

NATIONAL PAYROLL REPORTING CONSORTIUM, INC.

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PO Box 850 HENRIETTA, NY 14467-0850
WWW.NPRC-INC.ORG

September 13, 2006

Mr. Kevin M. Brown
Commissioner, Small Business Self Employed
Rm IR-3406
1111 Constitution Ave., NW
Washington, DC 20224

Dear Commissioner Brown:

We are writing to express concerns regarding the Form 944 program and to recommend alternative means for certain taxpayers to opt out of the program.

The National Payroll Reporting Consortium (NPRC) is a non-profit trade association whose member organizations provide payroll processing and related services to over one million employers nationwide, covering over one-third of the private sector work force. Payroll service providers serve an important role in the tax collection and reporting system as a conduit between employers and tax authorities, improving the efficiency of government tax collection and reporting and improving compliance.

Burden reduction measures should be voluntary. While Form 944 was intended to reduce taxpayer burden, such burden was actually increased for a substantial percentage of affected taxpayers. The 944 program demands the attention of those affected to understand the change and take action, whether that be changing their deposit schedule or filing form, notifying their CPA, or writing a letter to opt out of the program, and then watching for an IRS response permitting them to continue filing as they have in the past.

Affected employers must also monitor their status and determine annually whether to file Form 944 or Form 941. Employers who transition in and out of Form 944 eligibility from year to year as a result of varying tax liability are subject to substantial new complexities and burdens, including different deposit rules and possible penalties. The transition issues are described in the attached letter dated April 3, 2006.

A large number of 944 filers are disabled individuals who are deemed to be the employer of home care workers. Many of these individuals rely on Reporting Agents (RAs) to take care of their employment tax responsibilities, and may be unaccustomed to making tax administration decisions. The IRS has, in effect, forced the very taxpayers with the least connection to the employment tax reporting system to understand a confusing set of rules and make a determination that seems very risky to them.

944 filers who rely on RAs receive no monetary benefit or burden reduction from the 944 program. Reporting Agents generally provide a comprehensive array of services associated with payroll, with no price difference based on the number of federal tax returns filed or deposits made. RAs facilitate and simplify tax administration for the disabled and other small employers. Such employers' payroll and related taxes are effectively on 'autopilot', requiring minimal effort on their part - - generally just information about newly hired workers and hours worked each pay

period. It is not in their best interests, or in the interests of the IRS, to force such individuals into making complex decisions on matters they know little about.

The annual 944 program is a dramatic departure from other burden reduction measures because it is not voluntary. Other simplified tax forms, such as 1040-EZ, 940-EZ, 1120-EZ, etc., are voluntary. But, with Form 944, the Service requires taxpayers to take affirmative action to opt out in order to continue filing the quarterly 941s. In every other program, the IRS recognized that taxpayers have their own reasons for preferring whatever tax form they use; e.g., their current tax form may already be automatically generated and electronically filed, and any change would necessitate additional expense or effort on their part.

In addition, the IRS has always permitted – and sometimes encouraged - small employers to make their federal tax deposits under the more frequent semi-weekly rule, rather than under their assigned monthly deposit rule. Such departures have caused no ill effects for the Internal Revenue Service or for the taxpayers. Wisely, the Service does not force those taxpayers to use the least cumbersome or least costly option available to them. The same rationale should be applied to Form 944.

The NPRC has been informed that opting out of filing Form 944 is an election and that the limited authority of the Reporting Agent Authorization, Form 8655, does not allow RAs to opt out of Form 944 on behalf of their clients. However, the IRS' very own recent actions negate the premise that Form 944 opt out is an election that can only be made by the taxpayer or his representative holding a valid Power of Attorney, Form 2848. Contrary to all the published 944 instructions and guidelines, the IRS arbitrarily changed thousands of taxpayers' 944 filing requirements back to 941 – confusing taxpayers and RAs alike. In brief, these are the two situations that we are aware of:

- ◆ Approximately 20,000 944 filers were changed back to 941 after RAs e-filed 2006-03 Forms 941 for new clients who were not identified as 944 filers.
- ◆ Approximately 3200 944 filers were notified in August that the IRS changed them back to 941 filers and that their 2006-03 and 2006-06 Forms 941 were now due. Although the IRS properly identified these LM-SB employers as 944 filers based on their tax accounts in the eligibility determination period, the IRS unilaterally changed these taxpayers to 941 filers once tax deposits started to be made for those entities.

As the IRS itself has subsequently changed 944 filers back to 941 filers even though the taxpayers did not opt out of filing Form 944, it appears the Service does not actually consider Form 944 opt out as an election to be made solely by the taxpayer.

