IRS 2018 Form W-4 and New Withholding Calculator Released

On February 28, 2018, the Internal Revenue Service (IRS) released a revised Form W-4, Employee's Withholding Allowance Certificate, for 2018, as well as an online “Withholding Calculator.” Employers should consider notifying employees of the new IRS Form W-4 and Withholding Calculator to help employees determine whether they should change their withholding allowances for 2018.

Background

The Tax Cuts and Jobs Act (TCJA) made significant changes to tax rates, deductions, tax credits, and withholding calculations, beginning in 2018. New IRS withholding tables were published on January 11, directing employers to begin using them no later than February 15. All ADP® systems implemented the 2018 withholding calculations in the week following the IRS release, so payrolls processed after January 18 generally reflected the new tables.

Employees use the Form W-4 to establish marital status and withholding allowances for federal income tax withholding calculations. Additionally, many states permit use of the Federal Form W-4 for state withholding purposes. The IRS will not require all employees to file a new Form W-4 for 2018. However, for some people it may be advisable.

How the Tax Cuts and Jobs Act Affected Withholding

For most people, the TCJA will result in a tax reduction, and many have noticed reduced federal income tax deductions and a corresponding increase in net pay. However, even though the 2018 withholding tables were designed to be as accurate as possible, changes to withholding may not correspond closely to changes in actual full-year income tax liability. In some circumstances, even employees that ordinarily receive an IRS tax refund may find that they owe additional tax to the IRS in early 2019 (for tax year 2018).

Unless an employee has already filed a new Form W-4 in 2018, tax withholding calculated for 2018 payrolls could be based on outdated withholding allowances. Most significantly, the law eliminated personal exemptions. In 2017, each personal exemption (e.g., for the employee, any spouse and any dependents) reduced federal taxable income by $4,050 per person. In 2018, the value of personal exemptions is zero. The value of each withholding allowance is $4,150 for 2018, and to the extent that withholding allowances on file in 2018 represent personal exemptions, an employee’s withholding allowances may be overstated for 2018, which could result in tax under-withholding.

The new IRS tax tables adjusted for this and other factors to some extent, but because Forms W-4 permit withholding allowances based on factors such as expected tax credits and itemized deductions (such as mortgage interest, and state/local taxes), employers are not able to automatically adjust withholding allowances to eliminate personal exemptions.

Time for a “Paycheck Checkup”

With the release of the new online W-4 Calculator and revised Form W-4, the IRS will promote the concept of a “paycheck checkup,” to suggest that employees should use the online withholding calculator, found at https://www.irs.gov/individuals/irs-withholding-calculator to determine the correct number of withholding allowances (either adjusting for the TCJA, or for changes in personal circumstances).

The online IRS calculator will ask a number of questions about income, marital status, anticipated deductions and eligibility for tax credits, to estimate annual taxable income and suggest the most appropriate number of withholding allowances.

Prominent among IRS “Frequently Asked Questions” is the following:

Q: Should all employees check their withholding?
A: Yes. Employees should check their withholding at the beginning of each year or when their personal circumstances change. It’s even more important this year for people to do a “paycheck checkup” following the changes in the new tax law. With the new tax law, it’s especially important for people who have previously itemized their deductions, have two or more jobs in their household, or have dependents, to check their withholding. Using the Withholding Calculator is the best way to check that you aren’t having too much or too little tax withheld from your paychecks.
What to Do Now

Employers should consider notifying employees of the 2018 Form W-4 and withholding calculator. A sample letter follows.

Example Notice to Employees

Re: 2018 Income Tax Withholding

Dear ____________:

You may have noticed lower federal income tax deductions and a corresponding increase in net pay in your recent paychecks. The recent Tax Cuts and Jobs Act (TCJA) changed federal income tax rates and brackets, among other things, beginning in 2018. New IRS withholding tables were put into effect in late January.

The TCJA generally reduced federal income taxes for most people. However, depending on your specific tax situation, you might owe additional tax when you file your 2018 income tax return, even if you normally receive a tax refund from the IRS at year-end.

You may want to consider updating your withholding allowances at this time. The IRS recently released the 2018 Form W-4, Employee’s Withholding Allowance Certificate, and related instructions, which you can find at www.irs.gov/W4.

The IRS also offers an online “W-4 Calculator,” at https://www.irs.gov/individuals/irs-withholding-calculator. This calculator may help you determine the correct number of withholding allowances to claim.

The IRS will not require all employees to file a new Form W-4 for 2018. However, for some people it may be advisable. The TCJA made many other changes that could affect your 2018 income taxes. For questions regarding your personal tax situation, talk with your tax advisor, or visit www.IRS.gov.

ADP Compliance Resources

ADP maintains a staff of dedicated professionals who carefully monitor federal and state legislative and regulatory measures affecting employment-related human resource, payroll, tax and benefits administration, and help ensure that ADP systems are updated as relevant laws evolve. For the latest on how federal and state tax law changes may impact your business, visit the ADP Eye on Washington Web page located at www.adp.com/regulatorynews.