



# PAYROLL CURRENTLY

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## President Bush Vetoes Appropriations Bill With Minimum Wage Increase

As reported previously in PAYROLL CURRENTLY (see [Issue No. 8, Vol. 15](#)), legislation to increase the federal minimum wage was tacked on to H.R. 1591, an unrelated “war supplemental” appropriations bill, in an effort to spur House and Senate negotiators to agree on a package of accompanying business tax incentives. The strategy worked, and a compromise was approved by the House (4-25-07) and Senate (4-26-07) as part of the appropriations bill, which was presented to the President on May 1. However, because the bill was vetoed by the President for reasons related to the conflict in Iraq, the timing of any increase in the federal minimum wage remains in doubt.

The minimum wage and business tax incentives portions of H.R. 1591, as agreed to by House and Senate negotiators, are discussed below. *Note:*

Several provisions in earlier versions of the bill were eliminated, including provisions on professional employer organizations, punitive damages, nonqualified deferred compensation, and enforcement (see PAYROLL CURRENTLY, [Issue No. 4, Vol. 15](#)).

### Fair Minimum Wage Act

The Fair Minimum Wage Act of 2007 would increase the federal hourly minimum wage rate to:

- \$5.85, effective 60 days after the date of enactment;
- \$6.55, effective 12 months after the date of enactment; and
- \$7.25, effective 24 months after the date of enactment.

The bill would also specify an hourly minimum wage rate for the Northern Mariana Islands (NMI) of \$3.55, effective 60 days after the date of enactment. This rate would be increased by \$0.50 an hour (or, if necessary, a lesser amount) every six months thereafter until the minimum wage applicable to the NMI is equal to the federal hourly minimum wage in the U.S.

### Small Business and Work Opportunity Tax Act

The Small Business and Work Opportunity Tax Act of 2007 contains several provisions of interest to payroll professionals.

**FICA tax credit on employee tips.** The bill would freeze the current minimum wage at \$5.15 per hour for the sole purpose of determining the employer’s business tax credit for the employer’s share of social security and Medicare (FICA) taxes paid on employee tips above the minimum wage (IRC §45B).

Under present law, businesses providing, delivering, or serving food or beverages for consumption are allowed

a business tax credit (taken on the employer’s corporate income tax return) for the employer’s share of FICA taxes paid on employees’ tips treated as paid by the employer under IRC §3121(q). The tax credit is available only for FICA taxes paid on tips exceeding any amount treated as wages in meeting the minimum wage required by the Fair Labor Standards Act (the “tip credit” – see *The Payroll Source*®, p. 3-89). Without this provision, if the minimum wage were to increase, the amount of the tax credit would automatically be reduced.

**EXAMPLE:** Under present law, with the minimum wage at \$5.15 and a tip credit of \$3.02, a qualifying employer gets a tax credit for any FICA taxes it pays on reported and unreported tips above the \$3.02 in tips needed to bring a tipped employee’s wages from \$2.13 to \$5.15. So, if the cash wage, tip credit, and other tips reported or deemed paid total \$10 an hour, the employer gets a credit for employer FICA taxes paid on the \$4.85 above the \$5.15 minimum wage.

If the minimum wage rises to \$7.25, the FLSA tip credit will rise to \$5.12 (\$7.25 - \$2.13), and the employer in the example would only get a credit for FICA taxes paid on the \$2.75 above the minimum wage and below the total cash wages and tips (\$10).

Freezing the minimum wage just for purposes of the FICA tax credit would allow the employer the same tax credit it gets now.

**Work Opportunity Tax Credit.** The bill would extend the Work Opportunity Tax Credit for qualified individuals who begin work for an employer after December 31, 2007, and before September 1, 2011.

The bill would also expand targeted

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groups as follows:

- expand the “qualified veterans” targeted group to include individuals with service-related disabilities and (1) having a hiring date not more than one year after being discharged or released from active duty or (2) having been unemployed for six months or more during the one-year period ending on the date of hire; and expand the definition of qualified first-year wages from \$6,000 to \$12,000 in connection with these individuals.

- rename the “high risk youth” targeted group the “designated community residents” targeted group and expand it to include otherwise qualifying individuals age 18 but not yet 40 (currently 25) on the date of hire.

- expand the “vocational rehabilitation referral” targeted group

to include handicapped individuals with individual work plans developed and implemented by an employment network pursuant to the Social Security Act (also applies to plans developed pursuant to the Rehabilitation Act and for veterans).

