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DOL Issues Revised FMLA Regulations

The U.S. Department of Labor (DOL) has issued final revisions to the regulations under the Family and Medical Leave Act (FMLA) [73 F.R. 67934, 11-17-08; http://edocket.access.gpo.gov/2008/pdf/E8-26577.pdf]. The regulations are effective on January 16, 2009.

☞ **FMLA EXPANSION FOR MILITARY FAMILIES** – The final regulations incorporate new military family leave entitlements enacted as part of the National Defense Authorization Act for Fiscal Year 2008 (see PAYROLL CURRENTLY, Issue No. 3, Vol. 16). The procedures applicable to military family leave under the regulations are generally the same as those for other types of FMLA leave.

Military caregiver leave. The regulations implement the requirement to expand FMLA protections for family members caring for a covered service member with a serious injury or illness incurred in the line of duty while on active duty. These family members are able to take up to 26 workweeks of leave in a 12-month period.

Leave for qualifying exigencies for families of National Guard and Reservists. The regulations implement the provision allowing families of National Guard and Reserve personnel on active duty to take FMLA job-protected leave if there is a "qualifying exigency" related to the military member's service requirements. The regulations define "qualifying exigencies" as: (1) short-notice deployment, (2) military events and related activities, (3) childcare and school activities, (4) financial and legal arrangements, (5) counseling, (6) rest and recuperation, (7) post-deployment activities, and (8) additional activities where the employer and employee agree to the leave.

Joint employer coverage: PEOs

The final regulations clarify that Professional Employer Organizations (PEOs) that contract with client employers merely to perform administrative functions – including payroll, benefits, regulatory paperwork, and updating employment policies – are not joint employers with their clients, provided they merely perform such administrative functions. On the other hand, if a PEO has the right to hire, fire, assign, or direct and control the employees, or benefits from the work that the employees perform, such rights may lead to a determination that the PEO is a joint employer with the client employer, depending on all the facts and circumstances.

The final rule also clarifies that, unlike the situation involving traditional placement agencies, the client employer most commonly would be the primary employer (i.e., the employer with primary responsibility for job restoration) in a joint employment relationship with a PEO.

Employee eligibility: break in service

The final regulations provide that although the 12 months of employment required for leave eligibility need not be consecutive, employment prior to a continuous break in service of seven years or more need not be counted. Thus, under the final rule, if an employee in 2009 has worked five months for an employer during that year and worked for the same employer for two full years in 1997-1998, the employer does not have to consider the two years of prior employment in determining whether the employee currently is eligible for FMLA leave. *Note:* Proposed regulations issued in February 2008 included a five-year cap on breaks in service in order for prior

Payroll Solutions

Q. We are acquiring another company. Some of the employees at the company we are acquiring have exceeded, or will soon exceed, the social security wage base for this year. Can we count the wages these employees have already earned this year toward the social security wage base when we begin paying them?

A. Generally, the earnings from different employers cannot be combined for purposes of determining whether the social security wage base has been reached. However, a "successor employer" may credit wages earned by an employee for the "predecessor employer" during the calendar year toward the wage base. In order to be eligible for this exception:

- the successor must have acquired all or substantially all of the property used by the predecessor in its business or in a separate unit of its business;
- immediately before and after succession, the employee in question must have been employed by the predecessor and successor, respectively; and
- the employee must have been paid wages by the predecessor during the calendar year of the acquisition (see *The Payroll Source®*, p. 6-47).

employment to count toward the 12-month requirement (see PAYROLL CURRENTLY, Issue No. 4, Vol. 16).

In two situations, employment prior to the break in service would have to be counted regardless of the length of the break in service:

- A break in service resulting from the employee's fulfillment of military obligations; and
- A period of approved absence or unpaid leave, such as for education or child-rearing purposes, where a written agreement or collective bargaining agreement exists concerning the employer's intent to rehire the employee.

The final regulations clarify that nothing prevents an employer from considering employment prior to a continuous break in service of more than seven years, provided the employer does so uniformly with respect to all employees with similar breaks in service.

The final regulations also clarify that when an employee is on leave at the time he or she meets the 12-month eligibility requirement, the period of leave prior to meeting the statutory requirement is non-FMLA leave and the period of leave after the statutory requirement is met is FMLA leave.

Continuing treatment

The final regulations specify that the two visits to a health care provider required to establish the existence of a serious health condition must occur within 30 days of the beginning of the period of incapacity (unless extenuating circumstances exist). In addition, the regulations clarify that the definition of "periodic" visits for treatment of a chronic serious health condition is "at least twice a year."

Adoption or foster care

The final regulations provide that spouses may each take their full 12 weeks of FMLA leave to care for an adopted or foster child with a serious health condition, regardless of whether the spouses work for the same employer.

