Ignorance Is Not Bliss

CEOs May Be Personally Liable for Company Taxes - Even in Bankruptcy

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FACTS:

- Company is undergoing bankruptcy proceedings.
- Company has unpaid debts including payroll taxes.
- CEO has control of all aspects of the company.
- CEO submits to the Bankruptcy Court, on behalf of the company, several legal filings including the business's liabilities prepared by the CFO.
- CFO did not fully inform the CEO as to the extent or character of the outstanding business liabilities.
- CEO has to write a personal check to satisfy the outstanding New Mexico payroll withholding tax liability, penalties, and interest.

WAIT! WHAT??

The CEO is held personally liable for the business's unpaid New Mexico payroll withholding tax, the assessed penalties and interest.

This is one of those cases of "you actually know or should have known" that are often written into the tax laws. You see, even though the CEO did not have actual knowledge of the outstanding liabilities; he had all of the information available at his fingertips. And, since he had the power for enforcing policies for prioritizing and paying debts, writing checks, processing mail, and managing personnel, thereby making sure that those withholding taxes got paid to the state first, New Mexico deemed him to personally meet the definition of an "employer".

So in other words, he should have known that the taxes were not being paid and acted responsibly in the State's best interest. The fact that he was not directly informed by someone else was not reasonable cause when determining his personal liability. Keep in mind, he did sign the reports filed with the court.

Now, yes, this case is in New Mexico. And, yes, this is only for state payroll withholding taxes. But if there is one thing that is consistent in the Tax World, it's that if one Department of Revenue is successful, others will not only try the same tactic, they will push the boundaries of the case.

Payroll taxes are what is referred to as a "trust tax". This means the business is temporarily stepping into the shoes of the Tax Authority to collect the tax from someone and then is responsible for remitting it to that Authority. At no time do the funds belong to the business, they are merely the facilitator.

Why is this important? Well the payroll tax is only one type of "trust taxes" a business is responsible for handling. Others include state and local sales taxes and, in some states, unemployment taxes that are withheld from employees paychecks.

And from there, it's a short leap to other withheld liabilities such as State Disability Insurance.

The lesson to be learned here:
As a responsible person you need to be aware of the business's outstanding liabilities and the potential to be held personally liable if they are not satisfied.

Otherwise, you may be writing a check personally.

If you wish to learn more, contact your Client Service Coordinator or Victoria S Carlin, CPA at vcarlin@dopkins.com.

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Victoria has over 25 years of experience in providing tax consulting, compliance and tax audit representation to closely held businesses and the owners of closely held businesses. She delivers a full range of tax services in covering federal and multi-state laws and regulations for partnerships, S and C corporations, and individuals.