**Levies to collect employment taxes.** Levies issued to collect federal employment taxes would be excepted from the pre-levy collection due process (CDP) hearing requirement. Thus, under the proposal, taxpayers would have no right to a CDP hearing before a levy is issued to collect employment taxes. However, a taxpayer would have an opportunity for a hearing within a reasonable period of time after the levy. Collection by levy would be permitted to continue during the CDP proceedings.

**Tax return preparers.** The bill would broaden the scope of tax return preparer penalties to cover preparers of employment tax returns, and would change the standard of conduct that must be met to avoid imposition of a penalty – from “realistic possibility” to “reasonable belief” (for undisclosed positions) and from “not frivolous” to “reasonable basis” (accompanied by disclosure).

Finally, first-tier penalties would be increased from \$250 to the greater of \$1,000 or 50% of the income derived (or to be derived) from the preparation of the return or claim with respect to which the penalty is imposed. Second-tier penalties would be increased from \$1,000 to the greater of \$5,000 or 50% of the income derived (or to be derived) by the tax return preparer. **PC**

## IRS Issues Final Regulations on Distributions From Designated Roth Accounts

The IRS has issued final regulations on taxation, reporting, and recordkeeping requirements in connection with distributions from designated Roth accounts [72 F.R. 21103, 4-30-07]. The regulations are available at <http://a257.g.akamaitech.net/7/257/2422/01jan20071800/edocket.access.gpo.gov/2007/pdf/E7-8125.pdf>.

### Background

A designated Roth account is a separate account under a §401(k) plan or §403(b) annuity to which designated Roth contributions are made, and for which a separate accounting of contributions, gains, and losses is maintained.

Designated Roth contributions are provided for under IRC §402A, added by the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA; Pub. L. No. 107-16). Under §402A, beginning in 2006, a plan

may permit an employee who makes elective contributions under a §401(k) plan to designate some or all of those contributions as contributions to a Roth IRA (individual retirement account).

*Note:* Roth IRAs are different from traditional IRAs in that contributions to a Roth IRA are not deductible from income, but distributions are not included in gross income if they meet certain qualifications. Individuals may put up to the maximum deductible amount for a traditional IRA in a Roth IRA in a year, but that amount is reduced by any contributions by the individual to other IRAs for that year (see *The Payroll Source*®, pp. 4-78 to 4-81 for more on Roth IRAs).

### Qualified distributions

The taxation of a distribution from a designated Roth account depends on whether or not the distribution is a qualified distribution. A qualified

distribution from a designated Roth account is not included in the employee's gross income. A qualified distribution is a distribution that is made after a five-taxable-year period of participation that is made:

- on or after the date the employee reaches age 59½,
- after the employee's death, or
- on account of the employee's disability.

The five-taxable-year period during which a distribution is not a qualified distribution begins on the first day of the employee's taxable year for which the employee first had designated Roth contributions made to the plan and ends when five consecutive taxable years have been completed. However, if a direct rollover is made from a designated Roth account under another plan, the five-taxable-year period for the recipient plan

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## Payroll Solutions

**Q.** Our company hired a nonexempt employee who worked for seven months before her National Guard unit was activated for four months. Two months after she returned to work, she requested leave under the Family and Medical Leave Act (FMLA). Her supervisor thinks this request should be denied. Is this correct? (Our company is covered by the FMLA.)

**A.** No. This employee is probably entitled to FMLA leave. To be eligible for leave benefits, employees must have been employed by the employer for at least 12 months (not necessarily consecutively) and have worked at least 1,250 hours within the previous 12-month period. "Hours worked" are determined on the same basis as under the Fair Labor Standards Act (see *The Payroll Source*<sup>®</sup>, beginning at p. 4-32).

This employee's eligibility for FMLA leave is affected by the Uniformed Services Employment and Reemployment Rights Act (USERRA), which provides that reemployed members of the military are entitled to the same rights or benefits they would have had if they had been continuously employed. Guidance issued by the Department of Labor (DOL) in 2002 ([www.dol.gov/vets/media/fmlarights.pdf](http://www.dol.gov/vets/media/fmlarights.pdf)) addresses the FMLA eligibility of reemployed members of the military in the context of USERRA. The DOL said that, in determining whether a military veteran meets the FMLA eligibility threshold, the months actually employed and the hours actually worked for the employer must be combined with the months and hours that would have been worked during the 12 months prior to the start of the requested leave but for the military service. In a fact sheet explaining the interaction of the FMLA and USERRA ([www.dol.gov/vets/media/fmlaq-a.pdf](http://www.dol.gov/vets/media/fmlaq-a.pdf)), the DOL offers the following example:

**EXAMPLE:** An employee on the job for nine months is ordered to active military service for nine months after which the employee is reemployed. Upon reemployment, the employee must be considered to have been employed by the employer for more than the required 12 months (nine months actually employed plus nine months while serving in the military service) for purposes of FMLA eligibility.

begins on the first day of the employee's taxable year for which the employee first had designated Roth contributions made to the other plan, if earlier.

