



**MORTON C.P.A.'s, P.C.**  
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Dear Clients and Friends,

This mid-year letter is to update you on these recent, significant, payroll tax changes:

**Employee Healthcare Credit:**

Small Employers will get a credit for providing employees with healthcare coverage. The credit is based on the number of employees. This credit is not available to companies with 25 or more fulltime employees or average yearly wages more than \$50,000 per employee. Owner's wages do not count towards the credit.

The computation of the credit is complex and does not have to be completed until the year end tax return is prepared.

**Employer FICA Exemption for Hiring Unemployed Persons:**

If you hire an employee that has not worked more than 40 hours in the past 60-days, that employee will be exempt for the employer portion of social security payroll taxes on that new employees wages. This is for new hires after February 3, 2010 through December 31, 2010. This reduction of payroll taxes will be shown on your quarterly report Form 941. The new hire must fill out FORM W-11, on which the employee essentially attests to the fact (s)he has not worked more than 40 hours in the last 60 day period.

**Credit for Hiring the Unemployed:**

If you hire an employee who meets the above description and the employee stays on with your company for more than one year, you are entitled to an additional \$1000 tax credit.

**Arizona Withholding Changes – Arizona Form A-4:**

Beginning July 1, 2010 Arizona withholding will now be based on a percent of gross wages and no longer on a percent of Federal withholding. Every employee should fill out a new FORM A-4. However, if they do not fill out the form, there is a chart to assign new withholding rates based on their old percentages used. There is also a place on the form to put an additional dollar amount to be withheld per paycheck.

**Changes in Federal Payroll Tax Deposit Methods:**

Beginning in 2011, most employers will be required to use the Electronic Federal Tax Payment System (EFTPS) for payroll tax deposits. Only the very smallest employers will still be allowed to use the paper tax coupons. (Employers with less than \$2,500 liability per quarter employment taxes due.) We encourage all our clients to sign up for the EFTPS now because the transition can often take a considerable time.

Please call us with any questions you may have.

Thanks,

Morton CPA's PC

*NOTE: This form is effective for wages paid after June 30, 2010.*

Type or print your full name	Your social security number
Home address (number and street or rural route)	
City or town, state, and ZIP code	

**Arizona Withholding Percentage Election Options**

**Choose only one:**

- 1  My annual compensation is \$15,000 or more. I choose to have Arizona withholding at the rate of  
(check only one box):  1.8%    2.7%    3.6%    4.2%    5.1% of my gross taxable wages.  
Additional amount to be withheld per paycheck \$ \_\_\_\_\_
  
- 2  My annual compensation is less than \$15,000. I choose to have Arizona withholding at the rate of  
(check only one box):  1.3%    1.8%    2.7%    3.6%    4.2%    5.1% of my gross taxable wages.  
Additional amount to be withheld per paycheck \$ \_\_\_\_\_
  
- 3  I hereby elect an Arizona withholding percentage of zero, and I certify that I meet BOTH of the following qualifying conditions for this election:
  - I had NO Arizona tax liability for the prior taxable year, AND
  - I expect to have NO Arizona tax liability for the current taxable year.

I certify that I have made the percentage election marked above.	
_____	_____
SIGNATURE	DATE

**EMPLOYEE'S INSTRUCTIONS**

Arizona Revised Statutes (ARS) §43-401 requires your employer to withhold Arizona income tax from your compensation paid for services performed in Arizona for application toward your Arizona income tax liability. Arizona withholding is a percentage of your gross taxable wages of every paycheck.

"Gross taxable wages" is the amount from each paycheck that will be included in box 1 of your federal Form W-2 at the end of the calendar year (i.e. gross wages net of pretax deductions, such as your portion of health insurance premiums). You may also have your employer withhold an additional amount from each paycheck.

Complete this form to elect an Arizona withholding percentage and any additional amount to be withheld from each paycheck. Give the completed form to your employer.

**Current Employees**

ALL EMPLOYEES ARE REQUIRED TO COMPLETE THIS FORM FOR WAGES PAID AFTER JUNE 30, 2010. Complete this form to elect an Arizona withholding percentage and designate an additional amount to be withheld. If you want to increase or decrease the amount of Arizona withholding in the future, you must complete this form again to change the Arizona withholding percentage or change the additional amount withheld.

