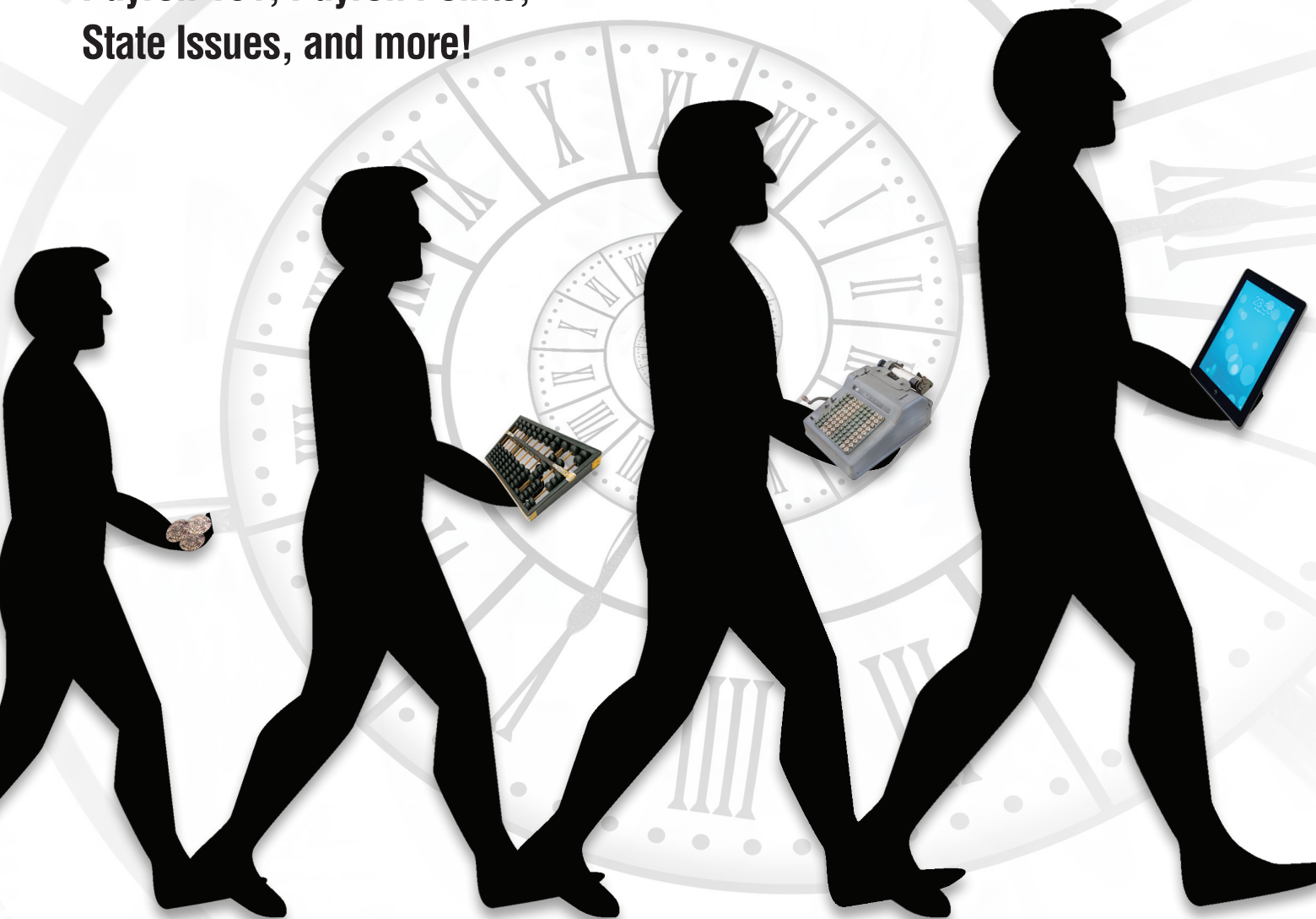


# PAYTECH

**INSIDE:**

**Payroll 101, Payroll Points,  
State Issues, and more!**

**Case Study Shows  
Value of Paycards**



**EVOLUTION OF PAYROLL**  
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P

ayroll is ever-changing, whether in technology or in compliance. To keep up with it all, thousands of payroll and accounts payable professionals just like you turn to the American Payroll Association for the constant support, education, and networking they need to stay on top of their careers.



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This 16-page special PAYTECH issue contains just a sampling of the articles, columns, and analysis for which APA is renowned.

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# PAYTECH

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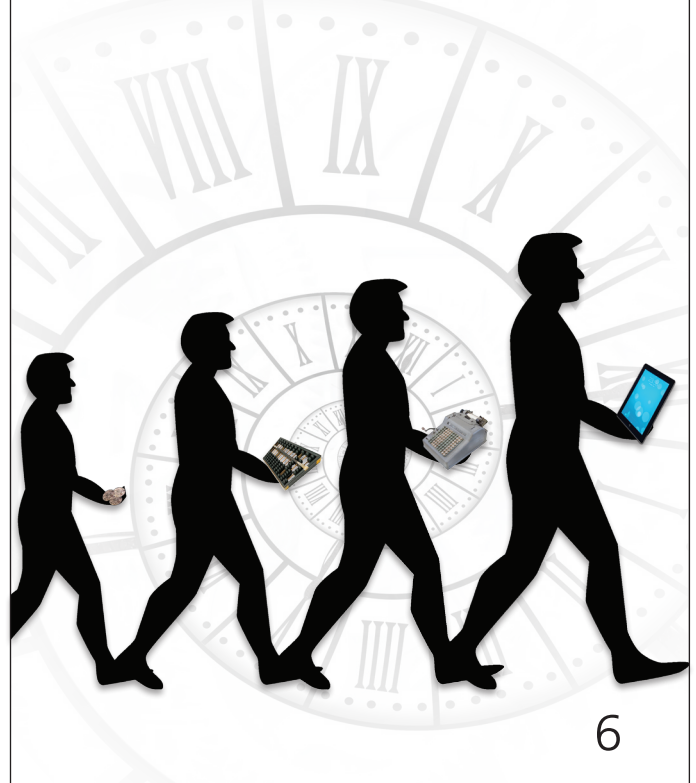
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This 16-page special edition of PAYTECH, APA’s exclusive monthly membership magazine, is just a sample of some of the articles that appear in a full-length edition. Each month you will receive at least 64 pages of payroll news and features as part of a complete lineup of APA membership benefits. Whether you need information about the latest trends in outsourcing, time and attendance technology, or legislative and regulatory issues, PAYTECH is your source.



