

2010

YEAR END PAYROLL ISSUES SEMINAR

James A. Erdekian
Director

Kevin S. Rogers
Tax Supervisor



Feeley & Driscoll, P.C. | 200 Portland Street | Boston, MA 02114
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**Why should payroll tax
be important to you?**

Penalty for Failure to Deposit Taxes

Penalty Assessed Against:

- Company, Owners, Officers and/or Employees
- Trust Fund Taxes-Responsible person can become personally liable

Amount of Penalty:

- Tax Penalty is 100% of the Payroll Tax Due
- 2% - 15% Penalty for Late Deposit

Who are **NOT** Employees?

- Partners of Partnerships
- Members of Limited Liability Companies
- Independent Contractors
 - Offset Provisions Available??

Why the IRS Cares

- Retirement Benefits
- Fringe Benefits
- Social Security
- Unemployment
- Family Medical Leave Act
- Income Tax Withholdings

Employee vs. Independent Contractor

- Control vs. Independence
 - ▣ Make sure there is a written plan.
- Consistent Treatment
- Massachusetts Differences

(See **Exhibit 1**)

Independent Contractor

- Form 1099-MISC.:
 - \$600 or more in calendar year payment for services
 - Reimbursed expenses of independent contractor included on 1099

- Incorporation exception not applicable to attorneys

2010 & 2011 U.S. Social Security Wage Bases

Taxable Wage Base (Maximum Annual Taxable Compensation) Applicable To:

	<u>2010</u>	<u>2011*</u>
Social Security	\$106,800	\$106,800
Medicare	Unlimited	Unlimited



2010 & 2011 Social Security Rates

Tax Rate (Employee and Employer Each) Applicable To:

	<u>2010</u>	<u>2011</u>
Social Security 6.20%	6.20%	
Medicare	<u>1.45%</u>	<u>1.45%</u>
Total	7.65%	7.65%

**Effective 2013, Medicare tax will increase to 2.35% for “high income” individuals with an additional 3.8% tax Medicare tax on investment income.

2010 & 2011 Unemployment Wage Base

Tax Rate (Employer Only) Applicable To:

2010 & 2011

Federal Unemployment (Gross Wages)	\$7,000 *
State Unemployment (Gross Wages)	\$14,000

**

*At a rate of .008 (after credit for SUT)= \$56 per employee

**Based on each employer's experience rate



What is Gross Salary?

- Wages
- Bonus
- Taxable Fringe Benefits
- Stock Options

(Other Compensation **See Exhibit 2**)



What is **NOT** Taxable Compensation?

- Certain Fringe Benefits:
 - Employer Paid Health Insurance
 - Employer Paid Retirement Contributions
 - Education Expenses (not in excess of \$5,250)
(* See Exhibit 3)

- Employee Contributions for:
 - Cafeteria Plans
 - 401(k) and 403(b) Contributions

- Qualified transportation expenses

- Reimbursed Expenses under “Accountable Plan”

Disability Benefits

- If employer paid disability benefits received was on a **pre-tax** basis then the benefits received by the employee would be includible in taxable income.
- If employer paid disability benefits received was on an **after-tax** basis then the benefits received by the employee would be excluded from taxable income.

Qualified Parking & Pass Limitations

Qualified Transportation Fringe:

□ Federal* 2011

Vehicle/Transit Pass Limit
\$230/month

Qualified Parking Limit \$230/month

□ Mass*

Vehicle/Transit Pass Limit
\$230/month

Qualified Parking Limit \$230/month

*Estimated as numbers have not yet been adjusted for inflation



Employee Expense Reimbursement

General Rule (Non Accountable Plan/No Substantiation):

Taxable To Employee, Added To W-2

Accountable Plan/Substantiation:

- ▣ Reimbursement is Taxable On Excess
- ▣ Must Be A Written Plan

Accountable Plans

Employees must meet all of 3 rules:

- Incurred expense while performing services
- Account to employer within a reasonable time (60 days)
- Returned amounts in excess of expense within a reasonable time (120 days)

Non Accountable vs. Accountable

	<u>Non- Acct.</u>	<u>Acct.</u>
Expense Allowance	\$3,600	\$3,600
□ Amount Substantiated	<u>0</u>	<u>2,400</u>
□ W-2 Amount	\$3,600	\$1,200

Note: W-2 Amount Subject to FICA,
Medicare and Income Taxes

Type of Reimbursements

For Use Of Employee's Auto:

- Mileage, Tolls, Parking:

2010

50.0

2011

50.0 (As of now)

- Travel (Airfare, Cabs)
- Meals, Lodging (Per Diem **Exhibit 5**)

Substantiation of Business Expenses by Employees

- Complete Monthly Expense Report and require inclusion of receipts

(See Exhibits 6 through 12)

Taxable Fringe Benefits

- Personal Use of Company Owned Auto
- Transportation Benefits
- Group Term Insurance
- Shareholders Health Insurance (S Corps Only)
- Officer's Life and Disability Insurance

Personal Use of Company Owned Auto

- Commuting Value--EE < \$195k
- Annual Lease Value--Owner and EE > \$195k

(See Exhibit 6-12)



(Note: Subject to FICA, Medicare and Income Taxes)

Annual Lease Value Calculation

Personal Use of Company Owned Auto

- A uses a corporate owned vehicle. The fair market value of the vehicle is \$35,000. A determines the personal use of the auto to be 20%.

