



MANUAL TRANSMITTAL

Department of the Treasury
Internal Revenue Service

5.17.7

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EFFECTIVE DATE

(06-23-2025)

PURPOSE

- (1) This transmits revised IRM 5.17.7, Legal Reference Guide for Revenue Officers, Liability of Third Parties for Unpaid Employment Taxes.

MATERIAL CHANGES

- (1) IRM 5.17.7 has been updated in compliance with presidential executive order 14151.
- (2) Fixed formatting errors throughout the IRM.

EFFECT ON OTHER DOCUMENTS

This material supersedes IRM 5.17.7 dated January 22, 2024.

AUDIENCE

Small Business/Self-Employed Collection Employees.

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5.17.7

Liability of Third Parties for Unpaid Employment Taxes

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5.17.7.1
(01-22-2024)
Program Scope and Objectives

- (1) **Purpose:** This IRM section provides legal guidance for Collection employees on the use of the Trust Fund Recovery Penalty (TFRP) as defined under IRC 6672, Failure To Collect And Pay Over Tax, Or Attempt To Evade Or Defeat Tax. This IRM section also discusses the liability of third parties paying or providing for wages under IRC 3505, Liability Of Third Parties Paying Or Providing For Wages.
- (2) **Audience:** The primary users of this IRM are Field Collection revenue officers (RO) and group managers (GM).
- (3) **Policy Owner:** Director, Collection Policy, Small Business/Sell-Employed Division (SB/SE).
- (4) **Program Owner:** Collection Policy, SB/SE, Employment Tax (ET) is the program owner of this IRM.
- (5) **Primary Stakeholders:**
 - Revenue officers
 - Revenue officer group managers
 - Specialty Collection – Insolvency (SCI) employees
- (6) **Program Goals:**
 - Explain the statutory requirements for determining liability for the Trust Fund Recovery Penalty under IRC 6672.
 - Explain the liability of third parties paying or providing for wages under IRC 3505.
 - Impart the provisions pertaining to the collection of the Trust Fund Recovery Penalty, including the authority to collect liabilities under IRC 3505(a) and IRC 3505(b).
 - Discuss the provisions pertaining to the collection of the Trust Fund Recovery Penalty when a taxpayer is in bankruptcy.
- (7) **Contact Information:** Email recommendations and suggested changes for this IRM to the Content Product Owner. The owner is listed on the Product Catalog Information page which is found in the Forms/Pubs/Products IRM listing of the Media and Publications web site. *Find a Product.*

5.17.7.1.1
(01-22-2024)
Background

- (1) The Trust Fund Recovery Penalty is based on IRC 6672(a) and facilitates the collection of tax and enhances voluntary compliance. The Trust Fund Recovery Penalty serves as an alternative means of collecting unpaid trust fund taxes when taxes are not fully collectible from the company/business that failed to pay the withheld taxes. Internal Revenue Manual (IRM) 5.17.7, Legal Reference Guide for Revenue Officers, Liability of Third Parties for Unpaid Employment Taxes, provides legal guidance on the use of the Trust Fund Recovery Penalty as defined under IRC 6672. This IRM section also addresses the liability of third parties paying or providing for wages under IRC 3505.

5.17.7.1.2
(01-22-2024)
Authority

- (1) The authorities for the actions discussed in this IRM are found in the following Internal Revenue Code:

U.S. Code Section	Title
IRC 3101	Rate Of Tax
IRC 3102	Deduction Of Tax From Wages
IRC 3202	Deduction Of Tax From Compensation
IRC 3402	Income Tax Collected At Source
IRC 3403	Liability For Tax
IRC 3505	Liability Of Third Parties Paying Or Providing For Wages
IRC 3509	Determination Of Employer's Liability For Certain Employment Taxes
IRC 3511	Certified Professional Employer Organizations
IRC 6103	Confidentiality And Disclosure Of Returns And Return Information
IRC 6303	Notice And Demand For Tax
IRC 6501	Limitations On Assessment And Collection
IRC 6502	Collection After Assessment
IRC 6671	Rules For Application Of Assessable Penalties
IRC 6672	Failure To Collect And Pay Over Tax, Or Attempt To Evade Or Defeat Tax
IRC 7501	Liability For Taxes Withheld Or Collected
IRC 7521	Procedures Involving Taxpayer Interviews
IRC 7602	Examination Of Books And Witnesses
IRC 7609	Special Procedures For Third-Party Summonses
40 U.S.C. 3131	U.S. Code, Performance Bond Provisions of the Miller Act

5.17.7.1.3
(01-22-2024)
**Roles and
Responsibilities**

- (1) The Director Headquarters Collection is the executive responsible for providing policy and guidance for IRS employees and ensuring consistent application of policy, procedures, and tax law to effect tax administration while protecting taxpayer rights.
- (2) The Director Collection Policy reports to the Director Headquarters Collection and is responsible for the delivery of policy and guidance that impacts the TFRP program.
- (3) The Program Manager, Employment Tax, reports to the Director, Collection Policy and is responsible for providing policy and procedural guidance on specialized processes to IRS employees.
- (4) Revenue officers are responsible for making collection determinations including Trust Fund Recovery Penalty recommendations.
- (5) Group managers have the authority and responsibility to review and approve Trust Fund Recovery Penalty recommendations.
- (6) Field Collection is responsible for ensuring taxpayers are informed of their rights in accordance with the Taxpayer Bill of Rights (TBOR) adopted in June of 2014.