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# Former Employee Can't Get Back FICA Taxes

BY CURTIS E. TATUM, ESQ.

The U.S. Court of Appeals for the Federal Circuit has affirmed that an airline pilot was not entitled to a refund of FICA taxes paid on deferred compensation—retirement benefits—he never received [*Balestra v. U.S.*, No. 2014–5127, 2015 U.S. App. LEXIS 17756 (Fed. Cir. CA, 10-13-15)].

Louis Balestra was a pilot for United Airlines from 1979 until his retirement on October 1, 2004—two years after United entered bankruptcy proceedings. As a result of these proceedings, which concluded in 2010, United's obligation to pay Balestra's nonqualified deferred compensation (NQDC) benefits was discharged, with the majority of the benefits never having been paid.

United withheld FICA tax based on a present value calculation of the NQDC benefits at the time of Balestra's retirement, so he paid \$4,199.22 of FICA tax—which reflects the 1.45% Medicare tax rate applied to the \$289,601.18 present value of the benefits. *Note:* Balestra did not pay social security tax on his NQDC benefits because his other compensation in that year exceeded the social security wage base.

After his retirement, Balestra actually received \$63,032.09 of NQDC benefits. He sued for a refund of \$3,285.26 of FICA (Medicare) tax on the unpaid balance.

**The special timing rule.** FICA taxes are generally imposed on wages in the year that they are actually or constructively paid by employers to employees (IRC §3101). The special timing rule is an exception to this general rule, as it permits NQDC benefits to be taxed before they are paid.

Under the special timing rule, the determination of FICA taxes (social security tax and Medicare tax) on employer contributions to an NQDC

plan does not depend on whether the plan is funded or unfunded. Employer contributions and earnings are subject to FICA taxes on the later of two dates—the date services are performed that form the basis for the contributions or when there is no substantial risk of forfeiture of the employee's interest in the funds (IRC §3121(v)(2)).

IRS regulations implementing the special timing rule (26 C.F.R. §31.3121(v)(2)-(1)) provide for the taxation of deferred compensation based on a present-value calculation that does not discount the promised benefits for the risk of employer default. The regulations do not explicitly allow refunds in the event of nonpayment due to plan failure, unlike in other circumstances.

## Balestra's Argument

Because United made the calculation after it had already entered bankruptcy proceedings, Balestra argued that the present value of the deferred compensation should have been based on a "fair market value" that took United's financial condition into consideration. He argued that the regulation was unreasonable as applied to employers in bankruptcy. He also argued that the regulatory definition of "present value" was arbitrary and capricious because it differed from the plain meaning of "present value" without a sufficient explanation.

## The Court's Decision

**Statute is silent.** The court said the statute itself did not address the question in this case—i.e., how employers must calculate the "amount deferred" under NQDC plans for FICA tax purposes, and specifically, whether the present value of the amount deferred can be determined without considering the employer's financial condition. However, the legislative history—namely, statements made on the floor of the U.S. Senate—gives no indication that Congress intended to calculate "present value" by considering



an employer's financial status. It merely suggests that Congress expected that "simple rules" for calculating present value would be established. The court said this legislative history supports the regulation—a relatively simple rule that Balestra simply dislikes.

### **Regulation is reasonable.**

Rejecting Balestra's position, the court pointed out that the IRS definition of present value allows for the consideration of some contingencies but not others. For example, it does not include the contingency that if the employer becomes bankrupt, an adjustment in the employee's tax will be made. The IRS was not obligated to include this contingency under the statute. The court concluded that the decision to define present value without regard to the financial condition of the employer was reasonable, and the regulation is therefore valid.

**Regulation is not arbitrary and capricious.** The court also rejected the argument that the regulation is arbitrary and capricious. The IRS wanted simple, workable, and flexible rules for valuing future benefits. It devised a regulation that satisfied these goals while aligning with the statute.

"It may seem unfair in a specific instance such as this," but an agency must be allowed "a reasonable degree of discretion" in balancing the desire for simplicity against the ideal of ultimate comprehensiveness. The court could not say that "this one example of consequent unfairness by the agency results in the invalidating of the rule-making." ■

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*Curtis E. Tatum, Esq., is Senior Manager of Payroll Information Resources for the APA.*

# A Paycard Case Study

We Make Paycards Easy



## Company profile for Pillar Hotels & Resorts

- Provides on-site management services for an expansive portfolio of well-respected brands recognized the world over.
- Manages 220 hotels
- Consists of nearly 23,900 rooms
- Operates in 37 states
- Represents 19 brands

“ We chose Global Cash Card over one of the mega-banks as a result of their technology and implementation team. We have over 6,000 employees spread over 37 states and we knew that Global would do a better job in implementing the paycard solution. We have not been disappointed. The implementation team was incredible and our rollout was more successful than I could imagine. Global Cash Card has saved us a significant amount of time and money both at the corporate and field locations. I would recommend the product to anyone.

