ADP National Account Services
Outsourcing for HR, Benefits and Payroll

TECH FLEX

JULY 2008 **ISSUE VII**

The topics covered in this issue are:

IRS INCREASES MILEAGE REIMBURSEMENT RATES

On June 23, 2008, the Internal Revenue Service (IRS) communicated via Announcement 2008-63 an increase in the optional standard mileage rates for the final six months of 2008. Taxpayers may use the optional standard rates to calculate the deductible costs of operating an automobile for business, charitable, medical or moving purposes. As a way of background, the optional business standard mileage rate is used to compute the deductible costs of operating an automobile for business use in lieu of tracking actual costs. This rate is also used as a benchmark by the federal government and many businesses to reimburse their employees for mileage.

In the announcement increasing the mileage rates, IRS Commissioner Doug Shulman stated the following:

> Rising gas prices are having a major impact on individual Americans. Given the increase in prices, the IRS is adjusting the standard mileage rates to better reflect the real cost of operating an automobile. We want the reimbursement rate to be fair to taxpayers.

The rate will increase to 58.5 cents a mile for all business miles driven from July 1, 2008, through December 31, 2008. This is an increase of eight cents from the 50.5 cent rate in effect for the first six months of 2008.

The new six-month rate for computing deductible medical or moving expenses will also increase by eight cents to 27 cents a mile, up from 19 cents for the first six months of 2008. The rate for providing services for charitable organizations is set by statute, not the IRS, and remains at 14 cents a mile.

Mileage Rate Changes

Purpose	Rates 1/1 through 6/30/08	Rates 7/1 through 12/31/08
Business	**50.5**	**58.5**
Medical/Moving	**19**	**27**
Charitable	**14**	**14**

For a copy of Announcement 2008-63, please click on the link provide below:

http://www.irs.gov/pub/irs-drop/a-08-63.pdf

FURTHER HSA GUIDANCE RELEASED BY IRS

On June 25, 2008, the Internal Revenue Service (IRS) issued via Notice 2008-59 (2008-59), enhanced guidance on number of health savings account (HSA) issues.

Background

An HSA is a medical savings account available to taxpayers that enable individuals to pay for current health expenses and save for future qualified medical and retiree health expenses on a tax-free basis. For an individual to be eligible to contribute to an HSA, or have contributions made on their behalf to an HSA, an individual must be enrolled in a "high deductible health plan" (HDHP) and have no "impermissible coverage." The funds contributed to an HSA are not subject to federal income tax at the time of deposit. Also taxes are not assessed on investment gains. Funds may be used to pay for qualified medical expenses at any time without federal tax liability. Withdrawals for non-medical expenses are also allowable but non-medical expense withdrawals are subject to federal income tax plus an additional 10% excise tax. However, the 10% excise tax does not apply where the account holder reaches age 65, or is disabled or dies.

A HDHP is a health plan that meets certain requirements in relation to annual deductible amounts and out-of-pocket expenses. These amounts and expenses are determined on whether an individual has self-only coverage or family coverage and are indexed each year based on inflation.

Generally any coverage that provides benefits prior to the applicable HDHP deductible being met is considered impermissible coverage and results in elimination of HSA eligibility. However, an individual may have certain permitted coverage and remain HSA eligible. The permissible types of coverage include those that provide accident, disability, dental, vision, and long term-care benefits, as well as limited purpose flexible spending accounts (LPFSA) and post deductible flexible spending accounts (PDFSA). An LPFSA is permissible coverage if reimbursement under the LPFSA is limited to dental, vision and preventive expenses. A PDFSA may reimburse for any eligible expense and still constitute permissible coverage if no expense is reimbursed prior to the HDHP deductible being satisfied.

Highlights of Notice 2008-59

The guidance released in 2008-59 came in the form of 42 frequently asked questions (FAQs) and answers on a wide range of HSA topics. A small sampling of the FAQ topics addressed include the following:

On-Site Clinics as Permissible Coverage (Question 10)

The IRS determined that an otherwise HSA eligible individual who has access to an employer's on site clinic providing free or low –cost health care will not be found to be HSA-ineligible as long as the health care provided is limited to permitted coverage, preventive care, and other benefits that are not "significant benefits in the nature of medical care." The IRS provided the following examples as services that could be provided at on-site employer clinic without resulting in HSA ineligibility.

