



National Payroll Reporting Consortium

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American Payroll Association

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March 11, 2011

Mr. Steven J. Fishman
Chief Counsel
Department of Economic and Community Development
400 North Street
Plaza Level
Harrisburg, PA 17220-1225

Re: Early Implementation of 2008 Act 32

Dear Mr. Fishman:

Thank you for your time and hospitality on March 2nd. We appreciated the opportunity to discuss employer concerns with early implementation of Act 32 of 2008, which reformed the Pennsylvania local Earned Income Tax collection system. Employers and employer associations were closely involved in support of Act 32, which represents a significant improvement over the prior EIT collection system. However, employers are facing unrealistic burdens during this transitional year because a handful of Tax Collection Districts (TCDs) are mandating Act 32 compliance in 2011. We sought DCED's assistance in clarifying what elements of Act 32 could be implemented early on a mandatory basis, and are recommending three measures that would facilitate the transition through 2011.

Background

The American Payroll Association (APA) is a nonprofit professional association representing more than 21,000 payroll professionals and their companies in the United States and Canada, including thousands of companies with employees in Pennsylvania. The APA's primary mission is to educate its members and the payroll industry regarding best practices associated with paying America's workers while complying with applicable federal, state, and local laws. In addition, the APA's Government Affairs Task Force works with the legislative and executive branches of government to find ways to help employers satisfy their legal obligations, while minimizing the administrative burden on government, employers, and individual workers.

The National Payroll Reporting Consortium (NPRC) is a non-profit trade association whose member organizations provide payroll processing and related services, including electronic filing of periodic payroll withholding and related employment tax reports, to over 1.4 million employers nationwide, covering over one-third of the private sector workforce. Payroll service providers serve an important role in our nation's tax collection system as a conduit between employers and government tax authorities, improving the efficiency of tax collection through electronic filing and improving compliance.

Employers and payroll service and software providers are diligently working on extensive software changes and taking the steps necessary to convert employees over to the new system in 2012. However, a poorly understood clause inserted in the final moments of Act 32 is being used to accelerate diverse employer mandates to January 2011. Announcements are being issued from various tax collectors that appear to demand retroactive implementation effective

January 1, 2011, which would pose unreasonable difficulties and financial liabilities.

The prior tax regime was famously complex and burdensome. The new Act 32 EIT system will also require significant investments in software development and employer involvement. However, the prospect of a *combined and mixed* regime of old and new rules that vary across geographical areas during the transition year would require systems development of the same magnitude as the overall Act 32 changes, just to accommodate the transition year, after which it would be discarded.

Although employers and the payroll services industry were aware that there could be early adopters, the early adoption TCDs list has changed several times based on information provided to the Department by the Tax Collection Committees (TCCs). In addition, new information continues to be released by the TCCs and their appointed tax collectors, and several have announced intentions to implement Act 32 in 2011 on a mandatory basis. Significant penalties apply for noncompliance with the provisions. Some of the TCDs have issued announcements that leave employers and service providers with the understanding that immediate and full compliance is expected, and that significant penalties will result for less than full compliance; e.g.,

“Act 32 includes significant fees and penalties on employers for not withholding, non-reporting and incorrect reporting. During 2011, LCTCB will consider waiver of penalties for employers that are in good faith attempting to comply with the requirements of Act 32”.

- Lancaster County Tax Collection Bureau announcement – January 26, 2011
http://www.lctcb.org/employer-act-32/employer_letter_01_26_2011.pdf

EIT withholding is administered on an annual basis. That is, employers are expected to withhold the appropriate tax in relation to the total wages paid to each worker for an entire year. Withholding tables are typically published in late fall so that payroll systems have the new rates for January payrolls. In this case, significant announcements have been issued in late January with retroactive effect, leaving employers with the expectation that they must recalculate all prior payrolls and adjust tax collections. This is extremely burdensome and costly, and in some cases may not be possible; for example for employees who have since left the company.

