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2012 Key Employer Highlights

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2012KEY EMPLOYER HIGHLIGHTS FOR WASHINGTON BUSINESSES

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We prepared this guide to serve as a resource tool for common issues we often get questions about. We haven't covered everything. Please call us to discuss your unique business situation. A quick set up question can save hours later in the year.

SOCIAL SECURITY TAX RATES AND LIMITS

The maximum earnings subject to the OASDI employee and employer portion of FICA are \$110,100 for calendar year 2012. The Medicare portion has no limit.

The employee's portion of the old age, survivors, and disability insurance (OASDI) tax rate under the payroll tax cut is reduced by two percentage points to **4.2** percent for January and February 2012. Similarly, the OASDI portion of the self-employment tax is reduced by two percentage points to 10.4 percent for the first two months of 2012.

(UPDATE: the payroll tax cut was extended through the end of 2012 with a bill signed by the President on February 22, 2012.)

Employers must begin using the new withholding tables no later than January 31, 2012. In the event that the changes could not be made for the first payroll period in January the difference in employees withholding must be corrected no later than March 31, 2012.

Recapture. Under the terms negotiated by Congress, the law also includes a new "recapture" provision, which applies only to those employees who receive more than \$18,350 in wages during the two-month period (the Social Security wage base for 2012 is \$110,100, and \$18,350 represents two months of the full-year amount). *(UPDATE: the recapture provision was repealed with the extension of the payroll tax cut signed by the President on February 22, 2012.)*

The employee's portion of the old age, survivors, and disability insurance (OASDI) tax rate under the payroll tax is back to 7.65% on March 1st. Similarly, the OASDI portion of the self-employment tax will be 15.3%.

The IRS has released revised Federal Withholding Tables. <http://www.irs.gov/pub/irs-pdf/n1036.pdf> or check Circular E once revised.

Wages Subject To Tax		Tax Rate			Maximum Tax		
		Employee	Employer	Total	Employee	Employer	Total
FICA:	\$110,100	4.2 or 6.20%	6.20%		\$6,055.50	\$6,826.20	\$12,881.70
Medicare	All Wages	1.45%	1.45%	2.90%	No limit	No limit	No limit

Self employed- Since you are both the employer and the employee, your maximum tax for Social Security is \$12,881.70. There is no limit to the Medicare portion and the tax rate is 2.9%. See the Social Security Administration (SSA) web site www.ssa.gov for more information.

The 2012 Social Security cost of living increase is 3.6%. There was no 2011 Social Security increase.

CHANGE OF ADDRESS FORM 8822-B

Beginning in 2012, employers must use the new Form 8822-B, Change of Address-Business, for any address change.

FORM 940, FEDERAL UNEMPLOYMENT TAX (FUTA)

The FUTA tax rate remains unchanged at 6.0% for 2012. The FUTA rate was 6.2% from January 1, 2011 through June 30, 2011 (quarters 1 and 2) and decreased to 6.0% July 1, 2011 through December 31, 2011 (quarters 3 and 4). The maximum taxable earnings are \$7,000. If state unemployment is paid on all wages you may receive a credit reducing the maximum tax to \$42 per employee based on a net rate of .6% with maximum wages subject to the tax equal to \$7,000. If the state unemployment contribution is zero, the FUTA rate is 6.0% of the first \$7,000 of an

employee's wages or \$420. The Employer Identification Number (EIN) on your Washington Employment Security form must match the EIN on your 940 or the IRS will not give you the state credit. You are no longer required to list your state reporting number on Form 940.

Do not use any Employment Administrative fund payments to calculate your FUTA tax.

Employers are required to make a quarterly deposit for Federal Unemployment Taxes if the accumulated tax due exceeds \$500. If at the end of any calendar quarter, the accrued undeposited amount totals \$500 or more, the tax must be deposited before the end of the following month. Interest and penalty charges are assessed on late deposits at the same rate as Social Security/Medicare employment tax penalties. The annual return for 2011 (Form 940) is due by January 31, 2012.

If any wages subject to FUTA tax are not subject to state unemployment tax, you may be liable for FUTA at a higher rate (up to 6%). For instance, in Washington, wages paid to corporate officers can be exempt from state unemployment tax but not FUTA.

Example: Employee A and Employee B are corporate officers whose wages are excluded from state unemployment tax in your state. Employee C's wages are not excluded from state unemployment tax. During the first quarter, you paid \$11,000 to Employee A, \$2,000 to Employee B, and \$4,000 to Employee C.

\$9,000	Total FUTA wages for Employees A & B in 1st quarter (7,000 plus 2,000)
<u>x .06</u>	Tax rate
\$540.00	Your liability for the first quarter for Employees A & B

\$4,000	Total FUTA wages subject to state unemployment tax
<u>x .008</u>	Tax rate (based on maximum credit of 5.4%)
\$32.00	Your liability for the first quarter for Employee C

\$540	Your liability for the first quarter for Employees A & B
<u>+ 32</u>	Your liability for the first quarter for Employee C
\$572	Your liability for the first quarter for Employees A, B, & C

In this example, you must deposit \$572 by April 30 because your liability for the 1st quarter is greater than \$500. QuickBooks does not always calculate this correctly if there is more than one exempt officer.

FORM 941, EMPLOYERS QUARTERLY TAX REPORT

Form 941 is due quarterly. The IRS will continue to scrutinize 941s and compare them to W-2 data submitted to the SSA. Use your 941s as a double check for your W-2/W-3 reconciliation to avoid penalties.

Form 941-X is now used for all corrections.

FORM 943, EMPLOYERS ANNUAL FEDERAL TAX RETURN FOR AGRICULTURAL EMPLOYERS

Form 943 is due on January 31, 2012. If your software program does not support 943 reports, run the 941 report quarterly to double check that you are current. At least quarterly you should verify that all payroll deposits have cleared. If you are calculating your payroll manually, use a blank Schedule B and record your liability during the year using the date the paychecks are dated, not the date of the payroll deposit or the last day of the pay period.

FORM 945, ANNUAL RETURN OF WITHHELD FEDERAL INCOME TAX

This form is due January 31, 2012 for the year ended December 31, 2011. This form is used to report non-payroll tax liability, including backup withholding, income tax withheld from gambling winnings, pensions, annuities and IRAs. You cannot combine deposits for Form 941 and Form 945.

Generally, the deposit rules that apply to Form 941 also apply to Form 945. However, because Form 945 is an annual return, the rules for determining your deposit schedule are different from those for Form 941. See section 11 of Circular E for a detailed discussion of the deposit rules.

WASHINGTON STATE EMPLOYMENT SECURITY TAX (UNEMPLOYMENT) (SUTA)

*Employment Security Tax is based on an experience rating system with a taxable wage base of **\$38,200** for 2012. Your new rates should arrive in December. For 2012, the average UI tax rate is estimated to be 2.12% down from 3.26 percent in 2011. It ranges from a low of .143% to a high of 5.82% for qualified employers.*

If you are a new employer or haven't been in business long enough, you won't have enough "experience" to get your own tax rate. Instead, you will be assigned a rate based on your industry.

If you hire a nanny or someone to clean your house and pay them more than \$1,000 in gross wages during a calendar quarter, you must report to the Employment Security Department.

Delinquent employers will also receive a range of delinquent tax rates with an additional 2 percent delinquency tax. You must send all past-due taxes and/or late reports by September 30 to avoid a delinquent rate for the following year.

This tax is paid quarterly on a form provided by the Employment Security Department. Hours reportable are all hours paid including holidays, sick leave and vacation. The maximum hours reportable for salaried employees are 520 hours per quarter. The tax, however, is computed on the dollar amount of the wage paid.

