

Businessweek Archives

How To Avoid Your Very Own Nannygate

August 16, 1998



Personal Business: TAXES

HOW TO AVOID YOUR VERY OWN NANNYGATE

Ryan Flickinger was barely three months old last fall when his parents sat staring cross-eyed at Internal Revenue Service Publication 926, a 12-page recipe for parental colic otherwise known as Household Employer's Tax Guide. With mom Margaret returning to her business-development post at a law firm, she and her husband, Brad, had to figure out how to pay taxes on the nanny the McLean (Va.) family would soon need. "We flipped through the book and said, `You know what? Someone else has already figured this out,'" says Brad, a commercial real estate manager.

The Flickingers are one of thousands of couples who have concluded that paying for professional help beats spending hours mastering the tax rules that apply to anyone who employs a nanny, nursing aide, cook, or other helper. Generally, if you pay a household employee \$1,100 or more this year, you're obliged to cough up Social Security and Medicare taxes, plus state and federal unemployment insurance premiums.

Were it that simple, few would seek aid from a pro. But there are exclusions, and exceptions to the exclusions, detailed in Publication 926 (800 829-3676; www.irs.ustreas.gov). Then there are the forms to fill out, not all of them tax-related. For instance, you have to verify your employee can work legally in the U.S., then prepare a Form I-9 for the Immigration & Naturalization Service (800 870-3676; table).

Worst of all, the rules keep changing. Now, all employers must report information on new employees to state agencies, a result of 1996 federal welfare reform that aims to cut fraud and ease enforcement of court-ordered child support. And this year, the feds no longer let you settle on your return whatever household payroll-tax liabilities you run up, a change from rules that have held since 1995. Now you have to pay as you go, by filing quarterly estimated taxes on Form 1040-ES or by asking your employer to withhold a greater amount from your paycheck. "You have to pay at least what you paid last year or be within 10% of what you'll owe," says Guy Maddalone, president of GTM Associates, a payroll-services firm in Albany, N.Y. Otherwise, you'll owe an underpayment penalty.

Because the laws are so complex, you don't have to be a militia member to want to ignore the taxes. Through the end of April, the IRS counted 300,000 taxpayers using Schedule H, the form for figuring household employment taxes. That's up 50% from April '97 but is less than 0.3% of all returns filed--and less than half the estimated number of nannies, not to mention other workers.

By ignoring the taxman, of course, you risk a guilty conscience if not the IRS's wrath. Kathleen Webb, CEO of Sterling (Va.)-based Home/Work Solutions, reports a steady business in preparing amended returns, often for political appointees wishing to avoid the fate of former Attorney General nominee Zoe Baird. THE WORKS. Neither wanting to master the system nor run afoul of the law, the Flickingers chose Breedlove & Associates' service (table). The Austin (Tex.) firm helped them determine how much net salary to offer Ryan's nanny so they didn't pay more than they could afford after payroll taxes. Breedlove, like similar services, files withholding forms, secures employer ID numbers, prints pay stubs, and prepares quarterly and annual tax filings.

If you're interested in a service, check whether you'll be charged extra for adding a new employee. It's also worth seeing how much more it will cost to have the service deposit your employee's pay directly in a bank account.

An alternative is to add these tax duties to your accountant's chores. Or there's software. NannyPay from Essentia Software (888 999-1722) costs \$29.95 by mail or \$24.95 off the Internet (www.essentia-soft.com). But that still requires brainpower, which many aren't willing to give to nanny taxes. EDITED BY AMY DUNKIN Return to top