

“PAYROLL AGENT” AMENDMENTS TO HR 1528:
PROPOSED REVISIONS

As passed by the Senate on May 19, 2004, HR 1528, The Tax Administration Good Government Act, includes provisions that would impose new regulatory requirements on “payroll agents.” While the National Payroll Reporting Consortium (NPRC)¹ recognizes that there have been isolated instances of unscrupulous persons collecting tax payments from businesses and failing to transfer such payments to tax authorities, we are concerned that any legislative response to these isolated instances not impose a cumbersome regulatory burden on a payroll services industry that has been functioning very effectively, to the benefit of the Federal Government and our taxpayer customers alike. Accordingly, while we do not believe there is need for this amendment as a whole, several changes in the payroll agent provisions must be made to eliminate drafting ambiguity and to ensure that the provisions, if enacted, are effective in accomplishing the intended goals.

The payroll agent provisions were added as a Senate floor amendment to section 141 of H.R. 1528, a provision initially designed to impose new requirements on federal income tax return preparers and refund anticipation loan providers. The payroll agent provisions added by the amendment direct the Treasury to prescribe regulations requiring payroll agents to register and to post a “reasonable” bond. As written, payroll agents might potentially be subject to other requirements more properly applicable to return preparers and refund anticipation loan providers. In addition, section 154 of the bill, added by the Senate amendment, would subject payroll agents to the current IRC penalties under section 6672 relating to the failure to collect and pay over taxes.

Payroll Processing Industry

Payroll agents serve a critical role in our nation's tax collection system by facilitating accurate and timely tax payments from employers to federal, state and local tax authorities. Payroll agents provide payroll and employment tax administration services for approximately 20 percent of U.S. employers, covering one-third of the private sector work force. They accurately and timely transmit more than \$500 billion annually in employment and income taxes to the Federal Government, or approximately 25 percent of the Federal Government’s annual receipts. Payroll and tax administration are among the most complex U.S. business activities, and the ability to outsource payroll and tax administration frees business owners to concentrate on improving their businesses.

¹ NPRC members contributing to this paper include Automatic Data Processing, Inc., Ceridian Corporation, Compupay, Inc., Federal Liaison Services, Inc., Intuit Inc., Paychex, Inc., Payroll People, Inc., PrimePay, Inc.

In recent history, there have been rare instances of the failure of small payroll service providers in which client tax funds were not transmitted to federal and/or state tax authorities. It is important to note that 99.99% of payroll agent clients nationwide have not suffered any losses and have benefited significantly from the specialized knowledge and sophisticated systems that payroll service providers employ to administer employment taxes. The annual amount lost nationwide due to the fraud or failure of a payroll service provider is .00097% (.000097) of total federal taxes deposited by payroll service providers.

Proposed Revisions to Senate Payroll Agent Provisions

In order to establish rules for payroll agents that are clear and precise, the Senate amendments should be modified as follows:

- ❖ Create separate IRC provision to govern payroll tax deposit agents. Issues involved in the registration and bonding of payroll tax deposit agents are different from rules designed to regulate income tax return preparers and refund loan providers. Payroll tax deposit agents provide an administrative service; they do not provide technical tax assistance in the completion of tax returns, nor are they in the business of lending funds to clients.
- ❖ Establish definition of payroll tax deposit agent. The statute should be clear that the new rules would apply to any person that provides payroll tax deposit services if such person has the authority to take control of an employer-client's funds for the purpose of making federal payroll tax deposits.
- ❖ Registration fees and penalties for failure to register. Registration fees and penalties for failure to register should be set forth in the statute.
- ❖ Bonding requirements. The bonding requirement should be set forth in statute and be sufficient to ensure that a bond surety company will undertake the necessary due diligence before issuing the bond, but not so onerous as to prevent payroll tax deposit agents from securing a bond. As was established with bonding under ERISA, the importance of this requirement is to ensure that "another set of eyes" (i.e. the surety company) examines the character and financial responsibility of the entity handling funds. The bonding requirement may be waived if the payroll tax deposit agent meets such fiduciary standards as may be established by the Secretary.
- ❖ Disclosure requirements. IRS should require payroll tax deposit agents to disclose to potential employer clients that the employer remains liable for all employment taxes and that the employer should verify periodically that all tax payments are credited to their account with tax authorities.
- ❖ Verification of address change. Standards should be set to ensure that employer address changes are not falsely reported to the IRS. The Secretary should issue a

notice of confirmation of any address change relating to an employer making tax payments under subtitle C, and such notice should be sent to both the employer's former and new address.

- ❖ Section 6672 penalties. The language extending the section 6672 “failure to collect” penalties to payroll agents should be clarified to apply only where the employer had actually made the necessary transfer of funds to the payroll tax deposit agent. In addition, a clerical change is needed to ensure that the other provisions of this section (e.g., preliminary notice requirement, etc.) apply to both the taxpayer and the payroll tax deposit agent.

A draft of the proposed new payroll tax deposit agent section and the proposed changes to section 154 of the Senate amendment (the section 6672 amendments) are attached.

SEC. [XXX]. REGULATION OF PAYROLL TAX DEPOSIT AGENTS.

(a) IN GENERAL- Chapter 77 (relating to miscellaneous provisions), as amended by this Act, is amended by adding at the end the following new section:

SEC. 7531. PAYROLL TAX DEPOSIT AGENTS.

