

PRACTICAL

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APRIL 2008



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An automated screening process can shift the compliance burden and efficiently identify an employer's eligibility for tax credits available when qualifying employees are hired.

SCREEN FOR EMPLOYMENT TAX CREDITS

BETH HENRICKS

Traditionally, the tax credit process has been managed by a company's tax department. With the increasing adoption of an applicant tracking system (ATS) or hiring management system (HMS) that allows companies to automate their hiring processes, the overall management of the hiring tax credit process is shifting to organizations' human resource (HR) teams.

When a company implements an ATS/IHMS, it expects to see a return on investment through many soft-cost savings, including reduction in shrinkage, increased tenure, and higher sales through better hiring of employees. Embracing automation also brings a hard-dollar return on investment by increasing tax credit opportunities through consistent employee screening processes. In many instances, the operational and tax savings derived from the tax credit process are sufficient to pay for the ATS.

Employee related tax credits

Most companies in America hire individuals who qualify their employers for federal, state, and local tax credits. With more than 150 employment-related tax credits available, the financial benefits can be significant, with some companies earning

an average credit of \$1,500 per qualified employee. For large companies, this can represent millions of dollars.

Employment-related tax credit programs typically fall into one of two groups:

1. *Hiring tax credits.* These types of credits encourage and reward employers for hiring individuals with barriers to employment. Qualifying individuals can include welfare recipients, at-risk youth, ex-felons, and disabled veterans.
2. *Location-based credits.* These credits provide financial incentives to businesses operating in specific geographic areas that hire individuals from the same area.

Hiring Tax Credits. Both federal and state programs offer credits based on the characteristics of potential employees.

The work opportunity tax credit (WOTC) is the most commonly known federal hiring tax credit.¹ Created in 1996 as part of the Small Business Job Protection Act, WOTC allows employers to earn a federal income tax credit based on the wages of certain categories of disadvantaged workers, including former welfare recipients. The credit helps employers with some of the costs associated with the training and retention of disadvantaged workers, and moving people from welfare to employment.

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EXHIBIT 1. Average federal screening credit value matrix

Wage rate	Qualification rate	Turnover				
		25%	50%	75%	125%	200%
\$ 7.50	12%	\$1,556	\$1,175	\$ 842	\$439	\$143
\$ 8.50	10%	\$1,764	\$1,331	\$ 954	\$496	\$162
\$ 9.00	8%	\$1,867	\$1,409	\$1,010	\$526	\$172
\$10.00	6%	\$2,075	\$1,567	\$1,122	\$585	\$190

The Small Business Tax Act of 2007 extended the WOTC to apply to wages paid to (or incurred by) individuals who begin work by 8/31/11. Additionally, this Act extends a waiver of the limitation of business credits to offset alternative minimum tax (AMT) liability to WOTC. As the AMT is imposed to ensure that at least some tax is paid by all entities, tax credits allowed to offset the AMT are extremely limited. This AMT offset ability gives WOTC the potential to have a major positive impact on a company's overall tax strategy. As with most general business credits,² WOTC may be carried back one year and carried forward for 20 years.³

WOTC rewards businesses for hiring individuals from one of nine targeted groups. These groups including food stamp recipients, Temporary Assistance to Needy Family recipients, and ex-felons, Over a two-year period, employers can earn up to:

1. \$4,800 for each qualified veteran with a service-related disability.
2. \$2,400 for each designated community resident.
3. \$9,000 for each long-term family assistance recipient.

To determine if a potential new hire is WOTC eligible, the job applicant must complete IRS Form 8850, "Pre-Screening Notice and Certification Request for the Work Opportunity Credit," during the application process. The employer must submit the form with an original signature and all supporting documentation to the appropriate state agency within 28 days of the new employee's first day of work. After receiving certification from the state agency that the employee is WOTC-eligible, the employer tracks wages earned and hours worked to calculate the credit.

Exhibit 1 contains the average federal screening credit value matrix. This matrix shows how the relationship between wages and employee turnover

affects the average federal credit a company may earn.

In addition to the federal WOTC, state and local governments offer dozens of hiring tax credit programs. The new hire qualifications vary by program, but are similar to the WOTC and may provide incentives to assist a much broader population. For instance:

- Illinois provides a credit for 5% of wages paid to qualified veterans for up to \$600 per eligible employee.
- Kansas offers a credit of 25% of compensation paid to qualified military personnel up to \$7,000 per qualified employee per year.
- Qualified employer benefits associated with the New Mexico Rural Jobs Credit for wages paid for a qualifying job performed or based in a rural location range from \$1,000 to \$4,000 per employee.

