

Payroll Trends

1st Quarter 2007

Minimum Wages

The House of Representatives and the Senate have both approved a \$2.10 increase in the minimum wage; from \$5.15 to \$5.85 60 days after being signed into law, to \$6.55 one year later and to \$7.25 two years after becoming law.

The Senate version included \$8.3 billion in tax breaks for small businesses, with the House now passing additional language for the minimum wage bill to add \$1.3 billion in small business tax breaks.

The legislation will now go to a joint House-Senate conference committee to iron out differences. Leaders of both legislative bodies think differences will be resolved and the legislation sent to the President for signing into law.

The conference committee could include in the final law an expanded Work Opportunity Tax Credit, FICA tax credits on tips based on the \$5.15 current minimum wage, increased limits for deferred compensation and increased penalties for willfully not making estimated tax payments, keeping proper records or not filing tax returns. If, and when, the law passes, be alert to the effective dates and accompanying changes.

Payroll Drives America

A recent Congressional study clearly shows the importance of payroll to the federal government. For 2005, individual income taxes were 43% of federal revenues, while social security and medicare taxes made up 36.9% of federal revenue. With payroll collecting most of these taxes, employers are truly the tax collectors for the federal government. Add all the state and local taxes on payroll, as well as withholding for benefits, etc., and the importance of payroll is clearly apparent to the well being of not only all government activities, but individuals as well.

Exempt Computer Employee

There has been confusion regarding the wage requirement for exemption of computer professionals as defined by Department of Labor (DOL) regulations under the Fair Labor Standards Act (FLSA). If a person meets the other tests and are compensated by a salary of at least \$455 per week or on an hourly basis of at least \$27.63 per hour, then they are exempt under the FLSA.

Identity Theft

As we have reported several times, human resource and payroll departments, along with their data systems, are tempting targets for identity thieves. With "everything" they need in one place (names, address, key identification numbers, dependents, etc.), it is imperative that employers utilize diligent safety measures to assure information does not fall into the wrong hands. This applies to businesses of all sizes and often merely requires common sense measures, such as passwords, locked doors and files, etc.

April 17 Filing Date

Federal law defines "legal holiday" as a legal holiday in the District of Columbia. New city legislation designated April 16 as "Emancipation Day" in DC. The normal filing day for payroll tax deposits, filing of various tax returns, etc., is April 15, 2007. The tax code states that filing and payment deadlines that fall on Saturday, Sunday or legal holiday are extended until the next business day. Therefore, payments and returns due April 15 will be considered timely if filed or paid on Tuesday, April 17, 2007, thanks to the new DC holiday. Check to see if your state and local deadlines have also been extended.

Summer Labor

Employers are reminded that child labor laws cover any employees age 17 or under. The rules are different by age groups: 14-15, 16-17 and 17 and older. Therefore, if you are considering employees in these age groups, you may wish to go to www.dol.gov/elaws/flsa/cl to refresh yourself on the unique requirements.

Fringe Benefits

Do you ever wonder if a payment, award or expense is a taxable fringe benefit? The IRS provides a free resource with the rules for valuing and taxing various benefits, Publication 15-B. Titled Employers Tax Guide to Fringe Benefits, it is a must that every employer have access to this information to properly handle payroll related activities for their employees. Like most things payroll, it may be secured from www.irs.gov.

Contributions

The IRS has issued guidelines to substantiate charitable donations through payroll deductions. The Pension Protection Act of 2006 made the recordkeeping requirements for claiming tax deductions for cash contributions more strict. The IRS indicates a pay stub, Form W-2, or other document from the employer showing the amount and purpose of the donation, along with a donor card or other donor document showing the name of the organization will meet the substantiation requirements.

Exempt Employee Deductions

The Department of Labor (DOL) has ruled deductions can be made from an exempt managers bonus checks to repay cash shortages and bad checks as provided in the written bonus plan. Since the manager makes at least \$455 per week in salary, any compensation beyond that amount is a matter on contractual agreement between the parties and does not constitute improper deductions from the salary of the employee.

Professional Partners

Are you tired of fighting to stay current with the ever changing federal, state and local rules that apply in minimum pay bills now in conferaying your employees? Would you rather be spending your time on the things you do well in making your business a success? As a professional resource in a constantly changing area many employers are not comfortable, we provide services to allow your in-house resources to be used in your areas of specialization. Please feel free to contact us regarding the services, or additional services, we can provide and let us partner together to maximize your business potential.

Backup Withholding

Payers making certain "reportable" payments may be responsible for federal income tax withholding. These non-payroll withholdings are generally referred to as "backup withholding" and the current withholding rate is 28% of the gross payment amount.

Reportable payments include interest, dividends, rent, royalties, non-employee compensation and commissions, as well as other items reported on the various Information Return Forms 1099. Thus vendors and independent contractors could both fall under backup withholding requirements.

Payments to government agencies and tax-exempt organizations are not subject to backup withholding under current rules. Also, payments to corporations are exempt unless for medical or health care payments, or for gross proceeds payable to attorneys.

Since the payer is required to provide the payee a Form 1099 with the payee name and taxpayer identification number (TIN), it is the payees responsibility to provide the payer correct information to facilitate this reporting.