David Altshuler,  
Chief Financial Officer  
Pillar Hotels & Resorts

## Situation

Pillar Hotels was looking to reduce the cost and complexities of their payroll processing, especially for their unbanked staff. The financial benefits of the Global Cash Card program, along with the dedication of the Field Support Team, convinced them that a paycard program was the key to achieving their fiscal and operational goals.

## Implementation

Pillar Hotels decided to launch the program with seven pilot locations in California and Minnesota. Global Cash Card's Field Support Team facilitated train-the-trainer webinars for the general managers, assistant general managers and human resources administrators at the pilot locations. As part of the introduction, paycheck stuffers were included in the employees' checks notifying them of the opportunity of the Global Cash Card paycard program. All employees who did not enroll in direct deposit were required to attend an informational meeting about Global Cash Card paycards. Global Cash Card's Field Support Team facilitated in-person employee meetings to train them on paycards and enroll new cardholders for the California locations. Similarly, they facilitated conference call employee trainings for Minnesota locations.

## Results

The initial pilot was considered a success by Pillar Hotels, and, after best practices were established, the program was rolled out to the rest of their locations. This roll out was conducted by Global Cash Card's Field Support Team via train-the-trainer webinars, 30 minute conference call trainings, and Q&A sessions for the employees enrolling in Global Cash Card. This training was in both English and Spanish. Prior to implementation, Pillar Hotels' percentage of electronic participation was in the low 40's. After two months of the Global Cash Card program, overall participation has soared to over 90%. Pillar Hotels are also using Global Cash Card to provide final pay for employees in states that require pay immediately upon termination.

## Summary

Much of the success of the paycard program is owed to the customized implementation program provided by Global Cash Card's Field Support Team which included paycheck stuffers, webinar training, conference call training, and customized materials, such as enrollment forms, training guides, and FAQ's. Going forward, Pillar Hotels has set a goal of reducing live checks to 10% or less by using Global Cash Card.

## Savings

Pillar Hotels projects that by the end of year they will achieve over \$50,000 in savings from both the cost of printing, as well as their FedEx charges. Additionally, employees of Pillar Hotels are saving money on expensive check cashing fees and overcoming the inconvenience of only having cash.

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# How TECHNOLOGY Is CHANGING PAYROLL

BY MICHAEL PAPPAS, CPP

**F**or those payroll professionals who began their payroll careers 10 years ago, the technological jump has been amazing. For those of us who began our careers 20 or more years ago, this jump has been nothing short of fantastic.

My first involvement in the world of payroll exposed me to what was then cutting-edge technology, a calculator with the ability to add subtract, multiply, and divide. It had adding machine tape as a backup in case of error. Laugh if you will, but five of us, plus the paymaster, processed a weekly payroll of more than 500 employees using only our calculators, pen and ink, payroll ledger sheets, and a roller-type device that contained the tax tables. So, for me, payroll technology has taken a quantum leap.

Let's take a quick look at the evolution of payroll. While not the payroll we know today, archaeologists have found evidence of payroll records in clay tablets dating back to 7000 B.C. There are also records from Athens in the fifth century showing that the Greeks liked to keep things in order. The Greek system is the first known system that bears some resemblance to the HR and payroll systems we use today. The Athenians developed a system for managing pay in which public servants, treasurers, and clerks kept records by chiseling payment details and financial records into stone!

Payroll as we know it today largely came about during the Industrial Revolution of the 18th and 19th centuries. With the onset of mass employment and production, the need arose to keep accurate records of workers and their pay. Without financial documentation, it would have been impossible to keep up with cash flow. This is when the term "payroll" was first used.

Computers have been around for a very long time. In 1822, Charles Babbage conceptualized and began developing the Difference Engine, considered to be the first automatic computing machine (although there are differing opinions on how successful it really was). But what is considered the first modern computer was developed and built around World War II. Alan Turing, along with a group of cryptographers, developed and built the Bombe, a code-breaking machine that decrypted the German "Enigma" code (remember the 2014 movie "The Imitation Game"?).

## First Payroll Computers

An early IT-based payroll system began to take shape in the 1950s, when the first computerized LEO (Lyons Electronic Office) was developed to handle clerical tasks. Its first applications were

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*Michael Pappas, CPP, is the Owner and Managing Director of MP Consulting Services, which provides solutions to payroll, human resources, and benefits problems as well as payroll educational training and expert witness services. He is a member of PAYTECH's Board of Contributing Writers.*

for valuations, but it was soon used to manage other clerical tasks, including payroll services. While this technology was revolutionary, it was only available to those companies that could afford the rather large investment it took to acquire it. Flash forward to the 1970s. Technology had advanced so much that individuals, mostly hobbyists and electronics buffs, could purchase and assemble computer kits, or "microcomputers." While these early microcomputers were a lot of fun, they could not perform the tasks that the computers of today can. We can all thank Bill Gates, Paul Allen, Steve Jobs, and Steve Wozniak for creating the bases for today's sophisticated and powerful computers. Just as an aside, *TIME Magazine* named the personal computer its 1982 "Man of the Year."

What does all of this have to do with payroll and its changing landscape and evolution? Everything! If the computer had never been invented, payroll would never have evolved past changing the payment method from cash to check. Because of the computer, a group of California bankers got together back in the late 1960s to figure out a way to stem the growing tide of paper checks being processed through the national check clearing system. That meeting was the forerunner of what we know as NACHA, which today oversees the local automated clearing houses (ACH) that serve more than 20,000 financial institutions across the United States. Those financial institutions provide ACH-based services to more than 300,000 corporations and organizations and millions of their clients.

