

DRAFT  
FOR DISCUSSION ONLY

# UNIFORM WAGE WITHHOLDING PROCEDURE ACT

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NATIONAL CONFERENCE OF COMMISSIONERS  
ON UNIFORM LAWS

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MEETING IN ITS ONE-HUNDRED-AND-TWELFTH YEAR  
WASHINGTON, DC  
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# UNIFORM WAGE WITHHOLDING PROCEDURE ACT

*WITH PREFATORY NOTE AND PRELIMINARY COMMENTS*

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NATIONAL CONFERENCE OF COMMISSIONERS  
ON UNIFORM LAWS

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## **UNIFORM WAGE WITHHOLDING PROCEDURE ACT**

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**UNIFORM WAGE WITHHOLDING PROCEDURE ACT**  
**TABLE OF CONTENTS**

Prefatory Note ..... 1

SECTION 1. SHORT TITLE. .... 9

SECTION 2. DEFINITIONS. .... 9

    (1) "Employee" ..... 9

    (2) "Employer" means ..... 9

    (3) "Employment tax" ..... 9

    (4) "Internal Revenue Code" ..... 10

    (5) "Wages" means ..... 10

SECTION 3. FILING AND PAYMENT DATES. .... 20

SECTION 4. EFFECTIVE DATE AND TRANSITION RULES ..... 22

# UNIFORM WAGE WITHHOLDING PROCEDURE ACT

## Prefatory Note

In 1966 the Simplified Tax and Wage Reporting System Program, commonly referred to by the acronym STAWRS, was created by the Internal Revenue Service and consisted of a working group of representatives from the Internal Revenue Service, Department of Labor, Department of the Treasury, Office of Management and Budget, Small Business Administration, Social Security Administration and various states<sup>1</sup> and private sector organizations<sup>2</sup>. STAWRS conducted a study to determine the extent of definitional differences for the term “wage” found in federal and state income tax withholding and unemployment insurance statutes with a view towards modifying the term “wage” in each of those various provisions in order to achieve a substantially uniform definition across all the statutory frameworks.

The fifty states, the District of Columbia, and the federal government have a total of 96 different employment tax laws. Within the 96 employment tax laws, there are almost 500 different components or provisions. Employers must maintain separate wage records for federal income tax withholding, state income tax withholding, the federal insurance contributions act (FICA), the federal unemployment tax act (FUTA), and state unemployment insurance (SUI) taxes. *In many cases, employers must report this information to government agencies at different times, on different forms, and on assorted media. ...* In addition to requiring employers to report tax-and wage-related information, employment tax laws require government agencies to process the information reported, verify that the information complies with the laws, work with employers to correct reports that do not comply, and provide assistance to employers attempting to comply. The diversity in current laws

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<sup>1</sup> The State and Federal agencies represented in this working group were: California Employment Development Department and Franchise Tax Board, Commonwealth of Kentucky,, Minnesota Department of Revenue, Montana Department of Labor and Department of Revenue, Nevada Employment Security Division, New York Department of Labor, Social Security Administration, Simplified Tax and Wage Reporting System Program, U.S. Department of Labor, Texas State Comptroller of Public Accounts, U.S. Department of the Treasury (Office of Tax Policy)Wisconsin Unemployment Insurance Division. Also, the Federation of Tax Administrators was a member of the working group.

<sup>2</sup> The private sector representation was: American Bar Association, American Payroll Association, Ceridian Tax Service, Inc., Federal Liaison Services, Inc., Paychex, Inc., and Planmatics, Inc.

1 and filing dates makes it difficult for government agencies to  
2 provide consistent, accurate, and timely service to their  
3 customers.

4 The diverse state and federal laws governing wage taxes and  
5 withholding significantly increase employer burden....<sup>3</sup>  
6

7 Reporting complexities caused by existing statutes are very costly to everyone. Small  
8 employers must attempt to understand sometimes subtle distinctions, have knowledge of a  
9 large number of definitions and attempt to understand the different requirements of them for  
10 two different codes within their state. Large and small employers that do business in more  
11 than one state must deal with these issues in each state and the administrative complexities  
12 caused by multi-jurisdictional differences. On the governmental side of the ledger, states must  
13 maintain two separate taxpayer auditing capabilities (and staffs) to insure compliance with two  
14 separate laws. By harmonizing the definition of wages substantial compliance cost savings<sup>4</sup>,  
15 both for private industry and government, were, and are, anticipated.  
16

17 As part of their study the STAWRS group analyzed and compared hundreds of federal  
18 and state statutory provisions and administrative positions to determine the existing degree of  
19 harmony of various definitions in various jurisdictions for purposes of determining in each  
20 jurisdiction amounts subject to income tax withholding and amounts subject to unemployment  
21 insurance assessment (and, tangentially, unemployment benefits). The project encompassed  
22 two studies: one focused on income tax withholding, the Harmonized Wage Code for Income  
23 Tax Withholding, and the other, The Harmonized Wage Code for Unemployment Insurance<sup>5</sup>,

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1 <sup>3</sup> The Harmonized Wage Code For Income Tax Withholding (unpublished study, IRS, 2001)(copy  
2 on file at the University of Dayton School of Law with Prof. Laurence B. Wohl; hereinafter  
3 sometimes referred to as the “HWC/ITW”) at pg. 1-1. (Emphasis Added) This report together with  
4 The Targeted Harmonized Wage Code (discussed, *infra*, note 6) was published electronically on the  
5 STAWRS website maintained by the Internal Revenue Service. In 2001 the IRS redesigned its  
6 public website, and in the transition to the new website both reports were removed. These reports,  
7 together with a supporting data base, are no longer available. Neither the reports nor the data base  
8 were published in hard copy.

