

# The Legal Review

Sharing Case Law that Affects the Household Employment Industry

A Complimentary Resource from  
**Breedlove & Associates**

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*In an effort to help you strengthen your business practices and steer clear of legal trouble, The Legal Review will share findings from relevant legal cases. We've found that the easiest way to gain a practical understanding of complex tax and labor law is by reviewing real-life situations. These stories will illuminate potential legal landmines for your agency and/or your clients, and more importantly, show you how to avoid them.*

## **VA Department of Labor vs. Family: Evading Household Employment Taxes**

When families and caregivers agree to have wages paid “under the table,” they often do so with a false sense of security. The common misconception is that the government does not enforce household employment taxes and, therefore, there is little risk of getting caught.

This misconception is slowly but surely changing as more and more families have become entangled in time-consuming and expensive legal action because they did not pay their caregiver professionally. The fact is there are numerous events that can “trigger” the tax authorities and cause families to get caught. The most common events:

- Unemployment benefit claims after termination
- Employee credit check/job history review during loan process
- Wage disputes
- Employer OR employee audit

Here is a case that highlights the avalanche of trouble caused by a former employee filing for unemployment benefits.

### **The Mistake**

A family paid their nanny “under the table” for 9 months. After her employment terminated, she filed an unemployment benefits claim with the VA Department of Labor.

### **The Law**

An employer is required by law to pay employment taxes to the state and the IRS, in addition to withholding taxes from their employee’s pay. One of these required taxes is State Unemployment Insurance. This tax is relatively small per employee, but the dollars collected from unemployment taxes in total feed a large state fund that provides financial assistance to employees who lose their jobs due to no fault of their own. When an employer does not pay unemployment taxes, their previous employee is not entitled to financial benefits from the fund. In addition, a claim filed by an employee paid “under the table” will trigger immediate notification from the state informing the employer of their tax obligations, the number of delinquent tax filings, and an estimated amount of tax due. This event will also trigger notification of unpaid employment taxes at the federal level, although it may take several months for the IRS to notify the employer.

It is important to note that, although employees terminated for cause are generally not eligible to receive unemployment benefits, the employee still has the right to file a claim. At that point, it doesn't matter whether the state ultimately considers the claim legitimate or not. The bigger problem is the government is now aware of the employer's tax evasion.

### **The Mess**

- After the employee filed for unemployment benefits, the employer received notification from the VA Department of Labor stating that their previous nanny had filed a claim. The purpose of notification was to provide the employee's reasons for termination and to request the employer's confirmation or dispute of the statement in order to accurately award or deny benefits under the law. The family disputed the employee's statement, citing specific reasons for termination with cause.
- Unfortunately, the employer was also notified that the VA Dept. of Labor had no record of unemployment taxes paid or returns filed for any period of the employment.
- The VA Department of Labor notified the IRS of the employer's failure to meet the employment tax obligations.
- The family hired Breedlove & Associates to get them caught up and compliant – and to provide guidance through the claim process. Because the employee had been fired rather than laid off, we advised the employer to dispute the employee's claim for unemployment benefits. Simultaneously, we established tax accounts, filed prior tax returns, and remitted tax payments and penalties on behalf of the family.
- The employer took care of their employer tax responsibilities in total as quickly as possible (approximately \$1,800). Because Social Security and Medicare taxes had not been withheld from the employee's pay, the employer was now obligated to also pay the **employee's** portion of Social Security and Medicare taxes (an additional \$1,600).

### **The Outcome**

- The unemployment benefits claim could not be resolved based on the written statements from the two parties. The case worker scheduled a hearing and required both employer and employee to appear in person.
- The employee was awarded benefits, resulting in an increase in the employer's unemployment tax rates. Had the employer paid legally from the outset, the unemployment benefits claim would most likely have been denied because she was terminated with cause. It is generally believed that the employer's tax evasion factored heavily into the case worker's punitive decision.
- The cost to resolve this nightmare was high – from both a monetary and time standpoint. The employer was sickened to learn later that, if they had paid legally from the beginning, the employer's additional cost over-and-above the nanny's wages would have been less than \$150 (this includes the cost of the employer's taxes, Breedlove & Associates' service fees and the offsetting tax break available when you pay legally).
- The nanny was hired through an agency which had done a thorough job of informing the family of their tax and legal responsibilities during the placement process. Although the family did not blame the agency, they did seek ongoing assistance from the agency throughout the process. The agency tried to help in hopes of salvaging a positive employment experience and, therefore, future business and referrals from the family. The investment by the agency ended up being fairly substantial. However, it might have been radically higher if they had not taken a few minutes during the placement process to inform the family of their tax obligations.

### ***How the Whole Thing Could Have Been Avoided***

The family could have easily avoided all this mess (and expense) if they had established household employment tax accounts with the state of VA and the IRS, withheld payroll taxes from their employee, and remitted those taxes – along with some employer taxes – each quarter to the state and federal tax agencies. While it seemed like a hassle at the time, the family learned the true meaning of the word “hassle” when their former nanny waltzed into the unemployment office.

*To help your clients understand the tax obligations for both employer and employee, we have developed a simple educational flyer entitled “Tax Law 101”. The flyer can be downloaded from <http://www.breedlove-online.com/partners/library-of-educational-literature-helpful-tools> along with our other helpful resources. Or feel free to invite your clients to call us for a complimentary, no-obligation phone consultation. In about 10 minutes, we can assess their situation and give them comprehensive household employment tax guidance. Whether they sign up with our service or not, we'll make sure this kind of ugly situation never happens to one of your clients.*

*If you would like hard copies of our “Tax Law 101” flyer, just send an email to [info@breedlove-online.com](mailto:info@breedlove-online.com).*

**If you have additional questions, please call 888-BREEDLOVE (273-3356) or visit [www.breedlove-online.com](http://www.breedlove-online.com). We're here to help our agency partners provide their candidates and clients with information, tools and resources that improve the employment relationship, eliminate legal risk for all parties, and increase the professionalism of the industry.**



*Tax & Payroll Services for Household Employers*