5.17.7.1.4
(01-22-2024)
**Program Management
and Review**

- (1) Program Reports: The Automated Trust Fund Recovery (ATFR) program is used for group controls of imminent assessment statutes and timely TFRP case actions. ATFR pulls data from the Integrated Collection System (ICS) and the Integrated Data Retrieval System (IDRS).
- (2) Program Effectiveness: Embedded Quality (EQ) reviews conducted by GMs assess the timeliness of TFRP case actions. Collection Automation Support and Security (CASS) provides monthly ATFR timeliness reports that measure TFRP program timeliness goals. These reports provide the information necessary to allow ROs the opportunity to make timely and appropriate TFRP recommendations and assessment actions. Collection Policy does periodic program reviews to identify trends and opportunities to improve timely and effective TFRP case actions.

5.17.7.1.5
(01-22-2024)
Program Controls

- (1) ATFR tracks and records TFRP assessment actions and history. Field employees are generally the primary users of ATFR based on the employees' duties and responsibilities.
- (2) Field Collection employees use ICS for inventory control and history documentation.
- (3) GMs approve TFRP determinations and assessment recommendations.
- (4) Territory Managers (TM) and Area Directors (AD) include TFRP timeliness trends in operational reviews.
- (5) GMs are required to follow program management procedures and controls addressed in IRM 1.4.50, Collection Group Manager, Territory Manager and Area Director Operational Aid.

5.17.7.1.6
(01-22-2024)
Acronyms

- (1) This table lists commonly used acronyms and their definitions:

Acronym	Definition
ATFR	Automated Trust Fund Recovery Penalty Program
ATM	Appeals Team Manager
CPEO	Certified Professional Employer Organization
FICA	Federal Insurance Contributions Act
FUTA	Federal Unemployment Tax Act
ICS	Integrated Collection System
IDRS	Integrated Data Retrieval System
IRC	Internal Revenue Code
IRM	Internal Revenue Manual
LLC	Limited Liability Company
LLP	Limited Liability Partnership
PEO	Professional Employer Organization
PSP	Payroll Service Provider
RO	Revenue Officer
SB/SE	Small Business/Self Employed
SERP	Servicewide Electronic Research Program
TBOR	Taxpayer Bill of Rights
TFRP	Trust Fund Recovery Penalty
USC	United States Code

- (2) Additional acceptable acronyms and abbreviations are found in the ReferenceNet Acronym Database, which may be viewed at: *ReferenceNet Legal and Tax Research Services*.

5.17.7.1.7
(01-22-2024)
Related Resources

- (1) IRM resources

IRM	Title
IRM 1.2.1	Servicewide Policy Statements
IRM 5.1.10	Taxpayer Contacts
IRM 5.1.18	Locating Taxpayers and their Assets

IRM	Title
IRM 5.1.24	Third-Party Payer Arrangements for Employment Taxes
IRM 5.7.3	Establishing Responsibility and Willfulness for the Trust Fund Recovery Penalty (TFRP)
IRM 5.7.4	Investigation and Recommendation of the TFRP
IRM 5.7.6	Trust Fund Penalty Assessment Action
IRM 5.7.7	Payment Application and Refund Claims
IRM 5.9.8	Processing Chapter 11 Bankruptcy Cases
IRM 5.14.1	Securing Installment Agreements
IRM 5.14.2	Partial Payment Installment Agreements and the Collection Statute Expiration Date (CSED)
IRM 5.19.14	Trust Fund Recovery Penalty (TFRP)
IRM 8.25.1	Trust Fund Recovery Penalty (TFRP) Overview and Authority
IRM 8.25.2	Working Trust Fund Recovery Penalty Cases in Appeals
IRM 25.5	Summons
IRM 25.27	Third Party Contacts

- (2) The Taxpayer Bill of Rights (TBOR) lists rights that already existed in the tax code, putting them in simple language and grouping them into 10 fundamental rights. Employees are responsible for being familiar with and acting in accord with taxpayer rights. See IRC 7803(a)(3), Execution Of Duties In Accord With Taxpayer Rights. For additional information about TBOR see: *Taxpayer Bill of Rights* and IRM 1.2.1.2.36, Policy Statement 1-236, Fairness and Integrity in Enforcement Selection.

5.17.7.2
(08-01-2010)
**Trust Fund Recovery
Penalty: Overview**

- (1) IRC 7501, provides that whenever any person is required to collect or withhold any internal revenue taxes from any other person and to pay over such tax to the United States, the amount of the tax shall be held in a special trust fund for the United States. Trust fund taxes include employment taxes and certain types of excise taxes.
- (2) The Trust Fund Recovery Penalty (TFRP) is authorized by IRC 6672(a), which states:

“Any person required to collect, truthfully account for, and pay over any tax imposed by this title who willfully fails to collect such tax, or truthfully account for and pay

over such tax, or willfully attempts in any manner to evade or defeat any such tax on the payment thereof, shall, in addition to other penalties provided by law, be liable to a penalty equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over. No penalty shall be imposed under section 6653 or part II of subchapter A of chapter 68 for any offense to which this section is applicable.”

