Payroll Trends

1nd Quarter 2009

Stimulus

The American Recovery and Reinvestment Act of 2009 (ARRA) was signed into law by the President on February 17, 2009. Continuing the trend of the last two decades, employers are at the forefront in implementing some of the major provisions of the new legislation.

In this issue we will provide an overview of some of the provisions involving employers. However, depending on how the economy reacts, employers could also be involved in additional initiatives as the year progresses. For more detailed and up-to-date information on any of the ARRA provisions, go to the IRS web site, www.irs.gov.

Making Work Pay

The largest dollar amount of the stimulus plan is the Making Work Pay tax credit for individuals. This part of the ARRA provides a tax cut for 2009 and 2010 of $400 for individuals with an adjusted gross income of $75,000 or less. For married persons filing jointly and making $150,000 or less, the credit will be $800.

Rather than receiving a refund check similar to the 2008 stimulus, Making Work Pay will be implemented no later than April 1, 2009, through new reduced withholding tables, incrementally providing the credit to employees. Thus, each employee will receive a small increase in take home pay each pay period throughout the year.

No action will be required by the employee to activate the new withholding from their checks. However, those employees and couples with more than one employer may wish to file a revised W-4 to assure they have enough withholding to cover their combined income.

The credit will be claimed when filing 2009 and 2010 income tax returns, up to the ARRA limits. For self-employed persons or those without adequate withholding, their tax return will be the only way to claim the tax credit. Most individuals will be eligible for the credit except nonresident aliens and those eligible to be claimed as a dependent on another tax return. A valid social security number will also berequired to secure the credit.

For persons on fixed incomes from social security, railroad retirement, veteran benefits and government retirement, a $250 payment will be made to them from their paying agency. Although there is no income cap for receiving this payment, the payment will reduce the Making Work Pay credit and will be adjusted through the individual tax return filed at year-end.

Earned Income Credit

The ARRA legislation also increases the Earned Income Tax Credit (EITC) percentage to 45% for larger families with three or more qualified children. The phase out threshold for married couples filing joint returns increases to $5,000 over the amounts for single taxpayers.

Like the revised tables for federal income tax withholding, new Advanced Earned Income Credit (AEIC) tables are required to reflect these ARRA changes. The maximum advanced credit available remains $1,826 for 2009.

Other ARRA provisions of interest to employers are covered in articles on the following pages. Employers should also be alert to information from their state and local tax authorities for other changes in these difficult financial times.

Transit Benefits

Qualified transportation fringe benefits are excluded from an employee's taxable wages up to specified dollar limits. The ARRA legislation increases the current $120 monthly exclusion for transit passes and van pooling to match the $230 monthly exclusion limit for parking. The new limits start March 1, 2009, at $230 and continue to match the indexed parking benefit amounts through 2010.

Work Opportunity Credit

The Work Opportunity Tax Credit allows employers to claim a tax credit of 40% of the first $6,000 of wages paid to employees in any of nine targeted groups. ARRA creates new groups eligible for the Work Opportunity Tax Credit for hiring unemployed veterans and disconnected youth in 2009 and 2010.

Unemployment Benefits

ARRA temporarily suspends federal income tax on the first $2,400 of unemployment benefits received per recipient in 2009. Benefits received in excess of $2,400 will still be subject to federal income tax for all recipients.

Minimum Wage

The Fair Minimum Wage Act of 2007 included phased increases to the federal minimum wage. The third phased increase is effective July 24, 2009, when the federal minimum wage becomes $7.25 per hour. Many states also have minimum wage laws, with the employee in those states entitled to the higher of the federal or state minimum wage.

Government Contractors

ARRA has delayed until January 1, 2012, previously approved rules that required information reporting and 3% withholding on payments to persons providing property or services to state or local governments that have annual expenditures of $100 million or more.