Payers normally use Form W-9 to secure a payees name and TIN, and to secure certification that the name and TIN are correct. If for any reason the payee does not provide a TIN to the payer, the payer generally must start backup withholding on all reportable payments and continue to do so until the TIN and certification are secured. Likewise, if the payer is notified that a TIN is incorrect, withholding could be required. The payer first solicits the payee for correct information, but if the payee does not provide corrected information in a timely manner, the payer must backup withhold on subsequent reportable payments. Publication 1281 provides more details on backup withholding for TIN/name mismatches. It is available at www.irs.gov/pub.

If you have not been complying with information reporting and/or backup withholding requirements, contact us for the services we can provide to help you with your tax deposit requirements, or other areas we may be of help to meet all your compliance responsibilities.

Budget Proposal

The budget proposal submitted by President Bush for the 2008 fiscal year (October 1, 2007-September 30, 2008) would once again require employers to shoulder the responsibility for implementation of a broad range of changes in the payroll related area. The budget items are only a proposal and have not yet been introduced for legislative consideration. However, they may be indicative of potential areas that could lead to some form of legislation in the future.

Permanent Tax Cuts

As proposed in the last few budgets, the 2001 legislation reducing taxes for individuals would become permanent. Currently, the 2001 provisions are scheduled to expire on December 31, 2010 and revert back to pre-2001 law. Some of these items are the 10% rate bracket, expanded 15% bracket and increased standard deduction to eliminate the "marriage penalty", increased child credit, and expanded income exclusions for employer-provided education.

Employer-Provided Health Benefits

Under the budget as proposed, high cost, employer-provided health care benefits would become subject to income and employment tax and be reportable separately on Form W-2s. Replacing the current exclusion from income, itemized deduction or self-employed deduction, individually purchased benefits would create new "standard" tax deductions of \$15,000 for family coverage and \$7,500 for single coverage. Businesses would continue to have an expense deduction for employer-provided health insurance.

Employer Retirement Savings Accounts (ERSAs)

The budget proposes to consolidate current defined benefit plans allowing pre-tax deferral or after-tax contributions into new ERSAs. These new Employer Retirement Savings Accounts would be available to all employers and would follow rules similar to current 401(k) plans.

Unemployment Insurance

The budget proposes to extend the 0.2% Federal Unemployment Tax Act (FUTA) surcharge through December 31, 2012. In addition, individual states would be allowed to redirect portions of overpayment recoveries to enforcement, with penalties required for obtaining benefits through fraudulent means.

Information Reporting

As proposed, independent contractors paid \$600 or more per year must furnish a W-9 to the payer and the business must verify the taxpayers identification number/name match. If no W-9 is provided, a flat- rate withholding must be made. Businesses would also be required to withhold tax if the recipient requests withholding from the gross payment. For the first time, information returns would also be required for all payments of \$600, even payments to a corporation (except tax-exempt organizations). Federal, state and local governments would also be required to provide information returns for most non-wage payments for property and services.

The budget would also increase penalties for non-compliance with information return reporting effective for 2008. For each information form not filed, the penalties could reach \$250, with total fines of up to \$1.5 million for non-compliance.

Retirement Savings Accounts (RSAs) and Lifetime Savings Accounts (LSAs)

The new budget would consolidate the three types of current individual retirement accounts (traditional IRAs, non-deductible IRAs and Roth IRAs) into a new single account known as a Retirement Savings Account. Since these accounts would be only for retirement, withdrawals for any other reason would be subject to regular taxation and penalties for early withdrawal.

Likewise, current non-retirement IRAs (such as 529 plans) would be convertible to new Lifetime Savings Accounts usable for any purpose, including health care and education. Contributions of up to an aggregate of \$2,000 per year would be allowed from after-tax dollars, with earnings on the accounts accumulating tax-free. Distributions would then be excludable from income regardless of when made.

Health Savings Accounts (HSAs)

Under the new budget, HSAs would be more flexible and provide more incentive to change to this type coverage for health care needs. Definition changes would be more liberal than current plans, making the amount of coverage and who could be covered more appealing to employees.

Work Opportunity Tax Credit

Although included in both versions of the minimum pay bills now in conference committee, the budget also proposes to extend the Work Opportunity Tax Credit for one year. Therefore, this is a provision that seems likely to be extended as Congress certainly seems in favor of an extension.

Child Labor Laws

If adopted, proposals are included to increase civil penalties for willful violation of child labor laws. Increases are also included to fund additional investigators specifically targeting child labor law violations.

Career Advancement Accounts (CAAs)

A new self-managed account is also included in the budget. The Career Advancement Account would provide help for workers entering the work force, transitioning between jobs or seeking new skills to advance in the workplace. Details are still sketchy as to how funds would be put in the account, taxability, etc., and hopefully will be outlined as the budget process continues.

Earned Income Credit

Eligibility requirements for the earned income credit would be clarified under the new budget for separated spouses and qualifying children. Also, only a person with a valid social security number for employment purposes could qualify.

Employee Leasing

Standards would be created under the budget for determining when an employee leasing company is liable for federal employment taxes and whether there would be joint liability with their client.

Other Proposals

Other proposals in the budget would increase collections in the child support area, increase funding to allow a national employment authorization verification system, make repeated failure to file tax returns a felony, and look at social security reform through previously discussed efforts.