

Social Security
Administration

Internal
Revenue Service

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Fall 2006

A Newsletter
for Employers

Editor's note: No one wants a disaster to happen, but almost as bad as a disaster is not being prepared for one. The events of 9/11 and the rash of hurricanes and other natural disasters over the last several years make disaster preparation and planning imperative.

Disaster in the Workplace: Proactive Steps for the Payroll Department

With the news in recent years of fires, floods, hurricanes, earthquakes, and terrorism, businesses must be prepared with ways to continue to serve their customers, pay employees, and withhold and deposit taxes. The following tips from the American Payroll Association may prove invaluable to you.

Every company should develop a Business Continuity Plan that includes:

1. Interim office space: A search should be conducted to locate interim office space (e.g., hotel meeting rooms, company warehouses) in case your facility is rendered uninhabitable. Agreements for more than one suitable space may be desirable for even greater protection. Some organizations have developed their own office space for such emergencies.

2. Office equipment rental: If your offices are damaged, or if you can continue in your location but your payroll

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IRS Offers Tips on How to Correct Reporting of Misclassified Employees

The number of natural disasters that have hit the United States in the last several years has caused many businesses to hire additional workers to help them meet increased demand for their goods or services. These businesses must classify their workers properly to make sure everyone can meet their tax obligations.

Most employers make every effort to meet their employment tax obligations. They take the care to review all factors affecting their relationship with their workers and classify their workers as employees or independent contractors accordingly. Occasionally, an employer does make an error and classifies an employee as an independent contractor and has to correct that mistake.

When an employer does incorrectly classify an employee as an independent contractor, the employer is still responsible for paying the employee's federal

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Form 940 Will Be Much Improved for Tax Year 2006

Payroll professionals and business owners filing Form 940 *Annual Federal Unemployment (FUTA) Tax Return*, for 2006 (due by 1/31/2007) will notice a big difference in the form and instructions. The IRS has completely redesigned Form 940 to be more user-friendly, reducing the burden for more than one million filers.

Many individuals and organizations have asked the IRS to change Form 940. Taxpayers often struggle to determine which lines to complete and which to skip. In addition, they find it difficult to make computations and to fill in explanations of exempt payments.

In May 2004, a team led by the IRS Office of Taxpayer Burden Reduction (TBR) began the process of redesigning Form 940. IRS employment tax experts worked with representatives from other federal and state agencies, gathering input from internal and

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income tax withholding and the employee's share of Federal Insurance Contributions Act (FICA)/Railroad Retirement Tax Act (RRTA), even if it was not withheld from the employee's wages. The employer still must pay the employer's share of matching FICA/RRTA and Federal Unemployment Tax (FUTA). Penalties and interest may also apply.

All these payments can add up for the employer, but the good news is that the Internal Revenue Service does provide some relief for employers who have made a classification error. Internal Revenue Code Section (IRC §) 3509 provides an opportunity to correct the tax treatment of misclassified employees. IRC § 3509 provides reduced rates for the employee's share of FICA taxes and for the federal income tax that should have been withheld. Employers are still responsible for the full amount of their share of FICA taxes. IRC § 3509 does not provide a reduced FUTA rate.

If the employer does not qualify for the reduced rates under IRC § 3509, the employer may still be relieved from paying the federal income tax that should have been withheld from the employee. They need to provide evidence that the employee reported the income on their federal income tax return and paid the federal income tax due. The employer who requests this relief must have the employee sign a Form 4669 (*Employee Wage Statement*) stating that the income was reported and the taxes attributable to the income have been paid.

The employer must complete and sign Form 4670, *Request of Relief from Payment of*

Income Tax Withholding and submit this form along with any properly executed Form(s) 4669 to request for relief from payment of this tax liability. This does not relieve employers of any penalties or additions to tax for failure to withhold the tax.

