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## Reminder: Notice of Special COBRA Election Period Must Be Sent By April 18 to Employees Terminated Before February 17

The American Recovery and Reinvestment Act of 2009 (ARRA; see **PAYROLL CURRENTLY**, Issue No. 4, Vol. 17), enacted on February 17, includes a provision that gives employees who have involuntarily lost their jobs the chance to pay for continued health insurance coverage at a deep discount.

The regular notice of the availability of COBRA continuation coverage that a plan administrator is required to provide to qualified beneficiaries when they become entitled to COBRA continuation coverage must now contain additional information and must also be sent to any assistance eligible individual (or any individual who would be an AEI if a COBRA continuation election were in effect) who had a qualifying event from September 1, 2008 – February 16, 2009, and

- who would be assistance eligible except that the individual did not elect COBRA continuation coverage by February 17, 2009, or
- who would be assistance eligible except that the individual elected COBRA continuation coverage between September 1, 2008, and February 17, 2009, and let it lapse before February 17, 2009.

Such individuals will have a special 60-day extended period in which to elect COBRA continuation coverage. The 60-day election period begins on the date that notice is provided to the individual of the special election period.

Employers must provide the notice of the special election period to all employees who terminated employment from September 1, 2008 – February 17, 2009, within 60 days after February 17, 2009 (by April 18, 2009). Note that according to the House-Senate conference report on ARRA, the notice of the special 60-day election period must be provided to all individuals who had a qualifying event related to an employee who was terminated between September 1, 2008, and February 17, 2009, not just those employees who were involuntarily terminated. *The Notice in Connection with Extended Election Periods* is available at [www.americanpayroll.org/members/Forms-Pubs/#non](http://www.americanpayroll.org/members/Forms-Pubs/#non).

**APA OFFERS ON DEMAND WEBINAR ON NEW COBRA PROVISIONS** – To learn more, sign up for an “on demand” webinar on *How to Implement the New COBRA Premium Subsidy Through Payroll Taxes* at [www.americanpayroll.org](http://www.americanpayroll.org). ■

## IRS Issues Guidance on the Making Work Pay Tax Credit, Amending Form W-4

The IRS has posted 22 questions and answers on the Making Work Pay tax credit under the American Recovery and Reinvestment Act of 2009 (ARRA; see **PAYROLL CURRENTLY**, Issue No. 4, Vol. 17) on its website at [www.irs.gov/newsroom/article/0,,id=205921,00.html](http://www.irs.gov/newsroom/article/0,,id=205921,00.html). In tax years 2009 and 2010, ARRA provides a refundable tax credit of up to \$400 for individuals and \$800 for married taxpayers filing joint returns. The credit is phased out for individuals with modified adjusted gross income (AGI) of \$75,000-\$95,000 (\$150,000-\$190,000

for joint filers).

The guidance clarifies that employers are not required to make determinations with regard to an employee's eligibility for the Making Work Pay tax credit. Withholding should be made consistent with an employee's filed W-4 (*Employee's Withholding Allowance Certificate*) and the newly modified withholding tables (see Publication 15-T, [www.americanpayroll.org/members/Forms-Pubs/#annual](http://www.americanpayroll.org/members/Forms-Pubs/#annual)).

Several of the questions address the issue of employees

who may want to file an amended Form W-4 to avoid being under- or overwithheld by the end of the year.

- Individuals working more than one job at the same time may want to adjust their Forms W-4 to have more withheld. An individual who works two jobs concurrently may have reduced withholding, up to \$400, at each job. However, he or she will be entitled to a credit of only \$400. Note that this problem does not arise for someone who moves from a single job to another single job (no matter how many times).

- Married couples with both spouses earning wages may also want to adjust their Forms W-4 to have more withheld. The new tables, compared with those originally in place for 2009, will generally decrease federal income tax withholding by \$600 for married individuals. So, while the tax credit caps at \$800 for a couple filing jointly, the new withholding tables may “give” them a total tax credit of \$1,200 if they both earn wages. Note that a married person with a non-working spouse will have \$600 less in withholding but be entitled to a credit of \$800.

- The new withholding tables are also used for withholding from pensions, which are not “earned income.” Private pension recipients (who do not receive retiree or

disability benefits from the Social Security Administration, Department of Veteran’s Affairs, or Railroad Retirement Board) are not eligible for the Making Work Pay tax credit unless they have earned income. So pensioners may have \$400 or \$600 less withheld, even though this income is not eligible for the credit.

- The one-time “economic recovery payment” of \$250 in 2009 (paid to those receiving federal retiree or disability benefits from the Social Security Administration, Department of Veteran’s Affairs, or Railroad Retirement Board) may also throw off taxpayers’ calculations. For example, if both members of a married couple earn wages and receive social security benefits, they could each see a \$600 reduction in withholding and each receive a \$250 payment from the SSA, amounting to total assistance of \$1,700, even though they are only eligible for a credit of \$800.

