

## NEW HIRE REPORTING ---

### An Additional Assignment For Employers, But One With Proven Social Value

Several states passed laws in the early 1990s requiring employers to report their newly-hired or re-hired employees to the state child support agency, or the state employment security agency. For child support purposes, new hire reporting is a method of notifying the state that a potential obligor (that is, someone who owes child support) has either become employed or has changed jobs. If appropriate, the state then serves a child-support withholding order on the individual's employer, and collects child support at the source---the paycheck.

Further, for unemployment compensation insurance purposes, new hire reporting is a method of reducing fraud by notification to the state that an individual is no longer eligible for unemployment benefits because of re-employment.

New hire reporting was so successful at the state level that Congress decided to mandate its use nationwide in an effort to reform the welfare system. One goal behind the Federal mandate was to shift the burden of supporting welfare children back to the non-custodial parents by enforcing court-ordered child support.

With few exceptions, new hire reporting was mandatory in every state beginning October 1, 1997, as required by the Personal Responsibility and Work Opportunity Reconciliation Act. This Federal law set certain minimum guidelines for states, but within those guidelines states have considerable leeway. States which already had reporting programs as of October 1, 1997 were given until October 1998 to meet the Federal guidelines.

**Who is affected.** All employers, without exception, are required to report all newly hired employees. Previously, various states limited the reporting requirements to specific industries that had a high turnover rate or that suffered from a high degree of unemployment fraud, while other states exempted certain individuals from being reported due to their age or their low income. Under the Federal requirements effective in October 1998, these exemptions ended, except as to any state or Federal employee performing intelligence or counter-intelligence work.

**Information to be reported.** New hire reports must contain information related to both the employer and the employee. At a minimum, each report is to contain the employer's name, address and Federal employer identification number, and the employee's name, address, and Social Security number. Some states require the reporting of additional items of information about the employee.

**Deadlines.** Reports must be filed within 20 days of the date of hire. Employers that report electronically or by magnetic media may limit their reports to two per month. Reports are due no more than 16 days apart and no fewer than 12 days apart.

**Reporting format.** Federal law directs that the required information shall be reported on Form W-4 (Employee's Withholding Allowance Certificate) or its equivalent, at the discretion of the employer. While the Federal Form W-4 contains spaces for all of the Federally-mandated information, it does not contain spaces for additional information that a state may require (such as date of birth or date of hire). Employers are free to develop their own forms and should note that several states have developed forms of their own for employers to use.

**Delivery.** New hire reports may be transmitted on paper or magnetic media (via first-class mail), or they may be transmitted by electronic means. Many states accept fax transmissions, internet filing, private delivery services and other means of reporting.

**Penalties.** Federal law allows states to assess fines for an employer's failure to report its newly-hired employees. Standard fines may not exceed \$25 for each employee the employer fails to report. But, if the failure to report is due to a conspiracy between employer and employee, the fine may be \$500 per employee.

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## WHAT MAKES A PERSON PERFORMING SERVICES A STATUTORY EMPLOYEE OR A STATUTORY NON-EMPLOYEE?

Before one can know how to treat payments made for services performed, it is necessary to determine the business relationship existing between the payer and the person performing the services. Most commonly, the relationship is that of employee or independent contractor, but two other categories also exist and have significant payroll tax requirements.

### Statutory Employee

One such relationship is that of STATUTORY EMPLOYEE. By statute, an independent contractor under the common law rules, may be treated as an "employee" for certain employment tax purposes if the worker falls within any one of the following **four categories**:

- 1.) **Agent-commission drivers** -- for example, a driver who distributes beverages (other than milk) or meat, vegetable, fruit, or bakery products; or who picks up and delivers laundry or dry cleaning, if the driver is the payer's agent or is paid on commission.
- 2.) **Life insurance sales agents** -- a full-time sales agent whose principal business activity is selling life insurance and/or annuity contracts, primarily for one company.
- 3.) **Home workers** -- an individual who works at home on materials or goods that the payer supplies (which are later returned to the supplier or other designated person), under work specifications furnished by the payer.
- 4.) **Traveling and city salespersons** -- persons working full-time to solicit orders from wholesalers, retailers, contractors, or operators of hotels, restaurants, or other similar establishments. The goods sold must be merchandise for resale or supplies for use in the buyer's business operation. The work performed must be the salesperson's principal business activity.

For workers in these four categories, the payer must withhold Social Security and Medicare taxes from the wages of the STATUTORY EMPLOYEE if **all three** of the following conditions apply:

- The service contract states or implies that substantially all the services are to be performed personally by the statutory employee.
- The statutory employee does not have a substantial investment in the equipment and property used to perform the services (other than an investment in transportation facilities).
- The services are performed on a continuing basis for the same payer.

For FUTA tax, the STATUTORY EMPLOYEE is treated the same as for Social Security and Medicare taxes, except that workers in categories 2.) and 3.) above are excluded. Thus, any individual who is employed under categories 1.) or 4.) is an employer for FUTA tax purposes and subject to FUTA tax.

