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## IRS Releases Revised Form 941, Instructions

The IRS has released revised versions of Form 941, *Employer's Quarterly Federal Tax Return*, and the *Instructions for Form 941*, dated April 2009. The revised form and instructions are available on the APA website at [www.americanpayroll.org/members/Forms-Pubs/#tax](http://www.americanpayroll.org/members/Forms-Pubs/#tax). Notably, the instructions for Lines 12a and 12b have been revised. The instructions for Lines 12a and 12b have been changed to read as follows:

### Line 12a: COBRA premium assistance payments

"Report on this line 65% of the COBRA premiums for assistance eligible individuals. Take the COBRA premium assistance credit on this line only after the assistance eligible individual's 35% share of the premium has been paid. For COBRA coverage provided under a self-insured plan, COBRA premium assistance is treated as having been made for each assistance eligible individual who pays 35% of the COBRA premium. Do not include the assistance eligible individual's 35% of the premium in the amount entered on this line."

### Line 12b: Number of individuals provided COBRA premium assistance on Line 12a

"Enter the total number of assistance eligible individuals provided COBRA premium assistance reported on Line 12a. Count each assistance eligible individual who paid a reduced COBRA premium in the quarter as one individual, whether or not the reduced premium was for insurance that covered more than one assistance eligible individual. For example, if the reduced COBRA premium was for coverage for a former employee, spouse, and two children, you would include one individual in the number entered on line 12b for the premium assistance. Further, each individual is reported only once per quarter. For example, an assistance eligible individual who made monthly premium payments during the quarter would only be reported as one individual." *Note:* The instructions for Line 12b now parallel the COBRA Q&A dated May 1 (see [PAYROLL CURRENTLY, Issue No. 10, Vol. 17](#)). ■

## IRS Offers Pensioners Relief From Underwithholding Caused by Making Work Pay Credit in 2009

The IRS has issued Notice 1036-P, *Additional Withholding for Pensions for 2009* [[www.irs.gov/pub/irs-pdf/n1036p.pdf](http://www.irs.gov/pub/irs-pdf/n1036p.pdf)]. Notice 1036-P includes optional 2009 withholding tables for calculating additional withholding amounts for

pension payments. The withholding amounts may be added to the amount of withholding determined from the percentage method, the wage-bracket method, or any other allowable method.

The procedure is an approximate offset for the withholding reduction included in the February 2009 withholding tables found in Publication 15-T, *New Wage Withholding and Advance Earned Income Credit Payment Tables*, which reflect the Making Work Pay credit. The IRS explains that the new procedure will help some pensioners avoid a smaller refund next spring or even a balance due in some situations. A wide variety of factors, such as outside jobs and other earned income, can affect how much, if any, withholding is needed by people receiving a pension to satisfy their annual tax liability.

Eligibility for the credit requires earned income, which does not include pension payments. Someone who receives a pension but not wages is not eligible for the Making Work Pay credit. Currently, however, pension payments are subject to

the same withholding tables as wage payments. Notice 1036-P aims to correct the underwithholding that would result in such a case.

Pension payers are not required to use this procedure, which is optional. Payers may continue to use only the February 2009 withholding tables to determine the amount of withholding.

*Note:* The IRS is encouraging pension payers that choose to implement the new withholding adjustment procedures to contact retirees who previously submitted a Form W-4P, *Withholding Certificate for Pension or Annuity Payments*, requesting additional withholding after the February withholding tables were issued. ■

## DOL Releases Form for Review of Denial of COBRA Premium Reduction

The U.S. Department of Labor (DOL) has posted an application on its website for those who believe they have been improperly denied a COBRA premium subsidy under the American Recovery and Reinvestment Act of 2009 (ARRA; Pub. L. No. 111-5; see *PAYROLL CURRENTLY, Issue No. 4, Vol. 17*). The *Application for Review of Denial of COBRA Premium Reduction*, together with a “quick check” on eligibility, general information, and instructions is accessible at [www.dol.gov/ebsa/COBRA/main.html](http://www.dol.gov/ebsa/COBRA/main.html).

An applicant requesting review of a denial of premium assistance may be either a former employee or a member of

the employee’s family who is eligible for COBRA continuation coverage or the COBRA premium assistance through an employment-based health plan. The applicant should include copies of any documents that will help the DOL in its review (examples are listed in the instructions). The DOL encourages applicants to complete and file the application online; the form may also be mailed or faxed, along with attachments.