- (3) The TFRP serves three purposes:
- It encourages prompt payment of income and employment taxes withheld from employees and other collected taxes;
 - It makes the responsible person liable for 100% of the unpaid trust fund taxes; and
 - It facilitates collection of trust fund taxes from secondary sources.
- (4) A person is liable for the TFRP if two statutory requirements are met:
- The person is “responsible” — had the duty to account for, collect, and pay over the trust fund taxes to the government; and
 - The person “willfully” failed to collect or pay over trust fund taxes to the government.
- (5) The IRS may collect trust fund taxes only once, whether from the business, from one or more of its responsible persons, or from the business and one or more responsible persons.
- (6) Refer to Policy Statement 5-14 (formerly P-5-60), Trust Fund Recovery Penalty Assessments, at IRM 1.2.1.6.3, and IRM 5.7, Trust Fund Compliance.

5.17.7.2.1
(07-18-2012)

**Persons Subject to the
Trust Fund Recovery
Penalty**

- (1) The term “person” in Section 6672 includes, but is not limited to, the following:

Type of Entity:
Officer or employee of a corporation
Partner or employee of a partnership
Member or employee of an LLC
Corporate director or shareholder
Another corporation
Surety or lender
Payroll Service Provider (PSP)
Responsible persons within a PSP
Professional Employer Organization (PEO)
Responsible persons within a PEO
Certified Professional Employer Organization (CPEO)
Responsible persons within a CPEO
Responsible persons within the common law employer (client of PSP/PEO/CPEO)

Note: The TFRP is not needed to assert liability against the owner of a sole proprietorship because the individual owner is personally liable for employment taxes under IRC 3101, IRC 3402 and, IRC 3403. However, the TFRP may be needed to assert liability against an employee or other non-owner of the sole proprietorship who exercises control over the finances.

(2) Regardless of a person's corporate title, a person will not be held liable for the TFRP unless they have the duty to account for, collect, and pay over the trust fund taxes to the government. Even an officer of the business will not be a responsible person if they are an officer in title only and have no substantive duties with the business. *O'Connor v. United States*, 956 F.2d 48 (4th Cir. 1992). On the other hand, a person who has no corporate title but has control of financial affairs or controls payment of funds by the business, may be held responsible for the TFRP.

(3) A determination of liability must take into account all facts and circumstances.

5.17.7.2.1.1
(11-02-2007)
Corporate Officers

(1) Most TFRP cases involve corporate officers.

5.17.7.2.1.2
(08-01-2010)
Corporate Directors

(1) A director who is not an officer or employee of the corporation may be responsible for the TFRP if they were responsible for the corporation's failure to pay taxes that were due and owing. *Commonwealth Nat'l Bank of Dallas v. United States*, 665 F.2d 743 (5th Cir. 1982).

5.17.7.2.1.3
(08-01-2010)
Partners/Members

- (1) In accordance with IRC 6671(b), a member of a partnership, Limited Liability Company (LLC), or Limited Liability Partnership (LLP) may be liable for the TFRP.
- (2) As a general rule, general partners are individually liable under state law for the debts of a partnership; therefore, assessments are made in the name of the partnership and the names of the general partners. Accordingly, there is usually no reason to make a separate TFRP assessment against the various partners. *United States v. Galletti*, 541 U.S. 114 (2004). In a limited liability partnership, however, general partners may not be individually liable for the debts of the partnership, depending on the jurisdiction. If you determine that the general partners are not individually liable for the debts of the partnership under state law, then a TFRP assessment against one or more partners may be appropriate. Contact Civil Enforcement Advice and Support Operations (CEASO) or Area Counsel with any questions.

5.17.7.2.1.4
(08-01-2010)
Employees

- (1) An employee may be liable for the TFRP if they made the decision not to pay the taxes due. *Gephart v. United States*, 818 F.2d 469 (6th Cir. 1987).
- (2) Employees are generally under the dominion and control of an employer; however, instructions from a supervisor not to pay taxes do not relieve an employee who is an otherwise "responsible person" from IRC 6672 liability. *Brounstein v. United States*, 979 F.2d 952 (3d Cir. 1992).
- (3) Allegations that an employee is a responsible person should be thoroughly investigated.

5.17.7.2.1.5
(08-01-2010)

Professional Employer Organizations (PEOs)

- (1) Professional Employer Organizations (PEOs), sometimes also referred to as employee leasing companies, and their owners, officers, and/or employees may be responsible persons with respect to client organizations in certain limited circumstances. If you have a case in which you believe that a PEO or an owner, officer, and/or employee of a PEO may be a responsible person, contact Area Counsel.

5.17.7.2.1.6
(01-22-2024)

Certified Professional Employer Organization (CPEOs)

- (1) The Tax Increase Prevention Act of 2014 (TIPA), enacted December 19, 2014, added IRC 3511, Certified Professional Employer Organizations, which provides that a (CPEO) be treated as the employer of any worksite employee performing services for any customer of such organization. Therefore, CPEOs and their owners, officers, and/or employees may be responsible persons with respect to client organizations in certain limited circumstances. If you have a case in which you believe that a CPEO or an owner, officer, and/or employee of a CPEO may be a responsible person, contact Area Counsel.