Amount of leave: holidays

The final regulations clarify that if an employee needs less than a full week of FMLA leave, and a holiday falls within the partial week of leave, the hours that the employee does not work on the holiday cannot be counted against the employee's FMLA leave entitlement if the employee would not otherwise have been required to report for work on that day. If an employee needs a full week of leave in a week with a holiday, however, the hours the employee does not work on the holiday will count against the employee's FMLA entitlement.

Accordingly, for an employee with a Monday through Friday workweek schedule, in a week with a Friday holiday on which the employee would not normally be required to report, if the employee needs FMLA leave only for Wednesday through Friday, the employee would use only 2/5 of a week of FMLA leave because the employee is not required to report for work on the holiday. However, if the same employee needed FMLA leave for Monday through Friday of that week, the employee would use a full week of FMLA leave despite not being required to report to work on the Friday holiday.

Intermittent or reduced schedule leave: overtime

The final regulations clarify that if an employee would be required to work overtime hours were it not for being entitled to FMLA leave, then the hours the employee would have been required to (but did not) work may be counted against the employee's FMLA entitlement. Where, in such a case, the employee works a part-time or reduced schedule, the employee's leave usage in any given week is proportionate to the scheduled hours in the week in which the leave is used.

For example, if an employee has a certified serious health condition limiting his or her work hours to 40 per week and that employee is scheduled for 48 hours in a week, the employee would take eight hours of FMLA-protected leave that week. This translates into 8/48ths or 1/6th of a week of FMLA leave. For ease of tracking, an employer may convert these fractions to their hourly equivalent so long as the conversion equitably reflects the employee's total normally scheduled hours.

Substitution of paid leave

The final regulations clarify that for FMLA purposes "substitution" means that unpaid FMLA leave and paid leave provided by an employer run concurrently.

The regulations also clarify that when providing notice of eligibility for FMLA leave to an employee, an employer must make the employee aware of any additional requirements for the use of paid leave and must inform the employee that he/she remains entitled to unpaid FMLA leave even if he/she chooses not to meet the terms and conditions of the employer's paid leave policies (such as by using leave only in full day increments or completing a specific leave request form).

Finally, the regulations allow the use of compensatory time accrued by public agency employees under the Fair Labor Standards Act to run concurrently with unpaid FMLA leave when leave is taken for an FMLA-qualifying reason.

Employee failure to pay health insurance premiums

The final regulations clarify that if an employer allows an employee's health insurance to lapse due to the employee's failure to pay his or her share of the premium while on FMLA leave, the employer still has a duty to reinstate the employee's health

insurance when the employee returns to work and can be liable for harm suffered by the employee if it fails to do so.

Equivalent pay: bonuses

If a bonus or other payment is based on the achievement of a specified goal – hours worked, products sold, or perfect attendance – and an employee has not met the goal due to FMLA leave, the final regulations allow an employer to disqualify the employee, unless the bonus or award is paid to employees on an equivalent leave status for a reason that does not qualify as FMLA leave. For example, if an employee who used paid vacation leave for a non-FMLA purpose would receive the payment, then the employee who used vacation leave for an FMLA-protected purpose also must receive the payment.

Eligibility notice: five-day rule

The final regulations generally require that the employer notify an employee of his/her eligibility to take FMLA leave within five business days after the employee either requests leave or the employer acquires knowledge that the employee's leave may be for an FMLA-qualifying reason, "absent extenuating circumstances" (language added in the final regulations). The employer is required to notify the employee whether leave is still available in the applicable 12-month period. However, the final regulations clarify that if, in the same leave year, an employee provides notice of a subsequent need for leave for a different FMLA-qualifying reason and the employee's eligibility status has not changed, no additional eligibility notice is required.

If the employee is not eligible or has no FMLA leave available, then the notice must indicate "at least one reason" (this language in the final rule relaxes the standard in the proposed regulations) why the employee is not eligible or that the employee has no FMLA leave available. For example, an employer might need to indicate that an employee has not worked long enough to meet the 12-month eligibility requirement.

Rights and responsibilities notice

The final regulations provide for a notice of rights and responsibilities separate from the notice of eligibility. Employers are required to provide this notice at the same time they provide the eligibility notice. The information that must be included in the rights and responsibilities notice is as follows:

- That the leave may be designated and counted against the employee's annual FMLA leave entitlement if qualifying. In addition, the final rule modifies the proposed regulations to require employers to notify employees of the method used for establishing the 12-month period for FMLA entitlement or, in the case of military caregiver leave, the start date of the "single 12-month period."

