The New Electronic Federal Tax Payment System

If Your Company Paid $50,000 or More in 1995 Payroll Taxes, You Must File Electronically as of July 1. Here’s What to Do to Comply, and What to Watch Out For

By Channing Hayden

What do George Jetson, Captain James T. Kirk and businesses that paid $50,000 or more in payroll taxes during 1995 have in common? As of July 1, they’ll pay their federal (or Federation, in Kirk’s case) taxes electronically.

The Internal Revenue Service says that the new Electronic Federal Tax Payment System will improve the quality of life for taxpayers in the electronic age. No more trips to the bank. No more Federal Tax Deposit coupons. Easy telephone or PC entry. Yet some have who have heard glowing promises from U.S. government agencies in the past are skeptical, and the regulations contain booby traps for the unwary.

Boon or Boondoggle

Dr. Richard Lesher, president of the U.S. Chamber of Commerce, predicts that EFTPS will result in a massive boondoggle. “For starters, the IRS has done precious little to inform small businesses about this new obligation. Basically, it sent a one-page notice to most affected companies,” he said.

According to a new report in Nations Business last year, few affected companies knew of the regulation. “In fact,” Lesher added, “a recent audience of 600 Certified public Accountants in Boston did not include one person who knew about this new mandate.”
Automatic Data Processing, Inc. of Roseland, N.J., surveyed businesses with fewer than 100 employees. ADP found that the companies most likely affected by the regulations had the lowest awareness of EFTPS and were the least prepared to comply.

Another problem Lesher anticipates is that EFTPS won’t work. “The IRS is operating a pilot project in Atlanta called TAXLINK that handles the electronic filings of larger firms that are already required to participate in the system. But TAXLINK will be swamped when 1.3 million small-business people begin to inundate it with deposits.

IRS regulations mandating electronic funds transfers for federal tax deposits were issued in July 1994. Companies paying employment taxes of more than $78 million in 1993 began electronic payments of all federal tax deposits Jan. 1, 1995; companies depositing more than $47 million in 1993-1994 came online Jan. 1, 1996. Now comes the big change that will catch many small and mid-size businesses in the federal electronic net. Companies paying more than $50,000 in employment taxes in 1995 were originally scheduled to begin electronic funds transfers on Jan. 1, 1997. Last summer, Congress gave these businesses a short reprieve until July 1, 1997.

**How It Works**

Covered companies have three payment options: Automatic Clearinghouse debits, Automatic Clearinghouse deposits and FEDWIRE. With ACH debits, the IRS automatically debits your bank account for the amount you specify. Choose ACH credits and you initiate each payment through your bank, if it offers the service. Companies required to pay employment taxes on the day after payday can use FEDWIRE, which involves wiring payments to the IRS, if their banks does so. ACH debit and credit transactions are made the day before tax payments are due.

When deciding which option to choose, be careful. With ACH credits or FEDWIRE, the burden to prove you paid your taxes falls on you. If your payment gets lost in electronic limbo, the IRS will assess a penalty. With ACH debits,
you get a confirmation number from the IRS. If anything goes wrong, it’s the tax collector’s problem, not yours.

Either ACH method requires you to enroll with the IRS. If you have more than one Employer ID Number, each has to be enrolled individually. Your location determines where you enroll.

**Payment Methods**

Before using ACH debits, you’ll be asked for business and bank account information. Companies can establish an upper limit for payments and receive a personal identification number for accessing the system.

You’ll also select one of the following input methods:
- Personal computer (Windows-based software available through NationsBank or First National Bank of Chicago.
- Audio response.
- Voice response.

Payments must be initiated no later than 8 p.m. (EST) one business day before the tax due date so your bank account can be debited when the taxes are due. You’ll receive a confirmation number for each ACH debit transaction. Treat them like receipts.

Another nice feature of the ACH debit procedure is that entries can be made up to 30 days before the tax due date. The system “warehouses” your tax payment report and debits your checking account on the tax due date you specify.

Companies selecting the ACH credit method also must initiate payment no later than one day before the tax due date. The cutoff time and charge are determined by your bank. You don’t get a confirmation number. However, you do have a PIN and can query the system to confirm the IRS has received and processed your payment. The PIN isn’t used when making an ACH credit payment. The ACH credit system has no built-in warehousing. Warehousing arrangements must be made with your financial institution.

You can alternate between ACH payment methods but must note that you wish to do so on your enrollment form. The start-up procedures are different for the two ACH methods.

To use FEDWIRE, first make arrangements with your bank, then make payments on the tax due date. FEDWIRE is an excellent fallback if you fail to make your ACH payments on time. As of this writing, it’s only available to companies required to make electronic payments. The fallback for other companies that miss the ACH deadline is filing as you do now, using FTD coupons.

Fail to make timely tax deposits and there’s a 10 percent penalty based on the taxes owed. The fine can be abated for reasonable cause, which will be determined by the facts of each case. “The dog ate my PIN” probably won’t cut it.

