FEDERAL TAX
LEGISLATION UPDATE

THREE PERCENT WITHHOLDING REPEAL AND JOB CREATION ACT (H.R. 674)

The House passed this Act on November 16, 2011 after it was passed by the Senate on November 10th. President Obama signed the Three Percent Withholding Repeal and Job Creation Act into law on November 21, 2011. The primary tax provisions in this law repeal the required three percent withholding provision on government contractors which were going to become effective in 2013 and extend the work opportunity tax credit for one year for certain qualified veterans. The repeal of withholding requirements and additional tax credits under this act are offset by changes to eligibility for benefits under the Affordable Health Care Act and delays in scheduled reductions in fees for VA mortgages.

Following is a summary of some of the key income tax provisions affecting individuals and businesses enacted in this legislation:

KEY CHANGES TO BUSINESS TAXES

- **REPEAL OF THREE PERCENT WITHOLDING ON PAYMENTS TO GOVERNMENT CONTRACTORS** – This act repeals the three percent withholding requirement on federal and state government contractors, originally created by the Tax Increase Prevention and Reconciliation Act of 2005 (TIRPA), that was scheduled to be effective January 1, 2012.[i]

- **RETURNING VETERANS TAX CREDITS** – This Act extends the work opportunity tax credit (WOTC) for qualified veterans through December 31, 2012, creating new provisions entitled the "Returning Heroes and Wounded Warriors Work Opportunity Tax Credits." For other classes of individuals (*i.e.*, non-veterans) the program still expires December 31, 2011.
  - Generally the WOTC allows a credit of 40% of the first $6,000 of qualified first year wages for hiring certain classes of targeted individuals. The credit is limited for employees working less than 400 hours of service in the first year and disallowed for employees working less than 120 hours. While veterans receiving food stamps and veterans with service related disabilities were already targeted groups under the WOTC, this Act extends and expands the credit available for hiring veterans.
  - The Act adds a new class of qualified veterans, veterans who are unemployed for at least four weeks in the year before they are hired, and increases the limit on wages eligible for the credit for all qualified veterans who are unemployed for at least six months in the year before they are hired. The wage limits and credits under the act are:

Unemployed Veterans

Unemployed:	Eligible wages:	Max Credit:
More than four weeks (but less than six months)	$ 6,000	$2,400
Unemployed more than six months	$14,000	$5,600

Veterans with Service Related Disability

Unemployed:	Eligible wages:	Max Credit:
Hired within one year of discharge	$12,000	$4,800
Unemployed more than six months	$24,000	$9,600

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- COMPLIANCE - As previously required under the WOTC, state workforce agencies must certify individuals eligible for the credit. Employers must complete Form 8850, *Pre-screening Notice and Certification for Work Opportunity Tax Credit*. The prescreening notice must be completed no later than the day the employee is offered a job and **the pre screening notice must be submitted to the designated agency within 28 days after the employee commences work.**

- CREDITS FOR TAX EXEMPT ORGANIZATIONS FOR EMPLOYING QUALIFIED VETERANS – The Act provides that tax exempt organizations will be allowed a payroll tax credit in the amounts that would be allowable under the work opportunity credit for hiring qualified veterans against their FICA obligation on wages paid to the veteran in the year after the veteran is hired.

  The percentage rates for credits allowed for tax exempt organizations are less than those allowed to for-profit businesses under the Act:

  - For tax-exempt organizations, the percentage of first year wages will be 26 percent (instead of 40 percent).
  - For employees performing fewer than 400 hours of service, the credit will be 16.25 percent (instead of 25 percent).

REVENUE OFFSETS

This Act provides for changes to income calculations for premiums under the 2010 Patient Protection and Affordable Care Act and also adds levies for vendors with unpaid tax liabilities.

- CHANGES TO THE DEFINITION OF AGI FOR ELIGIBILITY FOR BENEFITS UNDER THE HEALTH CARE ACT – The Act amends IRC §36B(d)(2) to include all social security benefits (adding amounts otherwise excluded from gross income) in the definition of AGI for purposes of eligibility for premium assistance tax credits under the Affordable Health Care Act.

- LEVIES ON GOVERNMENT VENDORS WITH FEDERAL TAX DELINQUENCIES – The Act amends existing law to expand the types of vendors subject to a 100% levy on payments due to vendors who have unpaid federal tax liabilities. In addition to vendors providing goods and services, vendors who sell or lease property to the government will be subject to such levies. This provision is effective for levies issued after November 21, 2011.

OTHER PROVISIONS

The Act also provides for various non-tax incentives and programs to promote employment and job training for veterans, delays scheduled reductions in fees for VA mortgage applications, allows veterans to begin the federal unemployment process before separation from service, and instructs the Treasury Department to prepare a report on methods to reduce the amount of unpaid tax owed by federal contractors.

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i. Implementation of the withholding requirement was delayed under the American Recovery and Reinvestment Act of 2009 (ARRA).

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