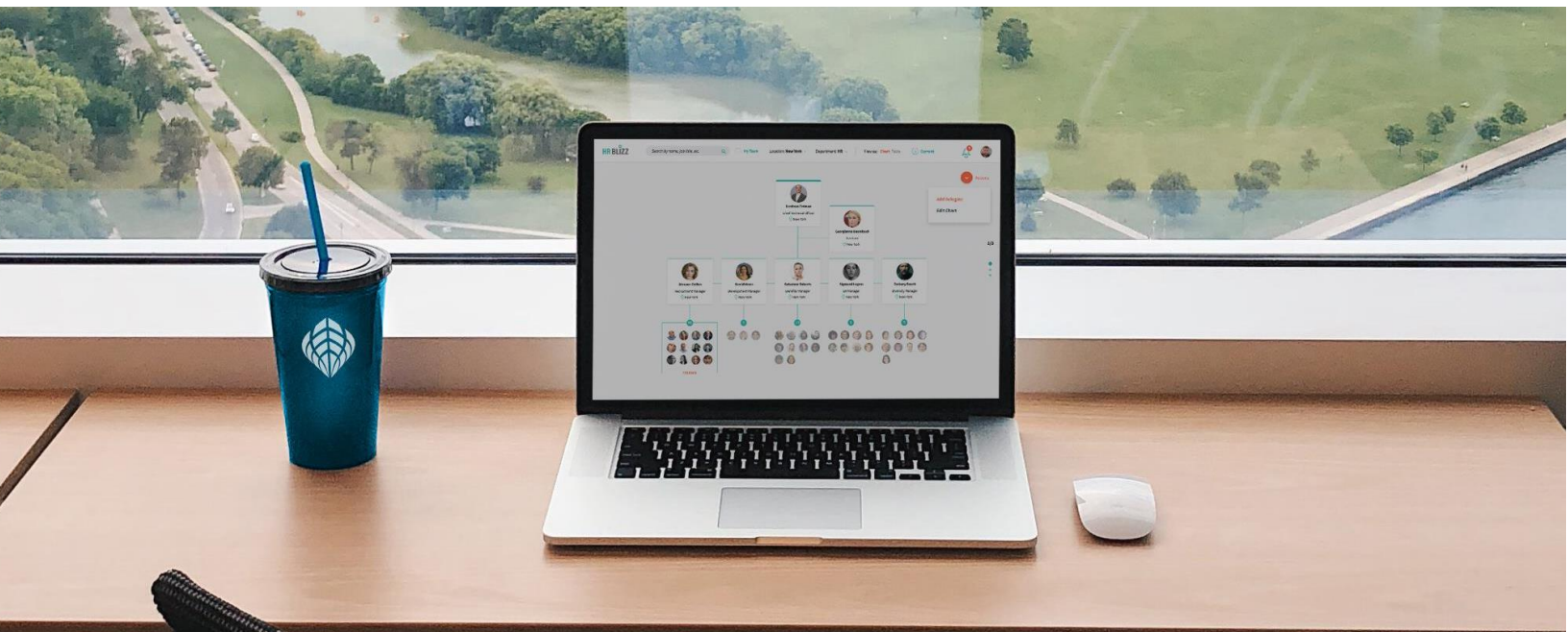




Simplifying Employment  
Tasks Worldwide

# Payroll & Tax Highlights

2021 Global Payroll Country Guide for United States of  
America



## UNITED STATES OF AMERICA



22 March 2021

# We help you achieve your global ambitions

Thank you for trusting Mercans to outsource your HR and Payroll functions. We propose HR consulting services, actionable solutions, and cost-effective global payroll processing tools to energize your human capital management in real-time and augment your performance. We are dedicated to becoming your business growth facilitator.



## **Global Payroll Solutions – Boost your HR brand and employee satisfaction**

Rationalize your HR budgets, monitor your data, and optimize your global payroll tasks in real-time. Systematize processes and streamline HRM lifecycles with HR Blizz™, our unified SaaS platform, to ensure your employees are paid accurately and on time.



## **PEO/GEO Services – Easily hire, deploy and manage your workforce abroad**

A reliable Professional Employer Organization (PEO), Mercans is your trusted employer of record to globally select, engage, and manage highly-qualified personnel on your behalf, through integrated Global Employment Outsourcing (GEO).



## **Global Talent Acquisition – Quickly fill vacancies with only the best candidates**

Mercans supports you in designing/deploying long-term HR strategies and processing full-cycle recruitment. Our ATS Suite Mesaar™ and our hiring experts help to screen, select, attract the right candidates for your organization, and populate your pipeline of prequalified talents.



## **BPO Services – Reclaim the focus on your core activities to expand your business**

Concentrate on the essentials: outsource non-primary activities and your front- and back-office functions to Mercans. Save the time, money, and energy needed to refine the value chain engagement of your customers and suppliers, and increase revenue.



## **HR Management SaaS – Access customizable cloud-based online platforms**

Centralize your HR function on an all-in-one user-friendly and self-service platform. Combined with the expertise of our consultants, the Mesaar SaaS offers a built-in applicant tracking system and easy-integration features to improve internal processes.



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### **Local Statutory Compliance – Forget the hassle of setting up branches abroad**

Mercans seasoned HR advisory team are compliance experts specialized in local cultures, business protocols, and tax and legal specificities. They are committed to ensure quick go-to-market abroad and achieve a compliant global expansion, risk-free from A to Z.

## Mercans at a Glance

|                                       |                                     |                                      |
|---------------------------------------|-------------------------------------|--------------------------------------|
| <b>160+</b><br>Countries              | <b>20</b><br>Years of Success       | <b>750+</b><br>Specialists           |
| <b>5k+</b><br>Customers Worldwide     | <b>97%</b><br>Client Retention Rate | <b>1.5X</b><br>Annual Revenue Growth |
| <b>25k+</b><br>Largest Single Payroll | <b>7.5M+</b><br>Pay Slips per Annum | <b>0</b><br>Security Breaches        |

**Number one** for outsourced payroll services, we are endorsed by international authorities.



Mercans has the highest industry quality and IT security certifications.





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## USA – Economic Superpower

The economy of the United States is that of a highly developed country with a mixed economy. It is the world's largest economy by nominal GDP and net wealth and the second largest by purchasing power parity (PPP). It has the world's fifth-highest per capita GDP (nominal) and the seventh-highest per capita GDP (PPP) in 2020. The United States has the most technologically powerful economy in the world and its firms are at or near the forefront in technological advances, especially in computers, pharmaceuticals, and medical, aerospace, and military equipment. The largest U.S. trading partners are China, Canada, Mexico, Japan, Germany, South Korea, United Kingdom, France, India, and Taiwan. The U.S. is the world's largest importer and the second-largest exporter. It has free trade agreements with several nations, including the USMCA, Australia, South Korea, Israel, and few others that are in effect or under negotiation.

The nation's economy is fueled by abundant natural resources, a well-developed infrastructure, and high productivity.

The U.S. not only has the largest internal market for goods, but also dominates the services trade. U.S. total trade amounted to \$4.2 trillion in 2018. Of the world's 500 largest companies, 121 are headquartered in the U.S. The U.S. has the world's highest number of billionaires with total wealth of \$3.0 trillion. US commercial banks had \$20 trillion in assets as of August 2020. US Global assets under management had more than \$30 trillion in assets.

The continued uncertainty in the international economy and globally weak investment due to COVID-19 has depressed the exports and investments of US companies. In 2020, export growth will be sluggish and there will be little in the way of investment.

The Bureau of Labor Statistics (BLS) expects total employment to increase by 6 million jobs between 2019 and 2029.

Computer and math occupations, and those based on alternative energy production, will also grow rapidly. On the other hand, manufacturing and retail industries will continue shedding jobs, while e-commerce continues to grow. That same shift could increase jobs in transportation and warehousing. Other declines will occur in the postal service, agriculture, and some information-related industries. In the years covered by the forecast, USA's export demand will begin to strengthen, but actual exports from USA, which are strongly weighted towards capital goods and intermediate goods, will join in the positive developments only towards the end 2022.

Mercans and its affiliates do not provide tax, legal or accounting advice. This material has been prepared for informational purposes only, and is not intended to provide, and should not be relied on for, tax, legal or accounting advice. You should consult your own tax, legal and accounting advisors before engaging in any transaction.







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## Doing Business in USA

Starting a U.S.-based business as a foreigner can be a long road, but the country makes it easy to register your company and open your business. Learning English is a basic requirement if you plan on doing business with Americans, but other aspects such as filing for your Employer Identification Number and choosing which type of company you want to be, can make matters more confusing.