**New Employees**

Complete this form within the first five days of employment to elect an Arizona withholding percentage. You may also have your employer withhold an

additional amount from each paycheck. If you do not complete this form, the department requires your employer to withhold 2.7% of your gross taxable wages until your employer receives a completed form from you.

**Electing a Withholding Percentage of Zero**

You may elect an Arizona withholding percentage of zero if you meet BOTH of the qualifying conditions for the election. You qualify for the election if: (1) you had no Arizona income tax liability for the prior taxable year, AND (2) you expect to have no Arizona income tax liability for the current taxable year.

Note that Arizona tax liability is gross tax liability less any tax credits, such as the family tax credit, school tax credits, welfare tax credits, or credits for taxes paid to other states. If you make this election, your employer will not withhold Arizona income tax from your wages for payroll periods beginning after the date of your election.

You should be aware that zero withholding does not relieve you from paying Arizona income taxes that might be due at the time you file your Arizona income tax return. Keep in mind that in order to elect zero withholding, you must meet BOTH conditions listed above. Therefore, if you have an Arizona tax liability when you file your return or if at any time during the current year conditions change so that you expect to have a tax liability, you should immediately complete a new Form A-4 and choose a withholding percentage that is applicable to your situation.

# Employer's Instructions for the Employee's Arizona Withholding Percentage Election

## Arizona Form A-4

Obtain additional information or assistance by calling one of the numbers listed below:

Phoenix (602) 255-2060  
From area codes 520 and 928, toll-free (800) 843-7196  
Hearing impaired TDD user  
Phoenix (602) 542-4021  
From area codes 520 and 928, toll-free (800) 397-0256

Obtain tax rulings, tax procedures, tax forms and instructions, and other tax information by accessing the department's Internet home page at [www.azdor.gov](http://www.azdor.gov).

**NOTE:** Senate Bill 1185 required the Department to develop rate tables for withholding. The new withholding rates are a percentage of gross taxable wages. "Gross taxable wages" is the amount that meets the federal definition of "wages" contained in IRC § 3401 and that will be included in box 1 of the employee's federal Form W-2 at the end of the calendar year (i.e. gross wages net of pretax deductions, such as the employee's portion of health insurance premiums).

Every employee is required to fill out a revised Arizona Form A-4 or Form A-4V effective for wages paid after June 30, 2010.

For more information about this withholding law change, visit our website at [www.azdor.gov](http://www.azdor.gov).

Arizona Revised Statutes (ARS) § 43-401 requires an employer to make Form A-4 available to employees at all times and to inform employees of the Arizona withholding election options. Through June 30, 2010, Arizona withholding was a percentage of the amount of federal income tax withheld. Beginning July 1, 2010, Arizona withholding is based on a percentage of gross taxable wages. "Gross taxable wages" is the amount that meets the federal definition of "wages" contained in IRC § 3401 and that will be included in box 1 of the employee's federal Form W-2 at the end of the calendar year (i.e. gross wages net of pretax deductions, such as the employee's portion of health insurance premiums). Employees may also designate an additional amount to be withheld from each paycheck.

### New Employees

New employees must complete this form within the first five days of employment. If the employee does not complete this form, the employer must withhold 2.7% of the employee's gross taxable wages, until the employer receives a completed form from the employee.

### Current Employees

Current employees must complete this form to elect a different Arizona withholding percentage or to change the additional amount designated to be withheld from each paycheck. If the employee wants to increase or decrease the amount of Arizona withholding, the employee must complete this form to change the Arizona withholding percentage or change the additional amount designated to be withheld each paycheck.

To facilitate the transition to the new rates, for existing employees who have not filed a revised Arizona Form A-4, employers may use the following table:

If the Employee's withholding rate before July 1, 2010, was:	Then use this rate for wages paid after June 30, 2010:
0%	0%
<del>10.7%</del>	<del>1.3%</del>
20.3%	1.8%
24.5%	2.7%
26.7%	3.6%
33.1%	4.2%
39.5%	5.1%

The rates in the shaded boxes are only available to employees whose compensation is less than \$15,000 annually.

