



Decker, Farrell & McCoy, LLP
 CERTIFIED PUBLIC ACCOUNTANTS
Litigation Specialists & Business Appraisers

Scott M. Decker, CPA/ABV/CVA
 Michael J. Farrell, CPA
 Leatha L. McCoy, CPA

H. Perry Dahm, CPA/CFE
 Kathy I. Jonas, CPA/CFE
 Allen R. Reyburn, CPA/PFS
 Erica V. Tarazon, CPA
 Seema Natha, Staff Accountant

Lynne Wysinger, Firm Administrator
 Charity Collins, Litigation Assistant
 Amaris Collins, Administrative Assistant
 Alli Johnson, Administrative Assistant

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Dear Client:

The new year will bring about the following changes in the law regarding payroll:

	2020		2019	
	WAGE BASE	TAX RATE	WAGE BASE	TAX RATE
SOCIAL SECURITY	\$137,700	6.2% & 6.2% Employer & Employee	\$132,900	6.2% & 6.2% Employer & Employee
SOCIAL SECURITY	\$137,700	12.4% Self-employed	\$132,900	12.4% Self-employed
- Individuals with earned income Over \$200,000 the rate will be 2.35% - Married couples filing jointly with earned income Over \$250,000 the rate will be 2.35%				
MEDICARE	No Limit	1.45% Employer & Employee	No Limit	1.45% Employer & Employee
MEDICARE	No Limit	2.90% ** Self-employed	No Limit	2.90% Self-employed
FUTA	\$7,000	0.6% Employer Only	\$7,000	0.6% Employer Only
SUI	\$7,000	Varies Employer Only	\$7,000	Varies Employer Only
SDI	\$122,909	1% Employee Only	\$118,371	1% Employee Only
Rates do not include Employment Training Fund contribution of 0.10%. Check with the EDD to find out if this applies to you.				

- As of January 2014, individuals with earned income of more than \$200,000 (\$250,000 for married couples filing jointly, \$125,000 for married couples filing separately, and \$200,000 for filing single) pay an additional 0.9% in Medicare taxes. For withholding tax purposes, covered wages in excess of \$200,000 will be taxed at a rate of 2.35% (1.45% + 0.9%), regardless of filing status. The Additional Medicare Tax is not matched by employers.
- Changes may be made in late January 2020 for the effects of the tax law changes made late in 2019. Be on the watch for the updated 2020 tables that will be released for Federal and California State withholdings. Be sure to use the updated tables once released.
- Effective January 1, 2020, the state minimum wage rate increases to \$12.00 per hour for employers with 25 or less employees. For employers with 26 or more employees the state minimum wage rate increases to \$13.00 per hour. Below is a schedule for wage rate increases 2019-2023:

Schedule for California Minimum Wage rate 2020-2023.

Date	Minimum Wage for Employers with 25 Employees or Less	Minimum Wage for Employers with 26 Employees or More
January 1, 2020	\$12.00/hour	\$13.00/hour
January 1, 2021	\$13.00/hour	\$14.00/hour
January 1, 2022	\$14.00/hour	\$15.00/hour
January 1, 2023	\$15.00/hour	

- The business mileage rate remains unchanged at 58 cents per mile driven. Be on the watch for any updates that may be issued in the coming weeks and adjust this rate accordingly.
- The Federal Unemployment Tax Act (FUTA) tax rate is normally 0.6% of taxable wages paid, or \$42 per employee per year. However, employers in certain states (which includes California) may pay an increased tax rate. When this “credit reduction” applies, the FUTA tax typically increased by 0.3%, or \$21 per worker, payable in January of the following calendar year with the Internal Revenue Service (IRS) Form 940. This credit is further reduced annually by 0.3% until loans are repaid.
- The U.S. Department of Labor identified the states that are subject to the FUTA Credit Reduction for 2019 on November 12, 2019. Per the U.S. Department of Labor, California repaid its unemployment account loan balance to the federal government, thus, there will be no FUTA credit reduction for the 2019 tax year. This means that the FUTA rate will remain 0.6% and will not increase to 2.7%.