My second involvement with payroll came many years later. After working in the accounting department of a company for a few years, I was asked to take over managing the payroll department because part of my accounting function was to supply payroll with money to be paid to employees. Here I had my first encounter with a payroll processor. It was still mainly a manual process, but we would code the payroll sheets and send them to the "service bureau," which would send back our payroll ledgers and checks. We checked everything, made corrections, created manual checks for any errors found, and all checks were picked up and delivered to the employees. The process was fairly simple but paper-intensive, and paycheck delivery was time-consuming. With the help of senior management, we started a direct deposit campaign. Eventually, the company had 85% of its employees on direct deposit. We all need to thank the computer and those California bankers. Without them, we all would still be running to the bank to cash a check in order to get spending money. But that was only the beginning of the changes in payroll and the evolution that is still taking place.

The third time I became involved in payroll, I stayed. Payroll had now become the challenge I had always sought. Not only had the processes evolved, so had the complexity of the payments. No

longer were you just doing addition, subtraction, multiplication, and division; you were reviewing tax law to make sure the firm was in compliance. You were looking for better ways to:

- Track employee hours
- Process the payroll
- Provide management with meaningful data regarding its payroll expenses
- Provide employees with accurate paychecks
- Allow employees to update their payroll information

The 1990s started the explosion of payroll technology. We could eliminate duplicate effort by integrating systems. Updating the payroll system became real-time or next-to-real-time. Then someone realized that instead of integrating the systems we could make them into a common database. With that change came a consistent look and feel to the systems. Those changes brought about standardized processes and, with them, best practices. Finally, the common database led to the modular concept. We not only could run HR and payroll off of a common database, we could incorporate time and attendance, absence management, talent management, workflow, accounting, and—what HR and payroll consider a boon as well as potential bane—employee self-service.

Now we are more than 15 years into the 21st century, and the technological advances in payroll have been coming quicker than a jackrabbit scurrying for its hole. Think about it. Since 2000, we have seen the advent of:

- Paperless payroll
- Payroll cards
- The move away from in-house payroll to Software-as-a-Service (SaaS)
- Remote data input
- Customized reporting instead of canned reports
- Electronic payroll tax filing

With all of these advances, payroll has become a more indispensable part of a business's success. One way a business can lead itself to failure is by making mistakes in how it pays its employees. To keep moving forward and to continue providing management with the data it needs, payroll needs to focus on technological changes that will help make a difference. In my estimation, four areas will make that difference: cloud computing, mobile technology, greater systems integration through what is known as “middleware,” and globalization and consolidation.

Why these four? Let's take a quick view of each.

### Cloud Computing

The biggest trend in 2014 and 2015 was to go paperless. Cloud-based solutions have propelled this trend. Why make the switch? Financially it makes sense; companies can save a great deal of time and money. Cloud-based systems are more user-friendly. Employees can check their payment status online, and employers have the ability to access payroll from anywhere, anytime. Plus, cloud-based computing gives the employer and the employee the ability to make use of mobile technology.

### Mobile Technology

It is estimated there are 1.8 billion smart phones in the world today—and that number is growing every day. With the smart

phone came the advent of apps. Apps allow the user to do everything from check a bank account balance to order a pizza. As more and more payroll providers take to the cloud, they have developed apps that help employees access self-service portals to quickly and easily access their work schedules, pay stubs, vacation accruals, and other important work information anytime, anywhere, and from any device. This capability is extremely important to those who work in remote locations. While they may not have access to a computer, almost everybody has a cell phone. I am not sure if it exists currently, but in due time you will be able to process payroll through an app.

### Middleware

You are probably asking yourself, “What is middleware?” Middleware is largely hidden from the payroll professional and, if done right, is invisible to the end user. You know middleware more typically as application programming interfaces, the programming and software that allow different systems to “talk” to each other. With the proliferation of systems in the market, it is critical that this “talking” goes as smoothly and efficiently as possible. Where you once took data from one system and pushed it to another on an individual basis, there is now a great deal of logic built in to the middleware. While this robust solution tends to be found in enterprise-class businesses today, it is slowly starting to show up in smaller operations. One example is Gusto (formerly Zen Payroll), an organization that specializes in small businesses, which says on its website that it can “seamlessly integrate online payroll with leading back-office products.”

### Globalization and Consolidation

We read more and more of companies going global. One of the biggest trends in payroll is a global company's movement toward integration of its employee population into a single “global system of record.” Global companies are beginning to realize that they need a complete view of their workforce and that workforce's payroll. You can see the results in the offerings by all of the major payroll providers as well as many of the second-tier providers. Just do an internet search on global payroll providers and see the number of hits you receive. The one I did while writing this article resulted in more than three million hits. The problem with global payroll is too much diversity in the payroll process from country to country. But if you refer back to my discussion on “middleware,” the diversity is surmountable. These interfaces will eventually make it possible to process global payroll under one system. This will be the starting point for what has been referred to as “Glocal”—going global with local expertise. Sometime in the near future, all of a global company's employees will be paid through one payroll system process.

Ever since the business world met the internet, modern technology has been of tremendous help to payroll and the payroll professional. The fusion of payroll and HR technology, at one time only available to the large business, is now available to the small business as well. Technology is changing business software, and payroll is one of the areas that is evolving quickly. Cloud computing, mobile technology, middleware, and globalization/consolidation are just a few of the trends that will be evolving and changing the world of payroll. Keep up with the changes! ■

# Year-End Lessons Learned

BY TRICIA RICHARDSON, CPP, SPHR, SHRM-SCP



**Y**ear-end can be a traumatic time of year for all payroll professionals. The most important tool you will ever need to make it less so, and the one I have found the most useful, is the list. This article will identify the lessons I have learned from year-end, in no particular order.