☛ **APA OFFERS ON DEMAND WEBINARS ON ARRA** – To learn more about ARRA, sign up for an “on demand” webinar at [www.americanpayroll.org](http://www.americanpayroll.org). APA offers *How to Implement the New COBRA Premium Subsidy Through Payroll Taxes and Tax Tables, EIC, Transportation Fringes, and More.* ■

## APA’s Capital Summit, Part 2

In the **last issue of PAYROLL CURRENTLY**, we covered presentations at APA’s 5th Annual Capital Summit in Washington, D.C. on Internal Revenue Service implementation of the American Recovery and Reinvestment Act, e-services enhancements, and employment tax initiatives; Department of Homeland Security law enforcement priorities, the Form I-9 revision, and E-Verify enhancements; paycards and the state law obstacles they continue to face; and highlights of the National Taxpayer Advocate’s annual report of interest to employers. This article covers presentations on Office of Child Support Enforcement (OCSE) and Department of Labor (DOL) initiatives, IRS identity theft prevention efforts, new data requirements for international ACH transactions, potential problems under proposed cafeteria plan regulations, and Obama Administration budget proposals that would impact employers.

### Office of Child Support Enforcement

After acknowledging the important role that employers play in collecting 70% of the \$25 billion in child support that was paid in 2008, Sherri Grigsby, Manager of the Employer Services Team at the Office of Child Support Enforcement, outlined several areas where OCSE is trying to ease the compliance burden for employers.

**e-IWOs.** Grigsby first announced that OCSE’s electronic income withholding order (e-IWO) portal is being used by 15 states, and said they hoped 10 more would be on board by the end of 2009.

The portal allows states to post e-IWOs in a format employers can use and facilitates the exchange of relevant information, such as the employment status of the noncustodial parent, or upcoming lump sum payments. The portal also allows employers to acknowledge receipt of the e-IWO in formats that do not require programming – spreadsheet or fillable PDF. The feasibility of expanding the portal to handle an electronic National Medical Support Notice is now being considered, Grigsby said.

**Electronic payments.** As she always does when speaking to employers, Grigsby encouraged the use of electronic payments (42% sent that way in 2008) as a cheaper, faster, and more accurate alternative to checks for getting payments to the state disbursement unit (SDU). She acknowledged that employers are

sometimes faced with withholding orders that direct payment somewhere other than the SDU and asked those in the audience to let OCSE know when that happens.

**Lump sum payments.** Grigsby acknowledged that withholding child support from lump sum payments continues to be a tough problem for employers because the states do not treat such payments uniformly under their state laws. Some treat them as income subject to the limits on child support withholding in state law and the Consumer Credit Protection Act, while others allow 100% of such payments to be taken to satisfy child support obligations. Grigsby said that information about state treatment of lump sum payments can be found at OCSE’s employer services website and employers can exchange information with state agencies through the e-IWO portal.

### Department of Labor: FLSA enforcement

Before leaving his post as Administrator of DOL’s Wage and Hour Division earlier this year, Alex Passantino helped set the Division’s enforcement priorities for fiscal year 2009. The areas that made the list are not that much different from those receiving attention in recent years, including:

- Child labor – underage use of balers and compactors;
  - Recidivism – did an employer that violated the Fair Labor Standards Act (FLSA) earlier commit new violations; did the employer receive enough education to avoid future violations;
  - Low wage industries – agriculture, day care, restaurants, garment manufacturing, guard services, health care, hotels/motels, janitorial services, and temporary help;
  - Regional issues – grocery stores, car washes, gas stations, Gulf Coast rebuilding, reforestation, construction, child labor in malls, and landscaping;
  - Regular rate of pay issues;
  - White collar exemption compliance;
  - Protecting day laborers;
  - Combating human trafficking;
  - Hours worked – is all time being tracked; donning and doffing; and
  - Increased enforcement of Davis-Bacon Act requirements
- That will be effective in carrying out its enforcement mandate, Passantino said the Division will request 300 more investigators,

which would boost the total to more than 1,000, plus more funding for DOL's solicitor to bring more lawsuits. And if Congress should enact comprehensive immigration reform, he noted, many more DOL personnel would be required since the Wage and Hour Division has co-enforcement authority under the Immigration Reform and Control Act with U.S. Immigration and Customs Enforcement.

### Identity theft

In his remarks, Robert Belair, a partner at Olaker, Belair & Wittie, LLP, warned attendees that the exposure of personally identifiable information (PII) continues to increase, with 656 data breaches reported in 2008, a 47% increase from the year before. He also said that 44 states now have data breach laws that require reporting of breaches to state and local agencies, notification of affected individuals (e.g., employees, customers), and mitigation of the effects of the breach (e.g., free credit reports).

**Identity theft prevention.** Belair offered some hints on how employers and third-party service providers can help prevent data breaches from occurring:

- Employ comprehensive security;
- Use effective employee screening, training, and supervision, including background checks;
- Don't allow PII to be maintained on employees' laptops or other mobile devices;
- Encrypt data;
- Pay attention to physical security, access controls (i.e., passwords, logins), and "shoulder surfing";
- Implement a sufficient data archive and destruction policy;
- Avoid collecting and maintaining "trigger data" where possible, including full SSNs and bank account numbers;
- Identify your risks;
- Audit your policies and procedures; and
- Have a comprehensive training program.

