

## Featured story

- ▶ What are the payroll tax withholding rules for nonqualified deferred compensation?



# State Year- End Essentials

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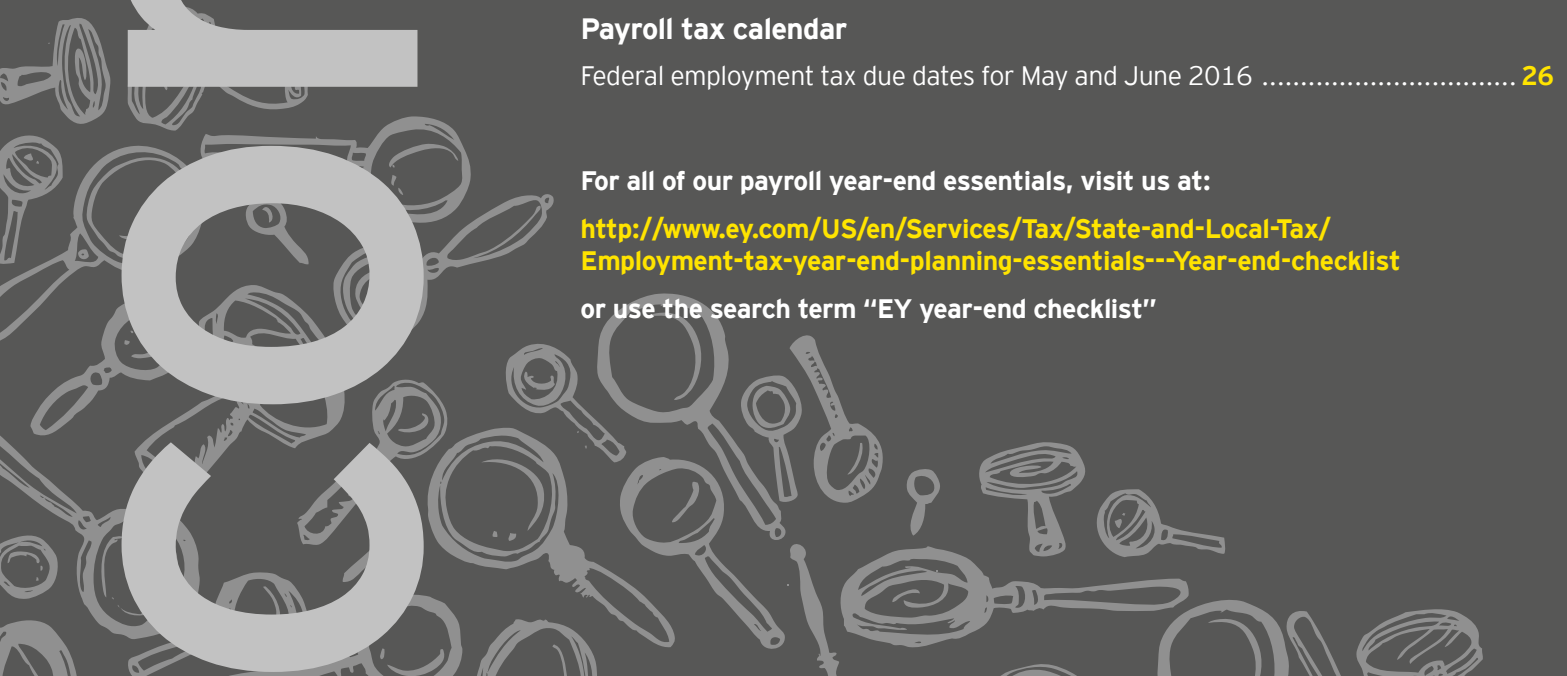
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# From the editor



**Debera Salam, CPP**  
Editor-in-Chief  
*Payroll Perspectives from EY*

As businesses increasingly seek to provide incentives that are tied to market performance and length of service, nonqualified deferred compensation and equity plans have grown in popularity. At the same time, the changing regulatory framework governing the operation of these plans has amplified compliance concerns.

From plan design to taxation and reporting, consideration must be given to a number of laws and regulators, including the Internal Revenue Service (IRS), the U.S. Department of Labor, the Financial Accounting Standards Board, and their state and local counterparts. Consequently, successful management of these plans requires people with knowledge and experience in a variety of disciplines and the skillful coordination of their efforts. For instance, tax withholding and reporting errors can occur if there is a breakdown in communicating certain plan details to the payroll department.

In this edition of *Payroll Perspectives*, we have brought together our professionals experienced in tax, compensation and benefits, and employment tax to provide their insights on the payroll withholding rules that apply to nonqualified deferred compensation.

Warmly,

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## Many tax and reporting errors can be avoided

The accuracy of payroll withholding calculations depends largely on the configuration settings for each of your earnings and deductions codes. That's why a regular review of these settings is so important.

If you are looking for a holistic approach to confirm your tax settings, you might want to consider Ernst & Young LLP's new and innovative **TaxAbility™**. Learn more about the tool and services [here](#).



# FICA tax obligations and the importance of timing

## Meet the authors



**Deborah Spyker**  
Ernst & Young LLP  
*Executive Director*  
Employment Tax Advisory Services  
[deborah.spyker@ey.com](mailto:deborah.spyker@ey.com)



**Debera Salam**  
Ernst & Young LLP  
*Director Payroll Information Services*  
Employment Tax Advisory Services  
[debera.salam@ey.com](mailto:debera.salam@ey.com)



**Bing Luke**  
Ernst & Young LLP  
*Senior Manager*  
People Advisory Services  
[bing.luke@ey.com](mailto:bing.luke@ey.com)



**Jason S. French**  
Ernst & Young LLP  
*Senior Manager*  
People Advisory Services  
[jason.french@ey.com](mailto:jason.french@ey.com)



**Clark Good**  
Ernst & Young LLP  
*Senior*  
People Advisory Services  
[clark.good@ey.com](mailto:clark.good@ey.com)

FICA taxes, paid by both the employer and the employee, include the 6.2% Old Age, Survivors and Disability Insurance (OASDI) – or “Social Security” – tax and the 1.45% Hospital Insurance (HI) – or “Medicare” – tax. Social Security tax is capped and for 2016 applies only to the first \$118,500 of covered wages. There is also a 0.9% Additional Medicare Tax, paid only by employees, that employers are required to withhold from Medicare wages paid to an employee in excess of \$200,000 in the year.

## Special-timing rule

Certain nonqualified deferred compensation (NQDC) plans provide benefits that, while payable at a later date, must be recognized as FICA wages at an earlier date. This early inclusion of deferrals in FICA wages, termed the special-timing rule, not only is required but also may benefit plan participants and employers. Recent court decisions further highlight the importance of employers' adherence to this rule, as explained later. (*IRC* §3121(v)(2); *Treas. Reg.* 31.3121(v)(2)-1(d)(1)(ii)(B).)<sup>1</sup>

The special-timing rule pertains to plans in which the employee has a legally binding right to compensation in a later year that has not been constructively or actually paid in the current year. Examples include certain salary continuation benefits, a restricted stock unit plan, phantom equity (an arrangement where the employee receives the right to receive a fixed payment equal to the value of a specified number of shares of employer stock), Supplemental Executive Retirement Plans and Top Hat Plans.

Stock options, stock appreciation rights or other stock value benefits may not be included in the definition of NQDC for purposes of the special-timing rule under the Treasury Regulations.

The special-timing rule requires that the amounts deferred be recognized as FICA taxable in the later of:

- (1) The date services are performed
- (2) The date as of which there is no substantial risk of forfeiture

<sup>1</sup> IRS Reg. §31.3121(v)(2)-1(d)(1)(ii) (discussed later) provides rules for including nonqualified deferred compensation in taxable wages if it was not taken into account at vesting.

Benefits accrued under a nonqualified deferred compensation arrangement are generally subject to federal income tax and federal income tax withholding at the time actually or constructively paid (typically upon distribution). But under the special-timing rule, they are generally subject to FICA tax earlier, when the amount is vested.

## Non-duplication rule

Under the so-called non-duplication rule, once a deferred amount is taken into account under the special-timing rule, neither that amount nor the income attributable to that amount will be subject to FICA taxes at the time of distribution. Thus, benefits accrued under a nonqualified deferred compensation arrangement are generally subject to federal income tax and federal income tax withholding at the time actually or constructively paid (typically upon distribution). But they are subject to FICA taxes at that time only to the extent not previously taken into account as FICA wages under the special-timing rule. If FICA tax obligations are properly met under these rules, any subsequent NQDC benefit distributions (including any subsequent earnings thereon) are exempt from FICA tax pursuant to the non-duplication rule. (*IRC §3121(v)(2)(B)*; *Treas. Reg. §31.3121(v)(2)-1(a)(2)(iii)*.)

If the employer fails to subject the NQDC deferral to FICA tax at the time of vesting, and the Form 941 statute of limitations is closed for making a correction, the employer is subject to the general-timing rule and is required to withhold FICA tax (including Social Security up to the annual limit) on each future NQDC distribution and any earnings thereon, such as interest. (*IRC §31.3121(v)(2)-1(d)(1)(ii)*.)



