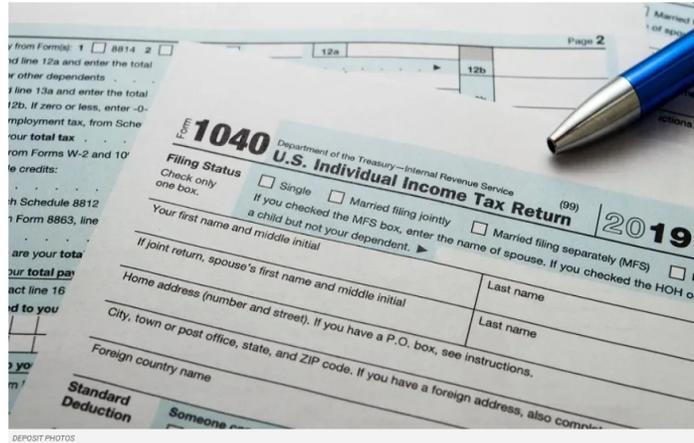


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DEPOSIT PHOTOS

## Former Massachusetts resident's stock transaction ruled taxable

Gain deemed employment, not passive investment income

Eric T. Berkman // April 16, 2025 // 6 Minute Read

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Capital gains that a former Massachusetts resident and his wife realized after he sold stock in the company he previously worked for were taxable as Massachusetts source income, the Appeals Court has determined.

Taxpayer Craig Welch acquired a 50-percent share in AcadiaSoft in 2005, shortly after the Massachusetts company was founded. He served as CEO for the next decade.

In April 2015, Welch moved to New Hampshire, resigned his position with the company that June, and sold his shares for \$4.7 million. Welch and his wife did not include the sum on their Massachusetts tax return as income from a Massachusetts source.

The Welches challenged a subsequent \$335,968 assessment. The Appellate Tax Board ruled that their gain from the stock sale constituted Massachusetts source income because it was effectively connected with his trade, business or employment in the commonwealth within the meaning of G.L.c. 62, §5A(a), the statute governing taxation of income earned by nonresidents.

The Appeals Court affirmed, noting that under the relevant state regulation that clarifies the statute, gain from the sale of stock in a C corporation like AcadiaSoft may constitute Massachusetts source income if "the stock is related to the taxpayer's compensation for services."

"Here, because Welch obtained the stock soon after founding AcadiaSoft, expected that in the future AcadiaSoft would be worth a lot more than it was when he started it, and was looking forward to the payout from his hard work, the board had substantial evidence on which to base its determination that Welch's gain from the sale of the AcadiaSoft stock was derived from his employment," Judge Marguerite T. Grant wrote for the panel.

The 16-page decision is *Welch, et al. v. Commissioner of Revenue*, Lawyers Weekly No. 11-021-25.

### 'Crawl under the table and cry'

Celine E. de la Foscade-Condon of the Massachusetts Department of Revenue argued the case for the commissioner. In a statement, the DOR praised the decision but did not comment on the substance of the ruling.

The taxpayers' attorney, Michael J. Bowen of Jacksonville, Florida, declined to comment on the record.

***We thought it was settled law that nonresidents selling corporate stock that wasn't acquired as compensation wouldn't be subject to tax when they sold that stock. It's unclear how broadly this could be applied, but it's certainly a new direction Massachusetts is taking — and a direction most states wouldn't take.***



RICHARD L. JONES

However, Boston tax attorney Richard L. Jones described the decision as a "bombshell."

"We thought it was settled law that nonresidents selling corporate stock that wasn't acquired as compensation wouldn't be subject to tax when they sold that stock," Jones said. "It's unclear how broadly this could be applied, but it's certainly a new direction Massachusetts is taking — and a direction most states wouldn't take."

Laura A. Brown, a tax attorney in Rockland, said it is the latest example of the DOR "getting greedy" with money earned by anyone with any connection to Massachusetts. It also shows how the regulations are being expanded to capture people who live out of state, she added.

"This is just going to drive businesses from Massachusetts to New Hampshire and Florida, and pretty soon [Boston Mayor Michelle] Wu's housing crisis will be resolved because everyone's going to sell their houses and work somewhere else," she said.

On a more serious note, Brown said the taxpayers in the case likely spent more money fighting the tax than the amount of the tax itself.

"If I'm counseling a client in a situation like this about whether or not to put something down as income in Massachusetts, I might say to them, 'OK, you're getting \$4.7 million. Do you want to pay a couple hundred

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grand as an insurance policy? Or would you rather spend so much more in penalties and interest, plus probably six figures in attorney fees and eight years of your life fighting this?" Brown said.

Leo J. Cushing of Waltham agreed that the ruling disturbs what the tax community viewed as settled principles.

Cushing pointed out that the relevant regulation states that income from a trade or business may include that which results from the sale of an interest in a business.

But the regulation also goes on to say that that generally does not apply to sale of stock in a C or S corporation if the income constitutes capital gain for federal tax purposes.