However, an employer will not owe employment taxes for misclassified workers, if they meet all three requirements described in § 530 of the Revenue Act of 1978, Publication 1976, (<http://www.irs.gov/pub/irs-pub/1976.pdf>) *Independent Contractor or Employee? Section 530 Employment Tax Relief Requirements:*

1. The employer must have had a reasonable basis for not treating the workers as employees.
2. The employer (and any predecessor business) must have treated the workers and any similar workers as independent contractors for all applicable periods beginning after December 31, 1977.
3. The employer must have filed Form 1099 MISC (Miscellaneous Income), for each worker, if such form was required.


If the employer meets the Section 530 requirements, the section provides businesses with relief from federal employment tax. It terminates the business's, not the worker's, employment tax liability (attributable to such workers) under Internal Revenue Code (IRC) Subtitle C (Federal Insurance Contributions Act (FICA)/Railroad Retirement Tax Act taxes, federal income tax withholding, and Federal Unemployment Tax Act (FUTA) taxes, and any interest or penalties attributable to the

liability for employment taxes (Rev. Proc. 85-18, 1985-1 C.B. 518).

However, the Section 530 relief provision does not apply in the case of a worker who, pursuant to an arrangement between the business and a client, provides technical services for that client as an engineer, designer, drafter, computer programmer, systems analyst or other similarly skilled worker engaged in a similar line of work. (Section 1706 of the Tax Reform Act of 1986)

For additional information on the worker classification issue:

- IRS Headliner 152, (<http://www.irs.gov/businesses/small/article/0,,id=155756,00.html>), *IRS Offers Tips on How to Correct Misclassification of Employees*
- Publication 15-A, (http://www.irs.gov/pub/irs-pub/p15A_05.pdf) *Employer's Supplemental Tax Guide*
- Publication 1779, (<http://www.irs.gov/pub/irs-pub/1799.pdf>) *Independent Contractor or Employee?* brochure.

Caution: Employee misclassification can affect retirement plan coverage, vesting, and funding. Relief may also be available for retirement plans. Information about the IRS correction programs that enable sponsors of retirement plans to preserve the tax benefits of their plans is available on the Employee Plans Compliance Resolution System (EPCRS) pages of IRS.gov (<http://www.irs.gov/retirement/article/0,,id=96907,00.html>). 

IRS Web Site an Invaluable Resource When Disaster Strikes

The IRS' objective is to provide resources and assistance to members of the payroll and practitioner community, individuals and businesses who have been impacted by one of these events or who might be. The IRS Web site (<http://www.irs.gov>) provides numerous links to this information. Although there is an emphasis on recent, hurricane-related events, information on the IRS Web site is pertinent in other disaster scenarios.

■ Help for Hurricane Victims:

Information on Tax Relief, Charitable Issues

<http://www.irs.gov/newsroom/article/0,,id=147085,00.html>

■ Disaster Relief Resource Center for Tax Professionals

<http://www.irs.gov/taxpros/article/0,,id=150578,00.html>

■ Tax Relief in Disaster Situations

<http://www.irs.gov/newsroom/article/0,,id=108362,00.html>

■ Additional Guidance for Those Affected by Hurricanes

<http://www.irs.gov/businesses/small/article/0,,id=157669,00.html>

■ FAQs for Hurricane Victims


<http://www.irs.gov/businesses/small/article/0,,id=156144,00.html> 

external stakeholders to create a plain language form that is logical, easy to follow, and compatible with optical scanning.

The new Form 940 incorporates the advantages of Form 940-EZ (discontinued for tax year 2006) into a simplified form for all filers. Highlights include:

- A logical sequence from the taxpayer's point of view;
- Eight separate parts with visual cues, breaking up the task into smaller steps;
- A new Schedule A for multi-state employers or credit reduction situations;
- Check boxes instead of "A, B, C" questions; and
- No more need for hand-written explanations of exempt payments.

Advance "vision drafts" of Form 940 and Form 940 Schedule A can be viewed on the "Vision Draft Forms" page of IRS.gov at <http://www.irs.gov/businesses/small/article/0,,id=146224,00.html>. Please note that these versions are subject to further revision and should not be used for filing.

The IRS is committed to reducing unnecessary taxpayer burden and welcomes input from tax and payroll professionals, business owners and the general public on opportunities to make it easier to comply with the tax laws. More information, including a link to Form 13285A, *Reducing Tax Burden on America's Taxpayers*, can be found on the TBR page of IRS.gov, <http://www.irs.gov/businesses/small/content/0,,id=146284,00.html>. 

