

The Legal Review

Sharing Case Law that Affects the Household Employment Industry

A Complimentary Resource from
Breedlove & Associates

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In an effort to help you strengthen your business practices and steer clear of legal trouble, The Legal Review will share findings from relevant legal cases. We've found that the easiest way to gain a practical understanding of complex tax and labor law is by reviewing real-life situations. These stories will illuminate potential legal landmines for your agency and/or your clients, and more importantly, show you how to avoid them.

Nanny vs. Family: Income Tax Payment on April 15th

Not many people understand taxes. They are withheld from our wages; they are paid to the government throughout the year by our employers; we reluctantly prepare our income tax returns by April 15th each year; and finally, when the dreaded paperwork is completed, we hold our breath hoping for a refund rather than a payment – although the vast majority of us have no idea how or why it worked out that way.

This month we highlight a case that provides some basic information about income taxes that we all should know. Today being April 15th, we thought it was an appropriate time to share the story. Hopefully, it will prevent some confusion and frustration for nannies and families at “tax time.”

The Lack of Understanding

Last year on the tax deadline, a nanny prepared her federal income tax return (Form 1040) and determined that she owed \$225.00 in income taxes. Upset by the surprise payment, she demanded that her employer pick up the bill.

The Law

Income tax withholdings are calculated using gross wages, an employee's filing status from Form W-4, and the tax tables provided by the IRS and the state. The tax tables and the method used in determining filing status are not exact. The IRS states that if the annual Form 1040 produces a refund or a payment within \$500.00, income tax calculations and withholdings throughout the year were successful. Many young taxpayers expect to come out “even” because they assume that the withholdings reflect a precise pre-payment of their tax liability. Meanwhile, the IRS views the withholding and pre-payment process as a rough, ballpark estimate. To them, “even” is within \$500.

The Mess

- A family paid their nanny legally, withheld her taxes appropriately per her filing status documented on Form W-4, and paid all household employment taxes on a timely basis through Breedlove & Associates' services. This was a picture-perfect situation. What could possibly go wrong?
- When the nanny filed her Form 1040 on April 15th, she owed an income tax payment of \$225.00. She became very frustrated with her employer, as she “understood” that all tax withholdings had been taken care of and she demanded that her employer pay her tax bill.
- The employer contacted Breedlove & Associates and demanded that we pay the bill. They felt that they met their responsibilities by withholding and remitting household employment taxes throughout the year.

- No one seemed to understand that every tax-paying American ends up with some form of a tax payment or tax refund on April 15th. Coming out exactly even has about the same statistical probability as winning the lottery. Think about it...have you ever heard ANYONE say, 'I hit zero right on the nose. I don't have a payment and I don't get a refund. I came out *exactly* even.'

The Outcome

- The family was correct. It was not their responsibility to pay their nanny's income tax bill.
- Breedlove & Associates withheld income taxes correctly using the tax tables and the nanny's filing status provided on Form W-4. It was not our responsibility to pay the nanny's income tax bill.
- So who was responsible for the income tax bill? The nanny.
- Breedlove & Associates explained to the family the details of the income tax withholding process, plus the fact that the nanny's income tax return was well within the IRS's acceptable range.
- Breedlove & Associates also explained this in detail to the nanny. Our goal was to help the nanny understand that she needed to plan for a small payment or refund on her annual income tax returns for the rest of her life. She paid her own tax bill. Meanwhile, we walked her through an adjustment to her Form W-4 so her withholdings would be more conservative. This year, because she paid a little more in taxes each pay period, she'll likely be getting a small refund.

How the Whole Thing Could Have Been Avoided

There is no simple solution. Because tax management is not taught in schools or explained well by the IRS, almost all young workers go through an adjustment the first few times they file their income tax returns. Remember those days?

Breedlove & Associates will continue to educate as completely as possible. Placement agencies should remember that payroll and tax education is as important for candidates as it is for families. We've tried to make this easy with our educational piece written specifically for household employees, *The Benefits of Being Paid Legally*. The more we educate both families AND candidates the more professional our industry will become.

To help your clients understand the tax obligations for both employer and employee, we have developed a simple educational flyer entitled "Tax Law 101". The flyer can be downloaded from <http://www.breedlove-online.com/partners/library-of-educational-literature-helpful-tools> along with our other helpful resources. Or feel free to invite your clients to call us for a complimentary, no-obligation phone consultation. In about 10 minutes, we can assess their situation and give them comprehensive household employment tax guidance. Whether they sign up with our service or not, we'll make sure this kind of ugly situation never happens to one of your clients.

If you would like hard copies of our "Tax Law 101" flyer, just send an email to info@breedlove-online.com.

If you have additional questions, please call 888-BREEDLOVE (273-3356) or visit www.breedlove-online.com. We're here to help our agency partners provide their candidates and clients with information, tools and resources that improve the employment relationship, eliminate legal risk for all parties, and increase the professionalism of the industry.