Note: An employer is permitted to choose any one of the following methods for determining the "12-month period" in which the 12 weeks of leave entitlement occurs: (1) the calendar year; (2) any fixed 12-month "leave year," such as a fiscal year, a year required by state law, or a year starting on an employee's "anniversary" date; (3) the 12-month period measured forward from the date an employee's first FMLA leave begins; or (4) a "rolling" 12-month period measured backward from the date an employee uses any FMLA leave.

- Any requirements for the employee to furnish certification of a serious health condition or call to active duty, etc., and the consequences of a failure to do so. *Note:* Under the final regulations, employers may include the medical certification with the notice of rights and responsibilities but are not required to do so.
- The employee's right to substitute paid leave, whether the employer will require the substitution of paid leave, the conditions related to any such substitution, and the employee's right to take unpaid FMLA leave if those conditions are not met.
- Any requirement for the employee to make any premium payments to maintain health benefits, the arrangements for making such payments, and the possible consequences of failure to make such payments on a timely basis.
- The employee's rights to maintenance of benefits during FMLA leave and restoration to the same or an equivalent job on return from FMLA leave.
- The employee's status as a "key employee" and the potential that job restoration may be denied following FMLA leave, explaining the conditions required for such denial.
- The employee's potential liability for payment of health insurance premiums paid by the employer during the employee's unpaid FMLA leave if the employee fails to return to work.

Designation notice: five-day rule

Under the final regulations, an employer is required to provide an employee notice of the designation of FMLA leave within five business days of receiving sufficient information from the employee to designate the leave as FMLA leave, "absent extenuating circumstances" (language added in final regulations). In addition, the employer must inform the employee of the number of hours, days, or weeks (if possible) that will be designated as FMLA leave.

The final regulations include a new provision requiring the employer to notify the employee if the information provided in the designation notice changes (e.g., if the employee exhausts the FMLA leave entitlement).

To the extent that future leave will be needed by the employee for a condition but the exact amount of leave is unknown (e.g., unforeseeable intermittent leave for a chronic serious health condition), the final regulations require that the employer inform the employee of the number of hours counted against his/her FMLA leave entitlement only upon request, and no more often than every 30 days if FMLA leave was taken during that period. *Note:* This relaxes the strict 30-day rule in the proposed regulations.

The final rule permits the employer to notify the employee of the hours counted against the FMLA leave entitlement orally and follow up with written notification on a pay stub at the next payday (unless the next payday is in less than one week, in which case the notice must be no later than the subsequent payday). "By clarifying that this requirement can be met with simple notation of FMLA leave on a pay stub, the Department believes that employers will be able to provide the necessary information to employees in a timely fashion with minimal additional burden."

The regulations also require an employer to notify the employee if leave is *not* designated as FMLA leave due to insufficient information or a nonqualifying reason.

Finally, the regulations require the designation notice to include a statement of the employee's essential job functions if the employer will require that those functions be addressed in a fitness-for-duty certification. *Note:* This requirement was included under the eligibility notice in the proposed regulations.

Consequences of failing to provide notice

The final regulations address concerns arising from the U.S. Supreme Court's decision in *Ragsdale v. Wolverine World Wide, Inc.* (535 U.S. 81 (2002)), which invalidated an earlier regulation (29 C.F.R. §825.700(a)): "If an employee takes paid or unpaid leave and the employer does not designate the leave as FMLA leave, the leave taken does not count against an employee's FMLA entitlement." This provision has been eliminated.

Instead, under new 29 C.F.R. §825.300(e), an employer's failure to follow FMLA notice requirements may constitute "an interference with, restraint, or denial of the exercise of an employee's FMLA rights." The employer may be liable for compensation and benefits lost by reason of the violation, for other monetary losses sustained as a direct result of the violation, and for "appropriate equitable and other relief, including employment, reinstatement, promotion, or any other relief tailored to the harm suffered."

Employee notice requirements and employer call-in procedures

The final regulations clarify the employee's obligation to provide notice "as soon as practicable." Absent emergency situations, where an employee becomes aware of a need for FMLA leave less than 30 days in advance, the DOL expects that it will be "practicable" for the employee to provide notice of the need for leave either the same day (if the employee becomes aware of the need for leave during work hours) or the next business day (if the employee becomes aware of the need for leave after work hours).

Where an employee's leave is foreseeable but the employee gives less than 30 days' advance notice, the employee must respond to a request from the employer and explain why it was not practicable to give 30 days' notice. Where an employee's leave is not foreseeable, the regulations clarify that it is expected the employee will provide notice to the employer as soon as practicable. "It generally should be practicable for the employee to provide notice of leave that is unforeseeable within the time prescribed by the employer's customary notice requirements applicable to such leave."

The regulations also clarify that an employee who takes FMLA leave, including intermittent leave, has an obligation to make a "reasonable effort," as opposed to an "attempt," to schedule his/her leave so as not to unduly disrupt the employer's operations.