Disaster in the Workplace: Proactive Steps for Payroll continued from page 1

department's equipment is rendered unusable, you will need temporary office equipment (e.g., computers, fax machines, phone lines). Make advance arrangements for rental, delivery and installation in case of emergency.

3. Temporary housing for employees: Having employees who can be at an interim office while the employer is recovering from a disaster is very important, so temporary living space must be arranged for them in advance. Even if your offices are relatively unharmed, your employees' homes may be uninhabitable, and you may want to provide housing to key employees so they can continue to work for you. Alternate transportation may also be planned in advance to get employees to and from the temporary housing and interim office.


4. Off-site backup files: A new location and ready employees won't serve you well unless you have an up-to-date copy of all payroll balances and employee files and backup copies of all necessary software. Besides the possibility of a disaster, frequently backing up your data is essential preparation for any system failure.

5. Paycards: Depending on the type and severity of the disaster, you may be able to print paychecks but not be able to distribute them to employees in certain geographic areas. Or, if you can print and distribute paychecks, your employees may have nowhere to cash them. You may want to make prior arrangements with banks to pay wages via paycards and have supplies of paycards available at your outlying locations, ready to have net pay amounts associated with them.

6. Employee safety: The safety, well-being, and whereabouts of employees should be the first things determined immediately after a disaster strikes and should always be kept in mind. All managers should have a list of their employees' home and emergency-contact phone numbers, as well as general emergency numbers, available at all times.

7. Communication: Make sure the Business Continuity Plan is documented and provided to all employees so everyone is thinking along the same lines should disaster strike. Indecision can cost employees their lives and employers their business. The plan should be periodically updated and reviewed: for example, have there been changes in personnel, phone numbers, software, or equipment?

8. Information from government agencies: In times of disaster, federal and state government agencies have been very responsive and flexible with adversely affected employers. For example, IRS has often granted immediate extensions of deposit and filing due dates and has posted the details at <http://www.irs.gov>. (See related article on page 2, "IRS Web Site an Invaluable Resource When Disaster Strikes.")

*APA's partnership with the IRS and SSA allows it to prepare its publications and classes, such as *Preparing for Year-End and 2007*, with the most accurate and up-to-date information to educate employers. Further information about disaster recovery, paycards, payroll education, and much more can be found at APA's Web site, <http://www.americanpayroll.org>.* 

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CHANGE OF ADDRESS? OUT OF BUSINESS?

Notify the IRS. Submit Change of Address Form 8822 available at <http://publish.no.irs.gov/FORMS/PUBLIC/PDF/12081L05.PDF> to the IRS center to which you sent your business returns. Please include your Employer Identification Number (EIN).

Cincinnati IRS Center
Cincinnati, OH 45999

Ogden IRS Center
MS:6273
Ogden, UT 84207
Attn: BMF Entity Control Unit

Outside US:
Philadelphia IRS Center
Philadelphia, PA 19255

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IRS and SSA "Help" Telephone Numbers and Web Addresses Now on IRS.gov

IRS and SSA "Help" telephone numbers and Web addresses are now posted on IRS.gov at <http://www.irs.gov/businesses/small/article/0,,id=109886,00.html>.

Top Reasons for Not Using FTD Coupons



1. Coupons Can Be Lost.

It happens. You receive your Federal Tax Deposit (FTD) coupon booklet and it gets misplaced just as it's time to make a payment. Suddenly you have no alternative for making a timely payment to avoid late penalties.

If you were enrolled in the Electronic Federal Tax Payment System (EFTPS), you could make your payment by phone or Internet and avoid the penalty.

2. It Takes Extra Time to Make a Payment With a Coupon.

To make a payment by FTD coupon, you have to complete the form, write a check, get it signed (if you're not the signer) and then take it to the bank. That takes a lot of time on a busy day.

If you were enrolled in EFTPS, you could make a phone call or log on to <http://www.eftps.gov> to make your payment in a matter of minutes. You could even schedule your payment in advance so it's made on the date you indicate. (Payments must be made at least one calendar day in advance of due date prior to 8:00 p.m. ET.)