**IRS identity theft prevention efforts.** Following Belair, IRS Director of the Office of Privacy, Information Protection and Data Security, Deborah Wolf, detailed what the IRS is doing to help prevent identity theft and mitigate its effects on taxpayers. She said that since October 2008, IRS's new Identity Protection Specialized Unit has handled 70,000 phone calls from people who feel they have been impacted by ID theft and attempted to quickly resolve their issues.

• **Account indicators.** They have also implemented account indicators that mark taxpayer accounts for a special ID theft review that can prevent victims from having tax problems in the future. And they will be sending out notices this year to taxpayers who the IRS thinks may be victims of ID theft because their SSN is shown on a Form W-2 filed with a tax return containing an Individual Taxpayer Identification Number (ITIN).

• **Rethinking SSN use.** As part of a federal government mandate to determine how SSNs are used and how their use can be reduced to help avoid ID theft, Wolf said the IRS reviewed SSN use on nearly 1,000 internal and external forms to see if the SSN is required. As a result, many internal IRS forms are being revised to eliminate, partially redact, or mask the SSN. The IRS is also testing the use of an alternative identifier to replace the SSN with combinations of fragments of PII data, where each fragment is not enough to allow disclosure of taxpayer identity but would still constitute a unique identification of a taxpayer.

At the same time, Wolf said, the IRS is preparing a revenue procedure for late summer or fall that would allow businesses to mask a TIN on a Form 1099 without penalty. She said that

allowing SSN-masking on Forms W-2 will require legislative action.

### International ACH transactions (IATs)

**New data requirements.** As part of this country's effort to prevent payments to foreign terrorists and drug dealers, the Office of Foreign Assets Control (OFAC) and NACHA-The Electronic Payments Association have created new Standard Entry Codes (SECs) and formats to identify International ACH Transactions (IATs) that must be used beginning September 18, 2009. Priscilla Holland, NACHA's Senior Director of International Programs, and Alexandre Manfull, OFAC's Chief of Implementation, expressed their concern to the Capital Summit audience that many employers and payroll service providers are not yet aware of the new requirements, or are not sure whether their payroll and pension payments qualify as IATs.

Holland said that a payment transaction is an IAT if it involves a financial agency's office that is outside the territorial jurisdiction of the U.S., and she emphasized that employers need to look at where the funding for the ACH payments is coming from. She also stressed that if a transaction is an IAT and the necessary information is not included, the payments will be rejected and people will not get paid. The typical payroll IAT may involve a U.S. subsidiary of a foreign corporation whose U.S. employees are paid with funding coming from the parent's bank in a foreign country through a U.S. bank. But Holland and Manfull said it gets more complicated when the funding coming from outside the U.S. is not explicitly for payroll, but may be for general accounts payable needs, with some part of it directed to fund payroll.

**Gearing up for the new requirements.** The purpose of their presentation was to alert audience members to contact their financial institutions and service providers and make them aware of the new data requirements for IATs. With less than six months to prepare, there is not a lot of time left, and the consequences – unpaid employees and retirees – can be very unpleasant and costly. Holland said that employers need to ask their financial institutions several questions:

- What will new reports look like?
- How can all the new addenda details be obtained?
- Do I need to receive all of the addenda details?
- How will the new transmissions be formatted?

She also said that businesses need to discuss the requirements and options with third parties that originate payments on their behalf, including payroll processors, electronic bill presentation and payment vendors, and accounts payable outsourcers.

### New cafeteria plan rules – a safe harbor or shark-infested waters?

When the IRS repropounded regulations under IRC §125 governing cafeteria plans in 2007, they did so in an attempt to update and consolidate guidance dating back to 1984, with the goal of finalizing the rules sometime in 2008 and having them take effect in 2009. As it stands now, noted Kevin Knopf, Attorney Adviser, Office of Benefits Tax Counsel at the Treasury Department, IRS and Treasury hope to finalize the new rules later this year, but he would not speculate on whether they would take effect in 2010 or 2011. Most commenters on the new rules, including APA, were generally pleased with the proposal, but there are several areas where we believe changes and clarifications still need to be made.

**Problems with the proposed regulations.** APA's Tax and Benefits Counsel, Mary Hevener, a partner at Morgan, Lewis &

Bockius LLP, and Senior Manager of Government Relations, Scott Mezistrano, CPP, said that one of the most problematic new rules makes §125 the exclusive vehicle for providing employees a choice between taxable and nontaxable benefits unless another Code section specifically provides for such a choice. If this proposed rule is finalized as is, Hevener argued, §125 would not be a safe harbor where employers that complied with its restrictions could be sure their employees would not be taxed when choosing nontaxable benefits over taxable ones. It would serve as a bludgeon creating a taxable benefit where an employee chooses a working condition fringe benefit such as a larger office or a more generous business travel expense arrangement over a higher salary.

