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# Treasury Financial Manual

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Transmittal Letter No. 609

Volume I

To: Heads of Government Departments, Agencies, and Others Concerned

## 1. Purpose

This transmittal letter releases revised I TFM 3-4000: Federal Income, Social Security, and Medicare Taxes. This chapter prescribes procedures for withholding, depositing, reporting, and paying taxes as follows:

- Withholding and depositing Federal income, Social Security, and Medicare taxes on wages paid to civilian and military employees.
- Filing tax returns with the Internal Revenue Service (IRS) for Federal income, Federal Insurance Contributions Act (FICA), Social Security, and Medicare taxes withheld.

## 2. Page Changes

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## 3. Effective Date

Upon receipt.

## 4. Inquiries

Direct questions concerning this transmittal letter to:

Office of Chief Counsel  
Internal Revenue Service  
Office of the Associate Chief Counsel  
(Employee Benefits and Exempt Organizations)  
1111 Constitution Avenue, NW., Room 5325  
Washington, DC 20224  
Telephone: 202-622-6040

Date: April 30, 2003

Richard L. Gregg  
Commissioner

## Part 3—Chapter 4000

# FEDERAL INCOME, SOCIAL SECURITY, AND MEDICARE TAXES

This chapter prescribes procedures for withholding, depositing, reporting, and paying taxes as follows:

- **Withholding and depositing Federal income, Social Security, and Medicare taxes on wages paid to civilian and military employees.**
- **Filing tax returns with the Internal Revenue Service (IRS) for Federal income, Federal Insurance Contributions Act (FICA), Social Security, and Medicare taxes withheld.**

### Section 4010—Scope and Applicability

Employers must withhold income taxes and the employee's portion of Social Security and Medicare taxes and pay the employer's portion of Social Security and Medicare taxes on wages paid to an employee. (See also TFM subsection 4020.30.)

For further instructions and/or guidance on these matters:

- Refer to IRS Circular E, Publications 15, *Employer's Tax Guide*, and 15-A, *Employer's Supplemental Tax Guide*. Circular E describes employer tax responsibilities: withholding, depositing, reporting, and paying taxes. It explains the forms employees use and the forms employers send to IRS and SSA.
- Contact an IRS office for additional information.

### Section 4015—Authority

Procedures in this chapter are authorized by provisions in the Internal Revenue Code (the IRC) [Title 26 of the

United States Code (U.S.C.)] regarding Federal income tax withholding, and Social Security and Medicare taxes under FICA. Services performed in the employ of the United States are excepted from the tax imposed under the Federal Unemployment Tax Act (FUTA) [IRC section 3306(c)(6)].

The head of an agency, or a delegate, subject to the Department of the Treasury (Treasury) regulations, has the authority to determine [IRC section 3122]:

- Whether the services performed by Federal employees constitute employment.
- The periods of such employment.
- Whether the remuneration paid for such services constitutes wages.

All employers, including Federal agencies, must deduct and withhold Federal income taxes from wages that exceed the total amount of withholding exemptions [IRC section 3402(a)]. If the employer is the United States or any agency or instrumentality of the United States, any officer or employee of the United States having control of the

payment of wages or an appropriate designee may file the tax return for the amount deducted and withheld from wages [IRC section 3404].

### Section 4020—Federal Withholding Rules

#### 4020.10—Specific Rules

IRC section 3101 imposes the employee's portion of Social Security and Medicare taxes on wages paid to the employee. IRC section 3102 requires the employer to withhold these amounts from wages paid to employees.

IRC section 3111 imposes the employer's portion of the Social Security and Medicare taxes on wages paid to employees.

#### 4020.20—Federal Income, Social Security, and Medicare Deposits

Most large agencies must make their tax deposits electronically [IRC section 6302(h)]. Employer agencies send withheld Federal income, Social Security, and Medicare taxes to the IRS through the FEDTAX II system. Those

agencies not established on the FEDTAX II system must contact FEDTAX II customer service or the Financial Services Division, Financial Management Service (FMS). See the Contacts page for the telephone numbers.

See Appendix 1 for the FEDTAX II User Profile Sheet and Appendix 2 for the Application for FEDTAX II Form 941 PIN Code.

If FEDTAX II is unavailable because a commercial financial institution rather than Treasury disburses the funds, agencies use the Electronic Federal Tax Payment System (EFTPS). See Circular E for instructions on enrolling in EFTPS.

#### **4020.30—Federal Income, Social Security, and Medicare Taxes Regarding Employee or Independent Contractor**

Generally, an employer must withhold income taxes and pay Social Security and Medicare taxes on wages paid to an employee. Employers do not have to withhold or pay any taxes on payments to an independent contractor. There is, however, a requirement to issue information returns for payments of \$600 or more in a calendar year to independent contractors. See Appendix 3, Guide to Information Returns, Form 1099-MISC.

#### **4020.40—Employee/Independent Contractor Status**

To determine a worker's status as an employee or an independent contractor, apply the common law rule:

*An employer-employee relationship exists when the person for whom the services are performed has the right to control and direct the individual who performs the services.*

This control refers not only to the result to be accomplished but also to the means and details by which that result is accomplished. An employee is subject to the will and control of the employer not

only as to what work must be done, but, also, as to how it will be done. It is not necessary that the employer actually direct or control the manner in which the services are performed; it is sufficient that the employer has the right to do so.

Employee status is determined by the presence of the employer's right to control. The sum of all the facts and circumstances always determines whether this right exists. See IRS Publication 15-A for more information.

Employers that want the IRS to decide if a worker is an employee should submit Form SS-8: Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding, to the IRS office listed on the Contacts page.

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### **Section 4025—IRC Instructions**

#### **4025.10—Withholding and Deducting Federal Income Tax**

Employers, including Federal agencies, must deduct and withhold Federal income taxes from wages [IRC sections 3402(a) and 3404].

#### **4025.20—Withholding Additional Income Tax**

Employers may withhold additional amounts of Federal income tax by agreement between the employer and the employee [IRC section 3402(i)]. The employee may claim fewer exemptions or may have an additional fixed amount withheld each pay period.