1 <sup>4</sup> Simplification of statutory compliance through adoption of common requirements across all  
2 federal and state taxing authorities will lead not only to reduced compliance costs for private industry  
3 but also to reduced resource commitment by the States for purposes of tax compliance education  
4 and enforcement. With a single set of statutory compliance rules within a state, that state will,  
5 presumably, be able to maintain a single rather than dual compliance and enforcement staffs.  
6 Additionally, a “harmonized” state would be able to reduce the costs of public education regarding  
7 its income tax withholding requirements and its unemployment insurance tax assessments.

1 <sup>5</sup> At the time the STAWRS program was terminated, in addition to the completed HWC/ITW, the  
2 group was also nearing completion on two additional reports and recommendations: (1) The

1 focused on unemployment insurance tax assessment.

2  
3 The goal of STAWRS was to identify items of compensation that could be excluded  
4 from the income subject to income tax withholding and the income subject to unemployment  
5 insurance tax assessment. These were to be items that were components of compensation but  
6 which were (1) given treatment for income tax withholding purposes differing from one state  
7 to another, (2) given treatment for unemployment tax purposes differing from one state to  
8 another, and (3) perhaps the most confusing for employers, given treatment by individual  
9 states that differed for that state's income tax withholding law and its unemployment tax law.  
10 These were items, because of the variety of their treatment, that created significant compliance  
11 complexity yet they clearly were items of compensation when paid. STAWRS identified 14  
12 such elements of wages<sup>6</sup> and recommended that they be excluded from wages for income tax  
13 withholding purposes. This recommendation forms the backbone of this act though this act  
14 goes beyond that recommendation.

15  
16 This act goes beyond the harmonization of the income tax withholding provisions of  
17 the THWC to include a harmonization of those provisions with the unemployment tax  
18 provisions of the various states. Adoption of a common definition for these items by all states  
19 for both income tax withholding and unemployment insurance tax wage base purposes will  
20 lead to substantial harmonization and significant compliance simplification. These items are  
21 common forms of employee compensation but are not ubiquitous. They are items that are  
22 more likely to occur in a large employer environment for income tax withholding purposes but  
23 are items that are frequently part of the unemployment tax wage base for both large and small  
24 employers. These items, for the most part, are excluded from a wage base for either income  
25 tax withholding or unemployment insurance purposes in some states but not in all.  
26 Harmonization of each component across the income tax withholding statutes and the

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3 Harmonized Wage Code/Unemployment Insurance report (sometimes referred to as HWC/UI)  
4 focused on inter-jurisdictional harmonization of state unemployment insurance taxes, FICA and  
5 FUTA, and (2) The Harmonized Wage Code/Filing Dates (sometimes referred to as HWC/FD).

1 <sup>6</sup> The HWC/ITW report resulted in a legislative recommendation titled the Targeted Harmonized  
2 Wage Code (sometimes referred to as the THWC) (unpublished study, IRS, 2001; copy on file at the  
3 University of Dayton School of law with Prof. Laurence B. Wohl). Both the HWC/ITW and the  
4 THWC reports focus on inter-jurisdictional harmonization of income tax withholding statutes. The  
5 THWC recommended the exclusion of 14 items of income from the withholding requirements. In  
6 other words, though still taxable income to an employee, these items of income would not be subject  
7 to withholding by the employer. The fourteen items set out by the THWC to be excluded from the  
8 withholding tax wage base are (in no particular order of importance): vacation pay, compensation  
9 for jury duty, employer provided meals and lodging, group term life insurance, dependent care  
10 benefits, tips, employee business expense reimbursements, health insurance, cafeteria plans, moving  
11 expenses, death benefits, sick pay, fringe benefits and contributions to qualified retirement plans.  
12

1 unemployment insurance tax assessment statutes of all states will simplify the compliance  
2 process and administration of reporting for large and intra-state employers and small single  
3 state employers alike. This act harmonizes the definition of wages for income tax withholding  
4 purposes by excluding the same components of compensation from withholding of taxes in all  
5 states that have an income tax. It also harmonizes the definition of wages for unemployment  
6 insurance assessment purposes by excluding the same components of compensation from the  
7 unemployment insurance tax wage base in all states. Additionally, for those states that have  
8 an income tax as well as unemployment insurance the definition of wages will be harmonized  
9 by the exclusion of the same components of compensation from both wage bases. The act  
10 creates substantial conformity of definitions, and thus simplification, between an adopting  
11 State's income tax wage base and its unemployment insurance wage base as well as  
12 substantial conformity of those wage bases among the States<sup>7</sup>.

13  
14 Problematically harmonization of the tax withholding provisions with the  
15 unemployment insurance provisions requires the meshing of two different, and somewhat  
16 conflicting, policies within each single jurisdiction as well as among the multiple jurisdictions.  
17 The income tax withholding regime is indifferent as to items in the wage base<sup>8</sup> whereas the  
18 unemployment insurance tax regime is deeply concerned about the items in the wage base. On  
19 the one hand the policies driving income tax withholding are focused on the single issue of  
20 collection, a ministerial act of collection rather than a political question of what should be  
21 taxed. Items of income that are subject to income tax will continue to be subject to that tax  
22 even if not subject to withholding. On the other hand, policies underlying unemployment  
23 insurance programs are concerned with dispersal of benefits as well as the collection of  
24 sufficient revenues to provide for those benefits. For purposes of unemployment insurance  
25 each item placed in the wage base and subject to unemployment insurance tax will assist  
26 employee's in meeting threshold requirements<sup>9</sup> and lead to increased revenues available for

---

1 <sup>7</sup> There are 43 different federal and state income tax codes and 53 social welfare tax codes.

1 <sup>8</sup>Though at first blush it might appear that the income tax withholding provisions of a state or federal  
2 statute may have something to do with the determination of taxable income by defining factors such  
3 as wages and employee, the fact is these definitions are important (from the perspective of income  
4 tax) only for determining whether a payer of income is required to withhold income taxes or whether  
5 the payee has the responsibility of paying owed taxes directly to the state or federal government.  
6 Whether an item of income is wages or some other form of income is irrelevant to the question of  
7 whether it is taxable income. That is an issue with which the income tax withholding provisions do  
8 not deal.

