CLIENT ALERT: Hiring Incentives to Restore Employment Act Provides Tax Incentives to Encourage Employers to Hire and Retain New Workers

On March 18, 2010, President Obama signed into law the Hiring Incentives to Restore Employment Act ("HIRE Act"). The HIRE Act has created two new tax incentives to make it easier for qualified employers to hire and retain new workers. Specifically, the HIRE Act provides for payroll tax forgiveness and a retention credit of up to $1,000 per worker.

Payroll Tax Forgiveness

The HIRE Act's payroll tax forgiveness exempts employers from paying the 6.2% Social Security portion of the Federal Insurance Contribution Act ("FICA") taxes on qualified new hires through the end of this year. This reduced tax withholding will not affect the employee's future Social Security benefits. Employers must still withhold the employee's 6.2% share of Social Security taxes, as well as income taxes. Also, the employer and employee's shares of Medicare taxes still apply to these wages. Qualified employers include businesses, agricultural employers, tax-exempt organizations and public colleges and universities. Household employers and government employers cannot claim this new tax benefit.

To qualify, the employer must hire an unemployed worker between February 3, 2010 and January 1, 2011. Qualified employees are those who have been unemployed or employed for less than 40 hours during the 60-day period ending on the date such employment begins. Family members of the employer or persons who own (directly or indirectly) more than 50% of the business are not qualified employees. The new employee can be an employee who was previously laid off by the employer or a recent graduate who was in school during the 60-day period preceding the start of employment. However, the new employee cannot take the place of an existing employee unless the existing employee leaves voluntarily or is terminated for cause. The new hire does not have to be hired as a full-time employee.

Upon hire, the new employee must certify by a signed affidavit, under penalties of perjury, that they have not been employed for more than 40 hours during the 60-day period ending on the date they started employment. A copy of this affidavit is available here.

Employers may claim the payroll tax exemption for wages paid to qualified employees during the first quarter on the employer's Form 941, Employer's Quarterly Federal Tax return, beginning with the second quarter of 2010. Employers may claim both the COBRA premium assistance credit and the HIRE Act payroll tax exemption for new hires on the same tax return. However, employers may not claim both the HIRE Act payroll tax exemption and the Work Opportunity Tax Credit in the same year.

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If the Work Opportunity Tax Credit would provide the employer a greater tax benefit than the payroll tax exemption, the employer can elect to pay the Social Security tax for the qualified employee so they can take the credit. Wages in excess of $106,800 are not subject to the Social Security payroll tax. Therefore, the maximum value of the payroll tax exemption is 6.2% of covered wages per employee up to $106,800, or $6,621.60.

Retention Credit

Employers may claim the retention credit for each employee who qualifies for the payroll tax forgiveness and who remains an employee for 52 consecutive weeks. The employer must also pay the employee wages equal to at least 80% of the wages paid during the first 26 weeks of the 52 consecutive week period, during the last 26 weeks of the period. The retention credit is equal to the lesser of $1,000 or 6.2% of the retained worker's wages during the 52 consecutive week period. Employers may claim the retention credit on their 2011 income tax return. The credit may be carried forward, but not backward. There is no partial credit if the employee leaves before the end of the 52-week period, even if the departure is voluntary.

As regulatory guidance interpreting the HIRE Act is still forthcoming, employers are advised to consult with their MBJ attorney with any questions about this or any other labor and employment related issues.

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