Subtitle C of the Internal Revenue Code – Employment Taxes

Government Employers are required to deduct and withhold federal income tax and Federal Insurance Contributions Act (FICA) taxes (social security and Medicare) from wages paid to their employees under sections 3402(a) and 3102(a), and are separately liable for the employer’s share of FICA taxes under section 3111. These taxes are collectively referred to for purposes of these proposed regulations as employment taxes. Sections 31.3102-1(d), 31.3202-1(e) and 31.3403-1 establish that the employer is the person liable for the withholding and payment of employment taxes, in spite of whether amounts are actually withheld.

An employer may enter into an agreement with a payroll service provider (PSP) to prepare employment tax returns using the EIN of the employer for the signature of the employer. A PSP may also process the withholding, deposit, and payment of the associated employment taxes for the employer. A PSP is not liable under Subtitle C of the Code as the employer, or as an agent of the employer, for the employer’s employment taxes.

Use of a PSP does not relieve the employer of its employment tax obligations or liability:

An employer may mistakenly believe it is relieved of employment tax liabilities merely because it has entered into an agreement with a third-party payor (for example, an employee leasing company) for assistance in fulfilling its employment tax obligations. However, an employer remains liable for employment taxes irrespective of any agreement it may enter into that purports to place the employment tax obligations and liabilities with the payor. In this regard, status as the employer of the worker is determined based on all the facts and circumstances under the common law test (or under other specific Code provisions related to particular types of employees, such as elected officials).

Though most third-party payors provide very good service, there are, unfortunately, some who do not have their clients’ best interests at heart. A number of individuals and companies providing payroll services have been prosecuted for stealing funds intended for the payment of payroll taxes. Here are some steps employers can take to protect themselves from unscrupulous third-party payers.

- Enroll in the “Electronic Federal Tax Payment System” (EFTPS) and make sure the third party payor uses EFTPS to make tax deposits. EFTPS gives employers safe and easy online access to their payment history when deposits are made under their Employer Identification Number, enabling them to monitor whether their third-party payer is properly carrying out their tax deposit responsibilities.
- Refrain from substituting the third-party’s address for the employer’s address. Though employers are allowed to and have the option of making or agreeing to such a change, the IRS recommends that employers continue to use their own address as the address on record with the tax agency. Doing so ensures that the employer will continue to receive bills, notices and other account-related correspondence from the IRS and gives employers a way to monitor the third-party payor.
- Contact the IRS about any bills or notices and do so as soon as possible. This is especially important if it involves a payment that the employer believes was made or should have been made by a third-party payor. Call the number on the bill, write to the IRS office that sent the bill, contact the IRS business tax hotline at 800-829-4933 or visit a local IRS office.