1 <sup>9</sup> For unemployment benefits purposes a recipient must have earned a minimum amount (which  
2 varies from state to state). Thus, any amounts removed from the unemployment insurance tax  
3 assessment wage base will make it more difficult for low income employees to reach the threshold  
4 and therefore qualify to receive unemployment benefits. It is certainly possible to maintain two  
5 separate wage base calculations – one for benefit calculation and the other for tax assessment

1 distribution to those in need. Conversely, each item removed from this wage base will make it  
2 more difficult for an employee to reach threshold requirements and will reduce the amount of  
3 revenue available for distribution. Thus, for purposes of unemployment insurance,  
4 components of the wage base are important on three counts. First, an item added to the  
5 unemployment insurance wage base makes it easier for an employee to meet the threshold  
6 amounts of income needed to qualify for benefits; second, an item of income added to the  
7 wage base increases benefits (up to statutory maximums) payable to an unemployed former  
8 employee; and third, the larger the unemployment wage base the greater the unemployment  
9 taxes collected and, thus, the larger the fund to pay benefits.

10  
11 In attempting to harmonize the two separate code constructs there must be a careful  
12 balancing of the need for simplicity, and thus compliance cost reduction, with the need not to  
13 compromise benefits that a state has deemed appropriate for its unemployed<sup>10</sup>.

14  
15 For large employers and those doing business in more than one state the harmonization  
16 of the most common elements of compensation provide significant alleviation of compliance  
17 complexity. However, relief from compliance burdens for small employers, most of which do  
18 business in a single state will likely be as great or greater than for larger employers. Because  
19 any one small employer has small numbers of employees it is not likely to have employees  
20 dedicated to compliance with federal and state tax and unemployment laws. Consequently,  
21 the small employer will (1) undertake the compliance regimen themselves (i.e., an  
22 entrepreneur will be responsible for compliance or will assign a most likely already  
23 overworked bookkeeper to such responsibility) with the commensurate cost in time and  
24 education necessary to comply (a cost that will be spread over a small employee base<sup>11</sup>), (2)

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6 calculation – however, that would appear to create a new level of bookkeeping complexity.  
7 However, the act does not address this issue.

1 <sup>10</sup> Not addressed by this act is the question of what methods might be used by individual states  
2 to correct for lost revenues to its unemployment insurance fund and the income threshold amounts  
3 needed to qualify for benefits for those whose qualifying income is reduced by the exclusion of items  
4 from the wage base.

1 <sup>11</sup> Eighty-five percent of the 6.7 million employers in the United States employ 20 or  
2 fewer workers. It is also known that these ‘small’ employers deal with fewer of the  
3 component provisions found in all the state and federal employment tax laws. Thus,  
4 most small employers will not be concerned with many of the components, usually  
5 those involving more complex forms of remuneration. Therefore, the project team  
6 looked at components that are most common among small employers and their  
7 employees...”

8  
9 HWC/ITW, *supra*, note 3, at pg. 1-7 [footnote omitted].



1 comply “by the seat of their pants” frequently, if not regularly, resulting in fines and interest  
2 bearing errors, or (3) place the compliance burden with contract professionals (accountants,  
3 lawyers and payroll services).<sup>12</sup>  
4

5 States may balk at conforming their own income tax and unemployment tax wage  
6 bases let alone conforming those wage bases to other states’ wage bases and, possibly, even  
7 the federal income tax withholding and FICA wage bases, for a number of good reasons. Two  
8 of these reasons are that conformity may lead to a loss of revenue in a state’s unemployment  
9 insurance system, and conformity may reduce unemployment benefits in some states.<sup>13</sup> A  
10 report commissioned by the STAWRS project set out the following example in explaining the  
11 revenue impact of reducing the unemployment insurance wage base:  
12

13 To illustrate the impact on tax revenues, consider the following:  
14 An employer has an employee in state A and an employee in  
15 state B and each earns \$20,000 per year. State A has a taxable  
16 wage base of \$10,000 as opposed to state B’s \$21,000.  
17 (Taxable wage base is that portion of an employee’s total wages  
18 subject to SUI tax [and may not be the same as that employee’s  
19 income tax wage base].) Consider as well that the reduction in

---

11 The note accompanying this statement in the study points out that “15% of the ‘large’  
12 employers employ more than 50% of all workers in the U.S.,” and further, that the components of  
13 their employees’ wages are far more complex than those of small employers. (Id. at note 17.)  
14

1 <sup>12</sup> As pointed out in a study conducted by an outside contractor to the STAWRS group, though  
2 small employers, “[a]s a group... generally deal with a smaller number of wage components... [they],  
3 in the aggregate, bear the greatest per employee costs associated with the payroll reporting process.”  
4 Lalith de Silva, Dominic Rotondi, Mikel Lasa, The Impact of the Targeted Harmonized Wage Code  
5 on Unemployment Insurance (unpublished study submitted to the Internal Revenue Service by  
6 Planmatics Inc., 2001; on file at the University of Dayton School of Law with Professor Laurence  
7 B. Wohl) at pg. 5 (hereinafter referred to as the “Planmatics study”).  
8

9 The Planmatics study examined the impact in twelve states of harmonizing the 14 items  
10 enumerated by the THWC. The states were California, Connecticut, Georgia, Iowa, Louisiana,  
11 Mississippi, Minnesota, Montana, Nevada, New Jersey, Pennsylvania and Texas. Id. at 14.

1 <sup>13</sup> Anything that reduces the taxable wage base potentially can result in loss of benefit because the  
2 base upon which benefits are calculated will be reduced. For example, in California benefits are  
3 calculated based upon minimum wages of between \$900 and \$1,300 earned during a base period.  
4 (Cal. Unemp. Ins. Code §1281). Anything that lowers amounts considered as wages under the  
5 unemployment insurance regime, therefore, will lower or possibly eliminate benefits available to any  
6 specific individual.