### Basic Facts

|  |  |
|--|--|
|  |  |
| <b>Official State Name</b>                   | United States of America   |
| <b>Population</b>                            | 332.3 million  |
| <b>Capital</b>                               | Washington, D.C.   |
| <b>Major Languages</b>                       | English, Spanish   |
| <b>Currency</b>                              | U.S. dollar  |
| <b>Main Industries &amp; Export Articles</b> | Petroleum, natural gas, steel, motor vehicles, aerospace, chemicals, telecommunications, electronics, food processing, pharmaceuticals, consumer goods, lumber mining, defense equipment, healthcare, information technology, construction, retail, real estate and financial services |
| <b>GDP Growth</b>                            | 2.2%   |
| <b>Internet Domain</b>                       | .us  |
| <b>International Dialing Code</b>            | +1   |
| <b>Dates &amp; Numbers</b>                   | mm.dd.yyyy. A full stop (period) is used for the decimal comma, and long numbers are written with a point (999,999,999.00)   |



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## Tax Requirements to Start a Business

It is important for businesses to comply with federal, state, and local tax laws.

Make sure to meet all federal tax requirements for starting a business. Follow this [checklist from the IRS](#).

Each state has additional tax rules when you start and operate a business. [Get information on state-level requirements](#).

Learn more about business taxes, including energy tax incentives that can help you save money.

## Setting Up A Payroll

When setting up a US payroll, the company should follow the below step:

- Get an Employer Identification Number (EIN)
- Find out whether they need state or local tax IDs
- Decide if they want an independent contractor or an employee
- Ensure new employees return a completed W-4 form
- Schedule pay periods to coordinate tax withholding for IRS
- Create a compensation plan for holiday, vacation and leave
- Choose an in-house or external service for administering payroll
- Decide who will manage their payroll system
- Know which records must stay on file and for how long
- Report payroll taxes as needed on quarterly and annual basis

The IRS maintains the [Employer's Tax Guide](#), which provides guidance on all federal tax filing requirements that could apply. The employer also needs to check with the applicable state tax agency for employer filing stipulations.

## Hiring Foreign Nationals

By law, all employers must only employ individuals who have permission to work in the U.S. The online E-Verify system allows companies to determine the eligibility of potential employees. Employers can register their company with [E-Verify](#) online.

## Entity Registration & Incorporation Requirements

### Company Registration Steps

1. Step 1: Register Your LLC. To start the process, you need to work with what is known as a "Registered Agent"
2. Step 2: Get a Physical Business Address
3. Step 3: Apply for an EIN
4. Step 4: Get a Bank Account
5. Step 5: Get a Payment Processor
6. Step 6: Set up a Bookkeeping System

### Type of Business

In USA, companies most commonly conduct business through private or public limited liability companies. Business can also be conducted through general or limited partnerships or co-operatives. A foreign organization or foundation can also establish a branch in USA.

### Limited Liability Company

A limited liability company (LLC) is a business structure in the United States whereby the owners are not personally liable for the company's debts or liabilities. Limited liability companies are hybrid entities that combine the characteristics of a corporation with those of a partnership or sole proprietorship.

Although the requirements for LLCs may vary by state, there are generally some commonalities across the board. The very first thing owners or members must do is to choose a name.

Once that has done, the articles of organization must be documented and filed with the state. These articles establish the rights, powers, duties, liabilities, and other obligations of each member of the LLC. Other information included on the documents includes the name and addresses of the LLC's members, the name of the LLC's registered agent, and the business' statement of purpose.

The articles of organization must be accompanied by a fee paid directly to the state. Paperwork and additional fees must also be submitted at the federal level to obtain an employer identification number (EIN).

Limited liability companies are corporate structures in the United States where owners are not personally liable for the company's debts or liabilities.



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Regulations surrounding LLCs vary from state to state.

Any entity can form an LLC including individuals and corporations; however, banks and insurance companies cannot.

LLCs do not pay taxes—their profits and losses are passed through to members, who claim them on their tax returns.

### *Advantages and Disadvantages of LLCs*

The primary reason business owners opt to take the LLC route is to limit the principals' liability. Many view an LLC as a blend of a partnership, which is a simple business formation of two or more owners under an agreement, and a corporation, which has certain liability protections.

Although LLCs have some attractive features, they also have several disadvantages, especially concerning the structure of a corporation. Depending on state law, an LLC may have to be dissolved upon the death or bankruptcy of a member.<sup>10</sup> This contrasts with a corporation, which can exist in perpetuity. An LLC may not be a suitable option when the founder's ultimate objective is to become a publicly traded company.

## **Branch**

A branch refers to a part of a foreign organization or foundation that conducts continuous business or professional activities in USA from a permanent place of business in USA in the name of and on behalf of a foreign organization or foundation.

Steps for Setting up a new U.S. branch of a Foreign company are the following:

1. Prepare a Business Plan
2. Set up the US Company
3. Set up a U.S Business Checking Account
4. Obtain a B-1 Business Visa to set up the physical office space
5. Apply for the L-1A Visa with USCIS

## **Private Entrepreneurs**

As a private entrepreneur or a self-employed person, an individual can easily engage in small-scale business activities mainly based on their own work input. Private entrepreneurship is the lightest and simplest company form. It is easy, fast and inexpensive to set up. As a private entrepreneur, an individual can engage in business activities alone, with their spouse or children or grandchildren who are under the age of 18.



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It is simple to set up a business as a private entrepreneur, as it does not require any special formalities.

After you finalize a name for the company, follow the below-mentioned steps:

1. Apply for DSC (Digital Signature Certificate)
2. Apply for the DIN (Director Identification Number)
3. Apply for the name availability
4. File the EMoa and EAOA to register the private limited company
5. Apply for the PAN and TAN of the company
6. Certificate of incorporation will be issued by RoC with PAN and TAN
7. Open a current bank account on the company name

With this, you will be all set to start your own private limited company. It is advised to consult with the right people and make the best choice for smooth growth.

## Cooperative

A cooperative is particularly suitable for collaborative entrepreneurship, regardless of the sector. It allows them to sell their own skills easily and in a risk-free manner without a large initial capital. A cooperative can be set either as an individual or as a company. The key governance bodies for a cooperative are the Board of Directors, the General Meeting and Managing Director.

Below are the steps for starting a cooperative:

1. Establish a steering committee
2. Carry out a feasibility Study
3. Draft Articles of Incorporation and Bylaws
4. Create a Business Plan and recruit more members
5. Secure financing
6. Launch

## Partnerships

A general partnership and a limited partnership are, in many ways, similar forms of business. In principle, they are set up the same way. A general partnership is ideal for a small business with a trusted partner. A limited partnership, on the other hand, is well suited for business activities based on your personal work input and combined with an investor.

The step for starting a partnership:

1. Choose a business name for the partnership and check for availability.



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2. Register the business name with local, state, and/or federal authorities.
3. Negotiate and execute a partnership agreement.
4. Obtain any required local licenses.
5. Determine what tax obligations the partnership has and take care of any necessary registrations.
6. Open a bank account for your business.

## Financial Statements

Financial statements consist of at least a profit and loss statement, a balance sheet, notes on the accounts, and a list of accounting and materials. The financial statement information recorded in the trade register is public.

All the companies irrespective of their size and status required to prepare the financial statements.

## Audit Requirement

Unlike in many foreign jurisdictions, no statutory audit requirements generally exist except for public companies. However, banks and other lending institutions often require specific financial information from their clients and may require a client to undergo an annual audit by an independent accounting firm.

Payroll records are frequently audited by both internal and external auditors.

## New Hires

When recruiting an employee, the employer and employee must conclude an employment contract that states the details of the employment relationship. The employment contract may also state the fringe and employee benefits. The employer must ensure that the employment relationship complies with the labor legislation and the applicable collective agreements.

Employers are required to comply with a federal new hire reporting requirement. For each newly hired or rehired employee, the employer must provide the following information to the state new hire directory:

- The employee's name, address, and social security number
- The employer's name, address, and Federal Employer Identification Number (FEIN)
- The date the employee first performed services for pay

However, states may request more information.

A rehired employee must be reported when the individual has been separated from employment with the organization for at least 60 consecutive days.



