

Federal Requirements for Payment and Reporting of Employee Wages and Benefits

The Municipal Assistance Center frequently fields questions from our members about the tax and reporting treatment for various wage and benefit arrangements. Internal Revenue Service (IRS) rules and regulations are complex, so it is easy to understand why we receive so many questions. Many of the answers can be found on the IRS website, www.irs.gov, but the site is not user friendly, even for those of us who use it frequently. This is the first in a series of articles that will explore the website with you, showing you how to navigate the site, and explain some of the vast amount of information that it contains.

Navigating the Site. Information for local governments is included under the Federal, State and Local Government (FSLG) section of the IRS website. The site has recently been redesigned, and it is unfortunately more difficult to find the FSLG pages. In the upper right corner is a drop-down menu identified by the words *Information for...* Place your cursor over that menu and click on the section titled *Government Entities* and to bring you to the home page for all types of government entities. Choosing the top selection, *Tax Information for Federal, State & Local Governments*, opens the FSLG home page.

The FSLG Home Page. The main body of the page contains links to topics that are timely, as well as some general links of interest to municipalities. For example, currently the page has links to information on the *Patient Protection and Affordable Care Act (PPACA)*, and *Quick Links for Government Entities*. On the left side of the page are additional links to FSLG topics, some of which are also found on the home page. As you explore the various sections and links on this page, you will find that there is often more than one way to find the information you are looking for. Let's spend a few minutes looking at some of the links on the page.

We can start with a closer look at what FSLG does. Its mission is to provide government entities with top quality service by helping them understand and comply with their tax responsibilities and applying the law with integrity and fairness to all. Its representatives provide assistance in employment tax withholding, reporting and filing, and for information return reporting for payments to vendors, as well as guidance on any federal tax-related issue. They provide these services both through individual interaction and educational seminars.

FSLG also works with the Social Security Administration (SSA) to educate government entities about Section 218 Social Security Agreements. These voluntary agreements provide social security and/or Medicare coverage for state and local employees. While the IRS is responsible for administering and enforcing the laws, SSA processes and interprets these agreements and related coverage issues. More information about Section 218 agreements can be found elsewhere on the website, or at SSA's State and Local Government Employers webpage, www.socialsecurity.gov/slge.

Also on the home page is a link to another timely topic, Affordable Care Act provisions, a number of which will become effective in 2013. This link will provide you with up-to-date information on, for example, new provisions for additional Medicare taxes on high income individuals, new rules about how much can be contributed to a Flexible Spending Account (FSA), requirements for reporting health care coverage on Form W-2 and available transition year relief, and implementation of the PPACA.

There is also a link to the IRS' *Compliance Self-Assessment Tool*, which allows you to review all areas of federal tax law that a government

typically deals with by providing links to resources that deal with specific issues.

FSLG Newsletter. A link on the left side of the home page will take you to the semiannual *FSLG Newsletter*. Not all topics in it will be of interest to all governments, but the newsletter addresses current concerns of FSLG. In addition, it provides phone numbers of FSLG specialists who represent Vermont. Issues addressed by these specialists include general information about SSA Section 218 agreements, worker classification as employee or independent contractor, special employment tax rules for public employees, and other federal tax issues for government entities.

Vermont's two specialists are Fran Reina (315-793-2932) and Stephen Polak (802-859-1049). Although you can direct questions to the general customer account services number (877-829-5500), these specialists can give you a more accurate answer as some issues differ from state to state.

FSLG Fact Sheets. To address the recurring issues that impact almost all local governments, FSLG has developed a series of fact sheets that can be accessed from the link on the left side of the home page. Some of them, such as the fact sheet for information return reporting for state and local governments, you may wish to access frequently. Others, such as how to treat group-term life insurance provided for employees, you may only need to access one time. Following are descriptions of other pertinent fact sheets.

Information Return Reporting for State and Local Governments provides guidance on requirements for information returns. Government entities are generally subject to the same information reporting requirements as businesses are, and must file information returns for each calendar year with respect to payments made during the course of the year. These information returns include Form 1099-MISC for miscellaneous payments such as rent (including both building rent and equipment rent), services (including parts and materials), prizes, awards, or other income payments; Form 1099-INT for reporting amounts of interest

income paid by a government entity during the course of the year; Form 1099-R for reporting distributions from certain pensions, annuities or retirement plans; and information about backup withholding.

Government Workers: Employees or Independent Contractors? answers the question of whether someone who works for you is an employee or an independent contractor has important tax consequences concerning paying and withholding income and social security/Medicare taxes, reporting requirements, workers' compensation, and other liability consequences. While each government entity that addresses this issue (Department of Labor, Internal Revenue Service, etc.) has its own particular requirement, most revolve around three tests:

1. behavioral control – whether the service recipient has a right to direct or control how the worker performs the task for which he or she is hired, including providing training or instruction;
2. financial control – whether the service recipient has a right to direct or control the financial aspects of the worker's activities, including whether the individual has a significant investment and expenses and has the opportunity for profit or loss; and
3. the type of relationship – whether the parties intend there to be an employee-employer relationship, including any written contract between the parties, whether employee-like benefits are being provided, and the permanency of the relationship.

Some employees are covered by special rules. Emergency workers are hired on a temporary basis in case of fire, storm, snow, earthquake, flood, or other emergency, and compensation for these workers is excluded from Social Security and Medicare withholding under IRC 3121(b)(7)(F)(iii). This does not include permanent employees who work regularly in response to emergencies. Election workers are provided an exception from the Federal Insurance Contribution Act (FICA, a payroll tax) withholding for services provided in that

capacity when the payments are below a specified amount during the course of the calendar year. This exception does not apply to these workers when they are engaged in non-election duties. For example, members of the Board of Civil Authority often serve as election workers, but also may be paid for property tax appeals and abatements. Persons performing these duties are not considered to be election workers for those hours worked.

Classification of Elected and Appointed Officials. Generally, any individual who serves as a public official is an employee of the government for which he or she serves. Accordingly, the government entity is responsible for withholding and paying income taxes, Social Security and Medicare taxes, and issuing a W-2 to a public official. While there is no precise definition for the term public official or public officer, it has generally been held that anyone who exercises significant authority pursuant to public laws is a public officer. This includes any official who administers or enforces public laws, whether the individual is elected or appointed.

Some factors that indicate the office is “public” include the fact that the office was created by the constitution or through legislation, or by a municipality or other body with similar authority; the office was delegated a portion of the powers of a government body; the powers conferred and the duties to be discharged are defined either directly or indirectly through law or legislative authority; the duties are to be performed independently and without control of a superior power other than the law; and the office has some permanency and continuity. Examples include a member of a legislative body (such as a city council or school board), a justice of the peace, a constable, a registrar of deeds, tax collectors and assessors, and members of advisory boards and committees.

Issues for Firefighters. Generally, tax laws apply to firefighters in the same manner as for other types of workers. It does not matter whether firefighters are termed “volunteers,”

are considered employees or are identified by any other name. If the work they do is subject to the will and control of the payer, they are considered employees for federal tax purposes. Similarly, it does not matter whether they are paid on an “on-call” basis, monthly, hourly, etc., or whether the worker is full-time or part-time. Some benefits may be excluded from income based on specific sections of the law, such as health insurance, education benefits, or meals provided for the convenience of the employer, or for reimbursement of expenses under an accountable plan. (Accountable plans will be discussed in a future article on Fringe Benefits.)

Future articles will cover some of the Frequently Asked Questions included on the website, as well as discuss some of the wage and tax topics covered in the various publications and other educational products that are available from the IRS.

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