Did I mention, use a list? I may be a “seasoned” payroll professional, but even I have found that a list will help keep you on track. Many people think payroll doesn’t change year to year. That is a huge falsehood. Payroll changes almost *every* year. This seems especially true the last several years. Every time there is a legislative change in benefits, human resources, or taxation, payroll changes. You need a list to help you keep track of these changes. Did you consider deceased employees, relocation expenses, gift cards given out during the year, group-term life, tuition reimbursement, and personal use of an auto, just to name a few? If you had that list, you wouldn’t forget. If you work for a larger corporation and/or have a lot of fringe benefits, divide your list further into categories. In either case, start that list now so that you will have it in time for this year’s year-end. Here are a few more tips I have found to help you with a successful year-end:

## Start Early

Do not wait until the last payrolls in December. First of all, many payroll year-end adjustments have taxable implications. When is the worst time of year to do these? December (think

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*Tricia Richardson, CPP, SPHR, SHRM-SCP, is Founder, Purposed Payroll Professional (P3).*

holidays, last-minute tax planning, etc.) My advice would be to start these year-end adjustments in October.

Consider why you are doing these adjustments at year-end. The taxable value of group-term life can be imputed each pay and, ideally, should be. Moving expenses should be reflected in the payroll when the reimbursement is made. Why not handle personal auto fringe benefits monthly or quarterly, rather than annually?

## Trust But Verify

I use those three little words whenever I think of payroll systems. Preferably in October, but no later than November, run a set of W-2s. Check the federal and state taxable wages. Look at Box 3 Social Security Wages—are they under or at the wage base limit for the year? Do the taxes calculate correctly? If you use a sampling, choose different states, localities, and high wage earners. Make sure you choose a few employees who will have to pay the extra Medicare tax of .09%. If there is a problem, December may be too late to fix it.

Also, never be a tax advisor. Let me repeat that. Never be a tax advisor. Even if you know the answer, you do taxes on the side, and it is a pretty easy answer, what you say and what the employee hears will almost always be different. You are a payroll professional, and that is hard enough. Tax laws are complicated, and you never know what is going on in an employee’s life, tax-wise. Repeat after me: “I recommend you speak to a tax accountant.” Oh, and, “No, I cannot recommend one.”



## Educate Your Employees

Educate your employees because no one else will. One company I did some consulting with actually put signs inside bathroom stalls that explained what the most common Box 12 codes meant, that W-2s would be mailed or otherwise made available no later than January 31 (even though people still ask on January 2), and that Box 1 was not their gross wages but rather their taxable wages and what that meant, etc. Why the bathroom stall? Everyone uses the bathroom and, frankly, what else are they going to do? Loved it! How many emails do we get in a day? How many do your employees ignore from payroll? Dare I say—most if not all.

Prepare your employees to receive the Affordable Care Act—1095 Forms. I am shocked at how little has been advertised about these forms. The ACA law may be known, but not Forms 1095-C and 1095-B. Briefly educate your employees. Let them know they are getting Form 1095-C from you (and Form 1095-B from their insurance company if you are not self-insured) and that they will need information on the forms to complete their tax returns. I refer to it as the “Healthcare W-2.” This helps give employees a point of reference. I asked an HR director and vice president how they were planning to handle 1095s for their employees. I am certain it would not shock you to know the response was, “What is a 1095?”

## HR or Payroll? Plan Out Tasks

Decide early, and get it in writing, who will answer what. Employees will have questions about their healthcare. This is not going away. Payroll, truly, has nothing to do with healthcare; we just deduct the employee share of premiums and report and calculate any applicable taxability. The problem is, employees are going to call payroll. I have learned this is because, of all of the departments in a business, payroll understands timeliness, and we are the most responsive. Employees just call us first because they know they will get an answer. Benefits or HR (whichever handles open enrollment and benefit enrollment) needs to take these questions. Employees will need help. Get this figured out in December and communicate it to your employees. This did not happen last year. Payroll handled it. So, I am adding it to my list for this year.

## SWOT Analysis

Complete a Strengths, Weaknesses, Opportunities, Threats (SWOT) analysis with your payroll team at the end of each year-end process. Just because something was always done a certain way does not mean it should always be done that way. As a matter of fact, payroll should be changed based on

Every time there is a legislative change in benefits, human resources, or taxation, payroll changes. You need a list to help you keep track of these changes.

changing regulations. A great example—stop with the gift cards already! But if your company has found the best way to recognize and reward them is cash (and, by the way, that is not the only way—but that is a whole different list), then add it to their check and gross it up. Make this recommendation and push hard. You will be saving the employee receiving the gift card, the employee who has to purchase the gift card, and accounts payable. Add it to the employee’s check. Payroll will have to do this anyway. It will help with year-end adjustments. Whatever saves you from begging other departments for data, do it. It will save you, and them, the hassle.

## Who Gets the 1099s?

Decide early where the responsibility for issuing 1099 Forms will “land.” I have seen them end up everywhere. Some companies ask payroll to do them. Some ask AP. Some ask HR. Honestly, I recommend that AP complete this task. Payroll is for employees. With all of the new regulations and auditors coming down hard on misclassification of employees as independent contractors, these two should really be kept separate. AP is paying the contractors; it should manage the 1099s. Payroll can certainly provide some really good guidance on the regulatory requirements for maintaining the backup documentation and meeting compliance needs, but the payments and 1099s should come from AP. Have that conversation no later than January 1 for the current year.