# Current litigation involving the timing of FICA tax



Recently, participants have raised legal challenges to how employers have administered NQDC plans as it relates to optimizing their FICA tax obligations. In 2015, a US District Court found that an employer violated the plan contract by improperly applying the special-timing rule when determining the FICA tax owed. The court ruled that failure to properly withhold FICA taxes at the time of the deferral subjected the participants to more taxes than would have been owed if the plan had paid taxes as they were due. Accordingly, the employer was held liable for damages for the error. (*Davidson v. Henkel Corporation, DC MI, 115 AFTR 2d 2015-369, 1/6/15.*)<sup>2</sup>

In a new development demonstrating the risk of improperly applying payroll tax rules to nonqualified deferred compensation, a US District Court held in 2015 that an employer violated the plan's contract by improperly applying the special-timing rule when determining the FICA tax owed.

Besides the litigation concern, this case highlights the potential benefits associated with early inclusion under the special-timing rule. When an employer includes deferrals as wages, the non-duplication rule provides that this deferral will not be subject to future FICA taxes. This includes any reasonable increase in benefit value due to the passage of time, such as interest, earnings or survivorship. If the deferrals are not included in FICA wages when earned, all such increases over time may be subject to FICA taxes when they are paid.

Finally, cumulative FICA taxes may be significantly less if paid according to the special-timing rule. Currently, the employer and employee each pay the Social Security tax of 6.2% up to the taxable limit (\$118,500 in 2016) and Medicare tax of 1.45% on all earnings. For the employee, an Additional Medicare Tax of 0.9% may also apply to wages in excess of \$250,000 (married filing jointly) or \$200,000 (single). (Note that the employer withholds Additional Medicare Tax when cumulative annual wages exceed \$200,000, regardless of the employee's marital status. The employee settles any adjustments on Form 8959, *Additional Medicare Tax*.)

Depending on their facts and circumstances, employees vested in NQDC plans may have already paid a significant portion of the Social Security tax obligation in years prior to distribution and likely would not be subject to any additional FICA taxes on increases in their account balance at distribution.

<sup>2</sup> The ruling in *Henkel* was not reached on the basis of tax law, but rather the specifics of the plan's contract. Nonetheless, had the mechanics of taxation been properly applied under the special-timing rule, the employees would not have asserted damages from the plan's operation.

# The risk of withholding too much federal, state and local income tax

Employers frequently ask whether there is any risk in computing federal, state and local income tax withholding in excess of the amounts prescribed by the governing income tax withholding regulations, particularly on large sums such as those connected with NQDC.

Businesses may prefer to use higher income tax rates if, for instance, they are estimating payroll withholding in advance of a vesting or distribution (e.g., when a third party is making distributions on behalf of the employer). Employees may also request additional withholding because they expect their income tax withholding to fall short of their estimated annual liability.

In arriving at a policy decision about income tax withholding calculations on NQDC, businesses must address various considerations, as discussed below.

**Before honoring an employee's request to withhold more income tax than required by law or regulation, employers should consider the risks of engaging in this practice.**

## ► Federal income tax withholding rules:

The IRS sets forth the regular and alternative income tax withholding calculations that employers are required to use. (See *IRC §3402 and the IRS-related regulations*.)

Special rules apply to supplemental wages, which include NQDC. If an employee's annual supplemental wages are below \$1 million, the employer may use the flat income tax withholding rate of 25%, provided that income tax was withheld from wages paid to the employee in the current or previous year. If the employee's wages exceed \$1 million, a flat income tax rate of 39.6% must be used, regardless of a Form W-4 claiming exemption from federal income tax withholding.

Where the 25% or 39.6% flat rate does not apply, the employer must compute federal income tax withholding on the aggregate of the supplemental wage and the last regular wage payment using IRS-prescribed withholding methods tied to the employee's Form W-4.<sup>3</sup>

<sup>3</sup> At various times, federal legislation has been enacted to limit a state's ability to impose income tax on out-of-state businesses and individuals. For instance, under [P.L. 104-95](#), certain distributions from nonqualified pension plans are protected from state income tax when the recipient is no longer a resident of the state.

- **Employer risk.** Although no employer penalties are imposed for withholding federal income tax in excess of IRS-prescribed amounts, consideration should be given to the hardship that excess income tax withholding can place on employees. (*IRC §31.3403-1; IRC §6656*.)

In this regard, employees could take action against the employer for any damages incurred as a result of income tax withholding variances. Damages could include, for instance, loss of investment income on the excess income tax withholding or recovery of tax preparer fees in seeking a refund from the IRS or other taxing authority.

Reputational risk is also a consideration should employees make public the company's inaccurate withholding calculations.

- **Employee risk.** In an IRS Information Letter, the agency opined that extra withholding may not be performed (for example, a 39.6% rate when the cumulative supplemental wages are less than \$1 million). If an employee wants additional withholding performed on cumulative supplemental wages of less than \$1 million, the employee must submit a new Form W-4 requesting an additional flat dollar amount of withholding. The employee would then have to submit a second Form W-4 to revert income tax withholding to the amount desired from subsequent regular wage payments. (*Information Letter 2012-0063*.)

**The IRS mentioned in Information Letter 2012-0063 that in the event income tax withholding exceeds that required by regulation, it may deny the employee a withholding credit at the source under IRC §31. Thus, the employee could incur estimated payment penalties.**

Information Letter 2012-0063 does not discuss the penalty risk that would occur for performing additional voluntary withholding at a flat percentage rate. But there is some risk, perhaps remote, that the IRS would deny the employee a withholding credit at the source under IRC §31. Thus, the employee could incur estimated payment penalties. Income tax withholding under IRC §31 is treated as paid ratably throughout the calendar year, whereas estimated tax payments are required to be made quarterly and to meet the taxpayer's quarterly tax liability.

# The risk of withholding too much federal, state and local income tax

Continued

## ► IRC §409A considerations

NQDC plans must meet the requirements of IRC §409A, particularly the prohibition on accelerated payments under IRC Reg. §1.409A-3(c).

Under IRC §409A, an exemption to the acceleration-of-payment prohibition holds that the employee is allowed to take a distribution at the time of vesting to provide funds to cover FICA tax owed. Essentially, the FICA tax is viewed as a taxable distribution from the plan that is then subject to income tax. Thus, IRC §409A also permits a distribution to meet the federal, state and local income tax requirements due on the pyramiding wages.

This exception is limited in that the accelerated portion cannot exceed the underlying FICA tax and the “income tax withholding related to such” amount.

Should income tax withholding materially exceed the regulatory guidelines, employees could be due a refund of the excess when filing their income tax returns. Consequently, there is the risk that excessive income tax withholding could indirectly make funds available to the employee before the distribution year and run afoul of the accelerated-payment rules of IRC §409A.

Although IRC §409A does not appear to apply any standard in calculating income tax withholding (such as limiting the tax to the statutory minimum), withholding in excess of the applicable wage withholding guidelines could nonetheless be viewed as an accelerated payment in violation of IRC §409A. (See page 5 for the federal income tax withholding rates on supplemental wages.)

It is emphasized that the risk of excess income tax withholding applies only in connection with the special-timing rule, when a distribution is made only to meet a FICA tax obligation.

Although IRC §409A does not appear to apply any standard in calculating income tax withholding (such as limiting the tax to the statutory minimum), withholding in excess of the applicable wage withholding guidelines could nonetheless be viewed as an accelerated payment in violation of IRC §409A.

- **Restricted stock unit (RSU) plans.** RSU plans are often considered NQDC and are generally subject to FICA tax on the vesting date, while federal, state and local income taxes are triggered when the RSU is paid out. These two dates (the FICA tax and income tax reporting dates) are often not the same because RSU plans typically give the employer a specified period to physically pay out the award after the vesting date.

A rule of administrative convenience can be used to “marry up” these two dates. Thus, an amount vesting in a calendar year can be taken into account at a later date during the same calendar year (e.g., the payment date). The lag rule for reporting can also be used to push the FICA reporting date forward (up to three months) to match the income tax reporting date. With the lag method, an interest component must be added to the amount reported as FICA wages. (*Treas. Reg. §31.3121(v)(2)-1(e)(5)*; *Treas. Reg. §31.3121(v)(2)-1(f)(3)*.)

RSU plans can also trigger discrepancies in the timing of FICA and income tax where the plan includes a retirement-eligible provision. Under a retirement-eligible provision, in the year an employee reaches the retirement-eligible age, the value of the stock grants is treated as vested for FICA and FUTA purposes. But such shares are not subject to federal income tax or federal income tax withholding until distributed at a later date. This RSU scenario is most often the result of an individual becoming eligible for a defined retirement benefit, such as meeting an age and years-of-service threshold. In this case, a FICA distribution is made from the plan, and the employer’s computation of income tax withholding, if in excess of regulatory guidelines, is subject to the various risks we discuss above and later as it pertains to equity accounting.

## ► Equity accounting

The Financial Accounting Standards Board (FASB) issued an Accounting Standards Update (ASU) that will change certain aspects of accounting for share-based payments to employees. (*ASU 2016-09, Improvements to Employee Share-Based Payment Accounting*.) The guidance is effective for public business entities for fiscal years beginning after December 15, 2016, and interim periods within those years. For all other entities, it is effective for fiscal years beginning after December 15, 2017, and interim periods within fiscal years beginning after December 15, 2018. Early adoption is permitted, but all the guidance must be adopted in the same period.