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Employers with employees in only one state must report newly hired employees to that state, either on paper, magnetically or electronically. Employers with employees in two or more states that report new hires magnetically or electronically may designate one state where they have employees as the state

to which they will report all their new hires. Multistate employers that wish to file all their new hire reports with one state must designate that state to the Secretary of Health and Human Services (HHS). Employers can notify HHS in one of several ways:

- By filling out an HHS form
- By writing a letter that can be mailed or faxed
- On the Internet at <https://ocsp.acf.hhs.gov/csp/home/employer>

Regardless of the method used, the following information must be provided:

- Employer's name, address, phone number, and Federal Employer Identification Number (FEIN)
- The state to which the employer will report new hires and the date on which multistate reporting will begin
- Other states in which the employer has employees
- Employer contact information (name, title, phone number, email address, fax number)
- FEIN, name, state and zip code of any subsidiary of the employer with a different FEIN for which the employer will be reporting new hires

In general, employers must report newly hired employees within 20 calendar days of the date of hire. If an employer reports new hires magnetically or electronically, it must send two transmissions for each calendar month which are 12–16 days apart. States can establish their own time frames for reporting new hires, but they can be no longer than the federal requirements. Multistate employers that submit reports twice monthly must submit information for a newly hired employee as soon as possible after the date of hire, but no later than the next semimonthly reporting period.

Some states may require employers to report more information than the elements required by federal law.

An employee's date of hire is the first day services are performed for wages by the employee, and employees who work for as little as one day must be reported. The federal reporting requirement does not apply to independent contractors, but some states do require such reporting. Also, employees who are rehired after being laid off, or who return to work after a leave of absence, do not need to be reported as new hires if they were not absent for more than 60 days.



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Employers can report new hires using the employee's Form W-4, or an equivalent form containing the required information, and can transmit the report by first class mail, magnetically, or electronically. Using the employee's Form W-4 to meet the new hire reporting requirement entails a burden not previously faced by employers, since the employer identifying information and date of hire do not otherwise need to be placed on a Form W-4.

## Working Hours & Work Week

### Definition of the Workweek

The workweek does not have to be the same as a calendar week or begin at the start of a day. However, the workweek must include seven consecutive 24-hour periods. The workweek may also differ from the pay period. The workweeks can also vary between employees.

The workweek is also important because it establishes when the calculation of overtime starts. Overtime is defined as all-time physically worked over 40 hours in a workweek. The Fair Labor Standards Act (FLSA) requires that nonexempt employees be paid at least 1½ times their regular rate of pay for all hours physically worked over 40 in a workweek.

Although the FLSA encourages employers to establish permanent workweeks, changes to the workweek may be necessary to meet changing business needs. To ensure employees receive all overtime pay to which they are entitled when workweeks change, several steps must be taken.

1. Add overlapping day(s) to the old workweek, then calculate overtime hours and pay for both the old and new workweeks.
2. Add overlapping day(s) to the new workweek, then calculate overtime hours and pay for both the old and new workweeks.
3. Pay the employee the greater amount from Step 1 or Step 2.

Assume that an employer changes its workweek from Monday through Sunday to Sunday through Saturday. A nonexempt employee works the following hours during a two-week period.

The employee's overtime is calculated as follows.

1. Add overlapping day (Sunday) to the time worked during the old workweek (40 hours + 8 hours = 48 hours).
2. Add overlapping day (Sunday) to the time worked during the new workweek (8 hours + 32 hours = 40 hours).
3. Pay overtime based on the greater of the two amounts (48 hours).





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## Labor Law

The Fair Labor Standards Act (FLSA), also known as the Federal Wage-Hour Law, is perhaps the most basic of all payroll and employment laws.

The FLSA:

1. Sets the minimum wage and overtime rates covered employees must receive for their work
2. Requires record keeping by all covered employers
3. Places restrictions on the types of work minors can do and the hours they can work
4. Mandates equal pay for equal work

The FLSA does not:

1. Require employers to provide paid vacations, sick days, jury duty leave, holidays, lunch breaks, or coffee breaks, but some states require certain employers to provide paid sick leave to employees meeting specific requirements.
2. Regulate how often employees must be paid, or when they must be paid after employment termination (voluntary or involuntary)
3. Restrict the hours that employees over 16 years of age may be required to work
4. Generally, items not covered by the FLSA are regulated by state laws.

The FLSA does not require that wages be paid within a certain time after services are performed. However, federal courts have ruled that wages are “unpaid” unless they are paid on the employees’ regular payday. Payment after that date violates the FLSA’s minimum wage and overtime pay requirements.

## Minimum Wage

The FLSA requires nonexempt employees to be paid a minimum wage, as set by Congress.

The federal minimum wage since July 24, 2009, is \$7.25 per hour. All employees who are not exempt must be paid at least the minimum wage for all hours worked. Employees may be paid on a piecework, salary, or commission basis if their hourly wages equal or exceed the minimum wage. Nonexempt employees paid solely on a commission or piecework must have their work hours tracked to ensure compliance with the minimum wage requirement.

## State Minimum Wage

In addition, many states have enacted a minimum wage and tip credit. If the employer is covered by both state and federal law and the two are not the same, the employer is required to pay the higher minimum wage based on the state in which the employee works.



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## Tips

Employees who regularly receive tips may be paid a lower rate of pay, when certain conditions are met, if their hourly rate of pay plus the tips received meets minimum wage requirements.

Under the FLSA, employers may pay tipped employees, who receive \$30.00 in tips during a month, at least \$2.13 per hour if the amount of the employee's tips is enough to raise the employee's regular rate of pay to the minimum wage for the workweek. If the tips are not enough to raise the regular rate of pay to the current federal minimum wage— \$7.25 per hour effective July 24, 2009—for the workweek, the employer must pay the difference, ensuring the employee the minimum wage for the week.

| Federal minimum wage | Tipped employee's minimum cash wage | Tip credit  |
|----------------------|-------------------------------------|-------------|
| \$7.25/hour          | \$2.13/hour                         | \$5.12/hour |

## Regular Rate of Pay

The regular rate of pay is an hourly pay rate. It is figured by dividing the employee's total regular pay earned for the workweek by the total number of hours worked. The regular rate of pay calculation only impacts nonexempt employees because employers are not required to compensate exempt employees beyond their salary.

## 8/80 Rule for Hospitals and Nursing Homes

The FLSA contains an exemption to the workweek standard for hospitals and nursing homes that is designed to give them more flexibility in scheduling. The law allows such employers to use a 14-day period, rather than a workweek, for determining overtime compensation. Additionally, this extended period can be used for different groups of employees as the employer sees fit.



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# Employee and Employer Taxes

All employees are subject to federal income tax and the payment of the tax. Employers are responsible for calculating and withholding the taxes on the employee's wages.

## Federal Income Tax Withholding

When calculating the federal income tax withholding from wage payments, the Internal Revenue Service (IRS) prescribes which methods to use. The employer may use the wage-bracket or percentage method. If a payment is considered supplemental wages, then the optional flat rate method or mandatory flat rate method may apply to that payment. Occasionally, an employer will provide cash or noncash payment of wages and gross the wages up in order to provide a specific net payment, after taxes, to the employee.

The Internal Revenue Code holds employers liable for federal income, social security, and Medicare taxes withheld from employees' wages. Other amounts required to be withheld (e.g., child support, state and local income taxes) fall under the jurisdiction of states or other federal agencies.

It is critically important for employers to calculate and withhold federal income tax correctly. Not calculating federal income tax withholding correctly may cause the employee to be under withheld and must pay the additional taxes when filing Form 1040. In addition, employers may be penalized for under withholding federal income tax.

Payroll professionals must understand the two most frequently used methods of calculating withholding federal income tax—the wage-bracket method and the percentage method.

## Pre-Tax Contributions to Retirement Plans

Employers may set up retirement (deferred compensation) plans under which employees can buy benefits with their wages before taxes are applied.

When plans meet the regulatory requirements, an employee may elect, in advance, to have his or her wages reduced by a specific amount to pay for the benefit. Under deferred compensation, the pre-tax deductions only reduce the amount of wages subject to federal income tax.



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## Deferred Compensation

Employers can provide their employees with a variety of deferred compensation plans; however, salary reductions into a deferred compensation plan are subject to social security and Medicare taxes.

These plans are designed to defer the employee's wages until the employee retires, when he or she will presumably be in a lower tax bracket. In effect, these deferred compensation plans provide employers with the ability to set up a retirement plan for the employee with minimal cost to the employer.

Deferred compensation plans come in two varieties: qualified and nonqualified plans. Qualified plans meet the requirements of the IRS Regulations. The two most common types of qualified plans to which employees defer wages are found in Sections 401(k) and 403(b) of the Internal Revenue Code. Section 401(k) plans are those provided to employees in private industry and non-profit organizations. Employees may defer a maximum of \$19,000 into a §401(k) plan for investment into a variety of funds, including the employer's stock.