*Note:* Individuals whose COBRA continuation coverage is provided through a federal, state, or local government plan, or pursuant to state insurance law, are advised to direct requests for review to the Department of Health and Human Services. ■

## IRS Announces HSA Limits for 2010

The IRS has issued guidance on the 2010 maximum contribution levels for Health Savings Accounts (HSAs) and out-of-pocket spending limits for High Deductible Health Plans (HDHPs) that must be used in conjunction with HSAs [Rev. Proc. 2009-29, 5-14-09; [www.irs.gov/pub/irs-drop/rp-09-29.pdf](http://www.irs.gov/pub/irs-drop/rp-09-29.pdf)]. The guidance is issued pursuant to the Tax Relief and Health Care Act of 2006 (Pub. L. No. 109-432; see *PAYROLL CURRENTLY, Issue No. 26, Vol. 14*), which provides that for taxable years beginning after December 31, 2006, the maximum annual HSA contribution is an indexed statutory amount. *Note:* The annual cost-of-living adjustments are released by June 1 for the following year.

### 2010 annual contribution levels for HSAs:

- The maximum annual HSA contribution for an eligible individual with self-only coverage is \$3,050 (\$3,000 in 2009).
- For family coverage, the maximum annual HSA contribution is \$6,150 (\$5,950 in 2009).
- The catch-up contribution for an individual age 55 or older is \$1,000 in 2009 and all years going forward.

*Note:* An individual who is an eligible individual on the first day of the last month of the taxable year (December for

most taxpayers) is allowed the full annual contribution (plus catch-up contribution, if 55 or older by year-end), regardless of the number of months the individual was an eligible individual in the year. For individuals who are no longer eligible individuals on that date, both the HSA contribution and catch-up contribution apply pro rata based on the number of months of the year a taxpayer is an eligible individual.

### 2010 amounts for out-of-pocket spending on HSA-compatible HDHPs:

- The maximum annual out-of-pocket amount for HDHP self-only coverage is \$5,950 (\$5,800 in 2009) and the maximum annual out-of-pocket amount for HDHP family coverage increases to twice that, \$11,900 (\$11,600 in 2009).

### 2010 minimum deductible amounts for HSA-compatible HDHPs:

- The minimum deductible for HDHPs increases to \$1,200 (\$1,150 in 2009) for self-only coverage and \$2,400 (\$2,300 in 2009) for family coverage.

*Note:* A fiscal year plan that satisfies the requirements for an HDHP on the first day of the first month of its fiscal year may apply that deductible for the entire fiscal year. ■

## DOL Explains Employee Notification Requirements Under New FMLA Regulations

In a Wage-Hour opinion letter, the U.S. Department of Labor (DOL) explains employee notification procedures under the Family and Medical Leave Act (FMLA) in light of final regulations issued in 2008 (see *PAYROLL CURRENTLY, Issue No. 24, Vol. 16*) [W-H Op. Ltr., FMLA2009-1-A (1-6-09)]. *Note:* the 2008 final regulations took effect on January 16, 2009.

### Background: FMLA-101

Under the FMLA, an employee is required to provide

notice of the need for leave for the birth or adoption of a child, to care for a seriously ill family member, or because the employee is seriously ill. Notice must be provided 30 days before the leave is to begin, where possible, and if it is not possible, then “as soon as practicable” (29 USC §2612(e)).

FMLA regulations issued in 1995 provided that when leave is foreseeable less than 30 days in advance, the practicability requirement “ordinarily would mean at least verbal notification

to the employer within one or two business days of when the need for leave becomes known to the employee” (former 29 C.F.R. §825.302(b)).

A Wage-Hour opinion letter issued in 1999 (FMLA-101) ruled that §825.302 prohibited an employer’s attendance policy that required employees taking intermittent FMLA leave to report within one hour after the start of their shift unless they were unable to report due to circumstances beyond their control because it was more stringent than the FMLA.

**Question.** An employer requests clarification of the one-hour policy in light of the 2008 FMLA regulations. It asks, for example, if it can enforce the policy against an employee who is absent on a Tuesday and Wednesday, does not call in on either day, and informs the employer of the need for FMLA leave when returning to work on Thursday.

**Ruling: FMLA-101 revisited**

The DOL explains that the “one or two business days” time frame in the 1995 regulations was misinterpreted to

permit employees two business days from learning of their need for leave to provide notice to their employers, regardless of whether it would have been practicable to provide the notice more quickly.

The 2008 regulations revised §825.302(b) to provide that when an employee becomes aware of the need for FMLA leave less than 30 days in advance, it should be practicable for the employee to provide notice of the need for leave on the same day or the next business day. In all cases, however, the determination of when an employee could practicably provide notice must take into account the individual facts and circumstances. To the extent that FMLA-101 has been interpreted to create a flat two-day notice rule, it is rescinded.