- Physicals and immunizations.
- Injecting antigens provided by employees (e.g. performing allergy injections).
- Provision of a variety of aspirin and other non-prescription pain relievers.
- Treatment for injuries caused by accidents at work.

HDHP Deductible Expenses Used for Post-Deductible FSA Purposes (Question 15)

The IRS stipulated that only medical expenses that would be covered under the HDHP plan provisions may be taken into account when determining whether the deductible under the HDHP has been met in relation to allowing expenses to be reimbursed under the LPFSA without making the individual HSA ineligible. For example, if the HDHP does not cover chiropractic services, chiropractic expenses will not count toward satisfying the HDHP deductible.

HSA Distributions via Debit Card (Question 27)

The IRS stated that debit cards that restrict payments and reimbursements to health care may be used in conjunction with a HSA administration process as long as the HSA accountholder also has access to HSA funds by other methods such as online transfers, withdrawals from automatic teller machines or check writing.

Establishment of an HSA (Questions 38 and 39)

It was stated by the IRS in these FAQs, that state trust law governs when an HSA is established. Most state laws require that for a trust to exist, an asset must be held in trust. As a result, most states require that a trust must be funded in order to be established. The establishment date of an HSA is of great significance, as per IRS Notice 2004-2, Q/A 26, only expenses incurred on or after the date of account establishment are eligible for reimbursement on a tax-free basis.

HSA Administration Fees as Distributions (Question 42)

It was noted by the IRS, that administration and maintenance fees withdrawn from an individual's HSA are not to be reported on Form 1099-SA as HSA distributions. Rather, these withdrawn fees should be reflected on the year end Form 5498-SA (distributed to accountholder and IRS) which indicates the "fair market value" of the HSA.

Link to Notice 2008-59

For a copy of Notice 2008-59 please click on the link provided below:

http://www.treas.gov/press/releases/reports/notice200859.pdf

CMS RELEASES UPDATED MEDICARE PART D NOTICES

The Centers for Medicare and Medicaid Services (CMS) posted updated Medicare Part D model notices on its website. These revised communications, for use after June 15, 2008, include the creditable, non-creditable, and personalized model notices and replace those issued in February of 2007.

Background

The Medicare Prescription Drug Improvement Act of 2003 (MMA) added a new voluntary prescription benefit (Part D) to the Medicare program, effective January 1, 2006. Individuals eligible for Part D are those already covered under Medicare Part A or B and include active workers and retirees, and their spouses and dependents that live in a "service area" of a Part D plan - that is, a location that meets certain pharmacy access standards.

All group health plans that offer prescription drug coverage must provide notices of creditable coverage to covered employees, retirees, and their dependents that are eligible for Medicare Part D. This requirement was effective beginning with the initial Medicare plan year beginning on January 1, 2006 and for each subsequent plan year. It is important to note that this requirement also extends to health plans that only cover active employees, because these individuals, although not yet retired, may still be Part D eligible. The purpose of the notice is to help individuals who are Part D eligible and currently covered under prescription drug coverage to decide whether they need to enroll in Part D when first eligible. If an eligible individual does not enroll in Part D coverage when he/she is first eligible and they do not have creditable prescription drug coverage, he/she may be accessed a late enrollment penalty if the individual eventually enrolls in Part D.

The creditable coverage notice must be provided at a minimum (a) prior to an individual's initial enrollment period for the Medicare prescription drug benefit; (b) prior to the effective date of enrolling in the sponsor's plan and upon any change that affects whether the coverage is creditable prescription drug coverage; (c) prior to the commencement of the annual coordinated election period that begins on November 15 of each year; and (4) upon beneficiary request.

Link to Revised Medicare Part D Notice

For a copy of the revised CMS model notices, please click on the link provided below:

http://www.cms.hhs.gov/CreditableCoverage/09_CCafterJune15.asp

CHANGES TO SUPPLEMENTAL MILITARY PAY TAXATION ENACTED

On June 17, 2007, President Bush signed into law the "Heroes Earnings Assistance and Relief Tax Act of 2008" which contains provisions that impact the taxation of supplemental military pay. The revised taxation rules are effective in relation to supplemental military pay paid after December 31, 2008.