State tax credits for many companies range from 30% to 250% of their federal tax credits depending on the geographic areas of sites, type of operations, and population of employees hired.

Location-based tax credits. Many federal and state agencies designate certain geographic areas within their boundaries as enterprise or empowerment zones, or renewal communities, as a core part of their economic development strategy. A catalyst for growth, these designated zones are designed to promote community revitalization, encourage business investment, and support job retention and creation. Depending on the governing authority, a wide variety of other state incentives may be available to eligible companies located in the enterprise zone. These include sales tax exemptions, property tax abatements, and utility discounts. The most common, and potentially most lucrative, incentive is an income tax credit based on the number of qualifying employees at a qualified location.

The federal empowerment zone tax credit program allows a qualifying employer to earn up to \$3,000 per year for each employee who works and lives in an established zone, regardless of the employee's date of hire. Qualified businesses located in a federal renewal community can earn up to \$1,500 per year per qualified employee. There are 40 federal empowerment zones.

States offer tax credits through enterprise zones. For example, California has 42 designated zones and offers lucrative incentives to businesses operating in these zones. One incentive allows businesses to earn as much as \$35,000 per qualified employee over a five-year period.

Which employees qualify

One important distinction between hiring tax credits and location-based tax credits is the employees who qualify. While hiring tax credits provide incentives for hiring new employees through new job positions or turnover, some zone-based tax credit programs allow for current and past employees to qualify a company for a tax credit.

Many eligible companies disregard these benefits based on the assumption that they are not applicable to exempt and professional level employees. Because these programs are focused on the creation of quality jobs and redevelopment initiatives, however, they typically provide benefits for all positions.

In addition to the direct tax credits and incentives offered by the jurisdictions, many zones also indirectly increase tax credit capture from other programs. For instance, qualified employees hired from federal enterprise communities are typically eligible for WOTC.

Tax credit screening process

The adoption of ATS/HMS moves the process of screening job applicants for tax credits from a labor-intensive manual process to a highly automated and outsourced solution that frees up both the tax and human resource departments.

Pre-hire manual process. The primary purpose of the pre-hire tax credit process is to screen all applicants for federal, state, and local tax credits. This screening information is matched with post-hire data to capture and calculate tax credits. In addition, screening can be used as a mechanism to identify pre-qualified candidates who appear to qualify for tax credits. Companies can increase

their tax credit capture while remaining 100% compliant with federal, state, and local EEO and labor laws by capturing this information during the hiring process.

In a manual screening process, the job applicant completes Form 8850 no later than the day of the job offer. The applicant may also need to complete additional forms to qualify for additional credits.

The hiring manager or a tax credit provider determines if the new hire is eligible for tax credits. If the applicant appears to be eligible for tax credits, the employer completes the remainder of the Form 8850 and the additional forms needed for state and local credits. To qualify for WOTC, the state workforce development agency must receive the Form 8850 within 28 days of the new hire's first day of work.

Pre-hire automated process. Integrated tax credit screening with the automated job applications process builds consistency, speeds filling job openings, reduces paperwork, eases hiring manager workload, and increases tax credit opportunities. Automated screening also ensures that all employees hired through the system are screened for tax credits. This consistent process helps reduce the risk that the applicant will not receive the required pre-hire screening.

Every applicant is guaranteed to receive the exact same language that describes the purpose of the questioning process, the ability for the applicant to "opt-out" of the tax credit screening process and, most importantly, ensures that hiring managers never have access to the detailed tax credit information filled out by the applicant or new employee.

The automated tax credit screening processes reduce the time a job applicant spends on completing tax credit forms. A job applicant takes, on average, less than two minutes to complete an automated questionnaire compared with more than seven minutes to complete Form 8850. If an applicant appears to qualify, the average time to complete associated paperwork is reduced from more than seven minutes to approximately four minutes. This time-spent reduction increases the likelihood that applicants will complete all information necessary.

Hiring managers receive only the required pre-populated tax credits forms for new hires that appear to qualify for a tax credit. This eliminates more than 94% of the paperwork associated with

the qualification process. Through the automated screening process, all relevant tax credit questions are answered during application. The need to interview a new employee or have him or her complete additional post-screening tax credit forms is eliminated.