Annual Lease Value for a \$35,000 auto
\$9,250

Personal use percentage (From Log) 20%

Amount includible in A's W-2 gross income \$1,850

Annual Lease Value Table

Automobile Fair Market Value

Annual Lease Value

\$0 to 999	600
1,000 to 1,999	850
2,000 to 2,999	1,100
3,000 to 3,999	1,350
4,000 to 4,999	1,600
5,000 to 5,999	1,850
6,000 to 6,999	2,100
7,000 to 7,999	2,350
8,000 to 8,999	2,600
9,000 to 9,999	2,850
10,000 to 10,999	3,100
11,000 to 11,999	3,350
12,000 to 12,999	3,600
13,000 to 13,999	3,850
14,000 to 14,999	4,100
15,000 to 15,999	4,350
16,000 to 16,999	4,600
17,000 to 17,999	4,850
18,000 to 18,999	5,100

Annual Lease continued

Automobile Fair Market Value

Annual Lease Value

19,000 to 19,999	5,350	
20,000 to 20,999	5,600	
21,000 to 21,999	5,850	
22,000 to 22,999	6,100	
23,000 to 23,999	6,350	
24,000 to 24,999	6,600	
25,000 to 25,999	6,850	
26,000 to 27,999	7,250	
28,000 to 29,999	7,750	
30,000 to 31,999	8,250	
32,000 to 33,999	8,750	
34,000 to 35,999		9,250
36,000 to 37,999	9,750	
38,000 to 39,999	10,250	
40,000 to 41,999	11,250	
44,000 to 45,999	11,750	

Annual Lease continued

Automobile Fair Market Value

Annual Lease Value

46,000 to 47,999	12,250
48,000 to 49,999	12,750
50,000 to 51,999	13,250
52,000 to 53,999	13,750
54,000 to 55,999	14,250
56,000 to 57,999	14,750
58,000 to 59,999	15,250

For vehicles having a fair market value in excess of \$59,999, the Annual Lease Value is equal to: $(.25 \times \text{the fair market value of the automobile}) + \500 .

Group Term Life

- Amount > \$50,000
- Age
- GTL Amount vs. Premium Paid
- Subject to FICA, Medicare and Income Taxes

Calculation of Fringe Benefit

X Corporation pays premium on a \$70,000 group term life insurance policy on the life of its president A. A is 50 years old. The IRS established uniform cost \$1,000 of group term coverage is \$2.76 (\$.23 X 12). The cost of the policy includible in A's gross income is computed as follows:

	Total insurance coverage
\$70,000	
	“Tax free insurance coverage”
<u>(50,000)</u>	
	Insurance coverage subject to tax
	<u>20,000</u>
	Excess Coverage/\$1,000= \$20,000/\$1,000 =
.....20	
	Group term coverage premium (\$.23x12)
<u>2.76</u>	
	Taxable cost of policy includible in A's



Group Term Life Insurance Fringe Benefit

Cost Per \$1,000 of Protection for One-Month
Period

<u>Age</u>	<u>Cost</u>
Under 30	6¢
30 through 34	8¢
35 through 39	9¢
40 through 44	10¢
45 through 49	15¢
50 through 54	23¢
55 through 59	43¢
60 through 64	66¢
65 through 69	\$1.27
70 and above	\$2.06

Additional Wages for Owners

- 2% S Corp. Shareholder Health Insurance must be included in the W-2 box 1 and box 14, subject to Federal and State income tax;
 - Available as a deduction on the shareholder's personal income tax return.