### Electing a Withholding Percentage of Zero

An employee may elect an Arizona withholding percentage of zero, if the employee meets BOTH of the qualifying conditions for the election. An employee making this election certifies that: (1) the employee had no Arizona income tax liability for the prior taxable year, AND (2) the employee expects to have no Arizona income tax liability for the current taxable year. If an employee makes this election, the employer will not withhold Arizona income tax from the employee's compensation for payroll periods beginning after the date of the employee's election.

**NOTE:** For any employee previously relying on their federal election to be exempt from Arizona withholding, an employer must obtain a revised Form A-4 with an Arizona exemption election or withhold at a rate of 2.7% until the employer receives a completed form from the employee.

### Voluntary Withholding Election by a Nonresident Employee Exempt Under ARS § 43-403(A)(5)

A qualifying employee may use this form to voluntarily elect to have a portion of the employee's compensation withheld under the provisions of ARS § 43-403(D)(1) for application toward the employee's Arizona income tax liability. The employee completes this form to elect an Arizona withholding percentage and to designate an additional amount to be withheld from each paycheck.

**NOTE:** This exemption does not apply to a nonresident employee who is in this state solely for athletic or entertainment purposes.

**QUALIFYING CRITERIA FOR THE ARS § 43-403(A)(5) EXEMPTION.** The exemption under the provisions of ARS § 43-403(A)(5) applies to wages paid to nonresident individuals who are:

1. Employed by a company having property, payroll, and sales in Arizona or by a related entity having more than 50 percent direct or indirect common ownership; **and**
2. Physically present in Arizona for less than 60 days in a calendar year for the purpose of performing a service that will benefit the employer.

Activities not included in determining the number of days of service are:

- a. Being in transit.
- b. Engaging in personal activities.

- c. Participating in training or professional development activities or attending meetings that are not directly connected to the Arizona operations of the employer.

A "related entity having more than 50 percent direct or indirect common ownership" means that the related entities are more than 50 percent owned by the same interests. The examples on the following page illustrate three different situations in which the nonresident employee is performing services in Arizona for such an entity for less than 60 days during a calendar year. In these examples, the employer has met the qualifying criteria for the ARS § 43-403(A)(5) exemption and, therefore, does not have to withhold Arizona income taxes from compensation paid to the employee for services performed in Arizona.

**Example 1:**

Corporation A is the U.S. domestic parent of Corporation B, a wholly owned foreign subsidiary corporation. Corporation A has property, payroll and sales in Arizona. Corporation B operates in China and does not have property, payroll and sales in Arizona. Individual R, an Arizona nonresident, is an employee of Corporation B. Individual R performs services for Corporation B in Arizona for 45 days during calendar year 2009.

**Example 2:**

Corporation F, based in California, is the common parent of Corporation W. Corporation F does not have property, payroll and sales in Arizona. Corporation W does have property, payroll and sales in Arizona. Individual L, an Arizona nonresident, is an employee of Corporation F. Individual L performs services for Corporation F in Arizona for 55 days during calendar year 2009.

**Example 3:**

Individual D owns 60 percent of Corporation K and 51 percent of Corporation S. Individual N owns 40 percent of Corporation K and 49 percent of Corporation S. Corporation S has property, payroll and sales in Arizona. Corporation K, based in California, does not have property, payroll and sales in Arizona. Individual T, an Arizona nonresident, is an employee of Corporation K. Individual T performs services for Corporation K in Arizona for 35 days during calendar year 2009.

**How to Determine if an Employee Qualifies to Elect the Minimum Withholding Percentage**

An employer determines if an employee qualifies to elect the minimum withholding percentage as follows:

1. If an employee whose annual compensation is less than \$15,000 elects the 1.3% withholding rate, that rate shall apply until one of the following situations occurs:
  - a. Until the employee has 12 full months of work history with the employer, the employer shall determine the employee's annualized compensation at the end of each month. *The employer may use any method of annualization that accurately reflects the employee's annual compensation.* If the employer determines that the employee's annualized compensation is \$15,000 or

more, the employer shall adjust the employee's rate of withholding beginning the next full pay period following the determination. The employer shall adjust the rate to 1.8%, unless the employee elects a higher rate of withholding. The 1.8% withholding rate shall apply until the employee has been employed for 12 full months, unless the employee elects a higher rate of withholding.