In 2008, regulations were revised to require recipients of federal contracts to use the E-Verify system to assure that employees working on government projects are eligible to work. This requirement was to begin on January 15, 2009, then moved to February 20, 2009. The U.S. Chamber of Commerce filed suit to block the implementation, and the new administration has now pushed implementation to May 21, 2009, the next date for the court case to be continued.

Publication 15-T

Employers will receive a new publication as the result of ARRA. The new Publication 15-T will contain revised wage withholding tables and advanced earned income credit tables. The new tables must be implemented no later than April 1, 2009. The new publication will contain a required notice to employees on how withholding will be affected. A copy of Form W-4 is included in the publication, but is not required for employees to receive reduced withholding.

Retire Online

The Social Security web site now includes an online retirement application that is touted as taking as little as 15 minutes to complete. In most cases, after submitting the application nothing else is required. If there are any questions, Social Security will contact you directly. If you are uncertain when to retire, there is an online fact sheet to answer your questions. If you are still in the planning stages, a personalized Retirement Estimator can project your retirement benefits at various ages. To utilize these features, go to socialsecurity.gov.

Worker Classification

The Treasury Inspector General has now joined the list of officials indicating one of the largest areas of non-compliance adding significantly to the tax gap is the misclassification of workers as independent contractors rather than employees. This results in uncollected and unpaid taxes that must be subsidized by other employers and taxpayers. The Inspector General is recommending there be a single area in the IRS responsible for resolving this issue.

Free Benefit Help

Fringe benefits provided to employees are generally taxable unless specifically excluded by law. There is a free resource available to   all employers that answers most of the common questions about these benefits. Publication 15-B, Employers Guide to Fringe Benefits isavailable online at www.irs.gov/publications.

Compliance Help

The ARRA is only the latest legislation impacting employers through payroll-related mandated activities. Managing these type changes has become an area of specialized expertise, often not reasonably available to many employers.

We are a professional resource available to partner with you to help with these type of compliance problems. We would like the opportunity to discuss our specific services with you and show the efficiency we can provide to your organization.

COBRA

The American Recovery and Reinvestment Act of 2009 (ARRA) provides for premium reductions and additional election opportunities for health benefits under the Consolidated Omnibus Budget Reconciliation Act of 1985, commonly called COBRA. Eligible individuals pay only 35 percent of their COBRA premiums and the remaining 65 percent is reimbursed to the coverage provider through a tax credit.

The premium reduction for COBRA continuation coverage is available to "assistance eligible individuals." An "assistance eligible individual" is the employee or a member of his/her family who is eligible for COBRA as a result of the employee's involuntary termination between September 1, 2008, and December 31, 2009.

Those who are eligible for other group health coverage (such as a spouse's plan) or Medicare are not eligible for the premium reduction. There is no premium reduction for premiums paid for periods of coverage prior to February 17, 2009.

ARRA treats assistance eligible individuals who pay 35 percent of their COBRA premium as having paid the full amount. The premium reduction (65 percent of the full premium) is reimbursable to the employer, insurer or health plan as a credit against certain employment taxes. The 65% premium reduction is not treated as taxable income to the individual receiving COBRA assistance.

The IRS has revised Form 941, Employers Quarterly Federal Tax Return, to facilitate recovery of the subsidy payments through credit against quarterly payroll tax remittances. Tax deposits during the quarter may be reduced with no penalty, as long as the balance due for the quarter is paid in full. If the COBRA credits exceed the taxes due, a credit can be carried forward to the next quarter or a refund can be requested.

Although not remitted with the Form 941, those claiming the credit must maintain supporting documents showing the following:

- Dates and amounts for receipts of eligible 35% premiums.
- Copies of invoices from insurers and proof of payment of full premiums.
- If self-insured, proof of premium amounts and coverage provided.
- Proof of involuntary termination, including dates, for those eligible for the subsidy.
- Proof of COBRA eligibility and election of coverage.
- Record of SSN, amount of subsidy and whether individual or family coverage for whom credit is claimed
- Any other documents to prove the correctness of reimbursement.

