

Eye On Washington

Regulatory Update



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IRS 2019 Form W-4 Represents Major Changes to Payroll

On June 6, 2018, the Internal Revenue Service (IRS) released a draft Form W-4, [Employee's Withholding Allowance Certificate](#), for 2019. Several changes are fundamental in nature, potentially requiring significant reprogramming of payroll systems. State and local tax authorities are also expected to respond with similar changes.

Background

Employees use IRS Form W-4 to establish marital status and withholding allowances for federal income tax withholding calculations. Many states use the Federal Form W-4 for state withholding purposes.

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 in January, and the 2018 Form W-4 was released in February. The IRS made few changes for 2018, and determined that employees would not be required to complete a new Form W-4 for 2018. However, it was strongly recommended and for some people it may be advisable.

Highlights of the Draft Form W-4 for 2019

Number of Allowances Eliminated

Perhaps the most prominent change on the 2019 Form W-4 is that Line 5, "Total number of allowances you're claiming," is eliminated.

Employees will be "strongly encouraged, but not required" to complete a new W-4 for 2019. Employers will still be able to use 2018 and prior Forms W-4 for employees that don't complete a 2019 W-4. As a result, payroll systems will need to maintain both 2018 and 2019 withholding systems and calculations simultaneously.

New Marital Status Box - Head of Household

A third IRS withholding calculation/table will be added to correspond with this new marital status, in addition to the existing tables for Single and Married Filing Jointly.

New Line 5. Additions to Income

This line asks employees to enter estimated nonwage income not subject to withholding (such as interest and dividends). Previously, employees with significant nonwage income had to convert such amounts to equivalent per-payroll additional amounts to withhold. Line 5 amounts will be full-year estimates, so employer payroll systems will need to be modified to include these full-year amounts in withholding calculations.

New Line 6. Itemized and Other Deductions

Line 6 prompts employees to enter estimated subtractions to income based on expected deductions (such as state and local taxes, mortgage interest, and charitable contributions). Previously, employees needed to convert deductions into equivalent withholding allowances. Again, amounts entered will be full-year estimated deduction totals, so payroll systems will need to include full-year amounts in withholding calculations.

New Line 7. Tax Credits

This line asks employees to enter the full-year amount of any tax credits for which they expect to qualify, such as the child tax credit. As a reminder, the 2017 Tax Cuts and Jobs Act significantly expanded child and dependent tax credits. Previously all tax credits were translated by employees into additional withholding allowances. With the 2019 Form W-4, full-year tax credit amounts will be directly entered into payroll systems.

Critically, any tax credits should only be entered for the highest paying job in households with multiple incomes. Taxes may be significantly under-withheld for a household if both spouses enter the full-year credit



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expected, resulting in a large tax amount due at year-end. Conversely, taxes may be significantly over-withheld if neither spouse enters the total tax credit amount, resulting in reduced net paychecks during the year, and a large tax refund at year-end.

New Line 8. Additional Household Income Due to Multiple Jobs

If applicable, employees will enter the (full-year) income associated with any second job (e.g., a second job that the employee holds, or the annual wage income of any spouse, if they are employed). Additional wage income should only be entered for the highest paying job in households with multiple incomes. There are special instructions for households with more than two incomes. Previously, employees used a Form W-4 worksheet to calculate a specific additional amount to withhold per pay period.

Employers will include these full-year amounts in withholding calculations in order to determine the appropriate tax bracket and rates for the employee.

Alternatively, the instructions will offer a calculation to estimate an additional tax amount to withhold per pay period, which was the solution prior to 2019. Employees will also be able to go to the online calculator (discussed below) or IRS Publication 505, Tax Withholding and Estimated Tax, to bypass Lines 5 and/or 8.

Line 9. Additional Amount, If Any, You Want Withheld From Each Paycheck

This line is unchanged. Employees will continue to be able to enter an additional per-pay period amount to withhold. Line 9 is the only entry with a per-pay period result.

A “Paycheck Checkup” Remains Important for 2018

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 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.

The IRS published a new online W-4 Calculator in February, and strongly recommended that employees access the calculator at <https://www.irs.gov/individuals/irs-withholding-calculator>, to determine the correct number of withholding allowances (either adjusting for the TCJA, and/or 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.

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Actions for 2019

The **Draft 2019 Form W-4 should not be provided to employees at this time**, since it may change. It should not be used for payrolls dated before 2019.

Employers should consider reminding employees of the withholding calculator, which will help employees check their tax withholding at any point in the year compared to their total expected full-year tax liability. It is important to do this as early as possible in the year to allow a smaller adjustment (if needed) during the balance of the year. A sample letter follows.

Example Notice to Employees

Re: 2018 Income Tax Withholding

Dear _____:

This is a reminder that the 2017 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.

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.

The IRS offers an online "W-4 Calculator," at <https://www.irs.gov/individuals/irs-withholding-calculator>. This calculator can help you check your tax withholding at any point in the year, compared to your total expected 2018 tax liability. It is important to do this as early as possible in the year to allow a smaller adjustment (if needed) during the balance of the year.

Although the IRS did not require all employees to file a new Form W-4 for 2018, for some people it may be advisable. The TCJA made many other changes that could affect your 2018 income taxes.

To update your withholding allowances, see the IRS 2018 Form W-4, Employee's Withholding Allowance Certificate, and related instructions, which you can find at www.irs.gov/W4.

For questions regarding your personal tax situation, talk with your tax advisor, or visit www.IRS.gov.

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