Hevener also pointed out that the proposed rules would disqualify an employer's entire cafeteria plan and tax plan participants on the taxable benefits they could have chosen if the plan does not meet all the detailed regulatory requirements. When she asked Knopf if the IRS was planning to include provisions allowing employers to "cure" their plans to avoid disqualification, he said the IRS was "sensitive to this issue" and will address it in the final regulations. He also said employers can avoid individual mistakes by not giving pre-tax treatment to employees who make a late election under the plan or do something else wrong.

**What to do until the final regulations take effect.** Hevener also had some advice for employers on what to do in the meantime, until the final regulations are issued and take effect:

- Employers may be holding off on making plan changes until the proposed rules are finalized, but they should update their plan documents to describe any current benefits they provide, including a grace period for a medical FSA or pre-tax or rollover contributions to an HSA.

- Employers should be gearing up for the new nondiscrimination rules being proposed, which will require uniformity in benefits and pricing.

- Make sure that payroll processes do not allow participants to pay for retroactive coverage on a pre-tax basis, with limited 30-day window and FMLA catch-up payment exceptions.

- Make sure FSA administrators are correctly handling the substantiation requirements of the new rules, including special rules for debit cards.

- Ensure that electronic communications and elections meet

the safe harbor in the proposed rules.

- Let employees know now that cafeteria plans are subject to nondiscrimination rules that may limit pre-tax benefits for certain employees.

### Obama budget initiatives on the horizon

**Automatic IRAs.** In discussing upcoming initiatives contained in President Obama's FY 2010 budget, Melissa Mueller, Tax Counsel for the House Ways and Means Committee, and Tom Reeder, Benefits Tax Counsel in the Office of Tax Policy at the Treasury Department, both said that "automatic IRAs" are a distinct possibility. Employers with more than 10 employees that don't offer a qualified retirement plan would be required to deduct pre-tax contributions from their employees' pay (unless an employee elects not to contribute) and move the amounts to a fund picked by the employee or the employer, or to a fund similar to the thrift savings plan that is available to federal government employees.

**Health care W-2 reporting.** On the issue of health care reform, President Obama has said that "everything is on the table," including a cap on the income tax exclusion for employer-provided health insurance. If that actually comes to pass, said Reeder, then employers should expect that the cost of employer-provided coverage would have to be reported on Form W-2 so the tax implications for the employee can be determined. Mueller cautioned the audience that putting a cap on the income tax exclusion is still a very sensitive political issue, and its inclusion in any overall health care reform package is not a certainty.

**Increased frequency of wage reporting.** Another issue brought up by Reeder was the possibility of increasing the frequency of wage reporting by employers to the SSA – which also appears in the President's FY 2010 budget proposal – to help the SSA in its retirement benefit predictions. This issue was also addressed briefly at an earlier session by Chuck Liptz, SSA's Director, Division of Electronic Services Support and Communications. Liptz acknowledged that, in analyzing the wage reporting system and looking at ways to improve it, one of the changes being considered is more frequent wage reporting by employers. To make sure that payroll professionals are heard on this subject before any final decisions are made, APA is creating an Earnings Reporting Subcommittee of its Government Affairs Task Force. ■

## IRS Issues Updates to Publications 15, 15-B

The IRS has posted notes on its website [items dated 4-6-09 (15-B) and 4-13-09 (15); [www.irs.gov/formspubs/article/0,,id=109875,00.html](http://www.irs.gov/formspubs/article/0,,id=109875,00.html)] cautioning taxpayers about updates to the 2009 Publications 15 (Circular E), *Employer's Tax Guide*, and 15-B, *Employer's Tax Guide to Fringe Benefits*, based on tax law changes in the American Recovery and Reinvestment Act of 2009 (ARRA; see *PAYROLL CURRENTLY*, Issue No. 4, Vol. 17).

### Publication 15

New tables for withholding and advance earned income credit (EIC) payments have been developed due to changes made to the tax law by ARRA. The new tables can be found in Publication 15-T, *New Wage Withholding and Advance Earned Income Credit Payment Tables (For Wages Paid Through December 2009)*.

On page 11, the first sentence under *Employee business expense reimbursements* has been changed to read as follows: "A reimbursement or allowance arrangement is a system by which you pay the advances, reimbursements, and charges for your employees' business expenses."

On page 11, under *Accountable plan*:

- The last sentence in item (1) has been changed to read as follows: "The reimbursement or advance must be paid for the expense and must not be an amount that would have been paid by the employee."

- Item (2) has been changed to read as follows: "They must substantiate these expenses to you within a reasonable period of time."

- Item (3) has been changed to read as follows: "They must return any amounts in excess of substantiated expenses within a reasonable period of time."

On page 20, in the *Caution* under the section titled *How to figure the advance EIC payment*, amounts previously reported as "\$35,464" and "\$38,584" have been changed to "\$35,463" and "\$40,463," respectively.