Transition-year difficulties would defeat the purpose of Act 32, which was to simplify and rationalize Pennsylvania's local Earned Income Tax collection system. The previous system was widely acknowledged to be onerous for employers, and Act 32 promises to improve the system significantly for all involved. However, the prospect of a mixed system in the transition year would create complexities that would be prohibitively expensive to overcome. Examples of some of the most challenging issues include:

1. The mix of rules. If an employee is working in an early adopter county, they must be coded with the appropriate worked in and lived in codes in order to deduct the correct tax and remit to the correct collector. But an employee working in a non-early adopter county cannot be coded that way if the employer does not have a relationship with the lived in jurisdiction because we will automatically apply today's reciprocity rules for taxing and remitting. For Payroll systems to have to determine taxing rules on an employee level based on some hard coded interim rules is contrary to most rules-based statutory logic payroll providers have in place today.

For example, Bruce Phipps of the APA explained that his organization currently has doctors who in any given payroll period may work in as many as six different tax jurisdictions and different counties. The added complexity of early adopters vs. non-early adopters would make this an accounting nightmare.

For employees that work in an early adopter county but live in a non-early adopter jurisdiction, how would the employer determine which rate to withhold in 2011? How would the TCD know where to send the taxes that were withheld for the employee if their lived in county was not an early adopter? This will add much confusion to the process in 2011 and complicate W-2 reporting for employees. Generally, diverse rules, forms and announcements have added significantly to employer confusion. For example, at least one TCD will require that withholding certificates be filed with their office rather than be held by the employer, which is another reporting burden and liability. Employers would benefit from guidance from the Department as to which tax collection districts have recognized authority to enforce Act 32 in 2011.

2. The significant effort required by employers. Each employer having workers in one of the early adopter counties must solicit new employee Resident Certifications from every Pennsylvania employee, look up the applicable Political Subdivision (PSD) code, and change each employee's records within their payroll system. For large employers in particular, this is a time consuming task which must be completed before their last payroll of the first quarter is processed. This could create a high volume of amendments, which are costly for both employers and tax authorities to process. For the changes the industry is already working on for 2012, clients are generally being provided with at least four or five months to make the appropriate changes to each employee's payroll files. This time frame is not possible for the early adopters.
3. Generation of filing information and W-2s. Significant changes are required to support the remittance requirements and the W-2 reporting requirements. Today, we generate W-2s for the localities where the tax was deducted. Act 32 requires the W-2 be generated for the worked in location regardless of where the tax was deducted. This may seem easy, but with employees moving from one jurisdiction to another during the course of the year, some work may be in early adopter localities and some may not. W-2 logic must be completely revamped.

In some scenarios, expectations are unclear on what should be displayed on Forms W-2; e.g., what PSD code(s) to use as the employee's worksite PSD code when an employee works in more than one location (more on this in the appendix). DCED Regulations should include a sample presentation of the individual withholding statement described in Section 512(7)(ii) of the Act that requires reporting, among other things, of income tax paid to the tax officer and the numerical code of the tax collection district where the payments were remitted.

Another requirement that should be clarified is Section 512(7)(i), concerning W-2 Withholding statements. This section appears to require separate display of amounts withheld and amounts paid to the tax officer. Normally the two amounts are always the same; and in any event payroll systems are usually not directly linked to tax payment systems. In other words, if there was a difference, the W-2 would not be the appropriate form on which to show a discrepancy. To our knowledge, no other federal, state or local tax authority requires both elements on the W-2.

4. The late implementation of early adopting jurisdictions presents employers with a dilemma on how to go back and withhold at the higher rate from employees, which can be difficult if an employee is no longer with a company. Many announcements indicate that employers are now responsible for the higher-rate withholding during the transitional year of 2011.
5. Monthly reporting – Some TCD announcements appear to mandate monthly reporting for certain large or multi-site employers, with detailed employee information, such as names, SSNs, wages and withholding. Act 32 provides for monthly reporting as a voluntary alternative available for multi-site employers that prefer to report to a single TCD. Monthly deposits of total EIT withholding are not a problem, but payroll systems are not designed to produce detailed reporting of employee-level detail more often than quarterly.

Recommendations:

The payroll services industry, American Payroll Association and other interested organizations are seeking assistance from the Department of Community and Economic Development, state policymakers and other interested officials to clarify that any implementation of Act 32 in 2011 must be on a voluntary basis. We have identified three measures that would facilitate the 2011 transition year. We would appreciate the Department's assistance in issuing guidance to the TCDs on the provisions of concern.