<b>Example</b>		
At the end of the month, an employer must annualize the compensation of an employee with 3 1/2 months of work history with the employer. The employee's compensation is annualized as follows:		
First full month of compensation		\$ 1,500
Second full month of compensation	+	1,500
Third full month of compensation	+	1,500
Fourth partial month of compensation	+	925
Total compensation (3 1/2 months)	=	\$ 5,425
Divide by number of payroll periods in the 3 1/2 months	÷	7
Average payroll period compensation	=	\$ 775
Multiply by number of payroll periods in a calendar year	×	26
Annualized compensation	=	\$ 20,150

After 12 full months of employment, the employer shall determine the rate under (b) below;

- b. If the employee has 12 full months of work history with the employer, the employer shall determine the employee's total compensation for the 12-month period. If the records for that period show that the employee earned \$15,000 or more, the employer shall adjust the rate of withholding beginning the next full pay period following the determination. The employer shall adjust the rate to the 1.8% withholding rate, unless the employee elects a higher rate of withholding. The 1.8% withholding rate shall apply through the end of the calendar year, unless the employee elects a higher rate of withholding. At the end of that calendar year and at the end of each succeeding calendar year, the employer shall redetermine the employee's total annual compensation. If the employee's annual compensation for the preceding year changes the employee's rate of withholding, the rate change shall begin the next full pay period following the determination unless the employee makes a zero percent withholding election for the taxable year; or
- c. If the employee receives a salary increase that makes the employee's annualized compensation \$15,000 or more, the employer shall adjust the employee's rate of withholding to the 1.8% withholding rate, beginning the next full pay period following the receipt of the increase by the employee.
2. An employee who has elected a withholding rate higher than the minimum withholding rate may later elect to reduce the rate to a lower rate for the employee's annual compensation.

# Employee's Arizona Withholding Percentage Election

## Voluntary Withholding Election by Certain Nonresident Employees

Compensation earned by nonresidents while physically performing work or services in Arizona for temporary periods is subject to Arizona income tax. However, under the provisions of ARS §43-403(A)(5), compensation paid to certain nonresident employees is not subject to Arizona income tax withholding. These nonresident employees need to review their situations and determine whether they should elect to have Arizona income taxes withheld from their wages or compensation. Nonresident employees may request that their employer withhold Arizona income taxes from their compensation by completing this form to elect an Arizona withholding percentage.

### How do I Determine Which Percentage to Elect?

In an effort to assist employees in electing a withholding percentage, the following simple examples are provided for general guidance. However, each employee must take into consideration the particular facts of their own situation and adjust their election accordingly.

If you want to keep your withholding approximately the same as last year, you can use your federal Form W-2 for 2009 or your last pay stub to calculate which withholding percentage to elect. For example, if box 1 of federal Form W-2 shows \$40,000 in wages and box 17 shows \$1,000 in state income tax withheld, divide box 17 by box 1 to determine your percentage ( $1,000 / 40,000 = .025$  or 2.5%). In order to keep your withholding the same as 2009, choose 1.8% ( $40,000 \times .018 = 720$ ) and an additional \$10.77 per biweekly pay period ( $1,000 - 720 = 280 / 26 = 10.77$ ). Be sure to take into account any amount already withheld for 2010.

If you want to withhold more, choose one of the higher percentages or choose to have an additional amount withheld.

**CAUTION: Underwithholding can result in payment of tax due when you file your Arizona return and/or underpayment penalties.**

If you would rather more closely approximate your tax liability from last year, use your tax liability from your 2009 Arizona income tax return. Divide that number by the number of paydays in calendar year 2010. This will be the amount of withholding you will try to have withheld out of each paycheck. For instance, if your 2009 tax liability was \$1,500 and you are paid every two weeks (26 paydays a year) divide \$1,500 by 26 ( $1,500 / 26 = 57.69$ ). This is your withholding goal per paycheck. Next, divide your withholding goal by your biweekly gross taxable wages, \$2,000 in this example, to determine the percentage of withholding to gross taxable wages ( $57.69 / 2,000 = .028845$  or 2.88%). An election of 2.7% would result in \$54.00 ( $2,000 \times 2.7\% = 54$ ) withheld for Arizona from each paycheck (\$1,404 annually), while electing 3.6% would result in \$72.00 ( $2,000 \times 3.6\% = 72$ ) withheld for Arizona from each paycheck (\$1,872 annually). Be sure to take into account any amount already withheld for 2010.