1 taxable wages resulting from these definitional changes is  
2 \$1,000 per year. There would be no impact in state A inasmuch  
3 as the portion of the employee's taxable wages would be  
4 unchanged. However, in state B taxable wages would be  
5 reduced from \$20,000 to \$19,000 and there would be a  
6 commensurate reduction in tax paid by the employer.  
7 When considering worker unemployment benefits, there are two  
8 types of impacts that can occur. First, there are minimum  
9 earning levels in each state that must be met before an employed  
10 worker becomes eligible for benefits. If any reduction in wages  
11 would drop a worker's earnings below the minimum earnings  
12 level, that worker would no longer be eligible for benefits...  
13 Second, and more likely, is the potential reduction in weekly  
14 benefit amounts (WBA). These amounts are calculated on a  
15 worker's earnings, generally a combination of annual earnings  
16 and high-quarter earnings. Any reduction of annual or high-  
17 quarter earnings reduces the worker's WBA...<sup>14</sup>  
18

19 Though traditional contributions might be diminished and benefits reduced under some  
20 circumstances, it does not appear that the amount of loss of revenue or aggregate reduction in  
21 benefit payments will likely be dramatic if the fourteen items of income are harmonized  
22 within a state and among the states and federal government. However, it is possible that, at  
23 least as to reduction of benefits, though the macro problems will not be significant the micro  
24 problems could be devastating. The dollar amounts of benefits paid to any one individual, or  
25 individuals within any single employee sector, may be reduced by a significant percentage or  
26 eliminated altogether.<sup>15</sup>

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1 <sup>14</sup> Planmatics study, *id.* at pgs. 10-11.

1 <sup>15</sup> "The most controversial recommendation of the HWC Project is that dealing with 'meals and  
2 lodging.' ... Most states...[concur with the Internal Revenue Code Section 119 exclusion of meals  
3 and lodging from the income tax wage base], but about one-third of the states include 'meals and  
4 lodging' for UI purposes. This recommendation has caused a great deal of concern ... [in those states  
5 that do not exclude meals and lodging for their unemployment insurance wage base] primarily  
6 because of the possible impact such payments if made excludable might have on the amount of  
7 revenue available and the payment of benefits." draft HWC/ITW, *supra*, note 3 at pg. 2-8.  
8

9 The 23 states that do not exclude meals and lodging from the unemployment insurance wage  
10 base have more than 26% of the countries work force and the impact of the meal and lodging  
11 exclusion from the unemployment benefits wage base can be substantial. For example,  
12 "...California's data indicate the average benefit claim over its duration is \$2,422 and the average  
13 value of the exclusion of the meals and lodging component on affected claims is \$487, amounting  
14 to 20% of the claim of the workers affected. This percentage of reduction, or one close to it, could

1  
2           The Commissioners believe that the act creates the proper balance between efficiency  
3 and cost savings on the one hand and the necessary flexibility required by each State to meet  
4 its citizens' unique needs. The Commissioners recognize that issues of jurisdictional integrity  
5 and different needs of the various States could create stumbling blocks to harmonization.  
6 Nonetheless, the Commissioners believe that adoption of this act will lead to significant  
7 simplification and cost savings for employers and States.

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15   occur in New Jersey, New York and Texas as well.” Planmatics study, *supra*, note 15, at pg. v.

1                                   **UNIFORM WAGE WITHHOLDING PROCEDURE ACT**

2

3

4                   **SECTION 1. SHORT TITLE.** This [act] may be cited as the Uniform Wage

5 Withholdings Act.

6                   **SECTION 2. DEFINITIONS.** In this [act]:

7                   (1) "Employee" means an individual whose remuneration for services paid by the

8 individual's employer is subject to, or would be subject to, if not excluded under subsection

9 (5) of this Section 2, withholding of income tax under the laws of this state or for whom an

10 employer makes contributions under the unemployment insurance laws of this state.

11                                   **Preliminary Comments**

12                   The definition of employee is intended to exclude any relationship in which the service

13 provider is found to be an independent contractor. The distinction between an employee and

14 an independent contractor has been the subject of intense controversy between the Internal

15 Revenue Service and state authorities on the one hand and Taxpayers on the other hand

16 primarily because the recipient of the services of an independent contractor does not make

17 contributions to FICA or FUTA or state unemployment insurance programs on behalf of the

18 service provider whereas the recipient would be required to make these contributions for

19 compensation paid to an employee. Though employment status is a question of common law

20 the Internal Revenue Service has instructed taxpayers that there are 20 factors, each of which

21 is given different weighting depending on the circumstances, which must be considered in

22 making the determination of employee or independent contractor status. (*See*, Rev. Rul. 87-

23 41, 1987-1 C.B. 296). The states generally conform to these 20 factors though interpretations

24 of these factors vary from state to state and court to court. This act does not address the

25 correctness of any position in this regard, it simply accepts whatever status is deemed

26 appropriate under applicable state and federal law.

27

28                   (2) "Employer" means a person that pays remuneration for services to an individual who

29 does not have the status of independent contractor.

30                   (3) "Employment tax" means, at any given time, the total of income taxes withheld from

1 an employee's wages and unemployment insurance taxes incurred by an employer on those  
2 wages which are held by the employer and not yet paid to the appropriate government entity.

3 (4) "Internal Revenue Code" means Title 26 of the United States Code [, as amended].

4 (5) "Wages" means all remuneration, including any remuneration in a medium other than  
5 cash valued at its fair market value, received by an employee from the employee's employer  
6 and aggregate tips received by the employee in excess of \$20 a month from a person other  
7 than the employer for services arising in the context of the employment relationship between  
8 the employer and the employee.

