Beware Risks Of Delaying Tax Payments

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As the coronavirus or COVID-19 outbreak has impacted almost every part of American business, many owners, officers and accountants are left wondering: Do I still have to pay my taxes on time? The default answer to this question should be yes, as to most tax types.

If you think that there might be an exception to this rule, it is important to confirm that position, and then double-check your sources. Recently, articles have been circulating that give bad advice and contain inaccurate information, advising businesses to delay payment of trust fund taxes.

Tax compliance with respect to trust fund taxes is critical because of the harsh repercussions that may apply to those officers and "responsible persons" who fail to make tax payments on time. These harsh repercussions include personal liability, not only taxes but also penalties and interest that can often double the amount owed, and potentially criminal punishment for those responsible persons.

The recent postponement of certain income tax filing deadlines does not apply to all taxes.

There has been a recent wave of news regarding the delay or suspension of tax filings in response to the coronavirus crisis. Importantly, these delays mainly involve income taxes, not all taxes.

For example, Secretary of the Treasury Steven Mnuchin announced by tweet on March 20 that the deadline for 2019 federal income tax filings would be postponed until July 15. Later that same day, the IRS issued Notice 2020-18, reiterating Mnuchin's announcement and explaining that the deadline applied to 2019 and first-quarter 2020 income tax filings for any individual, trust, estate, partnership, association, company or corporation.

This same notice also confirmed the following:

No extension is provided in this notice for the payment or deposit of any other type of federal tax, or for the filing of any federal

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information return.

As of the date of this article, Ohio has not yet officially postponed its income tax filing deadline or any other tax deadline. However, several other states, such as Indiana, have come forward in confirming that they will also be extending their deadline for 2019 income taxes only. It is important to keep this limitation in mind as there are many other types of taxes (federal, state and local) that a company may remain responsible to pay on schedule.

Even if some taxes are permissibly deferred, defer at your own risk.

Some states are making statements that certain tax payments may be deferred or postponed for certain taxpayers. For example, in its March Informational Bulletin, Illinois announced that it was permissible for small and mid-sized bars and restaurants (those that paid less than $75,000 in sales taxes in the calendar year 2019), to delay their sales tax payments. Such businesses still will have to file returns for March, April and May, but will be allowed to withhold payment without interest or penalty, provided they make the payments in four installments, from May 20 to Aug. 20.

While this deferral along with the deferral of other payments, such as rent, may seem enticing, taxes can be a whole other animal.

As referenced above, responsible persons can have personal liability and other repercussions for failing to pay certain taxes. While the tax types can vary, two types of taxes that are nearly always involved are payroll and sales/use taxes.

Payroll and sales/use taxes are considered “trust fund taxes” because a business is collecting the sales tax and withholding the employment tax on behalf of the taxing authority. A simple example of this is with sales tax: The business making the sale does not truly pay the sales tax; the cost is imposed on the buyer and the seller is responsible for holding that tax in trust before remitting it to the government.

In many jurisdictions, including federal, there are severe penalties for noncompliance with these trust taxes that could be imposed on

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owners and officers personally. For example, assume a restaurant chief financial officer defers payment of sales taxes pursuant to a government notice. What happens if the business runs out of money between the time of deferral and the time of payment? The answer is simple and unfortunate: The CFO could have personal liability for this underpayment, including penalties, interest and possibly other repercussions.

Who is a responsible person?

Jurisdictions vary as to how they classify someone as a "responsible person," but the most common indicators include:

- Officer/manager status;
- Control over the business activities;
- Responsibility for the preparation and filing of tax returns;
- Authority to sign tax return and checks on behalf of the business;
- Equity ownership in the business; and
- Authority to hire and fire employees.

These responsible persons often hold the title of chief financial officer, treasurer or manager, but can include many other stakeholders of a company. Certain states might deem certain titleholders to presumably be a responsible person. Other states and the IRS focus more on a person's duties as opposed to their title.

