

HUNTER HAGAN & COMPANY, LTD.

2007 EMPLOYER TAX UPDATE

WITHHOLDING TAXES

As an employer, you are responsible to withhold and/or pay various types of Federal and State taxes on your employee's salaries. Here is a brief description of each kind of tax.

FEDERAL INCOME TAX WITHHELD

Federal income taxes are required to be withheld from all employees unless they are exempt from these withholdings (as indicated on Form W-4). Each employee must complete a Form W-4 and submit it to the employer before being paid. An employer determines how much to withhold by using the Internal Revenue Service's Publication 15, Circular E, Employer's Tax Guides. This publication is available at www.irs.gov/formspubs/index.html.

F.I.C.A. WITHHELD

F.I.C.A. taxes consist of Social Security and Medicare taxes withheld from each employee. The rate for 2007 is 6.2% of the first \$97,500 of annual wages for Social Security taxes and 1.45% of *all earning* for Medicare taxes. The employer is required to match the employee's contributions dollar for dollar. Federal taxes, F.I.C.A. taxes withheld and the employer matching the F.I.C.A. taxes are required to be reported quarterly on Form 941.

Self-employed individuals pay 12.4% of the first \$97,500 of self-employment earnings for social security taxes and 2.9% of all self-employment earnings for Medicare taxes.

FEDERAL TAX DEPOSIT REQUIREMENT

The federal income taxes withheld and the F.I.C.A. taxes withheld, along with the employer's "matching" of F.I.C.A. taxes must be deposited as required at a Federal Depository, unless the employer is required to deposit electronically.

2007 DEPOSIT RULES

The following EFTPS (Electronic Federal Tax Payment System) rules went into effect on **January 1, 2000**. If the aggregate of your corporate income tax, corporate estimated taxes, payroll taxes and tax deposits in calendar year 1998 or any calendar year thereafter exceeded \$200,000, you are required to make ALL federal tax deposits (not just withhold taxes) electronically. A special sign up form should be completed for the IRS and requires information regarding your banking institution. If your aggregate tax deposits first exceed \$200,000 in 2001 or a later year, you must begin making all federal tax deposits electronically in the second year after the year in which the \$200,000 threshold was met. A taxpayer that exceeds the

\$200,000 threshold and is required to deposit electronically, may not resume making paper coupon deposit if its deposits fall below \$200,000 in a later year. Most (but not all) payroll services comply with these requirements and will provide you with this service for all tax payments.

If you do not fall under the EFTPS rules, you will deposit under a separate schedule.

The IRS will notify you each November whether you are a monthly or semi-monthly depositor for the coming calendar year. Call us if you unsure as to when to make your deposits.

ARIZONA INCOME TAX WITHHELD

Arizona income taxes are withheld based upon a percentage of the Federal income taxes withheld. If the employee earns less than \$15,000 per year, 10% of the Federal income taxes can be withheld. If earnings exceed \$15,000, the withholding can be 19%, 23%, 25%, 31% or 37%. Form A-4 should be completed annually to elect the appropriate withholding rate for the state.

STATE TAX DEPOSIT REQUIREMENTS

The state is also requiring that tax payments be made electronically if your average quarterly state withholding tax liability for the

preceeding year is \$20,000 or more. The state is in process of issuing regulations that may substantially reduce the threshold for the required electronic payment of withholding taxes. Again, your payroll service can help you comply with these regulations.

Most small employers may remit taxes withheld quarterly with the filing of Form A1-QRT. Late or incomplete filing of this report may result in penalties and interest.

We recommend deposits be made on the same schedule for the federal deposits.

UNEMPLOYMENT TAXES

FEDERAL UNEMPLOYMENT TAXES (FUTA)

Of the first \$7,000 of each employee's annual wages, .8% is paid to the Internal Revenue Service. These amounts are usually deposited quarterly and are reported annually (on a calendar year basis) on Form 940 or Form 940EZ.

Employers are required to make a quarterly deposit for unemployment taxes if accumulated tax exceeds \$500.00.

**STATE UNEMPLOYMENT TAXES (SUTA)
(DEPT. OF ECONOMIC SECURITY)**

The State Unemployment Tax Fund is paid on a quarterly basis. The rate is determined by the state (2% for a new employer), on the first \$7,000 of wages paid to each employee annually. This is *state mandated insurance*.

Based upon the state's experience with the employer, an annual notice reflecting a new rate factor is sent to the employer. Payments are remitted quarterly with Form UC-018.

PAYROLL SERVICES

There are various payroll services which will assist you with most of your legal obligations related to your payroll. We *highly recommend* you retain one of these services. For a small fee they help you track all of the record keeping obligations, ensure deposits are made in a timely manner and complete and file all required quarterly and annual forms. They can help administer other employee benefit programs such as Section 401(k) plans and medical premium withholdings.

INDEPENDENT CONTRACTORS

There are numerous factors which determine whether an individual is classified as an independent contractor or your employee.

BE VERY CAREFUL before making this determination yourself. Here are just *a few* of the issues involved:

*Does the person render services which only they personally can provide?

*Do they provide the same service to other employers at the same time?

*Do they provide their own tools?

*Can they follow their own set hours of work?

Failure to properly classify someone as your employee can be very costly and the burden of proof falls to you, the employer, despite what the individual involved may have told you regarding their responsibilities. You could be required to pay back taxes.

FORM W-9

This form should be completed by any entity or individual, other than employees, performing services for the company. If the individual fails to furnish a taxpayer identification number, you are required to withhold 28% of their payment for federal income taxes. This backup withholding is reported on Form 945 by the payer and on Form 1099 to the payee.