- Officers' Life & Disability Premiums
 - Subject To All Three Withholdings
 - Tax insurance disability premium should make future disability benefit non-taxable

Multi-State Withholding

- US workforce is more mobile and it is not uncommon to find employees that work in several states for one employer in a single year

- In which state do you withhold?
 - The Default Rule
 - Where services are performed
 - Rule One
 - Residency
 - Rule Two
 - Reciprocity
 - Rule Three
 - Resident/Nonresident Taxation Policy

Work State vs. Resident State

- Step One
 - Determine state of residence
 - Not necessarily “home” state
 - Resident by either being domiciled in the state or spending more than a certain number of days in the state
- Step Two
 - Reciprocal agreement:
 - Allows you to withhold in the state of residence instead of where services are performed (See [Exhibit 13](#))
- Step Three
 - Resident/Non-Resident taxation policies
 - If resident of one state, performing services in another and no reciprocal agreement, you must consider the laws of both states.
 - State of residence is important in this determination

Non-resident Withholdings

- **Alabama, Arkansas, Connecticut, Delaware, Kansas, Massachusetts, Missouri, Oregon, Rhode Island, Utah, and Vermont require withholdings from residents and nonresidents performing services within their States without any exceptions.**
- **Arizona** does not require withholding if the nonresident is physically present in the State for fewer than 60 days in a calendar year. **Hawaii** does not require withholding if the nonresident individual does not perform services in the State for more than 60 days. Nonresident individuals who work in the State of **Maine** are not subject to the State's withholding laws if they perform services in the State for 10 days or fewer. **New Mexico** does not require withholding if the nonresident employee performs services in the State for 15 days or less.

Nonresident Withholdings

- **California, Idaho, Maryland, Nebraska, New Jersey, Ohio, Oklahoma, South Carolina, Virginia, West Virginia, and Wisconsin** measure their withholding liability for nonresident individuals on a specified dollar amount earned in the State. For example, in Idaho, nonresidents who earn less than a \$1,000, for the year, for work performed in the State are exempt from withholding.
- **Georgia** does not require withholding if the nonresident has not been employed in the State for more than 23 days or if the amount paid for services performed in Georgia does not exceed the lesser of five percent of total income received or \$5,000.
- **The State of New York** does not require withholding on wages paid for services performed in the State for a short time and if the wages will not exceed the employee's personal exemption.
- **District of Columbia** does not withhold from any nonresident individual provided the necessary forms are completed and submitted.

Payroll Taxes For Workers Abroad

- Must withhold taxes, including FICA (Social Security & Medicare)
- Tax Treaty Exclusions- Depends on the country
- Section 911 Exclusion
 - Employee must complete Form 673 to exclude Federal Income Tax Withholding on Foreign Earned Income & Housing Exclusion wages
 - FICA Taxes must generally still be withheld

(See **Exhibit 14**)

Federal Tax Levies

Withholding

- If an employer receives a Notice of Levy on Wages, Salary, and Other Income, the employer **MUST** withhold certain amounts from employee wages
- Only bankruptcy orders & child support take precedence over these federal tax levies
- Failure of the employer to remit wages to the IRS subject to levy results in liability to the employer for the wages withheld, plus penalties and interest

(See **Exhibit 15**)

Child & Medical Support Withholding

- Employers are required to withhold state ordered child support and medical support for that child
- Uniform Interstate Family Support Act (UIFSA) requires that employers comply on out of state orders as well

(See **Exhibit 16**)

HIRE Act Tax Incentives

- Employers who hire unemployed workers this year (after Feb. 3, 2010, and before Jan. 1, 2011) may qualify for a 6.2-percent payroll tax incentive, in effect exempting them from the employer's share of Social Security tax on wages paid to these workers after March 18.
- Businesses may also claim a new hire retention credit of up to \$1,000 per worker on their income tax return.
- All wages paid after 3/18/10, need to be included on the employee's W-2 in Box 12 code CC for HIRE exempt wages.

COBRA Medical Coverage Credit

- ❑ Eligible former employees, enrolled in their employer's health plan at the time they lost their jobs, are required to pay only 35 percent of the cost of COBRA coverage.
- ❑ The employers are entitled to a credit for the other 65 percent of the COBRA cost on their payroll tax return.
- ❑ Not yet extended for 2011.

Reporting of Benefits on W-2's

22222		Void <input type="checkbox"/>	a Employee's social security number		For Official Use Only ▶ OMB No. 1545-0008	
b Employer identification number (EIN)			1 Wages, tips, other compensation		2 Federal income tax withheld	
c Employer's name, address, and ZIP code			3 Social security wages		4 Social security tax withheld	
			5 Medicare wages and tips		6 Medicare tax withheld	
			7 Social security tips		8 Allocated tips	
d Control number			9 Advance EIC payment		10 Dependent care benefits	
e Employee's first name and initial		Last name	Suff.	11 Nonqualified plans		12a See instructions for box 12
f Employee's address and ZIP code			13 Statutory employee <input type="checkbox"/> Retirement plan <input type="checkbox"/> Third-party sick pay <input type="checkbox"/>		12b	
			14 Other		12c	
15 State			Employer's state ID number	16 State wages, tips, etc.	17 State income tax	18 Local wages, tips, etc.
19 Local income tax			20 Locality name			

Form **W-2** Wage and Tax Statement

2009

Department of the Treasury—Internal Revenue Service

For Privacy Act and Paperwork Reduction Act Notice, see back of Copy D.

