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THE TAX LAWYER

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IRS Unveils Key Penalty Findings

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I keep noting how bad IRS payroll tax penalties can be. See When Payroll Taxes Go Criminal. Although any tax dispute is bad, payroll tax disputes are ***especially*** bad. How does the IRS build a case against you? An IRS internal memorandum provides guidance to IRS employees how to document cases against employers.

If you're in business you must withhold tax money from employee pay. Then you must account for it and send it promptly to the IRS. Failing to pay not only makes the business responsible—you are personally on the hook. When you withhold tax but fail to remit it the IRS will come after you. The IRS views it as trust fund money.

In a cash-strapped business, keeping the lights on or the warehouse stocked can ***seem*** more important. You may ***think*** you can pay the IRS later. But these problems have a way of snowballing, so keep payroll taxes current at all times.

Business owners and other "responsible persons" have personal liability. The IRS can assess a Trust Fund Recovery Assessment—also known as a 100% penalty—against ***every*** "responsible person." Under Section 6672, the penalty equals the entire amount of trust fund taxes. The IRS can seek to collect 100% from the business and 100% from ***each*** responsible person. The IRS often makes an assessment against every officer, watching them turn on each other. One person may get stuck while others get off scot-free.

The new IRS memorandum says revenue officers should determine case-by-case how much documentation will support a penalty. Key issues are the “responsibility” and “willfulness” factors. In determining “willfulness,” courts focus on whether you had knowledge of the non-payment of taxes or showed reckless disregard whether they were being paid.

But a person need not actually perform the withholding and payment functions to be considered “responsible.” If you have signature authority (whether or not you exercised it) while other (non-IRS) payments are being made, that can be enough to result in liability. Most of the time, here’s what the IRS will collect to sink you:

1. “Form 4180” interviews: Form 4180 is the form that is used by the IRS to conduct interviews with each potentially responsible person;
2. Articles of incorporation;
3. Bank signature authority cards or electronic PINS/passwords; and
4. Copies of cancelled checks (or electronic payments or debits) demonstrating payment to ***other*** creditors (not the IRS). If the IRS can’t get the records easily from the business, the IRS will issue a summons to the business, the bank or both.

Individual factors will influence the amount of documentation needed to support a penalty. IRS revenue officers are directed to exercise judgment whether they need more. Often, though, these key elements will be enough to impose and support the penalty so be careful.

For more, see:

Supreme Court Deaf To Payroll Tax Woes

Don’t Cross The IRS On Payroll Taxes

Fail To Pay Payroll Tax: Go To Jail

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