Background

As background, compensation paid by an employer to an employee while on military duty that represents the difference between the employee's regular pay and the pay provided by the state or government is known as supplemental (or differential) military pay. The taxation of supplemental military pay is dependent on the circumstances of the employee's military service.

Under the current regulations, the following rules apply.

- If the supplemental military pay is provided while on the employee is on temporary assignment (30 days or less) with the state National Guard or the Armed Forces Reserve, it is considered wages subject to federal income withholding or social security, Medicare and federal unemployment tax act (FUTA) taxes.

- If the supplemental military pay is provided while the employee is on active duty (more than 30 days) with the United States Armed Forces or on an indefinite assignment with the state National Guard, the Internal Revenue Service (IRS) considers the employment relationship to be broken. The result of the IRS position is that military supplemental pay received while on active duty is not subject to federal income tax withholding, or social security, Medicare or FUTA taxes.

In cases where the military duty is temporary, the supplemental military pay is considered wages and must be reported on the employee's Form W-2. However, if the military service is active or indefinite, the supplemental military pay is not considered wages and if the amount paid is $600 or greater must be reported on Form 1099-MISC in Box 3 titled "Other Income."

New Law Impact

As a result of the new law, the definition of wages is amended for purposes of federal income tax withholding to include any supplemental military payment made by employer to an employee. This means that any supplemental military payment made by an employer should be included as wages for federal income tax purposes regardless as to whether the employee is on temporary assignment or active duty. In addition, supplemental military pay would be treated as compensation for retirement plan purposes.

It is important to note that the new law does not change the current rule in relation to social security, Medicare of FUTA taxes. Therefore, employees on active duty receiving supplemental military pay will continue to not be subject to employment taxes.

Link to New Law

For a copy of the “Heroes Earnings Assistance and Relief Tax Act of 2008”, please click on the link provided below.

HTTP://FRWEBGATE.ACCESS.GPO.GOV/CGI-BIN/GETDOC.CGI?DBNAME=110_CONG_BILLS&DOCID=F:H6081EH.TXT.PDF

USCIS REVISES EXPIRATION DATE ON FORM I-9

The United States Citizenship and Immigration Services (USCIS), on June 26, 2008 modified the expiration date noted on Form I-9. Form I-9 is utilized by employers as a tool to verify the identity and work eligibility of new employees at the time they are hired. As a result of the Immigration Reform and Control Act of 1986 (IRCA), all employers in the United States are responsible for completion and retention of the Form I-9 for each individual, citizens and non-citizens, hired after November 6, 1986, for employment in the United States.

The revised version of Form I-9 resulted in no substantive changes made to the form itself. USCIS recently had replaced the form's revision date of “6/5/07" (found in lower right hand corner of each page with a revision date of "6/16/07”. However, on June 26, 2008, the agency restored the "6/5/07" version which replaces all prior versions of the form. The primary change was to the form's expiration date since the prior version was set to expire at the end of June. Now the Form I-9 expires June 30, 2009. Employers must immediately start using the latest version of Form I-9 for employment verification and record retention purposes.

Although, the form is not submitted to the federal government, employers must retain completed I-9 forms for the later of three years after the employee's date of hire or one year after the date that employment is terminated. Therefore, a Form I-9 needs to be retained for all current employees, as well as terminated employees whose records remain within the retention period. The Form I-9 may be completed and stored in hard copy or electronically and must be made available to the federal government if requested as part of an audit.

Link to Revised Form I-9

For a copy of the revised Form I-9, please click on the link provided below:

http://www.uscis.gov/files/form/I-9.pdf

SUPPLEMENTAL WAGE WITHHOLDING GUIDANCE RELEASED

On June 16, 2008, the Internal Revenue Service (IRS) via Revenue Ruling 2008-29 (2008-29) released guidance with respect to income tax withholding in nine different situations involving the payment of supplemental wages. The goal of the IRS communication was to assist employers in determining the amount of income tax required to be with respect to certain supplemental wages the employer pays to an employee. It is important to note that as result of the release of 2008-29, previous Revenue Rulings 66-294 and 67-131 are now obsolete.

