

Payroll Trends

4th Quarter 2007

W-4/W-5

Employers are reminded that a new Form W-4 must be secured by February 15 each year for employees claiming exemption from federal tax withholding, or withholding must begin based on the single with zero exemption rates.

Employees eligible for advanced earned-income credits must also submit a new Form W-5 for 2008 to employers for eligibility.

Tax Gap

The top priority for legislators and the IRS is the Tax Gap, the difference between the amount of tax collected and what should be collected if all taxable income were properly reported.

One of the key areas of concern continues to revolve around the proper classification of employee/independent contractor, and the resulting proper reporting as W-2 or 1099-MISC income.

The use of another persons social security number is also bringing the identity theft problem to the work place and contributing to unreported income problems.

As the Tax Gap continues to widen, look for more pressure to require withholding on more types of payments and tightening of the definition of employee.

Vehicle FMV

Employers can use the standard mileage rate (page 1) to determine the taxable amount of an employee's personal use of company vehicles in 2008, only if the vehicle has a fair market value of \$15,000 or less. The amount for a van or truck is \$15,900. Fleet owners have special rules and should refer to the IRS web site.

New I-9 Dec. 26

Employers are reminded the revised Form I-9 must be used for verification of employment beginning December 26, 2007. Use of previous versions after this date may result in employer penalties according to the Department of Homeland Security.

401(k) Sample Notice

The IRS web site has a sample notice for plan sponsors to use to notify employees of the rules regarding automatic contributions to 401(k) plans. Use of the sample text will

satisfy the notice requirements of the Department of Labor. Final rules on automatic enrollment were published in October. More information is available under the index heading for Retirement Plans.

Free Resources

The IRS, Social Security and Labor Department all offer free, annually updated, publications to answer many employer questions. So take advantage of these resources, as it is one of the best values around.

Circular E, the Employer's Tax Guide, is mailed to every employer by early January each year. This book, IRS Publication 15, provides an overview of current tax-law changes, answers basic payroll questions, and provides payroll withholding tables.

The employer's Tax Calendar, IRS Publication 509, provides information on when federal tax deposits and various forms are due.

Another valuable resource is the Employer's Tax Guide to Fringe Benefits, IRS Publication 15-B, that provides basic answers to taxability of fringes, exclusion rules, valuation rules and withholding on fringe benefit amounts.

These publications and other valuable resources may be found at www.irs.gov/formspubs/index.html.

Daylight Saving Time

Daylight Saving Time (DST) will begin on Sunday, March 9, 2008. Employees working during the time change will have their payroll calculation impacted. Federal and state law, as well as labor agreements and company policy, will impact how the pay will be calculated.

Reimbursed Expenses

The IRS continues to find cash allowances to cover expenses not being treated as income to the recipient. Only reimbursed expenses where the the amount and business purpose are documented would avoid taxation for payroll purposes. Tool allowances, travel allowances and other such payments not requiring documentation as to amount and purpose, are merely additional compensation and not accountable plans under the tax code.

Baby Boomers

Beginning on January 1, 2008, the first baby boomers will become eligible for Social Security benefits. During the next 20 years, over 80 million Americans will become eligible, or over 10,000 per day. This influx of new recipients will put a long-term strain on the Social Security system and lead to more discussion on reform of the system.

Deferred Compensation

The IRS has issued a series of notices allowing employers until December 31, 2008, to bring their non-qualified deferred compensation (NQDC) documents into compliance with the final regulations under Code Sec. 409A.

Under the final rules, NQDC plan deferred amounts are included in current income for payroll tax purposes to the extent there is not a substantial risk of forfeiture, unless the plan meets the requirements specifically stated in Sec. 409A.

The notices extend the document compliance deadline, but does not extend the January 1, 2008, effective date for the final regulations. During 2008, employers must operate a NQDC plan in compliance with the final regulations, even if the plan documents have not yet been updated. This will be considered good faith by the IRS and avoid penalties. The complete regulations may be found at www.irs.gov and should be reviewed if you have any non-qualified deferred compensation.

Fringe Limits

Cost-of-living adjustments (COLA) for qualified plans and other benefits for 2008 have been released, with the more common items of interest to employers and employees summarized below.

As in prior years, these automatic changes require no amendment to plan documents. For additional information about your specific plans, contact your plan administrator. The full announcement for the various COLA changes can be obtained at www.irs.gov.

Pension Plans

- The maximum elective deferral for an employee under a 401(k), 403(b) or 457 plan remains \$15,500 in 2008.
- The maximum elective deferral under a SIMPLE account remains \$10,500 for 2008.
- The limit on total additions to a defined contribution plan in 2008 will increase to \$46,000, from \$45,000 in 2007.
- The maximum benefit payable under a defined benefit plan increases from \$180,000 to \$185,000 in 2008.
- The maximum compensation used to determine contributions for qualified plans increases to \$230,000.
- For 2008, the compensation used to define a key employee goes to \$150,000, while the amount to define a control employee remains at \$90,000. The highly-compensated employee limitation increases from \$100,000 to \$105,000.
- The minimum compensation amount requiring coverage under a SEP remains unchanged at \$500.
- The limit for additional elective deferrals for employees age 50 or over for 401(k), 403(b) and 457 plans remains unchanged at \$5,000 for 2008. For SIMPLE accounts, the amount also remains unchanged at \$2,500.

Mileage

The 2008 standard mileage rate used for employer reimbursement, employees not reimbursed for their expenses, and self-employed persons, will be 50.5 cents per mile for business miles driven. This is an increase from 48.5 cents per mile in 2007, and reflects the results of an independent study of the annual fixed and variable cost required to operate a vehicle.