*Corporate officers who provide services in Washington will be covered for unemployment insurance unless their employer specifically exempts them. Corporations that want their officers to be covered by unemployment insurance do not need to file for coverage, but must include the officers and their Washington wages in the unemployment insurance quarterly reports. State unemployment taxes on corporate officers must be paid each quarter, and they may be eligible for unemployment benefits if they lose their jobs. Check with Employment Security regarding your specific situation as a corporate officer who owns greater than 10% of the Company or if you are a family member of an owner. You may not be eligible for benefits. Corporations should not report individual corporate officers who have been approved for exemption. By law, corporate officers **need to be notified in writing** that they are ineligible for Unemployment Insurance coverage. The notice must contain the officers' names and signatures and must be kept on file for audit purposes. If you have questions regarding coverage of corporate officers, please check with our office. If your corporation requested exemption and you are unsure if the exemption was approved call 1(360)902-9360.*

If you don't have payroll during the quarter you can file your report by phone 1(888) 836-1900. <http://www.esd.wa.gov/uitax/taxreportsandrates/fileandpaytaxes/file-your-taxes.php> has different electronic filing systems based on your computer operating system. The electronic filing software remembers employees from quarter to quarter so only new employee information needs to be added. Electronic payment options are available and easy to use. It will calculate excess wages!

Use only the original paper form sent by Employment Security . Do not use old forms.

WORKERS' COMPENSATION PREMIUM (INDUSTRIAL INSURANCE, L&I)

There will be no overall increase in workers' compensation rates for 2012. Individual employers may see their rates go up or down, depending on their recent claims history and changes in the frequency and cost of claims in their industry. You will receive a notice from the Department of Labor and Industries indicating your composite rate for 2012. This composite rate also includes amounts for Medical Aid and Supplement Pension Assessment.

Employers may withhold one-half of the Medical Aid and Supplemental Pension Assessment from the employee.

For hourly employees, report the hours actually worked. Do not include vacation, holidays, or sick leave. For salaried employees, use either 40 hours per week or 160 hours per month. Sole proprietors, partners and their spouses are exempt from Industrial Insurance, but these persons may elect to be covered. Please note corporate officers will not be covered under Industrial Insurance unless they file an election to be covered. Corporate minutes must exist which discuss making the election to be covered and letters should be sent to each officer informing them of the election. You may be required to pay industrial insurance for independent contractors.

WARNING: *Partners, sole proprietors and corporate officers who are not covered by Industrial Insurance should check their group/individual medical insurance policy. Unless the policy has 24/7 coverage that includes "on the job" coverage they may be uninsured if injured at work.*

The Department of Labor and Industries website has a list of methods to reduce your L&I tax rate. Go to <http://www.lni.wa.gov/ClaimsIns/Insurance/default.asp> for questions or to sign up for electronic filing.

W-2 AND W-3s

For a terminated employee, your company must provide the W-2 by the final 941 due date. However, if the employee requests a W-2, you must supply it within 30 days of the request.

Starting in tax year 2011, the Affordable Care Act requires employers to report the value of the health insurance coverage they provide employees on each employee's annual Form W-2. However, to provide employers the time they need to make changes to their payroll systems or procedures in preparation for compliance with this requirement, the IRS will defer the reporting requirement for 2011, making that reporting by employers optional in 2011. This reporting is for informational purposes only, to show employees the value of their health care benefits so they can be more informed consumers. The amount reported does not affect tax liability, as the value of the employer contribution to health coverage continues to be excludible from an employee's taxable income. Code DD has been added to box 12 to report the cost.

File paper copies of Form W-3 with copy A of all of the W-2s by February 29, 2012, or file electronically by April 2nd to the Social Security Administration (SSA). W-2s should be mailed to recipients by January 31st. It is no longer necessary to use the red scannable forms for W-2s. Many software products will print acceptable forms on plain paper.

New this year is the requirement to fill in box b on Form W-3. If none of the other checkboxes apply check the None apply checkbox.



Wait to mail (or electronically file) the Federal copies until close to the due date. If you discover an error after the Form W-2 has been issued to the employee but before Copy A of Form W-2 and the accompanying Form W-3 are filed with the SSA, mark the "Void" box on the original Copy A. Then prepare a new Form W-2 for the employee, write the word "Corrected" on the copies given the employee and send Copy A of the new form to the SSA. (This new Copy A should not be marked "Corrected"). If a W-2 is corrected before the SSA receives their copy, it will not be necessary to prepare Form W-2c.

For information on electronically filing your employer information with the Social Security Administration, please go to <http://www.ssa.gov/employer/>.

W-4s

W-4 instructions state that withholding must be based on allowances you claimed and may not be a flat amount or percentage of wages. If the IRS suspects that an employee has not had the correct amount of FIT withheld, it can ask for a copy of the related W-4. If it determines that the employee claimed an incorrect number of allowances, it will send you a "lock-in letter" directing you to use x withholding allowances and may specify what marital status to use. Once you get the lock-in letter, the employee cannot submit another W-4 to have less withheld (but can request that more be withheld). The W-4 is available at www.irs.gov/pub/irs-pdf/fw4.pdf, and the worksheet is at www.irs.gov, type in "withholding calculator."

ELECTRONIC FEDERAL TAX PAYMENT SYSTEM (EFTPS)-REQUIRED

Use Form 9779 or go to www.eftps.gov to enroll. Businesses can schedule payments up to 120 days in advance and individuals can schedule payments up to 365 days in advance of their tax due dates. You can use the Electronic Federal Tax Payment System (EFTPS) to make all your federal tax payments including income, employment, estimated and excise taxes. Enrollment forms can also be obtained by calling 1(800) 555-4477. If your business is new, IRS will automatically pre-enroll you in EFTPS when you apply for an employer identification number (EIN).

Electronic deposits can be made by telephone 1(800)555-3453 or online.

All tax deposits must be made electronically, including under payments, estimated tax payments, 941/943/945 deposits, extension payments, and 940 deposits unless you are below the deposit requirement threshold.

There is a 10% penalty if you fail to use EFTPS.

Payments must be scheduled at least one business day by 8 p.m. ET in advance of their due date. You will be given an EFT acknowledgement number which will verify your timely initiation of the tax payment and thus avoid penalties.

941/943/945 DEPOSIT REQUIREMENT THRESHOLD OF \$2,500

If your net taxes for the quarter are less than \$2,500, you are not required to make deposits and may pay the taxes with Form 941. You may file Form 941 electronically. Form 943 payments may also be made with Form 943 if your net tax liability for the year is less than \$2,500. The rules are the same for Form 945. All forms must be filed timely for this rule to apply. Federal Tax Deposit Coupons Are Obsolete

Federal Tax Deposit Coupon Book, Form 8109-B, has been eliminated. **Shred them.**

\$100,000 NEXT-DAY DEPOSIT RULE

If you accumulate a tax liability of \$100,000 or more on any day during a deposit period, you must deposit the tax by the next banking day **no matter what type of schedule depositor you are.** If you are a monthly schedule depositor and accumulate a \$100,000 tax liability on any day during a month, you become a semiweekly schedule depositor on the next day and remain so for at least the rest of the calendar year and for the following calendar year. Please refer to Circular E for more details. A copy is available on the IRS website at www.irs.gov.



DEPOSIT PENALTIES-FEDERAL

The penalties for failure to make deposits of taxes are based on applicable percentages of the amount of underpayment determined by the number of days the deposit is late. If the failure is:

- Not more than 5 days late, the applicable percentage is 2% of the under-deposited taxes;
- More than 5 days but less than 15 days late, the applicable percentage is 5% of the under-deposited taxes; or
- If the failure is more than 15 days late, the penalty is 10% and
- the penalty becomes 15% if you fail to make the deposit on or before the earlier of
 1. 10 days after the first notice and demand to you for these amounts or
 2. the day on which notice and demand for immediate payment is given to you under a jeopardy assessment.

There is a 10% penalty for deposits paid directly to the IRS when subject to electronic deposit, or paid with the return unless the deposit shortfall rules apply. Publication 15, IRS Circular E, Employer's Tax Guide has more details about failure to deposit (FTD) penalties.

Deciding correctly which day is "payday" is important in determining the date when certain liabilities arise. Failure to correctly make this determination can be costly in penalties and interest. Employer liability normally arises at the time wages are paid to the employee, either actually or constructively. **The liability does not arise at the time the wages were earned.** For example:

A payroll is prepared for the pay period March 1-31. Payday is April 1st. The liability was incurred April 1st; it is a second quarter liability.