The guidance will increase the amount an employer can withhold to cover income taxes on awards and still qualify for the exception to liability classification for shares used to satisfy the employer's statutory income tax withholding obligation (i.e., the employer repurchases some of the employee's shares and uses the employee's cash proceeds from the repurchase to pay income taxes it is obligated to withhold on the employee's behalf). An employer with a statutory FICA and income tax withholding obligation will be allowed to withhold shares with a fair value up to the amount of tax owed using the maximum statutory tax rate in the employee's applicable jurisdiction(s). The guidance allows an entity to determine only one maximum rate for all employees in each jurisdiction, rather than a rate for each employee in the jurisdiction. (See *EY FASB alert No. 2016-15, April 28, 2016.*)

**Recent FASB guidance increases the amount an employer can withhold to cover FICA and income taxes on share-based awards and still qualify for the exception to liability classification for shares used to satisfy the employer's statutory income tax withholding obligation.**

It is important to note that the term "statutory minimum withholding rate" is not defined under Subchapter C of the Internal Revenue Code (the employment tax code and regulations). As noted above, an employer has the choice of withholding at the flat 25% supplemental rate or the Form W-4 rate for cumulative supplemental wages under \$1 million and must withhold at the mandatory 39.6% rate for cumulative supplemental wages over \$1 million. As compared with the flat 25% rate, cumulative supplemental wages of less than \$1 million that are subjected to the regular withholding methods will generally result in more withholding because of the graduated nature of those tax rates. Accordingly, the 25% rate would generally be considered the minimum withholding rate.



# What you can do

Employers should carefully review when they are collecting and remitting FICA taxes for all their nonqualified deferred compensation plans. If they discover that FICA taxes were not taken into account at the time of vesting, and the statute of limitations has not expired, the FICA wages and taxes should be reported and paid under the special-timing rule using Form 941-X. Keep in mind that adjustments timely reported on Form 941-X carry no interest or penalty.

It is also important to carefully review the terms of NQDC plans to confirm they are properly administered. Employees can bring costly suits against the employer for plan administration failures, including those that result in the erroneous timing or calculation of withholding taxes and reporting of wages on Form W-2.

Finally, careful consideration must be given to federal, state and local income tax withholding processes and methods, even if a third party is tasked with making plan distributions. In working with a number of clients, we have observed that income tax is sometimes significantly understated, resulting in an employer liability for underpayment and penalties. Even when withholding calculations are consistently too high, businesses must carefully assess the various risks we have discussed in this guide.

## Nonqualified deferred compensation

Six payroll tax questions to ask

1

### Special-timing rule

Are you timely and accurately including vested plan amounts in FICA wages?

2

### FICA-only distributions

Are you meeting the federal, state and local income tax requirements on FICA-only distributions?

3

### General-timing rule

If you failed to include vested amounts in FICA wages, what is your remediation plan?

4

**Income tax withholding**

What are the federal, state and local rules for calculating income tax withholding?

5

**Nonresident income tax**

Where is the distribution required to be sourced for income tax purposes, taking into account work locations during the holding period?

6

**Form W-2 reporting**

Does special federal or state reporting apply, such as box 11?



# How we can help

Our People Advisory Services and Employment Tax Advisory Services teams can help you and your client assess risk and achieve compliance with the payroll tax requirements for your NQDC plans.

## People Advisory Services

- ▶ Determine whether certain nonqualified deferred compensation plans fall under the special-timing rule
- ▶ Identify when benefits are reasonably ascertainable, including assessing whether various optional forms constitute subsidized options
- ▶ Review plan documents to verify that they clearly define both the proper expectation about participant benefit levels and the responsibility for managing tax consequences
- ▶ Help with key considerations involved in the calculation of FICA taxes, such as the selection of “reasonable” assumptions, avoidance of duplication of taxes through application of the non-duplication rule and the assessment, when applicable, of voluntary early inclusion strategies

## Employment Tax Advisory Services

- ▶ Review payroll tax and reporting configuration settings for earnings and deduction codes, including compliance with state and local payroll tax rules using our TaxAbility™ tool
- ▶ Analyze employment tax returns and information statements and help prepare amended federal, state and local returns and information statements
- ▶ Assist in risk controversy, including voluntary disclosures with state and local taxing authorities and audit defense services
- ▶ Allocate NQDC, equity and other trailing compensation for multi-state and short-term business traveler employees

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## Ernst & Young LLP contacts

### People Advisory Services

**Megan Alessi**  
+1 213 977 3368  
[megan.alessi@ey.com](mailto:megan.alessi@ey.com)

**Tanner Coulter**  
+1 214 969 0866  
[tanner.coulter@ey.com](mailto:tanner.coulter@ey.com)

**Kevin Hacker**  
+1 215 448 5000  
[kevin.hacker@ey.com](mailto:kevin.hacker@ey.com)

**Helen Morrison**  
+1 202 327 7016  
[helen.morrison@ey.com](mailto:helen.morrison@ey.com)

**Mike Schoonmaker**  
+1 212 773 6014  
[michael.schoonmaker@ey.com](mailto:michael.schoonmaker@ey.com)

**Rachael Walker**  
+1 212 773 9180  
[rachael.walker@ey.com](mailto:rachael.walker@ey.com)

### Employment Tax Advisory Services

**Jennie DeVincenzo**  
[jennie.devincenzo@ey.com](mailto:jennie.devincenzo@ey.com)  
+1 732 516 4572

**Ken Hausser**  
[kenneth.hausser@ey.com](mailto:kenneth.hausser@ey.com)  
+1 732 516 4558

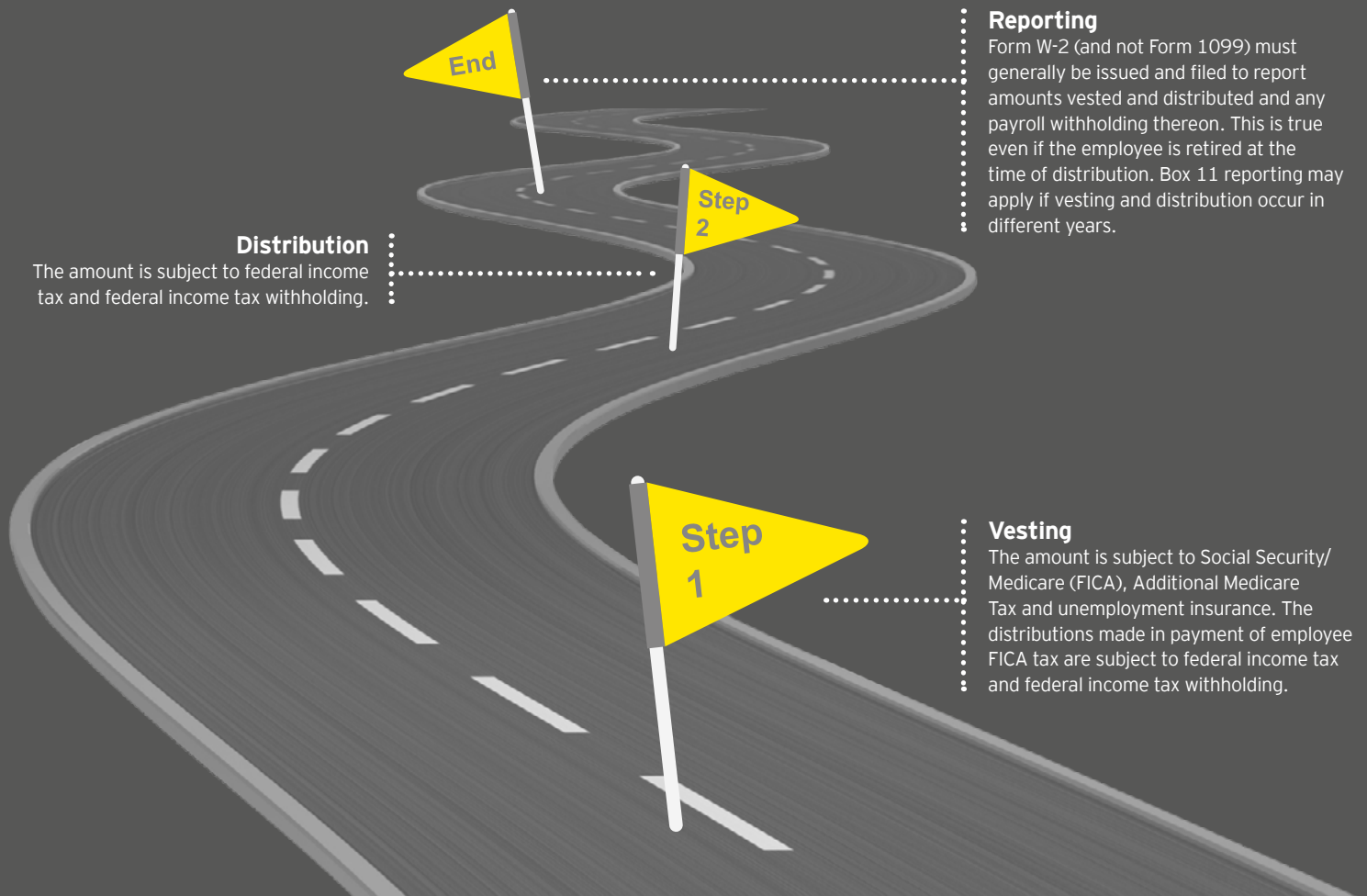
**Kristie Lowery**  
[kristie.lowery@ey.com](mailto:kristie.lowery@ey.com)  
+1 704 331 1884