**Example:** This example assumes these wages are your only income and your employment situation is the same as last year. If you are paid every two weeks and last year's federal Form W-2 shows \$52,000 in box 1 and \$1,800 in box 17, \$900 has already been withheld from your paychecks for 2010, there are 13 paychecks remaining in the calendar year, and you want to keep your withholding approximately the same, the following worksheet shows how to keep your Arizona withholding the same.

	Example:		Your Calculation:	
Line 1: Annual gross taxable wages.	\$52,000			
Line 2: Number of paychecks per year.	26			
Line 3: Divide line 1 by line 2. This is wages per paycheck.	$52000 / 26 =$	\$2,000	$/$	$=$
Line 4: Annual withholding goal. $(52,000 \times 3\%)$	\$1,800			
Line 5: Amount already withheld.	\$900			
Line 6: Balance of withholding for the calendar year.	$1800 - 900 =$	\$ 900	$-$	$=$
Line 7: Number of paychecks remaining in the calendar year.	13			
Line 8: Divide line 6 by line 7. This is your Arizona withholding goal per paycheck.	$900 / 13 =$	\$69.23	$/$	$=$
Line 9: Percentage: divide line 8 by line 3.	$69.23 / 2000 =$	3.4615%	$/$	$=$ %
Line 10: Withholding percentage that is less than line 9. Check this box on line 1 of Form A-4.	2.7%			Select Withholding Percent
Line 11: Multiply line 10 by line 3.	$2.7\% \times 2000 =$	\$54.00	$\times$	$=$
Line 12: Subtract line 11 from line 8. Enter this amount in the additional amount space on line 1 of Form A-4.	$69.23 - 54.00 =$	\$15.23	$-$	$=$

# Hiring Incentives to Restore Employment (HIRE) Act Employee Affidavit

▶ Do not send this form to the IRS. Keep this form for your records.

**To be completed by new employee. Affidavit is not valid unless employee signs it.**

I certify that I have been unemployed or have not worked for anyone for more than 40 hours during the 60-day period ending on the date I began employment with this employer.

Your name \_\_\_\_\_ Social security number ▶ \_\_\_\_\_

First date of employment \_\_\_\_ / \_\_\_\_ / \_\_\_\_ Name of employer \_\_\_\_\_

Under penalties of perjury, I declare that I have examined this affidavit and, to the best of my knowledge and belief, it is true, correct, and complete.

Employee's signature ▶ \_\_\_\_\_ Date ▶ \_\_\_\_ / \_\_\_\_ / \_\_\_\_

## Instructions to the Employer

Section references are to the Internal Revenue Code.

### Purpose of Form

Use Form W-11 to confirm that an employee is a qualified employee under the HIRE Act. You can use another similar statement if it contains the information above and the employee signs it under penalties of perjury.

Only employees who meet all the requirements of a qualified employee may complete this affidavit or similar statement. You cannot claim the HIRE Act benefits, including the payroll tax exemption or the new hire retention credit, unless the employee completes and signs this affidavit or similar statement under penalties of perjury and is otherwise a qualified employee.

A "qualified employee" is an employee who:

- begins employment with you after February 3, 2010, and before January 1, 2011;
- certifies by signed affidavit, or similar statement under penalties of perjury, that he or she has not been employed for more than 40 hours during the 60-day period ending on the date the employee begins employment with you;
- is not employed by you to replace another employee unless the other employee separated from employment voluntarily or for cause (including downsizing); and
- is not related to you. An employee is related to you if he or she is your child or a descendent of your child,

your sibling or stepsibling, your parent or an ancestor of your parent, your stepparent, your niece or nephew, your aunt or uncle, or your in-law. An employee also is related to you if he or she is related to anyone who owns more than 50% of your outstanding stock or capital and profits interest or is your dependent or a dependent of anyone who owns more than 50% of your outstanding stock or capital and profits interest.

If you are an estate or trust, see section 51(i)(1) and section 152(d)(2) for more details.



**Do not send this form to the IRS. Keep it with your other payroll and income tax records.**