

FAQs About Claiming the Payroll Exemption

PE1: How does the employer claim the payroll tax exemption for wages paid to qualified employees?

A-PE1: The payroll tax exemption is claimed on Form 941, Employer's QUARTERLY Federal Tax Return, beginning with the second quarter of 2010.

PE2: How does the employer claim the payroll tax exemption for wages paid to qualified employees during the period March 19 through March 31, 2010 (the first quarter of 2010)?

A-PE2: The payroll tax exemption for wages paid during this period will be claimed on the employer's Form 941 for the second quarter of 2010.

PE3: Can an employer claim the COBRA premium assistance credit and the payroll tax exemption for new hires on the same employment tax return?

A-PE3: Yes.

PE4: How does application of the payroll tax exemption to wages paid to a qualified employee affect the availability of the Work Opportunity Tax Credit with respect to that employee?

A-PE4: If an employer applies the payroll tax exemption to wages paid to a qualified employee, such wages paid to the employee during the one-year period beginning with the employee's hiring date may not be taken into account for purposes of the Work Opportunity Tax Credit. An employer that wishes to claim the Work Opportunity Tax Credit with respect to a qualified employee can elect out of the payroll tax exemption with respect to wages paid to that qualified employee.

PE5: What is the significance of Feb. 3, 2010, and March 19, 2010, under the HIRE Act?

A-PE5: An employee must begin employment after Feb. 3, 2010, and before Jan. 1, 2011 in order to be a qualified employee. The payroll tax exemption applies to wages paid to the qualified employee from March 19, 2010 (the day after the date of enactment) through December 31, 2010.

PE6: How does the social security wage base affect the payroll tax exemption?

A-PE6: The exemption is applicable to wages that would otherwise be subject to the employer's share of social security tax (i.e., wages up to the social security wage base) that are paid to qualified employees from March 19, 2010, through December 31, 2010. The employer is still liable for the employer share of Medicare tax on all wages and for withholding both the qualified employee's share of social security tax on wages up to the social security wage base (\$106,800 for 2010) and Medicare tax on all wages.

PE7: Is the payroll tax exemption based on when wages are earned by a qualified employee or when they are paid to a qualified employee?

A-PE7: The exemption is based on when wages are paid. Thus, only wages paid from March 19, 2010, through December 31, 2010, qualify for the exemption (regardless of when those wages are earned).

PE8: The HIRE Act allows qualified employers to elect out of the exemption. How is this done?

A-PE8: To elect out of the payroll tax exemption, the employer simply reports and pays the employer share of social security tax on wages paid to qualified employees, along with the employee share of social security tax, Medicare taxes, and withheld income tax. In other words, an employer does not need to specifically state that it is electing out of the exemption.

PE9: Does an employer have to choose to apply the payroll tax exemption with respect to all of its qualified employees?

A-PE9: No, the employer can choose to apply the exemption with respect to none, some, or all of its qualified employees. However, if the employer applies the exemption with respect to any wages paid to a particular qualified employee, the exemption must be applied to all wages paid to that employee from March 19, 2010, through December 31, 2010.

PE10: If an employer properly applies the payroll tax exemption on Form 941 for one or more prior quarters for a qualified employee who, as a certified member of a targeted group, also qualifies the employer for the work opportunity tax credit (WOTC), can the employer later elect out of the exemption, so it can instead claim the WOTC?

A-PE10: Yes, if an employer applied the payroll tax exemption for a qualified employee on Form 941 for one or more prior quarters, the employer can later elect out of the exemption by filing Form 941-X for each affected prior quarter to correct its original return and pay the employer's share of social security tax for each such prior quarter. The employer is then eligible to claim the WOTC on its income tax return.

PE11: If an employer chooses to claim the WOTC for a qualified employee, can the employer still claim the new hire retention credit for that qualified employee?

A-PE11: Yes, an employer may claim the retention credit for a qualified employee even if the employer has also claimed the WOTC for the same employee.

The new hire retention credit can be claimed for any qualified employee, as defined for purposes of the payroll tax exemption, once the employee is employed for 52 consecutive weeks, so long as the employee's wages (as defined for income tax withholding purposes) for the last 26 weeks of employment equal at least 80% of the employee's wages for the first 26 weeks of employment.

PE12: How will employers claim the payroll tax exemption for wages paid to qualified employees from March 19, 2010, through March 31, 2010?

A-PE12: The payroll tax exemption that would be applicable to wages paid during the first quarter of 2010 cannot be applied on the first quarter Form 941. Instead, the amount by which the employer's social security tax would have been reduced as a result of applying the exemption to wages paid during the first quarter is treated as a payment for the second quarter. The credit for this payment may be claimed only on the second quarter Form 941 (lines 12c-12e) and may only be claimed with respect to wages paid to qualified employees from March 19, 2010 (the day after the date of enactment), through March 31, 2010. A seasonal employer that does not otherwise have to file Form 941 for the second quarter must file Form 941 for that quarter in order to claim credit for the amount of the exemption that would have applied to wages paid during the first quarter. The amount of the credit claimed on Form 941 for the second quarter will be refunded to the employer or may be applied against a liability for a later quarter.