(a) REGISTRATION-

(1) IN GENERAL- The Secretary shall establish a system for the annual registration of persons seeking to be qualified as payroll tax deposit agents authorized to make federal tax deposits on behalf of employer taxpayers. Such system shall --

(A) establish such payroll tax deposit agent standards as may be relevant and appropriate to perform federal payroll tax deposit services including annual registration, character and fitness,

(B) require disclosure to the Secretary of such business information as the Secretary deems necessary to carry out the requirements of this section,

(C) provide that the Secretary shall take into consideration any additional information, including third party reports, submitted by the registrant to establish its character and fitness,

(D) establish an annual registration fee for each payroll tax deposit agent registrant in an amount not to exceed \$1,000,

(E) require a bond or, in lieu of such bond, the meeting of fiduciary standards as specified in subsection (b),

(F) require such disclosures as are specified in subsection (c), and

(G) provide penalties for persons not registered under this section who are acting as payroll tax deposit agents with respect to federal tax deposits in an amount not to exceed \$25,000 for each 30 days of noncompliance.

(2) DEFINITION OF PAYROLL TAX DEPOSIT AGENT- For purposes of this section, the term "payroll tax deposit agent" means any person that provides payroll tax deposit services to one or more employers (other than an employer acting on its own behalf) if such person has the contractual

authority to take control of such employer's funds for the purpose of making payroll tax deposits. In the case of a corporation (or a controlled group of corporations under section 1563) or a partnership that carries on a trade or business as a payroll processor providing payroll tax deposit services to employers, such corporation or partnership (and not its individual employees) shall be considered the payroll tax deposit agent.

`(b) BONDING-

`(1) IN GENERAL- Every payroll tax deposit agent required to register pursuant to this section shall be bonded.

(2) AMOUNT OF BOND- The amount of such bond shall be not less than \$50,000 nor more than \$500,000.

(3) SURETY- Any bond or security furnished pursuant to this section shall be in such form and with such surety or sureties as may be prescribed by regulations issued pursuant to section 7101.

(4) WAIVER - The Secretary shall waive the bonding requirement under paragraph (1) if the payroll tax deposit agent meets such fiduciary standards as may be established by the Secretary.

`(c) DISCLOSURE- The Secretary shall require payroll tax deposit agents to disclose to each potential and existing client prior to or at the time of contracting for payroll services --

(1) the client's continuing liability for payment of all federal and state taxes notwithstanding any contractual relationship with a payroll tax deposit agent, and

(2) the mechanisms available to the client to verify the amount and date of payment of all tax deposits made by the payroll tax deposit agent on behalf of such client.

‘(d) AGENT AUTHORITY- A payroll tax deposit agent who is not registered under this section shall not have authority to sign and file federal employment tax returns on behalf of a taxpayer or to access confidential tax information relating to such taxpayer.

‘(e) VERIFICATION OF ADDRESS CHANGE- The Secretary shall issue a notice of confirmation of any address change relating to an employer making tax payments under subtitle C. Such notice shall be sent to the employer's former and new address.

(f) REGULATIONS- The Secretary shall prescribe such regulations as may be necessary to carry out the provisions of this section.

(b) CLERICAL AMENDMENT- The table of sections for chapter 77, as amended by this Act, is amended by adding at the end the following new item:

`Sec. 7531. Payroll Tax Deposit Agents.'

(c) EFFECTIVE DATE- The amendments made by this section shall take effect on the first day of the first month beginning more than 180 days after enactment of this Act.

SEC. 154. PAYROLL TAX DEPOSIT AGENTS SUBJECT TO PENALTY FOR FAILURE TO COLLECT AND PAY OVER TAX, OR ATTEMPT TO EVADE OR DEFEAT TAX.

(a) IN GENERAL- Section 6672(a) is amended by inserting `, including any payroll tax deposit agent (as defined in section 7531(a)(2)) who has assumed the obligation to pay over any tax by contract with a taxpayer but only to the extent that such payroll tax deposit agent has received irrevocable payment of funds for the corresponding tax liabilities from such taxpayer,' after `and pay over' the first instance it appears.

(b) PENALTY NOT SUBJECT TO DISCHARGE IN BANKRUPTCY- Section 6672(a) is amended by adding at the end the following new sentence:
`Notwithstanding any other provision of law, no penalty imposed under this section may be discharged in bankruptcy.'

(c) CONFORMING- Section 6672(b)(1) is amended by striking the word `taxpayer' and inserting the word `person' each time it appears.

(d) CONSTRUCTION- The amendment made by subsection (a) shall not be construed to create any inference with respect to the interpretation of section 6672 of the Internal Revenue Code of 1986 as such section was in effect on the day before the date of the enactment of this Act.

(e) EFFECTIVE DATE- The amendments made by this section shall apply to failures occurring after the date of the enactment of this Act.

Draft Report Language

A payroll tax deposit agent is any person who provides payroll tax deposit services to one or more employers (other than an employer acting on its own behalf) if such person has contractual authority to take control of employer funds for the purpose of making payroll tax deposits. A business or person who provides payroll processing services but does not have authority to access a client's bank accounts or other sources of client funds does not have control of employer funds and, therefore, would not be treated as a payroll tax deposit agent. Similarly, a person or business who provides payroll processing services and who only is authorized to initiate on behalf of an employer tax deposits using EFTPS that flow directly from the taxpayer's account to the Internal Revenue Service does not have control of employer funds and would not be treated as a payroll tax deposit agent.