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THE TAX LAWYER

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No Get-Out-Of-Jail-Free Card For Payroll Tax Liability



As a full-time tax lawyer in private practice for [30 years](#), I've seen my share of tax messes. One of the most repetitive and serious is a failure to pay [payroll taxes](#). The IRS breaks this problem into two parts, with the worst part being withholding the taxes from employee pay and then using it for something else—**anything** else.

Quite rightly, the IRS views this as government money, a [trust fund](#) that belongs to the IRS. In a cash-strapped business it may be tempting to think you can always pay the IRS later. After all, keeping the lights on or the warehouse stocked seems more important.

But these problems have a way of snowballing and it is best not to be tempted. Besides, business owners and other "[responsible persons](#)" have personal liability for these taxes. For these reasons, I've long suggested that businesses consider using payroll services.

That way the service does the withholding and all funds are taken out of the business' account when employees are paid, even the portion intended for the IRS. No matter what your cash needs, if you have enough to pay employees you must pay the IRS too. In my experience, the IRS is a big fan of payroll services, especially for businesses that have previously run afoul of these rules.

Yet recently, the IRS has made it clear that the mere fact you use a payroll service does **not** mean you are not on the hook. See [IRS e-News for Small Businesses, Issue No. 2011-17, 8/3/2011](#). Employers are responsible for paying the income tax withheld, plus the employer and employee portions of Social Security and Medicare taxes. This is so even if you outsource your payroll responsibilities to a third party.

Plainly, outsourcing can help ensure that filing deadlines and deposit requirements are met. It can even streamline your operations. But ultimately it's the employer's responsibility to pay these taxes even if the failure is due to the payroll company's negligence or fraud! See [IRS: Outsourcing Payroll Duties](#).

The IRS offers these suggestions:

- **Address of Record is Key.** Don't change your address with the IRS to that of your payroll service. That can be tempting, since you want the payroll service to deal with all these payroll issues. But don't do it! If there are any problems with your account, you want the IRS to contact you—the employer—right away. If you change your address to the payroll company's and something goes wrong you may not get a timely notice. That may cut short your rights.
- **Use Electronic Federal Tax Payment System.** Make sure that your payroll service is using the Electronic Federal Tax Payment System ([EFTPS](#)). EFTPS maintains a business's payment history for 16 months and can be viewed on-line. That means you can immediately confirm payments electronically, 24 hours a day, 7 days a week, through the Internet or by phone. Employers should register on the EFTPS system to get their own PIN and use this PIN to periodically verify payments. Employers with an EFTPS account can also make additional tax payments their payroll service isn't making on their behalf (e.g., estimated tax payments).
- **Don't Forgive Late or Missed Payments!** A red flag should go up the first time a payroll service provider misses a payment or is late.

- **Beware Fraud.** There have been cases where individuals and companies acting under the guise of payroll service providers have stolen funds intended for employment taxes. See [Examples of Employment Tax Fraud Investigations](#) for some recent IRS employment tax fraud investigations. If you believe that a bill or notice is due to a problem with your payroll service, contact the IRS ASAP by calling the number on the bill, writing to the IRS office that sent it, calling (800) 829-4933, or visiting a [local IRS office](#).

For more, see:

[IRS Penalties Despite Dead/Embezzling Accountant!](#)

[Personal Tax Liability When A Business Goes Under](#)

[Personal and Transferee Liabilities](#)

[With Taxes “Responsible” Means Holding The Bag](#)

[IRS “Responsible Person” Label Hurts](#)

[IRS Publication 15 \(2011\), Employer’s Tax Guide](#)

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