**Deborah Spyker**  
[deborah.spyker@ey.com](mailto:deborah.spyker@ey.com)  
+1 720 931 4321

**Debera Salam**  
[debera.salam@ey.com](mailto:debera.salam@ey.com)  
+1 713 750 1591

# Nonqualified deferred compensation

## Federal payroll tax timeline



# Health Savings Account limits for 2016 and 2017

## Time to review HSA and other employee health spending account benefits

Plans eligible for Health Reimbursement Arrangements (HRAs) and HSAs constitute “consumer-driven” health plans (CDHPs) because they give employees the choice of electing plan options that best meet their projected out-of-pocket medical expenses. CDHPs also raise payroll challenges because the rules governing each of these reimbursement account options – HRAs, HSAs, Flexible Spending Arrangements (FSAs) and Medical Savings Accounts (MSAs) – are unique in their tax treatment and reporting.

How companies name their health plans may not clearly communicate the type of medical reimbursement vehicle that applies, causing time-consuming and potentially costly errors in payroll system configurations.

To avoid year-end reporting complications, now is a good time to review employee elections and how they are being handled in your payroll system.

For our special report on health spending accounts, click [here](#).

In *Rev. Proc. 2016-28*, the IRS announced the 2017 inflation adjustments that will apply to Health Savings Accounts (HSAs) under IRC §223 effective for calendar year 2017.

Health Savings Account limit type	2016	2017
<b>Contribution *</b>		
Self (IRC §223(b)(2)(A))	\$3,350	\$3,400
Family (IRC §223(b)(2)(B))	\$6,750	\$6,750
<b>Out-of-pocket</b>		
Self (IRC §223(c)(2)(A))	\$6,550	\$6,550
Family (IRC §223(c)(2)(A))	\$13,100	\$13,100
<b>Deductible (high-deductible health plan)</b>		
Self (IRC §223(c)(2)(A))	\$1,300	\$1,300
Family (IRC §223(c)(2)(A))	\$2,600	\$2,600

\* An additional contribution of \$1,000 is permitted for individuals age 55 and older. Those enrolled in Medicare are not eligible to participate.

## Form W-2 reporting reminder

Employer contributions and employee pretax contributions to HSAs must be reported on Form W-2, box 12, Code W. Employer and employee pretax contributions that, when combined, exceed the annual calendar year limit must be treated as taxable wages and reported in Form W-2, boxes 1, 3 (up to the Social Security limit) and 5. (2016 Form W-2 instructions.)

To avoid excise tax, employees should consider contributions they make directly to their HSA accounts when determining whether the annual contribution limit has been reached. (*IRS Publication 969*.)

# IRS incorrectly assessed late-deposit penalties in connection with Emancipation Day holiday

The Internal Revenue Service (IRS) announced that because of a programming error, deposits made on April 18, 2016, rather than April 15, 2016, were considered late, and failure-to-deposit penalties were assessed. This error affected some monthly and daily deposits of payroll taxes, the IRS said.

Emancipation Day was observed as a federal holiday in Washington, DC, on April 15, 2016. Accordingly, federal payroll deposits were not required to be made until the next business day – April 18, 2016. The programming error resulted in treating some deposits made on April 18 as late and automatically assessing failure-to-deposit penalties.

The IRS is working to resolve the issue and correct the erroneous penalty assessments in the near future. The IRS states that no taxpayer action is required at this time and that those affected will receive correspondence when the issue is resolved.

## Ernst & Young LLP insights

Employers that correctly made federal payroll tax deposits on April 18, 2016, should carefully review their IRS tax accounts to confirm that any erroneous late-deposit penalties are removed.

Businesses that continue to see erroneous penalties may contact Debbie Spyker at [deborah.spyker@ey.com](mailto:deborah.spyker@ey.com) or Debby Salam at [debera.salam@ey.com](mailto:debera.salam@ey.com) for further assistance.



# Change in overtime exemption rules to apply effective December 1, 2016



## How the new overtime rules affect employment tax

Employers should consider the extent these overtime regulations will increase their employment tax expenses.

The unemployment insurance wage base and/or tax rate schedules are tied directly to the average annual wage in some states (e.g., Washington). In these states, higher overall wages could mean a bump in employers' unemployment insurance taxes. (See *EY Payroll NewsFlash*, Vol. 16, #164, 6-25-2015.)

If additional employees are hired to avoid overtime costs, employers should consider the employment tax impact of restarting the wage base for added employees (e.g., Social Security and unemployment/disability insurance).

Other increases in benefit costs, and the related employment tax expense, should also be considered, such as employer matching contributions to qualified retirement plans; higher disability benefits and insurance costs; and increases in other benefits tied to earnings, such as premiums for group term life insurance.

If you have further questions about the employment tax impact of these regulations, contact Kenneth Hausser at [kenneth.hausser@ey.com](mailto:kenneth.hausser@ey.com).

On May 18, 2016, the U.S. Department of Labor issued the long-awaited revised rules governing the exemption from overtime pay that applies to qualified exempt employees. The new requirements take effect December 1, 2016, and are expected to extend overtime pay to 4.2 million employees currently exempt and boost wages by \$12 billion over the next 10 years. (*Email from President Obama*, May 17, 2016.)

Last year, at the behest of President Obama, the Labor Department issued [proposed regulations](#) to increase the minimum salary for exempt workers from \$455 per week (\$23,600 per year) to \$970 per week (\$50,440 per year). It also proposed raising the bright-line test from \$100,000 to \$122,148. (See *EY Payroll NewsFlash*, Vol. 16, #171, 7-1-2016.)

Under the final rule that applies on December 1, the salary threshold for salaried exempt employees will be \$913 per week (\$47,476 per year), double the current amount but slightly less than proposed last year. This salary test will be adjusted for inflation every three years and is expected to rise to \$981 per week (\$51,000 per year) when it is first updated on January 1, 2020.

**Puerto Rico note:** Under proposed legislation [H.R. 5278](#) introduced on May 18, 2016, Puerto Rico employers would be temporarily exempt from these revised overtime rules.

Under the final regulations, and for the first time, in meeting the salary test, up to 10% of bonuses, commissions and incentive payments may be taken into account.

## The bright-line test for highly compensated employees

The bright-line test for meeting the definition of highly compensated employee will also increase on December 1 to \$134,004, significantly higher than the current \$100,000 and more than the \$122,148 proposed last year.

## Exempt employees' duties test

As a result of commentary on the proposed regulations, these final regulations do not change the current duties test.

## Additional guidance is forthcoming

In the near future, the Department intends to release three technical guidance documents to help private employers, nonprofit employers and institutions of higher education comply with the new regulations.

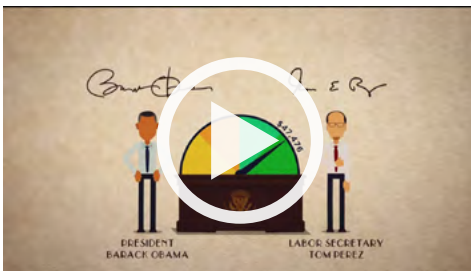


### Ernst & Young LLP insights

The White House states in its [fact sheet](#) that employers have several ways to comply with the new regulations for salaried employees who are not highly compensated (earning less than \$134,044 per year):

1. Increase the pay of exempt employees to at least \$913 per week (\$47,476 per year), taking into account up to 10% of bonuses, commissions and other incentive pay
2. Pay overtime to currently salaried/exempt employees who will earn less than the minimum salary above
3. If the salaries will not increase to the required minimum for employees currently exempt from overtime, reduce their overtime hours (this may require hiring additional employees or adjusting the work schedules of other employees)

Businesses should discuss the wage-hour implications of the new overtime regulations with their legal advisors.



Watch the U.S. Department of Labor video explaining why President Obama directed that the overtime rules be updated.

# More California cities enact local paid sick leave benefits

On April 19, 2016, the Los Angeles City Council [voted](#) to request that the city attorney prepare and present an [ordinance](#) to create a paid sick leave policy for employees in the City of Los Angeles. Under the plan, a city employer would have to provide twice the number of hours of paid sick leave required under the state law.

Under state law, employees must be allowed to take 24 hours (or three days, if the employee regularly works eight or more hours per day) of paid sick leave per year, provided up front by the employer or accrued at a rate of one hour per every 30 hours worked (up to 48 hours can be accrued each year and carried over to the next year).

Under the Los Angeles City Council's recommendations, employees would be entitled to take 48 hours of paid sick leave per calendar year. It must be provided up front by the employer or accrued at a rate of one hour per every 30 hours worked. Accrued leave would carry over to the following year and be capped at 72 hours.

