



Insight Paper # 04:

Arranging Household Help – The "Nanny Tax" Law

It's tough enough to find the right person to care for your child in the home, without having to worry about the tax complications of becoming a household employer. And although the rules have been liberalized in some ways, other requirements are just as stringent as they've always been. Here's a snapshot of what you must do to steer clear of trouble with the IRS when you hire someone to take care of your children in the home.

Social Security and Medicare tax (FICA). If you have household workers, you are required to withhold and pay FICA taxes if cash wages paid in 2009 total \$1,700 or more. As the employer, you have to report and pay the required employment taxes for these domestic employees on Schedule H (Household Employment Taxes), with the tax amount then transferring to the appropriate line on your Form 1040 or 1040A. Not paying the "nanny tax" is income tax evasion. There is one limited FICA exception for wages paid to domestic employees who are under 18. Social security and Medicare tax doesn't apply at all to these employees if domestic work isn't their principal occupation. This exception may help with steady evening and weekend baby-sitters, but otherwise it's not important to those parents who need help with children during the day.

Unemployment tax (FUTA). You must pay the FUTA tax for any household employee whom you pay \$1,000 or more in a calendar quarter. The effective FUTA tax rate varies state-by-state. We can give you all the details.

Payroll tax paperwork. The FICA and FUTA you owe for any household employee is computed on Schedule H of Form 1040 and paid along with your regular income tax bill. Although you're not required to make estimated tax payments for FICA and FUTA, it might be a good idea to make quarterly payments to avoid winding up with an unexpectedly large bill at tax return time. We can assist you in determining the appropriate amount of any quarterly tax payments you may choose to make.

Federal income tax withholding. Thankfully, you aren't required to withhold federal income tax from the wages of household employees. But you are required to file a Form W-2 for every domestic employee whose wages are subject to the social security tax. And you will need to get an Employer Identification Number for yourself, which is not the same as your social security number. We can assist you in obtaining a federal Employer Identification Number.



If you pay the nanny's share of social security taxes in addition to your share rather than have the nanny incur that expense, you or the nanny won't need to pay additional social security taxes on that amount. The nanny, however, will be considered to have additional income for income tax purposes.

There may be other tax complications as well. For example, depending on state law, many employers of even household help may have to file and pay state unemployment insurance tax for each quarter in which the state wage threshold is reached. And the rules may be somewhat different if you have other employees.

Although you are not required to do so, your household employee may ask you to withhold federal income tax. If you agree, you should be aware of the Making Work Pay credit (MWPC), which is provided to employees through reduced income tax withholding. The MWPC is equal to the lesser of 6.2 percent of the nanny's earned income or \$400.

As you can see, the tax rules for child-care help are still complicated. We're in a position to advise you of the least troublesome way to take care of all your tax responsibilities. Please do not hesitate to call if we can be of assistance to you.

The Marston Group, PLC