Finally, whether an employee's absence from work for an FMLA-qualifying reason is foreseeable or unforeseeable, absent unusual circumstances, the final regulations provide that an employee may be required to follow established call-in procedures (except procedures that impose a more stringent timing requirement than provided under 29 C.F.R. §825.302(a)), and failure to properly notify an employer of an absence may cause a delay or denial of FMLA protections. In other words, an employer may delay FMLA coverage until the employee complies with the rules. Where unusual circumstances prevent an employee seeking FMLA-protected leave from complying with the procedures, the employee will be entitled to FMLA-protected leave so long as the employee complies with the policy as soon as he or she can practicably do so.

Medical or military certification: five-day rule

Under the final regulations, an employer should request medical or military exigency or caregiver certification from an employee within five business days of receiving notice of an employee's FMLA leave.

In addition, the employer must give the employee at least 15 calendar days to provide the certification, whether the FMLA leave is foreseeable or unforeseeable, unless it is not practicable to do so despite the employee's diligent good faith efforts.

Light duty

Under the final regulations, time spent in "light duty" work does not count against an employee's FMLA leave entitlement, and the employee's right to job restoration is held in abeyance during the light duty period. If an employee is voluntarily doing light work, he or she is not on FMLA leave.

Waiver of rights

Employees and employers may voluntarily agree to settle FMLA claims without court or departmental approval. The regulations clarify that only prospective waivers of FMLA rights are prohibited. ■

Tables Issued for Figuring Amount Exempt From Levy in 2009

Publication 1494, *Table for Figuring Amount Exempt from Levy on Wages, Salary, and Other Income*, provides tables showing the amount of an individual's wages that is exempt from a Notice of Levy used to collect delinquent federal income tax in 2009 (see *The Payroll Source®*, beginning at p. 9-2). The exempt amounts are based on the employee's standard deduction and the number of exemptions claimed by the employee on the Notice of Levy. The tables are available at www.americanpayroll.org/members/Forms-Pubs under "PUBLICATIONS." ■

Federal Contractors Must Use E-Verify to Check Employees' Eligibility for U.S. Employment

The Federal Acquisition Regulation has been amended to require certain contractors and subcontractors to use the E-Verify system administered by the Department of Homeland Security (DHS), U.S. Citizenship and Immigration Services, as the means of verifying that new hires and current employees working on federal contracts are eligible to work in the U.S. [73 F.R. 67651, 11-14-08; http://edocket.access.gpo.gov/2008/pdf/E8-26904.pdf].

The regulations implement Executive Order 13465 (see below). They are effective January 15, 2009.

Background

In order to "promote economy and efficiency in federal government procurement," President Bush signed an Executive Order on June 6, 2008, ordering that all contracts entered into by "executive departments and agencies" require that the contractor agree to use "an electronic employment eligibility verification system designated by the Secretary of Homeland Security" to verify the employment eligibility of: (1) all persons hired during the contract term by the contractor to perform work in the U.S.; and (2) all persons assigned by the contractor to perform work in the U.S. on the federal contract (Ex. Order 13465, 73 F.R. 33285, 6-11-08; http://edocket.access.gpo.gov/2008/pdf/08-1348.pdf). Civilian and defense acquisition authorities were ordered to amend the Federal Acquisition Regulation "to the extent necessary and appropriate" to implement the Executive Order.

In response to the Executive Order, DHS Secretary Chertoff designated E-Verify as "the electronic employment eligibility verification system to be used by federal contractors," and

amendments to the Federal Acquisition Regulation were proposed (see PAYROLL CURRENTLY, Issue No. 13, Vol. 16).

Elements of the proposed rule that are retained in the final rule

The final rule inserts a clause into federal contracts committing government contractors to use the E-Verify system to verify that all of the contractors' new hires, and all employees (existing and new) directly performing work under federal contracts, are authorized to work in the U.S. Consistent with the requirements contained in the proposed rule, the final rule:

- Exempts contracts that are for commercially available off-the-shelf (COTS) items and items that would be COTS items but for minor modifications.
- Requires inclusion of the clause in subcontracts over $3,000 for services or construction.
- Requires contractors and subcontractors to use E-Verify to confirm the employment eligibility of all existing employees who are directly performing work under the covered contract.
- Applies to solicitations issued and contracts awarded after the effective date of the final rule. Under the final rule, departments and agencies should amend existing indefinite-delivery/indefinite-quantity contracts to include the clause for future orders if the remaining period of performance extends at least six months after the effective date of the final rule.
- In exceptional circumstances, allows a head of the contracting activity (this authority would not be delegable) to waive the requirement to include the clause.
- Applies to employment in the U.S. – including the 50 states, the District of Columbia, Guam, Puerto Rico, and the U.S. Virgin Islands. It does not apply to employment outside the U.S., including work on U.S. embassies or military bases in foreign countries.
- Does not apply to any employee hired prior to November 6, 1986.