As with the state law, the proposed Los Angeles ordinance would apply to an employee who works in the city for the same employer for 30 days or more within a year. The ordinance would take effect on July 1, 2016, and an employee could use paid sick leave beginning on the 90th day of employment, or July 1, 2016, whichever is later. Employers of 25 or fewer employees would be granted a one-year [delay](#) in the effective date of the ordinance.

## Other California localities that have paid sick leave ordinances

### San Francisco

Under the San Francisco paid sick leave [ordinance](#):

- ▶ An employee accrues one hour of paid sick leave for every 30 hours worked. Whereas the state law allows an employer to limit an employee's use of paid sick leave to 24 hours per year, a San Francisco employee can use however much he or she has accrued.
- ▶ The employee may not start using paid sick leave until 90 days after the start of employment.
- ▶ The cap on accrual is 40 hours for small businesses having fewer than 10 workers and 72 hours for other businesses. The state law provides for a cap of 48 hours, regardless of the size of the employer.
- ▶ The cap is not annual. Whenever an employee's accrued leave drops below the cap because of usage, the employee begins to accrue again; this is called a "floating" cap.

### Oakland

Oakland's ordinance is similar to San Francisco's. Under the Oakland paid sick leave [ordinance](#):

- ▶ An employee working at least two hours per workweek accrues one hour of paid sick leave for every 30 hours worked. Whereas the state law allows an employer to limit an employee's use of paid sick leave to 24 hours per year, an Oakland employee can use however much he or she has accrued.
- ▶ The employee may not start using paid sick leave until 90 days after the start of employment.
- ▶ The cap on accrual is 40 hours for small businesses having fewer than 10 workers and 72 hours for other businesses. The state law provides for a cap of 48 hours, regardless of the size of the employer.
- ▶ The cap is not annual. Whenever an employee's accrued leave drops below the cap because of usage, the employee begins to accrue again.

### Emeryville

Under Emeryville's paid sick leave [ordinance](#):

- ▶ An employee accrues one hour of paid sick leave for every 30 hours worked. Whereas the state law allows an employer to limit an employee's use of paid sick leave to 24 hours per year, an Emeryville employee can use however much he or she has accrued.
- ▶ The employee may not start using paid sick leave until 90 days after the start of employment.
- ▶ There is a cap on accrual of 48 hours for small businesses of 55 or fewer employees and 72 hours for other businesses. The state law provides for a cap of 48 hours, regardless of the size of the employer.
- ▶ The cap is not annual. Whenever an employee's accrued leave drops below the cap because of usage, the employee begins to accrue again.

## Santa Monica

As we reported in *EY Payroll NewsFlash* Vol. 17, #031 (2-9-2016), the city of Santa Monica passed an ordinance at the beginning of the year to require employers to provide paid sick leave starting July 1, 2016. Recently, the Santa Monica City Council voted to postpone the effective date of the ordinance to January 1, 2017, and provide for a phased-in implementation.

Under the Santa Monica [ordinance](#):

- ▶ Employers must comply starting January 1, 2017 (before this date, employers are instructed to comply with state law).
- ▶ An employee accrues one hour of paid sick leave for every 30 hours worked. Whereas the state law allows an employer to limit an employee's use of paid sick leave to 24 hours per year, a Santa Monica employee can use however much he or she has accrued.
- ▶ Accrual limits are as follows:
  - ▶ January 1, 2017: 32 hours for small businesses of 25 or fewer employees; 40 hours for larger businesses
  - ▶ January 1, 2018: 40 hours for small businesses of 25 or fewer employees; 72 hours for larger businesses
- ▶ Employees can carry over accrued sick leave annually (calendar year, fiscal year or hiring date) up to the accrual cap.
- ▶ Employers can provide sick leave at the start of the year as a whole rather than by accrual, as long as this provides leave consistent with the required accrual amounts.

## San Diego

San Diego passed a paid sick leave and minimum wage [ordinance](#) in 2014, but it is on hold until voters decide its fate on June 7, 2016 (see Proposition I on page 107 of the [ballot measures](#)). Under the proposal, an employee would accrue one hour of paid sick leave for every 30 hours worked. Whereas the state law allows an employer to limit an employee's use of paid sick leave to 24 hours per year (with an accrual cap of 48 hours), a San Diego employee could use 40 hours in a benefit year, but employers must allow employees to continue to accrue sick leave hours with no cap.

## Ernst & Young LLP insights

The California state paid sick leave [law](#) does not pre-empt local paid sick leave ordinances, so employers must comply with the law that has the more generous provisions.

The states of California, Connecticut, Massachusetts, Oregon and Vermont, as well as the District of Columbia and numerous other cities, such as New York City, mandate that employers provide paid sick leave.

The president's fiscal year 2017 budget [proposal](#) calls for states to establish paid sick leave programs, providing more than \$2 billion for a Paid Leave Partnership Initiative to help up to five states launch paid family and medical leave programs.

Another trend is the call for paid parental leave. California, New Jersey and Rhode Island currently are the only states that have laws on employee-funded paid parental leave that provide for partial wage replacement for a limited amount of time spent bonding with a new child.

As we reported in the April 2016 issue of *Payroll Perspectives*, a recently enacted New York budget bill provides for employee-funded paid parental leave starting January 1, 2018. The New York program will also provide only partial wage replacement.

As also reported in the April 2016 issue, San Francisco recently passed an ordinance that requires employers to make up the difference between the partial wage replacement under the California Paid Family Leave (PFL) program and the employee's normal weekly wages to employees taking parental leave.

Vermont Senator Bernie Sanders has sponsored a bill to provide paid federal parental leave benefits funded by employee contributions into an insurance fund, such as Social Security ([S. 786](#)).

Legislation to provide for paid family and/or sick leave has been considered in several states – Arizona, Colorado, Connecticut, the District of Columbia, Illinois, Louisiana, Maryland, Massachusetts, Minnesota, New Jersey and Ohio.

# Colorado

## Ballot measure calls for single-payer universal health care program, funded by employer/employee payroll tax

Amendment 69 ([Initiative 20](#)), placed on the November 8, 2016, ballot, would create a single-payer universal health care program. Once fully implemented, *ColoradoCare* would be funded by a \$25 billion-per-year tax increase, collected primarily through employer contributions and employee payroll withholding.

### Funding

To fund the program, the initiative proposes a premium tax on most sources of income, including:

- ▶ Wages, salaries and tips
- ▶ Dividends, interest and rents
- ▶ Business proprietors' income, including farm proprietors' income
- ▶ Capital gains
- ▶ Pensions, annuities and Social Security benefits, to the extent taxed by the state under current law

Initially, the Colorado Department of Revenue would collect transitional operating fund taxes from state residents beginning July 1, 2017, at the following rates: 0.6% of payroll from employers, 0.3% of payroll from employees, and 0.9% from non-payroll income.

The transitional tax would change over to premium tax the month prior to *ColoradoCare*'s assumption of responsibility for health care payments. At that time, the tax rate would increase to 10%, collected as follows: 6.667% of employer payroll; 3.333% of employee payroll; and 10% non-payroll income.

For calendar year 2017, the premium tax on individuals would be limited to incomes of \$350,000 for individual income tax filers and \$450,000 for joint income tax filers, and indexed for inflation in subsequent years.

Employers could choose to pay part or all of the employee's share of the transitional and premium tax. Premium taxes could be increased once per year if voters approve.

See the Initiative 20 [summary](#) for more on the proposed program. See also the *ColoradoCare* [website](#).

### Ballot title

On the ballot, voters will be asked the following:

"Shall state taxes be increased \$25 billion annually in the first full fiscal year, and by such amounts that are raised thereafter, by an amendment to the Colorado Constitution establishing a health care payment system to fund health care for all individuals whose primary residence is in Colorado, and, in connection therewith, creating a governmental entity called *ColoradoCare* to administer the health care payment system; providing for the governance of *ColoradoCare* by an interim appointed board of trustees until an elected board of trustees takes responsibility; exempting *ColoradoCare* from the Taxpayer's Bill of Rights; assessing an initial tax on the total payroll from employers, payroll income from employees, and nonpayroll income at varying rates; increasing these tax rates when *ColoradoCare* begins making health care payments for beneficiaries; capping the total amount of income subject to taxation; authorizing the board to increase the taxes in specified circumstances upon approval of the members of *ColoradoCare*; requiring *ColoradoCare* to contract with health care providers to pay for specific health care benefits; transferring administration of the Medicaid and Children's Basic Health Programs and all other state and federal health care funds for Colorado to *ColoradoCare*; transferring responsibility to *ColoradoCare* for medical care that would otherwise be paid for by workers' compensation insurance; requiring *ColoradoCare* to apply for a waiver from the Affordable Care Act to establish a Colorado health care payment system; and suspending the operations of the Colorado Health Benefit Exchange and transferring its resources to *ColoradoCare*?"

### Proposal faces challenges

News sources and anti-Amendment 69 groups have indicated that Democratic Governor John Hickenlooper, former Democratic Governor Bill Ritter and Republican State Treasurer Walker Stapleton [oppose](#) Amendment 69. The Denver Chamber of Commerce also [opposes](#) the measure.

