

Handling Overpayments Correctly

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The department of Labor accepts inadvertent overpayments if the employer and the employee do not agree that the wages were overpaid or if employee refuses to repay the amount, legal options must be considered or if both agree the wages were overpaid there are methods to recoup. When the employer makes a loan or advance of wages, it may deduct the principle from the employee's wages. The principal may be deducted even where such deduction cuts into minimum wage or overtime due under (Fair Labor Standards Act) FLSA. Here are a few situations of handling overpayments correctly.

Vacation Pay

A situation where an employee is granted vacation pay prior to that individual's established date of entitlement, with the understanding that the pay constitutes an advance on pay and the employee quits or is terminated before that date, employer may recoup the advanced vacation pay, even where such recoupment cuts into MW (monthly wage) or OT (over time) pay as required.

Federal Income Tax-Same Calendar Year

Each type of tax requires different handling when it comes to overpayment. So you must begin by taking the rules for that tax into account. If an employee repays in the same calendar year when he was overpaid, the employer excludes the employee from income on Form W-2. If it results in overpayment of FIT, the employee will receive refund upon filing of Form 1040.

Federal Income Tax (FIT) in Prior Calendar Year

Employee receives an overpayment in prior year but repays in current calendar year. Amount cannot be excluded from employee's income for any year. Can take a deduction on Form 1040 but Form W-2 is unaffected. A separate receipt should be given. Since the repayment occurred in a subsequent quarter Acme would need to file a Form 941-X to correct the wages and FIT withheld.

Federal Insurance Contributions Act in Current Year

Federal Insurance Contributions Act (FICA) Taxes in Current Year is nothing but an employee receiving and repaying overpayment in current calendar year. If returned after Form 941 is filed, employer refunds all FICA taxes on overpayment to the employee. Form 941-X is processed claiming both employee and employer portions of FICA on overpayment. Employer keeps record

of the refund. Employee provides signed statement that he or she will not seek refund from IRS.

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