Changes made in the final rule

Significantly expanded timelines. The final rule amends the proposed rule to permit federal contractors participating in the E-Verify program for the first time a longer period – 90 calendar days from enrollment instead of 30 days as initially proposed – to begin using the system for new and existing employees.

The final rule also provides a longer period after this initial enrollment period – 30 calendar days instead of three business days – for contractors to initiate verification of existing employees who have not previously gone through the E-Verify system when they are newly assigned to a covered federal contract.

Contractors already enrolled and using the program as federal contractors will have the same extended timeframe to initiate verification of employees assigned to the contract, but the time limits will be measured from the contract award date instead of from the contractor's E-Verify enrollment date.

With regard to verification of new hires, a contractor that has already been enrolled as a federal contractor for 90 calendar days or more will have the standard three business days from the date of hire to initiate verification of new hires. Those contractors that have been enrolled in the program for less than 90 calendar days will have 90 calendar days from the date of enrollment as a federal contractor to initiate verification of new hires (within three business days after the date of hire).

Covered prime contract value threshold. The final rule requires the insertion of the E-Verify clause in prime contracts above the simplified acquisition threshold ($100,000) instead of the micro-purchase threshold ($3,000).

Contract term. The final rule clarifies that the E-Verify clause need not be inserted into prime contracts with performance terms of less than 120 days.

Institutions of higher education. The final rule modifies the contract clause so that institutions of higher education need only verify employees assigned to a covered federal contract.

State and local governments and federally recognized Indian tribes. Similarly, under the final rule, state and local governments and federally recognized Indian tribes need only verify employees assigned to a covered federal contract.

Sureties. Under the final rule, sureties performing under a takeover agreement entered into with a federal agency pursuant to a performance bond need only verify employees assigned to the covered federal contract.

Security clearances and HSPD-12 credentials. The final rule exempts employees who hold an active security clearance of confidential, secret, or top secret from verification requirements. The rule also exempts employees for whom background investigations have been completed and credentials issued pursuant to Homeland Security Presidential Directive (HSPD)-12.

All existing employees option. The final rule provides contractors the option of verifying all employees, including existing employees not currently assigned to a government contract. A contractor that chooses to exercise this option must notify DHS and initiate verifications for the contractor's entire workforce within 180 days of such notice.

Expanded COTS-related exemptions. The final rule provides expanded COTS-related exemptions:

- The rule will not apply to prime contracts for agricultural products shipped as bulk cargo that would otherwise have been categorized as COTS, and
- Certain services associated with the provision of COTS items or items that would be COTS items but for minor modifications.

Waivers. The final rule allows the Head of the Contracting Activity to waive E-Verify requirements after contract award, either temporarily or for the period of performance.

Definition of 'employee assigned to the contract.' The final rule clarifies that employees who normally perform support work, such as general company administration or indirect or overhead functions, and who do not perform any substantial duties applicable to an individual contract, are not considered to be directly performing work under the contract. ■

Cents-Per-Mile Maximum Car Value for 2009 Remains at $15,000

Under the vehicle cents-per-mile method of valuing an employee's personal use of a company-provided car, the IRS's standard business mileage rate is multiplied by the personal miles driven by the employee. For cars put into service in 2009, this valuation method can be used only if the car (i.e., a passenger automobile other than a truck or van) does not have a fair market value of more than $15,000 (unchanged from 2008). The maximum value for passenger trucks or vans (including minivans and sport utility vehicles that are built on a truck chassis) is $15,200 (down from $15,900).

For employer-provided vehicles under the fleet-average valuation rule, applicable to an employer with a fleet of 20 or more automobiles, the 2009 maximum value is $19,900 for a car (unchanged) and $19,900 for a truck or van (down from $20,800). *Note:* The fleet-average valuation rule may not be used if any of the automobiles in the employer's fleet exceeds its maximum allowable value. ■

IRS Releases Form 940 for Tax Year 2008

The IRS has released Form 940 (*Employer's Annual Federal Unemployment (FUTA) Tax Return*) for 2008, as well as Schedule A (Form 940) (*Multi-State Employer and Credit Reduction Information*). Both forms and the *2008 Instructions for Form 940* are available on the APA website at www.americanpayroll.org/members/Forms-Pubs under "FORMS AND INSTRUCTIONS."

Items to note

• ***No credit reduction states.*** The U.S. Department of Labor has announced that there are no credit reduction states for tax year 2008. Therefore, do not complete lines 2 and 11 of Form 940 or Part 2 of Schedule A.