#### Ernst & Young LLP insights

As we reported previously, Vermont attempted to establish a similar single-payer universal health care program funded by payroll taxes, but state leaders eventually concluded it was too costly. In a January 2015 blog entry, Governor Peter Shumlin [said](#):

"Earlier this week, I made one of the most difficult decisions of my public life when I announced that I cannot support a move to a publicly-financed health care system in Vermont at this time. I have advocated for such a system for much of my public life, but over the past two weeks it has become clear to me that the risks and economic shocks of moving forward at this time are too great."

# Maryland

## Paid sick leave bill passes House, awaits Senate approval

Maryland [H.B. 580](#), recently rejected by the Senate, would require employers with 15 or more employees to provide paid sick leave to employees age 18 or older. Employers with fewer than 15 employees would be required to provide *unpaid* sick leave.

Effective January 1, 2017, an employee who regularly works eight or more hours per week would earn at least one hour of sick leave at the same rate as the employee normally earns for every 30 hours worked. An employer would not be required to allow an employee to earn or carry over more than 56 hours of earned sick leave in a year, use more than 80 hours of earned leave in a year, accrue more than 80 hours at any time, or use earned sick leave during the first 90 calendar days worked or first 480 hours worked, whichever is shorter.

### Eligibility

An "employer" includes the state or local governments and a person who acts directly or indirectly in the interest of another employer with an employee. An "employee" does not include specified independent contractors, specified associate real estate brokers and real estate salespeople, individuals younger than 18 before the beginning of the year, workers in a specified agricultural sector, or construction workers (not including specified employees) covered in a collective bargaining agreement.

### Use and accrual of leave

Earned sick leave would begin to accrue the later of January 1, 2017, or the date that an employee begins employment with the employer.

Earned sick leave could be used to care for or treat the employee's mental or physical illness, injury, or condition; to obtain preventive medical care for the employee or employee's family member; to care for a family member with a mental or physical illness, injury, or condition; and for specified circumstances due to domestic violence, sexual assault, or stalking committed against the employee or the employee's family member.

An employer would not be required to compensate an employee for unused earned sick leave when the employee leaves the employer's employment. An employer who rehires an employee within nine months after leaving employment would be required to reinstate any unused earned sick leave that had accrued at the time of separation unless the employer voluntarily paid out the unused earned sick leave. The bill does not require an employer to modify an existing equivalent paid leave policy or affect specified workers' compensation benefits.

## Notice to employees

An employer would have to notify employees that they are entitled to sick leave. The Maryland Commissioner of Labor and Industry would be required to provide a poster and a model notice that employers could use, including information on earned sick leave and the rights of employees.

### Ernst & Young insights

The bill would have preempted the authority of a local jurisdiction to enact a law on or after January 1, 2016, that regulates sick leave provided by an employer other than the local jurisdiction. Since Montgomery County, Maryland, [passed](#) its paid sick leave ordinance in June 2015, it would appear that the county's requirements would continue to apply should H.B. 580 be enacted. For more information on Montgomery County's paid sick leave requirements, see the September 2015 issue of *Payroll Perspectives*.

Maryland would join California, Connecticut, Massachusetts, Oregon and Vermont, as well as the District of Columbia and numerous other localities, such as New York City, in mandating that employers provide paid sick leave. Several other states (i.e., Colorado, Louisiana and New Jersey) have introduced legislation to require employers to provide paid sick leave.

The president's fiscal year 2017 budget [proposal](#) calls for states to establish paid sick leave programs, providing more than \$2 billion for a Paid Leave Partnership Initiative to help up to five states launch paid family and medical leave programs.



# New Hampshire

## SUI tax rates unchanged for second quarter 2016

The New Hampshire Department of Employment Security announced that the “fund balance reduction” will remain 1.0% for the second quarter 2016. Negative-balanced employers will continue to see a 0.5% inverse rate surcharge added to their state unemployment insurance (SUI) tax rates for the second quarter 2016. As a result, employers will pay at the same SUI tax rates as for the first quarter 2016 and the fourth quarter 2015. (*New Hampshire Department of Employment Security website, April 2016.*)

The fund balance reduction drops the tax rate at most to the minimum of 0.1%. Therefore, employers originally assigned the minimum rate, or close to it, will not see the full 1.0% reduction. Employers registered with the Department’s *Webtax* electronic reporting system can access the rate that will apply each quarter.

### New employer rate

The new employer rate will continue to be 1.7% for second quarter 2016, including the additional 0.2% administrative contribution surcharge.

### Taxable wage base

The taxable wage base continues at \$14,000 for calendar year 2016. (*New Hampshire Department of Employment Security website; RSA §282-A69.*)



## State law provides for reductions when the UI trust fund is strong

A 0.5% reduction in the assigned SUI tax rate is allowed if the state UI trust fund equals or exceeds \$250 million throughout the preceding quarter. A 1.0% reduction is allowed if the trust fund equals or exceeds \$275 million. And a 1.5% reduction is allowed if the trust fund equals or exceeds \$300 million.

## Fund balance reductions resumed in fourth quarter 2014

As we reported previously, a fund balance reduction of 0.5% took effect for the fourth quarter 2014; increased to 1.0% for the first quarter 2015; decreased to 0.5% for the second and third quarters 2015; and increased to 1.0% for the fourth quarter 2015 through the second quarter 2016. Prior to the fourth quarter 2014, a fund balance reduction had not been in effect since the fourth quarter 2008.

## Inverse rate surcharge

An inverse rate surcharge has been added to negative-balanced employers’ tax rates since first quarter 2010 at 1.5%, decreasing to 1.0% for the fourth quarter 2014 and to 0.5% for the first quarter 2015; increasing to 1.0% for the second and third quarters 2015; and decreasing to 0.5% for the fourth quarter 2015 through the second quarter 2016.

## Emergency surcharge

State UI law gives the Commissioner of Employment Security the discretion to add or remove a surcharge based on the trust fund balance.

Because of the economic downturn, a 0.5% emergency surcharge was added to all employers’ tax rates in 2009 to help increase the UI trust fund balance. A second 0.5% surcharge was added in 2010 as the downturn continued to impact the state. New Hampshire borrowed briefly from the federal government in March 2010 when the trust fund was temporarily insolvent but repaid the loan before the end of that year. The first 0.5% surcharge was removed beginning October 1, 2012, and the second was removed as of the fourth quarter 2013.

For more information on SUI taxes in New Hampshire, see the Department’s [website](#).

# New Jersey

## Employers to see decrease in SUI taxes beginning July 1, 2016

Governor Chris Christie [announced](#) that because the state's unemployment insurance (UI) trust fund has continued to have a positive balance of over \$1 billion, employers will save \$200 million in state unemployment insurance (SUI) taxes for fiscal year 2017.

A representative of the New Jersey Department of Labor and Workforce Development confirmed that SUI tax rates for fiscal year 2017 (effective July 1, 2016, through June 30, 2017) will be based on [Schedule D](#), with rates ranging from 0.6% to 6.4%. Schedule E, with rates ranging from 1.2% to 7.0%, has been in effect for several years. The new employer rate will decrease to 3.1% for fiscal year 2017, down from the current 3.4%. (*Telephone conversation, April 21, 2016.*)

### Mailing of fiscal year 2017 rate notices

Fiscal year 2017 tax rate notices are expected to be issued as usual by the first week of August 2016.

### New Jersey's UI trust fund status

New Jersey began borrowing from the federal government in March 2009, with the debt reaching an all-time high of \$2.1 billion in April 2011. As a result, employers saw a FUTA credit reduction of 0.3% for calendar year 2011 and 0.6% for calendar year 2012. The state repaid its federal loan balance in August 2013 but borrowed again on a short-term basis in December 2013 and then repaid this loan on May 1, 2014. As a result, employers did not see a FUTA credit reduction for calendar years 2013-15 and stopped seeing a federal interest assessment beginning with calendar year 2014.

As we reported previously, Department Commissioner Harold J. Wirths [announced](#) in mid-2015 that by the end of May 2015, the UI trust fund had a balance of over \$1 billion, the highest in more than seven years. He stated then that the health of the trust fund was anticipated to begin triggering annual incremental SUI tax rate reductions for employers, projected to amount to SUI tax savings of at least \$1 billion over the next five years.

See the August 2015 issue of *Payroll Perspectives* for more information on the fiscal year 2016 tax rates.



# Ohio

## Workers' compensation rates to decrease effective July 1, 2016; new method applies to successor employers

The Ohio Bureau of Workers' Compensation (BWC) [announced](#) that its Board of Directors approved an 8.6% decrease in overall average rates for the state's private employers beginning July 1, 2016.

The move will decrease projected annual premiums by \$113 million next year, and private employers will pay \$463 million less annually than at the beginning of 2011, representing a combined 28.2% decrease.

"This reduction will add to the \$4.3 billion in rate cuts, rebates and credits Ohio's employers have realized over the past five years," said BWC Administrator/CEO Steve Buehrer. "Since 2011, BWC has moved from being a barrier to success for Ohio's businesses to becoming a partner in economic growth, making life simpler and cheaper for employers."

