

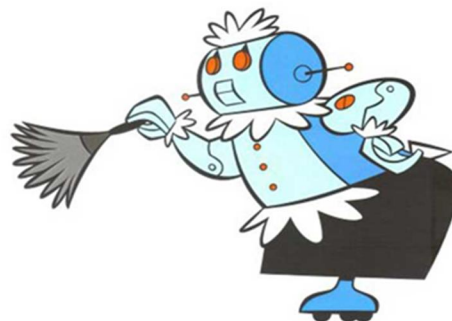
# NELSON | TAX & ACCOUNTING

## Fact Sheet

January 2024

### **Nanny Tax Summary: Calendar Year 2023 Wages**

Employing someone in your home comes with certain tax obligations. These obligations are often referred to as the "Nanny Tax" but the "Nanny Tax" isn't limited to a nanny. It also applies to a housekeeper, home health care worker, baby-sitter, gardener or other household employee who isn't an independent contractor. The tax doesn't apply to a household employee who is also a farm worker.



### **What makes someone a household employee?**

According to the IRS, a household worker is an employee if you control not only *what* work is done, but also *how* it is done. Generally speaking, that means the employee is coming to your home on the schedule you dictate while following your rules. It doesn't matter whether the work is full-time or part-time or if you hired the worker through an online platform, they are still considered a household employee subject to taxes if you pay them more than \$2,400 per calendar year.

### **What happens if I do not provide my household employee with a W2?**

Families that misclassify their nanny as an independent contractor by providing a Form 1099 for filing taxes can be charged with tax evasion. If you're caught, you'll owe all the back taxes you should have been paying to the IRS and the state during the time you had a caregiver and be subject to additional fines. The IRS, Department of Labor and the majority of states have signed a formal Memorandum of Understanding to share information between agencies in order to combat worker misclassification.

### **What are my tax obligations?**

The nanny tax is a combination of federal and state tax requirements that families must manage when they hire a household employee, such as a nanny, senior caregiver or

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personal assistant. The taxes include:

- **Taxes withheld from the employee:** Social Security & Medicare taxes (FICA), as well as federal & state income taxes (if applicable).
- **Taxes paid by the employer:** Social Security & Medicare taxes (FICA), as well as federal & state unemployment insurance.

**IRS Publication 926** is detailed at <https://www.irs.gov/forms-pubs/about-publication-926>

If you employ someone who is subject to the "Nanny Tax" you aren't required to withhold federal income taxes. You are required to withhold only if your employee asks you to and you agree to withhold. (In that case, have the employee fill out a Form W-4 and give it to you, so you can withhold the correct amount.) However, you may be required to withhold Social Security and Medicare tax (FICA). And you may also be required to pay (but not withhold) federal and state unemployment (FUTA and SUTA) tax.

**FICA:** You are required to withhold and pay FICA taxes if your employee earns cash wages of \$2,400 or more (excluding the value of food and lodging) during calendar year 2023. If you reach the \$2,400 threshold, all of the wages (not just the excess) will be subject to FICA. However, if your employee is under age 18 and this isn't their principal occupation, you don't have to withhold FICA taxes. Thus, if your employee is really a student under age 18 who is a part-time baby-sitter, there's no FICA tax liability for their services. On the other hand, if your employee is under age 18 and the nanny job is their principal occupation, you must withhold and pay FICA taxes.

You should withhold from the start if you expect to meet the \$2,400 test; your employee won't appreciate a large, unexpected withholding from their pay later on. If you aren't sure if the test will be met, you can still withhold from the start. If it turns out the \$2,400 isn't reached, just repay the withheld amount. (If you make an error by not withholding enough, withhold additional taxes from later payments.)

Both the employer and the employee have an obligation to pay FICA taxes. As an employer, you are responsible for withholding your employee's share of FICA. In addition, you must pay an additional amount for your share of the taxes. The FICA tax is divided between Social Security and Medicare. The Social Security tax rate is 6.2% for the employee and 6.2% for the employer equaling a total rate of 12.4%. The Medicare tax is 1.45% each for both an employer and an employee for a total rate of 2.9%

*Example:* Assume you pay your nanny \$300 a week. You must withhold a total of \$22.95, consisting of \$18.60 for your nanny's share of Social Security tax ( $\$300 \times 6.2\%$ ) and \$4.35 ( $\$300 \times 1.45\%$ ) for your nanny's share of Medicare tax. You would pay her a

net of \$277.05 (\$300 - \$22.95). For your (employer's) portion, you must pay \$22.95 (\$18.60 Social Security and \$4.35 Medicare). The total taxes owed on the \$300 gross wage is \$45.90.