On page 24, under *How to deposit with a FTD coupon*, three new paragraphs have been added at the end of this section to advise that the Financial Agent cannot process foreign checks. If a check written on a foreign bank to pay a federal tax deposit

is sent to the Financial Agent, generally you will be charged a deposit penalty and will receive a bill in the mail.

☞ **IMPORTANT NOTE** – Revised Publication 15 and Publication 15-T are both available on the APA website at [www.americanpayroll.org/members/Forms-Pubs/#annual](http://www.americanpayroll.org/members/Forms-Pubs/#annual).

#### Publication 15-B

On page 20, under the heading *Exclusion from wages*, the first bullet point should read as follows:

- For combined commuter highway vehicle transportation

and transit passes:

- \$120 per month for the months of January and February 2009 and
- \$230 per month for the months of March through December 2009.

☞ **IMPORTANT NOTE** – The IRS advises that the publication will not be revised at this time. The update will be reflected in a future revision. ■

## IRS Issues More Q&A Guidance on Premium Assistance for COBRA Continuation Coverage

IRS Notice 2009-27, issued March 31, 2009, provides guidance in the form of 58 questions and answers on several issues related to the new COBRA premium subsidies under the American Recovery and Reinvestment Act of 2009 (ARRA; see *PAYROLL CURRENTLY*, Issue No. 4, Vol. 17) not covered in earlier releases. A sample of the guidance is included here; the complete document is available at [www.irs.gov/pub/irs-drop/n-09-27.pdf](http://www.irs.gov/pub/irs-drop/n-09-27.pdf).

#### Involuntary termination

**Q. What circumstances constitute an involuntary termination for purposes of the definition of an assistance eligible individual?**

A. An involuntary termination means a severance from employment due to the independent exercise of the unilateral authority of the employer to terminate the employment, other than due to the employee's implicit or explicit request, where the employee was willing and able to continue performing services. An involuntary termination may include:

- The employer's failure to renew a contract at the time the contract expires, if the employee was willing and able to execute a new contract providing terms and conditions similar to those in the existing contract and to continue providing the services.
- In addition, an employee-initiated termination from employment constitutes an involuntary termination from employment for purposes of the premium reduction if the termination from employment constitutes a termination for good reason due to employer action that causes a material negative change in the employment relationship for the employee.

**Other qualifying events.** Involuntary termination is the involuntary termination of employment, not the involuntary termination of health coverage. Thus, qualifying events other than an involuntary termination, such as divorce or a dependent child ceasing to be a dependent child under the generally applicable requirements of the plan (such as loss of dependent status due to aging out of eligibility), are not involuntary terminations qualifying an individual for the premium reduction. In addition, involuntary termination does not include the death of an employee or absence from work due to illness or disability.

**Facts and circumstances.** The determination of whether a termination is voluntary is based on all the facts and circumstances. For example, if a termination is designated as voluntary or as a resignation, but the facts and circumstances indicate that, absent such voluntary termination, the employer would have terminated the employee's services, and that the employee had knowledge that the employee would be terminated, the termination is involuntary.

**Q. Does an involuntary termination include a lay-off period with a right of recall or a temporary furlough period?**

A. Yes. An involuntary reduction to zero hours, such as a lay-off, furlough, or other suspension of employment, resulting in a

loss of health coverage is an involuntary termination for purposes of the premium reduction.

**Q. Does an involuntary termination include a reduction in hours?**

A. Generally no. If the reduction in hours is not a reduction to zero, the mere reduction in hours is not an involuntary termination. However, an employee's voluntary termination in response to an employer-imposed reduction in hours may be an involuntary termination if the reduction in hours is a material negative change in the employment relationship for the employee.

#### Assistance eligible individual (AEI)

**Q. If the involuntary termination occurs before September 1, 2008, but the loss of coverage resulting in eligibility for COBRA continuation coverage occurs after September 1, 2008 (but no later than December 31, 2009), can the individual become an AEI?**

A. No. The involuntary termination resulting in COBRA continuation coverage must occur during the period from September 1, 2008, through December 31, 2009. Although IRC §4980B(f)(8) allows a plan to provide that the COBRA continuation coverage does not begin until the loss of coverage, that does not change the date of the involuntary termination.

**Q. If an individual's involuntary termination occurs no later than December 31, 2009, but the loss of coverage resulting in eligibility for COBRA continuation coverage occurs after December 31, 2009, is the individual an AEI?**

A. No. Both the involuntary termination and eligibility for COBRA continuation coverage must occur during the period from September 1, 2008, through December 31, 2009. If the loss of coverage is after December 31, 2009, the individual cannot become an AEI.

**Q. Does an involuntary termination of an employee following another qualifying event, such as a divorce, satisfy the requirement for the qualified beneficiary from the first qualifying event to be an AEI?**

A. No. Generally, if COBRA continuation coverage is based on a qualifying event before the involuntary termination, the later involuntary termination does not cause the qualified beneficiary to become an AEI. However, if in anticipation of an involuntary termination that would otherwise qualify an individual as an AEI, the employer takes action other than the involuntary termination of the individual that results in a loss of coverage for the individual (for example, a reduction in hours for the employee in anticipation of involuntarily terminating the employee), the action causing the loss of coverage prior to the involuntary termination is disregarded in determining whether involuntary termination is the qualifying event that results in the COBRA continuation coverage for the individual (see Notice 2009-27,

A-15, for examples).