The income tax and the employees' share of FICA you withhold from your employees' paychecks are the part of their wages you pay to the United States Treasury instead of to your employees. The portion of their wages you hold is called "**Trust Fund**" taxes. There are extremely large penalties (up to 100%) for employers that delay in turning over employment taxes to the United States Treasury.

W-9

The IRS matches the Employer Identification Number (EIN) to the business name by computer. If you get a notice of back-up withholding from someone you do business with, check your original EIN application (SS-4) and provide the identical information on the W-9. The IRS cross matches by computer the first four letters on the SS-4 application to the number they assigned. If they do not match there is an automatic letter generated to the business entity that submitted the Form 1099 requiring back up withholding of 28%. A "doing business as" (d.b.a.) name cannot be used as the primary name. Sole proprietors should use their EIN and last name.

Individuals- the IRS uses the first 4 letters of the last name.

Trusts- the IRS uses the first 4 letters of the name of the trust unless the trust was established before 2006. Pre 2006 trusts use the first 4 letters of the last name of the grantor.

Partnerships- the IRS uses the first 4 letters of the trade or business name, if none, the first 4 letters of the last name of the first partner listed on the original SS-4.

All other organizations- the IRS uses the first 4 letters of the entity's name on the SS-4.

LETTER 147C

Some businesses receive requests from vendors for a Form 147C. The IRS has notified the vendors that they must use backup withholding unless a 147C is received. The 147C is actually a letter from the IRS verifying the EIN and name of your company. It is required when there is a matching problem between your W-9 and the IRS records. To get this letter you must call and request it from the IRS.

FORM 1099

The pilot program for truncating an individual's identifying number on paper payee statements has ended. Filers must show the recipient's complete identifying number on all copies of the form.

All Form 1099s must be mailed to recipients by January 31, 2012. Form 1096 with copy A of all forms 1099 must be mailed to the IRS by February 28th or electronically filed by April 2nd.

Each 1099 that is sent to a recipient must contain the payer phone number. The IRS assesses **\$50** fines to those who do not respond to requests for a phone number. The number must provide direct access to an individual (not the recipient) who can answer questions about the statement. Payers are permitted to include the telephone number in any conspicuous place on the statements. The number is not required on Copy A (IRS copy).

If more than one 1099 (for example, a 1099-Misc for rents and one for non employee compensation) is issued to an employer identification number or Social Security number, there must be a unique control/account number for each statement such as 001, 002 or A1, A2.

New Form 1099-K. Payments made with a credit card or payment card and certain other types of payment, including third party network transactions, must now be reported on Form 1099-K by the payment settlement entity under section 6050W and are not subject to reporting on Form 1099-MISC.

Form 1099-INT is filed for each person to whom payments of \$10 or more in interest were paid during the year.

Form 1099-DIV is filed for payments of gross dividends and other distributions of stock.

Form 1099-MISC is used to report aggregate payments of \$600 or more to persons not treated as employees for services performed for your trade or business (independent contractors). It is also used for rents and royalties. If you bartered your services you still report the business value received on form 1099-MISC (and the value you give is income on your business or personal tax return).

Form 1099-MISC should not be used to report employee payments or bonuses. Ordinarily, payments made to corporations are not reported on Form 1099-MISC, however, there are exceptions. Medical and health care payments, commercial fish purchases for cash, attorney's fees, and gross proceeds paid to an attorney are the most common exceptions.

The 1099 reporting exception for payments to a corporation does not apply to attorneys. Reporting is required for payments to an attorney or law firm including a corporation. All payments to attorneys are reported on Form 1099-MISC. If you made a payment to an attorney in the course of your business in connection with legal services, report the amount paid in box 7 if it exceeds \$600. If the attorney's fee cannot be determined, you must report the total fees and cost reimbursements paid to the attorney in Box 14 on Form 1099-MISC.



When an independent contractor performs services, have them fill out a W-9 for you **before** you pay them. This ensures you have an address and identification number available when you prepare the 1099 the following January. If someone refuses to provide you with their Taxpayer Identification Number (TIN), you are required by law to withhold 28% from payments made until you receive a TIN. Call 1(800) 772-6271 for TIN verification.

Some states also require reporting and sometimes require withholding. For instance if you are a Washington company and pay an independent contractor for work performed in California, you must report the amount paid to the Franchise Tax Board. If the independent contractor does not reside in California you will also be required to withhold on that payment. Call us before you do work outside of Washington so that all nexus issues are discussed proactively.

DIRECTOR'S FEES

Director's fees should be reported on Form 1099-Misc unless they are part of an employee's compensation. The amount reported should include all travel and reimbursed expenses. The total fees including the value of stock options are subject to B&O tax by the director. The corporation can elect to report them for the director using the corporate director fees B&O tax payment agreement found at <http://www.dor.wa.gov>.

WASHINGTON STATE MINIMUM WAGE

The Washington State minimum wage rate, effective January 1, 2012, is **\$9.04** per hour, an increase of 37¢ from 2011. The minimum wage applies to all workers in the state except workers under age 16 who may be paid \$7.68 (85% of minimum). The state recalculates the wage each September as required by an initiative passed by voters in 1998. The initiative requires the State to adjust the minimum wage based on the federal "CPI-W," which is a national index covering the cost of goods and services needed for day-to-day living. That index rose 4.258% during the 12 months ending August 31st. The Seattle-Tacoma CPI-W growth rate through October 2011 rose 3.8%.

Tips cannot be included to calculate the minimum wage. Overtime (1.5 times an employee's regular rate) need only be paid for all hours actually worked in excess of 40 in a week. Paid non-work hours (paid vacation, holidays, sick days, jury duty, etc.) do not count for overtime purposes. Bonuses are wages in the year paid and are subject to all Federal and State taxes except Labor & Industries (workers compensation). When an employee is terminated or quits the wages due may be paid at the end of the established pay period. This does not apply to union or other labor-management agreements that provide otherwise (RCW 49.48.010).

The Fair Labor Standards Act (FLSA) requires that most employees in the United States be paid at least the federal minimum wage for all hours worked and overtime pay at time and one-half the regular rate of pay for all hours worked over 40 hours in a work week.

The FLSA provides an exemption from both minimum wage and overtime pay for employees employed as bona fide executive, administrative, professional and outside sales employees and certain computer employees. To qualify for exemption, employees generally must meet certain tests regarding their job duties and be paid on a salary basis at not less than \$455 per week. Job titles do not determine exempt status. In order for an exemption to apply, an employee's specific job duties and salary must meet all the requirements of the U.S. Department of Labor's regulations. For details see <http://www.dol.gov/whd/regs/compliance/whdfs14.htm>.

BONUSES, CHRISTMAS GIFTS AND OTHER EMPLOYEE INCENTIVES

Wages subject to federal employment taxes generally include all pay that you give to an employee for services performed. The **pay may be in cash or in other forms**. Gifts in excess of \$25 (totalled for the year) are considered compensation and subject to payroll taxes. It includes salaries, vacation allowances, bonuses, commissions, and fringe benefits. It does not matter how you measure or make the payments. Amounts an employer pays as a bonus for signing or ratifying a contract in connection with the establishment of an employer-employee relationship and an amount paid to an employee for cancellation of an employment contract and relinquishment of contract rights are wages subject to Social Security, Medicare, Federal Unemployment taxes and income tax withholding.

THE WORK OPPORTUNITY TAX CREDIT (WOTC)

The program expired December 31, 2011 for all new hires except for unemployed veterans.

The work opportunity credit for hiring qualified veterans has been extended through December 31, 2012. The credit has been modified to allow a credit for hiring unemployed veterans, doubles the credit for hiring qualified veterans with service-connected disabilities who have been unemployed, and continues the credit for all veterans with a service-connected disability. In addition, a tax-exempt organization will also be allowed a tax credit against its' FICA tax obligations for hiring a qualified veteran.