3. You Don't Have a Convenient Record of All Your Payments.

When it comes time to filing your tax returns, you need to look through the check register or locate any copies you made of your coupons and checks to determine what you paid when. This can be a time consuming task.

With EFTPS, you have 16 months of your payment history immediately available to you on-line so you can easily calculate all your payments. You can even download or print out your payment history.

4. You're Never Quite Sure When Your Payment Gets to IRS.

Even though you take your payment to the bank, sometimes glitches happen and you're not quite sure when IRS received your payment and if it was on time.

EFTPS gives you an immediate confirmation that your payment was received. You get an acknowledgement number for every transaction and that number can be used in referencing payments with the IRS.

5. Paying By Coupon and Check Could Be Costly.

It takes staff time out of the office to take a payment to the bank. That costs you money. If you use a courier to deliver your payments to the bank, that costs, too. And if your payment is somehow late or lost, that can be very costly.

EFTPS is free. There are no costs from the government for using EFTPS. All you need is a phone, or a computer with a secure Internet browser.

6. You Don't Know if Your Payroll Provider Made Your Payments.


If you turn over your FTD coupon booklet to your payroll provider, you don't know exactly when those payments are being made. And if you change providers, you may not have coupons when you need them.

If you ask your payroll provider to use EFTPS for your payments, then you could enroll in EFTPS as a business and you would have complete access to your payment history online. You would be able to see when your payments are being made. Many payroll providers using EFTPS encourage their clients to do just that—so clients have peace of mind knowing their payments are being made in a timely manner. In addition, if you change providers, you can always make your own payments by phone or online until you find a new payroll company and you can pay all your other federal taxes using EFTPS.

7. Your Payroll Provider Needs to Make Your Payments But You Have the Coupon Booklet.

Many times clients forget to send the booklet to their provider or the client needs to retain it to make other form type tax payments. When it is time to make the payment, the party without the FTD Coupon Book has to call or visit IRS to get additional coupons. This adds additional time to the payment process and could cause a penalty to be incurred.

If you and your payroll company were both using EFTPS to make payments you wouldn't have to worry about who has the coupons.

There are many reasons to use EFTPS, these are just a few. Consider enrolling in EFTPS to make it easier to pay federal taxes. You can enroll online at <http://www.eftps.gov>, or call EFTPS Customer Service at 800-555-4477 for an enrollment form. 

What to Do If You Receive a National Medical Support Notice

If one of your employees has child support obligations, a state child support enforcement agency (CSEA) may send you a National Medical Support Notice (NMSN). The NMSN is a standardized form that advises you when your employee has been ordered to provide health insurance coverage for his or her child through your company's health care plan.

The NMSN is a federal form that all state child support enforcement agencies must use. Once an order to provide medical coverage has been established and health care coverage is available through the employer, the Plan Administrator must enroll the child.

Some of the form's advantages are:

1. It simplifies the work of employers and plan administrators by providing uniform documents requesting health care coverage;
2. It constitutes a Qualified Medical Child Support Order and meets the requirements of the Employee Retirement Income Security Act (ERISA) (sections 609(a)(3) and (4));
3. It satisfies state law provisions for withholding employee contributions for health care coverage, and provides the priority of withholding between child support and medical support where available funds are insufficient to cover both; and
4. The form states the duration of the obligation and the name and address of a contact at the child support enforcement agency.

The NMSN is actually four documents and instructions:

- Part A, "Notice to Withhold For Health Care Coverage"
- Employer Response
- Part B, "Medical Support Notice to Plan Administrator"
- Plan Administrator's Response

The form is divided into parts for the employer and for the plan administrator. As the employer, the first part, "Part A—Notice To Withhold For Health Care Coverage," is important as it gives you the identifying information for the case. If you provide health insurance coverage to your employees and there is no delay of coverage due to a waiting period, you do not need to complete any part of the form. Simply send "Part B—Medical Support Notice to the Plan Administrator" to your plan administrator.