The standard mileage rate can be used if the business purpose and mileage are properly documented. The standard rate cannot be used if the actual expenses are being reimbursed, the vehicle is being depreciated or is used for hire, or if more than four vehicles are being used at the same time. Amounts paid in excess of the standard are considered wages for payroll taxes.

For 2008, the mileage rate for medical and moving expense is 19 cents per mile, and for charity, it remains at 14 cents per mile.

Transportation Fringes

Amounts that may be excluded from gross income for employer-provided "qualified transportation" fringe benefits for 2008 increases to \$115 per month from \$110 in 2007. This limit applies to transit passes and commuter highway vehicles. Qualified parking benefits increase to \$220 from \$215 in 2007.

Medical Savings Accounts

To be eligible for a Medical Savings Account, an employee must be covered by a high-deductible health plan. For 2008, the annual deductible must be \$1,950-\$2,900 for individual coverage and \$3,850-\$5,800 for family coverage. Maximum out-of-pocket expenses cannot exceed \$3,850 for individual coverage or \$7,050 for family coverage.

Health Savings Accounts

For 2008, the annual limit for single coverage contributions is \$2,900 and \$5,800 for family coverage. A high deductible plan has an annual deductible between \$1,100-\$2,200 for single coverage and \$2,200-\$5,600 for family coverage.

Adoption Assistance

The maximum amount excludable from an employee's gross income for adoption assistance is \$11,650 in 2008. The income exclusion phases out for adjusted gross incomes between \$174,730 and \$214,730.

No Match Letters

In our last issue, we reported on the proposal by the Department of Homeland Security (DHS) to use the Social Security Administration (SSA) W-2 no-match letters as an immigration enforcement tool. It was also reported a California District Court had put the DHS initiative on hold. The Court has now granted an indefinite delay in both the mailing of the W-2 no-match letters and implementation of the DHS final regulations.

The SSA W-2 letters are designed to secure correct information when a social security number and name do not match, so wages can be properly credited.

The DHS final regulations, called "Safe Harbor Procedures," outlined steps an employer would be required to follow after receiving a no-match letter. Failure to follow these "rules" could result in employer penalties by the DHS for knowingly employing an illegal immigrant.

DHS told the Court they would address the issues raised, including not following the Regulatory Flexibility Act. This Act requires that no new burdens or cost be imposed on the employer.

DHS seems determined to try to move forward with this initiative, so look for more information as 2008 progresses.

Social Security Base

This first issue of 2008 highlights many changes to payroll related activities for the new year.

Changes include the standard social security wage base increases and cost-of-living adjustments (COLA) for fringe benefits, as well as new rules. As we go to print, legislation to approve the fiscal-year federal budget for 2007-2008 has not yet been passed, so be alert for late changes that might impact your employees' withholding or other functional items. As in prior years, employers continue to be responsible for implementing much of the revenue and social legislation at the federal, state, and local level.

Social Security Wage Base

The Social Security wage base for 2008 will increase by 4.6%, a \$4,500 increase from \$97,500 to \$102,000. The tax rate remains at 6.2% for the employer and employee, for a maximum tax of \$6,324 each. This increase is estimated to impact 12 million employees.

The separate Medicare tax remains at 1.45% each for the employer and employee, with no maximum wage base in 2008.

A self-employed person must pay 12.4% Social Security tax on the first \$102,000 of self-employment income, or \$12,648 in 2008. The 2.9% tax on self-employment income, with no maximum, will also continue for Medicare.

Social Security benefits will also increase by 2.3% in 2008. The maximum benefit will increase to \$2,185 per month, with the average benefit being \$1,079 per month.

Social Security recipients not yet reaching their full retirement age in 2008 will have benefits reduce \$1 for each \$2 of earnings over \$13,560 per year, or \$1,130 per month. As in prior years, after reaching full retirement age, benefit recipients can earn an unlimited amount without any benefit amount reduction.

SUI

Employers operating in at least 18 states will see their unemployment maximum wage base per employee increase for 2008, with only one state indicating a reduction in their base.

For 2008, all state unemployment programs have qualified for employers to take credit for timely paid state unemployment taxes against their federal unemployment tax liability when filing Form 940s.

In 2008, the FUTA wage base for calculation of federal unemployment tax remains unchanged at \$7,000 per employee.

The following table indicates the states with known 2008 increased maximum wage bases as we go to print.

AK	\$31,300
DE	\$10,500
IL	\$12,000
IA	\$22,800
MN	\$25,000
MO	\$12,000
MT	\$23,800
NV	\$25,400
NJ	\$27,700
NM	\$19,900
NC	\$18,600
ND	\$22,100
OK	\$13,600
OR	\$30,200
SD	\$ 9,000
UT	\$26,700
WA	\$34,000
WY	\$20,100

Hawaii has indicated their wage base will decrease to \$13,000 for 2008 through 2010.

Idaho and DC have not announced their 2008 wage base as we go to print. They could adjust their rates in early 2008, so if you have operations in these locations, look for possible announcements from their state agencies.

The remaining 30 states have indicated no change in their wage base for 2008.

State unemployment insurance (SUI) is one tax where employers can be proactive in helping to control the tax rates applied to the base, thus potentially reducing their total tax in this area. SUI benefits are not a guaranteed right and are payable to employees who lose their jobs through no fault of their own. Documenting personnel files for terminations, answering all notices timely, contesting benefit awards when terminations are for cause and making voluntary contributions in experience-rating states, can all contribute to lower rates over a period of time. Learn your states specific rules and procedures, and manage your SUI tax rates.