5.17.7.2.2
(08-01-2010)

Responsibility

- (1) A responsible person may be held liable for the TFRP if such person willfully fails to perform any one of the three duties listed in the statute: collecting, truthfully accounting for, and paying over the taxes. *Slodov v. United States*, 436 U.S. 238 (1978).
- (2) The statute does not impose upon the responsible person an absolute duty to pay over amounts that should have been collected and withheld by prior responsible persons. *Slodov v. United States*, 436 U.S. 238 (1978).
 - a. A person who becomes a “responsible person” when the business does not have the funds to pay an employment tax liability that arose under previous management and who uses funds acquired after they became a “responsible person” to pay the operating expenses of the business rather than to pay the prior withholding tax delinquency is not personally liable for the delinquency under Section 6672. *Slodov, Id.* at 254.
 - b. If funds are available to pay delinquent trust fund taxes at the time a responsible person assumes control of the business and the responsible person fails to use those funds to pay the delinquent taxes, that person will be liable for the delinquent taxes to the extent of the funds available to pay the trust fund taxes. *Id.* at 255.
- (3) One or more persons may be responsible persons within the meaning of IRC 6672 for the same quarter. *Thomas v. United States*, 41 F.3d 1109 (7th Cir. 1994).

Note: If the determination is made that more than one person is liable under IRC 6672, the RO may recommend that individual assessments of the penalty be made against each person.

- (4) A determination of “responsibility” depends upon the facts and circumstances of each case. Common factors considered by the court include the following:
 - Identification of the person as an officer, director, or principal shareholder of the corporation, a partner in a partnership, or a member of an LLC;
 - Duties of the officer as set forth in the by-laws;
 - Authority to sign checks;

- Identification of the person as the one in control of the financial affairs of the business;
- Identification of the person as the one who had authority to determine which creditors would be paid and those who exercised that authority;
- Identification of the person as the one who controlled payroll disbursements;
- Identification of the person as the one who had control of the voting stock of the corporation; and
- Identification of the person as the one who signed the employment tax returns.

Note: See *Cook v. United States*, 52 Fed. Cl. 62, 89 AFTR2d 2002-1541, 2002-1 USTC ¶ 50,328 (Fed. Cl. 2002); *Datloff v. United States*, 252 F. Supp. 11, *aff'd*, 370 F.2d 655 (3d Cir. 1966).

- (5) The crucial test is whether the person has the “effective power to pay the taxes owed.” *Purcell v. United States*, 1 F.3d 932, 937 (9th Cir. 1993). A person is deemed to have such power if they possess the authority to exercise significant control over the company’s financial affairs whether or not such control is in fact exercised. *Purcell* at 937. Significant control generally relates to the person’s status, duty, and authority in the business that failed to carry out one of the three statutory duties. *Davis v. United States*, 961 F.2d 867 (9th Cir. 1992).
- (6) Those performing ministerial duties without exercising independent judgment will not be deemed responsible. See Policy Statement 5-14 (formerly P-5-60), at IRM 1.2.1.6.3.
- (7) An unpaid, voluntary board member of a tax-exempt organization will not be considered a responsible person if the board member is solely serving in an honorary capacity, does not participate in the day-to-day or financial operations of the business, and does not have actual knowledge of the failure on which the penalty is based. IRC 6672(e). This exception, however, does not apply if it results in no person being liable for the TFRP. Also, a voluntary board member of a tax-exempt organization who is intimately involved in the financial decisions of the company may be a responsible person. See *Jefferson v. United States*, 459 F.Supp.2d 685 (N.D. Ill. 2006) (twenty year voluntary board president of a non-profit organization who was unpaid but did not serve solely in an honorary capacity, who had check signing authority and control of financial affairs, and who was aware that trust fund taxes had not been paid, was a responsible officer who willfully failed to pay the tax).

5.17.7.2.3 (01-22-2024) Willfulness

- (1) Under IRC 6672(a), the failure to collect or pay over trust fund taxes must be willful.
- (2) Definition of willful — intentional, deliberate, voluntary, reckless, knowing (not accidental). No evil intent or bad motive is required. *Domanus v. United States*, 961 F.2d 1323 (7th Cir. 1992).
- (3) To show “willfulness,” the government must show that the responsible party was aware of the outstanding taxes and either deliberately chose not to pay the taxes or recklessly disregarded an obvious risk that the taxes would not be paid. *Phillips v. United States*, 73 F.3d 939, 942 (9th Cir. 1996).