Section 403(b) plans are provided by educational institutions and non-profit organizations. These plans allow a maximum deferral of \$19,000 into investments in annuities and mutual funds.

In addition, employees 50 years of age or older may defer an additional \$6,000.

Nonqualified plans do not meet the requirements of the IRS Regulations. They provide employees with some of the benefits of a qualified plan by delaying taxation for federal income tax purposes but there is more risk of loss of the deferrals and severe restrictions on elections for deferrals and distributions from the plan.

State and local government employers may offer deferred compensation plans under Section 457(b) of the Internal Revenue Code that are technically classified as nonqualified plans. Section 457(b) plans limit deferrals to \$19,000.

## Deferred Compensation Regulations

Your firm's benefit programs may be of great value to you personally and complex for you as a payroll practitioner. One of the key benefits many companies offer their employees is the opportunity to have some of their current income deferred and accumulated until retirement. To provide these benefits, qualified plans must meet many requirements found in IRS regulations.



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## Qualified Plans

A plan is qualified if it complies with the provisions of Section 401 of the Internal Revenue Code. Qualified plans include profit-sharing plans, defined contribution plans, defined benefit plans, and the popular 401(k) plan, named after its section of the tax code.

Similar plans, which fall under other sections of the tax code, have been established for certain types of employees. Section 403(b) applies to employees of public schools and nonprofit organizations.

Essentially, qualified plans must:

- Be in writing and be communicated to employees
- Be established for the exclusive benefit of employees or their beneficiaries
- Be nontransferable and nonforfeitable (that is, be vested)
- Satisfy the rules related to eligibility and minimum vesting of employees' interest in the plan
- Perhaps most importantly, not discriminate in favor of officers, shareholders, or highly compensated employees. However, benefits can vary with length of service.

## Nonqualified Plans

Unlike qualified plans, nonqualified plans can be discriminatory. Section 457(b) plans for public sector employees are like nonqualified plans in that they can be discriminatory. Any employer plan designed to provide employees with compensation that will be deferred to a later date (usually after retirement) and that does not meet the requirements of IRC §401(a) is a nonqualified deferred compensation plan. Employers often use such plans to compensate certain high-level executives because they are not restricted by the nondiscrimination requirements that apply to qualified plans or the contribution and benefit limitations (for example, the indexed annual contribution limit and the limit on annual compensation used to calculate benefits or contributions). A nonqualified plan may also base benefits on compensation that is not included in calculations for other employees, such as bonuses.

Deferrals to a nonqualified plan include:

- Employee pretax salary reductions,
- Employer contributions, and
- Earnings credited to the employee's account.



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## Calculation of Social Security and Medicare Taxes

Employers and employees both must pay taxes required by the Federal Insurance Contributions Act (FICA). These taxes provide funding for two federal benefit programs: social security and Medicare. Social security is comprised of Old Age and Survivor's Insurance (OASI) and Disability Insurance (DI). Medicare benefits are provided by the Health Insurance (HI) program.

### Employee Taxes

#### *Social Security Tax Withholding Requirements*

The employee's portion of social security taxes is withheld from the employee's wages and the employer pays their portion of the social security tax. The employer then pays both portions to the federal government. When determining the amount of social security taxes to withhold and the employer's portion, employers may round fractions of cents to the nearest cent.

#### There Is No Age Limit

As an employer, you are required to withhold social security and Medicare taxes and pay the employer's portion for all employees, even those who are receiving social security and Medicare benefits.

#### Employers Must Withhold Up to the Maximum

When a taxpayer works for more than one employer during the calendar year, it is possible that the employee's social security wages paid by all employers will be over the limit. Employees receive credit for any social security tax withheld in a year due to excess withholding when they file their annual tax returns. All employers are required to withhold and match the amount up to the maximum each year, regardless of an employee's previous earnings with another employer.

#### Employers Must Withhold for New Employees

In most cases, when an employee begins working for a new employer, that employer must begin withholding social security taxes even though the employee's year-to-date wages may have exceeded the social security wage base.

#### Social Security Wage Base

Social security tax is applied only up to a certain wage base. In 2021, the social security wage base is \$142,800. Wages earned beyond the wage base are not taxable.



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## Social Security Tax Withholding Rate

The amount of social security tax is a percentage of the employee's taxable wages. In 2021, the employee's social security tax rate is 6.2%. Both employees and employers pay the social security tax. The employer's social security tax rate in 2021 is 6.2%. The combined employee/employer social security tax rate is 12.4%.

The maximum social security tax that can be withheld from an employee's wages in 2021 is \$8,853.60 and the wage base is \$142,800. The maximum social security tax paid by employers in 2021 is \$8,853.60.

## *Medicare Tax Withholding Requirements*

The employee's portion of Medicare taxes is withheld (1.45% from all wages plus 0.9% from wages in excess of \$200,000.00) from the employee's wages. In addition, the employer pays Medicare tax currently at 1.45% on all wages. The employer then pays both portions to the federal government. When determining the amount of Medicare taxes to withhold and the employer's portion of the tax, employers may round fractions of cents to the nearest cent.

## Medicare Wage Base

Until 1994, the Medicare tax was also applied only up to a certain wage base. Now, however, there is no Medicare wage limit. Because social security tax has a wage base and Medicare tax does not, separate accounting and reporting for each tax is necessary on forms sent to the Internal Revenue Service (IRS), Social Security Administration (SSA), and employees.

## Medicare Tax Withholding Rate

In 2021, the Medicare tax rate is 1.45% on all wages plus 0.9% on wages in excess of \$200,000. Both employees and employers pay the Medicare tax. The employer's Medicare tax rate is 1.45% on all wages.

## *Federal Unemployment Tax*

The federal and state unemployment insurance programs are coordinated by the Federal Unemployment Tax Act (FUTA). The federal unemployment taxes are collected to pay the administrative costs of both federal and state programs. State unemployment taxes (SUTA or SUI) are collected to pay unemployment insurance benefits for eligible individuals. The federal law places requirements and limitations on the state programs. The FUTA tax is paid entirely by employers. Except for three states (New Jersey, Pennsylvania, and Alaska), the state



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unemployment (SUTA) tax is paid by employers. Employees subject to SUTA in New Jersey, Pennsylvania, and Alaska pay SUTA tax along with their employer.

### FUTA Tax Rate and Wage Base

Employers pay the FUTA tax on their employees' wages at the rate of 6.0%. The rate is applied to the first \$7,000 of an employee's covered wages in a calendar year.

### FUTA Tax Credit

However, most employers do not pay the full 6.0% tax. Employers paying their state unemployment taxes in full and on time can receive a credit against their FUTA tax rate of up to 5.4%. Employers receiving the full credit have an effective FUTA tax rate of 0.6% and pay \$42 for each employee receiving at least \$7,000 of covered wages ( $\$7,000 \times 0.006 = \$42$ ).

However, when a state unemployment insurance program has borrowed from the federal program to pay benefits and the state does not timely repay the federal program, employers in the state may lose a portion of the 5.4% credit. In 2018, employers in one territory lost a portion of the 5.4% credit. In 2018, employers in the Virgin Islands lost 2.4% of the credit.

### Calculating State Credits Against FUTA Tax Liability

As noted previously, an employer's FUTA tax rate of 6.0% can be reduced by up to 5.4% through credits the employer can take based on the amount and timeliness of its state unemployment tax payments. There are two types of credit against FUTA liability.

- The "90%" or "normal" credit provides a reduction in FUTA liability for payments required and made under state unemployment compensation laws.
- The "additional" credit allows employers whose state unemployment tax rate is less than 5.4% because of a favorable unemployment history to receive credit for the difference between 5.4% and the percentage actually paid.

An employer's total normal and additional credits against the FUTA tax rate of 6.0% cannot exceed 5.4%. Most employers pay an effective FUTA tax rate of 0.6%.

## Group-Term Life Insurance

One of the more popular benefits offered employees is employer-provided life insurance. The most common type of insurance is group-term life insurance, which most often provides a death benefit payable in a lump sum to the employees' designated beneficiaries. Special rules in the Internal Revenue Code (IRC) govern the taxation of employer-provided group-term life insurance coverage.





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The value of employer-provided group-term life insurance up to \$50,000 is excluded from employees' income. The value of coverage in excess of \$50,000, minus any amount paid for the coverage by employees after taxes, must be included in the employees' income. The value of the excess coverage is subject to social security and Medicare taxes, but is not subject to federal income tax withholding or federal unemployment (FUTA) tax. At their option, employers may withhold federal income tax on the value for employees.