### Annual premium notice mailed on May 1, 2016 (NEW)

The BWC [announced](#) that the *Notice of Estimated Annual Premium* for the policy year that begins July 1, 2016, would be mailed to employers on May 1, 2016. Employers can also view policy year 2016 information by accessing the installment schedule through the BWC My Policy webpage.

The BWC bases the estimated premium on payroll amounts that a private company previously provided. Employers should review this information for accuracy and notify the BWC at +1 800 664 6292 if the payroll amount is incorrect or the employer anticipates a change in operations that will affect its payroll for the policy period beginning July 1, 2016.

The BWC also reported that the first-ever payroll true-up period is coming July 1, 2016. This new process requires employers to report their actual payroll for the previous policy year and reconcile any differences in premiums paid. Even if an employer's payroll for the year matches the estimate BWC provided or the employer had zero payroll, a true-up report must be completed. The BWC recommends that the true-up be submitted online with a BWC e-account. For information on how to create an e-account, go [here](#). For more information, contact the BWC call center at +1 800 644 6292.

## Assistance for companies acquiring other Ohio businesses

Effective January 1, 2016, the BWC implemented a new method, using the successor methodology developed by the National Council on Compensation Insurance, to determine successorship (transfer of experience and liability) when one Ohio company acquires another. A [fact sheet](#) details the new decision-making process and the factors BWC uses to determine whether the purchase, acquisition or merger will result in a successorship.

Employers that are considering purchasing another business can submit [Form AC-4, Request for Business Transfer Information](#). Submission of the form, which both the successor and predecessor must sign, will allow the BWC to release information on the predecessor to the potential successor.

For more information on workers' compensation in Ohio, see the BWC's [website](#).

## Ruling holds supplemental executive retirement is pension-exempt from Cleveland's income tax

In its recent ruling in *MacDonald v. Cleveland Income Tax Board of Review*, the Ohio Board of Tax Appeals (BTA) reversed the City of Cleveland Income Tax Board of Review's decision and held that amounts reported in box 5 of an individual income taxpayer's Form W-2 attributable to a Supplemental Executive Retirement Plan (SERP) was a pension benefit exempted by the Cleveland Income Tax Ordinance.

The taxpayer was a resident of the City of Shaker Heights and had been employed by a Cleveland-based bank until his retirement at the end of 2006. The taxpayer qualified for benefits under the bank's SERP and elected to receive SERP benefits in 2007. The present value of the SERP benefit was included in Medicare wages (box 5) of the taxpayer's 2006 Form W-2. When the taxpayer filed his municipal income tax returns, he calculated his liability on the amount reported in local wages (box 18) of the Form W-2 (i.e., excluding the SERP benefit). The City of Cleveland recalculated the taxpayer's Ohio local income tax liability by including as taxable income the amount appearing in box 5.



## Oklahoma

In issuing its decision, the BTA was influenced by its prior decision in *MacDonald v. City of Shaker Heights*, which was upheld by the Franklin County Court of Appeals. Ohio Revised Code Sections 718.01(F) and 718.03(A)(2)(c) (which is part of the law authorizing the imposition of Ohio municipal income taxes) provides that cities can only tax “qualifying wages,” which are further defined as those appearing in box 5 of the Form W-2, including amounts attributable to nonqualified deferred compensation plans, unless such plans are specifically exempt under local ordinance.

Cleveland, along with many other Ohio municipalities, does not exempt amounts attributable to nonqualified deferred compensation plans. But the Cleveland ordinance exempts pension benefits from tax and does not limit the exemption to “qualified” pension plans. Based on testimony and other evidence provided, the BTA concluded that the SERP was a pension within the meaning of the local ordinance and that the general inclusion of nonqualified deferred compensation within the local tax base in the Ohio Revised Code does not trump the specific exclusion for pensions under the local ordinance.

### Ernst & Young LLP insights

The City of Cleveland is expected to appeal the BTA’s decision to the Supreme Court of Ohio. If the court takes the case, there may finally be a definitive decision on the treatment of this type of income. Currently, many other cities are actively pursuing taxation of this type of income as they do not believe that the decisions previously discussed are binding on them. Affected taxpayers should continue to monitor this litigation.

### Employers to be required to file annual withholding reconciliation and Forms W-2 beginning with calendar year 2016

Recently enacted legislation ([H.B. 2775](#)) will require that employers electronically file an annual withholding tax reconciliation return and corresponding Forms W-2 by February 28 following the tax year. The change is effective for calendar year 2016, with the annual reconciliation and Forms W-2 due by February 28, 2017.

According to an Oklahoma Tax Commission (OTC) Tax Policy and Research representative, the OTC has no plans to conform to the new federal Form W-2 deadline of January 31. (*Telephone conversation, April 27, 2016.*)

Currently, Oklahoma employers do not have to file an annual reconciliation or Forms W-2. Now, the OTC is stepping up tax fraud prevention efforts by matching employer-supplied Form W-2 data to individual income tax returns.

Employers will be required to file the annual reconciliation form and Forms W-2 electronically over the Oklahoma Taxpayer Access Point [system](#).

Additional information on the new reporting requirement is expected to be posted to the OTC [website](#) later this year.



## Oregon

### For now, penalties will not apply for failure to report in new income tax withholding field

As we reported in the March and April 2016 issues of *Payroll Perspectives*, a new reporting element in Column 6 of paper Form 132, *Unemployment Insurance Employee Detail Report*, as well as an accelerated January 31 Form W-2 due date beginning for calendar year 2016, will be used to prevent future individual income tax fraud.

According to a representative of the Oregon Department of Revenue (DOR), employers were asked to begin reporting the withholding tax per employee as of the first quarter 2016, with reports due May 2, 2016. However, those that were unable to comply will not be assessed penalties for failure to include the new information. (*Telephone conversation, April 20, 2016.*)

For questions about reporting this additional data, contact the DOR at +1 503 945 8100, extension 4, option 4, or the Employment Department at +1 503 947 1544, option 6. Employers may also email questions to [OED\\_Taxinfo\\_User@oregon.gov](mailto:OED_Taxinfo_User@oregon.gov).



## South Carolina

### Employers must file state copies of Forms W-2 by January 31

Recently enacted legislation requires South Carolina employers to submit Forms W-2 to the South Carolina Department of Revenue by January 31, rather than the previous due date of the last day of February. (*H.B. 4328, signed by the governor on April 21, 2016.*)

As we reported in the March 2016 issue of *Payroll Perspectives*, the change is effective upon enactment (making the January 31 Form W-2 due date effective for the filing of calendar year 2016 Forms W-2 in 2017).

Employers submitting 250 or more Forms W-2 must file electronically over the Department's MyDORWAY [system](#).

The bill also changes the due date for [Form WH-1606, South Carolina Withholding Fourth Quarter and Annual Reconciliation Return](#), to January 31.

For more information about withholding tax, see the Department's [website](#), call +1 803 898 5000 or send an email to [withholdtax@dor.sc.gov](mailto:withholdtax@dor.sc.gov).

#### Ernst & Young LLP insights

Passage of this bill aligns South Carolina's Form W-2 deadline with federal legislation enacted under the Protecting Americans from Tax Hikes (PATH) Act of 2015 ([Public Law 114-113](#)). The PATH Act accelerates the federal Form W-2 deadline from February 28 (March 31 for electronically filed forms) to January 31, effective with calendar year 2016 Forms W-2 filed in 2017.

# Virginia

## Law requires electronic filing of Forms W-2 by January 31

Virginia [H.B. 1331](#) codifies the requirement that employers file Forms W-2 electronically by January 31, eliminating inconsistencies between the 2014 Appropriations Act, which contained the provision for the accelerated deadline, and statutory provisions. The bill also codifies a provision in the Appropriations Act that permits employers to request waivers from the electronic filing mandate when such requirements create an unreasonable burden.

Finally, H.B. 1331 codifies the requirement in effect since July 1, 2013, that all employers file all withholding returns and payments electronically.