### 9 **Preliminary Comments**

10 In kind payments of wages ("medium other than cash") will be included at the property's  
11 fair market value at the time of payment to the employee by the employer. Cash, of course,  
12 will be valued at its face value. It is assumed that cash payments of wages made in a  
13 denomination other than United States currency will be its official exchange rate value as of  
14 the date of payment.

15  
16 In general all States currently provide that tips or gratuities are wages and that the employer  
17 has the legal obligation to withhold income taxes and to make unemployment insurance  
18 contributions on those wages. This provision assumes that each state has or will have a  
19 reporting procedure similar to the federal requirement that the employee provide a monthly  
20 statement in writing to the employer stating the amount of tips earned during the preceding  
21 month. Because tips are frequently paid for via credit and debit cards the record keeping  
22 requirements for both employer and employee are somewhat less burdensome than they may  
23 have been when such payments were generally made in cash.

24  
25 This definition of wages is intended to include vacation pay. Currently, vacation pay is  
26 defined by all states as a wage with the exception of Delaware. Delaware does include  
27 vacation pay as wages for purposes of both income tax withholding and assessment of  
28 unemployment insurance taxes except for vacation pay paid during a period of unemployment  
29 which is excluded.

30  
31 *Legislative Note: It is anticipated that a jurisdiction adopting this statute will amend both*  
32 *its statute dealing with income tax withholding and its statute dealing with unemployment*  
33 *insurance. In that event, if, subsequent to adoption of this act, a jurisdiction should amend the*

1 *provisions of this Section 1. of this act in either its income tax withholding statute or its*  
2 *unemployment insurance statute care must be taken to amend both statutory provisions in*  
3 *order to maintain the common definition of wages. To avoid the problem of a legislature*  
4 *inadvertently adopting an amendment effecting one or the other of these statutory schemes but*  
5 *not both, it would be preferable to adopt this act as a whole and have both the jurisdiction's*  
6 *income tax withholding statute and its unemployment insurance statute incorporate this act's*  
7 *definition by reference. No matter which method of adoption is chosen, the jurisdiction needs*  
8 *to be certain that adoption of the definition of wages in this act does not have an unintended*  
9 *impact on other statutes that currently incorporate by reference the definition of wages found*  
10 *in either its income tax withholding or unemployment insurance provisions.*

11  
12 The term does not include:

13 (A) the value of any meals or lodging furnished by or on behalf of an employer if, at  
14 the time of furnishing, it is reasonable to believe that the employee will be able to exclude the  
15 value from income under Section 119 of the Internal Revenue Code;

#### 16 **Preliminary Comments**

17 This provision excludes from both the income tax withholdings wage base and the  
18 unemployment insurance tax and benefits wage base amounts that are excluded because they  
19 are items provided by the employer primarily because the physical location for the  
20 performance of services requires the employee to live and/or eat on the business premises. No  
21 state that imposes income taxes does not already provide such provision or, at least, a  
22 provision similar to Internal Revenue Code Section 119 for income tax withholding purposes.  
23 However, as stated by a report made to STAWRS:

24  
25 At present, 23 states treat meals and lodging as wages in their  
26 [unemployment insurance] laws and would be affected by this  
27 recommendation [to exclude meals and lodging from the compensation wage  
28 base]. These states include California (included in this study), New Jersey,  
29 New York, and Texas. They represent in excess of 26% of the nation's work  
30 force. In terms of impact on affected claims, analysis of California's data  
31 indicate the average benefit claim over its duration is \$2,433 and the average  
32 value of the exclusion of the meals and lodging component on affected  
33 claims is \$487, amounting to 20% of the claim of the workers affected. This  
34 percentage of reduction, or one close to it, could occur in New Jersey, New  
35 York and Texas as well.<sup>16</sup>  
36

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1 <sup>16</sup> Planmatics study, *supra*, note 7 at pg. v.

1 The report making the above quoted statement pointed out that in California this  
2 reduction represents only "...about 0.2% of the total benefit outlay, [however,] it represents  
3 almost a 20% reduction for the 7600 affected claimants. Additionally, 660 claimants, or 0.1%  
4 of the claimant population would lose their eligibility entirely."<sup>17</sup> Any attempt to harmonize  
5 the income tax withholding provisions with the unemployment insurance provisions within a  
6 given state will have to recognize the difficulty of dealing with these two different policy  
7 concerns. Of course, for those who have remuneration from their employers other than meals  
8 and lodging at, or in excess of, the maximum taxable unemployment insurance wage base the  
9 exclusion of the value of meals and lodging is of no consequence.

10  
11 As an example of this problem consider an employee who receives from an employer  
12 meals that qualify as exempt from income tax under statutory provisions similar to Section  
13 119 of the Internal Revenue Code<sup>18</sup>. Though the value of the meals is correctly excluded from  
14 the income tax withholding wage base it is considered income for purposes of establishing the  
15 unemployment insurance tax imposed on the employer and considered part of the wage base  
16 for determining an unemployed individual's unemployment benefits. Not all income for  
17 unemployment insurance purposes is income for tax withholding purposes.

18  
19  
20 (B) any payment made to, or on behalf of, an employee or the employee's beneficiary  
21 under a cafeteria plan under Section 125 of the Internal Revenue Code if the payment would  
22 not be treated as wages without regard to the plan and it is reasonable to believe that Section  
23 125 of the Internal Revenue Code would not treat the payment as included as taxable wages  
24 because of the constructive receipt of the payment;

### 25 Preliminary Comments

26 This provision provides that benefits otherwise excludeable from an employee's gross  
27 income and subject to income tax and unemployment insurance tax will not be considered  
28 includeable in either the income tax or unemployment insurance wage base merely because of  
29 constructive receipt issues. Section 125 of the Internal Revenue Code permits taxpayers to  
30 select from a group of benefits provided by their employer. Individually, these benefits are  
31 permitted, under the Internal Revenue Code, to be provided on a tax free basis to an  
32 employer's employees. Without the intervention of this code provision, however, the fact that

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1 <sup>17</sup> *Id.* at 34.