Background:

On July 25, 2006, the IRS issued final regulations on determining the method and amount of income tax withholding on supplemental wages, including the higher flat rate applied to supplemental wages exceeding $1 million in a calendar year. The final regulations applied to payments made on or after January 1, 2007.

Generally, supplemental wages include any wages paid by an employer that are not regular wages. Regular wages are defined as amounts paid by an employer for a payroll period either at a regular hourly rate or in a predetermined fixed amount. Wages that vary from payroll period to payroll period based on factors other than the amount of time worked are supplemental wages.

The final regulations listed several examples of supplemental wage payments, including:

- reported tips;
- overtime pay;
- bonuses;
- back pay;
- commissions;
- wages paid under reimbursement or other expense allowance arrangements;
- nonqualified deferred compensation;
- noncash fringe benefits;
- sick pay paid by a third party as an agent of the employer;
- amounts includible in gross income under IRC §409A;
- income recognized on the exercise of a nonstatutory stock option;
- imputed income for health coverage for a non-dependent; and
- income recognized on the lapse of a restriction on restricted property transferred from an employer to an employee.

In addition, the 2006 final regulations provided the following guidance:

- **Withholding on supplemental wages of $1 million or less in a calendar year**

Specifically, the regulations provide that if an employee has not received cumulatively more than $1 million in supplemental wages during the calendar year, there are two withholding methods available to an employer with respect to a payment of supplemental wages.

Aggregate method. Under this method, the employer calculates the amount of withholding due by aggregating the amount of supplemental wages with the regular wages paid for the current payroll period or for the most recent payroll period of the year of payment, and treats the aggregate as if it is a single wage payment for the regular payroll period. If the supplemental wages are paid concurrently with wages for the current payroll period, then they must be aggregated with the wages paid for the current payroll period.

Optional flat rate method. Under this method, the employer disregards the amount of regular wages paid to an employee as well as the withholding allowances claimed by the employee on his/her Form W-4 (Employee's Withholding Allowance Certificate), and uses a flat percentage rate in calculating the amount of withholding. This method is available only if two conditions are met:

(1) the employer has withheld income tax from regular wages paid to the employee during the same year as the payment of supplemental wages or during the preceding calendar year; and

(2) the supplemental wages are either (a) not paid concurrently with regular wages or (b) separately stated on the payroll records of the employer.

- **Mandatory withholding on supplemental wages over $1 million in a calendar year**

The regulations provide that if a supplemental wage payment, when taken together with all other supplemental wage payments paid by an employer to an employee during the calendar year, exceeds $1 million, then the employer must withhold federal income tax from the supplemental wages in excess of $1 million at a flat rate equal to the maximum rate of tax in effect that year.

Highlights of the new IRS Guidance--Revenue Ruling 2008-29

In 2008-29, the following nine different situations including detailed fact scenarios involving supplemental wage payments are examined:

(1) commissions paid at fixed intervals with no regular wages paid to the employee;

(2) commissions paid at fixed intervals in addition to regular wages paid at different intervals;

(3) draws paid in connection with commissions;

(4) commissions paid to the employee only when the accumulated commission credit of the employee reaches a specific numerical threshold;

(5) a signing bonus paid prior to the commencement of employment;

(6) severance pay paid after the termination of employment;

(7) lump sum payments of accumulated annual leave;

(8) annual payments of vacation and sick leave; and

(9) sick pay paid at a different rate than regular pay.

In all nine situations, it was assumed, for income tax and income tax withholding purposes, that there is no constructive receipt or constructive payment of wages before the actual payment of wages, and that all payments are made on or after January 1, 2007.