An employer must obtain written certification from a state employment security agency on or before the day the individual begins work. Alternatively, as part of a written certification request, the employer may complete a prescreening notice on or before the day the employee is offered a job, and submit the notice to the designated local agency within 28 days after the employee commences work.

<http://www.wa.gov/esd/business-services/taxcredits.htm>

SHARED-WORK PROGRAM

The Shared-Work Program offers you an alternative to laying off workers. The program allows you to reduce the work hours of your full-time employees, while the workers collect partial unemployment benefits to replace a portion of their lost wages. The program helps you retain your skilled workers, reduce your payroll costs and avoid the expense of recruiting, hiring and training new employees when the economy improves.

Any company can participate if the company is registered in Washington for at least six months prior to applying for the program.

Your participating employees must:

- *Be full-time and hourly;*
- *Be eligible for regular unemployment benefits; and*
- *Be able and available to work all hours offered by the shared-work employer.*

The Shared-Work Program is not for slowdowns that are an expected part of an industry or business. The program cannot be used to support seasonal businesses during the off season or companies that traditionally use part-time employees.

You must reduce the weekly work hours of your participating employees by at least 10 percent, but not more than 50 percent. For example, the work schedule for a full-time employee who typically works 40 hours a week must be reduced by at least 4 hours, but not more than 20 hours.

A shared-work plan can last up to one year. If your request is for less than a year, it still counts as your one plan for the year. In most instances, it is best to open a plan for the full year so it will be available if you need it.

Similarly, employees can receive up to 52 weeks of shared-work benefits in each one-year plan as long as there is a balance available. The weeks do not need to be consecutive. Go to <http://www.esd.wa.gov/uibenefits/faq/shared-work.php> for details on all programs.

HEALTH CARE CREDIT

The small business health care tax credit helps small businesses and small tax-exempt organizations afford the cost of covering their employees. Your business may be eligible for the credit. The maximum credit is worth up to 35 percent of a small business' premium costs (25% for tax-exempt employers) for tax years 2010 to 2013. On Jan. 1, 2014, this rate increases to 50 percent (35 percent for tax-exempt employers). The credit phases out gradually for firms with average wages between \$25,000 and \$50,000 and for firms with the equivalent of between 10 and 25 full-time workers.

A qualifying employer must cover at least 50 percent of the cost of health care coverage for some of its workers based on the single rate and must have less than the equivalent of 25 full-time workers (for example, an employer with fewer than 50 half-time workers may be eligible). The average annual wages must be below \$50,000. A good calculator for determining whether your business qualifies is located at www.nfib.com/issues-elections/healthcare/credit-calculator.

Small employers, whether businesses or tax-exempt organizations, will use new Form 8941, Credit for Small Employer Health Insurance Premiums, to calculate the small business health care tax credit.

INDIAN EMPLOYMENT TAX CREDIT

A nonrefundable income tax credit is allowed for the first \$20,000 of qualified wages and health insurance costs paid or incurred for each qualified employee who works on an Indian reservation. The credit is equal to 20 percent of the employer's costs for a qualified employee's wages and health insurance paid or incurred during the tax year that exceed the amount the employer paid or incurred for such costs during 1993. Employees are qualified employees if they (or their spouses) are enrolled members of an Indian tribe, they perform substantially all of their services within an Indian reservation, and their principal place of abode while employed is on or near the reservation where they are working. Ineligible employees include those whose total wages exceed \$45,000 per year (as adjusted for inflation) during the tax year.

The Indian employment tax credit is extended for two years, through December 31, 2011. Employers should use Form 8845, Indian Employment Credit, to compute the credit. It is to be attached to the employer's income tax return.

TREATMENT OF MEDICAL INSURANCE PREMIUMS FOR S CORPORATION SHAREHOLDERS AND THEIR RELATED EMPLOYEES

*Medical insurance premiums paid for greater than 2% shareholders of S corporations are deductible by the corporation and are included in income on the W-2s of the greater than 2% shareholders. Covered family members who are also employees of the S corporation must also have premiums included in gross wages. The premiums are not subject to withholding for Social Security or Medicare tax if the premiums are paid under a health plan covering all employees. **100%** of the premiums may be deductible on Form 1040 as self-employed health insurance deductions if the family is not covered by another employer sponsored plan. In the case of an employee who is related to a more than 2% shareholder, a statement should be attached to the W-2 issued to the employee. The statement should explain the reason for the taxable income increase and notify the employee that he/she may be eligible for the self employed health insurance deduction for any month the family is not covered by another employer sponsored plan. This statement should also be attached to the employee's tax return. We can provide a sample statement.*

CAUTION: If the 2% shareholder medical insurance is not included on the W-2 the shareholder will not be allowed to deduct their medical insurance premiums on page one of their 1040 even if they otherwise qualify. Instead, the

insurance premium will only be deductible on schedule A, as an itemized deduction subject to the 7.5% of adjusted gross income limitation.

GARNISHMENT

Act on garnishment notices immediately. Garnishment is a court-ordered (or other legal or equitable procedure such as the Internal Revenue Service) process whereby a person's property is confiscated to pay a debt; in the case of wage garnishment, that property is one's paycheck. The federal government protects debtors and sets limits on the amount of wages that can be garnished from an individual. State governments have established and enforce their own separate debt collection laws, Washington state rules can be found on this website:

<http://www.dol.gov/compliance/guide/garnish.htm>

In the wage garnishment process, there are three parties: your employee (the debtor), the party that's owed money (the creditor) and you, the employer (the garnishee). As an employer, you're legally bound to comply with wage garnishment court orders. It's your responsibility to make the proper deductions from your employee's paycheck and send payments to the creditor. Common reasons for wage garnishment include:

- Alimony
- Child support
- Defaulted student loans
- Bad debts
- Bankruptcy
- Tax levies

It is illegal to fire an employee or to take any negative action against them because their wages are being garnished. However, if there are 2 or more separate garnishments during a calendar year the employee may be terminated.

If your employee quits, you are no longer required to make payments.

If an employee's wages are to be garnished, the creditor will notify you by sending you a Wage Garnishment package (SF-329). This package includes a letter to the employer (SF-329A), the wage garnishment order (SF-329B), a wage garnishment worksheet (SF-329C) and an employer certification form (SF-329D). Complete and return the employer certification form (SF-329D) within 20 days of receipt. If you don't, you may be subject to civil and criminal action. A copy of the wage garnishment package can be downloaded from [http://contacts.gsa.gov/webforms.nsf/0/9C03A2413FAAA05585256A3F0002E630/\\$file/SF%20329.pdf](http://contacts.gsa.gov/webforms.nsf/0/9C03A2413FAAA05585256A3F0002E630/$file/SF%20329.pdf).

Calculating the proper amount to garnish can be extremely complicated. Do it wrong and you could face legal repercussions. Even if you're within the legal limits, you can still draw heat from a creditor for garnishing too little or from your employee for garnishing too much. Payments are generally made each pay period.

In some cases, an employee's wages may be garnished by more than one creditor. For instance, you may be asked to garnish wages for child support and for a defaulted student loan. It's your responsibility to know which types of garnishments take priority.

Child Support Orders: in Washington, the employer can charge a fee to the employee for administrative costs of processing a court-ordered support withholding. For child support payments the fee is \$10 for the 1st remittance and \$1 thereafter per remittance. **Wage garnishment orders:** in Washington, the administrative fee for a commercial garnishment may be deducted from the payment to the creditor, or paid to the employer at the outset when the withholding order is served. In Washington, the reimbursement of employer administrative costs related to commercial garnishment orders is \$20 for the first answer and \$10 at the time the second answer is submitted. Employers can now make payments on the Internet by using Washington State's Child Support Internet Payment Service <https://fortress.wa.gov/dshs/csips/>.

When your employee's debt has been paid off, the creditor will notify you with a Notice of Termination of Wage Garnishment Order (SF-329E). Once you receive this form, you are to stop deducting withholdings from the employee's paycheck immediately. Download a copy of form SF-329E from the [U.S. General Services](#) Web site.