Federal laws require that applicants be screened for tax credits on or before the day of the job offer and that Form 8850, with an original signature, is received in the controlling agency's office no later than 28 days after the employee's first paid date of work. In the manual process, Form 8850 is completed along with the job application and stored. If the form is lost, the individual cannot complete a new form without attaching a signed affidavit stating that the original form was completed and confirming which answers were included on that form. In the automated environment, answers are electronically stored and are time-and-date stamped in a secure database. This process allows printing of the form at any time and reprinting if the form is lost or misplaced. This simple option increases forms compliance and federal tax credits by increasing program flexibility.

Automation safeguards

Many companies that use a manual tax credit screening process increase audit exposure due to their current process. Common risks inherent in a manual process involve interview timing, new hire tracking, and forms processing.

In the manual environment, tax credit questions are typically asked twice, once pre-job offer and once as a new employee. Under the calling approach, some tax credit providers may receive a more favorable tax credit answer during the post-offer interview. Unfortunately, neither employers nor their tax credit vendors are allowed to change the original answers on Form 8850, as the law requires the screening to be completed on or before the day of the job offer.

Many companies measure the success of their tax credit screening program by calculating the percentage of new hires that call into their tax credit screening provider post-hire. While this can be an important part of the overall process, federal law requires that all screening take place prior to the job offer. The most important aspect of the program is to track the number of new hires that properly complete the federal screening form prior to job offer. By placing too much emphasis on the phone-

COMPARISON OF PRE-HIRE SCREENING PROCESSES

A manual pre-hire tax credit screening process involves four steps:

- 1. All applicants complete employment application (including federal tax credit Form 8850).**
- 2. The hiring manager stores tax credit forms.**
- 3. All new employees complete new hire tax credit forms and/or call a toll-free tax credit screening number.**
- 4. The hiring manager retrieves the tax credit paperwork for *qualified new hires* and sends it to the tax credit provider.**

An automated pre-hire tax credit screening process can streamline the task into three steps:

- 1. All applicants apply online and complete a tax credit questionnaire.**
- 2. *Qualified new hires* sign pre-populated tax credit forms as part of the new hire paperwork package.**
- 3. The hiring manager retrieves the tax credit paperwork for *qualified new hires* and sends it to the tax credit provider.**

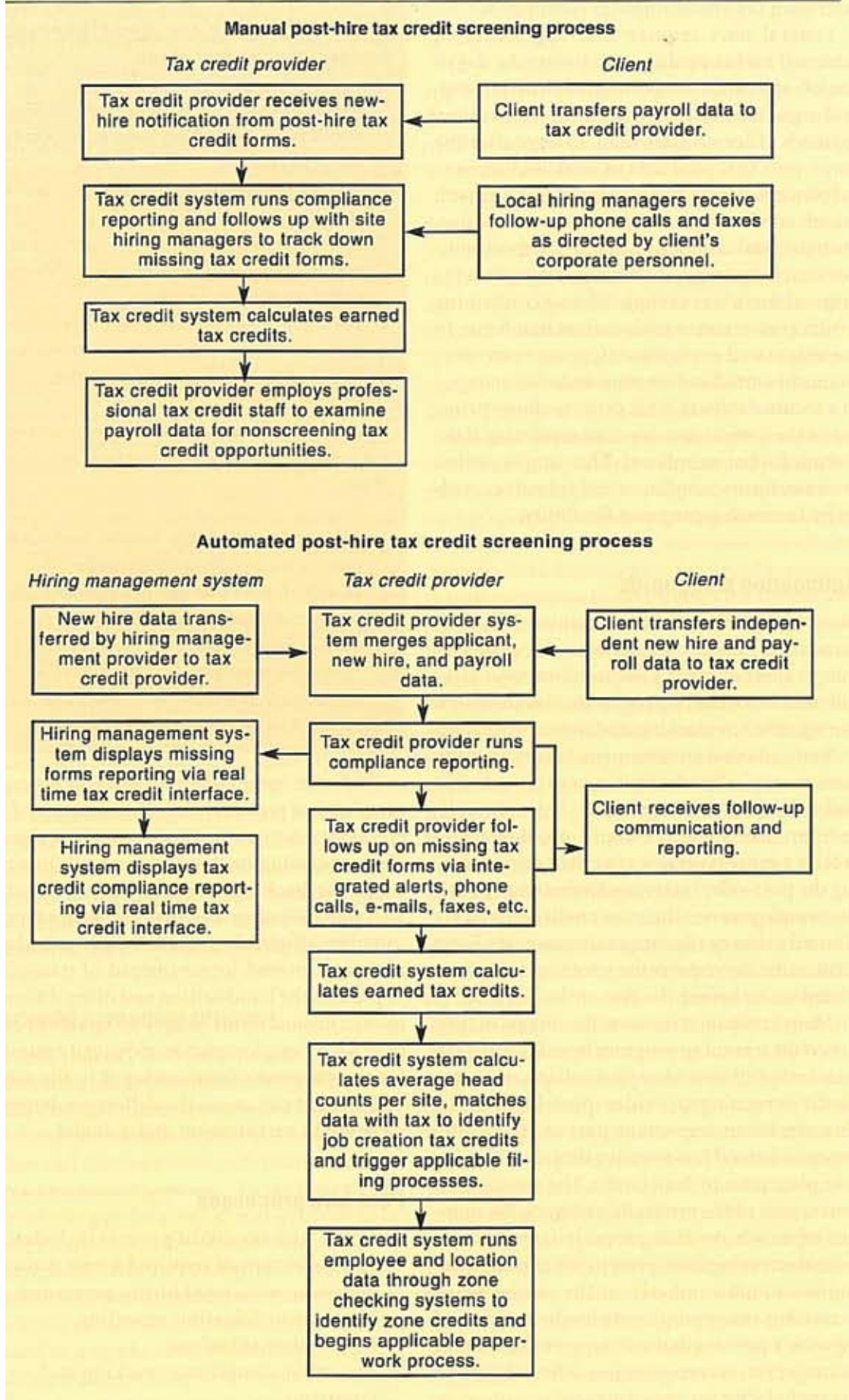
based screening, many employers inadvertently end up with a process that encourages their hiring managers to screen post job offer, which can create liability for the company.

