



IN THE BUSINESS OF YOUR SUCCESSSM



LEGISLATIVE UPDATE

Eye on Washington

IRS “REAL-TIME TAX SYSTEM” MAY DRAMATICALLY CHANGE EMPLOYER REPORTING

Over the past sixteen months, Internal Revenue Service (IRS) Commissioner Douglas Shulman and other senior IRS officials have proposed an ambitious plan for technology modernization that could accelerate employer deadlines for Forms W-2 and 1099 reporting, and make other changes to employers’ reporting requirements.

Real-Time Tax System

The “Real-Time Tax System” (RTTS) outlined in early 2011 is founded on the premise that all third-party information returns, such as Forms W-2 and 1099, would be electronically available to the IRS *during* the income tax season rather than after. The RTTS would be able to identify discrepancies and permit individuals filing income tax returns to address problems at the time of filing.

The RTTS would also help the IRS to prevent fraudulent tax refunds, which is a growing concern. The normal deadline for employers to electronically file Forms W-2 data with the Social Security Administration (SSA) is March 31 (February 28th if filed in paper format). However, many large employers already receive annual requests from the IRS to provide an early electronic copy of the W-2 data in mid-January. This voluntary program to obtain early W-2 data has helped the IRS to prevent substantial tax refund fraud. According to IRS Deputy Commissioner Steven Miller, “Overall, IRS identified and prevented the issuance of over \$14 billion in fraudulent refunds in 2011.”¹

Electronic Delivery

Realization of the RTTS seems to be a question of logistics: How might employers most efficiently deliver W-2s and 1099s to the IRS in electronic format, prior to the start of the income tax filing season? This is a difficult issue, given that the filing season begins around January 20.

Although the goals of the RTTS are laudable and worthwhile, earlier deadlines for W-2 and 1099 reporting may create new problems for both the IRS and employers. While an employee’s cash wages for a year are generally known as of December 31, businesses gather and report as many as 50 different elements of taxable compensation, many of which are administered by third parties. Some of these elements cannot be determined by December 31. Reportable amounts for disability and sick pay administered by third parties, for example, is not required to be provided to employers for inclusion on the W-2 until January 15th. Other compensation, such as taxable stock transactions, dependent care assistance, non-accountable plan expense reimbursements, the value of company travel or personal use of a vehicle, often are not known to the employer until well after the end of the year.



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Alternatives

The alternatives available to the IRS and employers were outlined during public hearings² on the subject in December and January, generally falling into the following categories:

- **Earlier deadlines:** Shift deadlines for submitting W-2 and 1099 data to the government from March 31 to January 31, or even mid-January.
- **More frequent reporting:** Require quarterly reporting of W-2 data, as some states already do. This alternative, perhaps in conjunction with an earlier deadline, would enable the IRS to detect most fraudulent refund claims.
- **Increase electronic filing:** Require electronic reporting from most employers. Only 1% of employers are presently required to file electronically under a mandate crafted in 1982, long before technology improvements made electronic filing widely possible.
- **Direct reporting to the IRS:** Have employers report directly to the IRS instead of, or in addition to, the SSA.
- **Estimated and final versions:** The IRS could receive preliminary W-2 and 1099 reports in mid-January, followed by revised information returns later, if necessary.

Each of these alternatives has advantages, disadvantages and cost implications for both the IRS and employers. The IRS is now considering what changes, if any, to include in future regulations. Congressional action may also be necessary. ADP will continue to monitor this important initiative affecting employers, and will report significant changes in future Eye on Washington editions.

¹Testimony before the Senate Finance Subcommittee on Fiscal Responsibility and Economic Growth on Identity Theft, March 20, 2012

²IRS to Host Public Meeting Dec. 8, 2011 on Real-Time Tax System (IR-2011-114); IRS to Host Second Real-Time Tax System Meeting Jan. 25, 2012 (IR-2012-10)

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