Instead of withholding, you may prefer to pay your employee's share of Social Security and Medicare taxes from your own funds. If you do pay your employee's share of these taxes for them, your payments aren't counted as additional cash wages for Social Security and Medicare tax purposes. In other words, you don't have to compute tax on the taxes. (But your payments of their taxes are treated as additional income to the employee for federal income tax purposes, so you would have to include them as wages on the Form W-2 you provide) Thus, using the figures from the above example, for each \$300 wages, you would pay your nanny the full \$300 and also pay all of the total \$45.90 in taxes (i.e., both the employee and your tax amounts). Your employee would pay income tax on \$322.95 (\$300 gross plus the \$22.95 you paid on their behalf)

**FUTA:** You also have an obligation to pay (but not withhold) FUTA taxes if you pay a total of \$1,000 or more in cash wages (excluding the value of food and lodging) to your employee in any calendar quarter of the current year or last year. The FUTA tax (at a maximum rate of 6.0%) applies to the first \$7,000 of wages paid. You pay the FUTA, not the employee, so don't withhold FUTA from the employee's wages. If you pay all your state unemployment obligations (see below) the maximum rate can be reduced by up to 5.4% to a rate of 0.6% on the first \$7,000 of wages.

**Reporting and paying:** These taxes add to your personal tax liability. You must satisfy your "Nanny Tax" obligations by increasing your quarterly estimated tax payments or increasing your withholding from your wages, rather than making an annual lump-sum payment.

As an employer of a household employee, you don't have to file any of the normal employment tax returns, even if you're required to withhold or pay tax (unless you own your own business, see below). Instead, you just report the employment taxes on your tax return, Form 1040, Schedule H.

On your income tax return, you must include your employer identification number (EIN) when you report the employment taxes for your employee. The EIN isn't the same number as your social security number. If you already have an EIN from a previous household employee, you may use that number. If you need an EIN, you must file Form SS-4 to get one. You will also need a state identification number if you withhold state income taxes and a state unemployment identification number. Those numbers cannot be obtained until you have your Federal EIN.



However, if you own a business as a sole proprietor, you must include the taxes for your employee on the FICA and FUTA forms (Forms 940 and 941) and state reporting forms that you file for your business. And you use the identification numbers from your sole proprietorship to report the taxes for your employee.

You're also required to provide your employee with a Form W-2 by January 31, 2023 if their 2022 wages are subject to FICA or income tax withholding. Additionally, you must file a Form W-2 with the Social Security Administration by January 31, 2023. Your EIN must be included on the Form W-2.

**MN Unemployment Insurance (MN UC):** You have an obligation to pay (but not withhold) Minnesota unemployment insurance once you pay more than \$1,000 in wages in a calendar quarter. Minnesota has a quarterly filing requirement. The due dates of the quarterly returns AND payments are April 30, July 31, October 31 and January 31. There are substantial penalties for not paying on time. All reporting must be done online. Taxable wages for MN unemployment purposes include the value of room, board and other non-cash advantages.

**Record-keeping:** Be sure to keep careful employment records for each household employee. Keep the tax records for at least four years from the later of the due date of the return or the date when the tax was paid. Records should include: employee name, address, social security number; dates of employment; dates and amount of wages paid; dates and amounts of withheld FICA or income taxes; amount of FICA taxes paid by you on behalf of your employee; dates and amounts of any deposits of FICA, FUTA, MN UC or income taxes; and copies of all forms filed.

We realize this is a lot of information to absorb. We'd be happy to go over any questions you still have about how to comply with these employment tax requirements. We can assist you in obtaining the appropriate ID numbers, filing the required forms and preparing any necessary W-2's. If you think you might have any problems for earlier years we can also help. We look forward to hearing from you.

### **One final word - What if YOU are the worker?**

If you are the babysitter, personal care attendant, lawn-mower, etc. YOU have a responsibility to report ALL income on your personal tax return regardless of whether or not you receive a 1099 or W2. All income is subject to income tax unless specifically excluded. There is no exclusion for payment for services rendered no matter your age or what the services are.