Responsible-person liability can be severe.

States are traditionally aggressive in holding responsible persons liable for any failures to withhold or pay appropriate taxes. For example, in Kentucky, managers of a limited liability company or any person holding any equivalent office will be personally and individually liable, jointly and severally,[1] for the collection and remittance of the taxes.

Similar rules apply in Ohio. However, Ohio will even impose personal liability on employees "who are responsible for the execution of the corporation's, limited liability company's, or business trust's fiscal

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responsibilities" regardless of whether they are an officer, manager or equity owner.[2]

There may also be criminal penalties imposed on responsible persons. With respect to federal taxes, under IRC 7202, a responsible person who fails to collect, account for, and pay over the trust fund taxes, such as the employee portion of payroll taxes, is guilty of a felony, punishable by a $10,000 fine or imprisonment of up to five years, for each offense.[3] For Kentucky payroll taxes, there is also a criminal penalty. Under KRS 141.990, if the failure to pay is willful, the person will be guilty of a Class D felony.

Importantly, in many states, the dissolution of the company does not remove liability, nor does ceasing to no longer hold the position as a responsible person. Liability can attach at the time the taxes become due.

Even more surprising to some, the definition of "tax" often includes the accruing interest and penalties for the purposes of "responsible-person" liability. This means that state tax debts of a company can haunt individuals long after their involvement with the company, and can also unwittingly create liability for those who assume "responsible-person" positions long after the original liability was incurred. In Ohio, responsible persons can remain liable for a company's tax debts even after a bankruptcy.[4]

A particularly stringent application of responsible-person liability was found in *Gillan v. Testa*.[5] In this case, the Ohio Board of Tax Appeals found that a corporate officer was personally liable for a corporation's unpaid sales taxes despite the fact that the corporation had gone into receivership.

The court affirmed the application of derivative liability, granting the former officer no ability to argue the merits of the underlying assessment or whether tax was paid. The court also confirmed that a responsible officer or employee needs to only have knowledge of a duty to pay taxes and authority to write checks; he or she does not have to participate in or supervise the company's fiscal duties.

The court also held that responsible-person liability can attach to more than one individual and there is no requirement that liability

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must attach to the most "appropriate" person. Additionally, the court held that a corporate receiver's appointment does not alter the duties of a responsible person, even when the officer had no right to control payments made by the company while in receivership.

Conclusion

These responsible-person rules should serve as a warning to any officer (or other responsible person) who is considering delaying their tax payments in the wake of the coronavirus disruption. Even if the state permits a company to postpone a payment, this will (typically) not diminish the amount of underlying assessment or amount due.

If the company were ever to enter a restructuring (e.g., bankruptcy) because it cannot satisfy its tax debts or any other debts, the tax debts of the company can remain attached to the responsible person at the time the tax debt was incurred.

More importantly, if companies have questions about whether they can or should postpone a tax payment, they should verify their eligibility with a tax professional and consider whether it can lead to risk of personal exposure for any stakeholder.

For more information please contact Mark Sommer, Daniel Mudd, Elizabeth Mosely or any attorney in Frost Brown Todd's Tax practice group.

Note: This article originally appeared on Law360's State and Local Tax Wire *and has been reprinted with permission from Law360.* Click here to read the full article.

To provide guidance and support to clients as this global public-health crisis unfolds, Frost Brown Todd has created a Coronavirus Response Team. Our attorneys are on hand to answer your questions and provide guidance on how to proactively prepare for and manage any coronavirus-related threats to your business operations and workforce.

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[1] When two or more parties are jointly and severally liable for a tortious act or error, each party is independently liable for the full extent of the harm stemming from the tortious act or error.

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[2] See O.R.C. 5739.33.

[3] See United States v. Sertich , 879 F.3d 558 (5th Cir. 2018).

[4] See O.R.C. 5739.33.

[5] Gillan v. Testa , Ohio BTA Case No. 2014-1340 (Oct. 22, 2014).

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