#### **4025.30—Additional Withholding Allowance**

Employees may claim additional withholding allowances based on estimated itemized deductions and credits [IRC section 3402(m)]. Form W-4: Employee's Withholding Allowance Certificate, provides a

schedule and instructions for determining total withholding allowances.

#### **4025.40—Withholding Not Required**

Employers should not deduct and withhold Federal income tax from employee wages when the employee certifies (as prescribed by IRS) that no income tax liability was incurred the preceding year nor is one anticipated for the current year [IRC section 3402(n)].

#### **4025.50—Rounding Amounts of Federal Income Tax Withheld**

Employers may round to the nearest dollar the tax withheld from each employee. Rounding eliminates amounts less than 50 cents and increases amounts greater than 50 cents to the next higher dollar.

#### **4025.60—Submission Requirements for Form W-4**

Employers must submit a copy of Form W-4 to the IRS if an employee claims 10 or more withholding allowances or exemption from withholding when he or she earns more than \$200 a week. Before filing the FEDTAX II Form 941: Employer's Quarterly Federal Tax Return, send Forms W-4 to the local IRS Service Center (see the IRS Web site at <http://www.irs.treas.gov> for addresses) with a cover letter giving the agency name, address, Employer Identification Number (EIN), and number of forms attached. Alternatively, attach the W-4's to a paper Form 941. If IRS informs the agency in a written notice that the employee's Form W-4 is defective, the agency must provide the employee a copy of the notice. The agency should withhold based on the maximum number of allowances in the notice unless the employee files a new Form W-4 that is consistent with the notice.

**4025.70—Expiration of Form W-4**

Employees must submit new Forms W-4 by February 15 if they claim exemption from withholding. If an employee does not do so, the employer must withhold taxes as though the employee was single, claiming zero exemptions.

**4025.80—Backup Withholding**

Backup withholding is required in the following situations:

- An employee does not provide the employer with a Taxpayer Identification Number (TIN).
- IRS tells the employer that an employee's TIN is incorrect.
- IRS notifies the employer that backup withholding is required.

For amounts paid before August 6, 2001, the backup withholding rate is 31 percent. For payments on and after August 6, 2001, the rate is 30.5 percent. For payments after December 31, 2001, the rate is 30 percent.

**Section 4030—Federal Insurance Contributions Act (FICA)**

Employers must deduct and withhold the employee's portion of FICA taxes from wages paid to employees [IRC section 3102]. Employers must pay the employer's portion of the FICA tax [IRC sections 3111 and 3112]. FICA taxes consist of two different taxes:

- Old-Age, Survivors and Disability Insurance (OASDI) (Social Security tax) [IRC sections 3101(a) and 3111(a)].
- Hospital insurance (Medicare tax) [IRC sections 3101(b) and 3111(b)].

**4030.10—Civilian Employees Hired before January 1, 1984**

Civilian employees hired before January 1, 1984, and covered under the Civil Service Retirement System (CSRS) are not subject to the Social Security tax. These employees are only subject to the Medicare tax [IRC sections 3121(b)(5) and 3121(u)(1)].

**4030.20—Employees Subject to Social Security and Medicare Taxes**

Both Social Security and Medicare taxes are imposed on the following groups:

- All Federal employees hired on or after January 1, 1984, including those with previous Federal service who have experienced a break in Federal service of 366 or more days.
- All legislative branch employees not participating in the CSRS as of December 31, 1983.
- All members of Congress, the President, and the Vice President.
- All sitting Federal judges, executive level and noncareer appointees in the Senior Executive Service, and noncareer members of the Senior Foreign Service.

**4030.30—Employees Not Covered for Social Security and Medicare under the IRC**

The following employees are not covered for Social Security and Medicare under the IRC:

- Inmates of a U.S. penal institution.
- Student nurses, student dietitians, and student physical or occupational therapists described in 5 U.S.C. section 5351(2), who are attached to a

hospital or clinic, etc., operated by the U.S. Government. Medical or dental interns or residents in training are subject to the rules described in TFM subsections 4030.10 and 4030.20.

- Individuals serving under temporary conditions in connection with emergencies due to fire, storm, earthquake, flood, or other similar emergencies.

**Section 4035—Correcting Income and FICA Tax Withholding Errors**

An agency should correct errors in withholding income taxes made in a prior pay period of the current calendar year if the employee is still on the agency's payroll. Employer agencies:

- Make corrections by adjusting the current pay period deduction by an amount that offsets the error in the employee's withheld income taxes and net pay.
- Make no adjustment if the error occurred in a prior calendar year or the employee is no longer on the payroll. The employee makes the adjustment when filing the employee's individual Federal income tax return.
- Correct errors in withholding FICA taxes on Form 941 and prepare Form 941c: Supporting Statement To Correct Information, to explain the correction. If unable to make such adjustments, claim a refund by filing Form 843: Claim for Refund and Request for Abatement.

If an agency makes an adjustment or applies for a refund of FICA and Medicare taxes overcollected from an employee, the agency must repay the employee's portion to the employee. Obtain from the employee a written receipt showing the date and amount of

the repayment and a written statement that the employee will not claim a refund or credit for the amount.

Generally, an agency may make an adjustment or claim for refund only within 3 years of the due date of the return or the date the return was filed, whichever is later. For statute of limitations purposes, the filing date for Forms 941 is April 15 of the year after the calendar year for which the forms were filed. For example, the four quarterly Forms 941 for 1998 are all treated as filed on April 15, 1999, provided they were filed timely. If 1998 Forms 941 were filed on or before April 15, 1999, agencies may make adjustments for any of the quarterly returns until April 15, 2002.

FEDTAX II Form 941 filers should send the Form 941c by fax to the IRS Memphis Service Center. Refer to Circular E and the FEDTAX II User Guide for further instructions.

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### **Section 4040—Privacy Act Requirements**

Each agency must publish notices for routine use in the Federal Register in accordance with the Privacy Act of 1974. These notices must indicate information routinely disclosed by the agency to IRS and SSA and the circumstances under which disclosure is made.

