

Subject: From APA – Fiscal Cliff Impacts First 2013 Payrolls

## **AMERICAN PAYROLL ASSOCIATION Compliance Update**

### **Employers Should Use 2012 Withholding Tables Until 2013 Tables Are Available; Other Changes Take Effect January 1, 2013**

President Obama and Congress continue to be divided about how to avoid the “fiscal cliff” caused by the simultaneous expiration of the Bush-era tax cuts and the implementation of deep cuts in federal government spending scheduled to take effect January 1, 2013. Because of the failure to resolve the fiscal cliff problem and the underlying uncertainty as to what the income tax rates will be in 2013, the Treasury Department has not issued withholding tax tables for 2013 or any other official guidance on how employers should proceed.

When asked by callers during the monthly conference call between IRS personnel and payroll stakeholders on December 6 how employers should determine 2013 withholding from their employees’ wages, John Tuzynski, Chief of Employment Tax Policy at IRS, said “it would be consistent with the past for employers and payroll providers to continue using the 2012 withholding tax tables in 2013 if no new tables are issued by the time they begin processing 2013 payroll.” Tuzynski and other IRS personnel also stated that they hoped to receive guidance from Treasury soon on how to calculate 2013 withholding.

Earlier this week, APA sent a letter to Treasury and the IRS asking that they issue official guidance on processing 2013 payrolls without 2013 withholding tables, but so far none has been forthcoming. It is now December 21, and employers should put Tuzynski’s advice into effect by continuing to use the 2012 withholding tables as they gear up to process their first payrolls of 2013, even though the 2012 tables state they are to be used for wages paid “through December 2012” and income tax rates are scheduled to increase for nearly all taxpayers.

#### **Other rate changes take effect on January 1**

How to calculate withholding without 2013 withholding tables is certainly not the only unresolved issue for payroll as January 1 approaches. If Congress does not act by then, other withholding changes will take effect that do not depend on new withholding tables.

- **Supplemental withholding rates increase.** For supplemental wage payments (e.g., bonuses) made on or after January 1, 2013, the optional flat rate for amounts up to \$1 million in a year increases from 25% to 28%. For supplemental wage payments made on or after January 1, 2013, the mandatory flat rate for amounts over \$1 million in a year increases from 35% to 39.6%. Remember that these rates apply when the payments are made, not when they are earned.

- **Backup withholding rate increases.** The rate of withholding on payments that are subject to backup withholding because of a missing or incorrect Taxpayer

Identification Number increases from 28% to 31% for payments made on or after January 1, 2013.

- **Employee social security tax rate increases.** The payroll tax cut that reduced the employee share of social security tax from 6.2% to 4.2% in 2011 and 2012 expires on December 31, 2012. Therefore, social security tax must be withheld at the rate of 6.2% from employees' wages paid on or after January 1, 2013.

#### **Other fiscal cliff issues for payroll**

- **Educational assistance exclusion expires.** Currently, employers can provide employees with up to \$5,250 in nonjob-related tax-free educational assistance under IRC §127. However, §127 expires on December 31, 2012. Therefore, amounts paid on behalf of or reimbursed to employees under a §127 educational assistance plan on or after January 1, 2013 are taxable and must be treated as supplemental wage payments. This is true even if the education was provided to the employee in 2012, but the payment is not made until 2013.

- **Exclusion for certain health profession scholarships expires.** On December 31, 2012, the income exclusion for amounts paid for services under §117(c) for certain government health professions scholarship programs expires.

- **No new tax levy tables.** The IRS also has not issued Pub. 1494 for 2013, with the tables showing the amount of wages exempt from a federal tax levy. Therefore, tax levy notices sent by the IRS will continue to contain the 2012 Pub. 1494 amounts until a new edition is published.

- **WOTC expansion for veterans expires.** The Work Opportunity Tax Credit (WOTC) expansion for hiring certain qualified veterans is not available for those hired after December 31, 2012.

- **Some adoption assistance provisions expire.** Certain provisions under §137 related to employer-provided adoption assistance expire on December 31, 2012, resulting in lower income exclusion amounts and lower maximum income amounts for eligibility.

Congress waited until the very end to deal with the looming "fiscal cliff."  
[Register for the APA's webinar on January 3](#) to find out which of the Bush-era tax cuts have been extended and which are being allowed to expire on December 31.