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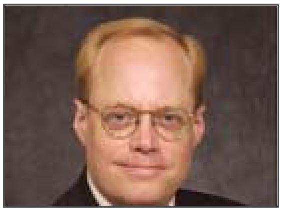

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True Think Different? Neither An Officer Nor Director Be

Remember “neither a borrower nor lender be?” Shakespeare said it, although some credit Benjamin Franklin. Whoever gets the by-line, most of us violate it on both sides of the equation. After all, it feels good to be named an officer, director or both. And it can carry perks too.

Still, if you are facing the IRS, it’s worth rethinking whether there’s a downside to having a title and authority. If taxes aren’t being paid or there’s the risk they may not be in the future, consider steering clear of being an officer or director. Either can land you in the hot seat for taxes.

Take Schiffman v. United States, recently decide by a federal court in Rhode Island. The case involved a company that was years behind on both income and payroll taxes. The officers and directors ran for cover, but the IRS pursued them. And when the case went to court, the court agreed with the IRS.

(Photo credit: Wikipedia)

The tax code imposes a 100% penalty on any person who: (1) is responsible for collecting, accounting for, and paying over payroll taxes; and (2) willfully fails to perform this responsibility. Why is the penalty 100%? It equals the amount of tax that was not collected.

Section 6672 of the tax code imposes this 100% penalty on responsible persons who fail to withhold, or who withhold but fail to hand it over to the IRS. The penalty can be assessed against more than one responsible person. IRS can collect only once, but it can come after them all and see who coughs up the money first.

Think it's really hard for the IRS to prove someone is responsible? Think again. In determining whether an individual is responsible, courts consider whether the individual: is an officer or member of the board of directors, (2) owns shares or has an entrepreneurial stake in the company, (3) is active in day-to-day affairs, (4) can hire and fire employees, (5) makes decisions about when and in what order to pay debts or taxes, (6) exercises control over bank accounts and disbursements, and (7) has check-signing authority.

Officers and directors are usually responsible, but what about willfulness? That's also usually not hard to satisfy. The courts ask if you have knowledge about the nonpayment of the payroll taxes, or if you showed reckless disregard with respect to whether the payments were being made.

Here, the court found the officers and directors did have enough authority that they were responsible. Plus, the court said that they were wilful. After all, each of them could have directed that money being used to pay creditors should go to the IRS.

How long does this responsible person liability last? The IRS statute of limitations on collection is normally 10 years. That's a long time. And would you believe in one recent case the IRS was able to go back 30 years?

In Beeler v. Commissioner, the Tax Court held Mr. Beeler responsible for 30 year- old payroll tax penalties. That may sound crazy, but sometimes, the IRS has a memory like an elephant.

Pay your payroll taxes. If you can't handle it in-house, hire a good payroll service so you won't have any discretion about it. If you aren't an owner, try to avoid check signing authority. If you can't avoid it, get a written indemnity, and make sure payroll taxes are always paid.

You can reach me at Wood@WoodLLP.com. This discussion is not intended as legal advice, and cannot be relied upon for any purpose without the services of a qualified professional.