• ***FUTA rate for 2009.*** The FUTA tax rate was scheduled to decrease from 6.2% to 6.0% in 2009, when the 0.2% FUTA surtax was set to expire. However, the Emergency Economic Stabilization Act of 2008, signed into law by President Bush on October 3, includes a provision extending the surtax and the current 6.2% rate through 2009 (see PAYROLL CURRENTLY, Issue No. 21, Vol. 16).

• ***Disregarded entities and QSubs.*** Final IRS regulations effective for wages paid on or after January 1, 2009, treat eligible single-owner disregarded entities and qualified subchapter S subsidiaries (QSubs) as separate entities for employment tax purposes (72 F.R. 45891, 8-16-07). Business owners may no longer elect to treat the related employment taxes as a liability of the owner. Instead, report the employment taxes on employment tax returns filed by the disregarded entity or QSub.

Revisions to the form and instructions

• ***Balance due instructions.*** The Part 4 (Determine your FUTA tax and balance due ...), line 14 (Balance due) instructions have been revised so that the second bullet reads as follows: "If line 14 is $500 or less, you may pay with this return. For more information on how to pay, see the separate instructions."

• ***Third-party designee phone number.*** A box has been added to Part 6 (May we speak with your third-party designee?) for the third-party designee's phone number.

• ***Paid preparer's signature.*** A preparer must sign Form 940 and provide the information requested in the Paid Preparer's Use Only section of Part 7 (Sign here ...) if the preparer was paid to prepare Form 940 and is not an employee of the filing entity. Also, the preparer must give the filing entity a copy of the return in addition to the copy to be filed with the IRS.

The following sentence has been added to the perjury statement above the signature box in Part 7: "Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge."

Generally, do not complete the Paid Preparer's Use Only section if you are filing the return as a reporting agent and have a valid Form 8655, *Reporting Agent Authorization*, on file with the IRS. However, a reporting agent must complete this section if the reporting agent offered legal advice, for example, by advising the client on determining whether its workers are employees or independent contractors for federal tax purposes.

The "self-employed" checkbox in the Paid Preparer's Use Only section has been moved to the top right-hand corner of the section. And a parenthetical has been added to the instructions for the box for the firm's name as follows: "(or yours if self-employed)."

A box has been added to the Paid Preparer's Use Only section for the preparer's phone number.

• ***State rules may differ.*** The instructions for Part 2 (Determine Your FUTA Tax Before Adjustments ...) now include the following cautionary note: "Wages may be subject to FUTA tax even if they are excluded from your state's unemployment tax." ■

IRS Releases Publication 3823, Employment Tax e-file Guidelines, for 2008

The IRS has released Publication 3823, *Employment Tax e-file System Implementation and User Guide*, for Processing Year 2008. Publication 3823 contains the procedural guidelines and validation criteria for the Employment Tax *e-file* System. It is available at www.irs.gov/pub/irs-pdf/p3823.pdf.

Reminders

• The Employment Tax *e-file* System was designed to replace all previous electronic filing options for returns in the 940 and 941 families. Previous e-file formats were maintained in order to allow for transition to the new Extensible Markup Language (XML) based system. The Electronic Data Interchange (EDI) and proprietary e-file formats were discontinued in November 2006. Magnetic tape has also been discontinued. XML is now the *only* acceptable format for electronically transmitting Forms 940, 941, and 944.

• For Processing Year 2008, the Employment Tax *e-file* System will process the following forms, schedules, and attachments: Form 941, Form 941PR, Form 941SS, Form 940, Form 940PR, Form 941 Schedule B, Form 941PR Anexo B, Form 941c, Form 944, Schedule D (Form 941), PIN Registration, and Payment Record.

• The 2008 edition of Publication 3823 specifies that participants in the Employment Tax *e-file* System must follow the legal and administrative guidelines set out in Rev. Proc. 2007-38 and Rev. Proc. 2007-40. If there is a conflict between these revenue procedures and Publication 3823, Publication 3823 should be followed.

• Software developers and transmitters should use the guidelines provided in Publication 3823, along with electronically published XML schemas and test scenarios, to develop and test their software. If information in Publication 3823 changes before the publication is revised, a change page(s) may be issued. Any information that is changed, added, or deleted will be posted to the IRS website in the 94x XML Developers' Forum (www.irs.gov/taxpros/providers/article/0,,id=97753,00.html). Updates will also be provided to software developers, transmitters, and electronic return originators subscribing to the "Quick Alerts" system (www.envoyprofiles.com/QuickAlerts/) and through the IRS website.