FAMILY EMPLOYEES

An important exemption from Social Security taxes applies to sons and daughters under 18 years of age employed by their parents in a trade or business. The trade or business must be a sole proprietorship or a partnership in which all partners are parents of the child. The child's wage must be reasonable and the hours and services carefully documented. Payments for the services of a child under age 18 who works for his or her parent in a trade or business are not subject to Social Security and Medicare taxes or FUTA. If these services are for work other than in a trade or business, such as domestic work in the parent's home, they are not subject to Social Security and Medicare taxes until the child reaches age 21. Payments for the services of a child under age 21 who works for his or her parent whether or not in a trade or business are not subject to FUTA tax. Although not subject to FUTA tax, a child may still be subject to income tax withholding.



Open a Roth-IRA in your child's name with the money saved on Social Security and Medicare taxes (up to a maximum of \$5,000 or their earnings, whichever is less).

CHARITABLE PAYROLL DEDUCTION RECORDKEEPING

To substantiate a deduction, a taxpayer must maintain a bank record or a written communication from the donee showing the name of the donee organization, the date of the contribution, and the amount of the contribution. For a charitable contribution made by payroll deduction, a pay stub, Form W-2, or other employer furnished document that sets forth the amount withheld for payment to a donee organization, along with a pledge card prepared by or at the direction of the donee organization, will be deemed to be a "written communication from the donee organization" that satisfies the requirements of Internal Revenue Code section (S) 170(f) (17). The substantiation record must be dated prior to the date the tax return is filed.

COMPANY REIMBURSEMENTS

There are strict requirements for non-taxable treatment of cash payments to employees. Some examples are substantiated employee reimbursements for meals and entertainment, travel expenses, automobile mileage and other necessary business expenses.

Payments made by an employer to an employee do not qualify as a working condition fringe benefit (non-taxable to the employee) unless the employer maintains an "accountable plan" that requires the employee to:

- Use the payment for expenses in connection with a specific activity for which a deduction is allowed as a business expense;
- Substantiate the expenditures that the payment was for; **and**
- Return to the employer any part of the payment not so used.

Failure by the employer or employee to meet these conditions will cause the payments to be taxable to the employee (and subject to withholding and employment taxes) and require the employee to deduct the "unreimbursed" business expenses as a miscellaneous itemized deduction on Schedule A of their 1040.

Auto allowances are considered wages if the employee is not required to substantiate the business mileage and return the unused portion. The allowances are subject to Federal income, Social Security, Medicare and FUTA taxes and are reported on the employee W-2 as well as Forms 941 and 940.

The per diem continental U.S. (CONUS) standard rate effective Oct 1, 2011 is \$111 for lodging and \$52 for meals and incidental expenses. See IRS publication 1542 for updated rates during the year. Other rates including foreign, Hawaii, Alaska, and high rate areas are available at <http://www.gsa.gov/perdiem>. Employer-provided cell phones can now be a tax free fringe benefit. If used primarily for non-compensatory business purposes the value of the cell phone is excludable from the employee's income. In addition, any personal use of the employer-provided cell phone, if issued primarily for non-compensatory reasons, will also be excludable from the employee's gross income as a de minimus fringe benefit. The IRS will no longer require recordkeeping of business use of an employer-provided cell phone in order to receive this tax-free treatment as long as the phone is issued and used primarily for business reasons.

The IRS will also take a similar administrative approach that applies with respect to arrangements common to small businesses that provide cash allowances and reimbursements for work-related use of personally-owned cell phones. Under this approach, employers that require employees, primarily for non-compensatory business reasons, to use their personal cell phones for business purposes may treat reimbursements of the employees' expenses for reasonable cell phone coverage as nontaxable. This treatment does not apply to reimbursements of unusual or excessive expenses or to reimbursements made as a substitute for a portion of the employee's regular wages.

Reasons for providing cell phones that do NOT qualify include, but are not limited to: promoting employee morale or goodwill; attracting a prospective employee; or giving additional compensation to an employee.

STANDARD MILEAGE RATE FOR 2011 AND 2012



Mileage	Jan 1- June 30 2011	July 1- Dec 31 2011	2012
Standard	51¢	55.5¢	55.5¢
Medical/Moving	19.3¢	23.5¢	23¢
Charitable	14¢	14¢	14¢

Taxpayers who use no more than four vehicles at the same time for business purposes may use the standard mileage rate.

A taxpayer may not use the standard mileage rate for a vehicle after using any depreciation method under the modified accelerated cost recovery system after claiming a Code Section 179 deduction for that vehicle, or for any vehicle used for hire.

RETIREMENT PLANS

	<i>Under Age 50</i>	<i>Over Age 50</i>
<i>Qualified retirement plan limits for 2012</i>		
<i>Pretax contributions for 401(k), SEP plans and 403(b) annuities</i>	<i>\$17,000</i>	<i>\$22,500</i>
<i>Combined employer/employee pay-in limits for all defined contribution plans</i>	<i>\$50,000</i>	<i>\$50,000</i>
<i>Annual defined benefit plan limitation</i>	<i>\$200,000</i>	<i>\$200,000</i>
<i>Maximum annual compensation limit for retirement plan computations</i>	<i>\$250,000</i>	<i>\$250,000</i>
<i>Minimum compensation limit for SEP participation</i>	<i>\$550</i>	<i>\$550</i>
<i>Highly compensated employee definition</i>	<i>\$115,000</i>	<i>\$115,000</i>
<i>SIMPLE pretax contribution limit</i>	<i>\$11,500</i>	<i>\$14,000</i>

Employee pretax contributions (elective deferrals) to a qualified plan, such as a 401(k), SEP, or SIMPLE plan, are exempt from Federal income tax but are subject to Social Security/Medicare and FUTA taxes and are reported on the Form 941, lines 6 and 7(not on line 2). In other words, taxable wages will be less than gross wages by the amount of the contribution.

All participant contributions should be deposited with the plan trustee as soon as they can be reasonably segregated from the employer's assets (generally within 3 business days from the date on which the contributions are withheld from payroll) and no later than the 15th day of the month immediately following the month in which the contributions are received or would otherwise be available to the employees in cash.

TRADITIONAL AND ROTH IRAS

IRA and Roth IRA contribution limits are the lesser of \$5,000 or earned income for 2012. For those over 50, there is a "catch-up provision" which allows the lesser of \$6,000 or earned income. 2012 IRAs can be funded no later than April 15th 2013. For 2011 contributions of the lesser of \$5,000 (6,000 for those over 50) or earned income can be made until April 17th, 2012.

SAVINGS INCENTIVE MATCH PLANS FOR EMPLOYEES (SIMPLE)

SIMPLE plans are available to employers with 100 or fewer employees. The IRA form of this plan allows the employer to adopt and maintain a plan with relative ease and few administrative costs. The employer is required to either match employee elective contributions on a dollar-for-dollar basis up to 3% of the employee's compensation or, in lieu of making a matching contribution, make a 2% of compensation non-elective contribution for each eligible employee regardless of whether the employee puts any of his/her own money in the plan. Employer-matching and non-elective contributions to a SIMPLE account are not subject to employment taxes. If you are self-employed and file a Schedule C, all matching and/or non-elective contributions that are made to your own personal SIMPLE plan account are subject to self-employment taxes. If you have a SIMPLE plan you are still eligible to contribute to a Roth or regular IRA provided you qualify with respect to the income limits (\$107,000 single filer, \$169,000 joint filer). SIMPLE matching contributions for 2011 must be funded by Jan 31, 2012.

Distributions from a SIMPLE plan generally are taxed under the rules applicable to traditional IRAs. Tax-free rollovers can be made from one SIMPLE account to another. A SIMPLE account can be rolled over to a traditional IRA on a tax-free basis after a two-year waiting period that starts the day the individual first became a participant in the SIMPLE plan. If an employee is no longer participating in a SIMPLE plan and two years have passed since the

employee first participated in the SIMPLE plan, the employee's SIMPLE account is treated as a traditional IRA. It can be rolled over to a Roth under the traditional IRA rules at this stage. Withdrawals of any kind within the first two years of participation are subject to federal income tax (FIT) plus a **25% penalty**. Early withdrawals from a SIMPLE account after the two years have passed are subject to the 10% early withdrawal penalty applicable to IRAs.

