

## Illegal Aliens: A Balance Sheet Liability

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**E**mployers with undocumented workers face potential fines, penalties and unpaid employment tax liabilities that could be a substantial unreported balance sheet liability. Even if the employer has hired only legally-documented workers, sizable fines can be imposed if proper documentation is not adequately gathered and maintained. CPAs signing audits must be aware of these potential liabilities and issue accurate financial statements in accordance with GAAP.

### Introduction

In 2011, the Pew Hispanic Center estimated that there were 11.2 million unauthorized immigrants in the U.S., 8 million of whom worked in the civilian labor force, comprising 5.2% of the total civilian labor force. Hispanics and Asians are becoming employed at a faster rate than whites and blacks. While most aliens enter the country legally and are legally authorized to work in the U.S., some are not.

If a company has unauthorized aliens working for them, the federal government can assess significant penalties and fines. In some cases, these fines and penalties—along with unpaid employment taxes—could be high enough to significantly affect the viability of the business. Given this potential liability, CPAs should be acutely aware of whether their clients have illegal aliens working for them. CPAs should work with their clients in at least two ways: helping their clients acquire the expertise to comply with the government's I-9 regulations, including the required documentation, and assisting clients in identifying any employees who might not have legal status.

Even if immigration reform is passed, the liability issue for clients will not disappear. There are two reasons. First, clients in certain industries may be predisposed to hire illegal workers due to the lower wage rate they can pay. Second, even if a client hires only legal workers, the client must know what information to collect and maintain in order to avoid a disruption in the workplace should the government decide to audit the firm's records.

### Employer's Responsibility

Employers must verify the identity and employment status of every employee via Form I-9, Employment Eligibility Verification Form. The original I-9 must be maintained for each current employee and for former employees for the one year after employment ends or for three years from the date of hire, whichever period is longer. These I-9s must be available for inspection by the U.S. Immigration and Customs Enforcement (ICE). If ICE decides to audit a business, it will issue a Notice of Inspection. The business then has three business days to produce the original I-9s and supporting documentation. Given the short period of time allowed to produce the documents, each business must have organized, up-to-date I-9s and supporting documentation.

Since ICE can take the business' computers and other records, the business should be certain to back up important files every night, especially since ICE may keep the computers and other documentation for an unlimited period of time.

### Penalties and Fines Imposed on Employers

There are two types of fines and penalties: Penalties for Knowingly Hire/Continuing to Employ Violations and Penalties for Substantive/Uncorrected Technical Violations. These two penalties can each be subjected to the increases in the Enhancement Matrix for businesses that, for example, didn't act in good faith or have a history of hiring undocumented workers.

In 2011 ICE conducted 2,496 I-9 audits, criminally arrested 221 employers and assessed over \$10 million in fines. Some of these employers will serve time in prison for hiring undocumented workers. 2011 was an unprecedented year for I-9 audits. ICE planned to increase the number of employer audits in 2012. In addition, employers are being penalized even when they do not have any illegal alien employees. ICE can fine an employer up to \$1,100 per worker for paperwork errors and mistakes.

### Employment Taxes

Fines and penalties aren't likely to be the only outstanding liability with respect to illegal workers. Presumably, the employer has not been paying or withholding employment taxes on the illegal workers. The employer will be responsible for paying its share of the employment taxes. Further, the employer, and specific employees who work for the employer, can be held responsible for paying the illegal workers' share of the employment taxes. Fines and penalties may apply in this category as well.

### I-9 Attorneys

Given that regulations governing employers' requirements with respect to employee documentation are in a constant state of change, the business should hire an attorney who is well-versed in I-9 audits to provide assistance in complying with I-9 regulations. The attorney could provide information on the new I-9 form that was released in March, 2013, I-9 preparation and compliance seminars to Human Resources and other appropriate personnel; analyze the business' current I-9 compliance program and provide a general assessment and recommendations; instruct Human Resources and other appropriate personnel on how to self-audit the I-9 program; conduct a mini-audit of the I-9s and the business' I-9 system and provide an analysis/report of the strengths and weaknesses of the program and a list of how to improve the I-9 compliance system; and/or conduct a comprehensive audit of the I-9 system. The attorney can also introduce the employer to the e-Verify program, which is an Internet-based system that provides a free, automated link to the Social Security Administration database and the

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Department of Homeland Security Administration immigration records in order to help determine the legal status of a prospective employee.