**Answer.** In the employer’s example, this means that unless unusual circumstances prevent the employee from providing notice of the need for FMLA leave in accordance with the employer’s policy, the employer may deny FMLA leave for the absence. ■

## Wage & Hour Roundup

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

**Child labor violations: penalties**

- The Wage & Hour Division has fined Atlanta-based Demon Demo, Inc. a total of \$53,162 following an investigation into the death of a teenage worker at a company demolition site from a second floor fall. This penalty is the first assessed under the Genetic Information Nondiscrimination Act of 2008 (see *PAYROLL CURRENTLY, Issue No. 11, Vol. 16*), which increased the maximum civil money penalty to \$50,000 for each child labor violation that results in the work-related death or serious injury of a minor. In addition to the \$50,000 penalty under the 2008 Act, an additional \$3,162 in fines was assessed because the company failed to keep accurate records and allowed the minor to work in a hazardous occupation.

- East Side Dairy Queen Co. of East Grand Forks, Minnesota, has been fined \$11,495 for violations of FLSA child labor provisions. The company allowed employees under 16 years of age to operate meat slicers, broilers, and deep fryers in violation of child labor occupation restrictions. Additionally, in violation of hour and time standards, employees under age 16 worked over three hours on school days and as late as 11:15 p.m. throughout the year.

**Compensable time: waiting time**

- Lozano Car Wash has paid \$268,501 in back wages owed to 270 employees. Wage & Hour investigators found that the workers were required to arrive at the car wash at a scheduled time but had to wait to be placed on the clock based on car wash service volume. Workers waited between 15 minutes to over an hour each day, and were not paid for this time.

**Hours worked: affiliated employers**

- Harris Farms, Inc., which employs people to work in several different support activities at the North American Stainless Steel Mill in Ghent, Kentucky, has agreed to pay \$374,184 in back wages to 417 employees. Wage & Hour investigators found that Harris failed to total all hours worked by employees among its several companies, resulting in employees being paid straight time wages despite working more than 40 hours in a workweek. In addition, Harris did not include monthly attendance and production bonuses in its employees’ regular rate of pay when computing earnings.

**Overtime: misclassification**

- Merrill Lynch & Co., Inc. has agreed to pay \$516,924 in back overtime wages to 60 employees at its New York City headquarters. Wage & Hour investigators found that the company erroneously classified “senior specialists” as FLSA-exempt administrative employees. Many of these employees worked as many as 55 hours per week but were paid only a straight salary for all hours worked.

**Overtime: straight time**

- Houston-based IFCO Systems, which manufactures and repairs reusable plastic containers and wooden pallets, has paid \$1,602,267 in back overtime wages to 1,751 employees in 17 states. Wage & Hour investigators found that the company did not pay its employees time and one-half for hours worked over 40 in a workweek.

- Bentonville, Arkansas-based America’s Car Mart, Inc. has paid \$117,023 in back overtime wages owed to 103 current and former management trainees. These employees were not compensated at time and one-half their regular rate of pay for overtime hours while in training. ■

## Update on Income Tax Treaties

The U.S. has income tax treaties with more than 60 countries. Income tax treaties may exempt or reduce the amount of withholding from wages earned by nonresident aliens in the U.S. if certain conditions are met (see *The Payroll Source*®, pp. 14-17 and 14-18 for additional discussion of income tax treaties). Since *PAYROLL CURRENTLY* last reported on the subject (see *Issue No. 18, Vol. 16*), an income tax treaty and protocols with Bulgaria have entered into force, as well as a protocol updating the income tax treaty with Canada, and a replacement income tax treaty with

Iceland.

**Treaty and protocols enter into force**

On September 23, 2008, the U.S. Senate ratified an income tax treaty and protocols with Bulgaria, a tax protocol with Canada, and a replacement income tax treaty with Iceland. The treaties and protocols all entered into force on December 15, 2008. They generally apply to tax years beginning on or after January 1, 2009.

**U.S.-Bulgaria.** The U.S. and Bulgaria signed their first income

tax treaty and protocol on February 23, 2007. On February 26, 2008, the two countries signed another protocol making technical corrections to the treaty.

In general, the agreements require Bulgaria to exempt the income of a resident of Bulgaria from its income tax if the income may be taxed in the U.S., while the U.S. is required to provide a credit against its income tax to a U.S. resident for income tax paid or accrued to Bulgaria. The agreements reduce, but do not eliminate, the rates of taxation on cross-border dividends, interest, and royalty payments, and generally eliminate withholding when cross-border dividends are paid to pension funds, and when cross-border interest is paid to the government of the other country or to a financial institution resident in the other country. Like the agreement negotiated by the U.S. with Belgium, this agreement has "limitation of benefits" provisions designed to prevent treaty shopping, which is the inappropriate use of a tax treaty by third-country residents, as well as provisions to improve the exchange of information.