Importantly, the payer should not withhold Federal income tax from the wages of STATUTORY EMPLOYEES. However, the payer must furnish a Form W-2, and check "statutory employee" in box 13. Payments to the employee are considered "other compensation" and show in box 1. Social Security wages should be shown in box 3 and Medicare wages in box 5. Withheld Social Security tax displays in box 4 and Medicare tax in box 6.

**Statutory Non-employee**

Meanwhile, there are two categories of STATUTORY NON-EMPLOYEE workers who are given a different kind of special treatment for payroll tax purposes: **direct sellers** and **licensed real estate agents**. They are treated as self-employed for all Federal tax purposes, including income and employment taxes, IF:

1.) Substantially all payments for their services as direct sellers or real estate agents are directly related to sales or other output, rather than to the number of hours worked, and

2.) Their services are performed under a written contract providing that they will not be treated as employees for Federal tax purposes.

The term **direct sellers**, as used here, needs some clarification. Direct sellers include persons falling within any of the following three groups:

1.) Persons engaged in selling (or soliciting the sale of) consumer products in the home or place of business other than in a permanent retail establishment.

2.) Persons engaged in selling (or soliciting the sale of) consumer products to any buyer on a buy-sell basis, a deposit-commission basis, or any similar basis prescribed by regulations, for resale in the home or at a place of business other than in a permanent retail establishment.

3.) Persons engaged in the trade or business of delivering or distributing newspapers or shopping news (including any services directly related to such delivery or distribution).

Note that the I.R.S. considers direct selling to include the activities of individuals who attempt to increase the direct sales of their direct sellers, and who earn income based on the productivity of their direct sellers. Such activities include providing motivation and encouragement; imparting skills, knowledge, or experience; and recruiting.

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**SOLE PROPRIETORSHIP**

This is the most common form of business entity, chosen by perhaps 70% of all American business employers. Many who are just starting a business choose this form until it becomes practical or necessary to enter into a partnership or to incorporate.

A sole proprietorship is a business owned and operated by one person, although it may have employees, as well. Importantly, while the employees may be paid through a payroll process, the sole proprietor is not eligible to be paid through payroll. The logic is that as the "employer," the sole proprietor is paid from the profits (or losses) of the enterprise. The sole proprietor is considered to be self-employed.

Sole proprietorship is the least expensive and least regulated business legal structure, and can generally be established simply by registering the company's name (filing a D.B.A.) and obtaining a business license. All decision making is vested in the sole proprietor, who has total responsibility and control. Note, the sole proprietor also pays Self-Employment Tax.

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**ALL OF US HAVE SOME "DE MINIMIS" FRINGE BENEFITS ----- Can You Identify Them?**

Any employer-provided property or service having a value so small that accounting for it would be unreasonable or administratively impracticable, may be excluded from income as a "de minimis" fringe benefit. The frequency with which the benefit is provided is a factor to be considered when determining that the value is small. Examples of "de minimis" benefits include:

- An occasional ticket to the theater or a sporting event
- Occasional meal money or cab fare when employees are required to work overtime, provided the payments are not calculated on the basis of the number of hours worked
- Occasional typing of personal letters or personal use of office copying machines
- Occasional parties and picnics for employees, coffee and doughnuts
- The value of meals provided at a reduced price when provided at an employer-operated eating facility whose revenues at least equal its operating costs.

However, SEASON tickets to sporting or theatrical events, free use of a company car to commute to work, or the use of an employer-owned or leased boat, hunting lodge, etc. for a weekend, may not be considered "de minimis" benefits. Therefore, withholding for Federal income tax, Social Security and Medicare taxes, and the employer-paid FUTA tax, apply to the fair market value.

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**CALIFORNIA, MASSACHUSETTS AND OREGON INCREASE MINIMUM WAGE RATES**

Beginning 1/1/2007, the **California** minimum wage rate will be increased from \$6.75 to \$7.50 per hour. Then, on 1/1/2008, California will increase the state minimum wage rate from \$7.50 to \$8.00 per hour. California does not recognize tip credit, so California employers must pay tipped employees the same minimum cash wage as non-tipped employees. The youth sub-minimum wage rate will continue at 85% of the regular minimum wage rate.

Starting 1/1/2007, **Massachusetts** will make the first of two increases to the state minimum wage rate.

---- effective **1/1/2007**:

the regular rate increases from \$6.75 to \$7.50 per hour, and the minimum cash wage for tipped employees will remain unchanged at \$2.63 per hour. Therefore, the maximum tip credit will increase from \$4.12 to \$4.87 per hour.

----effective **1/1/2008**:

the regular rate increases from \$7.50 to \$8.00 per hour, and the minimum cash wage for tipped employees will remain unchanged at \$2.63 per hour. Thus, the maximum tip credit will increase from \$4.87 to \$5.37 per hour.

Beginning 1/1/2007, the **Oregon** minimum wage rate will be increased from \$7.50 to \$7.80 per hour. Because Oregon does not recognize tip credit, Oregon employers of tipped employees must pay the same minimum cash wage as to non-tipped employees. Oregon has no training or youth sub-minimum wage rate.

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