Seize payroll tax discount on acquisition

If your business is growing by leaps and bounds, you may be poised to gobble up one of your competitors. Naturally, this will increase your overall payroll tax bill. Just be careful that you don't overpay.

Strategy: Claim credit for payroll taxes paid earlier this year. If the combined business operation keeps some of the same employees, the taxes paid by the competitor can reduce the amount your firm owes this year.

In effect, you can obtain a payroll tax "discount" for amounts paid by another employer.

Here's the whole story: When an employee works for two employers during the year, each employer must pay the 6.2% Social Security tax portion up to the annual wage base ($113,700 in 2013). All wages are subject to the 1.4% Medicare portion of the tax.

However, if one employer acquires another during the year—and it continues to employ some of the same people—the successor can count the wages paid by the predecessor toward its own Social Security tax wage base.

To qualify for this payroll break, the following conditions must be met:

- The successor employer obtains substantially all of the property used in the prior employer's business (or in a separate unit of the prior employer's business).
- The employees worked for the predecessor immediately before the acquisition and for the successor immediately after the acquisition.
- All earnings were paid in the calendar year of the acquisition.

Note: An employer may benefit from this tax rule even if it acquires or consolidates its own subsidiaries. The IRS has said that the method of acquisition is immaterial *(see box below).*

Tip: The stakes are even higher now that the 2% payroll tax holiday has ended. (The Social Security tax rate was only 4.2% in 2011 and 2012.)

No taxation with consolidation

An employer doesn't necessarily have to acquire another company to benefit from the payroll tax discount.

Facts: A corporation (we'll call it Parent Corp.) owned a dozen subsidiaries it wanted to consolidate. So it formed a limited partnership and named itself as general partner. Then the limited partnership absorbed all the subsidiaries through various transactions.

The IRS ruled that each subsidiary qualified as a separate unit of Parent Corp.'s business. Also, the employees of the subsidiaries kept working for the consolidated corporation after the transactions. Because the limited partnership qualified as a successor corporation, it received a credit for all its wages paid by the subsidiaries. *(IRS Ltr. Rul. 9315007)*

7600 Leesburg Pike, Suite 300, Falls Church, VA 22043-2004 (800) 543-2002

Tip: At the end of the year, provide a single W-2 to “shared” employees.

7600 Leesburg Pike, Suite 300, Falls Church, VA 22043-2004 (800) 543-2002