PE13: How will the IRS treat the credit claimed for wages paid in the first quarter?

A-PE13: The IRS will treat the credit as a deposit made on the first day of the second quarter for quarterly payroll tax return filers.

PE14: What line on the revised Form 941 reflects qualified employees who begin employment in late March but are not paid until April? What line on Form 941 would reflect qualified employees paid wages and tips covered by the payroll tax exemption in March?

A-PE14: If a qualified employee begins employment in late March, but the employer does not pay the employee until April, the employer will include the employee in the number reported on both lines 6a and 6b of the second quarter Form 941 and will include wages paid to the qualified employee in the second quarter on line 6c. If a qualified employee receives wages during the period of March 19 through March 31, the employer will include the qualified employee on line 12c of the second quarter Form 941 and will include the wages paid in such period on line 12d.

PE15: If an employer does not apply the payroll tax exemption with respect to a qualified employee, is the employee still counted on lines 6a and 6b (or line 12c for 1st quarter) as a Qualified Employee?

A-PE15: The employer reports on lines 6a and 6b (or line 12c for 1st quarter) only qualified employees with respect to whom the employer is applying the payroll tax exemption. Similarly, the employer reports only wages paid to qualified employees to whom the exemption is applied on line 6c (or line 12d for 1st quarter).

PE16: Is the number reported on line 6b of the Form 941 cumulative for all qualifying employees?

A-PE16: Yes, line 6b is cumulative for qualified employees with respect to whose wages the employer is applying the payroll tax exemption in that quarter. For example, if an employer hires 30 qualified employees in March, 30 in April, 30 in May, and 30 in June and applies the payroll tax exemption with respect to wages paid to all of the qualified employees in the second quarter, Line 6b would show 120 employees on the second quarter return.

PE17: Must employers apply the payroll tax exemption on the return for the quarter they paid the related wages, or can they apply it on a return for a later or earlier quarter?

A-PE17: Employers must apply the exemption on the return for the quarter in which they paid the related wages.

PE18: If the Form 941 liability is below \$100,000 solely due to application of the payroll tax exemption, does the employer still need to make the deposit the next day?

A-PE18: No, if application of the payroll tax exemption to wages paid to qualified employees results in the liability being below \$100,000, the employer will not have a next-day deposit requirement. Instead, the employer will deposit based on its regular deposit schedule.

PE19: How will the employer report the payroll tax exemption on Schedule B? Does an employer reduce the liability reported and its deposits in the second, third, and fourth quarters of 2010 to account for the payroll tax exemption?

A-PE19: The employer will not separately report the payroll tax exemption or the first quarter credit on Schedule B. An employer's report of its liability for the second, third and fourth quarters of 2010 on Schedule B will reflect the reduction in liability due to application of the payroll tax exemption to wages paid to qualified employees during those quarters. Since the payroll tax exemption reduces an employer's liability on wages paid to qualified employees, the employer is not required to deposit the employer's 6.2 percent share of social security tax on such wages. In addition, since the payroll tax exemption does not apply to the first quarter and the first quarter credit must be claimed on the second quarter return, an employer may reduce its deposits for the second quarter by the amount of the first quarter credit.

PE20: When will updated forms be available (e.g., Forms 941, 943, 944, 941-X)?

A-PE20: The IRS has revised the Form 941 for the second quarter of 2010 and a draft of the revised form is available on IRS.gov. The IRS is in the process of updating Forms 943, 944 and 941-X.

PE21: When will the updated Form 94X Schema be available?

A-PE21: The IRS development of the 94X Schema is pending the finalized Form 941. The IRS anticipates it will be available in May.

PE22: Will the IRS revise Form 941 again in the third and fourth quarters to remove lines 12 (c) and 12(d) again in the third

and fourth quarters?

A-PE22: The IRS will not revise Form 941 for the third and fourth quarters of 2010. Employers will be directed by the form and the instructions to leave those lines blank on the returns they file for the 3rd and 4th quarters.

PE23: Since there will be changes to the electronic filing schemas for employment tax returns such as the Form 941, will electronic filers need to recertify for all applications with the IRS?

A-PE23: No.

PE24: How will the payroll tax exemption affect the breakout amounts on EFTPS?

A-PE24: There will be no changes to the EFTPS system as a result of the payroll tax exemption. When an employer makes EFTPS deposits, the employer should continue to enter amounts of Medicare tax, social security tax, and income tax withholding, taking into account the reduction in liability due to the payroll tax exemption and, for the second quarter, the credit for first quarter amounts (see Q&A-[u]).

PE25: Will employers have to indicate on the Form W-2 the qualified employees whose wages are exempt from the employers share of social security tax and/or separately report wages exempt from the employers share of social security tax?

A-PE25: Yes, new Code CC has been created for box 12 of Form W-2 for employers to identify qualified employees and report the amount of wages and tips covered by the payroll tax exemption. In addition, new box 12b has been created on Form W-3 to report the aggregate of Code CC.