The final regulations provide that certain contributions do not start the five-taxable-year period of participation:

- a year in which the only contributions consist of excess deferrals;
- excess contributions that are distributed to prevent an ADP failure; and
- contributions returned to the employee pursuant to IRC §414(w).

### ***Alternate payee or beneficiary.***

The final regulations clarify that, in the case of distribution to an alternate payee or beneficiary, the age, death, or disability of the participant is used to determine whether the distribution is qualified. The only exception is in the case of a rollover by an alternate payee or surviving spouse to a designated Roth account under a plan of his or her own employer.

***Reemployed veteran.*** The final regulations provide that designated Roth contributions made by a reemployed veteran are treated as made in the taxable year with respect to which the contributions relate. Reemployed veterans may identify the year for which a contribution is made for other purposes (e.g., entitlement to a match), and the treatment of the five-year period

of participation follows that identification. If an identification is not made, for purposes of determining the first year of the five years of participation, the contribution is treated as made in the veteran's first taxable year in which his/her military service begins or, if later, the first taxable year in which designated Roth contributions could be made under the plan.

### **Reporting and recordkeeping**

Under the final regulations, the plan administrator of a plan with a designated Roth account is responsible for keeping track of the five-taxable-year period for each employee and the amount of designated Roth contributions made on behalf of such employee. In addition, the plan administrator of a plan directly rolling over a distribution is required to provide the plan administrator of the plan accepting the eligible rollover distribution with a statement indicating either:

- the first year of the five-taxable-year period for the employee and the portion of such distribution attributable to basis, or
- that the distribution is a qualified distribution.

If the distribution is not a direct rollover to a designated Roth account under another eligible plan, the plan administrator must provide to the employee, upon request, this same

information, except that the statement need not indicate the first year of the five-taxable-year period.

The statement must be provided within 30 days following the direct rollover (or an employee request), and the plan administrator for the recipient plan is permitted to rely on these statements.

***Reporting a distribution includible in income.*** To the extent that a portion of a distribution is includible in income (determined without regard to the rollover), if any portion of that distribution is rolled over to a designated Roth account by the distributee rather than by direct rollover, then the plan administrator of the recipient plan must notify the IRS of its acceptance of the rollover contribution.

This reporting is only required to the extent provided in IRS forms and instructions, which will specify the address to which the notification must be sent and will require information such as the employee's name and social security number, the amount rolled over, and the year in which the rollover contribution was made. Until relevant forms and instructions are released, no such reporting is required.

***Reporting other distributions.*** With respect to other reporting, generally the same reporting requirements

apply to plans with designated Roth accounts as apply to other plans. A contribution to and a distribution from a designated Roth account must be reported on Form W-2 and Form 1099-R, respectively.

#### News Notes...

### Bereavement Leave Was Not FMLA Leave

Larry Hoban took three days of bereavement leave from his job at a nursing home after his brother died. He was scheduled to return to work on July 8, 2005, but called before the start of his shift to say he would not be in. He did not return to work until July 11, when he left early for a dentist appointment. The nursing home terminated his employment the next day, and Hoban sued under the Family and Medical Leave Act (FMLA). He argued that his request for bereavement leave was the equivalent of a request for FMLA leave and gave notice that he was suffering from a "serious health condition."

The court disagreed, saying that bereavement leave is not FMLA leave and that the nursing home did not violate the FMLA. In order to invoke the right to FMLA leave, an employee must first provide enough information about his/her illness to alert the employer to the possible involvement of the FMLA. Here, Hoban made no mention of his mental or physical condition in his communications with the nursing home.