FORM 1099/1096

Form 1099-MISC reports payments to any (independent contractor) individual or unincorporated company that received at least \$600 of rents or services during the calendar year. Form 1099-MISC must be issued for payments to attorneys of at least \$600, without regard to whether the payment was made to a corporation. Form

1099-INT or 1099-DIV must also be issued for interest and dividend payments of at least \$10 during the year. Form 1099's for 2006 are required to be provided to the recipient by January 31, 2007 and are required to be sent to the IRS by February 28, 2007. Form 1096 is the transmittal form which must be submitted to the IRS along with the corresponding Form 1099. The payer may be subject to penalties if a required Form 1099 is not filed.

The telephone number for a contact person is now required on all 1099 forms sent to a recipient (also on Forms W-2G and 1098's).

SUMMARY FILINGS	
<u>Quarterly</u>	<u>Annually</u>
941	W-2
UC-018	W-3
A1-QRT	A1-R
FUTA	940
	945
	1096
	1099
Deposits -- As Required	

OTHER FORMS

FORM W-2/W-3

This form must be provided to each employee annually by January 31st of the next year. Copies are sent to the Social Security Administration and the Arizona Department of Revenue along with the transmittal Form W-3 and Form A1-R, respectively.

FORM 945

Distributions from qualified retirement or pension plans are subject to a mandatory 20% withholding of federal income taxes unless the employee decides to have the distribution paid directly to an IRA or other qualified plan. Such withholding is reported annually for any year in which a distribution is made.

FORM I-9

Employers must verify that new employees hired are eligible to work in the United States. Form I-9 must be completed and kept as part of the employee's personnel file for three years after the date the person begins work or one year after the person's employment is terminated (whichever is later). This form must be completed within three business days of an employee's hire date.

COMPENSATION

MINIMUM WAGE

The Department of Labor requires employers to pay a minimum wage of \$6.75 per hour. However, certain state and local jurisdictions may have a higher minimum wage rate.

PERSONNEL MANUALS

In an Arizona court case, it was held that a personnel manual may create an implied employee contract.

As the result of this decision, it may be a prudent time to have your current and superceded personnel manuals reviewed for any potential problems. If the identified problems are currently resolved, you may be able to avoid costly litigation in the future.

OVERTIME PAY

An employer is required to pay time and one-half for all employees that work more than 40 hours per week unless you control overtime hours by giving time off during the same week the overtime was worked. Certain state and local jurisdictions may impose additional overtime requirements. For example, in the State of California an employer is required to pay time and one-half if the employee works more than 8 hours per day and double if the employee works more than 12 hours per day. In limited instances, certain professional and management positions are not required to be paid overtime. An employer should assume that all employees are subject to the overtime rules. If there are any questions regarding overtime and which occupations may be exempt, please call our office.

WORKERS COMPENSATION INSURANCE

Each employer is required to insure their employees against job related injuries either through Arizona State Compensation Fund or through their own insurance carrier.

The rates are competitive and employers can ask their insurance agent and the State Compensation Fund for bids. The rates are based upon the type of work performed by the employees and the respective risk of injury for the work performed. For example, office workers are generally insured at a much lower rate than truck drivers. Most carriers require a deposit and let the employer elect to pay premiums quarterly, semi-annually or annually.

Additionally, fringe benefits which result in salary reductions, such as cafeteria plans, must be included in wages reported for purposes of determining worker's compensation premiums.

NEW HIRE REPORTING

All employers doing business in the State of Arizona must report the hiring (or rehiring) of any person who resides or works in Arizona and to whom the employer anticipates paying compensation. The new hires can be reported directly on-line with the Arizona Department of Economic Security at <http://www.az-newhire.com>. Other states have similar reporting requirements.

UNCASHED PAYROLL CHECKS

Employer must report and remit to the State of Arizona any uncashed payroll checks that have been outstanding for 5 or more years. These checks are reported on a Form 601.

SOCIAL SECURITY NUMBER VERIFICATION

All employers are now required to verify that their employee's names match the social security numbers on record with the Social Security Administration (SSA). The SSA can impose a \$50.00 fine per incident where a name does not match the SSN on record when the W-2's are filed. To verify your employee's names and SSN's go to www.ssa.gov/employer/ssnv.htm.

AUDITS!

As an employer, you are subject to audit by the Internal Revenue Service, the Department of Labor, the State of Arizona, the Department of Economic Security and your worker's compensation insurance carrier. It is imperative that you maintain proper, neat, and accurate payroll records for each employee and for each payroll on a monthly, quarterly and annual basis. We can help you set up the proper payroll records. We can prepare the quarterly and annual returns, if you prefer.

MISCELLANEOUS LAWS

The following are government rules and regulations which, depending on your size, affect how you conduct your business.

This list is not intended to be comprehensive and additional rules and regulations may be imposed by the state and local jurisdictions.

AGE DISCRIMINATION
20 or more employees

OSHA REGULATIONS
all employers

FAMILY LEAVE RULES
50 or more employees

NOTICE OF PLANT CLOSINGS
100 or more employees

DISABILITY REGULATIONS
The employment provisions apply to the employers with 15 or more employees, while the public accommodation provisions apply to all businesses.

COBRA
(group health insurance)
20 or more employees

STATE & LOCAL REGULATION

Certain state and local jurisdictions may impose substantial additional regulations beyond those imposed under Federal law.

This is a limited overview of the rules and regulations that apply to employers. There may be additional taxes or considerations that are not listed here such as special rules and regulations, child labor laws and other rules for specific industries and businesses. If you have any questions, relating to these matters, we will be happy to discuss them with you.