If Federal forms used by the agency do not include a Privacy Act notice, the agency must provide a separate Privacy Act notice to the employee from whom information is solicited. A suggested notice follows:

*The Social Security number is required for identification purposes by Executive Order 9397, dated November 22, 1943. Other information is required under 26 U.S.C. section 3401-04 for collecting taxes at the source by withholding from wages. The information is used to compute the amount withheld,*

*and, if not furnished, a violation of the Internal Revenue laws may occur.*

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### **Section 4045—Accounting for Taxes**

#### **4045.10—Withheld Taxes**

Agencies must report separately on FEDTAX II or EFTPS Federal income, Social Security, and Medicare taxes withheld from employees' wages.

The Social Security Administration (SSA) records these amounts separately in employees' permanent earnings records.

#### **4045.20—Employer's Social Security and Medicare Tax**

Each agency employing individuals covered by Social Security and Medicare tax must pay the employer's share of these taxes on the employees' salaries and wages. These taxes are disbursed each pay period from the appropriation from which the payroll is paid. They are included with the amount of taxes withheld from employees' compensation in the payment issued for the taxes and reported on the employee's W-2: Wage and Tax Statement.

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### **Section 4050—Payment of Taxes**

#### **4050.10—Electronic Payment of Taxes**

Agencies whose funds are disbursed by Treasury should use FEDTAX II; agencies whose funds are disbursed from a commercial financial institution should use EFTPS.

#### **4050.20—Deadlines for Deposits**

Agencies must submit tax deposits in time to ensure credit to the Treasury's

General Account by the tax due date. Agencies that make payments using FEDTAX II must transmit the payments no later than the payment due date. Agencies that make payments using EFTPS generally must initiate payments the day before the due date, to settle on the due date.

#### **4050.30—Taxes Withheld from Supplemental Wage Payments**

Agencies must compute Federal income taxes withheld from wages other than regular salary payments following instructions in Circular E, section 7. Examples of this type of wage include the following:

- Prizes and employee awards valued at more than \$25.
- Cash awards.
- Bonuses.
- Retroactive wage increases.
- Overtime pay.
- Back pay.
- Reimbursement for nondeductible moving expenses.

Agencies must deposit the amount withheld in the same manner as other withheld taxes.

#### **4050.40—Back Pay**

Back pay is pay received in one period for employment (or potential employment) in an earlier period. Back pay is treated as wages in the year received. FICA tax and income tax withholding apply in the year of payment using the rates and the wage base in effect for that period. Back pay does not include amounts specifically and legitimately designated otherwise, for example, interest, penalties, and legal fees.

If the agency did not include back pay as wages on a previously filed Form W-2, the agency should prepare a wage correction report, on Form W-2c or

magnetic media, to add the back pay award to the wages of that employee.

For income tax purposes, the IRS treats back pay as wages in the year paid. The SSA, however, credits back pay awarded under a statute to the year(s) when it should have been paid. The agency must notify SSA of the payment so that SSA can allocate the back pay to the appropriate periods. If the agency paid the back pay in the tax year in which it was earned, it should report the wages on that year's Form W-2. No further action is necessary.

For further information, see SSA Publication 957, *Reporting Back Pay and Special Wage Payments to the Social Security Administration*.

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### Section 4055—Filing Quarterly Tax Returns

Agencies file quarterly tax returns with IRS on Form 941. If an agency uses FEDTAX II to submit the payment, FEDTAX II generates a Form 941 for review and approval. The agency then transmits Form 941 electronically to IRS.

If agencies do not use FEDTAX II, those within the United States mail their tax returns to the IRS Service Center serving the State in which the agency office is located (see Circular E). Agencies outside the United States mail their tax returns to the Philadelphia Service Center.

Agencies should file tax returns as soon as possible after the close of each quarter but not later than the 10<sup>th</sup> day of the second month following the close of the quarter. The Philadelphia Service Center processes foreign and military APO/FPO tax returns.

Agencies enter tax payment information under Schedule B, Employer's Record of Federal Tax Liability, on Form 941 from the agencies' record of payment. The total amount of the tax payments made during the quarter should equal the total taxes due, with no further payment required

with the tax return. For FEDTAX II filers, Schedule B is automatically generated from the liability information entered with the payments during the quarter.

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### Section 4060—Filing Annual Information Returns

This section applies to departments and agencies required to file annual information returns with SSA, covering salaries and wages, or with the IRS, covering other types of transactions subject to information reporting.

Keep records for at least 4 years and have them available for IRS review. Records should include:

- Employer Identification Number (EIN).
- Amounts and dates of all wage, annuity, and pension payments.
- The fair market value of in-kind wages paid.
- Names, addresses, Social Security numbers, and occupations of employees and recipients.
- Dates of employees' and recipients' employment.
- Periods for which employees and recipients were paid while absent due to sickness or injury, and the amount and weekly rate of payments made by the employer agency or by third-party payers.
- Copies of employees' and recipients' income tax withholding certificates.
- Dates and amounts of tax deposits made.
- Copies of returns filed.
- Records of fringe benefits provided including substantiation required under IRC section 274 and related regulations.

### 4060.10—Guide to Information Returns

Information returns include the Form W-2 series, Form 1098: Mortgage Interest Statement, and Form 1099 series. Appendix 3, Guide to Information Returns, lists these forms. For additional information, see "General Instructions for Forms 1099, 1098, 5498, and W-2G."

### 4060.20—Form W-2 Series Information Returns

The following paragraphs provide agencies with instructions on:

- Reporting and filing the Form W-2,

AND

- Reconciling Form 941 and Form W-3: Transmittal of Wage and Tax Statements.

#### **Annual Reporting**

Annually, use the Form W-2 series to report salaries, wages, and other payments to employees. In addition, agencies must file the Form W-2 and Form W-3 with the SSA.

#### **Instructions for Filing**

Refer to Circular E for information regarding classification of employees and for specific filing instructions.