Under the FMLA, a serious health condition is defined as "a period of incapacity requiring absence from work ... of more than three calendar days, and any subsequent treatment or period of incapacity relating to the same condition, that also involves ... treatment two or more times by a health care provider" (29 C.F.R. §825.114(a)(2)(i)(A)). Hoban did not work for four days, but this absence was caused by the death of his brother. Although a mental condition can be a serious health condition, Hoban merely stated that he was "a nervous wreck." Moreover, he failed to seek any medical attention [*Hoban v. West Bloomfield Nursing & Convalescent Ctr.*, No. 06-13142, 2007 U.S. Dist. LEXIS 25407 (ED Mich., 4-5-07)].

### Distribution of excess elective deferrals

Even though designated Roth contributions are not excluded from income when contributed, they are treated as elective deferrals for purposes of the annual limit under IRC §402(g). Thus, to the extent total elective deferrals for the year exceed the §402(g) limit for the year, the excess amount can be distributed by April 15th of the year following the year of the excess deferrals without adverse tax consequences.

However, if such excess deferrals are not distributed by April 15th of the year following the year of the excess, the final regulations provide that any distribution attributable to an excess deferral that is a designated Roth contribution is included in gross income and is not eligible for

rollover.

The final regulations provide that if there are any excess deferrals that are designated Roth contributions that are not corrected prior to April 15th of the year following the excess, then the first amounts distributed from the designated Roth account are treated as distributions of excess deferrals and earnings until the full amount of those excess deferrals (and attributable earnings) are distributed.

#### Effective date

The final regulations are generally applicable for taxable years beginning on or after January 1, 2007. However, certain provisions in the regulations are applicable at the same time as IRC §402A (i.e., taxable years beginning on or after January 1, 2006). **PC**

## Kansas Allows Mandatory Electronic Wage Payment

On April 16, 2007, Kansas Governor Kathleen Sebelius signed into law a bill allowing employers to pay wages through the use of a payroll debit card and mandate the use of direct deposit or payroll debit cards [H.B. 2316, L. 2007; K.S.A. §44-314].

### Payroll debit cards

Effective July 1, 2007, employers may choose to pay their employees' wages by payroll debit card. An employer must provide its employees at least one free withdrawal each pay period of an amount up to and including total net pay. Employers are prohibited from charging any initiation, loading, or participation fees to employees who are receiving wages on a payroll debit card, except for the cost required to replace lost, stolen, or damaged cards. The employer may make corrections, as provided by rules governing direct deposit, if an inadvertent overpayment occurs.

### Employers may require electronic wage payment

Federal Reserve Board (FRB) Regulation E establishes consumer protections that apply to Automated Clearing House (ACH) direct deposit payments. Regulation E allows employers to implement mandatory direct deposit programs provided employees are permitted to select their financial institution. However, most

states have enacted laws that supersede the regulation and restrict employer authority to determine how workers are paid. In 2006, Regulation E was amended to cover payroll debit cards, and the FRB said in the preamble to the interim final rule that an employer offering payroll debit cards and direct deposit as the only wage payment options would not violate Regulation E.

The change in Kansas law will generally allow employers to choose to pay wages solely by direct deposit in a financial institution of the employee's choice, without voluntary authorization by the employee. However, an employer that wants to mandate direct deposit must offer an alternate payment method as a default option for employees who do not designate a financial institution in which they maintain an account for electronic funds transfer or deposit. That default option can be a payroll debit card, cash, or check. The result is that Kansas employers can offer electronic payment of wages through direct deposit or payroll debit cards as the only wage payment methods.

### Employee education

If an employer wishes to offer only direct deposit or payroll debit cards as wage payment methods, the employer must conduct one or more employee forums to educate employees

regarding the use of direct deposit or payroll debit cards (as offered by the employer) or distribute to employees educational information on such topics at least 30 days prior to implementing the mandated electronic wage payment program.

#### APA reaction

The Paycard Subcommittee of the APA's Government Affairs Task Force, which followed this legislation closely, has worked with state policy makers and regulators on these issues since 2005. Pete Isberg, CPP, commented on the

bill's passage. "This is really a strong accomplishment for the [Subcommittee]. There were some adverse elements in the bill, and the legislature adopted our recommendations. It's a very positive bill for employers – the first to permit mandatory programs." **PC**

## Department of Labor Proposes Revised, Updated Child Labor Regulations

The U.S. Department of Labor has issued proposed regulations revising and updating the child labor regulations under the Fair Labor Standards Act [72 F.R. 19337, 4-17-07; <http://a257.g.akamaitech.net/7/257/2422/01jan20071800/edocket.access.gpo.gov/2007/pdf/E7-7053.pdf>]. The proposed regulations address 25 recommendations made by the National Institute for Occupational Safety and Health (NIOSH) in 2002 concerning existing Hazardous Occupation Orders (HOs) and implement a provision of the DOL Appropriations Act, 2004 (Pub. L. No. 108-199) that authorizes the employment of minors 14 to 18 years of age who are excused from compulsory school attendance beyond the eighth grade in businesses that use machinery to process wood products.