**Q. Can an individual become an AEI more than once?**

A. Yes. An individual who becomes a qualified beneficiary as the result of an involuntary termination and who otherwise meets the requirements to be an AEI is treated as an AEI even if previously treated as an AEI.

**Calculation of premium**

**Q. What premium amount is used to determine the 35% share that must be paid by (or on behalf of) an AEI?**

A. The premium used to determine the 35% share that must be paid by (or on behalf of) an AEI is the cost that would be charged to the AEI for COBRA continuation coverage if the individual were not an AEI. If, without regard to the subsidy, the AEI is required to pay 102% of the "applicable premium" for continuation coverage, i.e., generally the maximum permitted under the federal COBRA rules, the AEI is required to pay only 35% of the 102% of the applicable premium. However, if the premium that would be charged the AEI is less than the maximum COBRA premium, for example if the employer subsidizes the coverage by paying all or part of the cost, the amount actually charged the AEI is used to determine the AEI's 35% share.

In determining whether an AEI has paid 35% of the premium, payments on behalf of the individual by another person (other than the employer that involuntarily terminated the employee) are taken into account. For example, some or all of the 35% share of the premium could be paid on behalf of the individual by a parent, guardian, state agency, or charity (see Notice 2009-27, A-20, for examples).

**End of premium reduction period**

**Q. If an AEI is eligible for other group health plan coverage but does not enroll, is the premium reduction available for the individual's COBRA continuation coverage after the date the individual is first eligible for the other coverage?**

A. No.

**EXAMPLE 1.** An AEI begins employment with a new employer and is eligible to enroll in the employer's group health plan, with coverage effective the first day of the next month. The AEI declines the coverage and continues COBRA continuation coverage. Although eligibility for other group health coverage does not end the individual's eligibility for federal COBRA, the premium reduction is no longer available as of the first day of the next month.

**EXAMPLE 2.** Same facts as above, except that the new employer's group health plan imposes a two-month waiting period. The premium reduction stops being available as of the first day after the end of the waiting period, even though the employee declined coverage under the plan. It is the same result if the employee had enrolled for coverage; the premium reduction would apply until the first day after the end of the waiting period.

**EXAMPLE 3.** The spouse of an AEI (who is also an AEI) begins employment with a new employer and is eligible to enroll in the employer's group health plan with self-only or family coverage, with coverage effective the first day of the next month. The spouse enrolls in self-only coverage, and the AEI continues COBRA continuation coverage. Although the individual is allowed to continue federal COBRA, the premium reduction is no longer available for the COBRA continuation coverage as of the first day of the next month because the AEI is eligible for coverage under the group health plan of the spouse's employer.

**Q. Is an AEI who otherwise meets the eligibility**

**requirements for coverage under a group health plan, but who cannot enroll and have coverage take effect immediately, considered eligible for coverage under the group health plan for purposes of ending the period of premium reduction?**

A. No. An individual who is eligible to enroll for coverage under a group health plan is considered to be eligible for coverage under the group health plan for purposes of ending the period of premium reduction only from the first date that coverage can take effect. For example, if, as of February 17, 2009, an AEI meets the eligibility requirements for coverage under a group health plan maintained by the individual's spouse, but cannot enroll and have coverage take effect immediately, the individual may receive the premium reduction for periods of coverage until the first date that coverage can take effect under the plan maintained by the spouse's employer.

**Q. If an AEI receiving a premium reduction from an employer fails to provide notice of his/her eligibility for coverage under any other group health plan or Medicare and continues receiving the premium reduction, is the employer required to refund to the IRS the payroll tax credit relating to the premium reduction provided with respect to the period after the individual's eligibility for the premium reduction ended?**

A. No. If the employer has claimed a payroll tax credit for the premium reduction, the employer is not required to refund to the IRS the excess premium reduction received as a credit merely because the AEI failed to provide notice that he/she is no longer eligible for the premium reduction due to eligibility for coverage under any other group health plan or Medicare unless the employer otherwise knew of the eligibility for such coverage. The AEI who failed to provide notice may be subject to a federal tax penalty of 110% of the premium reduction improperly received.

**Q. How long is the period of premium reduction for an individual who becomes an AEI a second time?**

A. An AEI is eligible for up to nine months of premium reduction for each involuntary termination.

**EXAMPLE.** An individual is involuntarily terminated and loses coverage as of April 1, 2009. The individual otherwise meets the requirements for an AEI and is allowed the premium reduction for COBRA continuation coverage beginning April 1, 2009. On July 1, 2009, the individual ceases to be an AEI because of coverage under a group health plan provided by the employer of the individual's spouse. Subsequently, the spouse is involuntarily terminated, the individual loses coverage as of November 1, 2009, and, at that time, otherwise meets the requirements for being an AEI. The individual is allowed up to nine months of premium reduction with respect to the involuntary termination of the spouse.