#### **Reconciliation**

Reconcile the Forms 941 with wages reported on Forms W-2. Reconcile the Form W-3 with totals reported on the Form 941.

### 4060.30—Form 1099-C: Cancellation of Debt

An agency files a Form 1099-C for each debtor for whom the agency canceled a debt of \$600 or more. In addition, the agency files a Form 1099-C when an identifiable event has occurred, such as the bankruptcy discharge of the debtor.

An agency must report the forgiveness of debt regardless of whether the debtor is eligible to exclude the debt from income because of the debtor's insolvency, bankruptcy, or other reason. For further information on the reporting requirements, see the "General Instructions for Forms 1099, 1098, 5498, and W-2G." An agency should not report a debt as forgiven if the agency is attempting to collect the debt.

An agency participating in the Federal tax refund offset program or any other Federal debt collection mechanism should not report the debt as forgiven.

### **Reporting Mortgage Interest**

Agencies use Form 1098 to report mortgage interest received from individuals. The agency that receives the mortgage interest reports to the IRS and the payer. See Appendix 3 for filing requirements.

### **Taxpayer Identification Number (TIN) or Employer Identification Number (EIN)**

Forms 1098 and 1099 must show both a payer and a payee identification number. The agency must use the EIN assigned to it by the IRS. The agency's name must agree with the name used on other returns (such as Form 941) filed using this EIN. The taxpayer's identification number is the Social Security number for individuals (including operators of businesses as sole proprietorships) or the EIN for other entities.

### **Form 945: Annual Return of Withheld Federal Income Tax**

Agencies must secure a payee's TIN before issuing payments. Backup withholding is required if the payee does not furnish a TIN. See TFM subsection 4025.80 for backup withholding rates. Report backup withholding on Form 945, along with withholding on pensions and annuities. Deposit requirements for Form 945 are the same as for Form 941. Prepare and mail Form 945 to the local

IRS Service Center by February 10 of the year following the withholding.

### **Annual Reporting**

Agencies transmit Forms 1098 and 1099 to the IRS by February 28 of the year following the year for which the returns are filed. For instance, tax year 2001 returns are due on February 28, 2002. If forms are filed electronically (not by magnetic media), the due date is March 31. Statements to the payee are due by January 31. Prepare Form 1096: Annual Summary and Transmittal of U.S. Information Returns, to accompany the Forms 1098 and 1099 as a transmittal document. Prepare a separate Form 1096 for each type of document transmitted. For example, if filing Forms 1099-MISC and 1099-G, group the 1099s by type and use a separate Form 1096 as a transmittal for each group.

### **Instructions for Filing**

IRS publications *Instructions 1099* and *Package 1099* contain instructions for filing transmittal Form 1096 and Form 1099 series information returns, including Forms 1098, 1099, 5498, and W-2G. For technical specifications on magnetic media filing, refer to IRS' Revenue Procedure issued annually.

### **4060.40 — Other Reporting Requirements and Reporting Thresholds**

Report payments for services totaling \$600 or more to individuals, partnerships, and trusts. Executive agencies, military departments, the Postal Service, and the Postal Rate Commission also must report payments to corporations for services totaling \$600 or more. Federal agencies acting as financial institutions must report interest payments of \$10 or more.

## **Section 4065—Use of Magnetic Media for Filing Annual Information Returns**

### **4065.10—Scope and Applicability**

This section applies to all departments and agencies that file annual information returns. See TFM Section 4060.

### **4065.20—Magnetic Media Reporting to SSA and IRS**

#### **Magnetic Media Reporting of Form W-2 to SSA**

All agencies represented by an EIN must furnish annual information returns on magnetic media for the Form W-2 series to SSA as prescribed by SSA's magnetic media specifications. For specific instructions, see SSA's *Technical Instruction Booklet No. 4*.

#### **Magnetic Media Reporting of Form 1099 to IRS**

All agencies must furnish annual information returns for the Form 1099 series to IRS.

If an agency files 250 or more information returns, it must file on magnetic media. The 250-or-more requirement applies separately to each type of form. See IRS Publication 1220 or "General Instructions for Forms 1099, 1098, 5498, and W-2G."

#### **Installation of a New or Updated Magnetic Media System**

When an agency installs or updates a system with magnetic media reporting capability, the agency must comply with the requirements in system design and programming discussed in the previous paragraphs.

#### **Partial Use of a Computerized System**

An agency does not have to operate with a computerized system for its entire

output under that EIN to be subject to the magnetic media reporting requirements.

For example, SSA accepts the paper Form W-2 series for the noncomputerized portion of a payroll operation and magnetic media records for the computerized portion. IRS, likewise, accepts the paper Form 1099 series for the noncomputerized portion of a disbursement operation and magnetic media records for the computerized portion. File paper W-2 reports only if filing less than 250 W-2s for the year or if the IRS has granted a waiver of the magnetic media filing requirements for that year.

#### ***Use of Another Agency's Computer System***

If the payroll or other disbursement operation of an agency is serviced, in whole or in part, through another agency's computer system, the servicing agency must comply with requirements of this section. However, the EIN being reported is that of the agency authorizing payment.

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### **Section 4070—Resident and Nonresident Aliens**

In general, taxation varies for resident and nonresident aliens and could be subject to treaty provisions.

#### **4070.10—Withholding Federal Income Tax**

Generally, for wages paid to both resident aliens and nonresident aliens for services rendered in the United States as employees, agencies withhold Federal income tax according to the same rules, procedures, and rates applicable to employees who are U.S. citizens.

#### **4070.20—Withholding Exemptions**

Resident aliens may claim the full number of withholding exemptions they would be entitled to under the rules applicable to U.S. citizens. Nonresident

aliens who are residents of a contiguous country (Canada, Mexico), Japan, or South Korea also may claim the full number of withholding exemptions they would be entitled to under the rules applicable to U.S. citizens. All other nonresident aliens may claim only one withholding exemption.

#### **4070.30—Social Security and Medicare Taxes**

Nonresident aliens in the United States on "F-1," "J-1," or "M-1" visas do not pay Social Security and Medicare taxes on money earned while performing services for which such visas were granted. This income is not subject to Social Security and Medicare taxes even if it is for services not covered by the U.S. Government retirement system.

