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Dan Heller Presents: How to Settle the TFRP Devil

An Introduction to the Trust Fund Recovery Penalty
Disclaimer

Names, characters, businesses, identification numbers, places, events, locales, and incidents are either the products of the author’s imagination or used in a fictitious manner. Any resemblance to actual persons, living or dead, or actual events is purely coincidental.
Prologue: Once upon a time...

John P. Bentley was a receptionist. He made a moderate salary, and enjoyed his job. He worked for a small, 3-person company, Rain Forest Delivery, Inc., which was owned and operated by Rich Worthington.

After working at Rain Forest for a few years, he thought the company was thriving and that everything was going well. That is until he received a letter from the IRS.
We received information indicating you may be responsible for the unpaid trust fund tax for the business named below. We encourage you to contact us if you have information that would help us determine your personal liability.

Business Name: RAIN FOREST DELIVERY INC

The business has not paid its employment taxes. A portion of the owed amount relates to trust fund taxes. We're initiating an investigation to determine who may be personally responsible for the unpaid trust fund portion of the total unpaid employment tax.

We'll continue to correspond with you or your authorized representative on this issue. If you can't provide or verify information we need, we may need to contact other people such as neighbors, banks, employers, or employees. We'll give them limited information, such as your name, because the law prohibits us from disclosing more information than is necessary. We may need to contact other people for the duration of this investigation. You have a right to request a list of people contacted.

We've also included Publication 1, Your Rights as a Taxpayer. The publication describes the Taxpayer Bill of Rights and the processes for examination, appeal, collection, and refunds.

If you have questions about this letter or want to request a list of the other people we've contacted, you can contact the person at the top of this letter. When you write, include the person to contact's name and the employee ID number shown above.

Sincerely,

REVENUE OFFICER

Enclosure: Publication 1
What Now?

Suffice to say, John was confused and scared. He did not understand what this letter meant, or what could happen to him. He did what any prudent taxpayer would do, and Googled a local lawyer. He found you. And so the story begins.

*For the remainder of this webinar, you will be John’s lawyer.*
Chapter 1: What is the Trust Fund Recovery Penalty?

John had a lot of questions during your initial meeting. What were trust fund taxes and the Trust Fund Recovery Penalty? Was he going to be personally liable? What were the next steps?

The Trust Fund Recovery Penalty, or TFRP, is the personal assessment of a business’s payroll taxes that were withheld from its employees but not remitted to the United States. It is assessed pursuant I.R.C. §§ 6672 & 7501, which allow the IRS to pierce the corporate veil.
Calculating the TFRP

The TFRP is comprised of the following employment taxes reported on Form 941, Employer’s QUARTERLY Federal Tax Return:

• Federal income tax withheld from wages
• Social Security tax withheld from wages
• Medicare tax withheld from wages
Calculating the TFRP, cont’d
(the math portion of the story)

Rain Forest Delivery – Form 941 for the 2\textsuperscript{nd} Quarter of 2018

• Line 3: Federal income tax withheld: $2,834.64

• Line 5a: Social Security tax: $3,722.82
  • The tax rate is 6.2%. This tax is both withheld from the employee and matched by the employer, at 6.2% each. Only the withheld portion is subject to the TFRP.

• Line 5b: Medicare tax: $870.66
  • The tax rate is 1.45%. This tax is both withheld from the employee and matched by the employer, at 1.45% each. Only the withheld portion is subject to the TFRP.

• Total TFRP: $2,834.64 + $3,722.82/2 + $870.66/2 = $5,131.38
Who can be assessed the TFRP?

I.R.M. 8.25.1.3 (09-11-2018)

Requirements for Liability Under IRC 6672

(1) The TFRP may be asserted against any person "responsible" for collecting, accounting for, and paying over trust fund tax who:

   a. willfully fails to collect such tax, or
   b. fails to truthfully account for and pay over such tax, or
   c. willfully attempts in any manner to evade or defeat any such tax or the payment thereof.
Who is responsible?

I.R.M. § 8.25.1.3.1 (09-11-2018)

Definition of a Responsible Person

(1) A "responsible person" is one who has the duty to perform or the power to direct the act of collecting, accounting for, or paying over trust fund taxes.
A person is not presumed to be a responsible party merely because of his title. *O’Connor v. United States*, 956 F.2d 48, 51 (4th Cir. 1992). The Fourth Circuit Court of Appeals states that the “crucial inquiry is whether the person had the effective power to pay taxes—that is, whether he had the actual authority or ability, in view of his status with the corporation, to pay taxes owed.” *Plett v. United States*, 185 F.3d 216, 219 (4th Cir. 1992).
What is willfulness?

