

1099 LETTER

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SPECIAL POINTS OF INTEREST:

“Employers are required to report to their employees on Form W-2 the cost of employer-provided health insurance.”

REPEAL OF NEW INFORMATION REPORTING REQUIREMENTS

Taxpayers got some good news in April 2011 when Congress passed, and President Obama signed, legislation to repeal expanded information reporting requirements. The Comprehensive 1099 Taxpayer Protection and Repayment of Exchange Subsidy Overpayments Act of 2011 (P.L. 112-9) repealed expanded business information reporting requirements previously scheduled to take affect for payments made after December 31, 2011 and also repealed rental property expense reporting which was effective for payments made after December 31, 2010.

The two (now repealed) information reporting requirements were enacted by Congress in 2010. Both were intended to boost tax revenues.

The Patient Protection and Affordable Care Act (“PPACA”) generally required all businesses, charities and state and local governments to file an information return (Form 1099) when they made annual purchases aggregating \$600 or more to a single vendor, other than a tax-exempt vendor, for payments made after December 31, 2011. The PPACA also repealed the longstanding reporting exception for payments to a corpora-

tion. The IRS was planning to issue regulations on the expanded business information reporting requirements but repeal of them makes the regulations unnecessary.



The Small Business Jobs Act of 2010 required information reporting by landlords on certain rental property expense payments of \$600 or more in conjunction with their rental properties made after December 31, 2010. The types of expenses contemplated by the 2010 Small Business Jobs Act were, for example, payments to craftsmen, such as electricians and roofers. Payments for professional services, such as to accountants, also would have been covered by the 2010 Small Business Act. Some landlords, however, were exempt from reporting. They included, but were not limited to, landlords who received only a nominal amount of rental income. The IRS also was planning to issue

regulations but repeal of the rental property expense reporting requirement makes the regulations unnecessary.

The 1099 Comprehensive Taxpayer Protection Act did not repeal some other new information reporting requirements. In particular, taxpayers need to take notice of a new information reporting requirement for health insurance benefits that is now in effect after having withstood campaigns to have the requirement repealed. The PPACA of 2010 requires employers to report to their employees on Form W-2 the cost of employer-provided health insurance. This reporting requirement is optional for all employers in 2011, optional for small-employers only for 2012 and mandatory for all employers starting in 2013.



IRS VOLUNTARY CLASSIFICATION SETTLEMENT PROGRAM

The IRS recently announced a new voluntary settlement program for employers that have misclassified their employees as independent contractors or other non-employees. The Voluntary Classification Settlement Program (“VCSP”) offers employers a significantly reduced penalty framework, as well as audit protection for previous years, in exchange for agreeing to prospectively treat the misclassified workers as employees. VCSP is being described by employment tax experts as an extremely generous deal for businesses to set things straight and reclassify workers as employees in return for very limited federal employment tax liability on the past non-employee treatment.

The IRS has opened the VCSP to employers currently treating their workers, or a class or group of workers, as independent

contractors or other non-employees and that want to prospectively treat the workers as employees. The IRS requires that the employer consistently treated the workers as non-employees, and filed all required information returns such as Forms 1099 for the workers for the three preceding calendar years. Under VCSP, an employer qualifies whether or not the misclassification was the result of a close call in judgment or a more clear cut misinterpretation of the law.

In exchange for agreeing to prospectively treat the workers as employees, employers will pay only 10 percent of the employment tax liability that may have been due on compensation paid to the workers in the most recent year, as determined under the already reduced rates under Internal Revenue Code Sec. 3509 of

1.5 percent of wages and 20 percent of employee social security taxes. Employers also will not pay any interest and penalties on the liability, and will not be subject to an employment tax audit with respect to the classification of the workers for prior years.

The IRS also requires participating employers to agree to extend the period of limitations on assessment of employment taxes for three years for the first, second and third calendar years beginning after the date on which the employer agrees to begin treating the workers as employees. In most cases, this is an inconsequential concession.

The IRS announced the VCSP in September 2011. The IRS has not given the VCSP an end-date as of this time.



“Employers who are accepted into the VCSP will not pay any interest and penalties and will not be subject to an employment tax audit with respect to the classification of the workers for prior years.”