Compensation for services performed in and for the United States by other nonresident and resident aliens is subject to Social Security and Medicare taxes if such service is not covered by a retirement system established by the United States. Remuneration paid to resident aliens is subject to Social Security and Medicare taxes, whether the services are performed outside or in the United States. Remuneration paid to nonresident aliens for services outside the United States is not subject to Social Security and Medicare taxes. Report withholding on payments to nonresident aliens on Form 1042: Annual Withholding Tax Return for U.S. Source Income of Foreign Persons, and deposit the withholdings according to the same rules as Form 941.

#### **4070.40—Payment of Taxes and Tax Returns**

Handle withheld Federal income, Social Security, and Medicare taxes on wages paid to resident and nonresident aliens covered under this section in the manner prescribed in TFM Sections 4045, 4050, 4055, and 4060. Include these taxes in the total tax payment for withheld Federal income, Social Security, and Medicare taxes transmitted

on FEDTAX II or EFTPS and reported on Form 941.

#### **4070.50—Overseas Taxpayer Service Locations**

See Appendix 4 for a directory of IRS representatives in foreign countries.

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### **Section 4075—Deceased Employees**

If an employer pays a deceased employee's unpaid salary and wages and unused annual leave to the deceased employee's beneficiary or estate in the calendar year in which the employee died, these amounts are subject to Social Security and Medicare taxes. The employer deducts and withholds Social Security and Medicare taxes from the unpaid current compensation and the payment for unused annual leave.

Handle the amount withheld and the employer's contributions as prescribed in TFM Sections 4045, 4050, 4055, and 4060. Wages paid to a beneficiary or the employee's estate after the calendar year in which the employee died are not subject to FICA taxes. [See IRC section 3121(a)(14); Rev. Rul. 86-109, 1986-2 C.B. 196.]

According to Rev. Rul. 86-109, report the accrued wages and vacation pay of a deceased employee paid to an estate, or other person who has acquired the right to receive the payments, on Form 1099-MISC.

Do not treat these payments as wages for purposes of collecting income taxes at the source. Therefore, do not include these payments in Box 1, *Wages, tips, other compensation*, of the final Form W-2. Treat these payments as wages for the purpose of Social Security and Medicare taxes only if paid to the survivor or estate before the close of the calendar year in which the employee died. If they are paid before that date, the amount of the payment appears as Social Security wages (up to the amount of the wage base) and Medicare wages on the



final Form W-2. Do not include these payments in Box 1 as wages.

Report the entire amount of death benefits on Form 1099-R. Those benefits may be from a qualified plan paid to an estate or other person who has acquired the right to receive the payments solely because of the death of the employee. Also, report death benefit payments from a nonqualified plan on Form 1099-R.

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### **Section 4080—Levy for Unpaid Tax Liability**

The IRS collects delinquent Federal taxes by levy on the accrued salary or wages of any officer, employee, or elected official of the United States or the District of Columbia. Since the levy is served against the take-home pay of the employee, agencies should not permit employees to increase any voluntary allotment after notice of levy has been received until the tax liability is liquidated or other arrangements satisfactory to the IRS are made.

#### **4080.10—Service of Levy**

An IRS agent serves notice of levy on wages, salary, and other income of individuals. See TFM subsection 4080.20. The agent serves the notice in person or by mail. Service by mail is limited to the United States, its territories and possessions, and ships at sea. The notice includes the original and four copies. All copies must be signed and dated, and the time of receipt entered on the forms. The employer agency returns the original to the IRS agent and keeps one copy. IRS or the employer agency forwards one copy to the employee.

The person designated under TFM subsection 4080.20 honors all applicable notices of levy, whether served in person or received by mail. The General Accounting Office makes no disallowance nor does it raise charges against any disbursing officer or designated person for complying with notices of levy.

#### **4080.20—Designation of Individuals to Receive Service of Notice of Levy**

Each Government agency should designate one or more persons on whom notice of levy for delinquent taxes of the agency's employees may be served. These designees receive written statements from such employees regarding exemptions for dependents as provided for in the IRC.

#### **4080.30—Minimum Exemption from Levy for Wages, Salary, and Other Income**

A check to the employee each pay period includes exempt take-home pay and the amount by which the nonexempt take-home pay exceeds the levy amount. Agencies should refer to the IRC for specific exemptions and related procedures, or contact their local IRS office.

#### **4080.40—Continuing Levy on Salary and Wages**

The levy on salary or wages starts from the date IRS serves the levy and continues until IRS releases it.

#### **4080.50—Liquidation through Payroll Deductions**

An employee may arrange with IRS to liquidate his or her tax liability by payroll deduction. IRS Form 2159: Payroll Deduction Agreement, signed by a revenue officer (or other authorized IRS agent) and by the employee is the authorization for payroll deductions. Send the original to the payroll office. The employer agency deducts from each salary payment the agreed amount until the total tax liability is liquidated.

#### **4080.60—Payment to Internal Revenue Service**

The agency makes one payment each pay period to the IRS to cover amounts

deducted from employees' pay. Attach a list to the payment containing each employee's name and TIN, the amount, and the taxable year. Send the payment to the address specified by the revenue officer or other authorized IRS agent.

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### **Section 4085—Payment or Reimbursement of Employees' Expenses**

An employer may exclude reimbursement of employee business expenses from employees' incomes and should not subject it to Federal income, Social Security, and Medicare tax withholdings only if the employer has a reimbursement or other expense allowance arrangement that is an "accountable plan." Such a plan must require that the employee substantiate the amounts and business purposes of expenditures and return advances in excess of expenses to the employer. See section 1.62-2 of the Income Tax Regulations for the meaning of an accountable plan.

#### **4085.10—Payments under an Accountable Plan**

An employer may exclude reimbursement of employee business expenses from employees' incomes if it has a reimbursement or other expense allowance arrangement that qualifies as an "accountable plan." Under an accountable plan, employees must be required to substantiate all business expenses and to return amounts advanced for expenses that are not substantiated within a reasonable period. Payments under an accountable plan can be excluded from FICA and income tax.