Employees must pay the federal income tax owed on any amount of group-term life insurance above \$50,000 and report the amount on their personal income tax returns even though income tax withholding is not required. While income tax withholding is not required, social security and Medicare tax withholding is required. The value must be reported on the employees' Form W-2 in Boxes 1, 3, 5, and 12 (with code C), and on their employers' Forms 940 (Part 2, Lines 3 and 4) and 941 (Lines 2, 5a column 1, 5c column 1, and 5d column 1).

Employers must take the following steps to compute the monthly value of excess group-term life insurance to include in an employee's income.

1. Determine the total amount of the employee's group-term life insurance coverage under the employer's plan. Most plans figure coverage as a multiple of the employee's base salary, which may increase during the year if the employee gets a raise. Therefore, many employers use the employee's base salary as of January 1 of each year as the base amount for determining life insurance coverage. Many companies also have a maximum amount of employer-provided coverage.
2. Calculate the excess benefit over \$50,000 by subtracting \$50,000 from the total coverage.
3. Divide the excess insurance amount by \$1,000.
4. Determine the employee's age as of December 31 of the calendar year during which the benefit is taxable.
5. Use IRS Table I Uniform Premiums to calculate the FMV of one month of excess insurance per \$1,000 and multiply it by the answer obtained in Step 3.
6. Deduct any after-tax contributions by the employee from the value of the insurance.
7. Add the excess amount to the employee's income, withhold and pay social security and Medicare taxes, and report the amount as required.

The value of group-term life insurance over \$50,000 is not included in an employee's income when one of the following conditions is met:

- Beneficiary is the employer
- Beneficiary is a charitable organization
- Employee terminates employment during the year because of a permanent disability



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## Bonuses

Amounts paid to employees as bonuses in addition to their usual compensation must be included in the employees' income and are subject to federal income tax withholding and social security, Medicare, and FUTA taxes. The IRS has defined bonuses as supplemental wages. Employers may choose to withhold federal income tax using the optional flat rate or aggregate method when the employee's year-to-date supplemental wages are \$1,000,000 or less.

## Commissions

Commissions on sales of goods or insurance premiums are subject to federal income tax withholding and social security, Medicare, and FUTA taxes when paid to an employee (or a former employee entitled to deferred or renewal commissions). This is true whether the employee was directly involved in selling the products. The IRS has defined commissions as supplemental wages. Employers may choose to withhold federal income tax using the optional flat rate or aggregate method when the employee's year-to-date supplemental wages are \$1,000,000 or less.

## Jury Duty Pay

The tax treatment of wages received from an employer for time an employee spends on jury duty depends on the employer's policy in providing such wages.

1. If the employer pays an employee his or her regular wages in addition to jury duty pay received from the government unit involved, the wages are subject to federal income tax withholding and social security, Medicare, and FUTA taxes.
2. If the employer pays an employee the difference between the employee's regular pay and the jury duty pay, only that difference is subject to federal income tax withholding and social security, Medicare, and FUTA taxes.
3. If the employer pays an employee wages for time spent on jury duty but requires the employee to turn over the jury duty pay to the employer, only the difference between the amount paid and amount turned over is subject to federal income tax withholding and social security, Medicare, and FUTA taxes. The employee may deduct the amount turned over on his or her personal income tax return.

In cases where the employee can keep the jury duty pay, it must be included in income on the employee's personal tax return. If a juror is paid at least \$600 by a state or political subdivision, that amount is not considered wages, but must be reported on Form 1099-MISC in Box 3 as "other income." The juror compensation from the state or political subdivision is not subject to federal income tax withholding or social security, Medicare and FUTA taxes.



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## Retroactive Wage Payments

Retroactive wage payments are treated as wages when they are made and are subject at that time to federal income tax withholding and social security, Medicare, and FUTA taxes at current rates and under current wage limits. The IRS has defined retroactive wage payments as supplemental wages. Employers may choose to withhold federal income tax using the optional flat rate or aggregate method when the employee's year-to-date supplemental wages are no more than \$1,000,000.

## Taxable Tips

Generally, tips or gratuities provided voluntarily by customers are taxable wages to the employee receiving them. Because of the special nature of tip income, with the employee's wages being provided to a great extent by customers rather than by the employer, there are special rules that apply.

## Service Charges Are Not Tips

Where the customer is required to pay a service charge added to the bill, the service charge is not a tip. When the service charge is turned over to the employee, it is regular wages.

Tips are discretionary (optional or extra) payments determined by a customer that employees receive from customers. Tips include:

- Cash tips received directly from customers.
- Tips from customers who leave a tip through electronic settlement or payment. This includes a credit card, debit card, gift card, or any other electronic payment method.
- The value of any noncash tips, such as tickets, or other items of value.
- Tip amounts received from other employees paid out through tip pools or tip splitting, or other formal or informal tip sharing arrangement.

## Determining Whether a Payment Is a Tip or a Service Charge

Certain factors are used to determine whether payments constitute tips or service charges. The absence of any of the following factors creates a doubt as to whether a payment is a tip and indicates that the payment may be a service charge:

- The payment must be made free from compulsion.
- The customer must have the unrestricted right to determine the amount.
- The payment should not be the subject of negotiations or dictated by employer policy.
- Generally, the customer has the right to determine who receives the payment.



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## Identifying Service Charges

An employer or employee's characterization of a payment as a "tip" is not determinative. Examples of service charges commonly added to a customer's check include:

- Large dining party automatic gratuity
- Banquet event fee
- Cruise trip package fee
- Hotel room service charge
- Bottle service charge (nightclubs, restaurants)

Generally, service charges are reported as non-tip wages paid to the employee. Some employers keep a portion of the service charges. Only the amounts distributed to employees are non-tip wages.

### Employees Must Report Tip Income to Employer

Employees who receive at least \$20 a month in cash tips must report their tip income to their employer at least once a month by the 10th of the next month (more frequently if the employer requires it). The easiest way is for the employer to provide them with Form 4070, Employee's Report of Tips to Employer, although the employer may use its own form or electronic method.

## Withholding on Tip Income

Tip income is subject to federal income tax withholding and social security, Medicare, and FUTA taxes if the employee reports more than \$20 in tips for the month. Tip income for which no withholding is required is still income to the employee, who must report it on his or her personal tax return. The IRS has defined tips as supplemental wages, but the IRS allows employers to determine if tips are considered supplemental wages or regular wages. Income, social security, and Medicare taxes on tip income should be withheld from the employee's regular wages, either by combining the amounts or using the supplemental wage method.

Where the taxes to be withheld exceed the wages available, the employee can be asked to provide the employer with enough funds to satisfy the withholding obligation. If that is not done, or the amount provided is not enough, the employer should withhold taxes in the following priority:

- Social security and Medicare taxes on regular wages
- Federal income tax on regular wages
- Social security and Medicare taxes on tips
- Federal income tax on tips

The uncollected amount of social security and Medicare taxes must be reported on the employee's Form W-2 in Box 12 with Codes "A" and "B" respectively. Withheld amounts must be



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reported in Boxes 4 and 6 respectively. The employer must pay its full portion of social security and Medicare taxes even if the employee's portion was not fully collectable.

## **When Tips are Deemed Paid**

Tips are deemed paid to the employee when the employee furnishes the required report to the employer. If no report is furnished, the tips are paid when received from the customer (or from the employer if they are credit card tips or are otherwise required to be turned over to the employer initially).

## **Repayment of Employer-Provided Loans**

Many employers offer loans to employees. The repayment of these loans is not limited by the FLSA's restrictions on employer deductions because the employee has voluntarily agreed to repay the loan based on the repayment schedule identified at the time the loan was made. Employers can set the repayment schedule as they choose.

However, if at any time during the calendar year the value of all loans made to an employee exceeds \$10,000, the employer may be required to impute income to the employee if the interest rate on the loan is less than the interest rate the employer would pay on outstanding taxes owed to the IRS.

## **Workers' Compensation**

Workers' compensation is a form of insurance employers are generally required to buy to insulate them against lawsuits brought by employees who are hurt or become ill while working.

## **Benefit Payments**

Payments received as workers' compensation benefits are not included in an employee's gross income and are not subject to any employment taxes. This exemption applies only to amounts received as compensation for injuries or illnesses suffered on the job, and only to amounts that do not exceed the benefits provided under the applicable state or federal workers' compensation law.

## **Family and Medical Leave Act (FMLA)**

The Family and Medical Leave Act (FMLA) guarantees employees unpaid leave for the birth or adoption of children and for serious medical conditions of family members or themselves. Closely related to the FMLA's requirements and the benefit it provides to employees are the sick and disability policies most mid-size and large employers provide.