ONE PERSON 401(k) RETIREMENT PLAN FOR SELF-EMPLOYED

One-person 401(k) retirement plans are available to any business whose only full-time employees are its owners and their spouses. Corporations, partnerships, sole proprietorships, and not-for-profit organizations are all eligible. This plan allows the tax-deferral of a 401(k) with increased contribution limits. In 2012 the total contribution limit for a one-person 401k is \$50,000 or \$55,500 if age 50 or older. The annual one-person 401k contribution consists of 2 parts a salary deferral contribution and a profit sharing contribution. The total allowable contribution adds these 2 parts together to get to the maximum one-person 401k contribution limit. Business owners may contribute the greater of 25% of compensation or 100% of compensation up to \$17,000 (\$22,500 if age 50 and over). One-person 401k contributions are flexible. Both the salary deferral and the profit sharing contributions are discretionary and can be changed at anytime based on business profitability. The contribution limits can be doubled for husband and wife businesses. Businesses with a spouse on the payroll can also contribute to the one person 401k. There would be a single one person 401k for the business with two participants. Provided a business owner and spouse have sufficient income from the business, both may be able to contribute \$50,000 each or \$55,500 each if both are age 50+ in 2012. However, you may not contribute to a Simple IRA and establish a one person 401(k) within the same calendar year. A one person 401(k) must be set up no later than December 31, 2011 to be eligible for 2012 tax deductions.

A Form 5500 is required to be filed if the one person retirement plan assets exceed \$250,000. IRA, SEP, KEOGH, SIMPLE and 401(k) s are eligible for rollover into a one person 401(k).

Any Simple IRA contributions in 2012 will disallow the establishment of a one-person 401(k) until 2013.

CROSS TESTED OR MULTIPLE TIERED RETIREMENT PLANS

Another choice for businesses with employees is the cross tested retirement plan. This strategy most often advances the interests of professionals -- such as medical and law offices -- whose highly compensated employees may be older than its other employees.

Cross testing is nondiscrimination testing that determines if a profit sharing contribution, as valued at normal distribution age, is non discriminatory. It provides the highest allocation possible to the business owner and other highly compensated employees. Cross testing is used under two profit sharing allocation options: age weighted or new comparability formulas. The age weighted formula is based on employees' ages and salaries. The new comparability formula is based on separate employee categories determined by the business owner. Another term for this type of plan is multiple tiered.

WELFARE PLANS

There are many ways to provide employee medical, disability, life insurance and other benefits, including welfare benefit plans and cafeteria plans. While distinct from retirement plans, these plans are just as complex, and they come with their own sets of rules and regulations, as well as filing and testing requirements.

A welfare plan is the general name for most plans providing benefits other than retirement benefits or deferred compensation. Welfare plans, like qualified retirement plans, are governed by ERISA and may include health, dental

and vision coverage; life insurance; long- and short-term disability insurance; child care; transportation; and even legal benefits.

SECTION 125 FLEXIBLE SPENDING ACCOUNT (FSA)/CAFETERIA PLANS

A cafeteria plan is a written plan that allows participating employees to select qualifying benefits from a "menu" of choices the employer creates which can include dependent care, medical expense and the employee's share of medical insurance costs. The participant can direct a portion of their salary to the plan. The redirected salary is deposited to a trust account. When an expense is incurred for a qualifying benefit, the employee is reimbursed by the trust account. Reimbursements provide additional benefits to the employee, because they are free from Federal and state income tax, and payroll tax. With cafeteria plans, employees can use pre-tax dollars to pay for health insurance & dependent care. Both the employee and employer save on taxes: Federal income, Social Security/Medicare, and state income taxes (where applicable). The participant chooses the amount to be allotted to the Section 125 plan at the beginning of the year and cannot change the amount except under specific circumstances. Two and a half months after the end of the plan year any leftover employee dollars in the Section 125 plan account revert to the employer.

The tax savings make cafeteria plans very attractive. Inexpensive plan documents are available and the plans are relatively simple to administer. Flexible spending/Cafeteria plan benefits can help retain employees.

*Employees can use FSA balances that remain at the end of a plan year to pay for health care and dependent care expenses incurred during the first 2½ months of the following plan year **provided the Section 125 plan has been amended to allow it.***

Sole proprietors, LLC members, partners and 2% or greater shareholders in an S-corporation are not allowed to participate in a Section 125 plan.

Effective Jan. 1, 2011, the cost of an over-the-counter medicine or drug cannot be reimbursed from Flexible Spending Arrangements or health reimbursement arrangements unless a prescription is obtained. The change does not affect insulin, even if purchased without a prescription, or other health care expenses such as medical devices, eye glasses, contact lenses, co-pays and deductibles. See <http://www.irs.gov/publications/p969> IRS Publication 969, Health Savings Accounts and Other Tax-Favored Health Plans for more details.

HEALTH SAVINGS ACCOUNTS (HSAs)

A health savings account (HSA) is a tax-exempt trust or custodial account that an employee sets up with a qualified HSA trustee to pay or reimburse certain medical expenses they incur. They must be an eligible individual to qualify for an HSA. Contributions to the HSA made by the employer(including contributions made through a cafeteria plan) may be excluded from the employee's gross income.

An employee must be covered under a high deductible health plan (HDHP) and cannot have any other health coverage (with certain exceptions). They cannot be enrolled in Medicare or claimed as a dependent on someone else's tax return.

No permission or authorization from the IRS is necessary to establish an HSA. When an employee sets up an HSA, they will need to work with a trustee. A qualified HSA trustee can be a bank, an insurance company, or anyone already approved by the IRS to be a trustee of individual retirement arrangements (IRAs) or Archer MSAs. The HSA can be established through a trustee that is different from their health plan provider. See <http://www.irs.gov/publications/p969> IRS Publication 969, Health Savings Accounts and Other Tax-Favored Health Plans for more details.

HEALTH REIMBURSEMENT ARRANGEMENTS (HRAs)

A health reimbursement arrangement (HRA) must be funded solely by an employer. The contribution cannot be paid through a voluntary salary reduction agreement on the part of an employee. Employees are reimbursed tax free for qualified medical expenses up to a maximum dollar amount for a coverage period. An HRA may be offered with other health plans, including FSAs.

If any distribution is, or can be, made for other than the reimbursement of qualified medical expenses, any distribution (including reimbursement of qualified medical expenses) made in the current tax year is included in gross income. For example, if an unused reimbursement is payable to you in cash at the end of the year, or upon termination of your employment, any distribution from the HRA is included in your income. This also applies if any unused amount upon your death is payable in cash to your beneficiary or estate, or if the HRA provides an option for you to transfer any unused reimbursement at the end of the year to a retirement plan. See <http://www.irs.gov/publications/p969> IRS Publication 969, Health Savings Accounts and Other Tax-Favored Health Plans for more details.

FORM 5500 ANNUAL RETURN/REPORT OF EMPLOYEE BENEFIT PLAN

If you are a plan administrator for a retirement plan (Profit Sharing or Money Purchase Plan or Self-Employed 401(k)), defined benefit plan, corporate pension and profit sharing plan, certain 403(b) plans or a 401(k) plan, generally you must file a Form 5500 each year. A one person 401(k) may need to file a Form 5500 if total assets are over \$250,000 in 2011. Under ERISA, welfare plans must file Form 5500 unless they have fewer than 100 participants and the plan is unfunded (benefits are paid as needed solely from the employer's general assets), fully insured or a combination of the two. The number of participants is the number in the plan, not the number eligible, as of the beginning of the plan year. General assets include the account the employer uses for day-to-day business transactions or its corporate bank account. See www.dol.gov/ebsa for more information on Form 5500 filing requirements.

NEW HIRE

Federal law requires that all employers verify the identity and employment eligibility of all new employees (including U.S. citizens) within three days of hire.