In an "advance notice" of proposed rulemaking issued simultaneously, the DOL is inviting comments on four other NIOSH recommendations as well as the possible creation of an HO that would prohibit the employment of youth in construction occupations [72 F.R. 19328, 4-17-07; <http://a257.g.akamaitech.net/7/257/2422/01jan20071800/edocket.access.gpo.gov/2007/pdf/E7-7052.pdf>].

*Note:* There were 35 NIOSH recommendations in all. Final regulations issued in 2004 (see **PAYROLL CURRENTLY, Issue No. 2, Vol. 13**) addressed six of them and implemented the Compactors and Balers Safety Standards Modernization Act (Pub. L. No. 104-174) and the Drive for Teen Employment Act (Pub. L. No. 105-334).

#### Proposed regulatory revisions

##### 14- and 15-year-olds

- expand the list of jobs that are either permitted or prohibited for minors 14 and 15 years of age and remove language limiting authorized work to retail, food service, and gasoline service establishments;

- combine all provisions on power-driven machinery and expand the list of examples of prohibited equipment to include power-driven trimmers, weed-eaters, edgers, golf carts, food processors, and food mixers;

- expressly permit 14- and 15-year-olds to ride in the enclosed passenger compartments of motor vehicles, except when a significant reason for the minors being passengers in the vehicle is for the purpose of performing work in connection with the transporting (or assisting in the transporting) of other persons or property;

- expressly permit 14- and 15-year-olds to be employed to load and unload from motor vehicles the light non-power-driven personal hand tools they use as part of their employment, e.g., rakes, hand-held clippers, shovels, brooms (but not lawn mowers or other power-driven lawn maintenance equipment), and any personal protective equipment they use at the worksite, as well as personal items such as backpacks, lunch boxes, and coats;

- clarify that 14- and 15-year-olds may perform car cleaning, washing, and polishing, but only by hand;

- expressly permit 14- and 15-year-olds to perform such jobs as computer programmer and computer applications demonstrator for a college, print and runway model, and musical director at a church or school;

- clarify that the restriction that limits the employment of 14- and 15-year-olds in nonagricultural employment to no more than three hours on a day when school is in session also applies to Fridays;

- clarify that the term "week" means a standard calendar week;

- clarify that school would not be considered to be in session for a 14- or 15-year-old who has graduated from

high school or has been excused from compulsory school attendance once he or she has completed the eighth grade; and

- allow schools to apply for approval to operate work-study programs where certain 14- and 15-year-olds would be permitted to work during school hours and up to eight hours a day under specified circumstances.

##### 16- and 17-year-olds

- expressly prohibit 16- and 17-year-olds from working in forest firefighting and forest fire prevention occupations;

- expressly prohibit 16- and 17-year-olds from the work of tending, riding on, working from, servicing, repairing, or disassembling power-driven hoisting apparatus, including truck or equipment-mounted aerial platforms commonly referred to as cherry pickers and bucket trucks;

- revise the definition of "high-lift truck" to include, e.g., skid loaders, skid-steer loaders, and Bobcat loaders;

- expressly prohibit the employment of 16- and 17-year-olds in all meat products manufacturing industries, including those engaged in the processing of sausages and/or other prepared meat products and those engaged in poultry slaughtering and/or processing;

- revise the definition of "slaughtering and meat packing establishment" to include places where poultry are killed, butchered, and processed;

- add buffalo and deer to the list of animals contained in the definitions of "killing floor" and "slaughtering and meat packing establishments";

- expressly prohibit 16- and 17-year-olds from washing power-driven meat processing machine parts and attachments;

- allow employment of 16- and 17-

year-olds to operate lightweight, small capacity, portable counter-top power-driven food mixers that are comparable to models intended for household use;

- allow 16- and 17-year-olds to operate (but not set up, adjust, repair, oil, or clean) power-driven pizza dough rollers where specified safeguards are present on the machines, are operational, and have not been overridden;

- expressly prohibit 16- and 17-

year-olds from operating, loading, and unloading (with limited exceptions) all balers and compactors, regardless of the materials being processed; and

- expressly prohibit 16- and 17-year-olds from operating, setting up, adjusting, repairing, oiling, or cleaning chain saws, wood chippers, and reciprocating saws.