- The maximum contribution to a 401(k) Plan is increased from \$19,000 to \$19,500 for 2020. For employees over age 50, there is an additional catch-up provision of which increased from \$6,000 to \$6,500. Therefore, the maximum contribution is \$26,000 for those over age 50.

WHEN TO MAKE DEPOSITS

FEDERAL: You may make a deposit with Form 941 or 944 instead of depositing if you accumulate less than a \$2,500 tax liability either during the current or prior quarter, and you don't incur a \$100,000 next-day deposit obligation during the current quarter and you pay in full with a timely filed return. If you did not receive notification as to which type of deposit rule to use, you must determine your own deposit status by looking at the total tax reported on Form 941 for the four quarters ended June 30, 2018 (i.e., July 1, 2017 through June 30, 2018). If your total tax reported on Form 941 for this period was \$50,000 or less, you are a monthly depositor. Additionally, you are a monthly schedule depositor for the first calendar year of your new business. If the total tax was \$50,000 or more, you are a semi-weekly depositor.

- **Monthly Depositor Rule:** Employment taxes and taxes withheld during a calendar month must be deposited by the 15th of the following month.
- **Semi-weekly Depositor Rule:** If your payroll falls on a Wednesday, Thursday or Friday, deposit employment taxes and withholding the following Wednesday. If your payroll falls on a Saturday, Sunday, Monday or Tuesday, the payroll tax deposit is due by the following Friday.

If a deposit is required to be made on a day that is not a banking day, the deposit is considered timely if it is made by the close of the next banking day. If you accumulate a tax liability of \$100,000 or more on any day during a deposit period, you must deposit the tax by the next banking day, whether you are a monthly or semiweekly schedule depositor.

FUTA: If the FUTA cumulative liability exceeds \$500 for any of the calendar quarters, deposit must be made by using EFTPS, by the end of the month following the close of the quarter. If the liability is \$500 or less, no deposit is required; however, the liability must be added to the following quarter to determine the deposit requirement for that quarter.

ELECTRONIC FEDERAL TAX PAYMENTS SYSTEM (EFTPS)

You must use EFT to make all federal tax deposits, generally the payments are made using the EFTPS website. To register or find out more information about EFTPS, visit www.eftps.gov or call the customer service line at 1-800-555-4477.

The IRS announced that you are required to use the EFTPS and fail to do so, the business could be subject to a 15% penalty.

STATE PAYMENTS: Generally, a state payroll tax deposit should be made whenever a federal deposit is required. The current California Personal Income Tax (PIT) deposit threshold is \$350. Employers who meet federal deposit requirements and also meet the state PIT threshold

of \$350 must remit both State Disability Insurance and PIT withholdings to EDD on the Payroll Tax Deposit coupon (DE 88).

- All California employers are required to electronically submit the following returns and payroll tax deposits to the Employment Development Department (EDD)
- DE-9 Quarterly Contribution Return and Report of Wages
- DE-9C Quarterly Contribution Return and Report of Wages (Continuation)
- DE-3BHW Employer of Household Workers Quarterly Report of Wages and Withholdings
- DE 3HW Employer of Household Workers Annual Payroll Tax Return
- DE 3D – Quarterly Distribution Return
- DE 88 Payroll Tax Deposit

Penalties for not complying with E-File and E-pay mandate:

Type	Forms	Penalty
Tax Returns	DE 9 – <i>Quarterly Contribution Return and Report of Wages</i> DE 3HW – <i>Employer of Household Worker(s) Annual Payroll Tax Return</i> DE 3D – <i>Quarterly Contribution Return</i>	\$50 per return
Wage Reports	DE 9C – <i>Quarterly Contribution Return and Report of Wages (Continuation)</i> DE 3BHW – <i>Employer of Household Worker(s) Quarterly Report of Wages and Withholdings</i>	\$20 per wage item
Payments	DE 88 – <i>Payroll Tax Deposit</i>	15% of amount due

For more information, visit E-file and E-pay Mandate for Employers.

