tax when due. The payment of another creditor, together with a subsequent failure to pay taxes, should not be enough to establish the personal fault necessary for the 100% penalty.

Slodov Court.⁸⁵ As discussed in *Slodov*, the I.R.S. frequently allows a financially troubled corporation with few unencumbered assets to continue operations in the hope that the Service will thereby increase its chances of collecting unpaid taxes. Often in this instance, a monthly payment plan is set up for payment of back taxes.⁸⁶ Under the *Bloom* test, a subordinate corporate employee could be held liable for the 100 percent penalty for paying a supplier even while such monthly payments are being made. This would occur if the corporation eventually fails and files for bankruptcy, regardless of whether the employee was at fault for not paying the taxes in the first place.

A third example of a situation in which the outcome would be different under the personal fault test is the situation in *Roth*. In that case, Roth was instructed not to pay the taxes but was assured by the president of the corporation that the taxes would be paid by proceeds from the sale of other assets owned by the president. Roth apparently relied on this assurance. The Eleventh Circuit did not address the issue of Roth's reliance on the president's assurance.⁸⁷ It would be difficult to find personal fault in such a situation without a further showing that such reliance was unreasonable.

A final example that might produce a different outcome

85. *Slodov v. United States*, 436 U.S. 238, 252 (1978).

86. Installment agreements for the payment of delinquent taxes are described in INTERNAL REVENUE MANUAL, pt. V, § 5331.1 (1987). One element of the installment agreement is always that the future taxes will be paid in a timely fashion. *Id.* As discussed in *Slodov*, in the *Bloom* test the 100% penalty on the entire outstanding tax liability would attach to a corporate officer on the payment of the first dollar to a supplier, regardless of whether the corporation was being allowed to continue operating under a payment plan and regardless of any personal fault on the part of the officer in the failure to pay the tax in the first place. *Slodov* explicitly overruled this application of the *Bloom* test. However, as suggested in note 50 *supra*, some courts tend to limit *Slodov* to situations where the officer was not employed by the company at the time the tax liability accrued.

87. The District Court did take Roth's reliance into account in its analysis. *Roth I*, 53 AFTR 2d at 84-1155. The Eleventh Circuit also quoted from testimony that showed that Roth had relied on the president's assurances, and although the court stated that it must treat the case as though the jury believed this testimony, it never discussed Roth's reliance. In fact, the court never discussed the willfulness issue at all. The court found that, under the authority of *Howard*, Roth was a responsible officer and the president's instructions to Roth not to pay the taxes did not relieve Roth of that responsibility. *Roth II*, 779 F.2d at 1569-70. According to the court, since Roth was a responsible person, he was responsible for the penalty (apparently irrespective of his willfulness). In any case, under the *Bloom* test, Roth's reliance would have been irrelevant. He had paid another creditor knowing that taxes were due, and therefore his actions were willful under that test, regardless of the assurances.

under the personal fault test involves the policies of the I.R.S. in the allocation of payments. Frequently, the I.R.S. allocates receipts of tax payments to taxes other than the withholding taxes that the taxpayer is attempting to pay, as it did in the case of the 8,000 dollar payment that Howard made. The policy of the I.R.S. is to apply payments to other taxes whenever possible if the taxpayer has failed to specify which taxes are to be paid. This policy exists because the 100 percent penalty gives the Service an alternative means of collecting withholding taxes, which it does not have for other corporate taxes. The purpose of this practice is to maximize tax collections. However, as pointed out by Professor Vasek, in such instances the nonpayment of the taxes "is caused more by the IRS allocation method than by the personal fault of the responsible person."⁸⁸

Thus, there are some cases in which the personal fault test will produce a different outcome than the *Bloom* test. In light of *Slodov*, the different outcome in those cases is entirely justified.

C. *Why the Decision in Howard is Wrong*

The decision of the *Howard* court is wrong. The court should not have reached the willfulness issue because Howard simply was not a responsible person, the first requirement for liability under section 6672. Howard was not a responsible person because he did not have the authority to pay the taxes. Howard did not have the authority to pay the taxes because Jennings had demonstrated that Howard would be fired if he tried to pay the taxes.

The *Howard* court reached the wrong decision because the focus of the test it used for responsibility was wrong. The focus of the test should be on who has the duty and authority to pay the taxes. Instead, *Howard* used a three-part test of status, duty, and authority to pay creditors other than the I.R.S.

