

PUBLICATION

The Hazards of Being a Volunteer

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The U.S. District Court for the Eastern District of Tennessee issued a memorandum opinion on March 8, 2012, that may come as a surprise to those who are active in nonprofit organizations. The Court's opinion in *Bunch v. Commissioner of Internal Revenue* addresses the liability of an unpaid, volunteer director for the federal employment tax liability of a nonprofit organization which the director serves. The Court dismissed the volunteer's claim for a refund of over \$193,000 in employment taxes that he had paid on the organization's behalf. In dismissing the refund claim, the Court relied heavily on the fact that the volunteer, despite the fact that he was never paid for his services as a director and was never an employee, was a "responsible person."

Responsible Person Liability

Entities with statutory employees have a duty to collect and remit certain taxes to the Internal Revenue Service (IRS), commonly known as employment taxes, attributable to wages paid to those employees. The IRS views such taxes, to the extent deducted from an employee's paycheck, as being held in trust by the employer for the benefit of the government until such time as the employer remits the funds to the IRS. For this reason, Congress granted the IRS the authority to aggressively pursue the collection of employment taxes through assessments against individuals who are considered to be a "responsible person." Section 6672(a) of the Internal Revenue Code (Code) provides the IRS with the power to assess penalties that are otherwise the liability of an employer against persons who are responsible for collecting, accounting for and paying over such employment taxes willfully fail to perform such responsibility.

Troublesome Facts

The volunteer/plaintiff in the *Bunch* case was a director of a Tennessee nonprofit corporation (Organization) that provided health care services for the developmentally disabled. The volunteer was listed as an officer and director of the Organization but he did not hire or fire employees and, at least initially, had no check writing authority for the Organization. The volunteer did provide a building rent-free and made start-up loans and bridge loans to the Organization when the Organization lacked sufficient funds to pay bills. After making a number of loans to the financially struggling Organization, the volunteer eventually assumed check writing authority for the Organization in 2007, and, from that point forward, remained actively involved in the financial affairs of the Organization.

In making the determination of whether the volunteer was a responsible person under Section 6672, the Court relied on past precedent that generally looked to the duties of the individual as an officer under the corporate bylaws; the ability of the individual to sign checks of the employer; the identity of the officers, directors and shareholders of the employer; the identity of the individuals who hired and fired employees; and the identity of the individuals who were in control of the financial affairs of the employer. Additionally, the Court examined in this case whether the volunteer had access to the books and records of the Organization, and whether the volunteer made personal loans to the Organization.

The volunteer did not deny that he was a responsible person from the point at which he became involved in the financial affairs of the Organization forward, though he did deny responsibility prior to that date. Despite the

fact that the volunteer prior to the change in his role in the Organization in 2007, never drew a salary, never had check writing authority, and never viewed regular financial reports, the Court focused on the fact that the volunteer, by virtue of the numerous bridge loans he made to the Organization to keep it afloat throughout its existence, acted as a de facto line of credit, and, as such, exerted a significant and substantial amount of control over the financial affairs of the Organization. The Court found it immaterial that the volunteer never actually used any of the authority which he held as chief financier, and instead looked merely to the fact that he could, and should, have done so. Also important to the Court was the fact that the volunteer, in fulfilling his fiduciary duty as a director, suggested that it may not be in the Organization's best interest to give employees raises. The fact that Organization's management heeded the volunteer's advice was, in the eyes of the Court, evidence of his authority.

The inquiry into whether a taxpayer is a responsible person also involves an examination of whether his conduct was willful. The Court in the *Bunch* case looked to whether the volunteer knew of the employment tax delinquency yet failed to rectify it, regardless of whether there was intent to defraud the IRS. The Court found that the volunteer's willfulness was such that it rose to "a reckless disregard for obvious or known risks," such finding being requisite to the assessment of responsible person liability. In finding the volunteer liable under the reckless disregard standard, the Court held that the volunteer clearly should have known that there was a grave risk that employment taxes were not being remitted to the IRS and was in a position to find out for certain very easily. The Court once again looked to the fact that the volunteer should have known of the Organization's delinquent taxes due to his knowledge of the financial difficulties and the fact that he had to lend the Organization money on a monthly basis. Also important to the Court was the fact that the volunteer had full access to the books and records of the Organization, as well as any and all financial reports, by virtue of his role as a director. It was not possible, the Court stated, for the volunteer to escape liability by "wearing blinders" to avoid obtaining actual knowledge of the tax delinquency.

What You Should Know

The facts in the *Bunch* case, though not uncommon in the world of for-profit businesses, may often be overlooked by directors and executives participating in nonprofit endeavors. Under the Code, directors and executives of nonprofits can be just as culpable as their for-profit counterparts insofar as responsible person liability is concerned. With the *Bunch* decision in mind, it is important for nonprofit directors and executives to reexamine their roles and ensure that all applicable taxes are indeed being paid. Additionally, *Bunch* may also serve as a warning to those who volunteer their time that once a certain threshold of involvement in a nonprofit's operations is crossed, responsible person liability could very well attach -- which, as the volunteer's failed refund claim demonstrates in the *Bunch* case, can be very costly.

Regardless of any appeal that may follow, the Court's decision summarized in this article certainly needs to be kept in mind as individuals continue to participate and assist in numerous ways the nonprofits of their choice.