Individuals involuntarily terminated from September 1, 2008, through February 16, 2009, who did not elect COBRA when it was first offered OR who did elect COBRA, but are no longer enrolled (for example because they were unable to continue paying the premium) have a new election opportunity. This election period begins on February 17, 2009, and ends 60 days after the plan provides the required notice. COBRA coverage elected in this special election period begins with the first period of coverage, beginning on or after February 17, 2009.

Plan administrators must provide notice about the premium reduction to all individuals who have a COBRA qualifying event during the period from September 1, 2008, through December 31, 2009. Individuals eligible for the special COBRA election period also must receive a notice informing them of this opportunity. This notice must be provided within 60 days following February 17, 2009.

If an employer offers additional coverage options to active employees, the employer may (but is not required to) allow assistance eligible individuals to switch the coverage options they had when they became eligible for COBRA.

The ARRA does not modify any other COBRA provisions. Benefits are not extended beyond the normal 18 months as provided by COBRA and does not provide benefits to small employers of less than 20 employees.

If an individual's modified adjusted gross income for the tax year in which the premium assistance is received exceeds $145,000 (or $290,000 for joint filers), then the amount of the premium reduction during the tax year must be repaid.

Budget

The preliminary overview of the budget proposed by President Obama for the next fiscal year shows several areas of potential direct, or indirect, employer involvement. A few areas are indicated in this article. These are from the budget overview that may be reviewed at www.whitehouse.gov/omb/assets/fy2010_new_era/a_new_era_of_responsibility2.pdf.

The budget overview proposes to make permanent the $800 ($400 for single taxpayers) "Making Work Pay" tax credit as an offset to the first $6,450 of earnings for 95% of all American workers.

There is also a proposal to try to eliminate the over $3.9 billion of erroneous unemployment benefits paid in 2008, along with an estimated $300 million of evaded tax payments over the next ten years. This is an effort to stabilize the unemployment program for tax payments by employers and benefits for recipients.

Portions of the 2001 revised tax rates for individuals would be allowed to expire at the end of 2010, as provided in the original legislation. The effect would be to reinstate the 36% and 39.6% tax rates for taxable incomes over $250,000 (joint) or $200,000 (single).

Advanced earned income credit payments would be eliminated under the proposed budget, based on data that only 1% of those eligible for the earned income credit receive the advanced payments. To encourage work by low and middle-income families, the earned income credit would be expanded rather than use other forms of aid.

Another primary goal of the new administration is to lower health care cost from the current $8,000 per person in the United States, which represents approximately 16% of the economy and is one of the most expensive in the world. Likewise, ways to expand coverage to the full workforce will be explored. What this means to employers will be a topic of discussion as the year progresses.

As proposed, employers would automatically enroll employees in pension plans, with employee opt out availability. For employers without any type pension plan, a direct deposit IRA account would be required to be established by the employer for all employees not opting out.

Another outlined proposal without specifics would require wage reporting to the Social Security Administration more frequently than the current annual requirement. The intent is to improve tax administration and integrity of the overall tax system. A stated requirement would be to not increase the total tax burden to employers.

Other stated priorities would expand the Savers Credit to a fully refundable credit on the first $1,000 contributed to a retirement plan for families earning less than $65,000. There would also be an expansion of the E-Verify program to assure eligibility for employment.

These are only early proposals and may or may not move past the discussion stage, but provide some insight into items that may at least be considered in the future.

SUI

With the unemployment rate increasing in every state, many states are seeing dramatic decreases in their unemployment trust funds. Under the federal/state system, states not funded to meet their benefit requirements may borrow from the federal system to pay benefits.

If these loans remain unpaid by the end of the following year, the FUTA credits for those states are reduced, with the extra FUTA taxes applied to that state's federal loan balance.

At the least, states with outstanding loan balances will see employers pay more FUTA tax. However, some states may decide to increase taxable wage bases or to increase tax rates, also increasing taxes for employers. A few states could conceivably lower benefits, an outcome detrimental to employees in this economy.