**Future Status**

Even if we do see fundamental reform in immigration law, it is likely that the government will be even more aggressive in protecting the nation’s legal workforce by ensuring that illegal workers are not being employed. Further, it will still be mandatory that employers complete the I-9 verification process for each employee, so employers should, if they haven’t already, ensure that they are I-9 compliant.

**Recommendations**

Fines, penalties, and employment taxes for noncompliance by employers of illegal aliens can be significant. Being proactive can save the employer from worry should an audit by the government be commenced, since the employer will know that they are following all of the federal regulations that govern alien employees. In addition, the CPA may want some assurance from an I-9 attorney that the client is compliant, and therefore not subject to a potential liability on the balance sheet.

**Table 1:  
Penalties for Knowingly Hire/Continuing to  
Employ Violations**

Employers determined to have knowingly hire or continuing to employ violations shall be required to cease the unlawful activity and may be fined. The agent or auditor will divide the number of knowing hire and continuing to employ violations by the number of employees for whom a Form I-9 should have been prepared to obtain a violation percentage. This percentage provides a base fine amount depending on whether this is a First Tier (1st time violator), Second Tier (2nd time violator), or Third Tier (3rd time or subsequent time violator) case. The standard fine amount listed in the table relates to each knowing hire and continuing to employ violation. The range of the three tiers of penalty amounts is as follows:

**Knowing Hire / Continuing to Employ Fine Schedule  
(For violations occurring on or after 3/27/08)**

Knowing Hire and Continuing to Employ Violations	Standard Fine Amount		
	First Tier \$375 – \$3,200	Second Tier \$3,200 – \$6,500	Third Tier \$4,300 – \$16,000
0% - 9%	\$375	\$3,200	\$4,300
10% - 19%	\$845	\$3,750	\$6,250
20% - 29%	\$1315	\$4,300	\$8,200
30% - 39%	\$1785	\$4,850	\$10,150
40% - 49%	\$2255	\$5,400	\$12,100
50% or more	\$2,725	\$5,950	\$14,050

**Table 2:  
Penalties for Substantive and Uncorrected  
Technical Violations**

The agent or auditor will divide the number of violations by the number of employees for whom a Form I-9 should have been prepared to obtain a violation percentage. This percentage provides a base fine amount depending on whether this is a first offense, second offense, or a third or more offense. The standard fine amount listed in the table relates to each Form I-9 with violations. The range of penalty amounts are as follows:

**Substantive / Uncorrected Technical Violation  
Fine Schedule**

Substantive Verification Violations	1st Offense \$110 – \$1100	2nd Offense \$110 – \$1100	3rd Offense + \$110 – \$1100
0% - 9%	\$110	\$550	\$1,100
10% - 19%	\$275	\$650	\$1,100
20% - 29%	\$440	\$750	\$1,100
30% - 39%	\$605	\$850	\$1,100
40% - 49%	\$770	\$950	\$1,100
50% or more	\$935	\$1,100	\$1,100

**Table 3:  
Enhancement Matrix**

The following matrix will be used to enhance or mitigate the recommended fine contained on the Notice of Intent to Fine.

Factor	Aggravating	Mitigating	Neutral
Business Size	+5%	-5%	+/-0%
Good faith	+5%	-5%	+/-0%
Seriousness	+5%	-5%	+/-0%
Unauthorized aliens	+5%	-5%	+/-0%
History	+5%	-5%	+/-0%
Cumulative Adjustment	+25%	-25%	+/-0%

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