In general, the FMLA guarantees employees 12 weeks of unpaid leave within a 12-month period:



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1. To care for a newborn or newly adopted or foster child
2. To care for a child, spouse, or parent with a “serious health condition”
3. To care for themselves if they have a serious health condition that makes it impossible for them to continue working
4. Because of any qualifying exigency (situation) arising out of the fact that the employee’s spouse, son, daughter, or parent is a covered military member on active duty (or has been notified of an impending call or order to active duty)
5. “Eligible” employees of a covered employer may take unpaid leave, or substitute appropriate paid leave if the employee has earned or accrued it, for up to a total of 26 workweeks in a “single 12-month period” to care for a covered service member with a serious injury or illness.

The FMLA applies to all private and public (government) employers with 50 or more employees, including part-timers and employees on leave or suspension, but not laid-off employees. The definition of employee is the same as that under the Fair Labor Standards Act. An employee at a facility with less than 50 employees may still be eligible for the leave benefits if the employer has at least 50 employees working within a 75-mile radius of the facility.

To be eligible for leave benefits, employees must:

1. Have been employed by the employer for at least 12 months (not necessarily consecutively)
2. Have worked at least 1,250 hours within the previous 12-month period

Exempt employees who have worked for the employer for at least a year are deemed to have met the 1,250-hours requirement unless the employer can prove otherwise.

The law also guarantees continuation of the employee’s health benefits while on leave.

## Employment Forms

One of the responsibilities facing the employer and payroll professionals is compliance regarding the completion, filing, and storage of employment forms.

### Employee Forms

Once an employer hires a worker as an employee, the employee must prove to the employer his or her identity and right to work in the United States.

When first hired, employees generally must complete two forms:



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- Form I-9, Employment Eligibility Verification, and
- Form W-4, Employee's Withholding Allowance Certificate.

### *Form I-9*

#### **Purpose of Form I-9**

Once an employer hires a worker as an employee, the employee must prove to the employer his or her identity and right to work in the United States through the completion of Form I-9, Employment Eligibility Verification. The Immigration Reform and Control Act of 1986 (IRCA) makes it illegal for an employer to hire an unauthorized worker. Employers must comply with this requirement by verifying the identity and right to work of all employees hired after November 6, 1986.

Employers will not be penalized under IRCA if they have acted in good faith, even though they may have employed an unauthorized worker after accepting a fraudulent document offered as proof of the right to work. Employers can protect themselves by taking the following actions:

1. Having newly hired employees fill out section 1 of Form I-9 no later than the day when they begin work. Employers participating in E-Verify must have the employee enter their social security number in section 1. Employers not participating in E-Verify cannot require the employee to enter their social security number in section 1.
2. Completing the employer's part of Form I-9 (section 2) within 3 days of hire
3. Making sure the documents presented by the employee establishing the employee's identity and eligibility to work appear genuine
4. Keeping completed Forms I-9 for at least 3 years from the date of hire or 1 year from the date of termination, whichever is later (see chart below)
5. Presenting Form I-9 on request to an inspector from U.S. Citizenship and Immigration Services (USCIS) or the Department of Labor

### *Form W-4 Series*

Every employer must deduct and withhold federal income, social security, and Medicare taxes from wages paid to employees. The amount of income tax withholding is based on filing status and the number of withholding allowances claimed. Withholding allowances reduce the amount of wages subject to federal income tax withholding. Employers must use one of the withholding methods prescribed by the IRS to calculate the exact amount of withholding.



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## Form W-4 Requirements

Every employer must keep a Form W-4, Employee's Withholding Allowance Certificate, on file for each employee. The form kept on file may be a paper copy or an electronic version of the form. The W-4 tells the employer how many withholding allowances the employee is claiming along with the employee's marital status. It also tells the employer if the employee claims exemption from withholding. Employees may indicate on the W-4 if they want an additional dollar amount withheld in excess of the amount based on their marital status and withholding allowances. However, employees cannot designate a flat dollar amount to be withheld or a percentage of earnings as their withholding tax on Form W-4. See Tax Forms and Publications in the Resource Center for a copy of Form W-4.

## Filing Requirements

All newly hired employees should complete and submit a signed Form W-4 to their employer on or before the first day of work.

- If employee fails to furnish a Form W-4. If new employees do not furnish a Form W-4 by their first pay period, the employer must withhold as if they were claiming single with no allowances. This procedure maximizes the amount withheld (and may motivate compliance with the filing requirements). If an employee has not filed a Form W-4 and the employer receives a notice from the IRS concerning the W-4, the employer must request the employee complete a Form W-4.
- If allowances increase. Current employees can file an amended Form W-4 any time their number of allowances increases, for example, at the birth or adoption of a child.
- If allowances decrease. If allowances decrease (thus increasing the amount withheld each pay period), employees must file an amended Form W-4 within 10 days. This could happen when:
  - An employee is divorced or legally separated.
  - Someone else takes over support of a dependent.
  - A nonworking spouse takes a job.

Employers are not required to monitor employees for changes that decrease allowances.

- Death of spouse. The death of a spouse does not require the surviving spouse to file a new Form W-4 until January 1 of the year after the spouse's death.
- Death of a dependent child. The death of a dependent child does not require a new Form W-4 be filed until January 1 of the year after the dependent child's death.





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- Notify employees by December 1. The employer is encouraged to notify employees by December 1 that they need to file an amended Form W-4 if their filing status or number of allowances has changed.
- Changes cannot be made in advance. Employees cannot submit a revised Form W-4 in anticipation of a change. For example, if they expect to be married, they cannot change their marital status or number of allowances until after the wedding.
- When you must change withholding. After a current employee files an amended Form W-4, the change must be reflected in withholding no later than the first payroll period ending on or after the 30th day after receiving the amended Form W-4.
- New Forms W-4 annually. The IRS does not require employees to complete a new Form W-4 each year. Employees may be required to complete a Form W-4 when their circumstances change.

### Form W-2 Reporting/Filing Requirements

Employers must file a Form W-2 reporting the total amount of wages paid and money withheld for each employee in a calendar year. A calendar year runs from January 1 through December 31.

Form W-2 has a variety of purposes. It informs employees of their total wages and tax deductions so they may complete their personal income tax returns. If taxes were not withheld, the form provides the information necessary for employees to accurately determine the amount owed to the Internal Revenue Service (IRS). The W-2 also provides the SSA with the necessary information so that the employees' earnings and benefit accounts are properly credited. The SSA shares employees' earnings and tax information with the IRS.

The employer must determine whether to provide a Form W-2 for a particular employee. The Internal Revenue Code requires the employer to file a Form W-2 for the employee if one of the following situations applies.

- The employer is engaged in a trade or business that compensated an employee for work performed, even if the employee was not paid in cash.
- The employer withheld income, social security, or Medicare taxes from the employee.
- The employer would have withheld income tax if the employee had claimed no more than one withholding allowance on Form W-4.

The payroll practitioner must be familiar with more than 40 tax forms (summarized in the following table), differentiate between various versions of the same form, know when each is to be used, and complete and file the appropriate form by the due date.



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### Federal Forms Used by the Payroll Department:

- SS-4 Application for Employer Identification Number
- SS-5 Application for a Social Security Card
- SS-8 Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding
- W-2 Wage and Tax Statement
- W-2c Corrected Wage and Tax Statement
- W-3 Transmittal of Wage and Tax Statements
- W-3c Transmittal of Corrected Wage and Tax Statements
- W-4 Employee's Withholding Allowance Certificate
- W-4P Withholding Certificate for Pension or Annuity Payments
- W-4S Request for Federal Income Tax Withholding From Sick Pay
- W-9 Request for Taxpayer Identification Number and Certification
- 843 Claim for Refund and Request for Abatement
- 940 Employer's Annual Federal Unemployment (FUTA) Tax Return
- 940 (Schd.A) Multi-State Employer and Credit Reduction Information
- 940 (Schd.R) Allocation Schedule for Aggregate Form 940 Filers
- 941 Employer's Quarterly Federal Tax Return
- 941 (Schd.B) Report of Tax Liability for Semiweekly Schedule Depositors
- 941 (Schd.D) Report of Discrepancies Caused by Acquisitions, Statutory Mergers, or Consolidations
- 941 (Schd.R) Allocation Schedule for Aggregate Form 941 Filers
- 941-X Adjusted Employer's Quarterly Federal Tax Return or Claim for Refund
- 943 Employer's Annual Federal Tax Return for Agricultural Employees
- 943-A Agricultural Employer's Record of Federal Tax Liability
- 943-X Adjusted Employer's Annual Federal Tax Return for Agricultural Employers or Claim for Refund