If an agency gives an employee a per diem or standard mileage rate for auto expenses, the employee must establish the time, place, and business purpose of the expense. Then, if the reimbursed amount is the same as or less than the Government specified rates, do not include the amount in the employee's income.

The Federal per diem rates are published, by locality, at 41 Code of Federal Regulations, Chapter 301, Appendix A. Each year, the IRS publishes a revenue procedure that provides rules by which business expenses are deemed substantiated under the regulations.

Do not report amounts paid under an accountable plan as income on Form W-2 and do not withhold Federal income, Social Security, and Medicare taxes. Report such amounts in Box 13 of Form W-2 using Code L.

#### **4085.20—Amounts Treated as Paid Under a Nonaccountable Plan**

Report as wages on Form W-2 amounts paid to employees for business expenses if any of the following occur:

- The employee is not required to substantiate, or does not substantiate, the expenses with receipts or other documentation.
- The employer agency advances an amount to the employee for business expenses and the employee is not required to return, or does not return, the excess unsubstantiated amount used for business expenses.
- The employee is allowed a per diem or mileage rate that exceeds the Federal rate. Report the excess as wages.

Report payments under a nonaccountable plan, including unsubstantiated business expenses and unreturned excess amounts, as wages on Form W-2. These amounts are subject to FICA and income tax. Also report to the employee any amount of taxes withheld on unsubstantiated or excess amounts.

#### **4085.30—Payment or Reimbursement of Moving Expenses**

Exclude employer's payment or reimbursement of employees' moving

expenses from income, and from withholding taxes, only if it is paid under an arrangement similar to an accountable plan, as defined herein.

Exclude moving expense reimbursement from the employee's income, and from withholding taxes, only if it is a qualified moving expense (one which would otherwise be deductible by the employee) [IRC sections 127, 132(g)]. Do not exclude the reimbursement if the employee actually deducted the expense in a prior taxable year.

Report excluded moving expense reimbursements in Box 13 of Form W-2 using Code P. Refer to IRS Circular E or Publication 521, *Moving Expense Reimbursements*, for additional information.

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#### **Section 4090—Special Certifying Requirements of Federal Income Taxes Withheld from Salaries of U.S. Government Employees Employed in Guam or the Commonwealth of Northern Mariana Islands**

##### **4090.10—Special Certifying Requirements**

Authority governing special certifying requirements is as follows:

- Guam. Title 48 U.S.C. section 1421(h) provides that Federal income taxes derived from Guam will be transferred ("covered over") into the Treasury of Guam. According to IRC section 3401(a)(8)(D), excluded from the definition of "employment" for income tax withholding purposes are services performed for the United States (or agency thereof) within a possession of the United States, to the extent the United States withholds taxes on such remuneration pursuant to an agreement with such possession.

The effect of these provisions is that the Government transfers income taxes withheld on its employees who are resident or domiciled on Guam into the Treasury of Guam. This includes compensation paid to employees of a service or social organization associated with a military or civilian agency. The certification procedure contained in TFM subsection 4090.30 satisfies the statutory requirements.

- Commonwealth of Northern Mariana Islands (CNMI). Title 48 U.S.C. section 1681, note [Public Law 94-241, section 703 (b)] contains provisions resembling those for Guam.

#### **4090.20—Defining Income Taxes Derived from Guam or CNMI**

The term "Federal income taxes" used in TFM subsection 4090.10 includes the Federal income taxes withheld from compensation paid to the following:

- Federal civilian employees in Guam or CNMI.
- Military personnel stationed in Guam or CNMI.
- Active duty military personnel domiciled, but not stationed, in Guam.
- Recipients of Federal pensions (civilian or military, including survivors) resident in Guam.

#### **4090.30—Certifying Federal Income Taxes Creditable to Guam or CNMI**

All departments and agencies of the Government and service and social organizations associated with a military or civilian Federal entity that have Federal civilian or military employees stationed in Guam or CNMI must certify each calendar quarter the total amount of

Federal income taxes withheld from salaries. (See the Contacts page.)

Submit separate certifications for taxes creditable to Guam and CNMI. Certifications may be in a letter citing I TFM 3-4000 as the authority and should include identification of the certifying

entity, the EIN, the calendar quarter covered by the certifications, and the dollar amount withheld.

Submit certifications as soon as possible after the close of the calendar quarter but not later than the end of the month after the close of the calendar

quarter covered by the certifications. The amount shown in the certifications must agree with the amount of income tax withheld and entered in the quarterly Federal tax return of the agency (Form 941).

## **Contacts**

### ***Direct inquiries concerning material in this chapter to:***

Office of Chief Counsel  
Internal Revenue Service  
Office of the Associate Chief Counsel  
(Employee Benefits and Exempt Organizations)  
1111 Constitution Avenue, NW., Room 5325  
Washington, DC 20224  
Telephone: 202-622-6040

### ***Direct inquiries concerning the FEDTAX II system to:***

FEDTAX II Customer Service  
Telephone: 1-877-333-8292

OR

Financial Services Division  
Financial Management Service  
Telephone: 202-874-6550.

### ***Direct inquiries concerning EFTPS to the contacts listed on the Web site at <http://www.fms.treas.gov/eftps>.***

### ***Report amounts of Federal income taxes creditable to Guam or CNMI to:***

Commissioner of Internal Revenue  
Attn: Revenue Accounting Branch T:S:R  
Washington, DC 20224

**APPENDICES LISTING**

| <b>Appendix No.</b> | <b>Form/Title</b>  |
|---------------------|--|
| 1                   | FEDTAX II User Profile Sheet   |
| 2                   | Application for FEDTAX II Form 941 PIN Code                                |
| 3                   | Guide to Information Returns   |
| 4                   | Internal Revenue Service Directory of Representatives in Foreign Countries |

### FEDTAX II User Profile Sheet

|        |     |
|--------|-----|
| New    | ___ |
| Update | ___ |
| Delete | ___ |

Please complete this form for each individual that will be a FEDTAX II user.