"Historically, as long as you were selling your stock, whether it was a C corporation or an S corporation, you could rely on the regulations to advise clients who plan to sell their business to move to New Hampshire or Florida to avoid the Massachusetts income tax," he said. "Unfortunately, it's now a facts and circumstances test."

Cushing also called the case an example of bad facts making bad law, pointing out that the taxpayer gave deposition testimony during the Appellate Tax Board proceeding that he was AcadiaSoft's "chief evangelist" and "chief cook and bottle washer"; that he worked "24-7" to build up the company; and that he had been happy with a lower salary for many years because he looked forward to the payout from his hard work, whenever that might be.

"This is the kind of testimony that makes you want to crawl under the table and cry," Cushing said. "He set himself up for the commissioner to say, 'Yes, you're selling stock, but in reality, you're getting paid for a business that you ran in Massachusetts, and this is a form of compensation.'"

### Stock sale

Welch formed AcadiaSoft, a Massachusetts corporation that develops and markets management solutions for institutional investors, in 2003. At the time, he was the only stockholder and held the titles of president, treasurer, clerk and sole director.

In 2005, he voluntarily dissolved the corporation and organized another one by the same name. He was the CEO and treasurer, while an associate of his served as chief technology officer, president and secretary. The two were AcadiaSoft's sole directors and each held 50 percent of its stock.

Between 2003 and 2015, Welch worked exclusively for AcadiaSoft, focusing mainly on sales. He described himself as AcadiaSoft's "chief evangelist" and later testified that he worked 80 hours a week.

Welch reported no wage income from 2003 to 2005 and minimal income in 2006 and 2007, testifying that he had expected the company to be worth a lot more in the future and that he looked forward to the payout from his hard work "whenever that came."

In 2006 and 2007, when AcadiaSoft raised funding from angel investors, Welch's share of the stock was diluted to 35.9 percent.

Then, in 2009, when AcadiaSoft merged into a Delaware corporation by the same name, it obtained additional funding and Welch's share was diluted to 13 percent.

By 2010, Welch was focused on AcadiaSoft's operations, management and sales. While he frequently traveled to New York and London, he worked primarily out of his home in Lynnfield and spent about one day a week in AcadiaSoft's Norwell office.

In 2013, the company entered yet another round of financing, which left Welch with an 11.86-percent share.

By the following year, Welch perceived tension with other directors and grew concerned that his "sweat equity" was in jeopardy. As of January 2015, he was apparently CEO in name only with no operational role, though the board apparently requested that he keep his title because of his high profile in the industry.

At the end of April 2015, Welch and his wife moved to New Hampshire.

In June 2015, AcadiaSoft offered to purchase Welch's remaining shares. He accepted and, on June 26, resigned as officer and director.

AcadiaSoft subsequently issued Welch a 2015 1099-B tax form reporting that he received \$4.7 million in cash proceeds for the sale of his shares.

The Welches filed a 2015 Massachusetts nonresident/part-year resident tax return reporting that amount as having been included as a capital gain on their federal return. They did not include the \$4.7 million as gain from a Massachusetts income source.

After an audit, the commissioner notified the Welches of an assessment totaling \$338,968 in tax, interest and penalties based on their gain from the sale of the stock.

After their abatement application was denied, the Welches appealed to the Appellate Tax Board, which ruled that the gain was taxable as Massachusetts source income.

They then sought review in the Appeals Court.

### Business-related income

The Appeals Court found the Appellate Tax Board's characterization of the Welches' gain as compensatory to be reasonable.

Grant noted that the ATB emphasized multiple events that linked Welch's stock ownership to his compensation and which portrayed him as more than a passive investor.

"He acquired that stock soon after he founded AcadiaSoft, dedicated himself to the success of AcadiaSoft, and expected a payout for his sweat equity," Grant wrote. "In connection with the 2009 refinancing, he became bound by an agreement that tied his status as a key holder of AcadiaSoft stock to his continued employment with the company. Finally, Welch made his resignation from AcadiaSoft contingent on the sale of his shares."

Meanwhile, the panel rebuffed the Welches' attempt to apply to the case a Massachusetts regulation stating that the gain from an out-of-state resident's sale of stock purchased from a Massachusetts employer as an ordinary investment unrelated to compensation is not treated as Massachusetts source income.

Welch did not "purchase" his AcadiaSoft shares, and his acquisition of the stock was indeed related to his compensation, Grant said.

"[T]he board had substantial evidence on which it based its determination that Welch's gain from the sale of his AcadiaSoft shares was derived from his own trade or business of software development," she wrote.

#### Welch, et al. v. Commissioner of Revenue

**THE ISSUE:** Were capital gains that a former Massachusetts resident and his wife realized after he sold stock in the company he previously worked for taxable as Massachusetts source income?

**DECISION:** Yes (Appeals Court)

**LAWYERS:** Michael J. Bowen of Ackerman, Jacksonville, Florida (taxpayers)

Celine E. de la Foscade-Condou of the Massachusetts Department of Revenue, Boston (defense)

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