- (4) A responsible person's failure to investigate or correct mismanagement after being notified that withholding taxes have not been paid satisfies the IRC 6672 "willfulness" requirement. *Finley v. United States*, 123 F.3d 1342 (10th Cir. 1997).
- (5) The payment of net wages (wages minus trust fund taxes) to employees when funds are not available to pay withholding taxes is a willful failure to collect and pay over under IRC 6672. If funds are not available to cover both wages and withholding taxes, a responsible person has a duty to prorate the available funds between the United States and the employees so that the taxes are fully paid on the amount of wages paid. For purposes of determining willfulness, an employee owed wages is merely another creditor of the business, and preferences to employees over the government constitute willfulness. *Hochstein v. United States*, 900 F.2d 543, 548 (2d Cir. 1990).
- (6) The circuits that have decided the issue have split on whether **reasonable cause** negates a responsible person's willfulness and is a defense to TFRP liability.
 - a. The Eighth and First Circuits have determined that reasonable cause is not a defense. *Olsen v. United States*, 952 F.2d 236 (8th Cir. 1991); *Harrington v. United States*, 504 F.2d 1306 (1st Cir. 1974).
 - b. The Ninth Circuit has not stated specifically that the reasonable cause defense does not apply; however, it has determined that "conduct motivated by a reasonable cause may, nonetheless, be willful." *Phillips v. United States*, 73 F.3d 939, 942 (9th Cir. 1996).
 - c. The Tenth, Eleventh, Second, and Fifth Circuits have determined that the reasonable cause defense applies, at least conceptually, to willfulness determinations under Section 6672. Even these circuits, however, apply the defense narrowly. *Smith v. United States*, 555 F.3d 1158, 1170 (10th Cir. 2009) (reasonable cause defense must be narrowly construed with respect to Section 6672); *Thosteson v. United States*, 331 F.3d 1294, 1301 (11th Cir. 2003) (court does not decide whether reasonable cause applies, but notes that this defense is exceedingly limited); *United States v. Winter*, 196 F.3d 339, 345 (2d Cir. 1999) (reasonable cause defense negated willfulness only if the responsible person reasonably believed that taxes were being paid); *Logal v. United States*, 195 F.3d 229, 233 (5th Cir. 1999) (reasonable cause defense is exceedingly limited.).
 - d. The Sixth Circuit has determined that responsible persons qualified for an exception to being found willful when the responsible person relied on clean audit reports from an accounting firm, and their hiring of an assistant controller and CFO to support and supervise the controller, demonstrated that the responsible persons reasonably believed the trust fund taxes were being paid. *Byrne v. United States*, 857 F.3d 319 (6th Cir. 2017).
- (7) A mistaken belief that payments to other creditors were required to be made in preference to trust fund taxes does not make the failure to pay non-willful. *Thomsen v. United States*, 887 F.2d 12, 17-18 (1st Cir. 1989).

5.17.7.2.4

(08-01-2010)

Examination of Records

- (1) The RO has the initial duty to determine the identity of officers, partners, members, or employees who had the duty to collect or pay over the taxes.
- (2) Records to be examined may include the following:
 - Articles of incorporation or articles of organization
 - By-laws of the corporation or operating agreements
 - Minute books
 - Payroll records
 - Canceled checks and bank records and
 - Tax returns
- (3) The articles of incorporation should contain the names and duties of all officers and directors of the corporation.
- (4) Corporate by-laws and minute books may disclose the names of persons responsible for the filing of returns and payment of taxes. They may show who has the authority to sign checks, deposit money, and make loans on behalf of the corporation.
- (5) Bank records and canceled checks should be examined for payment of other financial obligations after the taxes became due.
 - a. Signature cards should identify the persons authorized to sign corporate checks.
 - b. Bank records may disclose possible diversion of corporate funds.
 - c. Financial statements provided to the bank in connection with a bank loan may provide additional information regarding responsibility and financial solvency of the corporation.
- (6) Tax returns, if filed, may provide the name of the person responsible for filing.

5.17.7.2.5

(08-01-2010)

Interview of Witnesses

- (1) Interviewing witnesses is an important factor in TFRP investigations.
- (2) The RO should prepare for the interview prior to meeting with the witness. This will increase the chances that the interview will be successful.
- (3) When conducting an interview with a potentially responsible person, the RO should determine the following:
 - Whether the person had a duty to account for, collect, and pay over trust fund taxes; and
 - Whether they willfully failed to perform any of these duties.
- (4) If a potentially responsible person asserts a defense for failure to comply with the statutory requirements, all of the details surrounding the defense should be thoroughly questioned and subsequently verified.
- (5) The interview of non-responsible employees who have knowledge of the business and its decision making process may be extremely helpful in determining who is both a responsible and willful individual.

5.17.7.2.6

(08-01-2010)

Extent of Liability

- (1) IRC 6672 is limited to the trust fund portion of the tax; that is, to the tax that the "responsible person" is required to collect or withhold from the wages of employees.

- a. To determine the application of payments and other credits for purposes of determining the TFRP, follow the guidelines in IRM 5.7.4.3.1, Sequence of Payment Application in Employment Tax Cases and IRM 5.7.7, Payment Application and Refund Claims.
 - b. After the application of payments has been made, the TFRP is based on the remaining outstanding amount of withheld income tax and employee's FICA tax. Refer to Policy Statement 5-14 (formerly P-5-60), at IRM 1.2.1.6.3.
- (2) The TFRP does not apply to direct taxes such as the employer's portion of FICA or FUTA. Neither does it apply to non-collected excise taxes.
 - (3) If during the investigation, the RO becomes aware of facts that indicate that a lender, surety, or third party may have indirectly or directly provided funds for the payment of employee wages, the RO should consider assertion of liability under IRC 3505(a) or IRC 3505(b). See IRM 5.17.7.3, below.

