

3

Federal and State Income Tax Withholding

Learning Objectives

After studying this chapter, you will be able to:

- Identify and distinguish between mandatory and voluntary deductions
- Determine taxable earnings
- Calculate federal income tax withholding using the wage-bracket method
- Calculate federal income tax withholding using the percentage method
- Discuss state and local income tax withholding

Deductions from Employee Earnings

There are two types of amounts withheld from an employee's paycheck:

- **Mandatory deductions** must be withheld.
- **Voluntary deductions** may be requested by employee.

Mandatory Deductions

- Federal income tax withholding
- State income tax withholding
- Local income tax withholding
- Social Security tax (OASDI)
- Medicare tax (HI)
- State disability insurance tax

Voluntary Deductions

- Union dues
- Retirement plans
- Medical plans
- Cafeteria plans
 - Flexible spending accounts for benefits such as dependent care and medical expenses

Distinguishing Between Gross Pay and Taxable Pay

- Gross pay encompasses all earnings in a given period.
- Taxable pay
 - An employer must subtract tax-deferred contributions from gross pay to arrive at taxable pay.
 - Taxable pay is used to calculate mandatory deductions.
 - State and local taxable earnings may differ from federal taxable earnings.

Federal Income Tax Withholding

Pay-as-you-go system

- This was established as a result of the Current Tax Payment Act of 1943.
- Employers withhold income tax from employees and remit to the federal government.
- Certain employees may be exempt.

The Wage-Bracket Method (Pre-2020 Form W-4)

- The employee completed a pre-2020 Form W-4 (providing marital status and number of withholding allowances).
 - The employer uses that information and tables in Publication 15-T to determine the correct withholding.
- | 2023 Wage Bracket Method Tables for Manual Payroll Systems With Forms W-4 From 2019 or Earlier | | | | | | | | | | |
|--|----------------------------------|--------------------------------------|-----|-----|-----|-----|-----|-----|-----|-----|
| WEEKLY Payroll Period | | | | | | | | | | |
| If the Wage Amount
(line 1a)
is | SINGLE Persons | | | | | | | | | |
| | And the number of allowances is: | | | | | | | | | |
| At least | But less than | 0 | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 |
| | | The Tentative Withholding Amount is: | | | | | | | | |
| \$0 | \$105 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| \$105 | \$115 | \$1 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| \$115 | \$125 | \$2 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| \$125 | \$135 | \$3 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| \$135 | \$145 | \$4 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| \$145 | \$155 | \$5 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| \$155 | \$165 | \$6 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| \$165 | \$175 | \$7 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| \$175 | \$185 | \$8 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |

[illegible]

The Wage-Bracket Method (2020 or Later Form W-4)

- The employee completes a 2020 or later Form W-4.
- The employer uses that information, Worksheet 2 in Publication 15-T, and the appropriate tax table to determine the correct withholding.

Worksheet 2. Employer's Withholding Worksheet for Wage Bracket Method Tables for Manual Payroll Systems With Forms W-4 From 2020 or Later


Keep for Your Records 

Table 5

Monthly	Semimonthly	Biweekly	Weekly	Daily
12	24	26	52	260

Step 1. Adjust the employee's wage amount

1a	Enter the employee's total taxable wages this payroll period	1a	\$	
1b	Enter the number of pay periods you have per year (see Table 5)	1b		
1c	Enter the amount from Step 4(a) of the employee's Form W-4	1c	\$	
1d	Divide the amount on line 1c by the number of pay periods on line 1b	1d	\$	
1e	Add lines 1a and 1d	1e	\$	
1f	Enter the amount from Step 4(b) of the employee's Form W-4	1f	\$	
1g	Divide the amount on line 1f by the number of pay periods on line 1b	1g	\$	
1h	Subtract line 1g from line 1e. If zero or less, enter -0-. This is the Adjusted Wage Amount	1h	\$	

2023 Wage Bracket Method Tables for Manual Payroll Systems with Forms W-4 From 2020 or Later

WEEKLY Payroll Period

If the Adjusted Wage Amount (line 1h) is		Married Filing Jointly		Head of Household		Single or Married Filing Separately	
		Standard withholding	Form W-4, Step 2, Checkbox withholding	Standard withholding	Form W-4, Step 2, Checkbox withholding	Standard withholding	Form W-4, Step 2, Checkbox withholding
At least	But less than	The Tentative Withholding Amount is:					
\$0	\$135	\$0	\$0	\$0	\$0	\$0	\$0
\$135	\$145	\$0	\$0	\$0	\$0	\$0	\$1
\$145	\$155	\$0	\$0	\$0	\$0	\$0	\$2
\$155	\$165	\$0	\$0	\$0	\$0	\$0	\$3

The Percentage Method (Pre-2020 Form W-4)

- Multiply the number of allowances by the figure in the allowance table.