The Small Business Administration is distributing ADP/SBA EFTPS Transition Kits. They provide information on
the new regulations, give tips on how to comply, answer frequently asked questions and include a sample enrollment form. ADP in partnership with the SBA, will conduct jointly sponsored seminars on the new regulations through the July deadline.

For information or seminar information, contact your nearest SBA office. Seminar information also is available from ADP at (800) 225-5237, ext. 5032. First National Bank of Chicago at (800) 345-8400 and NationsBank at (800) 555-4477 will answer taxpayer questions on EFTPS enrollment and payments.

The Booby Traps—Hidden Deadlines

Newly affected businesses must make all FTDs by EFTPS beginning July 1, 1997. Enrolling takes up to 10 weeks, according to the IRS and SBA; this puts the enrollment deadline around April 22, 1997.

If you’re not affected by these new regulations, wait. Your turn is coming. More businesses will be required to file electronically. Companies paying payroll taxes of $50,000 or more in 1996 must make all FTDs using EFTPS by Jan. 1, 1998. Those paying payroll taxes of $20,000 or more in 1997 must make all FTDs using EFTPS by Jan. 1, 1999.

Companies not yet required to file electronically might want to do so anyway. If my company’s

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**Are You Ready to Take a Byte Out of Taxes?**

**Taxes to Be Paid Electronically**

Although the criterion for participation is based on payroll taxes, all of a covered company’s Federal Tax Deposits must be made using EFTPS. This includes the following:

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<th>Form #</th>
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<tr>
<td>720</td>
<td>Quarterly Federal Excise Tax</td>
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<tr>
<td>940</td>
<td>Employer’s Annual Federal Unemployment Tax</td>
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<tr>
<td>941</td>
<td>Employer’s Quarterly Federal Tax</td>
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<tr>
<td>943</td>
<td>Employer’s Annual Tax Return for Agricultural Employees</td>
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<tr>
<td>945</td>
<td>Annual Return of Withheld Federal Income Tax</td>
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<td>1120</td>
<td>U.S. Corporate Income Tax</td>
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<td>990C</td>
<td>Farmer’s Cooperative Association Income Tax</td>
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<tr>
<td>CT-1</td>
<td>Employer’s Annual Railroad Retirement and Unemployment</td>
</tr>
<tr>
<td>990PF</td>
<td>Return of Private Foundation</td>
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<tr>
<td>990T</td>
<td>Exempt Organization Business Income Tax</td>
</tr>
<tr>
<td>1042</td>
<td>Annual Withholding Tax Return for U.S. Source Income of Foreign Persons</td>
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**Are You Covered?**

To determine if you must pay your federal taxes electronically by July 1, 1997, add the deposits made from the forms below for 1995. If the total is $50,000 or more, you’re covered.

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Taxes, continued from page 35

trial run (below) is any guide, EFTPS is a hassle-free way to the dirty job of paying taxes. Companies not required to use EFTPS may do so voluntarily. Hey, if it makes your life easier, why not?

One Company’s Experience

There’s an advantage to running a company and writing about how to do it: I get to practice what I preach. We received our EFTPS notice in July 1996. With only 14 full-time employees, we were caught in the federal electronic web. The moral here is not to think “They can’t mean me!” They probably do. Follow the instructions in the sidebar to the right to make sure.

The notice wasn’t obscure, as the U.S. Chamber of Commerce implies, and we certainly didn’t ignore it. Our office doesn’t treat letters from the IRS like junk mail. Our enrollment form went in on July 25, 1996, and we received enrollment confirmation as of Oct. 11, 1996, about 11 week later.

December 1996’s deposits were made using ACH debits with no problems. The bookkeeper likes the system. She has a high tolerance for those telephone punch-in-the-number setups. To make sure the process was idiot-proof, I tried it myself. It’s extremely easy, especially since I followed a filled-in copy of the worksheet in the EFTPS Payment Instruction’ Booklet that the Treasury Department sent us. With the worksheet as a guide, how could I make a mistake?

OK, so I found a way. Punch in a wrong number and the computer becomes extremely rude, making you start all over again. Naturally, my mistake came in the last number on the worksheet, so it was back to square one. Overall, EFTPS worked better than I did.

Will EFTPS melt down, as the U.S. Chamber predicts, when 1.3 million of us try to do the same thing simultaneously? Only time will tell, but I doubt it. Warehousing ACH debits should be the system’s salvation. Most of us can afford to make tax payments before they’re due. It wreak havoc on our cash flow. By warehousing ACH debits, we have the best of both worlds. We’re not all contacting the system at the last minute, yet we don’t use our cash until it’s absolutely necessary.

Don’t put EFTPS on the back burner. If you miss the deadlines for electronic filing (both July 1, 1997, and the future deadlines noted above), the IRS penalizes you 10 percent of the taxes that should have been paid using EFTPS. If you’re forced to wait 10 or 11 week to enroll, fines could be ongoing, making the IRS’s “byte” much bigger. ☰

About the Author

Channing Hayden is a New Orleans business executive, management instructor at Tulane University and freelance writer.