1 employees have the opportunity to select which tax free benefit, from a variety of offerings,  
2 they prefer to have is sufficient to make these otherwise tax free benefits taxable under the  
3 doctrine of constructive receipt. It appears that all states currently have extant a similar  
4 provision for income tax withholding purposes. However, many states do not exempt items  
5 paid under Internal Revenue Code Section 125 plans from tax liability (or benefit calculation)  
6 for unemployment insurance purposes. For any state that does not have a provision excluding  
7 from either wage base the items contemplated under Internal Revenue Code Section 125 it  
8 will be incumbent upon that jurisdiction to adopt such a conforming provision. In the absence  
9 of such provision in the unemployment insurance arena such amounts will be a component of  
10 the unemployment insurance wage base.

11  
12  
13 (C) remuneration paid to, or on behalf of, an employee for moving expenses if at the  
14 time of the payment it is reasonable to believe that a corresponding deduction is allowable to  
15 the recipient under Section 217 of the Internal Revenue Code, as determined without regard to  
16 Section 67 of the Internal Revenue Code, or is excludable from the employee's federal gross  
17 income under Section 132(a)(6) of the Internal Revenue Code;

#### 18 **Preliminary Comments**

19 This provision requires the exclusion from the wage base for purposes of income tax  
20 withholding and unemployment insurance tax and wage base calculation amounts paid for  
21 what are commonly referred to as moving expenses. All states that impose income taxes  
22 already provide such a provision except for two states with no provision. Generally it can be  
23 presumed that employer paid or reimbursed moving expenses will be paid primarily to those  
24 whose regular wages already exceed the maximum unemployment insurance wage base.  
25 Thus, this provision should have no impact on the benefits payable to any employee receiving  
26 unemployment benefits nor any employer's unemployment insurance tax liability even if a  
27 state's deductions or exclusions are not as generous as those provided under the Internal  
28 Revenue Code.

29  
30  
31  
32 (D) premiums paid by an employer for group-term life insurance on the life of an  
33 employee to the extent the premium is excluded from the employee's federal gross income  
34 under Section 79 of the Internal Revenue Code;



1 **Preliminary Comments**

2 There is no state that imposes either an income tax or an unemployment insurance tax  
3 that does not have either a provision similar to this provision or has no provision that would  
4 subject such premiums to income tax or have implications on their unemployment insurance  
5 regime.  
6

7  
8  
9 (E) payments made to an employee by an employer as an employee achievement  
10 award as defined in Section 274(j) of the Internal Revenue Code;

11 **Preliminary Comments**

12 Employee achievement awards are small awards given to employees for achievement in  
13 longevity or safety. For federal income tax purposes, if awards are not pursuant to a written  
14 plan, the sum of all achievement awards paid to any one employee during any year that the  
15 employer can deduct as a business expense cannot exceed \$400 per year. If awards are made  
16 pursuant to an established written plan or program that does not discriminate in favor of  
17 highly paid individuals (i.e., a qualified plan), then the sum of all achievement awards paid to  
18 an employee during any year that the employer can deduct as a business expense cannot  
19 exceed \$1,600 (including any awards from a non-qualified plan).  
20  
21

22 (F) payments paid by an employer for insurance or annuities or into a fund to provide  
23 for any payment made to, or on behalf of, an employee or any of the employee's dependents:

24 (i) because of sickness, if not mandated under [this state's workers' compensation  
25 law], made after six calendar months following the month in which the employee ceased  
26 working for the employer, if it is reasonable to believe that the payments are not subject to  
27 taxation as income to the recipient of the payments under [the income tax laws of this state];  
28 or

29 (ii) under a plan or system maintained by the employer which makes provision for  
30 the employer's employees, or the employees' dependents, generally or for a class or classes of

1 the employer's employees, or for a class or classes of employees and their dependents, on  
2 account of:

3 (I) sickness, if mandated under [this state's workers' compensation law];

4 (II) disability resulting from an accident and received under [this state's  
5 workers' compensation law] if it is reasonable to believe that it is not subject to income  
6 taxation to the recipient of the payments [the income tax laws of this state];

7 (III) medical or hospitalization expenses in connection with sickness or a  
8 disability resulting from an accident; or

9 (IV) death;

10 (iii) Notwithstanding the subparagraphs (i) and (ii), if an employee makes an  
11 election in writing to have income tax withheld on any payment of sick pay, the payment shall  
12 be considered wages for purposes of withholding of income taxes;

13 (G) a payment or series of payments made to an employee, or any of the employee's  
14 dependents, for death or disability which:

15 (i) is paid on or after the termination of an employee's employment with the  
16 employer because of the employee's death or retirement due to disability; and

17 (ii) would not have been paid if the employee's employment had not been so  
18 terminated;

19 (H) a payment made by an employer to a survivor or the estate of a former employee  
20 after the calendar year in which the employee died;

### 21 **Preliminary Comments**

22 In general only income from sick pay or wage continuation plans maintained by the

1 employer but not mandated by a state's workers' compensation law are included in an  
2 employee's income wage base for purposes of either income tax withholding or  
3 unemployment insurance benefit determination or tax assessment . Amounts paid due to an  
4 employee's death but are considered income in respect of a decedent (as defined at Internal  
5 Revenue Code Section 691)are not excluded and this act does not intend to change that  
6 treatment.