Employees are required to complete the Form I-9 and employees must provide employers with documentation establishing both identity and eligibility to work in the United States.

All new employees are required to fill out a W-4 and an I-9 that must be verified and completed by the employer. The requirement applies to all employers including household employers and not-for-profit organizations regardless of the number of employees. There are new I-9 forms <http://www.uscis.gov/files/form/i-9.pdf> and the required 2 pieces of identification has changed. It is important to physically check the documentation as the penalties for non-compliance include civil monetary fines as well as more serious criminal penalties. Social Security numbers of new employees can be verified online. Go to www.socialsecurity.gov/bsowelcome.htm to register. Another method of verification is through the E-Verify process.

*Federal law requires employers to submit to their state agency (ours is Washington Division of Child Support) six data elements for each newly hired employee. The purpose of the law and the program is to help locate parents who are not paying child support. The law also allows other state agencies like the Department of Labor and Industries and the Employment Security Department to use new hire information to detect claim fraud. Report all new hires and rehires to the Division of Child Support (DCS) within **20 days** after employment begins. A rehire is an employee who returns to work after a 30 day period regardless of the reason for non-work. Failure to report could result in a penalty.*

Employers may submit reports in a variety of ways. If faxing or mailing W-4s, copy them and then fill in the employer information in boxes 8-10 and add the employee birth date to box 1 of the form after the last name.

Mail: New Hire Program
P.O. Box 9162
Olympia, WA 98507-9162

Fax: 1 (800)782-0624

Phone 1 (800)562-0479 (up to four new hires) select option 3

Internet: <http://www.dshs.wa.gov/newhire> (only one new hire at a time).

E-VERIFY

The Department of Homeland Security (DHS) and the Social Security Administration (SSA) have established an electronic system called E-Verify to assist employers in verifying the employment eligibility of all newly-hired employees. In short, through E-Verify, employers send information from Form I-9 to SSA and DHS to ensure that the new hire is authorized to work in the United States and that the name, Social Security number, date of birth, citizenship status, and any other non-citizen information provided on the Form I-9 matches government records.

You can register for E-Verify at <https://e-verify.uscis.gov/enroll>, which provides instructions for completing the registration process. At the end of the registration process, you will be required to sign a Memorandum of Understanding (MOU) that provides the terms of agreement between you the employer, the SSA, and U.S. Citizenship and Immigration Services (USCIS). An employee who has signatory authority for the employer can sign the MOU.

- Employers must post a notice informing employees of their use of E-Verify.
- E-Verify must be used for new hires only. It cannot be used to verify the employment eligibility of current employees.
- E-Verify must be used for all new hires regardless of national origin or citizenship status. It may not be used selectively.
- E-Verify must be used only after hire and after completion of the Form I-9.
- Employers may not pre-screen applicants through E-Verify.
- If an employee receives an information mismatch from their Form I-9 and SSA and DHS databases, the employer must promptly provide the employee with information about how to challenge the information mismatch, including a written notice generated by E-Verify.
- If an employee decides to challenge the information mismatch, the employer must provide the person with a referral letter issued by E-Verify that contains specific instructions and contact information.
- Employers may not take any adverse action against an employee because he/she contests the information mismatch. This includes firing, suspending, withholding pay or training, or otherwise infringing upon his/her employment.
- The employee must be given eight federal government work days to contact the appropriate federal agency to contest the information mismatch.
- If an employee receives a SSA tentative non-confirmation (TNC), they have the option of visiting an SSA field office to update their record or if the employee is a naturalized citizen, the employee may choose to call USCIS directly to resolve the TNC. The phone number can be found on the SSA referral letter.

WHO IS AN EMPLOYEE?

Did you know that when you hire an individual to work or perform a job for you, no matter how small the job is, you need to [report](#) that individual to the Employment Security Department (ESD)? There is no minimum dollar/hour threshold that needs to be met before an individual is considered reportable as an employee.

Often businesses consider individuals who perform incidental work, or a one-time job, as casual labor or temporary help, and do not report these individuals to ESD as employees. Unemployment insurance tax is due from the first dollar that is paid to an individual who is working for and being compensated by you. Even if you have someone come and perform a job that takes one or two hours, you need to report that individual as an employee and pay the required quarterly unemployment insurance taxes on their gross wages.

There are also three new IRS programs focusing on Independent Contractors (ICs). The programs attempt to stop misclassification of employees as ICs, which currently costs the government \$2.72 billion in unpaid federal taxes, plus unpaid state workers' comp and UI.

The Worker Reclassification Settlement Program is a voluntary program which allows a participating employer that has misclassified workers as ICs to avoid problems with the IRS by agreeing to treat the workers as employees in the future. The employer pays 10% of the employment tax liability it would have paid for the last tax year had the workers been correctly classified as employees.

IRS-DOL joint program. The IRS and Department of Labor (DOL) have an agreement to share data related to worker misclassification and other payroll tax enforcement.

Federal-state programs. The IRS and DOL have agreements to share data on worker misclassification with more than 30 states.

To assist you in reporting these workers, make sure you always get an individual's Social Security number and name, so you can accurately reflect their gross earnings on the unemployment insurance quarterly tax report. Keep track of the hours worked and the gross payment made to them during the quarter, so you are ready to complete your quarterly ESD tax and wage report when due.

*The Washington State Employment Security Department has issued the following guidelines on the classification of workers hired as independent contractors or employees. It will not be considered employment if the following tests are met. **It is important to keep a record of the individual's verification of independence (i.e., UBI number).***

INDEPENDENT CONTRACTOR'S TEST

One of the most common mistakes businesses make when filing their unemployment insurance tax reports each quarter is misclassifying their employees as independent contractors. When the Employment Security Department discovers these errors, the business must pay back taxes for all misclassified workers, plus penalties and interest.

Use the following two tests to help you determine a worker's status. There is one test specifically for electrical and construction contractors and one for all other industries. If a worker passes one of the following tests, he or she is an independent contractor. If not, he or she is an employee and should be reported on your quarterly unemployment tax report. If you are unsure whether a worker qualifies as an employee, contact your district tax office.

Electrical and Construction Contractors in Washington

*Service performed for compensation by an individual in the electrical or construction industries is employment **unless** it is shown that:*

1. *The individual is free from direction and control over the performance of the service; **and***
2. *The service is either performed:*
 - Outside of the usual course of business for which the service is performed, **or***
 - Outside of all the places of business of the enterprise for which the service is performed; **or***
 - The individual has a principal place of business and is responsible for the costs; **and***
3. *The individual:*
 - Is customarily engaged in an independently established trade, occupation, profession or business of the same nature as that involved in the service contract, **or***
 - Has a principal place of business that is eligible for a federal income tax business deduction; **and***
4. *On the effective date of the contract of service, the individual is responsible for filing a schedule of expenses with the Internal Revenue Service; **and***
5. *On the effective date of the contract or within a reasonable period after the effective date of the contract, the individual has an:*
 - Active account with the Department of Revenue,*
 - Active account with any other state agencies, **and***
 - A Unified Business Identifier (UBI) number; **and***
6. *On the effective date of contract of service, the individual is maintaining a separate set of books or records that reflect all items of income and expenses of the business that the individual is conducting; **and***
7. *On the effective date of the contract, the individual has a valid contractor registration under RCW 18.27 or an electrical contractor license under RCW 19.28 if the work requires a registration or license.*

All Other Industries in Washington

*Service performed by an individual for compensation is employment **unless it is shown that:***

1. *The individual is free from direction and control over the performance of the service; **and***
2. *The service is either performed:*
 - Outside of the usual course of business for which the service is performed, **or***
 - Outside of all the places of business of the enterprise for which the service is performed; **and***
3. *The individual is customarily engaged in an independently established trade, occupation, profession or business of the same nature as that involved in service contract.*

*Or, as a separate alternative, service performed by an individual for compensation is employment **unless it is shown that:***

1. *The individual is free from direction and control over the performance of the service; **and***
2. *The service is either performed:*
 - Outside the usual course of business for which the service is performed, **or***
 - Outside of all places of business of the enterprise for which the service is performed, **or***
 - The individual has a principal place of business and is responsible for the costs; **and***
3. *The individual:*
 - Is customarily engaged in an independently established trade, occupation, profession, or business of the same nature as that involved in the service contract, **or***
 - Has a principal place of business that is eligible for a federal income tax business deduction; **and***
4. *On the effective date of the contract of service, the individual is responsible for filing a schedule of expenses with the Internal Revenue Service; **and***
5. *On the effective date of the contract or within a reasonable period after the effective date of the contract, the individual has an:*

- Active account with the Department of Revenue,
- Active account with any other state agencies, **and**
- A Unified Business Identifier (UBI) number; **and**

6. On the effective date of contract of service, the individual is maintaining a separate set of books or records that reflect all items of income and expenses of the business that the individual is conducting.