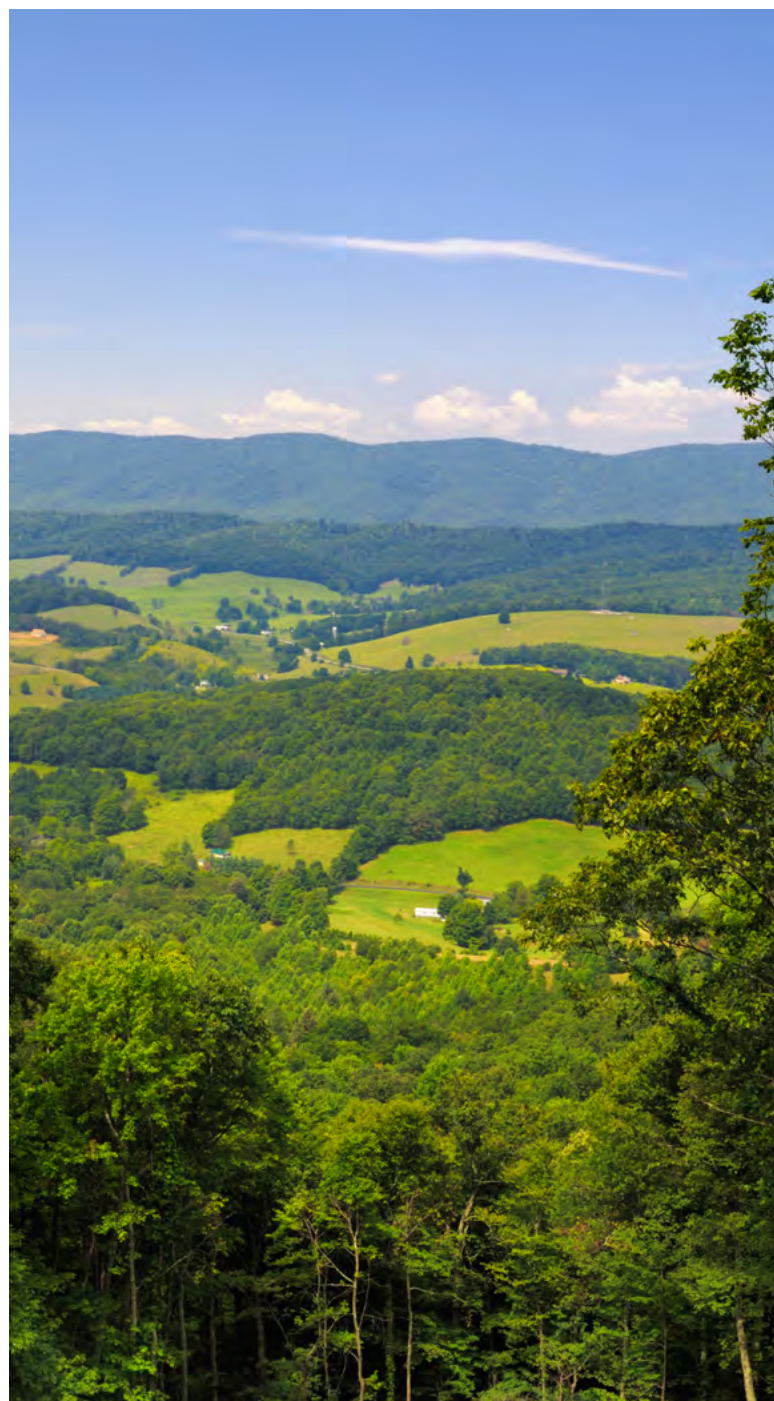
### Employers have been required to file electronically by January 31 for the past two years

As we previously reported, a provision of the Virginia Appropriations Act of 2014 changed the due date for electronically filing Form VA-6, *Employer's Annual Summary of Virginia Income Tax Withheld*, and the associated Forms W-2 and 1099 from February 28 to January 31. This change was effective for the filing of Forms W-2 for calendar year 2014, due January 31, 2015.

#### Ernst & Young LLP insights

According to the bill's [fiscal statement](#), neither the 2014 Appropriations Act nor existing statutory language imposes a penalty for the failure to meet the electronic filing and January 31 due date requirements. As a result, many employers have failed to comply with the January 31 due date and the electronic filing mandate. H.B. 1331 does not add a provision to the applicable statutory language providing for penalties.

Federal legislation enacted under the Protecting Americans from Tax Hikes (PATH) Act of 2015 ([Public Law 114-113](#)) accelerates the federal Form W-2 deadline from February 28 (March 31 for electronically filed forms) to January 31, effective with calendar year 2016 Forms W-2 filed in 2017, and imposes federal penalties for failure to file correctly and timely.



# Federal employment tax due dates for May to June 2016



Due date	Deposit or filing requirement
May 2	File Form 941 for the second quarter 2016. If all deposits were timely made and for the full amount, file Form 941 by the extended due date of May 10. Deposit the federal unemployment insurance tax owed for the first quarter 2016 if the liability exceeds \$500.
May 4	Semiweekly deposit due date for liabilities incurred April 27-29.
May 6	Semiweekly deposit due date for liabilities incurred April 30-May 3.
May 11	Semiweekly deposit due date for liabilities incurred May 4-6.
May 10	Form 4070 is due from employees who received \$20 or more in tips in April. File Form 941 for the first quarter 2016 if all deposits were timely made and for the full amount.
May 13	Semiweekly deposit due date for liabilities incurred May 7-10.
May 16	If the monthly deposit rule applies, deposit the tax for payments made in April.
May 18	Semiweekly deposit due date for liabilities incurred May 11-13.
May 20	Semiweekly deposit due date for liabilities incurred May 14-17.
May 25	Semiweekly deposit due date for liabilities incurred May 18-20.
May 27	Semiweekly deposit due date for liabilities incurred May 21-24.
June 2	Semiweekly deposit due date for liabilities incurred May 25-27.
June 3	Semiweekly deposit due date for liabilities incurred May 28-31.
June 8	Semiweekly deposit due date for liabilities incurred June 1-3.
June 10	Form 4070 is due from employees who received \$20 or more in tips in May. Semiweekly deposit due date for liabilities incurred June 4-7.
June 15	If the monthly deposit rule applies, deposit the tax for payments made in May. Semiweekly deposit due date for liabilities incurred June 8-10.
June 17	Semiweekly deposit due date for liabilities incurred June 11-14.
June 22	Semiweekly deposit due date for liabilities incurred June 15-17.
June 24	Semiweekly deposit due date for liabilities incurred June 18-21.
June 29	Semiweekly deposit due date for liabilities incurred June 22-24.
July 1	Semiweekly deposit due date for liabilities incurred June 25-28.
July 7	Semiweekly deposit due date for liabilities incurred June 29-30.

## Ernst & Young LLP contributors:

- ▶ Debera Salam, CPP, Editor-in-Chief
- ▶ Gregory Carver, National Director, Employment Tax Advisory Services
- ▶ Niko Arhos, National Tax
- ▶ Kyle Lawrence, National Tax
- ▶ Rebecca Bertothy, National Tax
- ▶ Peter Berard, National Tax
- ▶ David Chan, National Tax
- ▶ Alan Mierke, National Tax
- ▶ Gino Petrozzi, National Tax
- ▶ Deborah Spyker, National Tax

## Special contributing editor:

- ▶ Brian Farrington, Esq., Cowles & Thompson, Dallas, Texas

## State desk:

- ▶ Lisa Miedich, State Employment Tax Analyst

## Graphic design and production:

- ▶ Shaun Maxwell, Senior Designer
- ▶ Scott Mitchell, Copy Editor

## Public relations:

- ▶ Lizzie McWilliams  
[lizzie.mcwilliams@ey.com](mailto:lizzie.mcwilliams@ey.com)

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## Ernst & Young LLP Employment Tax Advisory contacts

Anthony Arcidiacono  
[anthony.arcidiacono@ey.com](mailto:anthony.arcidiacono@ey.com)  
+1 732 516 4829

David Germain  
[david.germain@ey.com](mailto:david.germain@ey.com)  
+1 516 336 0123

Peter Berard  
[peter.berard@ey.com](mailto:peter.berard@ey.com)  
+1 212 773 4084

Julie Gilroy  
[julie.gilroy@ey.com](mailto:julie.gilroy@ey.com)  
+1 312 879 3413

Gregory Carver  
[gregory.carver@ey.com](mailto:gregory.carver@ey.com)  
+1 214 969 8377

Ken Hausser  
[kenneth.hausser@ey.com](mailto:kenneth.hausser@ey.com)  
+1 732 516 4558

Bryan De la Bruyere  
[bryan.delabruyere@ey.com](mailto:bryan.delabruyere@ey.com)  
+1 404 817 4384

Jessica Heroy  
[jessica.heroy@ey.com](mailto:jessica.heroy@ey.com)  
+1 704 331 1869

Jennie DeVincenzo  
[jennie.devincenzo@ey.com](mailto:jennie.devincenzo@ey.com)  
+1 732 516 4572

Jimmy Kennedy  
[jimmy.kennedy@ey.com](mailto:jimmy.kennedy@ey.com)  
+1 732 516 4170

Richard Ferrari  
[richard.ferrari@ey.com](mailto:richard.ferrari@ey.com)  
+1 212 773 5714

Nicki King  
[nicki.king@ey.com](mailto:nicki.king@ey.com)  
+1 214 756 1036

Kristie Lowery  
[kristie.lowery@ey.com](mailto:kristie.lowery@ey.com)  
+1 704 331 1884

Debera Salam  
[debera.salam@ey.com](mailto:debera.salam@ey.com)  
+1 713 750 1591

Candylin Mendoza  
[candylin.mendoza@ey.com](mailto:candylin.mendoza@ey.com)  
+1 212 773 3664

Deborah Spyker  
[deborah.spyker@ey.com](mailto:deborah.spyker@ey.com)  
+1 720 931 4321

Chris Peters  
[christina.peters@ey.com](mailto:christina.peters@ey.com)  
+1 614 232 7112

Mike S. Willett  
[mike.willett@ey.com](mailto:mike.willett@ey.com)  
+1 404 817 4637

Matthew Ort  
[matthew.ort@ey.com](mailto:matthew.ort@ey.com)  
+1 214 969 8209

Gino Petrozzi  
[gino.petrozzi@ey.com](mailto:gino.petrozzi@ey.com)  
+1 615 252 2065

Stephanie Pfister  
[stephanie.pfister1@ey.com](mailto:stephanie.pfister1@ey.com)  
+1 415 984 7190