7  
8  
9  
10 (I) a payment made or the value of benefits provided which afford an employee  
11 dependent care assistance pursuant to a qualifying dependent care program if, at the time of  
12 the payment or provision of the benefit, it is reasonable to believe the payment or benefit is  
13 excludable from the employee's federal gross income under Section 129 of the Internal  
14 Revenue Code;

#### 15 **Preliminary Comments**

16 This provision excludes the value of benefits provided by an employer to an employee  
17 under an employer provided dependent care plan providing non-discriminatory access to  
18 dependent care for young children who are dependents and dependent adults who are unable to  
19 care for themselves due to physical or mental incapacity. It is intended that these individuals  
20 be the same as those defined as "qualifying individuals" at Internal Revenue Code Section  
21 21(b)(1). It is further intended that the State statutory provisions will require a written, non-  
22 discriminatory plan similar to that under and meeting the requirements of Internal Revenue  
23 Code Section 129. Inclusion of this provision will require many states to adopt dependent  
24 care provisions not currently extant. Currently, 42 states have concurring statutes for income  
25 tax withholding and 1 state has no provision (9 states have no income tax). On the  
26 unemployment insurance side of the ledger, however, only 15 states' statutes conform to these  
27 requirements, and 35 states have no provisions dealing with this issue. Two states, Alabama  
28 and Michigan provide that payments made directly to the care giver or care facility are not  
29 wages to the recipient employee while benefits provided through a wage reduction plan are  
30 considered wages to the recipient employee (presumably because of some degree of  
31 constructive receipt).

32  
33  
34  
35 (J) fringe benefits provided to or for the benefit of an employee if, at the time of  
36 provision or reimbursement, it is reasonable to believe that the benefit is excludable from the

1 employee's federal gross income under Section 132 of the Internal Revenue Code;

## 2 **Preliminary Comments**

3 Of those jurisdictions imposing an income tax forty-two have provisions that provide this  
4 treatment for purposes of income tax withholding and one state has no provision. For  
5 purposes of unemployment insurance withholding only thirty-three states have provisions  
6 similar to this provision. Ten states currently have no or minimally matching provisions.  
7  
8

9 (K) a payment that reimburses expenses incurred on behalf of an employer or as an  
10 allowance provided by an employer for, but not in excess of, those expenditures that meet the  
11 requirements of Section 62(a)(2)(A) of the Internal Revenue Code and that are not in excess of  
12 the lesser of the allowance or the substantiated expenses incurred by the employee for the  
13 expenditures;

## 14 **Preliminary Comments**

15 Though the THWC report indicates that all states provide this exclusion for both income  
16 tax and unemployment insurance tax purposes, there are numerous states that do not currently  
17 comply with the reporting requirements set out in the Internal Revenue Code. If those states  
18 should adopt reporting requirements similar to those mandated for federal tax purposes no  
19 additional compliance costs would be incurred by employers or employees who are currently  
20 complying with the federal requirements.  
21

22 (L) a payment made to, or on behalf of, an employee or the employee's beneficiary  
23 from or to a plan or plans described in Section 3306(b)(5)(A) through (F) of the Internal  
24 Revenue Code;<sup>19</sup>  
25

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1 <sup>19</sup>

2 These are payments from deferred compensation plans that are defined at Section C. of Article  
3 II. of the act.

1 **Preliminary Comments**

2 This provision deals with contributions to pension, profit-sharing and similar  
3 arrangements that meet the requirements for tax exemption under Sections 401 and 501 of the  
4 Internal Revenue Code. All states provide similar exclusions for both income tax and  
5 unemployment insurance tax purposes but the provisions for many states are complex and  
6 could be simplified. It should be noted that these amounts are subject to FICA taxes when  
7 contributed to such a plan.  
8  
9

10 (M) a payment made to an employee as the result of the employer's transitory passage  
11 through this state while engaged in the interstate transportation of goods or people;

12 (N) a payment made to an employee for services performed outside of this state if, at  
13 the time of the payment, it is reasonable to believe that the payment is excludable from the  
14 employee's gross income under [the statutes of this state] for income tax or unemployment  
15 insurance purposes;

16 **Preliminary Comments**

17 Forty six states have adopted provisions similar to this provision. At present no state  
18 imposes an income tax on wages earned by and paid to a state resident while out of state. If a  
19 State did include such income in its taxable base, it would be impossible to enforce a  
20 withholding requirement on a foreign corporation that had no presence in the state, but it could  
21 enforce withholding requirements on any corporation that is present in the state. Additionally,  
22 if a state exercised jurisdiction over a corporation and chose to include this income in the  
23 unemployment wage base there would be an impact on an employee's benefit wage base as  
24 well as an imposition of unemployment taxes on the employer.  
25  
26  
27

28 (O) an amount paid for a scholarship or fellowship by an employer to an employee or  
29 a dependent of the employee who is a candidate for a degree at an educational organization  
30 described in Section 170(b)(1)(A)(ii) of the Internal Revenue Code and used by the individual

1 for qualified tuition and related expenses, as the terms are defined in Section 117(b) of the  
2 Internal Revenue Code;

3 (P) any reduction in tuition provided by an employer that is an organization described  
4 in Section 170(b)(1)(A)(ii) of the Internal Revenue Code to an employee of the employer,  
5 including a retired and disabled employee and the surviving spouse of a deceased employee, or  
6 a dependent of the employee for the education, below the graduate level, of the employee or  
7 dependent of the employee at the organization or another organization described in Section  
8 170(b)(1)(A)(ii) of the Internal Revenue Code; and

### 9 Preliminary Comments

10  
11 Arizona, California, Indiana, Ohio, Kansas, and Mississippi are the only jurisdictions that  
12 have provisions comparable to this one. None of the other States or the District of Columbia  
13 have any provision dealing directly with this issue, though discussions with the STAWRS  
14 team indicates that most states currently follow the federal rule through administrative policy.  
15

16 The language of this provision is largely the same language of Internal Revenue Code  
17 Sections 117(a) and (b). Thus, like the federal law, this provision is intended to exclude from  
18 an individual's gross income only those amounts which are used to pay for tuition, fees,  
19 books, supplies and equipment required for enrollment at, or to take courses pursuing a degree  
20 at, "an educational organization which normally maintains a regular faculty and curriculum  
21 and normally has a regularly enrolled body of pupils or students in attendance at the place  
22 where its educational activities are regularly carried on..." Internal Revenue Code Section  
23 170(b)(1)(A)(ii).  
24  
25  
26

27 (Q) an amount paid to an individual for jury service by a court, or by a governmental  
28 entity on behalf of a court.