#### Comments

Comments are invited on both the proposed regulations (RIN docket

number 1215-AB57) and the “advance notice” of proposed rulemaking (RIN docket number 1215-AB44). Comments must be received by July 16, 2007. Send written comments to: Wage and Hour Division, Employment Standards Administration, U.S. Department of Labor, Room S-3502, 200 Constitution Avenue, NW, Washington, DC 20210. Or submit comments electronically at: [www.regulations.gov](http://www.regulations.gov). **PC**

## Employee Contributions to Pay for Medical Expenses After Retirement Are Not Excludable From Income

In a private letter ruling, the IRS has ruled that employee contributions to a plan in place of a portion of regular compensation or accrued leave (or both) to pay for medical expenses after retirement are not excludable from the employees’ gross income under IRC §106 [LTR 200704005, 1-26-07].

#### The plan

An employer proposes to adopt a plan under which employees will have the option to make contributions in place of regular compensation or accrued leave, or both. Once an employee makes an election, it will be irrevocable and the employee will not be able to obtain cash refunds of contributions.

Employees will be able to contribute regular compensation through salary reductions that decrease amounts otherwise payable to them. Employees will also be able to contribute up to 500 hours of accrued leave to the plan.

Retirees participating in the plan will be able to use their accounts only to pay for medical expenses as defined in IRC §213. Amounts remaining after a participant’s death will be available for use by the surviving spouse, dependents, or other beneficiaries.

#### IRC §106

IRC §106 provides that an employee’s gross income does not include employer-provided coverage under an accident or health plan. Reg. §1.106-1 provides that an employee’s gross income does not include employer contributions to an accident or health plan for compensation (through insurance or otherwise) for personal injuries or sickness of the employee or the employee’s spouse or dependents.

#### Analysis

The Service explains that where the employee has the *option* to receive a portion of accumulated sick leave as a cash payment or to apply it to continued participation in the employer’s health plan, the contribution cannot be excluded from gross income under §106 because the contribution is considered an *employee* contribution. However, where the employer contributes accumulated sick leave credits of the employee, which the employee *cannot* receive in cash, such contributions are excludable under §106.

The IRS also notes that for a plan to be considered a tax-favored health reimbursement arrangement (HRA),

employer contributions may not be attributable to salary reductions (which is the case here). A plan funded by salary reductions thus cannot be considered an HRA and is subject to the rules governing cafeteria plans under IRC §125.

Additionally, under §125 unused employee contributions to a cafeteria plan may generally not be carried forward to be used in subsequent coverage periods (here the employer’s plan permits use of the contributions after an employee retires).

Finally, the IRS points out that an employer plan qualifies as an HRA if it automatically, and on a *mandatory* basis, contributes all or a portion of a retired employee’s accumulated unused vacation and sick leave to a reimbursement plan (which is not the case here). However, an HRA may not allow unused amounts to be used to pay for the medical expenses of a beneficiary other than the employee’s spouse and dependents (as the plan here does).

**REMEMBER** – Private Letter Rulings may be relied on only by the taxpayer involved and may not be cited as precedent. **PC**

## DOL Wage & Hour Roundup

The U.S. Department of Labor’s Wage & Hour Division recently concluded the following Fair Labor Standards Act enforcement actions:

#### Big payouts

- Chestnut Petroleum Dist., Inc., with 37 gas station/convenience store locations in New York, New Jersey, and Connecticut, has agreed to pay 767 employees a total of \$900,000 in back wages plus a \$100,000 civil money

penalty to resolve a DOL lawsuit. Investigators found that employees at these various locations were paid less than the federal minimum wage and were not properly compensated for overtime hours worked. In addition, the employer did not keep required records showing the hours worked each day, total hours worked each week, and rates of pay.

- Watterson-Prime, LLC, a Bellevue,

Washington firm that performs mortgage reviews for financial and mortgage lending institutions, has agreed to pay 197 workers a total of \$766,334 in back wages to resolve a DOL lawsuit. Investigators found that the company failed to compensate the workers at the applicable federal minimum wage and did not properly compensate them for overtime hours worked, primarily for travel time.

