Outsourcing payroll? You need to know 5 things

Everyone wants a piece of you. Employees expect their paychecks to be correct all the time. The IRS expects your payroll taxes to be deposited on time and in the correct amount. And then there are those pesky quarterly 941 forms and those annual W-2s to file. That’s a lot of work and you haven’t even gotten to your own work, yet.

The solution? Outsource your payroll operations to a third party. But you can’t authorize any third party, like a payroll service provider, to handle your payroll unless you first sign Form 8655, Reporting Agent Authorization. Along with that form, your third party may also ask you to sign Form 8821, Tax Information Authorization.

Caution: Don’t sign forms blindly.

Tax information authorizations allow your third party to work with the IRS to resolve some basic issues on your behalf.

4 types of tax information authorizations

1. Checking the box. First, the third party can check the box on Form 941 or 940. Checking the box allows the third party to assist the IRS in processing that form.

2. Completing Form 8821. Completing Form 8821 allows the third party to receive tax information on your behalf. You can be as specific or as general with the authority you give on Form 8821.

Key: Forms 8655 and 8821 overlap in many respects, but a properly signed Form 8821 can be entered into the IRS’ Central Authorization File, or CAF for short.

What is it: The CAF is the IRS data base in which all third-party authorizations are stored. CAF numbers are powerful dispute resolution tools because they allow any IRS employee to access information and talk to your third-party designee.

Once you sign Form 8821, any employee of your service provider can receive information from the IRS.

3. Completing Form 4506 or Form 4506-T. Similar to the checkboxes on Forms 941 and 940, these forms allow a third party to obtain a copy of a previous filed return or tax transcript. It’s specific to those returns.

4. Verbal authorization. Finally, but not recommended, you can orally consent to a third party acting on your behalf.

Power of Attorney

The 5th thing you need to know about Payroll? You don’t need to be an attorney to hold a power of attorney, as long as you can practice before the IRS—enrolled agents or CPAs can hold a power of attorney.
Signing Form 2848 authorizes specified individuals to act on your behalf. Form 2848 is also entered into the CAF. You can revoke a power of attorney by slashing a line on your copy of the first page, writing “Revoked” at the top of the form, and filing it with the IRS.

You can tailor a Form 8821 power of attorney. But a power of attorney is more comprehensive than a tax information authorization, since it allows a third party to negotiate and settle issues, sign a closing agreement or consent to extend the statute of limitations.

Powers of attorney are personal and portable, which means that only the individuals you’ve designated can act on your behalf.