Frequently Asked Tax Questions

Answers to questions that may be on your mind. If you have any more questions, just let us know.

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Nanny.com

Is my worker a Household Employee or an Independent Contractor?

Most household workers are employees of the family for which they work. The difference between employees and independent contractors hinges on the amount of control one has over the worker. If the family controls work hours, work place, responsibilities, work tools (to name just a few), the worker is their employee. An independent contractor usually provides her own tools, her own place of work, sets her own hours and offers services to the general public. In addition, an independent contractor is responsible for both employee and employer payroll taxes. A household employee has payroll taxes withheld each pay period. The employee taxes withheld, along with employer payroll taxes, are remitted to federal and state tax agencies by household employers throughout the year.

What employee taxes need to be withheld each pay period?

Your employee's taxes usually range from 15-20% of gross wages. These include:

- Half of Social Security & Medicare (7.65% of employee's gross wages)
- Federal income taxes (based on the number of allowances chosen on Form W-4)
- State income taxes (if applicable)

Note: By law, employers are required to withhold Social Security and Medicare taxes from their employee's salary each pay period. Income taxes do not have to be withheld, but it is highly recommended in order to help your employee avoid a large tax obligation at year end.

Do I have taxes as an employer?

Yes. Household employers can expect to pay the following employment taxes:

- Half of Social Security & Medicare (7.65% of employee's gross wages)
- Federal and state unemployment insurance (usually 2-3% of employee's gross wages)

Good News! The employer tax breaks can offset most – if not all – of the employer taxes.

What are my tax breaks?

To lighten the burden that falls on working parents, Congress has enacted tax benefits for families through employer-provided dependent care assistance (Dependent Care Account) and the Tax Credit for Child or Dependent Care. However, these tax breaks are only available if the employee is paid legally.

Dependent Care Account. Most companies allow employees with child or dependent care expenses to contribute up to $5,000 of their pretax earnings to an individual Dependent Care Account. The money in this account is then used to cover childcare expenses, free of taxes. The savings are approximately $2,300 per year.

Tax Credit. For those who don't have access to a Dependent Care Account, they can claim the Tax Credit for Child or Dependent Care (Form 2441) on their income tax return at year-end. Basically, they can take a tax credit of 20% to 30% of qualifying childcare expenses. But only expenses of up to $3,000 for one dependent, or up to $6,000 for two or more dependents can be counted.

Note: The Dependent Care Account usually provides the greater tax savings. Oftentimes, the tax savings exceed the employer's share of the taxes – actually saving money by being legal!

Do I have to pay overtime?

According to federal law, household employees are entitled to overtime pay for all hours worked over 40 in a 7-day work-week. Overtime must be paid at 1.5 times the hourly wage. If a household employee is paid a salary, overtime should be addressed in the contract by breaking the salary into two pieces: the regular rate and the overtime rate. For example, an employee and family agree upon a gross salary of $600 per week for a 45-hour workweek. The regular rate for the first 40 hours is $12.63 per hour; the overtime rate for the remaining 5 hours per week is $18.94 per hour; and the total weekly salary is $600.

No limit is placed on the number of hours worked in a 7-day workweek, as long as the employment contract is fulfilled and the employee is fairly compensated.

Please note that **Live-In** household employees do not have to be paid overtime but are entitled to the regular wage for every hour worked (exception: live-in employees in the state of New York must be paid overtime for hours over **44** in a work week).

What are the requirements for vacation, holidays and sick days?

Paid vacation, holidays and sick days are not required by law (exception: San Francisco employers must provide paid sick leave; please call for details). Additionally, overtime is not required for holidays worked. These benefits are to be agreed upon as part of the employment agreement.

What is the process for handling payroll and taxes?

The payroll and tax process is quite detailed. Here's an overview of what's involved:

- Research employment tax and labor laws to understand legal obligations.
- Register for federal and state tax accounts.
- Complete and file New Hire Reporting.
- Identify and calculate taxes to withhold each pay period.
- Track gross pay, net pay and taxes withheld.
- Calculate the employer's federal and state tax liabilities.
- Prepare state and federal tax returns quarterly and remit the employer and employee taxes.
- Prepare year-end tax documents (W-2, W-3, Schedule H and state annual reconciliations).
- Respond to IRS and state inquiries.
- Monitor ever-changing household employment tax law.

Note: Comprehensive services offered by Breedlove & Associates can make this process simple and provide peace of mind at an affordable price.

What is Workers' Compensation?

Every state has a workers' compensation system. Under these systems, workers injured on the job are entitled to prompt payment of certain medical and wage-loss benefits with a minimum of legal formality and expense. The systems are based on the idea that the employee gives up the right to sue for any injuries from work-related accidents in exchange for receiving benefits regardless of fault. Most states now require household employers to procure a Workers' Compensation policy on their household employees. However, check with your homeowner's insurance provider first. Often, homeowner's policies include Workers' Compensation coverage for domestic employees. If it's not already included on your policy, usually they can add a rider. For more information on policies and benefits, see your state government web site or call us.

Are there tax breaks if I offer health insurance?

Yes. When a household employer contributes toward health insurance premiums, these dollars are not considered taxable income. Neither employer nor employee is required to pay taxes on these dollars. Families can choose to pay the health-care premium directly to the health insurance company or pay indirectly by giving these dollars to their employee. In this case, the family must keep a copy of a current health insurance card on file for proof of a current insurance policy.

Can I run my nanny's payroll through my own business?

No, this is illegal. Here's a simple explanation of the law: All businesses are allowed to take tax deductions on employee payroll. The logic is that employees are direct contributors to the success of the business, and therefore, the owner is allowed a "tax break" on a portion of total payroll to offset some of this expense. A nanny does not directly contribute to a business; therefore, it is illegal for a business to receive any kind of "tax break" on her payroll. A nanny is considered a contributing member of the household; therefore, the family is entitled to take a "tax break" on her payroll as a childcare expense instead.

Tax & Payroll Services for Household Employers