If you are unsure whether a worker qualifies as an independent contractor, contact your district tax office.

NOTE: According to the **IRS** a worker's status under the common law test is determined by applying 20 relevant facts that fall into the three main categories below. All facts must be considered. No single fact provides the answer.

Behavioral controls: A worker is an employee when the business has the right to direct and control the worker even if it does not actually exercise that right.

Financial controls: A worker who has the opportunity for profit or loss; or unreimbursed expenses; or a significant investment in the work may be an independent contractor.

Relationship of the parties: A written contract may show the relationship between the worker and the business.

Receiving benefits indicates the worker is an employee.

OUTSTANDING PAYROLL CHECKS AND OTHER UNCLAIMED PROPERTY

Outstanding payroll and other checks which have not been claimed or cashed are required to be turned over to the Unclaimed Property Division of the Department of Revenue. Outstanding checks through June 30, 2011 must be reported by November 1, 2012. Credits or outstanding checks should be reclassified to a liability account (call it unclaimed property). See <http://ucp.dor.wa.gov/>

WASHINGTON STATE SALES AND USE TAXES

The city of Bellingham's combined state and local tax is **.087** (8.7%) effective April 1, 2011. Whatcom County's combined state and local tax is **.085** (8.5%) effective January 1, 2010.

Sales and/or use tax must be paid when you are the end user of a product no matter where or how it was purchased. The Department of Revenue has been aggressively enforcing use tax. Use tax must be paid on all purchases (including freight and shipping) by catalog, telephone or internet when you are not charged sales tax. You must remit use tax with your excise tax return. The Department of Revenue has been sending out notices if you do not declare use tax on your excise tax return. The notice provides an estimate of your industry's average use tax which looks like an assessment. Verify your records and submit your actual use tax.

Retailers must collect local sales tax based on the destination of the shipment or delivery – "destination-based sales tax." This only affects shipments and deliveries to locations within Washington State. Please see the Department of Revenue website <http://www.dor.wa.gov/> for more information including a nice tax rate lookup tool and calculator.

For monthly filers the due date of the return is the 25th of the following month. All monthly and quarterly filers **must file and pay** their excise taxes electronically. Annual returns are due January 31st.

GIFT CERTIFICATES AND LAYAWAY TREATMENTS

In Washington State, purchased gift certificates/cards may not have an expiration date; assess a dormancy or inactivity charge; or include a service fee RCW 63.29.020. Gift certificates donated to charities may include an expiration date.

Taxes are due when the gift certificate is redeemed by the holder. When the certificate is used, the taxes due on the sale depend on the nature of the item or service purchased.

When a customer purchases tangible personal property, sales tax is collected and the seller reports retailing B&O tax and retail sales tax at that time. For purchases of sales tax exempt food products, only retailing B&O tax is due. The seller should report the income for sales tax, and then take an "exempt food products" deduction. No sales tax is due. If the certificate is used to purchase a service (a haircut, for example), the seller reports the transaction under the service B&O tax classification. No sales tax is due.

When an item is purchased on layaway, the seller does not enter the transaction as a sale until the customer takes delivery of the item. Upon delivery, the business will collect and report retail sales tax and retailing B&O tax. If the customer does not complete the terms of the layaway and forfeits the deposit, the seller will report this income under the service B&O tax classification, because there is no retail sale to charge sales tax.

PERSONAL PROPERTY TAX ON BUSINESS PROPERTY

You must report your business property, furniture, equipment, supplies, etc. to the assessor of the county in which your business is located. The report is due April 30th. For Whatcom County see <http://www.co.whatcom.wa.us>. Please give us a copy of your completed report so we can match it to your tax depreciation schedule.

BUSINESS LICENSES AND TAXES

Businesses in Washington State pay state Business & Occupation tax. The Department of Revenue will review your business activities for you and verify whether you have been reporting them correctly if you go into their office. See <http://www.dor.wa.gov> for more information. Also check to see if your business and/or the city you do business in requires a license. Some cities, including Bellingham <http://www.cob.org>, also have a business tax. Go to <http://bls.dor.wa.gov/citycounty.aspx> for exact licensing information for your company and the locations where it does business.

ACCIDENT PREVENTION PROGRAM

Every employer in the State of Washington, regardless of the number of employees, is required to have a safety and health committee plan. Additionally, Washington Industrial Safety and Health Act (WISHA) rules require each employer to establish an accident prevention program outlined in a written format.

You may contact our office if you need information on implementing this program or visit <http://www.lni.wa.gov/safety/basics/programs/accident/default.htm> for more information. The website has sample programs which can be downloaded.

BONUS DEPRECIATION AND SEC 179 CHANGES

Call us in advance to discuss your purchases, especially vehicles.

The 50% additional depreciation allowance (bonus depreciation) was extended for two years to apply to qualifying property acquired after December 31, 2007, and placed in service before January 1, 2013 (or pursuant to a written binding contract entered into after December 31, 2007, and before January 1, 2013). The bonus depreciation allowance rate was increased from 50 percent to 100 percent for qualified property acquired after September 8, 2010, and before January 1, 2012, and placed in service before January 1, 2012. A taxpayer may make an election out of bonus depreciation.

There are still depreciation caps on vehicles which can limit allowable depreciation. The election out of bonus depreciation is not made for individual assets. It is made on a property class basis. Automobiles are five-year property. Accordingly, a taxpayer would need to make an election out of bonus depreciation for all five-year property placed in service during the tax year in order to avoid any adverse consequence of claiming bonus depreciation on a vehicle. The election applies to all property in the property class that is placed in service in the tax year of the election.

Qualifying property is NEW, not used. property which qualifies for MACRS depreciation. It must have a recovery period of 20 years or less. Computer software and qualified leasehold improvement property may also qualify. Depreciation rules for qualified leasehold improvement property, qualified restaurant property, and qualified retail improvement property were extended for two years to apply to property placed in service on or before December 31, 2011. They do not qualify in 2012.

The Code Sec. 179 dollar limit for tax years beginning in 2012 is \$125,000. The investment limit for 2012 is \$500,000. The rule allowing off-the-shelf computer software to be expensed is extended for one year to apply to software placed in service in tax years beginning after 2002 and before 2013. The rule allowing taxpayers to make, change, or revoke a Code Sec. 179 election on a timely-filed amended return is extended for one year to apply to elections for tax years beginning after 2002 and before 2013.

We have tried to make this employer guide as complete and accurate as possible. Laws change, however, and we ask that you consult the applicable government websites or publications for the most recent regulations. Please call us if we can be of assistance. If you would like us to communicate with the IRS or a state agency regarding any employment or tax issues, we will need to file a limited power of attorney for tax purposes (IRS Form 2848).

A copy of this guide is on our website: www.metcalfhodges.com select the tab Resources and then this year's guide.

DISCLAIMER

Notice regarding reliance on tax advice in conformance with IRS Circular 230:

You may not rely on this communication to avoid penalties that may be imposed under the Internal Revenue Code unless you have engaged us to provide written tax advice in a form that satisfies IRS standards for "covered opinions". We make this disclaimer to avoid potential penalties that the IRS might assess against us for issuing an opinion that does not meet strict IRS standards of presentation. IRS covered opinion standards result in significantly increased cost.