Deposits made through e-Services for Business do not require a paper DE 88. Visit e-Services for Business to enroll and manage your employer payroll tax account(s) online.

- Only employers who have an approved e-file and e-pay mandate waiver can mail tax payments with a DE 88 to the EDD.
- Employment Training Tax (ETT) rate for 2020 is 0.1%. The Unemployment Insurance (UI) rate and ETT taxable wage limit remains at \$7,000 per employee per calendar year.

- State Disability Insurance (SDI) rate for 2020 will be 1.0% on maximum subject wages of \$122,909. Therefore, the maximum SDI for an employee for 2019 is \$1,229.09.
- If PIT, SDI, UI or ETT were overpaid, adjust the fund(s) on your next DE 88, Payroll Tax Deposit Coupon, or EFT transaction. Do not show credits on the DE 88 deposit coupon or on an EFT transaction.
- If PIT, SDI, UI or ETT were underpaid, pay delinquent fund(s) plus penalty and interest on a DE 88, or do two EFT transactions, one to pay fund(s) due and one to pay penalty and interest.
- For refunds of PIT, SDI, UI or ETT, if it is not feasible to offset the overpayment against your next tax deposit, you can request a refund on Form DE 678.
- There is an automated 24-hour telephone line that you can call for an employer's current year UI rate. Tax rates and benefit information: (916) 653-7795. This number will also give you SDI rates and prior-year rates. These updated rates are generally mailed to the employer in a Statement of Charges to Reserve Account – DE 428T, which lists the itemized list of Unemployment Insurance (UI) benefit charges to the UI reserve account, which covers a one-year period beginning July 1 and ending June 30. You may also obtain this rate online at www.edd.ca.gov/e-Services_for_Business, you will need your Employer account number.

NEW HIRE REPORTING

Businesses must report to the EDD, individual independent contractors subject to Form 1099 filing requirements within 20 days of making payments or entering into a contract for \$600 or more during the calendar year. If you file a Form 1099-Misc for tax year 2019. See Form 1099 information below for tax year 2020 changes that have a 1099-MISC and a new Form 1099-NEC Nonemployee Compensation. You must also report the individual contractor on Form DE 542, Report of Independent Contractor. However, a business is not required to file Form 542 for an independent contractor who is a corporation, partnership, limited liability company or limited liability partnership. Failure to report new hires within 20 days may be subject to a \$24 penalty. If the failure to report is an intentional agreement between the service-recipient and service-provider to not supply the required information or to supply a false or incomplete report, a penalty of \$490 may be charged.

QUITTING BUSINESS

Employers quitting business are required to file the payment and report of wages electronically first, and DE 88, DE 9 and DE 9C with the State of California within 10 days of quitting business regardless of the usual reporting due date.

FORM 1099

We suggest all businesses send all vendors a Form W9 to ensure the collection of needed information to complete 1099s correctly. There are updated filing requirements for Form 1099, whether you are preparing the information return in-house or are using our services.

For 1099s to be issued for the tax year 2019, you must file Form 1099-MISC for each person from whom you have withheld any federal income tax (report in box 4) under the backup withholding rules regardless of the amount of the payment. Also, all payments of interest, dividends and royalties must be reported if they are \$10.00 or more. Under the Protecting Americans from Tax Hikes Act of 2015 (PATH Acts), Forms 1099-MISC (and related Form 1096) containing Non-Employee Compensation (NEC) in box 7 must be filed with the IRS by no later than January 31, 2020.

The penalty for failure to file Form 1099 is \$100 per information return

Beginning with tax year 2020, there is a change to 1099 reporting of Non-Employee Compensation (NEC). A new Form **1099-NEC, Nonemployee Compensation (NEC)** is to be used to report nonemployee compensation, which has an accelerated due date of January 31, 2021.

See basic guidelines below for tax year 2020 reporting.

