

**CITY OF MIAMI  
CITY ATTORNEY'S OFFICE  
MEMORANDUM**

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**TO:** Scott J. Simpson, Director  
Finance Department

**FROM:** Jorge L. Fernandez, City Attorney

**DATE:** June 13, 2005

**RE:** Request for Legal Opinion – City’s Liability for Untimely Payments of Payroll Taxes  
(MIA 05-00006)

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You have requested a legal opinion on substantially the following question:

**COULD THE CITY OF MIAMI (“CITY”) BE HELD LIABLE FOR PENALTIES ASSESSED BY THE INTERNAL REVENUE SERVICE (“IRS”) FOR SUBMITTING PAYROLL TAXES (“TAX”) ON A DATE AFTER TAX BECAME DUE, BY VIRTUE OF PAYROLL CHECKS GIVEN TO EMPLOYEES ON THURSDAYS RATHER THAN ON FRIDAYS, EVEN THOUGH PAYROLL CHECKS ARE DATED AS OF FRIDAYS?**

**DISCUSSION**

The City collects Tax from each employee for the services performed for the City by the employee. The Tax includes amounts for social security, Medicare and withheld income tax. For purposes of paying the Tax to the IRS, an employer is either a monthly depositor or a semiweekly depositor.<sup>1</sup> In accordance with the Federal tax deposit rules, the City applies a semiweekly deposit schedule for its payroll. However, if the City accumulates \$100,000 or more of Tax within the semiweekly deposit period, the Tax must be deposited in an authorized financial institution by the *close of the next banking day*.<sup>2</sup> Under this “next-day deposit rule,” the City must deposit Tax to the IRS within one banking day after Tax accrues to the City. The Tax accrues to the City at the time employees are paid; and City employees are generally paid on

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<sup>1</sup> 26 C.F.R. § 31.6302-1(a).

<sup>2</sup> 26 C.F.R. § 31.6302-1(3). (Emphasis added).

Fridays. In applying the next-day rule to the wages paid on a Friday, the City has until the following Monday (or the next banking day, should Monday fall on a legal holiday) to deposit Tax with the IRS. However, some employees are not paid on Fridays, but rather, are paid on Thursdays.

An employer becomes liable to the IRS for payment of Tax at the time the employee is paid.<sup>3</sup> The Tax attaches at the time the wages are received by the employee,<sup>4</sup> and wages are received by an employee at the time that they are paid by the employer to the employee.<sup>5</sup> Under the rule, an employer must collect the Tax from such wages *as and when paid*.<sup>6</sup> In defining "as and when paid," wages are deemed paid by an employer at the time they are actually or constructively paid;<sup>7</sup> and wages are constructively paid when they are credited to the account of an employee so that they may be drawn upon at any time although not then actually reduced to possession.<sup>8</sup>

Deposits of Tax on Mondays, for wages paid on Thursdays, may not satisfy the next-day rule. If the amount of Tax accruing on Thursday is \$100,000 or more, then the "next-day deposit rule" requires a Tax deposit before the end of business on Friday.<sup>9</sup> Payment of wages on two different days would necessitate two Tax deposits; one on Friday and one on Monday. The payment of wages on Thursday constitutes a Tax liability for the City payable within the close of the next banking day, which is Friday. Depositing Tax on a date after the Tax became due, is deemed untimely by the IRS.

The fiduciary role of employers is to accrue Tax as a special fund in trust for the United States.<sup>10</sup> Employers such as the City are required to pay 100% of their tax liability *on or before the deposit due date* or penalties may apply.<sup>11</sup> However, penalties will not apply for depositing less than 100% if both of the following conditions are met:

- any deposit shortfall does not exceed the greater of \$100 or 2% of the amount of taxes otherwise required to be deposited; and

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<sup>3</sup> A corporation becomes liable for payroll taxes the moment it paid wages to its employees regardless of whether the it placed the withheld funds in a segregated account, *U.S. v. Mitchell*, 82 Fed. Appx. 781 (3d Cir. 2003).

<sup>4</sup> 26 C.F.R. § 31.3101-3.

<sup>5</sup> 26 C.F.R. § 31.3121(a)-2(a).

<sup>6</sup> 26 C.F.R. § 31.3102-1(a). (Emphasis added). See also, 26 U.S.C.S. § 3102(a) (2005), the tax shall be collected by the employer by deducting the amount of tax from the wages *as and when paid*. (Emphasis added).

<sup>7</sup> 26 C.F.R. § 31.3121(a)-2(a).

<sup>8</sup> 26 C.F.R. § 31.3121(a)-2(b).

<sup>9</sup> See, I.R.S. Publication 15, Circular E, *Employer's Tax Guide*, \$100,000 Next-Day Deposit Rule (January, 2005).

<sup>10</sup> *U.S. v. Hill*, 368 F2d 617 (5<sup>th</sup> Cir. 1966).

<sup>11</sup> See, I.R.S. Publication 15, Circular E, *Employer's Tax Guide*, Accuracy of Deposits Rule (January, 2005). (Emphasis added).

- the deposit shortfall is deposited by the shortfall makeup date.<sup>12</sup>

The City's makeup date would be earlier of : a) the first Wednesday or Friday (whichever comes first) that falls after the 15<sup>th</sup> of the month following the month in which the shortfall occurred; or, b) the due date of Form 941 (for the quarter of the Tax liability).<sup>13</sup> Should penalties apply, the amount of such penalties will depend on the length of delinquency,<sup>14</sup> whether failure to remit timely was due to reasonable cause<sup>15</sup> or willful neglect.<sup>16</sup>

### CONCLUSION

The City is required to deposit 100% of Tax on \_\_\_\_\_ before the deposit due date. The liability for penalties assessed by the IRS for submitting tax on a date after Tax became due would depend on several factors which determine the City's level of compliance with the IRS Code. If payments of wages to employees on Thursday violate the "next-day deposit rule," the City's liability for any penalties would depend on the following factors: 1) whether the Tax shortfall exceeds the greater of \$100 or 2% of the amount of Tax otherwise required to be deposited, 2) whether the shortfall was deposited by the shortfall makeup date, 3) the length of delinquency, and 4) whether failure to remit timely was due to reasonable cause or willful neglect. Notwithstanding the existence (or absence) of penalties in the instant case, the City has a fiduciary duty to the United States to accrue and deposit Tax on a timely manner.

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<sup>12</sup> Id.

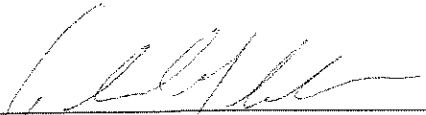
<sup>13</sup> *Employer's Tax Guide*, Makeup Date for Deposit Shortfall (January, 2005).

<sup>14</sup> 26 U.S.C.S. § 6656(b) (2005).

<sup>15</sup> 26 U.S.C.S. § 6656(a) (2005).

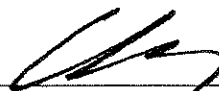
<sup>16</sup> IRC 1954 § 6672. Under the so called "100 percent penalty" statute, a person who is required to collect, truthfully account for, and pay over to the Federal Government withholding taxes, may be held liable to the government for a civil penalty equal to the amount of tax which he "willfully" failed to collect, or truthfully account for and pay over. C.T. Drechsler, Annotation, *Construction, Application, and Effect, with Respect to Withholding, Social Security, and Unemployment Compensation Taxes, of Statutes Imposing Penalties for Tax Evasion or Default*, 22 A.L.R.3d 8 (2005).

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