Each state agency that completes the tax credit certification process receives thousands of tax credit forms everyday, and many face significant processing backlogs as a result. In some states the backlog is more than six months. Through the automated process, state agencies can more efficiently process the pre-populated and easy-to-read forms instead of struggling to process the handwritten and often difficult-to-read manual forms. Simply being able to decipher a new employee's Social Security number for the purpose of comparing it to the state's



Federal laws require that applicants be screened for tax credits on or before the day of job offer and that form 8850 is received in the controlling agency's office no later than 28 days after the employer's first paid date of work

EXHIBIT 2. Comparison of manual and automated post-hire tax credit screening processes



benefits list can mean the difference between a tax credit certification and a denial.

Post-hire processes

The post-hire tax credit process includes:

- The collection of required forms through follow-up with local hiring personnel.
- New hire notification reporting.
- Payroll data transfers.
- Tax credit compliance tracking and reporting.

Using a manual post-hire process, tax credits are often lost due to inconsistent procedures, lack of reporting and tracking, and the increased likelihood of errors. Leveraging automation increases tax credit potential, reduces human error and improves the operational insight that drives performance. Exhibit 2 illustrates the manual and automated post-hire tax credit screening processes.

Automation increases forms compliance or the number of required tax credit forms submitted within the strict government filing deadline.

For example, under a manual environment, hiring managers are typically reminded of outstanding forms by telephone or by fax to ensure the tax credit service provider receives the forms in time to meet the 28-day post-hire filing deadline. In industries with significant customer-facing interaction, such as retail and restaurant/leisure, the individuals with hiring responsibilities are also focusing on customer service, management, and merchandising. These individuals may not have the time to receive a phone call from the tax credit provider. Through integrated reporting, the hiring managers receive notifications on their hiring management system dashboards. Best-in-class tax credit providers use multiple approaches to create a seamless reminder strategy that leverages e-mail, telephone and fax, as well as escalation methods that notify district and corporate management.

Companies are able to increase their tax credits without increasing workload or adding staff by expanding the breadth of tax credits that are automatically tracked and calculated. A fully automated system that goes beyond new-hire screening and includes post-hire tracking further increases tax credits through automated employee and location tracking and employment growth calculations and trend analysis.

A fully automated system reviews all changes in business locations and employee addresses against location-based credit databases to capture new opportunities as well as cease tax credit calculation if an employee moves out of a tax-qualified zone. By electronically verifying eligibility through weekly payroll data, a system can create a payroll and address history for all zone locations.