File Form 1099-MISC, Miscellaneous Income, for each person in the course of your business to whom you have paid the following during the year:

- At least \$10 in royalties or broker payments in lieu of dividends or tax-exempt interest.
- At least \$600 in:
 1. Rents (box 1);
 2. Prizes and awards (box 3);
 3. Other income payments (box 3);
 4. Generally, the cash paid from a notional principal contract to an individual, partnership, or estate (box 3);
 5. Any fishing boat proceeds (box 5);
 6. Medical and health care payments (box 6);
 7. Crop insurance proceeds (box 9);
 8. Payments to an attorney (box 10)
 9. Section 409A deferrals (box 12); or
 10. Nonqualified deferred compensation (box 14).

File Form 1099-NEC, Nonemployee Compensation (NEC), for each person in the course of your business to whom you have paid the following during the year:

- At least \$600 in:

1. Services performed by someone who is not your employee (including parts and materials) (box 1);
2. Cash payments for fish (or other aquatic life) you purchase from anyone engaged in the trade or business of catching fish (box 1); or
3. Payments to an attorney (box 1).

You must also file Form 1099-NEC for each person from whom you have withheld any federal income tax (report in box 4) under the backup withholding rules regardless of the amount of the payment.

W-2 AND W-3 REQUIREMENTS

Forms W-2 and W-3 must be filed with the Social Security Administration by January 31, 2020.

W-4 REQUIREMENTS

Employers are required to have on file a copy of Form W-4 for each employee. A valid Form W-4 remains in effect until the employee gives you a new one or unless the employee claims to be exempt from income tax withholding.

Note, that an updated and redesigned W-4 has been released for 2020. All new hire employees must use this form. Similarly, existing employees who wish to adjust their withholdings will also need to use this new form.

Effective April 14, 2005, employers no longer have to routinely send copies of Forms W-4 claiming more than 10 allowances and certain “exempt” Forms W-4 to the IRS. However, Forms W-4 are still subject to review by the IRS.

Due to the federal change, an employer must submit a copy of Form W-4 or DE 4 to the Franchise Tax Board if one of the following occurs:

- The employee claims 10 or more withholdings.
- The employee claims an exemption from state of federal income tax withholding and the employee’s usual weekly wage will exceed \$200.
- The employee makes major changes to Form W-4 or DE 4, such as crossing out words or writing more than is asked.
- The employee admits that Form W-4 or De 4 is false.

In any of these cases, a copy should be faxed to the FTB at (916) 843-1094 or it can be mailed to:

Franchise Tax Board
W-4 Unit MS F-180
P.O. Box 2952

FRINGE BENEFITS

- **Personal Use of Company Autos:** The value of personal use of company cars, or any other taxable cash or non-cash fringe benefit, must be included on Form W-2. In general, most fringe benefits are taxable and subject to income and employment taxes.
- **Cost of Group-Term Life Insurance:** The cost of group-term life insurance you provided for your employee needs to be included on the employee's W-2 to the extent that it exceeds \$50,000.00 of term coverage or 100% of any other type of life insurance coverage. The value is based on an IRS published table that assigns a value for each \$1,000 of excess coverage per month based on the employee's age.
- **Health and Accident Insurance Premiums Paid by an S Corporation:** When an S corporation pays health and accident insurance premiums on behalf of 2% shareholder/employees, the IRS rules specify two tax treatments:

Situation 1: If the premiums are paid under a plan that does not discriminate:

1. The premiums are treated as exempt for FICA and FUTA,
2. The premiums are included in the shareholder/employee's federal gross income, and
3. The premiums are reported on Form W-2 in box 1 and noted in Box 14.

Situation 2: If the premiums are not paid under such a plan:

1. The premiums are treated like normal compensation and as such are subject to FICA and FUTA,
2. The premiums are included in the shareholder/employee's gross income, and
3. The premiums are reported on Form W-2 in boxes 1, 3 and 5 and noted in Box 14.

3 COMMON W-2 ERRORS ON S CORPORATION SHAREHOLDERS

Although there are many ways shareholders can run afoul of IRS rules, the 3 most common errors that impact W-2 reporting are:

1. Failing to pay a reasonable wage to shareholder-employees on Form W-2,
2. Not reporting the personal use of a company owned vehicle as compensation on the shareholder's W-2, and,

3. Misreporting shareholder health insurance in Box 1 of Form W-2.

Please contact our office for assistance with these items.