Copy A For Social Security Administration — Send this entire page with Form W-3 to the Social Security Administration; photocopies are not acceptable.

Cat. No. 10134D

Do Not Cut, Fold, or Staple Forms on This Page — Do Not Cut, Fold, or Staple Forms on This Page

(See Exhibit 17 & 18)

Electronic Federal Tax Payment System (EFTPS)

- Penalty: 10% Of ALL Deposits not E filed
- Effective 2011, ALL businesses must make employment tax deposits ONLINE – unless \$2,500 or less quarterly payroll tax liability
- Web site: www.eftps.gov

(See Exhibit 19)

Massachusetts Electronic Filing Requirements

- In MA, all corporations must file their returns and pay their income taxes electronically if gross income is more than \$100,000.
- Partnerships with gross income of \$50,000 or more, \$50,000 or more in ordinary loss or with 25 or more partners must file electronically.
- All pension payments must file and pay electronically.
- All new businesses (as of September 1, 2003) must file and pay electronically.

Massachusetts Electronic Filing Requirements Continued

- **Employers with 50 or more employees** must submit wage reports electronically.
- **For wage withholding, room occupancy and sales/use taxes** must be filed and paid electronically **if the total is \$10,000** or more for the previous year.
- **A business filing entity must register for the E-file program**, the registration procedure can be found at the Webfile for business link at <https://wfb.dor.state.ma.us/webfile/>. There is a \$100 penalty for failure to file, report or pay electronically. Failure to use the electronic method will be deemed a failure to file.

IRS Grants Relief to Businesses

- Businesses may designate their estimated income tax overpayments as employment tax deposits - **helps cash flow**

W-4 for 2009

- When First Hired
- Changes in Personal Situation
- Nanny tax

(See Exhibit 20, 21, 22)

Payroll Forms-Federal

Quarterly Reports

- 941
 - Due
 - 1/31
 - 4/30
 - 7/31
 - 10/31

Annual Reports

- W-2
 - Due - 1/31
- W-3
 - Due - 2/28
- 940
 - Due - 1/31
- 1099
 - Due - 1/31
- 1096
 - Due - 2/28

Payroll Forms-State

Quarterly Reports

- State Unemployment Contrib
- WR-1
- M-941/M-942 (or monthly)

Annual Reports

- Copies of 1099/1096
 - Due 2/28

All Forms Due:

1/31

4/30

7/31

10/31

Year-End Payroll Activities

(See **Exhibit 23** for details)

New IRS Web Tool

IRS Retirement Plans Navigator

<http://www.retirementplans.irs.gov/>

- A side-by-side chart compares all the main features of these plans, including details on how the plan is set up and operated, maximum contributions, and accessibility features (i.e., whether loans and hardship withdrawals are allowed).
- Clicking on one of the types of plans covered calls up a list of its essential features, plus links for more information on how the plan works, operating it and correcting errors.

(See **Exhibit 24** for details)

Employment Tax Audits

- The IRS announced that it expects to expand its auditing activities by embarking on a 3-year campaign that will audit 6,000 businesses both big and small.
- While some companies deliberately mis-classify their workers in order to escape offering health insurance and 401K plans to their employees, some business owners are flat out confused as to how to correctly classify their employees

List of Handouts

1. Employee/Independent Contractor Factors
2. Items of Non-payroll Compensation
3. Employee's Income/Exclusion for Employer-provided Educational Assistance
4. IRS Revenue Rulings
5. Per Diem Rates
6. Employee Personal Automobile Usage
7. Monthly Statement for Employees Receiving Auto Expense Reimbursement
8. Handout Sample of an Expense Report
9. Personal Use of Company Owned Auto
10. Fringe Benefit Compensation Value for Employer-provided Auto
11. Handout Sample of Mileage for Employee Business Auto Use
12. Written Policy Statement
13. State Tax Reciprocal Agreements
14. Payroll Taxes and Withholding Requirements for U.S. Citizens and Resident Aliens Working Abroad
15. Federal Tax Levies
16. Child and Medical Support Withholding Orders
17. Copy of W-2
18. W-2 Preparation
19. EFTPS Payment Instruction Booklet
20. Copy of W-4
21. Employee Payroll Information Sheet
22. Payroll Change Form
23. Year-End Payroll Activities
24. IRS Pension Plan Tool & Pension Plan Limits 2010
25. Employment Tax Audits Tips Article
26. Massachusetts Healthcare Reform Information
27. Copy of W-9