In addition, the filing of four quarterly 941s rather than one annual Form 944 has no effect on tax administration other than the obvious benefit of receiving employers' liability information more frequently - allowing the IRS to perform more timely FTD compliance checks.

We suggest that the IRS allow designated 944 filers to continue to file quarterly Forms 941, without requiring each filer to advise the IRS of their choice. As was done with the first quarter 941s, the IRS could automatically cancel the 944 filing designation and re-establish the quarterly 941 requirement based upon receipt of a Form 941 filing or deposit. Notices could be issued to clarify the filer's choice only in those instances in which the taxpayer's filings were inconsistent, such as a 941 filed for the quarter ended March 31st but not June 30th.

If the Service determines that opt-outs are actually necessary, then we recommend that the IRS permit RAs to opt out on behalf of their clients. Reporting Agents file electronically, so this would result in no additional processing costs to the IRS. We urge the IRS to review this issue comprehensively, particularly in light of the actions the Service has taken to change 944 filers back to 941 filers. Clients of RAs are for all practical purposes uninvolved and unaffected by which form they file. Permitting RAs to continue automatically and electronically filing Forms 941 for such clients is an administrative detail that could hardly be said to constitute "representation" requiring more authority than granted in the Reporting Agent Authorization. Reporting Agents should be allowed to opt out of Form 944 on behalf of their clients.

Members of the NPRC would be happy to discuss alternatives and any concerns the IRS may have. As always, we appreciate the opportunity to work constructively with the IRS to improve tax administration. Please let us know if we can be of service.

Sincerely,



Pete Isberg
National Payroll Reporting Consortium

Cc: Beth Tucker, Director, Office of Taxpayer Burden Reduction
Nina Olsen, National Taxpayer Advocate

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April 3, 2006

Internal Revenue Service
CC:PA:LPD:PR Room 5203
1111 Constitution Avenue, NW.
Washington, DC 20044.

Via www.irs.gov/regs

Re: REG-148568-04 (Form 944 Program)
Time for Filing Employment Tax Returns and Modifications to the Deposit Rules

Gentlemen:

The National Payroll Reporting Consortium (NPRC) is a non-profit trade association whose member organizations provide payroll processing and related services to over one million employers nationwide, covering over one-third of the private sector work force. Payroll service providers have long served an important role in our nation's tax collection and reporting system as a conduit between employers and tax authorities. Payroll service providers improve the efficiency of government tax collection and reporting and improve compliance. We appreciate this opportunity to provide comments regarding the 944 program and its associated regulations.

In brief, for those employers who are clearly within the \$1,000 annual tax threshold for 944 inclusion and who remain there, Form 944 is beneficial. It reduces the number of filings and simplifies their responsibilities. However, for the roughly 10% of 944-eligible employers who will transition in and out of Form 944 eligibility from year to year as a result of varying annual tax liability, substantial new complexities and burdens have been created by Form 944, and some employers will incur penalties due to transition issues created by the 944 program.

There are also some aspects of the 944 program that unnecessarily increase burden and costs for affected taxpayers and their service providers. Comments were requested as to whether the Form 944 program should be expanded to include more taxpayers. We believe that expansion of the program to include taxpayers with annual employment tax liabilities of up to \$2,500 would make sense, and would eliminate the inconsistency between the threshold for annual filing and for annual deposit, which is a source of confusion for employers. However, the IRS should offer Form 944 as a voluntary option, with qualifying employers opting in rather than being forced to participate or take affirmative action to opt out. The relevant issues and alternatives are explained further below.

Transition issues

Generally, qualifying employers whose total employment tax liability for the year is less than \$2,500 may pay their employment taxes once annually when they file their 944 on January 31. If an employer's accumulated employment tax liability is more than \$2,500, however, deposits must be made either monthly or semi-weekly. To determine its status as a monthly or semi-weekly depositor, an employer determines the aggregate amount of employment taxes reported

in a previous 12-month period. For Form 941 filers, the 12-month period ends on the preceding June 30 (the deposit “look back” period). For Form 944 filers, however, since there are no quarterly returns, the deposit look back period is the second preceding calendar year (e.g., 2004 for tax year 2006).

To complicate matters, Form 944 filers whose employment tax liabilities are greater than \$1,000 will be required to transition back from Form 944 to Form 941. In such a year, the deposit look back period will remain the second preceding calendar year, as there will be no quarterly returns on which to base the regular 941-filer deposit look back period. Employers who transition in and out of Form 944 may be confused about which rules apply to them, especially which look back period applies to their current year deposit requirement.