### 29 Preliminary Comments

30 All states exclude this payment from income tax withholding requirements as well as  
31 unemployment insurance purposes. However, some states accomplish this exclusion by  
32 excluding such payments from the definition of wages and others simply exclude jury service

1 from the definition of employment. For those taking this later approach, this provision will  
2 require them to amend that portion of their statutes to conform to a treatment of these  
3 payments as exclusion from the definition of wages.  
4

### 5 **SECTION 3. FILING AND PAYMENT DATES.**

6 (a) All employment taxes must be reported quarterly unless it is reasonable to believe  
7 that the total amount owed by the employer for the entire calendar year will not exceed  
8 \$2,500, in which case the employment taxes must be reported annually.

9 (b) All reports of employment taxes must be filed and submitted to [insert state rule]  
10 on forms, or electronically, as prescribed by [the responsible state agency].

11 (c) All payments of employment taxes must be made by the employer by check,  
12 electronically, or any other form as required by [insert appropriate state agency].

13 (d) All payments of employment taxes must be made to the [insert appropriate state  
14 agency] as follows:

#### 15 **Preliminary Comments**

16 This provision anticipates a rather substantial administrative change in States' physical  
17 collection of withholding and unemployment insurance taxes. Currently, these taxes are  
18 collected by two separate entities – the income taxing authorities and the entity responsible  
19 for administering the unemployment insurance law. As drafted, this section of the act would  
20 require the collection function to be conducted by the same agency or department which  
21 would then be responsible for the ministerial act of properly allocating the funds between the  
22 State's income taxing authority and the department responsible for enforcing the State's  
23 unemployment compensation law.  
24

25 Ideally, this same "collection" agency will be able to verify compliance with both the  
26 income tax withholding and unemployment insurance tax laws because there will be no  
27 divergence between those laws regarding the definition of wages; at least to the extent of the  
28 conforming items set out in this act.  
29  
30  
31

1 (1) if the total amount owed at the end of a calendar year is no more than \$2,500, no  
2 later than January 31 of the following year;

3 (2) if the total amount owed on June 30 or December 31 is greater than \$2,500, but  
4 no more than \$5,000, no later than the end of the calendar month following the June or  
5 December in which the amount exceeds \$2,500;

6 (3) if the total amount owed is greater than \$5,000, but no more than \$50,000, no later  
7 than the 15<sup>th</sup> day of the calendar month immediately following the month in which the amount  
8 exceeds \$5,000;

9 (4) if the total amount owed is greater than \$50,000, but no more than \$100,000, no  
10 later than the third business day immediately following the Friday of the week in which the  
11 amount exceeds \$50,000; and

12 (5) if the total amount owed is greater than \$100,000, no later than three business days  
13 following the day the amount exceeds \$100,000.

#### 14 **Preliminary Comments**

15 In general payment thresholds and dates as well as filing dates for both withheld income  
16 taxes and unemployment insurance taxes are specified by statute only in general terms. The  
17 specifics are left to the various concerned administrative agencies. However, to enhance the  
18 possibilities of conformity, this recommended provision is set forth with greater detail than is  
19 found in most current state statutes.

20  
21 Analysis of the various States' filing requirements and payment thresholds show a wide  
22 variety of dates and amounts. In fact, there are approximately 90 different threshold amounts  
23 and 109 different filing dates among all the 50 States and the District of Columbia.  
24 Employers are unlikely to have to deal with more than a few jurisdictions and/or more than a  
25 few payment threshold amounts. Consequently, any multi-state employer likely will have far  
26 fewer than the nearly 200 different filing and payment requirements. Nonetheless, the  
27 multitude of dates and amounts with which any one employer may need to comply under the  
28 current state of the law is daunting. Further, the burden on small employers doing business in  
29 more than one state can be dramatic because the cost of keeping track of the various filing and



1 payment dates in relation to the size of the employer may be high.

2  
3 In any event, ignoring transition problems (which may, in some cases, be  
4 insurmountable), common dates for compliance will greatly ease burdens imposed on all  
5 employers. Further, the costs of auditing and assuring compliance incurred by the States  
6 presumably will be reduced simply because complexity is reduced.

7  
8 This provision also does not provide for a look back period as does the Internal Revenue  
9 Code and some state withholding statutes. A look back provision permits payors to base  
10 their payment thresholds, and thus frequency of payment of taxes, on prior year compensation  
11 history. Because the income taxes withheld and the taxes owed for unemployment insurance  
12 purposes are based upon current compensation, it does not appear that look back rules are  
13 essential to timely and accurate compliance with the payment rules. In an era of instant  
14 information and computerized payroll systems, it does not appear that essential data for proper  
15 compliance is difficult to aggregate. On the other hand it is recognized that payments based  
16 upon current payrolls may cause cash management problems for employers which have  
17 significantly fluctuating payrolls. Nonetheless, payments based upon current compensation  
18 rather than look back estimates will make it less likely that employers will become in arrears  
19 in payments of their Trust Fund obligations (i.e., their obligations to pay over withholding  
20 taxes). For large taxpayers, at least for federal taxes, this is not an issue because regardless of  
21 any look back rules at any time an employer has accumulated \$100,000 of payroll taxes they  
22 must be paid over to the government by the next business day after such accumulation. For  
23 mid-size taxpayers, particularly those with quickly growing business or those the business of  
24 which is highly volatile, the problem of temptation to use rather than pay over Trust Fund  
25 monies may cause them much difficulty and deprive the government of monies owed.

#### 26 27 28 29 **SECTION 4. EFFECTIVE DATE AND TRANSITION RULES**

30 (a) The effective date of this [Act] is \_\_\_\_\_.

31 (b) Reserved