**U.S.-Canada.** On September 21, 2007, the U.S. and Canada signed the fifth protocol updating their 1980 income tax treaty. The agreement eliminates source-country withholding tax on cross-border interest payments and clarifies the treatment of stock options. It also extends treaty benefits to limited liability companies. Existing treaty provisions governing pensions and annuities are modified to address cross-border pension contributions and benefit accruals, as well as Roth individual retirement accounts.

The protocol also provides for the arbitration of double-taxation issues – the third agreement by the U.S. to do so. As with arbitration provisions in agreements with Belgium and Germany, the "last best offer" by the competent authority of each country would be presented to an arbitrator, who would have to select one of the figures presented in order to settle the dispute.

*Note:* The Senate conditioned ratification of the Canadian protocol by requiring the Secretary of the Treasury to submit the rules of procedure to be used by the first arbitration under the Belgian, Canadian, and German agreements, as well as reporting requirements applicable to the 10th arbitration proceeding conducted under either the Belgian, Canadian, or German agreements.

**U.S.-Iceland.** On October 23, 2007, the U.S. and Iceland signed a new income tax treaty to replace the 1975 treaty between the two countries. The replacement treaty takes into account changes in the law and policies of both countries since the earlier treaty was signed. For example, it provides for a positive rate of withholding on certain cross-border royalty payments, in conformity with Iceland's current tax treaty policy. To conform to the current tax treaty policy of the U.S., the replacement treaty has a comprehensive limitation of benefits provision so that only residents satisfying the conditions of that paragraph enjoy the benefits of the treaty.

#### Treaties and protocols awaiting Senate ratification

**U.S.-France.** The U.S. and France signed an income tax treaty in 1994. A 2004 protocol amending the treaty entered into force in 2006. On January 13, 2009, the two countries signed a second protocol to further update the income tax treaty. It

provides for the elimination of source-country taxation of certain dividends and royalty payments. It also establishes a mandatory arbitration procedure for certain cases that cannot be resolved by the two countries' competent authorities, seeks to prevent treaty shopping, and modernizes rules for sharing taxpayer information between the two countries.

**U.S.-Malta.** On August 8, 2008, the U.S. and Malta signed an income tax treaty, the first between the two countries. It provides for reduced withholding rates on cross-border dividend payments, generally eliminates withholding on cross-border dividend payments to pension funds, and provides for withholding at 10% on interest, royalties, and other income. The treaty also contains a comprehensive limitation of benefits provision and provides for the exchange of information between the competent authorities to facilitate the administration of each country's tax laws. On January 15, 2009, the President transmitted the agreement to the Senate for ratification.

**U.S.-New Zealand.** On December 1, 2008, the U.S. and New Zealand signed a protocol to amend their existing income tax treaty, which dates from 1982. The protocol updates provisions governing limitation of benefits, nondiscrimination, and exchange of information to make the treaty more compliant with current U.S. tax treaty policy. It amends provisions governing relief from double taxation to clarify that it covers U.S. income taxes and excise taxes on private foundations imposed under the Internal Revenue Code, but not social security and unemployment taxes. And it removes a treaty article covering independent personal services (individuals performing services in an independent capacity).

#### Information about tax treaties

- Detailed summaries of the individual tax treaties currently in force between the U.S. and other countries can be found in the APA's *Guide to Global Payroll Management* (see [www.americanpayroll.org/publication/](http://www.americanpayroll.org/publication/)).

- IRS Publication 515 (*Withholding of Tax on Nonresident Aliens and Foreign Entities*) contains general tax treaty information, as well as a table of tax treaties providing information about tax exemptions for nonresident aliens. Publications 901 (*U.S. Tax Treaties*) and 597 (*Information on the U.S.-Canada Income Tax Treaty*) contain more detailed explanations. Form 6166 is a letter of U.S. residency certification for purposes of claiming benefits under an income tax treaty. Rev. Proc. 2006-54 ([www.irs.gov/irb/2006-49\\_IRB/ar13.html](http://www.irs.gov/irb/2006-49_IRB/ar13.html)) outlines the procedures for obtaining U.S. competent authority assistance under an income tax treaty to which the U.S. is a party. (The IRS Deputy Commissioner (International), Large and Mid-Size Business Division, acts as the U.S. competent authority in administering the operating provisions of tax treaties.)

All of these materials, plus tax treaties and proposed treaty documents themselves, and the current 2006 Model Income Tax Convention and its technical explanation (a Model Income Tax Convention is used by the U.S. as a starting point in negotiating bilateral tax treaties with other countries) can be found on the IRS website at [www.irs.gov/businesses/international/article/0,,id=96739,00.html](http://www.irs.gov/businesses/international/article/0,,id=96739,00.html). ■

## Employment Agency Assessed \$5.8 Million in Employment Taxes and Penalties

The U.S. Tax Court has upheld an IRS assessment of federal income and FICA tax deficiencies and fraud penalties totaling more than \$5.8 million against an employment agency that failed to report wages of nearly \$15 million on up to 90%

of its temporary laborers [*Hi-Q Personnel, Inc. v. Commissioner*, 132 T.C. No. 13, 2009 U.S. Tax Ct. LEXIS 12 (5-4-09)].