Example:

A theater company produces a major performance once every other year, and otherwise has no activity. They were a 941 filer in 2004 and 2005, and had less than \$1,000 in federal employment tax liability in the *filing requirement* determination period (July 2004 - June 2005 for 2006), so they are a Form 944 filer in 2006. However, they have more than \$50,000 in liability in the *deposit* look back period for 2006 (January - December 2004), so they must deposit semiweekly if they accumulate more than \$2,500 in employment taxes in 2006. If the company had been a 941 filer for 2006, their deposit schedule would be monthly (because the *deposit* look back period for 941 filers is July 2004 – June 2005).

In this case, the theater manager has probably become long accustomed to the July-June deposit schedule look back period and is likely to assume that it continues to apply. If their theater production (and resulting tax liability of over \$50,000) occurred between January and June 2004, she may mistakenly think that they are a monthly depositor for 2006 and, incur a penalty for late deposits. It seems impractical to expect small employers to understand that their look back periods for deposit requirements may vary depending on what employment tax form the IRS requires them to file.

Another source of confusion for employers who are required to transition in and out of Form 944 is that although an employer may realize in January, by completing their Form 944 for the prior year, that they are a Form 941 filer for the current year, the IRS expects them to remain a 944 filer until notified otherwise. In this situation, employers who know they are 941 filers for the current year may face difficulty depositing their employment taxes and possibly filing the 941 return. Until the IRS processes the prior year 944 and notifies the employer of their new 941 designation, a deposit to the 941 account may result in an IRS misposting notice, which will remind the employer that, according to IRS records, the employer is a 944 filer. If the IRS has not processed Form 944 for the prior year by the time the first quarterly 941 is due for the current year, the IRS may reject the 941 filing.

Burden Reduction Measures Should Be Voluntary

While Form 944 was introduced as a means to reduce taxpayer burden, by some measures taxpayer burden was actually increased by the 944 program. Many small employers who qualify for Form 944 rely on highly automated systems, such as Reporting Agents and off-the-shelf software, which already generate electronic quarterly 941 filings at no additional cost. They gain no reduction in cost by not filing quarterly. Any change, especially to computer systems and software, would instead impose additional costs.

The 944 program increases burden because it requires the attention of affected employers to understand the changes, and increases burden further if they have to take action, such as changing their deposit schedule or filing form, notifying their CPA, etc.. And because an employer's annual filing and deposit requirements may subsequently change (i.e., when tax liability unexpectedly increases or decreases), affected employers may be burdened by the need to monitor whether they need to transition in or out of the new filing requirement category.

Employers and Reporting Agents now have to keep track of another indicator – annual 944 or quarterly 941 – where previously there was no need to maintain records as to which category applies to which employer. Previously, employment taxes enjoyed the blissful simplicity that almost all taxpayers filed the same tax form at the same time. Every variable to be tracked presents another opportunity for error, and another cause for IRS posting problems and correspondence. Some employers will not receive or understand the notice of change in their filing requirement, and will file Form 941 as they always have. Those returns will be rejected, with a letter advising the employer to file annually. Thus, the level of burden will increase for many taxpayers, as well as for the IRS.

The annual 944 program would have been a more effective burden reduction measure if it had been implemented on a voluntary basis. Rather than requiring taxpayers to take affirmative steps to opt out, a process should have been put in place that would have allowed taxpayers to opt in. Similarly simplified tax forms, such as 1040-EZ, 1120-EZ, etc., were made available to taxpayers as a voluntary alternative, and in those cases the IRS recognized that taxpayers may have their own reasons for preferring whatever tax form they customarily used.

We suggest that the IRS allow designated annual filers to continue to file quarterly if they so choose, without requiring each filer to advise the IRS of their choice. The IRS could automatically cancel the annual 944 filing designation and re-establish the quarterly 941 requirement based upon receipt of a Form 941 filing or deposit. Notices could be issued to clarify the filer's choice only in those instances in which the taxpayer's filings were inconsistent, such as a 941 filed for the quarter ended March 31st but not June 30th. This approach would resolve the confusion and errors described above when a 944 filer realizes in January that they should be a 941 filer for the current year.

We support the concept of expanding the program to include taxpayers with annual employment tax liabilities of up to \$2,500; however we recommend that the IRS offer Form 944 as a voluntary option, with qualifying employers opting in. The IRS should also permit Reporting Agents to opt out on behalf of their clients. Reporting Agents file electronically, so this would result in no additional processing costs to the IRS.

Thank you for this opportunity to comment on the IRS' rules for Form 944. Please let us know if you have any questions.

Sincerely,



Pete Isberg
National Payroll Reporting Consortium