CALIFORNIA’S NEW PENALTIES FOR MISCLASSIFYING EMPLOYEES AS INDEPENDENT CONTRACTORS

Recent legislation was signed into law by the Governor that imposes dramatic penalties on employers found to have engaged in “willful misclassification” of workers as independent contractors. This new law takes effect on January 1, 2012.

In summary, the new law:

- Prohibits the willful misclassification of workers as independent

contractors to avoid properly classifying them as employees.

- Prohibits charging misclassified workers any fees or making deductions from their compensation where those acts would have violated the law if the individuals had not been mischaracterized.

- Subjects violators to civil penalties of \$5,000 to \$15,000 per violation, in addition to any other penalties or fines permitted by law.
- Subjects violators engaged in a pattern of violations to a civil penalty of \$10,000 to \$25,000 for each violation.

FORM W-2 AND W-3

The IRS requires all compensation to employees including Christmas bonuses, year-end bonuses, auto allowances, and the personal use of company owned vehicles be reported on Form W-2 subject to both FICA and Medicare taxes.

Personal Use of Company Owned Vehicle

If you have employees who use company owned vehicles, we recommend that a written policy regarding the personal use of the automobiles be implemented. This written policy should document the valuation method to be used and establish procedures for required records to be maintained by the employee and submitted to the employer. If you have any questions about how to calculate the personal use of vehicles or would like more information on company

automobile policies, please call us.

Expense Reimbursements

Reimbursements to employees of business expenses are considered taxable income and should be reported on Form W-2 unless the reimbursements were made under an "Accountable Plan." An Accountable Plan requires that 1) reimbursements, advances, or allowances are made only for business expenses incurred by the employee in connection with his performance of services as an employee; 2) employees must be required to substantiate to the employer the expenses covered by the arrangement; and 3) employees must be required to return any excess reimbursements. Thus, for example, a car allowance with no substantiation as to the amount of expenses incurred for business purposes would be fully taxable to the employee and should be

reported on Form W-2. Please call us if you have any questions about Accountable Plans.

More than 2% Shareholder/Employee of an S Corporation

IRS Notice 2008-1 states that health insurance premiums paid on behalf of a "more than 2% shareholder" of an S Corporation must also be reported as taxable wages on Form W-2 (Similarly, partnership payments of health insurance premiums for a partner must be reported as guaranteed payments on the Schedule K-1). Relief is provided, however, since an S Corporation shareholder can deduct 100% of these premiums on his or her individual tax returns provided the amount was included in wages.

ELECTRONIC TAX PAYMENTS

Federal Electronic Tax Payment System ("EFTPS")

Any business taxpayer can use EFTPS although some business taxpayers are required to use EFTPS because they have met certain criteria. Specifically, if your total deposits of designated federal taxes (including employment taxes, income taxes, Railroad Retirement taxes, Social Security taxes, and various other types of non-payroll withholding) during a calendar year exceed \$200,000; you are required to use EFTPS beginning in the second succeeding calendar year. Once you are required to

use EFTPS, you will continue to be required in subsequent years, even if your annual tax deposits fall below \$200,000.

California Electronic Funds Transfer ("EFT")

California's EFT deposit requirements differ from the Federal requirements. Each year, your account is reviewed to determine if you meet the requirements for mandatory EFT filing. If your average (per payment) payroll deposit for SDI and PIT is \$20,000 or more for the prior State Fiscal Year (July 1 to June 30), you are

required to pay all SDI and PIT deposits by EFT during the next calendar year, regardless of the dollar amount. Corporations must use EFT if any quarterly estimated income tax payment or extension payment exceeds \$20,000 or if their total tax liability exceeds \$80,000 for any income year. Once this threshold is met all future payments must be made via EFT.

"Health insurance premiums paid on behalf of a "more than 2% shareholder" of an S Corporation must also be reported as taxable wages on Form W-2."

ELECTRONIC TAX PAYMENTS (CONTINUED)

You will be subject to a 10% penalty if you meet the requirements to use EFTPS or EFT and fail to do so.

California Web Pay for Individuals

California law requires individual taxpayers who make a payment of more than \$20,000, or who have a tax liability of more than \$80,000

in a year beginning on or after January 1, 2009, to make all future payments electronically. Failure to comply with the mandatory e-pay requirement results in a penalty equal to 1% of the amount paid. The FTB began enforcing the mandatory e-pay requirements and the subsequent penalty for failure to comply as of January 1, 2011.