I.R.M. § 8.25.1.3.2 (12-07-2012)

Definition of Willfulness

(1) The trust fund recovery penalty is a civil penalty; so the degree of willfulness in failing to collect or pay over any tax leading to liability for this penalty is not as great as that necessary for criminal proceedings. Willfulness in the context of the TFRP is defined as intentional, deliberate, voluntary, and knowing, as distinguished from accidental. "Willfulness" is the attitude of a responsible person who with free will or choice either intentionally disregards the law or is plainly indifferent to its requirements.
What is willfulness?, cont’d

I.R.M. § 8.25.1.3.2(1) (12-07-2012)

Some factors to consider when determining willfulness are:

- Whether the responsible person had knowledge of a pattern of noncompliance at the time the delinquencies were accruing;
- Whether the responsible person had received prior IRS notices indicating that employment tax returns have not been filed, or are inaccurate, or that employment taxes have not been paid;
- The actions the responsible party has taken to ensure its Federal employment tax obligations have been met after becoming aware of the tax delinquencies; and
- Whether fraud or deception was used to conceal the nonpayment of tax from detection by the responsible person.
Chapter 2: The Assessment Process

John was very curious about his exposure after you educated him about the TFRP. As explained later, the IRS interviews any individuals who it believes might be subject to the TFRP, such as officers of the business, people with check-signing authority, or whomever signed the unpaid Form(s) 941.

The IRS’ interview of those individuals is based on Form 4180, Report of Interview with Individual Relative to Trust Fund Recovery Penalty or Personal Liability for Excise Taxes. At this point, you decided to conduct your own mock interview to gauge John’s TFRP exposure.
The Mock 4180 Interview

After reviewing the Form 4180 interview questions with John, you determined his exposure was minimal. Based on the letter from Revenue Officer Vogue, you knew the only period at issue was the 2nd Quarter of 2018. John did not sign that Form 941, and had no decision-making authority in the business, either financial or tax, for that period or others. He also did not have access to any of the business’ financial records.

However, John had check-signing authority, and he recalled signing some checks in the 2nd Quarter of 2018. He explained that any checks were signed per Mr. Worthington’s explicit instructions, typically as a convenience to his boss when he was not at the office. John could not choose which bills to pay, though.
Chapter 3: The TFRP Interview

You then contacted Revenue Officer Vogue to schedule the TFRP interview at your office. You informed John that he will need to be present, as all questions would be directed to him. Your role would be to ensure the Revenue Officer understands and accurately reports John’s answers and any other relevant facts he states, while acting professionally and appropriately.

A few weeks later, the interview occurred. It began with you explaining John’s role in the company, and how he did not meet the statutory criteria for the assessment of the TFRP (i.e., willfulness and responsibility). The Revenue Officer then asked John the questions directly from Form 4180.
The TFRP Interview, cont’d.

The interview went as expected. Revenue Officer Vogue focused on the fact that John had check-signing authority. The Revenue Officer produced copies of the bank statements and checks, which he obtained from the bank via an IRS Summons. Of the 30 checks written for the business in the 2nd Quarter of 2018, John signed about half.

After being presented with those checks, you reiterated that John was instructed to sign each of those checks by the company’s president, Mr. Worthington, and that John did not have the discretion to sign checks without explicit approval. Revenue Officer Vogue asked if this approval was in writing, and according to John, it was always a verbal request from his boss.
Before the interview was complete, the Revenue Officer allowed John and you to review the Form 4180 before John was instructed to sign it. You requested an opportunity to write more details about John’s check-signing restrictions, and his limited role in the company’s operations. Revenue Officer Vogue agreed to allow you to write such a statement on Page 4, under Additional Information. You took advantage of this opportunity to emphasize the facts supporting John’s position that he should not be assessed a TFRP. The Revenue Officer told you that he will follow up with you after he completes his interviews of other potentially liable individuals.
After the Interview

All in all, the interview went well. You believed the Revenue Officer was receptive of your arguments, and understood that John, based on his role in the company, did not meet the criteria for the assessment of the Trust Fund Recovery Penalty.

30 days later, you received a notice that John would not be assessed a TFRP. John was off the hook. He survived his encounter with the TFRP devil, and lived happily ever after.

But, what if things went differently...
Chapter 4: An Alternate Ending

All in all, the interview went well. You believed the Revenue Officer was receptive of your arguments, and understood that John, based on his role in the company, did not meet the criteria for the assessment of the Trust Fund Recovery Penalty.

30 days later, you received a Letter 1153 and Form 2751, Proposed Assessment of Trust Fund Recovery Penalty.