## Take a Break, Celebrate

Take a day off (at a minimum) before and after. When it is all over, celebrate. My payroll team takes leftover Forms W-2 and makes airplanes or paper balls, and we throw them at each other. Or we have pretend snowball fights or just rip them up. I will never tell what we did with the extra 1095s!

Remember, we make it all happen! I think about this sometimes: Without Forms W-2, there would be no tax returns. Without payroll professionals, there would be no Forms W-2 (correct ones, anyway). Congratulations, another successful year-end accomplished! Don’t forget to start that list! ■

# Making Sense of Mandatory State Retirement Plans

BY ALICE P. JACOBSON, ESQ.

“Laws previously created for retirement no longer make sense because people don’t work at the same place throughout their career,” Senator Ben Cardin (D-Maryland) once said at a Pew Charitable Trusts Retirement Savings Senate Briefing in Washington, D.C. He added, “We need to reform our tax code. There is a huge deficit in retirement security. Americans don’t save enough.”

## APA Participates in State Retirement Plans

The APA is participating in the Pew Charitable Trusts’ effort to develop a document, directed at state policymakers, detailing potential issues involved with the implementation and administration of state-level retirement savings plans. The goal of the Pew project is to share with policymakers the concerns of those who provide retirement services that may otherwise be overlooked. The document will not endorse or oppose any particular state proposal or program. Therefore, political concerns will only arise with regard to states’ decision-making framework. For example, some state legislatures are in session only part of the year or every other year. Different agencies within states may be responsible for program development and implementation and each has specific authorities.

The APA’s Government Relations Task Force (GRTF) Subcommittee on Retirement Accounts is watching state program developments closely. Payroll professionals play a role in transfers of deductions to employee retirement accounts. Depending on state plan requirements, they also may work with HR departments to prepare lists of employees eligible for state programs, distribute information to employees, and collect initial or program

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*Alice P. Jacobson, Esq., is Senior Manager of Government Relations for the APA.*



entry forms such as opt-out records. At the very least, employees may ask questions, and payroll professionals need to know how to direct them.

## Senate Briefing Details

Senator Cardin offered comments on the need for reform at the federal level and also commented on retirement programs. He stated that policies for savings need to be stronger to make pulling money from savings more difficult. Importantly, he emphasized that when employers contribute to retirement plans for their employees, participation increases exponentially. His message is that the tax code should include tax deferral options for retirement savings.



## Top Three Takeaways

**As part of the Pew Charitable Trusts' effort to share concerns about state mandatory retirement plans, the APA is working on issues that have a direct impact on payroll professionals. These issues include:**

1. Uniform definitions across states
2. Reporting and record-keeping
3. Managing multi-state plans

He cautioned that while tax incentives are important, they also are controversial. Politically, people still believe that wealthy people are the only ones who benefit from tax incentives. Cardin says this is not true, and that the problem can be fixed by focusing taxes on consumption, not income.

Discussing findings from an AARP Utah study commissioned by Notalys LLC, Debra Whitman, Chief Public Policy Officer at AARP, reported that 18% of retirees in the next 15 years will retire with more debt than savings. A 10% increase in net worth by individuals who are the least prepared for retirement will save taxpayers \$194 million through 2030. Whitman said state programs should utilize the “power of payroll deduction, automatic enrollment, and automatic escalation when possible.” Low fees and self-sustaining plans are the best to encourage participation.

“These programs allow employees and small businesses to benefit from the power of pooling,” she said.

Because states are concerned about the burden on state budgets caused by welfare for retirees with limited personal resources, they often consider the amount saved, not what is needed for retirement, when developing state plans.

### Employer Considerations

James Klein, President of the American Benefits Council, raised some issues with the proposal by the DOL to add a safe harbor for state plans from certain Employee Retirement Income Security Act (ERISA) requirements. In particular, a condition of the ERISA safe harbor allowance is mandatory employer participation, but the condition is not well defined. For example, if a state plan applies only to employers with 25 or more employees and voluntary for all other employers, will the ERISA safe harbor apply? Why are multiple employer plans only available to states and not private sector initiatives?

For state initiatives, Klein raised some questions:

- What happens if a state mandates its plan on an employer unless that employer’s program meets certain criteria such as automatic enrollment, offers of specific investment options, and required levels of employer contributions?
- What employer reporting will state plans require?
- How will employers comply with inevitable conflicting standards?

Klein also discussed changes to employer benefits that may impact retirement programs going forward.

“Employers are transitioning away from thinking of benefits in separate silos and instead are taking a holistic view of health and financial well-being or personal financial security,” he said.

Rather than separate retirement plans, health insurance coverage, disability protections, and long-term care benefits, these are being bundled through advanced funding on a tax-preferred basis into accounts that serve multiple income protections. The burden on payroll professionals is reduced in a holistic approach because only one wage distribution is required instead of multiple calculations for different benefits.

In addition, Klein offered some suggestions on how to promote retirement security by asking states to keep their plans voluntary, simple, and portable. States and federal agencies should exclude retirement plan assets and future retirement plan benefits—whether offered by an employer or government—from state or federal housing and food subsidies. Government entities should allow employers’ voluntary participation in an ERISA safe harbor retirement plan maintained by an entity other than employers themselves.

As a final note, Klein suggested that a federal framework for retirement programs is needed regardless of state plans because of the possibility of many different state plans.

“Different states, different programs—this is a huge burden on employers,” he said.