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- 944 Employer's Annual Federal Tax Return
- 944-X Adjusted Employer's Annual Federal Tax Return or Claim for Refund
- 945 Annual Return of Withheld Federal Income Tax
- 945-A Annual Record of Federal Tax Liability
- 945-X Adjusted Annual Return of Withheld Federal Income Tax or Claim for Refund
- 1042 Annual Withholding Tax Return for U.S. Source Income of Foreign Persons
- 1042-S Foreign Person's U.S. Source Income Subject to Withholding
- 1042-T Annual Summary and Transmittal of Forms 1042-S
- 1094-B Transmittal of Health Coverage Information
- 1094-C Transmittal of Employer-Provided Health Insurance Offer and Coverage Information Returns
- 1095-B Health Coverage
- 1095-C Employer-Provided Health Insurance Offer and Coverage
- 1096 Annual Summary and Transmittal of U.S. Information Returns
- 1099-MISC Miscellaneous Income
- 1099-R Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.
- 2159 Payroll Deduction Agreement
- 2555 Foreign Earned Income
- 2678 Employer/Payer Appointment of Agent
- 2848 Power of Attorney and Declaration of Representative
- 4419 Application for Filing Information Returns Electronically (FIRE)
- 4852 Substitute for Form W-2, Wage and Tax Statement, or Form 1099-R, Distribution From Pensions, Annuities, Retirement or Profit Sharing Plans, IRAs, Insurance Contracts, etc.
- 8027 Employer's Annual Information Return of Tip Income and Allocated Tips
- 8027-T Transmittal of Employer's Annual Information Return of Tip Income and Allocated Tips



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8233 Exemption From Withholding on Compensation for Independent (and Certain Dependent) Personal Services of a Nonresident Alien Individual

8508 Request for Waiver From Filing Information Returns Electronically

8655 Reporting Agent Authorization

8809 Application for Extension of Time to File Information Returns

8821 Tax Information Authorization

8922 Third-Party Sick Pay Recap

Nontax forms:

EEO-1 Employer Information Report

I-9 Employment Eligibility Verification

SSA-131 Employer Report of Special Wage Payments

SF-329B United States Government Wage Garnishment Order

## Resident/Nonresident Alien Taxation

Generally, foreign citizens working in the U.S. are considered nonresident aliens unless they qualify as residents. The determination of residency made under the Internal Revenue Code applies only to the alien's status for U.S. income tax purposes, and not for immigration or for other federal and state tax purposes. Under the Code, an alien qualifies as a resident if he or she meets either one of two tests: the lawful permanent resident test or the substantial presence test.

## Expatriates/Resident Aliens

In recent years, there has been much written in the business and general press about the "global economy" and its impact on the way U.S. companies conduct business. An increasing number of U.S. companies are buying, selling, and manufacturing goods in foreign countries. As they become more involved in business on a global scale, U.S. businesses are also sending more of their employees abroad on foreign assignments and bringing more employees from foreign countries to work in the U.S.

## U.S. Citizens and Resident Aliens Working Abroad

In general, wages earned by U.S. citizens and resident aliens working in a foreign country are subject to federal income tax withholding unless the wages can be excluded from the



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employee's gross income under the foreign earned income exclusion or foreign housing exclusion. Withholding may also be reduced for employees who are eligible for a tax credit for foreign tax payments, by increasing the number of allowances taken on the Form W-4. Wages earned abroad may be exempt from withholding if the employer is required to withhold foreign taxes under the law of the foreign country.

Employees working for U.S. companies abroad are generally also subject to social security and Medicare taxes, although coverage is optional if the employer is a foreign affiliate of a U.S. company. Such employees' wages are also subject to FUTA tax.

## Termination payment

There is no federal law made for termination pay of an employee. Termination pay is under jurisdiction of state. Each state has different way of doing it. Refer <https://www.nolo.com/legal-encyclopedia/final-paycheck-employee-rights-chart-29882.html> to see the jurisdiction of each state.

## Taxation and Reporting of Wages Paid to Deceased Employees

When an employer owes wages to an employee who has died, special reporting and taxing requirements are faced by the employer.

### Wages Paid After Death

The tax treatment and reporting obligations for wages paid after an employee's death depend on when the wages are paid in relation to the employee's death.

### Employee Dies Before Cashing Paycheck

If an employee dies after receiving a paycheck, but before cashing it, the employer should reissue the check to the employee's personal representative based on the laws of the employee's state of residence for the same net amount, since income and employment taxes were properly withheld. The wages and amounts withheld must be reported on the deceased employee's Form W-2.

### Check State Laws

Before reissuing the deceased employee's paycheck, the employer must check state law for any requirements regarding who can receive the check, how much can be paid, etc.



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## **Wages Paid After Employee Dies and in the Same Year**

Wages paid to a deceased employee's estate or legal representative after the employee dies but in the year of death are not subject to federal income tax withholding. They are subject to social security, Medicare, and FUTA taxes, however. Therefore, the employer must report the social security and Medicare wages and the amounts withheld on the deceased employee's Form W-2 in Boxes 3-6. The amount of taxable income should be reported only in Box 3 (Other) of Form 1099-MISC in the name of the beneficiary of the payment.

## **Wages Paid After the Year of Death**

Wages paid to a deceased employee's estate or legal representative after the year of the employee's death are not subject to federal income tax withholding or social security, Medicare, or FUTA taxes and should be reported only in Box 3 (Other) of Form 1099 MISC in the name of the beneficiary of the payment.

## **Tax Deposit Requirements**

The payment of withheld federal income, social security, and Medicare taxes, as well as the employer's share of social security and Medicare taxes and FUTA tax, is handled differently from the payment of other federal taxes. Rather than paying the taxes when filing a return, employers generally must deposit the taxes using the IRS' Electronic Federal Tax Payment System (EFTPS) or in very limited situations with a check and a tax return. This module explains the rules governing the timing of employer tax deposits.

## **Lookback Period**

To determine the frequency of payroll tax deposits the IRS uses a 12-month period called the lookback period.

## **Depositor Classification**

Employers are assigned one of two depositor classifications under the rules for employer tax deposits: monthly or semiweekly. The determination is based on the amount of the employer's total liability for federal income withholding, social security, and Medicare taxes (i.e., employment taxes) during a "lookback period" that generally "looks back over" a 12-month period. The lookback period is the 12-month period from July 1 of the second previous year through June 30 of the previous year.

If an employer's four quarterly Forms 941, Employer's Quarterly Federal Tax Return (see the Online Resource Center's Tax Forms and Publications), during the lookback period show a total federal income withholding, social security, and Medicare tax liability of \$50,000 or less, the



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employer is a “monthly depositor” for the upcoming year. If the total liability exceeds \$50,000, the employer is a “semiweekly depositor.”

## Deposit Requirements

Monthly depositors (i.e., employers with \$50,000 or less in employment tax liability during the lookback period) must deposit their accumulated tax liability for each calendar month by the 15th of the following month.

Semiweekly depositors (i.e., employers with more than \$50,000 in employment tax liability during the lookback period) must deposit employment taxes for wages paid on Wednesday, Thursday, and Friday by the following Wednesday. Employment taxes for wages paid on Saturday, Sunday, Monday, and Tuesday must be deposited by the following Friday.

Semiweekly Depositors:

| Pay Days On                           | Deposit Due        |
|---------------------------------------|--------------------|
| Saturday, Sunday, Monday, and Tuesday | the next Friday    |
| Wednesday, Thursday, and Friday       | the next Wednesday |

### *One-Day Deposit Rule*

If an employer’s accumulated employment tax liability reaches \$100,000 on any day during a monthly or semiweekly deposit period, the taxes must be deposited by the close of the next business day. In determining whether the \$100,000 threshold is met:

- Monthly depositors consider only those taxes accumulated during the current calendar month, not any previous months; and
- Semi-weekly depositors consider only those taxes accumulated during the current Wednesday–Friday or Saturday–Tuesday semiweekly period.

Employers do not total their payroll and nonpayroll withheld tax liabilities to determine whether the one-day deposit rule is triggered.

## Record Keeping

Federal record retention requirements are provided below.