You immediately reached out to Revenue Officer Vogue to ascertain why the TFRP was proposed. It appeared the Revenue Officer’s decision was solely due to the fact that John had check-signing authority. You explained that the statutory criteria requires more, but Revenue Officer Vogue was not interested in your argument. As explained in the Form 1153, you had 60 days to appeal this determination by filing a Protest.
Form 2751 (Rev. 1-2002)
Department of the Treasury – Internal Revenue Service
Proposed Assessment of Trust Fund Recovery Penalty
(See, e.g., Internal Revenue Code or corresponding provisions of prior Internal Revenue laws)
Report of Business Taxpayer’s Unpaid Tax Liability

Name and address of business
RAIN FOREST DELIVERY INC
71929 PRIME STREET
ALEXANDRIA, VA 20313-1317

<table>
<thead>
<tr>
<th>Tax Return Form Number</th>
<th>Tax Period Ended</th>
<th>Date Return Filed</th>
<th>Date Tax Assessed</th>
<th>Identification Number</th>
<th>Amount Outstanding</th>
<th>Penalty</th>
</tr>
</thead>
</table>

Agreement to Assessment and Collection of Trust Fund Recovery Penalty

Name, address, and social security number of person responsible
John P. Bentley, 5359 Audible CT, Alexandria, VA 20313-1317 231-89-1234

I consent to the assessment and collection of the penalty shown for each period, which is equal to the amount of federal employment taxes withheld from employees’ wages or to the amount of federal excise taxes collected from patrons or members, and which was not paid over to the Government by the business named above. I waive the 60-day protest on notice and demand set forth in Internal Revenue Code Section 6532(a).

Signature of person responsible

Date

Part 1 – Please sign and return this copy to Internal Revenue Service
Case No. 201-1234
Form 2751 (Rev. 7-2002)
The Protest

You decided to appeal the proposed TFRP by submitting a Protest to IRS Appeals, contesting the Revenue Officer’s determination. You followed the instructions detailed in the Letter 1153, which outlined the requirements of the Protest.

The Protest was your opportunity to explain the facts and legal arguments in support of John’s case. Your legal analysis focused on authority confirming that signing checks for a company does not automatically make an individual susceptible to the TFRP, as responsibility requires more (i.e., the duty to perform or the power to direct the act of collecting, accounting for, or paying over trust fund taxes).
The Appeals Conference

A few months later, you received a letter from IRS Appeals, confirming that a teleconference has been scheduled to discuss the proposed TFRP assessment. You informed John that he did not have to attend that hearing.

During the hearing, the Settlement Officer questioned your ability to prove that John only signed checks when instructed to do so by Mr. Worthington. You offered an affidavit from Mr. Worthington, as well as the business’ By-Laws, that confirmed only the President has financial decision-making authority. The Settlement Officer agreed to consider those documents, which you subsequently provided.

45 days later, you received a determination from Appeals, overturning the proposed TFRP assessment. John was off the hook. He survived his encounter with the TFRP devil, and lived happily ever after.
Chapter 5: One More Alternate Ending

The TFRP devil can be tricky, so what if the Settlement Officer upheld the proposed penalty? While this news disheartened John, you knew the law was on his side, and that he could still fight the assessment.

The next step was contesting the assessment by filing a refund claim. In order to file this claim, John had to first pay the withholding tax for one employee for the 2nd Quarter of 2018. Then, you submitted a Form 843, Claim for Refund and Request for Abatement, arguing that the TFRP assessment was improper, it should be overturned, and that John’s payment should be refunded.

If the request is granted, then John’s case is resolved. However, if this request is denied, you can still file a refund suit in federal court.
Epilogue

Some final thoughts:

• Proposed TFRP liabilities can be substantially higher than in this hypothetical. It is not uncommon for the proposed TFRP to be in the 6-figure range, depending on the size of the company and periods of non-compliance.

• Typically, your facts will be much less clear-cut. Your client might have signed the return, or had more authority in the company than John. In that case, you may end up in IRS Appeals or a refund suit, and you might need to consider settling for a partial TFRP assessment.

• If a potential client wants to know how to avoid potential TFRP exposure from his/her employer, you can use the TFRP criteria to suggest precautions (i.e., no check-signing authority; if any checks are signed, have the instructions / authorization to sign in writing; employment agreements detailing the employee’s scope of work; etc.).
When All Else Fails

If after exhausting all remedies, John’s TFRP assessment was upheld, you could still explore different collections alternatives to resolve the liability, based on his financial resources. The potential options include:

• Offer in Compromise
• Installment Agreement
• Partial Payment Installment Agreement
• Currently Not Collectible Status
Thank you for attending Dan Heller Presents: How to Settle the TFRP Devil.

If you have any questions, please contact me.

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