5.17.7.2.7
(01-22-2024)

**Limitation Period on
Assessment**

- (1) Withholding and FICA Taxes
 - a. IRC 6671 provides that the TFRP is required to be assessed and collected in the same manner as taxes.
 - b. IRC 6501(a) states that, except as otherwise provided in IRC 6501, any tax imposed by the Code shall be assessed within three years after the return was filed.
 - c. Generally, the TFRP must be assessed within three years after the return to which it relates was filed. *Lauckner v. United States*, 68 F.3d 69 (3d Cir. 1995).
 - d. A return of withholding and FICA taxes filed on or before the prescribed due date is deemed to have been filed on the due date. Thus, with respect to any taxable period within a calendar year, the period of limitations is three years from the succeeding April 15 (the due date of the return) or the date the return was filed, whichever is later.
 - e. A return executed by the RO is not considered the taxpayer's and, therefore, does not start the assessment statute.
 - f. If the return is fraudulent, the tax may be assessed at any time.
- (2) The assessment period may be extended prior to its expiration by the consent of the person against whom the penalty is to be assessed. This extension, however, applies only to the consenting person.
- (3) For further discussion of the statutory assessment period and extensions of such period, see IRM 5.7.3.6, Statutory Assessment Period, and IRM 5.7.3.7, Extension of Statutory Assessment Period.
- (4) Under IRC 6672(b)(3), the assessment statute may be extended when the IRS mails or hand delivers the Letter 1153, Proposed Trust Fund Recovery Penalty Notification, to the responsible person. Specifically, IRC 6672(b)(3) provides that if the assessment statute is open when the IRS mails or delivers in person the Letter 1153 to a responsible person, the assessment statute shall not expire before the later of the following dates:
 - The date 90 days after the Letter 1153 and supporting documents were mailed or hand delivered to the responsible person, or
 - If the person files a timely protest of the proposed TFRP, the date 30 days after the Independent Office of Appeals (Appeals) makes a "final administrative determination" regarding the proposed penalty.

Example: The limitations period for assessing the TFRP against the responsible person will expire on April 15, 2023. The RO hand delivers the Letter 1153 to the responsible person on April 1, 2023. Because the assessment statute was open when the Letter 1153 was delivered to the responsible person, the statute is extended to the date that is 90 days after April 1, 2023 (which is June 30, 2023), unless the responsible person files a timely protest. If the responsible person files a timely protest, then the assessment statute will not expire until the date that is 30 days after Appeals makes a final determination regarding the proposed penalty, assuming that date is after June 30, 2023.

Reminder: The IRS has an administrative requirement to mail Letter 1153 certified (return receipt requested) to the responsible person's last known address.

- (5) See also IRM 5.7.3.7.2, Impact of Letter 1153 on Assessment Statute.
- (6) The date of Appeals final determination is the earlier of the date of the Appeals Team Manager's (ATM's) signature on:
 - Form 5402, Appeals Transmittal and Case Memo, or
 - Form 866, Agreement as to Final Determination of Tax Liability or Form 906, Closing Agreement on Final Determination Covering Specific Matters.

5.17.7.2.8
(08-01-2010)
**Assessment Procedure
and Appellate Rights**

- (1) Refer to IRM 5.7.6, Trust Fund Penalty Assessment Action, and IRM 8.25, Trust Fund Recovery Penalty (TFRP).

5.17.7.2.9
(08-01-2010)
Collection of the TFRP

- (1) It is the IRS's policy to collect the unpaid trust fund taxes only once.
- (2) If, after the assertion of the TFRP, the corporation pays the delinquent tax, the TFRP assessment will be abated. See Policy Statement 5-14 (formerly P-5-60), at IRM 1.2.1.6.3.
- (3) Similarly, if an amount that has been collected from the responsible person(s) exceeds the amount that the corporation failed to pay, the excess may be refunded within the applicable statutory period to the person(s) that caused the excess payment. Refer to IRM 5.7.7, Payment Application and Refund Claims.

5.17.7.2.10
(08-01-2010)
**Limitation Period for
Collection**

- (1) The TFRP may be collected by levy or by a proceeding in court, but only if begun within ten years after the assessment was made. IRC 6502(a).
- (2) The IRS may no longer obtain waivers of the collection period except for those waivers secured in conjunction with an installment agreement. IRC 6502. Current policy limits the use of this authority to partial-payment installment agreements. Refer to IRM 5.14.2, Partial Payment Installment Agreements and the Collection Statute Expiration Date (CSED), for guidance.

5.17.7.2.11
(11-02-2007)
**Collection of TFRP in
Bankruptcy**

- (1) Section 507(a)(8)(C) of the Bankruptcy Code (11 USC 507(a)(8)(C)) grants priority to all taxes “required to be collected or withheld and for which the debtor is liable in whatever capacity.” This includes the TFRP under IRC 6672.
- (2) Except for a super discharge under 11 USC 1328(a) in a Chapter 13 bankruptcy case, an individual debtor is not discharged from liability for the TFRP. See 11 USC 523(a)(1)(A). Thus, the IRS may collect any unpaid TFRP after the automatic stay terminates.

Note: For bankruptcy cases filed on or after October 17, 2005, there is no longer a super discharge from the TFRP for responsible persons. See 11 USC 1328(a)(2).

5.17.7.2.12
(01-22-2024)
**Collection of TFRP when
the Underlying Business
Entity is in Bankruptcy**

- (1) The automatic stay provisions of the Bankruptcy Code do not prevent the IRS from assessing and collecting the TFRP from responsible persons who are not themselves in bankruptcy. 11 USC 362.
- (2) Responsible persons, therefore, may not enjoin assessment and collection of the TFRP against them when only the corporation is in bankruptcy. *In re Prescription Home Health Care*, 316 F.3d 542 (5th Cir. 2002) (holding that the bankruptcy court does not have jurisdiction over a non-debtor responsible officer).