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TEST YOUR KNOWLEDGE

Changes in Business Structure

Situation: Allen was the owner of a sole proprietorship doing business as Juniper Customizers ("Juniper"). Started as a one-person specialty metal fabricator, several employees had been hired to work at Juniper over recent years. With this continuing expansion, Allen had been reviewing plans to take in another owner and incorporate the business as Juniper Customizers, Inc. ("JCI").

Allen was aware that he had two related tax roles: (1) self-employed sole proprietor; and (2) employer. In his self-employed status, Allen reported the business operations on his individual tax return by attaching the applicable schedules (the self-employment tax and any resulting income tax on the business profit were remitted as quarterly estimated tax payments).

In his dual status of employer, Allen had obtained an employer identification number ("EIN") and withheld social security, Medicare, and federal income taxes from the employees' wages. Federal unemployment tax was also computed on the wage amounts and Allen (as the employer) matched the withheld social security and Medicare taxes.

Allen worked closely with a tax practitioner to stay current in the various withholding, depositing, and filing requirements for an employer and now wanted to understand the employment tax impact of forming JCI.

Question: What issues might be included in discussions with Allen's business advisor?

Answer: Changing a business structure involves the consideration of a range of factors including economic, legal, and tax. An appreciation of the employment tax aspects could help maintain compliance with filing and payment obligations.

If the business is incorporated, employees of the Juniper sole proprietorship will generally become employees of JCI. Additionally, as discussed in section one of Publication 15-A, *Employer's Supplemental Tax Guide* (<http://www.irs.gov/pub/irs-pdf/p15a.pdf>), corporate officers who work in the business (such as Allen, who plans to work as president of JCI) will generally be employees of the corporation. An officer who performs no services or only minor services, however, and neither receives nor is entitled to receive any pay, is not considered an employee.

JCI may be considered a "successor" employer since it will receive all or most of the property used in the trade or business of the "predecessor" Juniper sole proprietorship and will also be employing the same workers. Under these provisions, when JCI figures the annual wage base limit for social security, it may be able to count the wages of the "acquired" Juniper employees paid in the same calendar year before the transfer of property. Similar rules apply in computing the federal unemployment tax.

See further information on the successor employer rules in sections 9 and 14 of Publication 15, (Circular E), *Employer's Tax Guide* (<http://www.irs.gov/pub/irs-pdf/p15.pdf>). The items discussed include an additional schedule that may need to be filed with the IRS when there is an employer change and a revenue procedure applicable to several employer change situations.

Other Rules. As a new entity, JCI will generally need an EIN separate from the one used by the Juniper sole proprietorship owned and operated by the individual Allen. The chart (Do I Need an EIN?) on page 2 of Form SS-4, *Application for Employer Identification Number*, (<http://www.irs.gov/pub/irs-pdf/fss4.pdf>) provides a listing of general and special EIN situations for business structure changes and other events (such as when a new EIN would not be needed for certain entity classification changes by a limited liability company). The instructions (<http://www.irs.gov/pub/irs-pdf/iss4.pdf>) also provide a variety of ways to obtain an EIN (including applying online).

Resources for Additional Information:

Publication 542, *Corporations*
<http://www.irs.gov/pub/irs-pdf/p542.pdf>

Publication 583, *Starting a Business and Keeping Records*
<http://www.irs.gov/pub/irs-pdf/p583.pdf>

Businesses with Employees—Paying Yourself
<http://www.irs.gov/businesses/small/article/0,,id=101038,00.html> 

Medical Support Notice

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Here is a short summary of the steps that must be taken upon receipt of the NMSN. More detailed instructions are available at the Office of Child Support Enforcement Web site (http://www.acf.hhs.gov/programs/cse/newhire/employer/private/medical_support.htm)

Step 1: Determine whether any of the four categories on the Employer Response apply to you or this employee. If any apply, complete the Employer Response form and return it to the Issuing Agency within 20 business days.

Step 2: If none of the four categories on the Employer Response apply, forward Part B to your plan administrator.

Step 3: The plan administrator will notify you when enrollment has been completed. You must then notify your payroll department to make the appropriate deductions for the employee contribution required under the health plan.