FOREIGN BANK ACCOUNT REPORTING

United States persons who have a financial interest in or signature authority or other authority over any financial account in a foreign country, if the aggregate value of these accounts exceeds \$10,000 at any time during the calendar year, must report these accounts to the IRS.

These disclosures are made on a special U.S. government form, TD F 90-22.1, Report of Foreign Bank and Financial Accounts ("FBAR") which must be filed separately from your tax return and is due on or before June 30th annually.

Taxpayers who do not disclose their

foreign accounts, if required, risk many penalties. Depending on the taxpayer's facts and circumstances, some of the penalties include, but are not limited to, penalties for failing to file certain returns, fraud penalties, and an accuracy-related penalty on underpayment of tax. The IRS can also seek criminal sanctions against a taxpayer.

HOUSEHOLD EMPLOYEE (NANNY TAX)

Taxpayers who hire people to perform domestic services may be responsible for paying certain employment taxes for their workers. If, during any calendar year, a taxpayer pays a household employee (e.g., babysitter, house cleaner, yard worker, cook or driver) \$1,700 or more, the taxpayer must pay social security and Medicare taxes ("FICA"). Further, the taxpayer must pay federal unemployment tax ("FUTA") for that employee if the taxpayer pays the employee cash

wages of \$1,000 in any calendar quarter of the current or previous year.

If the employer is to withhold income taxes, the worker must provide a completed Form W-4, "Employee's Withholding Allowance Certificate." The W-4 will show whether the employee is married or single, the number of exemptions he or she is claiming, and any additional amounts of tax to be withheld. The amount to be withheld is provided in IRS

Circular E, "Employer's Tax Guide." A Form W-2 must be filed for each employee who is paid FICA wages and each employee who has income taxes withheld from his or her wages.

Withheld income tax is reported and paid using Form 1040, Schedule H, which is due on April 15th. In addition, separate California payroll returns must be filed.

"Taxpayers who do not disclose their foreign accounts, if required, risk many penalties."

FORM 1099 FAQ'S AND MISCELLANEOUS DETAILS

Any person engaged in a trade or business generally must file an information return with respect to certain payments aggregating \$600 or more in the calendar year. This information is reported on the Form 1099 series to satisfy federal requirements. Please note that the IRS shares Form 1099 information with the state of California. Therefore if you file with the IRS, you do not file a copy of the same forms with the Franchise Tax Board.

Payments to be Reported

Payments for various types of **non-employee** compensation must be reported on Form 1099. This requirement generally includes payments for personal services, as well as rental, interest, and dividend payments. Payments of any nature to banks or corporations (except to corporations organized for medical, health care or legal services) need NOT be reported. Following is a list of **some** of the common types of payments, which must be reported:

- Rents of \$600 or more and royalties of \$10 or more;
- Commissions, fees, prizes and awards, etc., paid to non-employees if they total \$600 or more;
- Interest totaling \$10 or more paid or credited to any person's

account;

- Corporate dividends of \$10 or more;
- Patronage dividends, rebates, or refunds totaling \$10 or more;
- Payments for medical or health care services of \$600 or more in the aggregate;
- Payments for attorney fees and gross proceeds paid to attorneys.

Payments Not Requiring Information Returns

The following list details some common examples of payments, which need NOT be accompanied by the filing of 1099's:

- Payments of any type made to a bank or corporation (other than for medical, health care or legal services);
- Any otherwise reportable payments of less than \$600 in the aggregate;
- Payments of bills for merchandise;
- Wages and other employee compensation reported on Form W-2;
- Payments made by those not engaged in a trade or business;
- Rent payments to real estate agents;
- Payments by a partnership to a partner where they are reflected on

Schedule K-1 of the partnership tax return.

Filing Due Dates

Forms 1099 must be issued to recipients on or before **January 31, 2012**, while Form 1096 and the duplicate 1099's must be transmitted to the IRS on or before **February 28, 2012**.

Penalties

The penalties are relatively stiff for failure to file information returns. Federal law provides for up to a \$50 assessment for each failure to give an information return to a recipient, and another \$50 for failing to give an information return to the IRS. Failure to supply taxpayer identification numbers ("TIN's") on information returns is also subject to a \$50 penalty. In certain instances, other penalties may apply. The maximum penalty is \$250,000 per year (\$100,000 for small businesses).