### Misclassification

- Parkland Health and Hospital System, of Dallas, Texas, has paid \$487,970 in back overtime wages to 459 current and former employees. Parkland incorrectly classified the employees as exempt from overtime, deducted half an hour for lunch each day when many employees did not take lunch breaks, and did not keep required records.

### Minimum wage

- First Ohio Banc and Lending, Inc., a mortgage lending company based in Independence, has paid \$307,702 in back wages to 298 loan officers. The employees were paid commissions on a

twice-monthly basis and received no pay if they had not closed loans during a pay period.

- Three Bronx, New York employers, all part of the same enterprise, have agreed to pay approximately \$208,000 in back wages to 75 workers. Pelham Bay Car Wash, Boston Road Car Wash, and MCA Oil Change Corp. shared the workers' tips with non-tipped employees, paid the workers straight time for all hours worked, and improperly documented how many hours each worker put in each day.

### Hours worked

- InfraSource Transmission Services,

a Kittitas, Washington construction company, has agreed to pay \$363,486 in back overtime pay to 153 workers. The company failed to compensate the workers for all hours worked performing pre-shift activities.

- Security Services Northwest, Inc., a Sequim, Washington security company, has agreed to pay \$207,852 in back overtime wages to 56 employees. While the company was providing hurricane-related security planning and protective services along the Gulf Coast, employees were not paid for all hours worked performing pre- and post-shift activities. **PC**

## School Security Officers Were Exempt Administrative Employees

Police officers hired by the Gwinnett County Board of Education to provide safety and security in county schools are administrative employees exempt from the minimum wage and overtime requirements of the Fair Labor Standards Act (FLSA), a U.S. District Court has ruled [*Ferrell v. Gwinnett County Bd. of Ed.*, No. 1:05-cv-2047-TCB, 2007 U.S. Dist. LEXIS 24297 (ND Ga., 3-30-07)].

### Background

The Gwinnett County (Georgia) School System has established a "school resource officer" (SRO) program. SROs are charged with proactively preventing and responding to school safety and security problems. Only police officers with a college degree and at least 10 years of law enforcement experience are eligible to work as SROs. Officers working as SROs wear their police uniforms and carry a standard police duty belt that includes handcuffs and a firearm. Each SRO is assigned to a cluster of schools.

The Gwinnett SROs sued the school board to recover unpaid overtime, asserting that they spend 85% to 95% of their time performing nonexempt "patrol officer" and "crime prevention duties." The school board countered that the SROs are exempt administrative employees, and the court agreed.

**WHAT THE LAW SAYS** – To qualify as an exempt administrative

employee: (1) the employee must be paid at least \$455 a week on a salary or fee basis, not including board, lodging, or other facilities; (2) the employee's primary duty must be the performance of office or nonmanual work directly related to the management or general business operations of the employer or the employer's customers; and (3) the employee's primary duty must include the exercise of discretion and independent judgment regarding matters of significance (see *The Payroll Source*®, p. 2-9). Here, only the primary duty qualifications for exemption were in dispute.

### Office or nonmanual work

The SROs' nonmanual duties include: participation in school security surveys; assisting with safety checklists; answering questions about safety and crime prevention; participation in staff orientation; writing reports; testifying at hearings; and patrolling hallways. It is also significant that the school board requires SROs to have a higher education level than rank-and-file police officers and pays them nearly \$10,000 more per year than police officers with comparable experience. Although SROs perform some manual work, such as making arrests or breaking up fights, the court said it was incidental to their primary duty of providing safety and security in

their clusters, which is, on the whole, a non-manual job.

### Directly related to management or general business operations

Police officers ordinarily do not satisfy this prong of the administrative exemption. Here, however, the court said that the SROs were not working for a law enforcement agency; they were servicing the school system's education business. Without a safe and secure school environment, the school system could not achieve its goal of educating students. The work of SROs was therefore directly related to the school system's general business operations.

### Discretion and independent judgment in matters of significance

The SROs satisfy this requirement, said the court, commenting that it is undisputed that safety and security are matters of significance in the school environment. The SROs formulate and implement school safety and security policies; serve as a liaison between the school system, local law enforcement agencies, and the community; initiate and direct investigations; and independently determine whether to make arrests or refer matters for prosecution. Moreover, the SROs are expected to perform their duties without direct supervision and, in fact, they are relatively free from supervision in their daily activities. **PC**

## Value of Employer-Provided Lodging Was Income

The U.S. Tax Court has ruled that the value of lodging provided by an employer to an employee in a town near the employer's facility was not

excludable from the employee's gross income [*Nielsen v. Commissioner*, T.C. Summary Op. 2007-53, No. 18883-04S (4-2-07)].