**Recapture of premium assistance**

**Q. Can a plan refuse to provide the premium reduction to an individual because of the individual's income?**

A. No. Even if an AEI's income is high enough that the recapture of the premium reduction would apply, COBRA continuation coverage must be provided upon payment of 35% of the premium unless the individual has notified the plan that he/she has elected the permanent waiver of the premium reduction (or the period for the premium reduction has ended).

**Q. How does an AEI make a permanent election to waive the right to the premium reduction?**

A. An AEI who wants to make a permanent election to waive the right to the premium reduction does so by providing a signed

and dated notification (including a reference to “permanent waiver”) to the person who is reimbursed for the premium reduction under IRC §6432. There is no separate additional notification to any government agency. If an AEI makes the permanent election to waive the right to receive the premium reduction, the individual may not later reverse the election and may not receive the premium reduction for any future period of COBRA continuation coverage in 2009 or 2010, regardless of modified adjusted gross income in those years.

#### Extended election period

**Q. If an employee was involuntarily terminated during the period from September 1, 2008, through February 17, 2009, and elected self-only COBRA continuation coverage, are a spouse and dependent children who are qualified beneficiaries in connection with the involuntary termination allowed to elect COBRA continuation coverage and receive the premium reduction under the extended election period?**

A. Yes. An individual who does not have an election of COBRA continuation coverage in effect on February 17, 2009, but who would have been an AEI if the election were in effect is allowed a second opportunity to elect COBRA continuation coverage. The resulting coverage begins with the first period of COBRA continuation coverage beginning on or after February 17, 2009. A spouse or dependent child who is a beneficiary under a group health plan that covers an employee on the day before the employee’s involuntary termination (whose termination was on or after September 1, 2008) would have been an AEI if the spouse or dependent child timely elected COBRA continuation coverage and thus qualifies for the second election, notwithstanding the prior election of self-only COBRA continuation coverage by the employee.

**Q. Is the extended election period available to involuntarily terminated employees whose continuation coverage is provided pursuant to state law only?**

A. Generally, no. The extended election period under ARRA applies to a group health plan that is subject to federal COBRA

or the temporary continuation requirements of the Federal Employees Health Benefits Program. It does not apply to plans subject to COBRA continuation coverage requirements under a state program that provides comparable continuation coverage. However, if a state program provides for a similar special election and an individual otherwise satisfies the requirements to be an AEI, the premium reduction is available for any resulting continuation coverage.

#### Payments to insurers under federal COBRA

**Q. In the case of an insured plan that is not a multiemployer plan and that is subject to the COBRA continuation provisions of the IRC, if the insurer and the employer have agreed that the insurer will collect the premiums directly from the qualified beneficiaries, is the insurer required to treat an AEI paying 35% of the premium as having paid the full premium, even before the employer pays the remaining 65%?**

A. Yes. If the insurer fails to treat a 35% payment by an AEI as a payment of the full premium, the insurer may be liable for the excise tax under IRC §4980B(e)(1)(B), which applies to each person responsible (other than in a capacity as an employee) for administering or providing benefits under the plan and whose act or failure to act caused (in whole or in part) the failure, if the person assumed responsibility for the performance of the act to which the failure relates.

#### Comparable state continuation coverage

**Q. In the case of an insured plan subject solely to state law requiring the insurer to provide continuation coverage, if the employer collects the reduced premiums from AEIs and pays the full premium to the insurer, is the employer eligible to take the payroll credit directly?**

A. No. Under IRC §6432(b)(3), in the case of an insured plan subject solely to state law with respect to the requirement to provide continuation coverage, the only person entitled to be reimbursed for the premium reduction through the payroll credit is the insurer providing the coverage under the group health plan. ■

## IRS Lists Countries for Which Foreign Earned Income Exclusion Requirements Are Waived for 2008

In Rev. Proc. 2009-22 [[www.irs.gov/pub/irs-drop/rp-09-22.pdf](http://www.irs.gov/pub/irs-drop/rp-09-22.pdf)], the IRS has announced the list of countries for which the foreign earned income exclusion requirements of IRC §911 are waived for 2008 (with departure dates). The list includes Chad (2-3-08), Serbia (2-22-08), and Yemen (4-7-08).

IRC §911 allows a “qualified individual” to exclude foreign earned income from gross income up to a certain amount (\$87,600 in 2008). An employer need not withhold federal income tax from any wages paid to a qualifying employee it reasonably believes will be excluded under §911. A qualifying individual is an individual who is a U.S. citizen and a bona fide resident of or present in a foreign country for a specified portion of the taxable year (see *The Payroll Source*®, beginning at p. 14-6, for a detailed discussion).

IRC §911(d)(4) provides an exception to these eligibility requirements if an otherwise qualified individual:

- leaves a listed foreign country because of war, civil unrest, or similar adverse conditions that preclude the normal conduct of business,
- on or after a certain date,
- pursuant to a determination by the Secretary of the Treasury (in consultation with the Secretary of State).