Table 7	Annually	Semiannually	Quarterly	Monthly	Semimonthly	Biweekly	Weekly	Daily
	\$4,300	\$2,150	\$1,075	\$358	\$179	\$165	\$83	\$17

- Subtract the allowance from taxable pay.
- Use the appropriate percentage method table from Publication 15-T to calculate the withholding.

The Percentage Method (2020 or Later Form W-4)

- The employee completes a 2020 or later Form W-4.
- The employer uses that information, Worksheet 4 in Publication 15-T, and the appropriate tax table to determine the correct withholding.

Worksheet 4. Employer's Withholding Worksheet for Percentage Method Tables for Manual Payroll Systems With Forms W-4 From 2020 or Later


Keep for Your Records 

Table 6

Monthly	Semimonthly	Biweekly	Weekly	Daily
12	24	26	52	260

Step 1. Adjust the employee's wage amount

1a	Enter the employee's total taxable wages this payroll period	1a	\$	_____
1b	Enter the number of pay periods you have per year (see Table 6)	1b		_____
1c	Enter the amount from Step 4(a) of the employee's Form W-4	1c	\$	_____
1d	Divide line 1c by the number on line 1b	1d	\$	_____
1e	Add lines 1a and 1d	1e	\$	_____
1f	Enter the amount from Step 4(b) of the employee's Form W-4	1f	\$	_____
1g	Divide line 1f by the number on line 1b	1g	\$	_____
1h	Subtract line 1g from line 1e. If zero or less, enter -0-. This is the Adjusted Wage Amount	1h	\$	_____

2023 Percentage Method Tables for Manual Payroll Systems With Forms W-4 from 2020 or Later

WEEKLY Payroll Period

STANDARD Withholding Rate Schedules (Use these if the box in Step 2 of Form W-4 is NOT checked)					Form W-4, Step 2, Checkbox, Withholding Rate Schedules (Use these if the box in Step 2 of Form W-4 IS checked)				
If the Adjusted Wage Amount (line 1h) is:		The tentative amount to withhold is:	Plus this percentage—	of the amount that the Adjusted Wage exceeds—	If the Adjusted Wage Amount (line 1h) is:		The tentative amount to withhold is:	Plus this percentage—	of the amount that the Adjusted Wage exceeds—
At least—	But less than—				At least—	But less than—			
A	B	C	D	E	A	B	C	D	E
Married Filing Jointly					Married Filing Jointly				
\$0	\$533	\$0.00	0%	\$0	\$0	\$266	\$0.00	0%	\$0
\$533	\$956	\$0.00	10%	\$533	\$266	\$478	\$0.00	10%	\$266

Other Federal Tax Withholding Considerations

- Certain changes (e.g., change in marital status or number of dependents) may require an updated W-4 Form.
- Dealing with deceased and terminated employees:
 - After death, a portion of the employee's earnings may be paid; these payments are not subject to federal tax withholding.
 - A terminated employee is entitled to all compensation earned; earnings are subject to federal tax withholding.

Changing the W-4 Form

- Reasons for changing:
 - Marriage
 - Divorce
 - Birth of a child
 - Job status change
- Changes result in an adjustment of federal income tax withholding.
- If making a change, an employee must submit the new 2020 or later Form W-4 rather than resubmitting an old version of the form.

State Income Tax Withholding

- This is calculated based on state taxable income (which may be the same amount used for federal taxes).
- Nine states do not collect state income tax.
- Some states levy a flat tax.
- Some states levy a graduated tax.

Local Income Tax Withholding

- Certain local jurisdictions levy taxes on those living and/or working there.
- Tax rates and how they are levied vary widely.
- They may differ for residents and nonresidents.