#### Background

Hi-Q Personnel, Inc. supplied temporary laborers to

more than 250 client companies for a fee. Clients were not allowed to pay any money, goods, or services to the laborers without Hi-Q's prior consent. Hi-Q agreed to: pay the laborers; withhold and deposit federal, state, and local payroll taxes; and provide workers' compensation insurance for the laborers. Hi-Q billed clients \$9 per hour for the services of its laborers, payable in full by check within seven days of Hi-Q's invoice. This rate included not only gross wages, but also a fee for Hi-Q.

When Hi-Q hired temporary laborers to work for client companies, it gave them the choice of being paid by check on its regular payroll (treated as employees, and subject to employment tax withholding and reporting) or in cash (off the company's payroll with no withholding or reporting of employment taxes). Up to 90% of the temporary laborers chose to be paid in cash and off the books.

The IRS issued a notice of determination of worker classification and assessed employment taxes (federal income and FICA taxes) and fraud penalties against Hi-Q.

#### **Officer of employment agency was responsible for paying employment taxes**

In 2002, Luan Nguyen, the president and sole shareholder of Hi-Q from 1995 to 1998 (the tax years in question), was criminally indicted on multiple charges, including conspiracy to defraud the U.S. and willful failure to collect and pay over taxes due the U.S.

In 2003, Nguyen agreed to a plea bargain in which he admitted guilt to all counts of the indictment in exchange for a sentence of 150 months in prison and \$1,000 in special assessments. The IRS argued that Nguyen's plea determined the issue of Hi-Q's responsibility to pay employment taxes and the court agreed.

In Nguyen's criminal case the ultimate issue was whether Hi-Q filed false or fraudulent Forms 941 for 16 calendar quarters between 1995 and 1998 because it failed to pay employment taxes to the laborers paid in cash. The court explained that a corporation can only act through its officers, and Nguyen's duty to file accurate Forms 941 grew out of his position as Hi-Q's president.

#### **Employment agency was the employer**

The Internal Revenue Code (IRC §§3102, 3111, and

3402) requires employers to withhold FICA and federal income taxes from wages paid to employees, and to pay the employer's share of FICA taxes. An "employer" is the person for whom an individual performs services; however, if the person for whom the services are performed does not control the payment of wages for those services, the employer is the person having control over the payment of wages (IRC §3401(d)).

Here, Hi-Q set and paid the wages of its temporary laborers. Therefore, said the court, the company was the employer of the temporary laborers and liable for all employment taxes associated with those payments. Clients did nothing more than pay Hi-Q according to rates set in their contracts, for the services performed by the temporary laborers.

#### **Assessment: withholding rate for unpaid employment taxes**

The IRS assessed employment taxes based on the same withholding rate the company used when filing Forms 941 for its employees paid by check, and the court said this approach was reasonable. Given Hi-Q's failure to secure Forms W-4 from the temporary laborers, a rate of 28% could have been proposed, so the rate used on the Forms 941 was more favorable to the company.

#### **Assessment: penalties for fraud**

If fraud is involved in the underpayment of tax, a penalty equal to 75% of the underpayment due to fraud is imposed (IRC §6663(a)). Here, the entire underpayment was attributable to fraud.

The court explained that even without Nguyen's conviction for conspiracy to defraud the U.S., the facts independently supported a finding of fraud. Hi-Q, acting through its agents, paid temporary laborers cash wages without deducting employment taxes. The company clearly understood its tax obligations because it met them with respect to workers paid by check. To hide client payments covering cash-paid workers, the company had some checks cashed at check-cashing establishments and failed to record them on its books. In this way, the company evaded its share of FICA taxes for the cash-paid laborers. ■

## **Horse Race Officials Were Nonexempt Employees Entitled to Overtime**

PNGI Charles Town Gaming, LLC, operates thoroughbred horse racing and video slot machines. Racing Officials employed by PNGI perform various roles during a typical racing day. The Fourth Circuit Court of Appeals has ruled that these Racing Officials are not FLSA-exempt administrative employees and are therefore entitled to overtime compensation under the Fair Labor Standards Act (FLSA) [*Desmond v. PNGI Charles Town Gaming, LLC*, No. 08-1216, 2009 U.S. App. LEXIS 9113 (4th CA, 4-30-09)] – reversing an earlier U.S. District Court decision (see [PAYROLL CURRENTLY, Issue No. 6, Vol. 16](#)).

