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TEAMWORK

Open lines of communication between the estate lawyer and the financial adviser are crucial for the best interests of their mutual clients. **Page 15**

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Next week: Top 100 Private Companies

Trust-based traps: Why it's vital to set aside these funds

By LOUIS J. LeMASTER
Special for Lehigh Valley Business

Primarily focused on operating their business and providing their family with the financial support and benefits to thrive, business owners can forget or overlook important tax and employment laws.

Here are three areas you need to ensure that your accounting system is prepared to handle for you:

LeMaster

■ UNCASHED CHECKS – UNCLAIMED PROPERTY

Until 2009, a business in Pennsylvania would regularly review a list of outstanding checks written to vendors and prior employees to determine if those uncashed checks could be voided, essentially returning those funds to the business. This found money became a one-time gain to the business.

Since the implementation of unclaimed property reporting requirements, businesses are required to keep track of those uncashed checks and make attempts to contact those recipients before turning the money over to Pennsylvania to administer. The gain from that found money now belongs to Pennsylvania.

Your accounting systems need to allow for tracking stale checks, documenting attempts to contact the recipients and eventually turning over the assets to Pennsylvania.

Detailed rules on reporting requirements can be found at the Pennsylvania Treasury website.

■ 401K ELECTIVE DEFERRALS

Once a business reaches a certain level of success, owners typically provide some form of a retirement plan to themselves and employees.

Retirement plans are governed under the federal Employee Retirement Income Security Act of 1974 – more commonly known by its acronym, ERISA.

Over the years, ERISA has continued to increase expectations about the money you let your employees withhold from their payroll for contribution their retirement – money which you hold in trust for your employees

PHOTO/JOSHUA DOUBEK

Internal Revenue Service headquarters in Washington, D.C. The IRS pays special attention to ensure that taxes withheld from employee paychecks are properly held in trust.

ERISA has rules about how long you can go without sending that money to the retirement account of your employee and can impose penalties and impute lost earnings that you must fund if those deposits are not made within what ERISA considers a reasonable amount of time.

The clock starts ticking as soon as you can identify the dollar amount withheld and the employee it belongs to, which normally coincides with payday. In addition to imputed lost earnings, the cost of compliance to correct these violations can add to the damage.

■ EMPLOYMENT TAXES

Nobody likes owing taxes. Owing taxes can result in otherwise avoidable penalty and interest and the additional cost of employing professionals to help remedy the situation.

An easy tax to fall behind on also happens to carry the most painful penalties. Employment taxes are mostly those which are withheld from the employee's paycheck and are classified by the Internal Revenue Service as trust taxes – funds deducted from employee payroll that do not belong to the employer.

Example: At the end of the quarter, an employer goes to file payroll taxes for the six payrolls paid over the past three months. It owes the $7,000 per payroll deducted from employee checks for each of six payrolls and another $10,000 of company-level payroll taxes for a total of $52,000.

The employer only has $5,000 in the bank. With only $5,000 in the bank account, it is clear the company spent the cash withheld from payroll to pay vendors, even though there should be at least $42,000 of cash representing those trust taxes not belonging to the company.

This type of scenario can occur very easily if you are not monitoring properly the amount of cash set aside for employment trust taxes.

Trust taxes hold a special place with the enforcement arm of the IRS, which has several tools in the Tax Code to assess significant civil and criminal penalties.

Recent communications from the IRS, depicting employment tax noncompliance as egregious, likely will lead to increased examinations of this area by the agency.

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The common thread to these three items that your business is holding money that does not belong to you.

If you do not have systems in place to set aside these funds as they are accumulated, it is very easy to lose track of how much of your bank balance really belongs to you – and how much needs to eventually be paid to others.

The simplest solution is to maintain a regular habit of moving trust funds to a separate bank account to avoid using those funds for other purposes.

If you find your business is off-course in any of these areas, it will be in your best interest to correct the error as quickly as possible. The IRS and ERISA become more difficult to deal with when they find you first, and that can make efforts to clean up the problem even more taxing.

Louis J. LeMaster, Certified Public Accountant, is the managing shareholder at Buckno Lisicky & Co., a regional CPA firm servicing the Lehigh Valley and beyond. Based in Allentown, he can be reached at 610-821-8580 or llemaster@blco-cpa.com.

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