What's new

The following Business Rules have been added to the 94x XML program for 2008 to allow the program to correspond to form instructions and to reduce IRS processing errors:

• Error Code 605 (Form 940): The value of FUTA Tax After Adjustments must equal the sum of values of Quarter 1 Liability, Quarter 2 Liability, Quarter 3 Liability, and Quarter 4 Liability, either if FUTA Tax After Adjustments is greater than $500, or if FUTA Tax After Adjustments is less than or equal to $500 and any Quarter Liability is not zero. (Error Message – The sum of

Quarter 1 Liability, Quarter 2 Liability, Quarter 3 Liability, and Quarter 4 Liability does not equal the entry for FUTA Tax After Adjustments.)

• Error Code 606 (Form 941): The value of Total Adjustment Amount must equal the sum of values of Fractions of Cents Adjustment, Sick Pay Adjustment, Tips Group Term Life Ins Adjustment, Withheld Income Tax Adjustment, Prior Quarter Adjustment Social Security/Medicare Taxes, Special Additions Federal Income Tax and Special Additions Social Security Medicare. (Error Message – The sum of the adjustment amounts does not equal the entry for Total Adjustments Amount.)

• Error Code 607 (Form 944): The value of Total Adjustments Amount must equal the sum of values of Current Year's Adjustment, Prior Year Withheld Income Tax Adjustment, Prior Year Adjustment Social Security Medicare Taxes, Special Additions Federal Income Tax, and Special Additions Social Security Medicare. (Error Message – The sum of the adjustment amounts does not equal the entry for Total Adjustments Amount.) ■

University Employees' Salary Reduction Retirement Plan Contributions Were Subject to FICA Tax

The University of Chicago maintains two retirement plans for its employees. One plan is for academic and highly compensated employees. The other plan is for nonacademic and nonhighly compensated employees. Under both plans, the university makes contributions on behalf of the employees, who are also required to contribute specified percentages of their salaries. From 2000 to 2003, the university failed to pay, report, or withhold FICA tax on contributions made to the retirement plans.

The IRS assessed FICA taxes, penalties, and interest on the contributions. The university made partial payments ("divisible portions") of the disputed amounts and sued for a refund. A U.S. District Court ruled that the contributions were FICA-taxable wages and ordered the university to pay additional taxes and penalties. The university appealed.

☞ **WHAT THE LAW SAYS** – The term "wages" for FICA purposes includes all remuneration from employment, with certain exceptions. One exception is for a payment made to, or on behalf of, an employee (or the employee's beneficiary) under or to an annuity contract under IRC §403(b), "other than a payment for the purchase of such contract which is made by reason of a salary reduction agreement" (IRC §3121(a)(5)(D)).

The question for the Seventh Circuit Court of Appeals was whether the contributions here were FICA-taxable because they were made by reason of a salary reduction agreement. The university argued that they were not because there was no salary reduction "agreement" – the university's employees were *required* to participate in the retirement plans.

Ruling

The court said that §3121(a)(5)(D) includes all "salary reduction agreements," whether voluntary or mandatory, as FICA wages. FICA-taxable salary reduction agreements are not limited to situations where an employee voluntarily chooses "to receive a lower stated salary plus payments to purchase annuity contracts in lieu of receiving cash."

Here, half the assessment against the university represented amounts that the university failed to withhold from its employees. The court upheld this portion of the assessment and rejected the university's "deputy tax collector" defense, which excuses an employer from withholding employment taxes from its employees unless the obligation to withhold is "precise and not speculative." The defense did not apply, said the court, because §3121(a)(5)(D) has long been held to exclude "salary supplements" (employer payments) but not "salary reductions" (employee payments) from the FICA wage base. Moreover, any doubt about whether a salary reduction agreement is limited to voluntary agreements was resolved in 1998 by a decision of the Tenth Circuit Court of Appeals.

The court also upheld failure-to-deposit and failure-to-pay penalties. Both penalties are mandatory unless a taxpayer can show that the failure is due to reasonable cause and not willful neglect. Here, the university did not act with reasonable cause because its interpretation of its obligations under the tax laws was unsupported and unreasonable, said the court.

Finally, the court rejected the university's assertion that it should not be subject to a failure-to-pay penalty because it made some tax FICA payments under the "divisible tax doctrine" (taxpayer challenges the assessment of a divisible tax by paying the full amount of one transaction, then sues for a refund and uses the outcome of the lawsuit to determine tax liability for other similar transactions). The court explained that the doctrine simply allows taxpayers to challenge taxes in court by making a partial payment; it does not change the fact that failure-to-pay penalties are mandatory unless the failure to pay is due to reasonable cause and not willful neglect [*University of Chicago v. U.S.*, No. 07-3686, (7th CA, 10-29-08)]. ■

Employee Who Took Two FMLA Leaves During the Year Was Not Eligible for a Third

On August 7, 2006, Katherine Lyons, a clinic assistant for the North East Independent School District, requested leave under the Family and Medical Leave Act (FMLA). The district denied her request and placed her on temporary disability leave. By the time Lyons returned to work on September 5, the district had placed someone else in the clinic assistant position, so she accepted a lower paying position. She then sued the district for violating her FMLA rights. The Fifth Circuit Court of Appeals has affirmed that the district did not violate Lyons' FMLA rights because she was not eligible for FMLA leave on August 7 [*Lyons v. North East Independent School Dist.*, No. 07-51366, 2008 U.S. App. LEXIS 9747 (5th CA, 5-7-08)].