The *Howard* court itself seemed to be uncomfortable with its decision, for in the final paragraph the court stated that:

[W]e cannot help feeling that it is Jennings who should pay these taxes However, Jennings is apparently no longer within reach of the long arm of the IRS. . . . Although we recognize that our holding today may appear harsh to some,

88. Vasek, *supra* note 49, at 70.

we are bound to follow the law as interpreted by the Supreme Court and this Circuit.⁸⁹

IV. INTERNAL REVENUE SERVICE ARGUMENT

The I.R.S. views section 6672 as merely an alternative collection device for withholding taxes.⁹⁰ Since the I.R.S. is responsible to the employees of the corporation for taxes withheld, the position of the I.R.S. is that someone from the corporation should pay rather than the government.⁹¹ However, the I.R.S. only refunds a portion of income taxes withheld and does not refund social security withholding in most cases until many years later, if at all. Presumably, most unpaid withholding taxes are collected through assessment and collection of the 100 percent penalty against officers who are truly responsible.

There is nothing in the wording or history of section 6672 to support reading it as an alternate collection device. The I.R.S. reading is not in accord with the *Slodov* holding that personal fault is necessary for imposition of the penalty. It is certainly not fair to saddle an individual corporate employee who is not responsible for the problem with a staggering corporate debt just to provide an alternate means of collection.

Under the alternate collection device theory, it is not important who is actually responsible. The main concern of the I.R.S. under this theory is simply to try to reach as many possible sources for payment of the tax. The 100 percent penalty is similar to joint and several liability. A penalty equal to the entire withholding taxes owed by the corporation can be assessed and collected against any one individual who meets the requirements, even if there is more than one corporate employee who does.⁹² As decided in *Sotelo*, the 100 percent penalty obligation cannot be discharged in bankruptcy; it could follow a corporate employee for the rest of that employee's life. Such a potentially crushing liability should be assessed only against employees actually responsible for not paying the tax.

The dicta in *Howard* concerning Howard's possible firing had he paid the taxes is actually at odds with the Internal Rev-

89. *Howard v. United States*, 711 F.2d 729, 737 (5th Cir. 1983).

90. See *supra* note 26 and accompanying text.

91. See *supra* text accompanying notes 13-15.

92. *Godfrey v. United States*, 748 F.2d 1568, 1575 (Fed. Cir. 1984).

enue Manual. Part V, section 726 of the Manual admits that most employees will do what they are told if a superior orders them not to pay the taxes. In such a case, the Manual states that the person who made the determination not to pay the taxes is the one who is responsible.⁹³

The position of the I.R.S. regarding willfulness is based on the idea that an employer is supposed to retain withheld taxes in trust for the government. For this reason, withheld taxes are commonly referred to as "trust fund taxes."⁹⁴ To pay another creditor without leaving enough funds to pay the taxes is a violation of the trust. This is a nice theory, but as some of the examples given above indicate, it does not always square with the reality of the situation. In addition, in many, if not most, cases in which a company is in trouble, there is only enough money to pay net wages when payroll is due. There are no funds available at that time to make up the "trust." The *Bloom* test for willfulness, which is preferred by the I.R.S.,⁹⁵ makes an employee liable for using after-acquired funds for other purposes, even without an intent to defeat the tax. However, the *Slodov* court expressly found that after-acquired funds are not impressed with a trust.⁹⁶ Willfulness should only be attributed to those persons who either willfully pay net wages without enough funds for the trust fund taxes or to those persons who willfully fail to pay the taxes, or as stated in section 6672, "who willfully fail to collect such tax, or truthfully account for and pay over such tax."⁹⁷

Thus, the position of the I.R.S. that the 100 percent penalty is merely an alternate collection devise is not supported by the wording or history of section 6672 and is not in accordance

93. INTERNAL REVENUE MANUAL, pt. V, § 726 (1987), which states:

An employee is under the dominion and control of his/her employer. He/she does what he/she is told to do. On record he/she may have the responsibility to perform the necessary act of withholding and paying over the trust fund taxes, but is nevertheless subject to his/her employer's specific direction. If he/she is told not to pay the tax, most likely he/she will not. Therefore, any allegation that an employee is the responsible person should be thoroughly investigated. In any event, the same tests would be applied to any person, including an employee. If the employee was the one who made the decision or the determination, he/she would be the one who would be held liable.

94. *Slodov v. United States*, 436 U.S. at 238, 243 (1978).

95. INTERNAL REVENUE MANUAL, pt. V, § 731(1) (1987). This section still states the *Bloom* test for willfulness. The Manual limits the application of *Slodov* to the precise facts of *Slodov*. *Id.* at § 722.

96. *Slodov*, 436 U.S. at 254.

97. I.R.C. § 6672 (West 1988).

with *Slodov*. Moreover, the extension of liability in *Howard* to persons who might be fired if they paid the taxes is at odds with the position of the I.R.S. as stated in the INTERNAL REVENUE MANUAL. Finally, the trust fund theory of the I.R.S. concerning willfulness, to the extent that it incorporates the *Bloom* test, is not in accord with the personal fault requirement of *Slodov*.