The APA believes that the federal government should exempt employers from state plans if employers set up their own plan. This would encourage employers to offer retirement plans to their employees.

As states progress in developing mandatory retirement plans, the APA is working through the issues that may impact payroll professionals. This includes uniform definitions across states, reporting and record-keeping, and managing multi-state plans. ■

# State Payroll News You Need to Know

BY LIA CONIGLIO, ESQ.

## Oregon Says Uber Drivers Are Employees

The Oregon Bureau of Labor and Industries (BOLI) has issued an advisory opinion regarding the employment status of drivers for Uber, a ride-sharing company [BOLI, Advisory Opinion, 10-14-15]. The BOLI concluded that under Oregon law, Uber drivers are employees and not independent contractors.

### Economic Realities Test

The BOLI uses the “economic realities test” to determine whether an individual is an employee under the federal Fair Labor Standards Act. The test considers the degree to which a worker is *economically dependent* upon the employer.

The economic realities test uses the following six factors:

1. The degree of control exercised by the employer;
2. The extent of the relative investments of the worker and the employer;
3. The degree to which the worker’s opportunity for profit and loss is determined by the employer;
4. The skill and initiative required in performing the job;
5. The permanency of the relationship; and
6. The extent to which the work performed by the worker is an integral part of the employer’s business.

The BOLI considered all six factors:

**Degree of control.** Uber dictates the fare to be charged to passengers, and a percentage of that fare is paid to drivers. Uber monitors the performance of drivers and may terminate drivers who do not perform. These factors show significant control by Uber.

**Relative investments.** A driver’s investment is mostly the use of a personal car, including fuel, maintenance, and insurance costs, while Uber provides the software application. This indicates an employment relationship, as the driver’s expenses are small when compared to Uber’s “multi-billion dollar infrastructure.”

**Worker’s profit and loss.** Uber sets the fare charged to passengers without input from the drivers. Because a driver’s ability to earn more money is dependent upon his or her ability to work and not his or her managerial skills, this indicates an employment relationship.

**Skill and initiative.** Drivers are dependent on Uber’s app in order to perform work and do not exercise managerial skills or initiative that would indicate that they are operating an independent business.

**Permanency of the relationship.** Uber does not hire drivers to perform services for a fixed period of time or on a contract basis. As long as drivers meet Uber’s standards, they may work

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*Lia Coniglio, Esq., is Manager of State Payroll Information Resources for the APA.*

indefinitely. The relationship may be expected to last for a long period of time and therefore indicated an employment relationship.

**Work as an integral part of business.** Uber provides transportation services to its customers, services it cannot provide without drivers. Therefore, the drivers’ work is a necessary part of Uber’s business.



## Florida Rules Uber Drivers Are Independent Contractors

The Executive Director of the Florida Department of Economic Opportunity (DEO) has ruled that Uber drivers are independent contractors—not employees—and therefore not entitled to file for unemployment insurance benefits in Florida [Raiser LLC v. Florida Department of Economic Security, No. 0026-282590-02, 9-30-15]. This is in contrast to opinions that have found the drivers to be employees of Uber in several other states, including Alaska, California, Oregon, and Vermont.

### Uber App

The ruling describes Uber as “a technology platform that, for a fee, connects transportation providers with customers seeking transportation.” The agreement between Uber and the drivers specifies that the drivers are independent contractors.

### Facts Show Drivers Have Control

The ruling states that drivers are independent contractors because they have “significant control over the details of their work.” The drivers use their own vehicles and choose when and if to provide services through Uber’s software app. Drivers also decide where to work and which customers to serve. The driver also controls many of the details a customer experiences. Drivers are allowed to provide services through other competing platforms and can work for competing companies when not using the Uber app. According to the ruling, the facts show that Uber operates as a middleman or broker for transportation services, not as an employer.

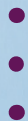
### Criticism of California, Oregon rulings

The Florida ruling argues that previous rulings issued in California and Oregon that concluded the drivers were employees of Uber were not persuasive. This is because they “largely ignore the contract” between the drivers and Uber, and misconstrue the actual course of dealings between the parties. The Florida ruling claims the previous rulings rest on the fact that Uber could not be in business without the drivers. According to the DEO, Uber is no more an employer to drivers than an art gallery is to artists. The DEO ruling references other applications such as “eBay, Airbnb, and Amazon Marketplace” and says they would not be in business without the goods and services providers that use their platforms. However, this does not mean the providers are automatically employees of the platform company. ■

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# IRS 'Reminds' Employers of Tax Obligations

BY CURTIS E. TATUM, ESQ.

The IRS has released a fact sheet “reminding” employers of the importance of properly depositing and reporting employment-related taxes. The fact sheet provides information on some of the more common employment tax problems, including worker classification, the voluntary classification settlement program, fringe benefits, officer compensation, and penalties associated with backup withholding and information returns [FS 2015-25; <https://www.irs.gov/uac/Newsroom/General-Employment-Tax-Issues>].

## Worker Classification

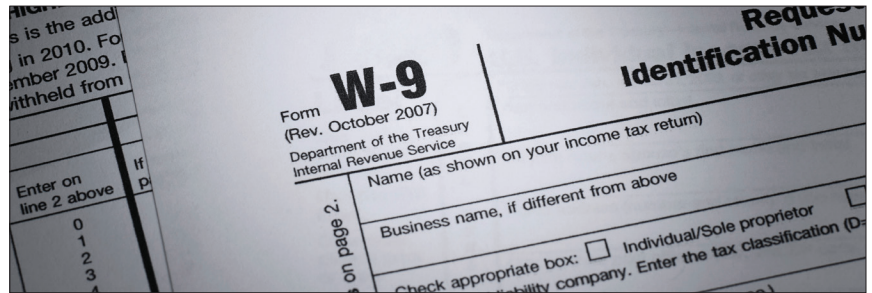
The IRS highlights incorrect worker classification as a common error and reminds employers that their tax responsibilities vary greatly based on whether the worker is treated as an employee or an independent contractor. Employers are required to withhold and pay the employer portion of the employment taxes on wages paid to employees while there are no such obligations on payments made to an independent contractor. Additional guidance on proper classification may be found in IRS Publication 1779, *Independent Contractor or Employee*.