To be eligible for FMLA benefits, an employee must have been employed by his or her employer for at least 12 months (not necessarily consecutively) and have worked at least 1,250 hours within the previous 12-month period (see *The Payroll Source®*, p. 4-33). The court explained that paid vacation, holidays, sick leave, and FMLA leave taken by an employee do not count toward the 1,250-hour calculation.

FMLA regulations permit employers to use one of four methods to determine the 12-month period during which the employee's hours of service are measured: the calendar year;

any fixed "leave year," such as a fiscal year, a year required by state law, or a year starting on an employee's "anniversary" date; the 12-month period measured forward from the date any employee's first FMLA leave begins; or a "rolling" 12-month period measured backward from the date an employee uses any FMLA leave (29 C.F.R. §825.200(b)).

Here, in accordance with the regulations, the district used a fixed 12-month leave year running from July 1 to June 30. When Lyons applied for leave on August 7, a new FMLA leave year that began July 1, 2006, was in effect, and in order to be FMLA-eligible she had to have worked 1,250 hours during the preceding 12 months. However, Lyons had taken two FMLA leaves during the 12 months before July 1, 2006, and worked only 1,141 hours in that time. ■

STATE AND LOCAL NEWS

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Alaska

UI employee contribution rate for 2009 announced. Alaska is one of only three states (New Jersey and Pennsylvania are the other two) that require employers to withhold unemployment insurance (UI) contributions from their employees' wages (see *The Payroll Source®*, p. 7-28). For 2009, the UI taxable wage base will increase to $32,700 from the 2008 wage base of $31,300 (this updates *The Payroll Source®*, p. 7-23). The UI employee tax rate will remain 0.5%. This converts to a maximum employee deduction of $163.50 for 2009, up from $156.50 for 2008.

Michigan

Withholding tables issued for 2009. Effective for wages paid on or after 1-1-09, the Department of Treasury (DOT) has issued wage-bracket and percentage method withholding tables. The withholding rate remains 4.35%; the personal exemption amount will increase to $3,600 from $3,500 [DOT, Form 446-I, *2009 Michigan Income Tax Withholding Guide*, and Form 446-T, *2009 Withholding Tax Tables*, at www.michigan.gov/taxes/0,1607,7-238-44079-203059--,00.html].

New Jersey

FLI notice requirements established. By 12-15-08, employers must post notices in their workplaces about the new Family Leave Insurance (FLI) program. Beginning 1-1-09, employers must begin withholding employee contributions for the FLI program (0.09% of annual earnings up to $28,900 for 2009; see PAYROLL CURRENTLY, Issue No. 17, Vol. 16). Employers must also provide employees with a written copy of the notification: (1) no later than 12-15-08; (2) at the time of an employee's hiring; (3) whenever an employee notifies the employer that he or she is taking time off to bond with a newborn or newly adopted child or to care for a seriously ill family member; and (4) at any time, upon the first request of an employee. The written notification may be electronically transmitted to employees. Employers may download a poster in letter or legal size at http://lwd.dol.state.nj.us/labor/fli/content/emp_important_info.html.

Wisconsin

Electronic filing of Forms W-2: requirement updated. Effective with 2008 Forms W-2 filed in 2009, the Department of Revenue (DOR) no longer accepts Forms W-2 filed on magnetic media (this updates *The Payroll Source®*, p. 8-106). Previously, cartridges were accepted, but 3.5-inch disks and CD-ROMs were not. Electronic filing is mandatory for employers filing 250 or more Forms W-2 with the DOR. Forms W-2 may be submitted through the DOR's website at www.revenue.wi.gov/eserv/w-2.html. The electronic W-2 files must be in the EFW2 format. The due date is 2-2-09 [DOR, *Wisconsin Tax Bulletin*, 10-08; Pub. 509, rev. 10-08, and Pub. CO-001, rev. 8-08].

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Publisher, Executive Director
Dan Maddux

Senior Director of Publications and Government Relations
Michael P. O'Toole, Esq.

Managing Editor
Anne S. Lewis, Esq.

Editors
Laura Lough, Esq.
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Inside Washington
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