STATEWIDE SALES AND USE TAX RATE

The minimum combined state, county, and local sale and use tax rate is 7.25 percent. Remember that if you are engaged in business in a special tax district, your sales are subject to additional district taxes. New tax rate charts are available by calling 1-800-400-7115, or you can download copies from the California Department of Tax and Fee Administration website <https://www.cdtfa.ca.gov/taxes-and-fees/sales-use-tax-rates.htm>.

OVERTIME LAWS

Generally, overtime must be paid at a rate of one and one-half times the employee’s regular rate of pay for more than 8 hours worked *per* day or more than 40 hours in a week. Double time should be paid for all hours worked in excess of 12 hours in any workday. However, there are certain exemptions from the overtime rules. One is the adoption of an alternative workweek schedule. If a majority of the employees agree to the adoption of the alternative workweek schedule, no overtime is required for a regular schedule of not more 10 hours per workday within a 40-hour workweek.

INDEPENDENT CONTRACTOR REPORTING

In September 2019, Governor Newsome signed Assembly Bill (AB) 5 into law. The new law addresses the “employment status” of workers when they are claimed to be an independent contractor and not an employee. AB 5 requires the application of the application of the “ABC test”. We provide a brief outline below, however, there are many exemptions and rules to this new law, thus we recommend employers navigate this with the assistance of their payroll service providers, tax professional or attorney.

Under the ABC test, a worker is considered an employee and not an independent contractor, unless the hiring entity satisfies all three of the following conditions:

- The worker is free from the control and direction of the hiring entity in connection with the performance of the work, both under the contract for the performance of the work and in fact;
- The worker performs work that is outside the usual course of the hiring entity’s business, and
- The worker is customarily engaged in an independently established trade, occupation, or business of the same nature as that of the work performed.

AB 5 changes the worker classification rules for California purposes, but the federal government will continue to apply the traditional right to control standards. This means that employers may choose to classify workers as employees for California purposes, and independent contractors for federal purposes.

This would result in employers not being required to pay FUTA for those workers, but employers must pay California SUTA and withhold SDI and California income taxes. In addition, the employer must cover workers' compensation, meet minimum wage and hour laws, and provide at least three days of sick pay benefits. Because they are independent contractors for federal purposes, these workers do not qualify for the employers' health or retirement benefits.

Employers will be required to submit two different forms to their workers. For federal purposes, the compensation paid will be reported on Form 1099. For California purposes, the compensation will be reported as state wages on a W-2 (\$0 will be reported for federal wages, Social Security and Medicare wages).

California law required business owners and landlords, to report individuals who perform services to the state's Independent Contractor Registry. The rules are somewhat complicated, and there are penalties for failing to comply.

You must report individuals who are independent contractors and are subject to federal Form 1099 reporting requirements who are service providers for your business and who you pay or will pay \$600.

You are only required to report independent contractors that are individuals. You do not have to report payments made to corporations, partnerships, limited liability companies or limited liability partnerships.

You must report service providers within 20 days of the earlier of:

- Making payment(s) of \$600 or more, or
- Entering into a contract for \$600 or more in any calendar year.

You report the individual's name, address and taxpayer ID number to the EDD using Form DE 542, Report of Independent Contractors. If you do not report the independent contractor as required, the EDD may assess you a penalty of \$24 per failure. If you and the independent contractor agree not to report the payments in an effort to circumvent the requirement, the penalty is \$490.

IMPORTANT NOTICE: Those clients for whom we do W-2s and 1099s must have all information to us no later than January 17, 2020, in order for us to have them finished by the January 31, 2020 deadline!

All of us at **DECKER, FARRELL & MCCOY, LLP** are ready to help with all your financial planning and reporting needs. If you have questions or comments regarding the information in this newsletter, or if we can assist you with any other financial matters, please do not hesitate to give us a call.

Thank you for the opportunity to be of service. Please accept our best wishes for a happy and prosperous 2020!

Sincerely,

DECKER, FARRELL & MCCOY, LLP