*Note:* The primary duty of an FLSA-exempt administrative employee must be the performance of office or nonmanual work directly related to the management or general business operations of the employer or the employer's customers (see *The Payroll Source*®, p. 2-9).

PNGI Racing Officials perform clerical tasks in the mornings and on non-race workdays, such as compiling race programs and completing race entries. During races,

they fulfill roles that require them to observe and examine the horses, the jockeys, the trainers or grooms, the relevant paperwork for the horses, and the order of finish for the race. They have no supervisory responsibility and do not develop, review, evaluate, or recommend Charles Town Gaming's business policies with regard to the horse races. While the Racing Officials perform duties important to the operation of the racing business, their positions are unrelated to management or the general business functions of the company.

Instead, a Racing Official's work consists of tasks similar to those performed on a manufacturing production line or selling a product in a retail or service establishment. Charles Town Gaming "produces" live horse races, and the position of Racing Official consists of the day-to-day carrying out of its affairs to the public.

The lower court erroneously concluded that the Racing Officials' duties were related to the general business operations of Charles Town Gaming because they were

indispensable to the operation of a race track in accordance with state law. The Fourth Circuit explained that an FLSA exemption depends on the type of work performed, not whether a particular position is required by business practice or applicable law. “State or local law may also require a

construction company to post a flagman around a highway work site in order to coordinate traffic, but no colorable argument can be made that the flagman’s work is directly related to the construction company’s general business operations.” ■

## Company Ordered to Pay \$85,000 for Canceling Health Insurance After Employee Took FMLA Leave

When Kathleen Ryl-Kuchar became pregnant with triplets in 2003, she was compensated as a full-time employee working a regular 40-hour workweek by Care Centers, Inc. When Ryl-Kuchar began working from home in May 2003 because of the pregnancy, she worked less than 35 hours per week. Ryl-Kuchar’s certification form for leave under the Family and Medical Leave Act (FMLA) indicated that she was incapacitated “from May 11th until two months post-delivery” but did not specify when her leave would begin. After giving birth, Ryl-Kuchar stopped working in August and left the company on October 1.

In November 2003, Care Centers cancelled Ryl-Kuchar’s health insurance retroactive to June 15, 2003, without notifying her. The cancellation left Ryl-Kuchar with unpaid medical bills from her pregnancy after June 15, and she sued for interference with her rights under the FMLA. A jury awarded Ryl-Kuchar \$31,621.08 as compensation for her unpaid medical bills. The court awarded her an additional \$11,105.59 in prejudgment interest plus \$42,726.67 in liquidated damages [*Ryl-Kuchar v. Care Centers, Inc.*, 564 F. Supp.2d 817 (ND Ill., 6-16-08)].

### Interference with FMLA rights

**The decision to terminate insurance.** The decision to cancel Ryl-Kuchar’s insurance was made by CCS Employee Benefits VEBA, Inc., which administered the company’s health program. The cancellation process began when the VEBA trustee audited Ryl-Kuchar’s timesheets. The trustee concluded that Ryl-Kuchar had ceased to be a full-time employee in June 2003, and therefore became ineligible for health insurance at that time. However, Care Centers did not independently audit Ryl-Kuchar’s timesheets to verify her eligibility for health insurance, so the court said it was reasonable to conclude that by terminating Ryl-Kuchar’s health insurance the company adopted VEBA’s decision as its own.

**The period of FMLA leave.** The jury concluded that Ryl-Kuchar’s FMLA leave began on July 28 and continued until her resignation on October 1. The company was on notice that Ryl-Kuchar was on FMLA leave because the VEBA trustee saw a picture of the triplets and suspected that Ryl-Kuchar was on leave to care for her newborn children – an event entitling an employee to FMLA protection.

While she was on FMLA leave, Ryl-Kuchar had accrued health insurance through July 27 and was eligible for

continuation coverage after that date. Although she worked less than 35 hours per week from June 15 through July 27, the company never notified her of a status change, and her paystubs continued to reflect that she was a full-time employee and show deductions from her pay for health insurance. The company never formally changed Ryl-Kuchar’s status from full-time to part-time. The retroactive cancellation of Ryl-Kuchar’s health insurance leave as of June 15 was therefore unlawful interference with her FMLA rights.

**The amount of damages.** The court rejected Care Centers’ argument that Ryl-Kuchar’s damages should be limited to the amount she would have had to pay in insurance premiums if she had elected COBRA continuation coverage. The company did not notify Ryl-Kuchar when it retroactively cancelled her health insurance. A COBRA termination notice was sent out, but the delivery address had a typographical error and Ryl-Kuchar did not receive it. As far as Ryl-Kuchar knew, she still had health insurance coverage because her paystubs showed insurance premium deductions and she never received any notice otherwise.