V. PROPOSED TEST FOR RESPONSIBLE PERSON

The *Howard* court was on the right track in establishing a three-part test of status, duty, and authority to determine who is a responsible person under section 6672. However, as noted in the analysis of the *Howard* decision, there are problems with that test as applied in *Howard*. Those problems would be alleviated by the adoption of a two-part test of duty and authority.

In most cases, both duty and authority to pay the taxes should be established to show that a person is responsible. A court should follow the example of the *Howard* court and examine the evidence to see if there are some indicia of duty and of authority. A corporation should not be allowed to subvert the test by separating duty and authority, however. There must always be at least one person in the corporation who is responsible to see that the withholding taxes are paid. In a case in which no one has both the duty and authority to pay the taxes, the more important element is the determination of who had the authority to determine whether or not the taxes would be paid.

The most important change that this new test would bring to the analysis is a shift in focus. This shift would bring the responsible person analysis in line with the reasoning of *Slodov*. The issue is not who had the duty and authority to pay other creditors. Duty and authority to pay other creditors may be a strong indication of duty and authority to pay the taxes, but it must be remembered that the issue is the payment of taxes, not the payment of other creditors. There may be many cases in which an employee has the duty and authority to pay small bills to suppliers who deliver their products to the corporation but does not possess the corresponding duty and authority to pay the much larger amounts usually associated with the payment of withholding taxes.

The elimination of status as a separate element in the

analysis could prove helpful to the government as well as provide a better focus on the issues. It is quite possible that a court applying the three-part test could find that an employee had the duty and authority to pay the taxes, but did not have the status necessary for section 6672 liability. Since status is not the issue, this would be an unwarranted result.

Status should come into the analysis as an indicator of the other two factors. The duty to pay the taxes may be conferred upon a person of a certain status, such as a treasurer, through the bylaws of the corporation. The duty in a person of a certain status may also be inferred from general commercial usage. In some cases, status may be the only indicator that a court has to determine who has the duty to pay the taxes. In other cases, status may indicate a duty to oversee the payment of taxes, as in the case of a president, especially of a small, closely-held corporation. Because of oversight duties and overlapping or jointly held duties, a number of persons within a corporation may be liable for the 100 percent penalty. Status may also indicate authority to pay the taxes when duty is otherwise established.

The suggested shift in focus should prevent the extension of liability to a person who would be fired for paying the taxes. Of course, any subordinate may be fired, and that fact is not enough to relieve an employee of liability. However, when an employee has specific instructions from a superior not to pay the taxes, especially if the instructions are under the express or implied threat of loss of employment, that employee does not have the authority to pay the taxes. In that case, it is the superior who should be responsible for the 100 percent penalty.

Thus, the new test of who had the duty and authority to pay the taxes will alleviate the problems associated with *Howard*. The most important change in the test is the shift in focus from who had the duty and authority to pay other creditors to who had the duty and authority to pay the taxes. The elimination of status as a separate element serves to emphasize which elements are really at issue in the analysis. The shift in focus will also prevent the extension of liability to an employee who would be fired for paying the taxes.

VI. CONCLUSION

Two separate requirements must be found for a person to

be held liable for the 100 percent penalty of section 6672. The person must be a "responsible person" and must have "willfully" failed to collect, truthfully account for, and pay over taxes. The three-part test defining a responsible person announced in *Howard*—status, duty, and authority—should be reduced to a two-part test of duty and authority, with status merely an indicator of duty. The focus of this test should be on finding whether the person had the duty and authority to pay the taxes. If it can be established that an employee would have been fired for paying the taxes, this should preclude a finding that the person had the authority to pay the taxes.

Although universally accepted at one time, the *Bloom* test for willfulness—preferring another creditor over paying the taxes—was never in accord with the legislative history of section 6672 because it established absolute liability on a responsible person to pay the taxes. The history of the statute shows that a culpability equivalent to criminal willfulness should be necessary. In any case, the Supreme Court introduced a personal fault test in *Slodov*. The lower courts should recognize this aspect of the *Slodov* decision and discontinue applying the old *Bloom* test as the court did in *Howard*.

The *Howard* court strained its reasoning to find Howard liable because the I.R.S. could no longer collect from Jennings, the corporation's chief executive officer. In so doing, the court was in accord with the I.R.S. position that section 6672 is an alternate collection devise for withholding taxes. However, that position is not in accord with the Supreme Court's decision in *Slodov*. Also, it is simply unjust to put subordinate corporate employees without authority in the position of facing the potentially staggering penalties of section 6672 or embezzling corporate funds with unauthorized tax payments in order to protect themselves. The proposed test for a responsible person delineates who has the duty and authority to pay the taxes and would help to prevent this unjust outcome.

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