Employer Identification Number: \_\_\_ - \_\_\_ - \_\_\_ - \_\_\_ - \_\_\_

Agency Location Code Number: \_\_\_ - \_\_\_ - \_\_\_ - \_\_\_ - \_\_\_

Agency Name: \_\_\_\_\_

Agency Address: \_\_\_\_\_

(no PO Boxes, please) \_\_\_\_\_

Tax Types paid for this Tax ID Number: \_\_\_ 941, \_\_\_ 945, \_\_\_ CT1, \_\_\_ 1042, \_\_\_ 720

Approximate Number of Employees? (Headcount for Census) \_\_\_\_\_

\*\*\*\*\*

**Primary Contact Name:** \_\_\_\_\_

(The Primary Contact person will be the name responsible on the Tax Return.)

Phone Number: \_\_\_\_\_

Fax Number: \_\_\_\_\_

E-mail Address: \_\_\_\_\_

**Security Level:** \_\_\_\_\_ Administrator (May input data and authorize payments)  
\_\_\_\_\_ User (May input data only)

Operating System (Circle one)      Windows 3.x              Windows 95/98      Windows NT

Floppy Drives (Circle one)              3.5" Floppy              CD ROM Drive

- (List additional users as Secondary contacts)

**Secondary Contact Name:** \_\_\_\_\_

Phone Number: \_\_\_\_\_

Fax Number: \_\_\_\_\_

E-mail Address: \_\_\_\_\_

**Security Level:** \_\_\_\_\_ Administrator (May input data and authorize payments)  
\_\_\_\_\_ User (May input data only)

Technical Contact Name: \_\_\_\_\_

(The technical contact is not assigned a User ID.)

Phone Number: \_\_\_\_\_

Fax Number: \_\_\_\_\_

E-mail Address: \_\_\_\_\_

**Please fax the completed form to FEDTAX II Customer Service at 720-332-0045.**

Questions concerning this form should be addressed to:

FEDTAX II Customer Service

1-877-FEDTAX2, Monday through Friday, 8:30 am to 8:00 pm, Eastern Time

or E-mail address: fedtax.2@firstdatacorp.com

### Application for FEDTAX II Form 941 PIN Code

Agency Name: \_\_\_\_\_ Agency EIN: \_\_\_\_\_

Agency Address: \_\_\_\_\_

City, State, ZIP: \_\_\_\_\_

(U.S. address required)

\_\_\_\_\_ **Initial Application.** Please issue a PIN Code to the person named below, who is authorized to approve and transmit Form 941 tax returns for the above Employer Identification Number (EIN). This authorization is effective when IRS has received your PIN acknowledgment letter and will remain in effect until revoked.

\_\_\_\_\_ **Notification of Change or Lost PIN.** Please issue a PIN code to the person named below and revoke all previous PIN's for this agency's EIN. This change is effective for Forms 941 beginning with the \_\_\_\_\_ quarter of \_\_\_\_\_ (year).

\_\_\_\_\_ **Revocation.** The person named below is no longer authorized to approve Form 941 for this agency.

**Agency approval:**

Signature \_\_\_\_\_

Title \_\_\_\_\_ Date \_\_\_\_\_

I recognize my responsibility to ensure that all tax deposits and returns are transmitted timely and accurately. By using this PIN Code, I certify, under penalty of perjury, that I have examined and have the authority to sign the Form 941, Employer's Quarterly Federal Tax Return, that I am transmitting, including any accompanying schedules, and, to the best of my knowledge and belief, is true, correct, and complete.

Signature of person to receive PIN \_\_\_\_\_ Date \_\_\_\_\_

Print Name \_\_\_\_\_

Mailing Address \_\_\_\_\_

(if different from above) \_\_\_\_\_

Phone number \_\_\_\_\_

**Mail to:** Internal Revenue Service  
PO Box 1231, Stop 6380 AUSC  
Austin, TX 78767

**or fax to:** (512) 460-8962  
Attn: Electronic Filing

## GUIDE TO INFORMATION RETURNS

| Form Number | Title   | What to Report  | Amounts to Report   | Due Date    |                                       |
|-------------|---|---|---|-------------|---------------------------------------|
|             |   |   |   | To IRS      | To Recipient                          |
| 1098        | Mortgage Interest Statement   | Mortgage interest you received in the course of your trade or business from individuals.  | \$600 or more   | February 28 | January 31<br>(To payer/<br>borrower) |
| 1099-A      | Acquisition or Abandonment of Secured Property  | Information about the acquisition or abandonment of property that is security for a debt for which you are the lender.  | All amounts   | February 28 | January 31<br>(To borrower)           |
| 1099-G      | Certain Government Payments   | Unemployment compensation, State and local income tax refunds, agricultural payments, taxable grants, and discharge of indebtedness   | \$10 or more for unemployment and tax refunds; \$600 or more for all others                                   | February 28 | January 31                            |
| 1099-INT    | Interest Income   | Interest payments not including interest on an individual retirement arrangement (IRA)  | \$10 or more (\$600 or more in some cases)  | February 28 | January 31                            |
| 1099-MISC   | Miscellaneous Income<br><br>(Also, use this form to report the occurrence of direct sales of \$5,000 or more of consumer goods for resale.) | Rent or royalty payments, prizes and awards that are not for services such as winnings on TV or radio shows.<br><br>Payments to crew members by owners or operators of fishing boats. Report payments of proceeds from sale of catch.<br><br>Payments to a physician, physician's corporation, or other supplier of health and medical services. Issued mainly by medical assistance programs or health and accident insurance plans.<br><br>Payments for services performed for a trade or business by people not treated as its employees. Examples: fees to subcontractors or directors, expenses incurred for use of an entertainment facility treated as compensation to a nonemployee, and golden parachute payments.<br><br>Substitute dividend and interest payments reportable by brokers. | \$600 or more except \$10 or more for royalties<br><br>All payments<br><br>\$600 or more<br><br>\$600 or more | February 28 | January 31                            |
| 1099-OID    | Original Issue Discount   | Original issue discount.  | \$10 or more  | February 28 | January 31                            |
| 1099-R      | Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.                                 | Distributions from pensions, annuities, retirement or profit-sharing plans or from IRAs. Use Form 1099-R only if the distribution closed the payee's account.   | All amounts   | February 28 | January 31                            |
| W-2         | Wage and Tax Statement  | Wages, tips, other compensation, withheld income and FICA taxes, and advance earned income credit (EIC) payments. Include bonuses, vacation allowances, severance pay, moving expense payments, some kinds of travel allowances, and third-party payments of sick pay.  | See separate instructions.  | February 28 | January 31                            |