Note: As a policy matter, the IRS is to refrain from asserting the TFRP against non-debtor responsible persons in cases where the corporation debtor’s Chapter 11 plan provides for full payment of trust fund taxes, as long as the plan is not in default. See IRM 5.9.8.11(1), Trust Fund Considerations in Chapter 11 - Policy Statement P-5-14.

5.17.7.3
(08-01-2010)
**Liability of Third Parties
Paying or Providing for
Wages**

- (1) In some cases, lenders, sureties, or other persons who are not employers may be personally liable for withheld taxes due. While employers are primarily liable for paying withheld taxes, in some cases they may be without sufficient resources to pay. As a result, recourse against them may be fruitless. IRC 3505 may provide an alternative means of collecting the withheld taxes.

5.17.7.3.1
(08-01-2010)
**Liability for Direct
Payment of Wages – IRC
3505(a)**

- (1) IRC 3505(a) makes third parties personally liable for the payment of withholding taxes where they pay wages directly to employees of another.
- (2) IRC 3505(a) applies to lenders, sureties, or other persons.
 - a. “Other persons” includes anyone similar to a lender or surety who pays the wages of employees of another out of its own funds. The most common situation in which a person other than a lender or surety (a statutory “other person”) may be found liable under IRC 3505(a) is where a prime or general contractor, out of necessity (to keep the employees of the subcontractor on the job) or by contract, pays net wages directly to employees of a subcontractor that is having financial problems. See *United States v. Kennedy Construction Co. of NSB, Inc.*, 572 F.2d 492 (5th Cir. 1978) (IRC 3505(a) liability imposed on a general contractor who co-signed payroll checks for a subcontractor’s employees).
 - b. IRC 3505(a) does not apply to a person who is acting only as agent of the employer or as agent of the employees (such as a union agent). See 26 CFR 31.3505-1(c), examples.

- (3) Liability under IRC 3505(a) extends to withholding under:
 - IRC 3402, withheld income taxes;
 - IRC 3102, withheld FICA taxes; and
 - IRC 3202, withheld railroad retirement taxes.
- (4) Liability does not extend to the employer's share of employment taxes; nor does liability extend to penalties that the IRS may impose on the employer.
- (5) IRC 3505(a) does not relieve an employer from responsibilities with respect to withholding taxes. The responsibilities continue even though a lender may be paying the employees' wages. The liability of the lender in such a case is to pay the taxes only where the employer does not do so.
 - a. The employer is obligated to file an employer's tax return (Form 941, Employer's Quarterly Federal Tax Return) and comply with other requirements generally imposed on employers.
 - b. The lender's liability is a sum equal to the taxes (together with interest) required to be deducted and withheld from the wages by the employer.
- (6) When evaluating whether wages are being paid directly, the IRS and the courts look to the "substance" of the transaction and may find the direct payment of net wages present even though a "subterfuge" is used to disguise the substance of the arrangement. See *United States v. Kennedy Construction Co. of NSB, Inc.*, 572 F.2d 492 (11th Cir. 1978) (subcontractor opened special payroll account out of which it issued payroll checks; however, the contractor provided the funds in the account after verifying the net wages owed each pay period and countersigned the pay checks).

5.17.7.3.2
(08-01-2010)
**Liability When Funds are
Supplied — IRC 3505(b)**

- (1) IRC 3505(b) provides that a lender, surety, or other person who supplies funds to or for the account of an employer for the specific purpose of paying wages of the employees of such employer may be personally liable for any unpaid withholding taxes even though this person does not directly pay the employees' wages.
- (2) A person within the meaning of Section 3505(b) includes the following:
 - A prime or general contractor who supplies funds directly to a subcontractor to meet its net payroll with knowledge of the subcontractor's inability to pay its withholding taxes. *United States. Algernon Blair, Inc.*, 441 F.2d 1379 (5th Cir. 1971).
 - A shareholder, including a parent company of a subsidiary, who makes a capital contribution or a direct loan, or who puts up collateral for a loan from a third party to a corporation if the loan is to be used by the corporation to pay net wages. *United States v. Intercontinental Industries, Inc.*, 635 F.2d 1215 (6th Cir. 1980).
 - A bank that honors a customer's/employer's overdrafts for payroll checks. *Fidelity Bank, N.A. v. United States*, 616 F.2d 1181 (10th Cir. 1980).
- (3) Before a person can be liable under Section 3505(b), the following two conditions must exist.
 - a. The person must know that the advanced funds are to be used for the payment of wages; this does not include an "ordinary working capital loan." "Ordinary working capital loans" are ones that are made to enable

the borrower to meet current obligations as they arise; they are not earmarked for any particular purpose.

Note: If the maker of an “ordinary capital loan” has actual notice or knowledge at the time of the advancement of funds that the funds or a portion of the funds are to be used to pay net wages, IRC 3505(b) will apply regardless of whether the written agreement states that the funds were advanced for another purpose. 26 CFR 31.3505-1(b)(3); *United States v. Intercontinental Industries, Inc.*, 635 F.2d 1215 (6th Cir. 1980).