1. No enforcement of the "higher of the two rates" EIT collections under Act 32 from the employer

As explained above, EIT withholding is administered on an annual basis. Employers are expected to withhold appropriate tax in relation to the total wages paid to each worker for the full year. TCD announcements were being issued in late January with retroactive effect, leaving employers with the expectation that they must recalculate all prior payrolls and adjust tax collections.

Additionally, a number of TCDs have made ambiguous offers of relaxed enforcement for part of the year; e.g., through June. It is not clear what this would mean. As a practical matter, employers would recognize potential liability for any differences in full-year withholding compared to full-year wages.

It is also not helpful to offer consideration waiver of penalty on a case by case basis. Employers are extremely alarmed because of the various announcements. TCDs could be flooded with requests for advance determinations from each employer, as they recognize the gap between transition-year requirements and their capabilities.

We believe that under the 2008 Act 32, and the prior EIT system, the ultimate liability for income taxes rests with the employee. Employers will adopt the new Act 32 withholding rates and systems as quickly as possible; but we ask that DCED and all TCDs recognize that if there is underwithholding at the end of 2011, TCDs should collect the difference from the employee, not the employer.

2. No requirement for PSD codes in 2011

As mentioned above, employers need time to solicit and collect new employee Resident Certification Forms and change each employee's records within their payroll systems. Employers will also need to manually look up corresponding PSD codes for each employee address. Many systems have not yet been modified to store these codes. Employers may have to store this data separately and somehow merge it with any reports that are produced for the TCD. This would involve a tremendous amount of manual work.

Employers should be asked to provide PSD codes if possible; however, quarterly reports and annual W-2s should be accepted without them for the 2011 transition year, without penalties.

3. Monthly reporting of detailed employee-level wage and withholding information should be on a voluntary basis.

Current systems are not designed for monthly reporting. All payroll reporting of employee information at the federal, state and local level is quarterly or annually. The quarterly payroll summarization and reporting process is extensive. It takes 30 days to perform all the necessary data collection, processing, balancing, formatting, and editing necessary to produce quarterly tax reports. Monthly reporting would represent a very costly and sweeping change to administrative systems. If required, employers would probably have to handle it manually for 2011. Some payroll systems might never adopt such a costly change, and would simply not offer support for monthly local tax reporting. It should be clarified that monthly reporting is voluntary.

It is not an overstatement to say that it would be effectively infeasible for many employers and service providers to implement Act 32 in 2011, for reasons explained (in part) above. If enforced, employers in those TCDs would likely need to develop entirely separate and manual recordkeeping systems for 2011. Many automated payroll systems could be unable to support Act 32 in 2011.

Again, we appreciated the opportunity to discuss our concerns with early implementation of Act 32. We continue to support the Act and believe that it represents a significant improvement over the prior EIT collection system. It is urgent; however, that certain provisions be clarified as quickly as possible concerning early implementation on a mandatory basis. Pennsylvania employers are diverting significant productive resources now in an effort to comply with recent announcements. DCED's assistance is vital in ensuring that Act 32 has the intended result of simplifying Pennsylvania local EIT collections and reporting for employers. We look forward to working with you and other stakeholders to ensure an orderly implementation. Thank you.

Sincerely,



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Appendix: Temporary Presence Rules

The American Payroll Association has received many calls from Drilling and construction companies asking how to handle withholding for employees who may be in a location for several weeks at a time and then move on to the next location. This raises another opportunity for DCED guidance, although it is not as time-sensitive as the three requested measures:

- There should be clear rules about how long an employee can work in a TCD before employer withholding and reporting obligations are invoked. We recommend no less than 60 days.
- Otherwise employers will face diverse and conflicting rules throughout the state, as TCDs seek to maximize collections by announcing increasingly stringent withholding requirements; e.g., one week, or one day.
- This would not only be extremely difficult for employers, but employees/ taxpayers who occasionally work in other locations would then receive potentially dozens of W-2s and may be required to file as many income tax returns.