



**Re: Extension of Employee Payroll Tax Reduction**

Dear Client:

The Temporary Payroll Tax Cut Continuation Act of 2011 (2011 Tax Cut Act) temporarily extends the two percent payroll and self-employment tax cut that was scheduled to expire at the end of 2011. The 2011 Tax Cut Act reduces the Social Security tax withholding rate from 6.2 percent to 4.2 percent on wages paid through Feb. 29, 2012, and reduces the self-employment tax from 12.4 percent to 10.4 percent through calendar year 2012. This reduced Social Security tax will have no effect on future Social Security benefits.

Employers should implement the new payroll tax rate as soon as possible in 2012 but not later than Jan. 31, 2012. For any Social Security tax over-withheld during January, employers should make an offsetting adjustment in workers' pay as soon as possible but not later than March 31, 2012.

Under the terms negotiated by Congress, the law also includes a new "recapture" provision, which applies only to those employees (or the self-employed who also earn wages) who receive more than \$18,350 in wages during the two-month period (the Social Security wage base for 2012 is \$110,100, and \$18,350 represents two months of the full-year amount). This provision imposes an additional income tax on these higher-income employees in an amount equal to 2 percent of the amount of wages they receive during the two-month period in excess of \$18,350 (and not greater than \$110,100).

This additional recapture tax is an add-on to income tax liability that the employee would otherwise pay for 2012 and is not subject to reduction by credits or deductions. The recapture tax would be payable in 2013 when the employee files his or her income tax return for the 2012 tax year. With the possibility of a full-year extension of the payroll tax cut being discussed for 2012, the IRS will closely monitor the situation in case future legislation changes the recapture provision.

The IRS will issue additional guidance as needed to implement the provisions of this new two-month extension, including revised employment tax forms and instructions and information for employees who may be subject to the new "recapture" provision. For most employers, the quarterly employment tax return for the quarter ending March 31, 2012, is due April 30, 2012.

Sincerely,

HEINOLD-BANWART, LTD.