- b. The supplier of funds must have “actual notice or knowledge” at the time such funds are advanced that the employer does not intend to, or will not be able to make timely payment or deposit of taxes required to be withheld. The lender has actual notice or knowledge of any fact from the time such fact is brought to its attention or would have been brought to its attention if the organization had exercised due diligence. See *United States v. Park Cities Bank and Trust Co.*, 481 F.2d 738 (5th Cir. 1973).

Note: The burden of establishing actual notice or knowledge in such cases is on the government.

- (4) It is the IRS’s position that notice to, or knowledge by, any agent of a third-party supplier of funds is imputed to the third party. This is true even if the agent conceals the facts from the supplier. *United States v. Park Cities Bank and Trust Co.*, 481 F.2d 738 (5th Cir. 1973).
- (5) Under IRC 3505(b), the liability of the third party may not exceed 25 percent of the amount supplied to the employer for the specific purpose of paying wages. The 25% limitation applies to accrued interest. *O’Hare v. United States*, 878 F.2d 953 (6th Cir. 1989).

Example: A lender advances \$100,000 to Employer A for the purpose of paying net wages. The employer fails to pay withholding taxes, and is assessed a liability of \$25,000 plus an additional \$10,000 in accrued interest. The IRS may file suit against the lender for \$25,000, which is 25% of the amount supplied to the lender. If the assessment had been \$20,000 plus an additional \$10,000 in interest, the IRS still could have brought suit for \$25,000 (\$20,000 in tax and \$5,000 in accrued interest).

Note: The lender’s liability does not include penalties that the IRS may impose on the employer.

- (6) The employer remains responsible for filing returns (Form 941).
- (7) Payments by the lender of withholding taxes reduces the liability of the employer. Similarly, payments by an employer of the withholding taxes reduces the liability of the lender.

5.17.7.3.3
(08-01-2010)
**Collection of Liabilities
under IRC 3505(a) and
(b)**

- (1) Under both IRC 3505(a) and IRC 3505(b), if the person liable does not voluntarily satisfy the liability, the government may collect such liability by a court proceeding only.
 - a. The suit must be instituted within 10 years after the assessment against the employer.

- b. In *Jersey Shore State Bank v. United States*, 479 U.S. 442 (1987), the Supreme Court held that IRC 6303(a) does not require the government to provide notice and demand for payment to a lender before bringing a civil suit against the lender to collect sums for which it is liable under IRC 3505. In so holding, the court drew a distinction between the employer, who is liable for the unpaid taxes, and the lender, who has a separate liability under IRC 3505 but is not liable for the taxes.

- (2) Do not overlook the possibility that alternative remedies exist, particularly the assertion of the Trust Fund Recovery Penalty. See *United States v. Security Pacific Business Credit, Inc.*, 956 F.2d 703 (7th Cir. 1992); *Muller v. Nixon*, 470 F.2d 1348 (6th Cir. 1972), *cert. denied*, 412 U.S. 949 (1973); *Turner v. United States*, 423 F.2d 448 (9th Cir. 1970).

Note: Section 6672 has advantages over Section 3505, such as the ability to assess the liability, and administratively collect.

5.17.7.4
(11-02-2007)
**Liability of Sureties —
Bond on Public Works
Contracts**

- (1) The Miller Act, 40 U.S.C. 3131, provides that every performance bond on federal construction projects shall specifically guarantee payment of federal payroll taxes. The obligation of the surety on the performance bond must guarantee the payment of taxes that are required to be collected, deducted, or withheld from wages by the contractor, whether or not the contractor does in fact collect, deduct, or withhold such taxes.
- (2) Notice of Unpaid Taxes
 - a. The government must notify the surety of any unpaid taxes attributable to any period within 90 days after the date when the contractor in fact files a return for such period.
 - b. If the contractor fails to file a timely return, the IRS must give notice to the surety no later than 180 days from the date when such return was required to be filed, whether or not such return was ever filed.
 - c. The notice requirements apply to each calendar quarter or other taxable period.

Example: The contractor on a federal construction project files a Form 941 for the third quarter 2022 on October 15, 2022. While the return was not due until October 31, 2022, the contractor did in fact file on October 15, 2022. Thus, the 90-day period would commence on October 16, 2022, and the notice must be given on or before January 13, 2023.

Example: The same contractor files a Form 941 for the third quarter 2022 on January 29, 2023. The government has until April 30, 2023, to notify the surety of the unpaid taxes. If the contractor had failed to file a return, April 30, 2023, would still be the last date of notification to the surety because the 180-day period begins to run from the date the return was required to be filed (October 31, 2022).

- (3) The government may offset any funds still due the prime contractor. In this case, because of the limited time in which notice can be given to the surety, the RO should still consider notifying the surety for the purpose of holding the surety liable under the provisions of the Miller Act.

- (4) The only way other than offset to collect is by bringing suit against the surety within one year after the day on which timely notice of the unpaid tax liability was given to the surety.

Example: If the surety is given timely notice on July 1, 2022, that the contractor failed to pay over the taxes applicable to a taxable period, the government must commence suit on or before July 1, 2023, to enforce the obligation under the performance bond. Because of this short statute of limitations, the RO should be alert for the necessity of prompt action.

- (5) The government will continue to assert its rights under a surety bond on other than federal construction projects, but only where the available evidence clearly and convincingly shows the bond was intended for the direct benefit of the United States.