## Voluntary Classification Settlement Program

The Voluntary Classification Settlement Program (VCSP) is a program that allows businesses to voluntarily reclassify their workers as employees for future tax periods for federal employment tax purposes and to obtain partial relief from the federal employment taxes due during the periods of misclassification.

To participate in the VCSP, the taxpayer must meet certain eligibility requirements, apply to participate and, if accepted, enter into a closing agreement with the IRS. Taxpayers should apply at least 60 days before the date that they want to begin treating their workers as employees. In order for their application to be considered, taxpayers must attach a list of names and social security numbers of all workers to be reclassified as part of the VCSP agreement. IRS Announcement 2012-45, which provides additional guidance about the VCSP, is available on the IRS website at [https://www.irs.gov/irb/2012-51\\_IRB/ar16.html](https://www.irs.gov/irb/2012-51_IRB/ar16.html).

*Curtis E. Tatum, Esq., is Senior Manager of Payroll Information Resources for the APA.*



## Fringe Benefits

A fringe benefit is a form of payment for the performance of services. Any fringe benefit is taxable and must be included in the worker's income unless the law specifically excludes it or the recipient pays for the benefit. Section 2 of IRS Publication 15-B, *Employer's Tax Guide to Fringe Benefits*, provides additional guidance on the taxation of fringe benefits.

## Officer Compensation

Corporate officers are, by statute, employees. Many S Corporations and closely held C Corporations fail to treat payments to their officers for services as wages and instead treat them as corporate distributions, loans, and payments of personal expenses. An IRS website that provides guidance on the proper treatment of payments to corporate officers is available at: <https://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/S-Corporation-Employees-Shareholders-and-Corporate-Officers>.

## Form 1099-MISC, Backup Withholding, Information Return Penalties

Businesses should always secure the Taxpayer Identification Number (TIN) for any workers treated as independent contractors to whom the business makes reportable payments (\$600 or more per year) so that they can properly report those payments on Form 1099-MISC. Businesses can use Form W-9, *Request for Taxpayer Identification Number and Certification*, to obtain the worker's TIN.

Certain reportable payments to individuals may be subject to backup withholding, currently at a rate of 28%, when a payee's TIN is missing or incorrect on an information return.

Information return penalties apply to the failure to file correct information returns, including Forms 1099-MISC and W-2. The penalties per information return depend on when the business correctly filed the information return, and there is a maximum penalty per year depending on the size of the business. ■

# Recognizing Taxes on Noncash Fringe Benefits

BY SALLY THOMSON, CPP

The IRS has established special rules for recognizing noncash fringe benefits, such as gifts or the value of group-term life insurance. The benefits must be reported as income at least once a year by December 31. Best practice is to report these benefits more often. Employers may elect to report noncash items every pay period, monthly, or quarterly. You can change the reporting period as often as you like, as long as all benefits provided in a calendar year are reported as paid no later than December 31. You can select different reporting frequencies for different noncash fringe benefits and for different employees. You can allocate the value of a benefit over multiple pay periods in a calendar year. Here is an example:

An employee, paid weekly, wins a trip with a fair market value of \$1,500 in a company contest. If the value of this benefit is added to one pay period, the additional tax withholding could result in the employee receiving little or zero net pay. The employer may elect to allocate the \$1,500 over multiple pay periods so as not to create a financial hardship on the employee.

There are three excellent reasons to report the value of these benefits as often as possible rather than waiting until the last pay period of the year:

**Reason No. 1 is for the payroll team.** December is a busy month for us. We're wrapping up end-of-year processing while preparing for upcoming changes in the new year. Why would we add more to our work load during this time if it's not necessary? Report those benefits as often as you receive the information. Better yet, be proactive! Communicate with human resources, accounts payable, and other departments that report this information to payroll. Ask that the details of all taxable benefits, prizes, gifts, etc., be provided to you as soon as the benefits or items are awarded.

**Reason No. 2 is for our employer.** If we wait until the last payroll processing of the year to report fringe benefits and any employees receiving benefits have terminated, they are no longer receiving wages from which to withhold taxes. The employer will have to pay the taxes for the employee. Grossing up is expensive for employers. By reporting benefits as soon as possible, we can eliminate gross-ups and save our employer money.

*Sally Thomson, CPP, is Director of Payroll Training for the APA.*



**Reason No. 3 is for our employees.** During December, employees appreciate every penny in their pay. It is the holiday season. There are gifts to be purchased. If we wait until December to report and withhold additional taxes from an employee's pay, it results in reduced net pay. Let's help to keep our employees happy by reporting taxable benefits as often as possible during the year.

Employers have another option for reporting certain noncash fringe benefits. It's called the special accounting rule. With this rule, noncash fringe benefits actually provided to employees during November and December, or a shorter period within these two months, can be reported as being paid in the next year. However, certain restrictions apply:

- Employers must notify employees of their decision to use the special accounting rule.
- If the rule is used for a benefit, it must be used for all employees receiving that benefit.
- This rule cannot be used to value taxable moving expenses, group-term life insurance, or personal property normally held for investment or real property. ■

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