### Interest

An employer that violates the FMLA is required to pay interest “calculated at the prevailing rate” on the amount of lost wages or employment benefits suffered by an employee as a result of the violation (29 USC §2617(a)(1)(A)(ii)). Here, the court said Ryl-Kuchar’s computation of interest – using daily prime rates and compounding the amounts monthly – was reasonable. And because Ryl-Kuchar’s insurance losses dated from June 15, 2003, it was appropriate to calculate the interest owed beginning on that date.

### Liquidated damages

The court awarded liquidated damages equal to the damage suffered by Ryl-Kuchar (i.e., the jury award plus interest) because Care Centers did not act in good faith and did not have reasonable grounds to believe that its conduct did not violate the FLMA. The company did not act in good faith because it cancelled Ryl-Kuchar’s health insurance retroactively and did not contact her directly about the cancellation. “A reasonable employer attempting to determine whether termination of an employee’s group health insurance would violate the FMLA would have contacted the employee before canceling the employee’s insurance.” ■

## Employer Did Not Have Reasonable Cause for Not Paying Employment Taxes Timely

St. Paul Cathedral School, a private school in Yakima, Washington, was not entitled to abatement of penalties imposed by the IRS for failure to timely file, pay, and deposit employment taxes, because it did not have “reasonable

cause” for its action, a U.S. District Court has ruled [*St. Paul Cathedral School v. U.S.*, No. 2:07-cv-03021, 2008 U.S. Dist. LEXIS 98526 (ED Wash., 12-5-08)].

During the tax periods in issue, the school employed

Sandra Page, a bookkeeper who was responsible for various financial duties that included paying employment taxes and filing tax returns. Page was supervised by the school principal and the parish pastor. After Page was hired, the school was notified that there was a criminal case pending against her, but the school did not act because it believed the charges were unwarranted. The school was not aware that Page had a criminal past that included convictions for theft and forgery. Page failed to pay employment taxes and file tax returns and stole \$240,000 from the school.

☞ **WHAT THE LAW SAYS** – Under IRC §6651(a)(1) (file), IRC §6651(a)(2) (pay), and IRC §6656(a) (deposit), additions to tax may be excused if the failure to perform the required action was the result of “reasonable cause” and not willful neglect. To demonstrate reasonable cause, a taxpayer must show that it exercised “ordinary business care and prudence” but (1) was nonetheless unable to file the return (or pay or deposit the taxes) within the prescribed time or (2) would have suffered an “undue hardship.”

#### Analysis

The court concluded that, given the budgetary challenges faced by the school, it had exercised ordinary business care by delegating to Page the sole authority for withholding, reporting, and remitting employment taxes. However, while that decision may have been reasonable as a corporate

matter, “it does not resolve the matter as to [the school’s] tax duties.”

**Inability to file, pay, or deposit.** The school argued that because of limited funds and consolidation of duties in one individual, Page should be considered equivalent to a Chief Financial Officer (CFO) with the capacity to disable a corporation. The court disagreed and said that the school was not disabled from complying with its tax obligations. Although Page might have had more authority than a typical bookkeeper, she was not the equivalent of a CFO. She did not participate in financial planning or policy development and had no role in setting tuition rates. The court also noted that the illness of the school principal did not prevent her from performing the essential functions of her job, including overseeing Page.

**Undue hardship.** There was no undue hardship in this case. The school was in financial trouble and losing money, but it did not attempt to justify its nonpayment by arguing that it paid other creditors ahead of the IRS, and in fact made no conscious decision to do so. Those in charge of the employee responsible for fulfilling the school’s employment tax obligations were simply unaware that taxes were due and were not being paid. Moreover, the school actually had ample funds available to pay the taxes in issue. ■

## Finance Employee Was FLSA-Exempt Executive

An employee described as a “jack of all trades” who performed duties involving preparing paperwork and data entry for construction loans, accounts payable, and payroll was not entitled to overtime wages under the Fair Labor Standards Act (FLSA) because she was an exempt executive employee, a U.S. District Court in New Mexico has ruled [*Slusser v. Vantage Builders, Inc.*, 576 F. Supp.2d 1207 (D N.M., 2-6-08)].

Diane Slusser sued Vantage Builders, Inc. (VBI) for unpaid overtime, saying that despite titles she held, such as “Operations Manager” and “Assistant Comptroller,” her duties were primarily clerical in nature.

☞ **WHAT THE LAW SAYS** – The FLSA executive exemption applies to an employee: (1) who is paid a salary of at least \$455 per week, not including board, lodging, or other facilities; (2) whose primary duty is management of the enterprise in which the employee is employed or of a customarily recognized department or subdivision of the enterprise; (3) who customarily and regularly directs the work of two or more other employees; and (4) who has the authority to hire or fire other employees or whose recommendations as to the hiring, firing, advancement, promotion, or other change of employment status of other employees are given particular weight (see *The Payroll Source*®, p. 2-12). The salary requirement was not in dispute here.