Link to a copy of Revenue Ruling 2008-29

For a copy of Revenue Ruling 2008-29, including IRS specific fact scenarios, analysis and findings, please click on the link provided below:

http://www.irs.gov/irb/2008-24_IRB/ar08.html

IOWA FURTHER CLARIFIES PAYMENT OF WAGES BY MAIL LEGISLATION

As reported in the June Tech Flex, effective July 1, 2008, Iowa laws changed regarding the mailing of paychecks by an employer to its employees. The newly enacted legislation states that an employer who fails to pay wages on time, regardless of the payment method is liable for any overdraft charges incurred by the employee as a result of the late wage payment. Generally, Iowa requires that wages be paid no later than 12 days from the end of the pay period, excluding Sundays and holidays.

In general, the terms employee, employer and persons are defined as follows:

Employee:

A natural person who is employed in this state for wages by an employer.

Employer:

A person who in this state employs for wages a natural person.

Person:

An individual, corporation, limited liability company, government or governmental subdivision or agency, business trust, estate, trust, partnership or association, or any other legal entity.

Subsequent to the release of the new legislation, the Iowa Workforce Development department issued additional guidance and clarification on the new laws. In the premise to the released guidance, the following was stated:

> The purpose of the revised law, passed by the Iowa Legislature and signed by Governor Culver, is to ensure that employees receive wages in a timely fashion. The law also makes an employer liable for any bank overdraft charges assessed an employee if the employer fails to pay an employee's wages on or by a regularly scheduled payday.

Below are the highlights of the guidance issued by the Iowa Workforce Development:

- An employer may not mail a paycheck to an employee without written consent by the employee**.** This is true even if an employer has historically sent paychecks to its employees via mail. The employer must obtain the employee's written authorization prior mailing an employees paycheck.

- The new Iowa requirement did not impact the current Iowa direct deposit provision. This provision allows employers to require employees hired after July 1, 2005, be required, as a condition of employment, to receive wages via direct deposit at a financial institution of the employee's choice. Further, the new Iowa provisions do not require that an employer obtain written authorization from an employee before mailing the **wage statement (pay stub)** if the actual wages are paid by direct deposit.

- An employer may not mail the employees paycheck unless the employer has received written authorization from the employee to do so, even where paychecks are normally

distributed in person and an employee is absent from work on the regularly scheduled payday.

In addition, the guidance addressed the items that should be included in an employee's written authorization to receive his or her wages via mail. It was noted that the change in legislation does not require that any specific provisions be used for written authorization. However, the following sample provision was provided:

I, _____, voluntarily authorize [*insert employer name*] to forward my paycheck by mail. I understand that without such written authorization, the employer may no longer forward my check paycheck by mail. I further understand that this authorization may be revoked at any time with written notice to the employer.

Name_____Date_____
Address_____
City_____State_____Zip_____

Link to the Iowa WorkForce Development guidance

For a copy of the Iowa WorkForce Development guidance, please click on the link provided below:

http://www.iowaworkforce.org/labor/wagelawmailpaychecks.pdf

MARYLAND RAISES MINIMUM WAGE

Effective July 24, 2008, the minimum wage rate in relation to Maryland state law will be changing from $6.15 per hour to $6.55 per hour. It is important to note that the raise in the Maryland minimum wage coincides with the increase to the federal minimum wage. As a result, both the Maryland state minimum wage and the federal minimum wage will be $6.55 per hour as of the date noted above.

The tipped employee minimum hourly rate in Maryland will be changing from $3.08 per hour to $3.28 per hour. Therefore, the maximum tip credit will be changing from $3.07 per hour to $3.27 per hour. ($3.28 + $3.27 = $6.55). The Opportunity Wage Rate will not change and will remain at $4.25 per hour.

Link to the Maryland Wage & Hour Fact Sheet

For a copy of Maryland Wage & Hour Fact Sheet providing documented details of the changes to be effective 7/24/2008, please click on the link provided below.

http://autopaydev/statchanges/Docs-US/08-0300-0399/080307A1.pdf

ADP National Account Services does not make any representation or warranty that the information contained in this newsletter, when used in a specific and actual situation, meets applicable legal requirements. This newsletter is provided solely as a courtesy and should not be construed as legal advice. The information in this newsletter represents informational highlights and should not be considered a comprehensive review of legal and compliance activity. Your legal counsel should be consulted for updates on law and guidance that may have an impact on your organization and the specific facts related to your business.

*****Please note that the information provided in this document is current as of the date it is originally published.*****