Step 4: If, in fact, you determine that the amount of support, coupled with the deduction for health care premiums, exceeds the maximum deduction allowable, you must look to state law in the state where the employee is employed to determine the priority for payment. If the state priority for withholding precludes the payment of the premium, complete the Employer Response and return it to the Issuing Agency.

Step 5: If enrollment cannot be completed until after a waiting period or other contingency, you must notify the plan administrator when the employee is eligible for enrollment. You should also notify the issuing agency of the timeframe for enrollment.

The Federal Office of Child Support Enforcement greatly appreciates your role in supporting the health and well-being of America's children. 

Social Security Announcements

Verify Social Security Numbers Online

The Social Security Number Verification Service (SSNVS) allows you to match the name and Social Security number of employees you hire with Social Security's records. Go to <http://www.socialsecurity.gov/bso/bsowelcome.htm> to use SSNVS.

You have two options for using SSNVS:

1. You can directly key up to 10 names/Social Security numbers at a time onto Social Security's website with immediate results, or
2. You can upload a file with up to 250,000 Names/Social Security numbers with next business day results.

It is important to remember that SSNVS cannot be used to prescreen employees before they are hired.

For more information go to <http://www.socialsecurity.gov/employer/ssnv.htm>.

Create an SSNVS File Using Spreadsheet Software Program

You can verify up to 250,000 names/Social Security numbers using a spreadsheet software program to create an SSNVS file, as long as you put it in the correct format. Social Security will not be able to process a file that is not in the correct format.

If you are using Excel, to ensure that your electronic file submission is processed successfully, the file must not be in the ".xls format."

To create the file you will need one column that is at least 130 characters long. This column will hold all data for each record. The specifications for the record layout can be found at http://www.ssa.gov/employer/ssnvs_handbk.htm. To get to the specifications quickly, select "Submission File Format" in the right hand column.

To save an Excel file for processing:

1. Select *Save As* on the File Menu;
2. In the *Save As* dialog box, select the drop down box *Save As type*;
3. Select *Formatted Text* (space delimited) (*.prn); and
4. Type the filename and click *Save*.

Once you have saved your file, check your file against the Submission File Format to ensure the record length is 130 characters and all fields are properly placed in their respective position. The Multiple Request Indicator field in positions 128-130 must be populated with "000" and may not be left blank.

Social Security Eliminates Diskettes and Tapes for W-2 Reporting

Social Security has eliminated magnetic tapes, cartridges and diskettes as acceptable media for submitting W-2 reports to SSA. Beginning with Tax Year 2006 (W-2s due to SSA in calendar year 2007), wage reports containing 250 or more Forms W-2's must be filed electronically via Social Security's Business Services Online (BSO). BSO is a suite of Internet services for companies conducting business with Social Security. It is wise to get ready for the 2007 filing season. Visit <http://www.socialsecurity.gov/bso/bsowelcome.htm> today and register for a PIN and password.

Elimination of the Paper Version of the Magnetic Media Reporting and Electronic Filing (MMREF) Publication

Social Security will discontinue mailing the paper version of the Magnetic Media Reporting and Electronic Filing (MMREF) document after 2006. In July, Social Security mailed a compact disk containing the MMREF to all employers who file electronically or on magnetic media.

If employers prefer, the web version of the MMREF publication is also available. Just go to <http://www.ssa.gov/employer/pub.htm>. Software developers are encouraged to visit the Social Security website to download the newest version of the MMREF. You also can subscribe to *W-2 News*, Social Security's electronic newsletter for employers, and receive an email when the latest version of the MMREF is available on the web.

AccuWage and AccuW-2C Now Available

AccuWage and AccuW-2C software for 2006 are designed to test current and prior year wage reports prepared in the MMREF formats. The software allows you to check Forms W-2 (*Wage and Tax Statement*) and W-2c (*Wage and Tax Statement Correction*) reports for correctness before you send them to Social Security. It is also a valuable tool for software developers to use as part of their process to validate their wage reporting (W-2) software.

A free copy of AccuWage and AccuW-2C is now available and may be downloaded from <http://www.socialsecurity.gov/employer/accuwage>.