In such a case, the income exclusion will apply even though the individual was not in the foreign country for the statutorily prescribed period, if the individual can show that *but for* the adverse conditions he or she had a reasonable expectation of meeting the requirements of §911. ■

## Facsimile Signature on Employment Tax Return Must Be That of a Person

The IRS Office of Chief Counsel has issued guidance interpreting Rev. Proc. 2005-39 (see [PAYROLL CURRENTLY, Issue No. 16, Vol. 13](#)), which permits “facsimile” signatures (defined as signatures “by rubber stamp, mechanical device, or computer software program”) on employment tax returns. The IRS clarifies that the signature affixed to an employment

tax return by an officer or agent using a facsimile means of signature must be that of a person [CCA 200912026, release date 3-20-09; [www.irs.gov/pub/irs-wd/0912026.pdf](http://www.irs.gov/pub/irs-wd/0912026.pdf)].

Rev. Proc. 2005-39 provides that, “Officers or agents using a facsimile means of signature are personally responsible for ensuring that their facsimile signature is affixed to returns.”

The Chief Counsel Advice explains that just as the signature on Forms 940/941 must otherwise be that of a person (the owner of a sole proprietorship or LLC, a duly authorized officer of a corporation, a duly authorized partner or officer

of a partnership, or a fiduciary of a trust or estate), “when a payroll service provider becomes the duly authorized agent for signature purposes, that duly authorized agent must also be a person.” ■



## STATE AND LOCAL NEWS

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### Arizona

**Withholding rates changed.** Effective 5-1-09 through 12-31-09, the withholding rates for state income taxes will increase as follows: 11.5% (currently 10%), 21.9% (currently 19%), 26.5% (currently 23%), 28.8% (currently 25%), 35.7% (currently 31%), and 42.6% (currently 37%) of the federal tax withheld. An employer must change an employee's withholding rate to the applicable new rate unless the employee completes a new Form A-4, *Employee's Arizona Withholding Percentage Election*, or Form A-4V, *Voluntary Withholding Request for Arizona Resident Employed Outside of Arizona*, electing a different rate. The Department of Revenue (DOR) will revise both forms.

Effective 1-1-10 through 6-30-10, the withholding rates for state income taxes will decrease as follows: 10.7% (from 11.5%), 20.3% (from 21.9%), 24.5% (from 26.5%), 26.7% (from 28.8%), 33.1% (from 35.7%) and 39.5% (from 42.6%) of the federal tax withheld. Effective 5-1-09 through 6-30-10, the withholding rate remains 0% for employees who had no state income tax liability in the prior taxable year and expect to have no state income tax liability in the current taxable year. Effective 7-1-10, withholding will be determined using tables adopted by the DOR by 3-15-10. This will allow the state to implement withholding rates that are not tied to the federal rates [S.B. 1185, L. 2009].

### California

**New bank for EFT.** Effective 7-1-09, the Employment Development Department's (EDD) electronic funds transfer (EFT) depository bank transactions for Automated Clearing House (ACH) payroll tax deposits (DE 88) will change to Citibank. The new data collector will be Metavante Corporation. ACH credit filers will receive a special notice dated 5-26-09 providing EDD's new banking information. For ACH debit filers, there will be a new website address and a new electronic payment option called “Just Pay It” (no processing fee, no registration required). For agents and payroll service companies, there will be a new web-based Bulk Filer Solution [EDD, Payroll Taxes, News; *California Employer*, First Quarter 2009].

### New York

**Income tax rate increased, fourth quarter return due date changed.** Effective for wages paid on or after 5-1-09, the Department of Taxation and Finance (DTF) has issued revised exact calculation method withholding tables to reflect changes in the New York State personal income tax rates and the Yonkers resident personal income surcharge tax rates [Publication NYS-50-T.1, *Revised New York State and Yonkers Withholding Tax Computation Rules*, available at [www.tax.state.ny.us/pdf/publications/withholding/nys50\\_t1.pdf](http://www.tax.state.ny.us/pdf/publications/withholding/nys50_t1.pdf)]. The DTF has issued a revised Form IT-2104, *Employee's Withholding Allowance Certificate*, which employers should begin using immediately (download at [www.tax.state.ny.us/pdf/2009/ffin/wt/it2104\\_409\\_fill\\_in.pdf](http://www.tax.state.ny.us/pdf/2009/ffin/wt/it2104_409_fill_in.pdf)).

Also effective 5-1-09, the supplemental wage tax rate for New York State increases to 11.03% from 7.35% (this updates *The Payroll Source*®, p. 6-36), and the supplemental wage tax rate for the Yonkers resident tax surcharge increases to 1.103% from 0.735%. Finally, the due date for the fourth quarter wage reporting and withholding reconciliation (Part C of Form NYS-45, *Quarterly Combined Withholding, Wage Reporting, and Unemployment Insurance Return*) is changed to January 31 from February 28 [A.B. 157, L. 2009].

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