A key element to receiving regular payroll fees is the ongoing calculation of an average monthly headcount per location. The highest volume workforce expansion for most companies is through organic growth. With a system to track employment trends, a tax credit provider can effectively identify when a business is eligible for additional tax credit programs and meet the necessary pre-certification requirements imposed by the controlling agency.

Detailed, accurate reporting is a critical element of a successful hiring tax credit program. Automation delivers real-time reporting for the hiring manager, district personnel, and corporate leadership. This detailed reporting not only increases tax credit potential, it provides additional accountability and visibility into the process.

Example. Bigco, Inc. has the following operations and staffing characteristics:

- Number of employees... 17,500.
- Number of locations... 450.
- Qualification rate ... 10%.
- Annual hires ... 10,000.
- Applicant to new hire ratio ... 5: 1.
- Qualified new hires ... 1,000.

Exhibit 3 shows the efficiency and time savings that would be derived from Bigco's using an automated tax credit process. Through the adoption of a hiring management system that includes full tax credit automation, for each 10,000 hires, a company can save approximately 1,500 hours-or more than \$35,000 in HR labor costs-and over 1,500 hours of new employee time that could be spent in training.

Reduced audit risk

As with the adoption of a hiring management system, the implementation of a tax credit system helps ensure a single, uniform process throughout an organization. This allows improved internal controls to help guarantee compliance with federal tax credit screening rules and federal and state labor laws.

EXHIBIT 3. Efficiency and time savings from Bigco's using an automated tax credit process

Manual tax credit process			
<i>Process point</i>	<i>Work required</i>	<i>Time for applicant or new employee</i>	<i>Time for HR manager</i>
Pre-hire tax credit screening	50,000 forms completed and stored	5,800 hours (applicants) at seven minutes per applicant	830 hours (HR manager) at one minute per applicant
Post-hire screening	20,000 forms completed and/or 10,000 calls made	1,600 hours (new employees) at 9-10 minutes per new hire	675 hours (HR manager) at four minutes per new hire
Forms follow up	50% of forms (500)	None	75 hrs (HR manager) at 1.5 phone calls per form to collect
Mailing of tax credit forms	1,000 forms tracked and sent in	None	50 hours (HR manager)
Totals	71,000 forms and 10,000 calls	7,400 hours	1,630 hours
Automated tax credit process			
<i>Process point</i>	<i>Work required</i>	<i>Time for applicant or new employee</i>	<i>Time for HR manager</i>
Pre-hire tax credit screening	None	1,700 hours (applicants) at two minutes per applicant	None
Post-hire screening	1,000 forms completed	35 hours (new employees) at two minutes per qualified new hire	50 hours (HR manager) at three minutes per qualified new hire
Forms follow up	10% of forms (100)	None	10 hours (HR manager) at 1.5 phone calls per form to collect
Mailing of tax credit forms	1,000 forms tracked and sent in	None	50 hours (HR manager)
Totals	2,000 forms	1,735 hours	110 hours
Savings	>69,000 fewer forms/calls	>5,600 hours	>1,500 hours

With all applicants completing tax credit questions through a kiosk or website, all of the applicant's data is stored in a secure data warehouse instead in an employee's desk or file cabinet. In addition to reducing audit risk, automation enables companies to better shield sensitive employee data.

Turning HR into a profit center

A company can realize operational efficiencies—including a 94% reduction in paperwork and printing expenses, reduction in salaries paid to human resources, and reduction of operational staff to oversee the paperwork—by automating its processes.

Automation increases tax credits through increased program compliance. This includes screening all new employees and securing forms within the filing deadlines from a higher percentage of qualified new hires. The scope of applicable tax

credits is greater as a result of improved pre-hire screening and post-hire automation. There is also reduced audit exposure through strict process controls.

With the increased adoption of hiring management systems, more companies are fully realizing the cost- and time-savings that come from increased efficiency and earning a greater percentage of the tax credits for which they are eligible. For HR executives, these systems also present a viable means of contributing to a better bottom line. Because the systems allow HR to take control of the crediting process from the finance and accounting departments, they offer yet one more path for HR leaders to increase their visibility and exercise more control over organizational success and growth.

NOTES
¹ Section 51.
² Section 38.
³ Section 39(a)(1)