#### Primary duty of management

An employee’s primary duty is usually what the employee does that is of principal value to the employer, not the collateral tasks performed by the employee, even if those tasks take up more than half the employee’s time (29 C.F.R. §541.700(a)). Here, the court cited the following evidence in support of its conclusion that Slusser’s primary duty was management:

**Relative importance of managerial duties.** Although

Slusser spent a lot of time on data entry and preparing paperwork, this was clearly less important to VBI than her managerial responsibilities. She assigned work to the employees she supervised, directed their work, answered employee questions (a form of employee training), and was responsible for the day-to-day operations of the payroll department. She was in charge of the accounts payable department and was responsible for developing an operations plan for the department. It did not matter that Slusser herself was subject to supervision.

**Amount of time spent performing exempt work.** Slusser performed nonexempt work on her own against VBI’s wishes. She had been instructed by her supervisor to “stop being a doer” and delegate her clerical work to the people she supervised.

**Relative compensation.** Slusser’s duties were primarily managerial. She was the second highest paid office employee at VBI and one of the few employees to earn a bonus. The people she supervised earned about half as much as she did.

#### Directing the work of two or more employees

Slusser customarily and regularly directed the work at two or more full-time employees. She also directed the work of temporary employees. Although Slusser spent most of her time doing the same work as the employees she supervised, she remained responsible for performing her managerial duties. The fact that Slusser’s supervisor sometimes contradicted Slusser’s instructions did not negate her supervisory responsibilities.

#### Authority to hire and fire employees

VBI gave particular weight to Slusser’s recommendations for hiring, firing, promoting, and demoting the employees she supervised. Slusser and her supervisor were in charge of hiring accounts payable clerks, and she was involved in hiring payroll clerks. She evaluated the employees working under her and had fired employees. ■



## STATE AND LOCAL NEWS

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### Arkansas

**UI taxable wage base will increase; alternative base period for claims adopted.** Beginning 1-1-10, the unemployment insurance (UI) taxable wage base will increase to \$12,000 from \$10,000 (this updates *The Payroll Source*®, p. 7-23). The state has also adopted an alternative base period for UI claims filed on or after 7-1-09 to receive federal stimulus funds [S.B. 429, L. 2009].

### Kansas

**Minimum wage and tip credit will increase.** Effective 1-1-10, the state minimum wage will increase to \$7.25 an hour from \$2.65 an hour (this updates *The Payroll Source*®, p. 2-68). Also effective 1-1-10, the minimum cash wage that a tipped employee must receive will be \$2.13 an hour. Currently, the tip credit is 40% of the state minimum wage (\$1.06 an hour). Thus, effective 1-1-10, the tip credit will increase to \$5.12 an hour (\$7.25 - \$2.13) from \$1.06 an hour (this updates *The Payroll Source*®, p. 2-69) [S.B. 160, L. 2009].

### Utah

**Defined contribution plan market to be established.** Recent legislation will establish a defined contribution plan (DCP) market available on an Internet portal. It will offer a range of health benefit plan choices to an employer's eligible employees. By 1-1-10, the DCP market must be available to small employers (not more than 50 employees), and it must be available to large employers beginning 1-1-12. An employer that elects to establish a DCP must establish a mechanism for participating employees to use pre-tax dollars to purchase a health benefit plan from the DCP market via the Internet portal. This may include a health reimbursement arrangement, an IRC §125 cafeteria plan, or another similar plan. Employers will be allowed to determine employee eligibility, enrollment, and participation in the plan, as well as the amount of the employer contribution. Employees will be enrolled in the default health benefit plan selected by the employer unless they notify the employer otherwise [H.B. 188, L. 2009].

### Virginia

**New online filing and payment service launched.** The Department of Taxation (DOT) has launched a free Web Upload Service for filing withholding (and sales tax) returns and paying taxes. Payroll service providers can use the service to file returns and make payments for multiple clients in a single file. Small business owners can use the service to submit a single return prepared on a program such as Excel. Visit [www.tax.virginia.gov/site.cfm?alias=webuploadinformation](http://www.tax.virginia.gov/site.cfm?alias=webuploadinformation) for more details and to register [DOT, News Release, 5-6-09].

### Wisconsin

**Forms W-2: electronic filing threshold reduced.** Effective 1-1-10, employers that are required to file 50 or more (currently 250 or more) Forms W-2 must file them electronically with the Department of Revenue (this updates *The Payroll Source*®, p. 8-116). Magnetic media is not accepted [A.B. 75, L. 2009].

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