### Federal Retention Requirements

IRS/SSA/FUTA documents - 4 years:

- Duplicate copies of tax returns/tax deposits
- Returned copies of Form W-2



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- Canceled/voided checks or reversed electronic payments
- Employee's name/address/occupation/social security number
- Amount/date of payments for wages, annuities, pensions, tips; fair market value of wages in-kind
- Record of allocated tips
- Amount of wages subject to withholding
- Taxes withheld (and date if different from pay date)
- Copies of Form W-4 (for at least four years after the date the last return was filed using the information on the Form W-4)
- Agreements to withhold additional amounts
- Dates when employee was absent due to injury and received payments; amount/rate of such payments (by employer or third party)
- Dates when employee was absent from work and payments were made under a contingency plan; amount/rate of such payments
- Copies of Forms 940, Schedule A (Form 940), Schedule R (Form 940), 941, Schedule B (941), Schedule D (Form 941), Schedule R (Form 941), 941-X, 943, 944, 945, 945-A, W-2, W-3, 1042-S, 1042-T, 1042, and other returns filed electronically
- An exception to the four-year record retention requirement for tax items is the record of allocated tips which must be kept for three years. Employers must keep records substantiating any information returns and employee statements regarding tip allocation for three years.
- Another exception to the four-year record retention requirement for tax items is the forms required for reporting health coverage information (Forms 1094-C and 1095-C) and the data supporting the forms under the Affordable Care Act, copies of which must be retained for three years.

### FLSA record retention - 3 years:

- Name of employee/address/occupation/birth date/gender
- Hours worked each day/week
- Amount and date of payment





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- Amounts earned for straight time and overtime/additions to and deductions from wages
- Collective bargaining agreements
- Sales and purchase records

IRCA/USCIS record retention - 3 years:

- Form I-9—three years after date of hire or one year after date of termination (whichever is later)

FMLA record keeping requirements - 3 years:

The following records must be kept for at least three years, in any format, and made available no more frequently than once every 12 months for Department of Labor inspection.

- Name, address, occupation, rate of pay, daily and weekly hours worked per pay period
- Additions to and deductions from wages, total compensation
- Dates of FMLA leave (or hours if taken in increments of less than one day)
- Copies of written notices of intention to take FMLA leave provided by employee
- Copies of general and specific notices provided to employees
- Plan descriptions/policies and procedures dealing with unpaid and paid leaves
- Premium payments for employee benefits
- Records of any disputes

FLSA supplemental record retention - 2 years:

- Time cards
- Wage rate tables
- Work time schedules
- Production/order/shipping/billing records
- Records of additions to or deductions from wages

## Penalties

In addition to the penalties the IRS can assess, the following agencies can also assess penalties.



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## Department of Labor

- Failure to pay minimum wage and overtime Recovery of back wages and equal damages, and for repeated willful violations the penalty can be up to \$2,014 per violation.
- Child labor violations - Fines up to \$12,845 per violation; \$58,383 if the violation causes death or serious injury of a child

### *New-Hire Reporting*

Failing to report newly hired employees.

States can issue penalties of:

- \$25.00 per new employee not reported, or
- \$500.00 if conspiring not to report an employee

### *Immigration and Nationality Act*

Failing to report newly hired employees.

States can issue penalties of:

- 25.00 per new employee not reported, or
- \$500.00 if conspiring not to report an employee

Knowingly hiring unauthorized aliens

- Fines from \$559 to \$22,363 depending upon the number of offenses

Failure to verify documentation

- Fines from \$224 to \$2,236

## IRS Penalties



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| Failure to File Correct Information Returns  | Penalties  |
|--|--|
| <ul style="list-style-type: none"><li>• Failure to file an information return with SSA or IRS by due date</li><li>• Failure to include all the information required on a return</li><li>• Including incorrect information on a return (for example, amounts, names, and social security numbers)</li><li>• Failure to file in the proper manner (filing on paper when required to file electronically)</li></ul> | <p>A three-tier penalty:</p> <ol style="list-style-type: none"><li>1. \$50.00/return (amounts adjusted annually for inflation) if corrected by March 2, maximum \$545,500</li><li>2. \$100.00/return if corrected March 3 to August 1, maximum \$1,637,500</li><li>3. \$270/return if corrected after August 1, maximum \$3,275,500</li></ol> <p>For failure to file correct information returns due to intentional disregard, the greater of \$540 or 10% of the aggregated amount of the items to be reported correctly.</p> |
| <ul style="list-style-type: none"><li>• Failure to furnish payee statement</li><li>• Failure to include all required information on payee statement</li></ul>  | <p>A three-tier penalty:</p> <ol style="list-style-type: none"><li>1. \$50.00/return (amounts adjusted annually for inflation) if corrected by March 2, maximum \$545,500</li><li>2. \$100.00/return if corrected March 3 to August 1, maximum \$1,637,500</li><li>3. \$270.00/return if corrected after August 1, maximum \$3,275,500 (adjusted annually for inflation)</li></ol>   |

| Failure to File Correct Information Returns  | Penalties  |
|--|--|
| <ul style="list-style-type: none"><li>• Failure to file an information return with SSA or IRS by due date</li><li>• Failure to include all the information required on a return</li><li>• Including incorrect information on a return (for example, amounts, names, and social security numbers)</li><li>• Failure to file in the proper manner (filing on paper when required to file electronically)</li><li>• Failure to furnish payee statement.</li></ul> | <p><b>A three-tier penalty:</b></p> <ol style="list-style-type: none"><li>1. \$50.00/return (amounts adjusted annually for inflation) if corrected by March 2, maximum \$556,500</li><li>2. \$100.00/return if corrected March 3 to August 1, maximum \$1,669,500</li><li>3. \$270.00/return if corrected after August 1, maximum \$3,339,000</li></ol> <p>For failure to file correct information returns due to intentional disregard, the greater of \$550 or</p> |



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- Failure to include all required information on payee statement. 10% of the aggregated amount of the items to be reported correctly.
1. maximum \$556,500
  2. \$100.00/return if corrected March 3 to August 1, maximum \$1,669,500
  3. \$270.00/return if corrected after August 1, maximum \$3,339,000.
- A three-tier penalty:**
1. \$50.00/return (amounts adjusted annually for inflation) if corrected by March 2,

| Accuracy-Related Failures   | Penalties  |
|---|--|
| <ul style="list-style-type: none"><li>• Understatement of taxes</li></ul> | 20% of the underpayment; 75% of the underpayment if due to fraud |

| Failure to Make Timely Deposits   | Penalties   |
|---|---|
| <ul style="list-style-type: none"><li>• Failure to deposit taxes on the due date</li><li>• Failure to deposit using EFT</li></ul> | <p><b>A four-tier structure:</b></p> <ol style="list-style-type: none"><li>1. 2% of underpayment if failure is for not more than 5 days</li><li>2. 5% if failure is for more than 5 days but not more than 15 days</li><li>3. 10% if failure is for more than 15 days</li><li>4. 15% if tax is not deposited within 10 days of first delinquency notice</li></ol> <p>10% of the deposit if not made with EFT when required to do so</p> |

| Withholding Failures  | Penalties  |
|---|--|
| <ul style="list-style-type: none"><li>• Failure to withhold federal income, social security, and Medicare taxes</li><li>• Failure to pay withholding taxes to the IRS</li></ul> | 100% of the withholding; in addition, officers or employees could be personally liable for an equal amount |



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# Immigration

Employers must retain the completed Form I-9, Employment Eligibility Verification, for at least three years after the date of hire or one year after the date of termination, whichever is later.

Form I-9 must be made available for inspection by the Department of Labor within three days of a request. Forms may be made available on microfilm, microfiche or electronic formats if they are clear and readable and viewing and printing equipment is made available to the inspector. The employer should also keep any copies it has made of documents provided by employees to support their right to work in the U.S.

## Visa

The Visa process of USA is complex compared to other countries. Please refer <https://visaguide.world/us-visa/how-to-apply-for-us-visa/> for USA visa process.



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# What Makes Mercans your HR and Payroll Partner of Choice?

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We are a borderless people engagement enabler, driven by technology and innovation. We deliver bespoke human capital management services and global payroll solutions to empower businesses across 110+ countries regardless of their organizations' size and their industry. We pride ourselves on being global people experts with a striking local presence, committed to making your teams happy, and ensuring the consistent and sustainable growth of your organization.

### Local Presence. Regional Strategy. Global Success

Supported by 500+ payroll and HR specialists with in-depth local knowledge, Mercans operate globally. Our pioneering human resources consulting services and trailblazing SaaS platforms are already satisfying 5,000+ international clients, ensuring timely measurable results and bottom-line savings. Thanks to success-oriented teams striving for excellence and taking care of our clients' tasks within budget, we have gained the trust of major multinational companies.

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### Trailblazing Cloud-Based SaaS Products

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**+1 877 MERCANS (637 2267) | Toll-Free**

Europe: +44 20 328 777 62

North America: +1 646 798 5541

Middle East: +971 43 999 260

Asia: +81 50 5539 5354

**[info@mercans.com](mailto:info@mercans.com) | [mercans.com](https://mercans.com)**

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