Additionally, failure to file a Form 1099 could result in disallowance of the deduction during an audit.

In the event a TIN is unavailable, the IRS has developed Form W-9, Request for Taxpayer Identification Number, on which to request this information from the payee. If the payee refuses to provide the requested information, the payee is subject to Federal

penalties. Also, taxpayers who refuse to furnish their TIN are subject to backup withholding.



“Form 1099 must be issued to recipients on or before January 31, 2012.”

FORM 1099 FAQ'S AND MISCELLANEOUS DETAILS (CONTINUED)

Backup withholding requires that payers must generally withhold 28% of taxable interest, dividends, and certain other payments required to be reported on Form 1099-MISC if the recipient fails to furnish the payer

with his correct taxpayer identification number. The backup withholding rules will generally come into effect if the recipient fails to furnish his taxpayer identification number to the payer; or the IRS

notifies the payer that the taxpayer identification number furnished was incorrect.

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27441 Tourney Road, Suite 200
Valencia, California 91355
Main: (661) 287-6333
Fax: (661) 287-6336
www.hedmanpartners.com



2012 TAX REFERENCE GUIDE

2010/2011 TAX DATA SCHEDULE				FEDERAL TAX RATE SCHEDULE							
				2012 Taxable Income			2011 Taxable Income				
				Is	But Not			Is	But Not		
				Over	Over	Tax Rate	Over	Over	Tax Rate		
Standard Deductions											
Single	\$	5,950	\$ 5,800								
Married Filing Jointly, Surviving Spouse		11,900	11,600								
Married Filing Separately		5,950	5,800								
Head of Household		8,700	8,500								
Taxpayer Claimed as a Dependent		950	950								
Personal or Dependent Exemption (Social Security Number required)				3,800	3,700						
California SDI											
Annual Wage Limit	\$	95,585	\$ 93,316								
Rate		1.00%	1.20%								
Tax		955.85	1,119.79								
RETIREMENT PLAN LIMITATIONS											
				2012			2011				
Maximum 401(k) or 403(b) Deferral	\$	17,000	\$ 16,500								
Maximum Defined Contribution Plan Contribution		50,000	49,000								
Maximum Annual Benefit for Defined Benefit Plans		200,000	195,000								
Annual Compensation Limit for Computing Plan Benefits		250,000	245,000								
Annual Compensation Limit for the Definition of Highly Compensated Employee IRC Section 414(q)		115,000	110,000								
Compensation Minimum for SEP Plan		550	550								
Maximum Contribution for SIMPLE Plan		11,500	11,500								
Catch-up Contribution for 401(k) or 403(b) for taxpayers age 50 and older		5,500	5,500								
Catch-up Contribution for SIMPLE for taxpayers age 50 and older		2,500	2,500								
Key-Employee for Top Heavy Purposes:											
Officers earning over	\$	165,000	\$ 160,000								
A 5-percent Owner or 1-percent Owner Earning Over		150,000	150,000								
SOCIAL SECURITY AND MEDICARE TAXES											
								2012		2011	
Social Security Tax											
Maximum wage base								\$110,100	\$106,800		
Social Security Rate-employee								6.2%	6.2%		
Social Security Rate-self-employed								12.4%	10.4%		
Medicare Tax											
Maximum wage base								Unlimited	Unlimited		
Medicare Rate-employee								1.45%	1.45%		
Medicare Rate-self-employed								2.9%	2.9%		
IMPORTANT PHONE NUMBERS											
Internal Revenue Service										(800) 829-3676	
										www.irs.gov/formspubs/index.html	
Franchise Tax Board										(800) 338-0505	
										www.ftb.ca.gov/forms/index.html	
Employment Development Department										(888) 745-3886	
										www.edd.ca.gov/Forms/	
TRADITIONAL AND ROTH IRAs											
				2012							
Contribution Limit	\$	5,000									
Catch-up Contribution age 50 and older		1,000									
IRA Deduction Phaseout for Active Participants											
Single		\$58,000-68,000									
Married Filing Jointly		92,000-112,000									
Married Filing Separately		0-10,000									
IRA Deduction Phaseout for Special Contributions											
Single		\$173,000-183,000									
Roth IRA Contribution Phaseout											
Single		\$110,000-125,000									
Married Filing Jointly		173,000-183,000									
Married Filing Separately		0-10,000									