### Background

While employed by Raytheon E-Systems, Inc., James Nielsen was assigned to work at the U.S.-Australian

Joint Defense Facility at Pine Gap Air Force Base in Australia. As a condition of his employment, Nielsen was required to accept housing assigned to him by the U.S. Air Force. Nielsen was assigned housing in a condominium in Alice Springs, a town about 22 miles from the air base. In 2000 and 2001, Raytheon issued Nielsen Forms W-2 reporting his wages and Forms 1099-MISC reporting the value of his lodging. The IRS issued a notice of deficiency when Nielsen did not include the amounts paid by Raytheon for his lodging on his personal income tax returns for those years. Nielsen said the lodging payments were excludable from his income under IRC §119.

**WHAT THE LAW SAYS** – Under IRC §119, the value of employer-provided lodging is excluded from the employee's income if: (1) the lodging is furnished on the employer's

business premises (including a camp provided by the employer near the work site, if it is in a remote area of a foreign country); (2) the employee is required to accept the lodging as a condition of employment; and (3) the lodging is furnished for the employer's convenience (see *The Payroll Source*®, p. 3-55).

Here, the only question was whether the lodging furnished to Nielsen in Alice Springs was on the employer's business premises. The court said that it was not.

#### **Lodging was not a camp**

The court explained that Nielsen's lodging was not excludable as a camp provided by his employer near the work site. Under §119(c)(2), a "camp" must be (1) provided by or on behalf of the employer for the convenience of the employer because the place where the employee renders service is remote, (2) located, as near as

practicable, in the vicinity of the place at which the employee renders services, and (3) furnished in a common area or enclave that is not accessible to the public and which normally accommodates 10 or more employees.

Nielsen's lodging did not satisfy the third requirement, said the court. Although his specific housing was not accessible to the public, it was located in a condominium community whose housing was available to the general public. Raytheon's assigned housing units were interspersed throughout Alice Springs, not separated into gated communities, and a cluster of housing units adjacent to, or surrounded by, substantially similar housing for the general public does not satisfy the requirements for a camp. "Moreover, we do not regard living in a residential suburb as fitting into the common parlance of the term 'camp.'" **PC**



## STATE AND LOCAL NEWS

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**Illinois** Effective 7-1-07, an employer must pay the full state minimum wage (\$7.50 an hour) to: (1) a day or temporary laborer who is 18 years of age or older; and (2) an employee who is 18 years of age or older and whose employment is occasional or irregular and requires not more than 90 days to complete. Under the subminimum wage requirements (also effective 7-1-07), an employer may pay an employee who is age 18 or older a minimum wage that is 50 cents less than the state minimum wage during the employee's first 90 calendar days of employment (S.B. 1268, L. 2006; see **PAYROLL CURRENTLY, Issue No. 2, Vol. 15** [H.B. 3752, L. 2007]).

**Kansas** As of 6-1-07, the Department of Labor (DOL) will no longer accept unemployment insurance (UI) wage information submitted on any form of magnetic media, including CDs or diskettes. Instead, employers must use the DOL's new file upload system to file quarterly UI wage reports and tax returns. Employers can also upload payment files to the DOL, which are processed as electronic checks. For more information, visit [www.dol.ks.gov/UI/QuarterlyWage/ElectronicSubmit.html](http://www.dol.ks.gov/UI/QuarterlyWage/ElectronicSubmit.html).

**Vermont** Effective with Form C-101, *Employer's Quarterly Wage and Contribution Report*, filed for the second quarter of 2007 (due 7-31-07), employers are required to calculate and pay a health care premium contribution on "uncovered" workers. This assessment is used to help fund health care reform legislation enacted last year. For more information about employer health care reporting, including rules, sample Forms C-101, and frequently asked questions, visit <http://labor.vermont.gov> (click on the link "Employer Health Care Contribution") or call 802-828-4333/4344.

**West Virginia** Effective 6-1-07, employers that withheld more than \$100,000 per month in the preceding calendar year are no longer required to make accelerated payments of withheld tax in June. Previously, these employers had to remit tax withheld for the first 15 days of June by June 23 each year (tax withheld for the remainder of June was due by July 20) [H.B. 2917, L. 2007].