



US tax reform

Update on payroll implications for businesses: IRS issues new withholding guidance



Overview

Following the passage of the US tax reform legislation in December 2017 (formally referred to as “An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018”) (“the Act”), employers have been eagerly awaiting withholding guidance to be issued by the Internal Revenue Service (IRS) in order to implement the tax rate changes for income tax withholdings via payroll.

On January 11, 2018, the IRS issued [Notice 1036](#) for 2018 (the “Notice”), along with an [explanatory statement](#) and [FAQs](#), to provide some important clarifications for employers. However, it is clear from the information released that the impact of tax reform will continue to affect employers and employees for a number of months.

What has changed with withholding rates?

Included in the Notice are highly anticipated changes in supplemental rates:

- The mandatory flat rate for supplemental wage payments exceeding \$1 million USD has been confirmed at 37%.
- The sub-\$1 million USD wage withholding rate has been reduced to 22%.
- The backup withholding rate is now 24%.

Withholding tables were adjusted to reflect the 2018 changes in individual income tax rates included in the Act.

Changes are not retroactive and are expected to be applied from the date at which they are implemented by employers, but no later than February 15, 2018.

What about Forms W-4?

The IRS previously stated that any withholding guidance would be designed to work with existing Forms W-4. Further details are provided in support of that original statement:

- Employees will not be required to complete revised Forms W-4 for 2018.
- Employees are encouraged to review their withholding positions to ensure they are accurate.
- A new withholding allowance calculator will be released on the IRS website (IRS.gov) by February 28, 2018, to support employees in reviewing their withholding levels.
- A new Form W-4 will be issued shortly to more fully reflect the new tax law and provide employees more detailed guidance on how to change their tax withholdings.
- In 2019, the IRS anticipates making further changes involving withholdings and has stated it will work with the business community to encourage employees to file revised Forms W-4 in 2019.



Deloitte's view

The confirmation of the position on supplemental rates will be welcome news to employers, withholding agents, and stock plan administrators who are updating systems to reflect the new withholding rates. A diversity in withholding positions for equity and bonuses had begun to surface in early 2018 among vendors and providers prior to the IRS guidance..

The IRS's expectation that changes be implemented by February 15, 2018 may cause challenges, especially considering many employers and payroll providers are also currently engaged in extensive year-end activities for 2017. Employers who rely on third-party payroll providers to implement and execute the changes may have an easier time adapting to the changes than those who handle payroll exclusively in-house. Of course, employees will want to see the changes reflected in their paylips as soon as possible.

Employees whose withholding allowances will be affected by tax reform may have a number of questions about how to adjust their withholding positions. These will be difficult to answer until the IRS's calculator is released at the end of February. Although the IRS has stated employees do not need to complete new Forms W-4, given the changes to individual tax rates, deductions, and exemptions, it seems likely that employees may want to submit new Forms W-4 to adjust their withholding positions. Implementing the various changes and addressing employees' questions could result in considerable additional work for payroll departments in the months to come.



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