**INTERNAL REVENUE SERVICE  
DIRECTORY OF REPRESENTATIVES IN FOREIGN COUNTRIES**

**Location****Area of Responsibility**

BONN, Germany  
c/o U.S. Embassy  
PSC 117, Box 225  
APO AE 09080-5000  
Phone: 9-011-49-228-339-2101

Austria, Hungary, Netherlands, Romania, Poland, Luxembourg, Czech Republic, Slovak Republic, Estonia, Latvia, Lithuania, former Soviet Republics (Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine, Uzbekistan), Lebanon, Iraq, Qatar, Syria, Iran, Yemen

LONDON, England  
E/IRS-U.S. Embassy  
PSC 801, Box 44  
FPO AE 09498-4044  
Phone: 9-011-44171-408-8085

United Kingdom, Denmark, Ireland, Finland, Norway, Sweden, Iceland, Angola, Botswana, Eritrea, Ethiopia, Kenya, Lesotho, Malawi, Mozambique, Namibia, South Africa, Sierra Leone, Somalia, St. Helena, Sudan, Swaziland, Tanzania, Uganda, Zambia, Zimbabwe

MEXICO CITY,  
Mexico  
P.O. Box 3087  
Laredo, TX 78044  
Phone: 9-011-525-211-0042

Mexico (1), Guatemala, Belize, El Salvador, Nicaragua, Costa Rica (1), Honduras (1), Anguilla, Antigua and Barbuda, Aruba (3), Bahamas, Barbados (1), Bermuda (1) (4), British Virgin Islands, Cayman Islands, Dominica (1), Dominican Republic (1), Grenada (1), Guadeloupe (2), Haiti, Jamaica (1), Martinique (2), Montserrat, Netherlands Antilles (3) (Curacao, Bonaire, St. Maarten and Saba), St. Barthelemy (St. Barts), St. Christopher (St. Kitts) and Nevis, St. Lucia (1), St. Martin, St. Vincent and Grenadines, Trinidad, and Tobago (1), Turks and Caicos

OTTAWA, Canada  
American Embassy/IRS  
P.O. Box 5000  
Ogdensburg, NY 13669-0430  
Phone: 9-1-613-563-1878

Canada

PARIS, France  
U.S. IRS  
American Embassy  
Paris  
PSC 116, Box E-414  
APO AE 09777  
Phone: 9-011-3314-312-4560

Spain, Portugal, Switzerland, Algeria, Liechtenstein, Morocco, Monaco, Belgium, Gibraltar, Andorra, Tunisia, Benin, Burkina Faso, Burundi, Cameroon, Cape Verde, Central Africa Republic, Chad, Comoros, Congo, Djibouti, Egypt, Equatorial Guinea, Gabon, Gambia, Ghana, Guinea, Guinea-Bissau, Ivory Coast, Liberia, Libya, Madagascar, Mali, Mauritania, Mauritius, Mayotte, Niger, Nigeria, Reunion, Rwanda, Sao Tome and Principe, Seychelles, Senegal, Togo, Zaire, Western Sahara

ROME, Italy  
American Embassy  
IRS  
PSC 59, Box 39  
APO AE 09624  
Phone: 9-011-396-4674-2607

Malta, Croatia, Slovenia, Bosnia-Herzegovina, Serbia/Montenegro, the former Yugoslavia Republic of Macedonia, Bulgaria, Israel, Cyprus, Greece, Albania, San Marino, Bahrain, Jordan, Kuwait, Oman, Saudi Arabia, Turkey, United Arab Emirates

LocationArea of Responsibility

SANTIAGO, Chile  
 IRS  
 U.S. Embassy  
 Santiago  
 Unit 4132  
 APO AA 34033  
 Phone: 9-011-562-330-3424

Argentina, Bolivia, Brazil, Chile, Columbia, Ecuador, French Guiana  
(2), Guyana (1), Panama, Paraguay,  
 Peru (1), Surinam, Uruguay, Venezuela

SINGAPORE,  
 Singapore  
 U.S. IRS  
 American Embassy PSC 470  
 FPO AP 96534-0001  
 Phone: 9-011-65-338-0251

Malaysia, Singapore, Thailand, Vietnam, Indonesia, Burma,  
 Bangladesh, India, Sri Lanka, Nepal, Bhutan, Brunei, Cambodia,  
Pakistan, Afghanistan

SYDNEY, Australia  
 U.S. IRS  
 PSC 280,  
 APO AP 96554  
 Unit 11025  
 Phone: 9-011-612-233-4437

New Zealand, Nauru, Fiji, Vanuatu, Papua New Guinea, Western  
 Samoa, and all areas south of the equator and west of the 130th degree  
 line of longitude.

TOKYO, Japan  
 U.S. IRS  
 Unit 45004,  
 Box 208  
 APO AP 96337-0001  
 Phone: 9-011-81-33-224-5460

Korea, China, Philippines, Hong Kong, Marshall  
 Islands (1), Taiwan, Federated States of Micronesia, Mongolia

Notes:Underlined Countries Have Income Tax Treaties in Force

- (1) Tax Information Exchange Agreements (TIEAs) are in effect with these countries.
- (2) Covered by treaty with France
- (3) Interest article only
- (4) Excise taxes on insurance premiums

## PART 3 - PAYROLLS, DEDUCTIONS, AND WITHHOLDINGS

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