

# Payroll Insights

Employment tax news to guide you now and for the future

May 2025



## John's *fresh take*: Mastering the art of tax management: Keeping overpayments and underpayments in check

Navigating the world of payroll taxes can feel like walking a tightrope. Overpayments and underpayments are almost inevitable. Imagine this: you file a Form 941-X to claim a credit, expecting a refund or to apply it to future taxes. But instead, the Internal Revenue Service (IRS) redirects that overpayment to cover an outstanding balance on your Form 1120. Suddenly, you're rallying your payroll team, corporate tax experts, CFO, and advisers to figure out where the funds should go and how to get them there.

To avoid this whirlwind, it's crucial to understand the IRS's approach, get ahead of it, and maintain control over these transactions.

### Decoding the IRS process

The IRS has established procedures for applying overpayments to underpayments, which are intended to streamline the process of settling tax liabilities. Here's how it typically works:

1. **Automatic adjustments:** The IRS may automatically apply an overpayment from one account to cover an underpayment in another. This process aims to efficiently clear tax liabilities without requiring your intervention.
2. **Notification:** You'll typically receive a notification when the IRS makes these adjustments, detailing the accounts involved and the amounts transferred. This helps you keep track of what's happening.
3. **Jurisdictional boundaries:** Once an overpayment is applied to an underpayment, the IRS might lose jurisdiction over the matter, especially if the underpayment is resolved. This can limit their ability to reverse the transaction or issue a refund without further action from you.

### Taking charge

Given the swift and often automatic nature of these processes, here's how you can stay in control:

1. **Open communication:** Foster clear communication across departments to identify potential account adjustments that could impact various parts of your organization. Ensure all teams are vigilant about monitoring IRS account transcripts for unexpected changes.

2. **Regular monitoring:** Keep a close eye on your IRS account transcripts. If they start looking more like a complex playbook than a straightforward list, it's time to act and ensure funds are correctly allocated.
3. **Verify refunds:** Before cashing any check from the Department of Treasury, verify its legitimacy. A refund check for Form 1120 might actually be a net credit from Form 941-X. Involve your mailroom and accounts receivable teams to ensure all checks are thoroughly vetted.

By understanding IRS procedures and implementing these strategies, you can effectively manage your tax accounts, minimizing disruptions and ensuring funds are applied as intended.

## Federal updates

### New feature and changes in the 2025 IRS Form 941-X instructions

The 2025 revision of the [IRS Form 941-X](#) introduces several important updates that employers should be aware of. One of the most significant changes is the ability to file Form 941-X, *Adjusted Employer's Quarterly Federal Tax Return or Claim for Refund*, electronically using the Modernized e-File system, which aims to streamline the filing process for employers.

Other updates include:

1. Lines 18a, 26a, 30, 31a, 31b, and 32, have been updated to be reserved for future use. In the prior version of the Form 941-X, those lines were used to report adjustments to the Employee Retention Credit and a specific work opportunity tax credit for periods prior to 2022. As of April 15, 2025, the period of limitations for making corrections for periods prior to 2022 has expired for most employers. The expiration of these correction periods generally applies to corrections of overreported taxes within three years of the filing date or two years from the date the tax was paid, whichever is later.
2. Employers should also note that credits related to COVID-19 for qualified sick and family leave wages can no longer be claimed. These credits were applicable for leave taken after March 31, 2020, and before October 1, 2021, and have since been removed from the form.
3. Form 941-SS and 941-PR were discontinued after the fourth quarter of 2023. Employers in US territories are now required to file Form 941 or its Spanish version, Form 941 (SP).
4. Employers must also use specific worksheets to adjust credits for qualified sick and family leave wages and COBRA premium assistance. These adjustments are detailed in Worksheets 1, 2, and 3 included within the instructions.
5. The limit for the payroll tax credit for increasing research activities has been increased to \$500,000 for tax years beginning after December 31, 2022, as per the Inflation Reduction Act of 2022.

## IRS announces interest rates for second quarter of 2025

The IRS has confirmed that [interest rates](#) will remain steady for the second quarter of 2025.

For individual taxpayers, the interest rate for both overpayments and underpayments will continue at 7 percent annually, with daily compounding. The specific rates are outlined as follows:

- Individuals will see a 7 percent rate for overpayments, while corporations will have a 6 percent rate.
- Corporate overpayments exceeding \$10,000 will be subject to a 4.5 percent rate.
- Underpayments will incur a 7 percent rate.
- Large corporate underpayments will face a 9 percent rate.

These rates are based on the federal short-term rate determined in January 2025. Further details are available in [Revenue Ruling 2025-7](#), which was published in the Internal Revenue Bulletin 2025-13 on March 24, 2025.

## Executive order mandates transition to electronic federal payments

President Donald J. Trump signed an [Executive Order](#) to transition federal payments from paper-based methods to electronic systems, effective September 30, 2025. This change aims to improve the efficiency and security of government financial transactions by requiring all federal disbursements, including benefits, vendor payments, and tax refunds, to be processed electronically. The transition will utilize electronic funds transfer methods such as direct deposit, debit and credit card payments, digital wallets, and real-time transfers.

The order also mandates that payments made to the federal government, such as fees and taxes, be processed electronically where legally permissible. To support this shift, the Treasury Department will phase out physical lockbox services and expedite electronic collection of federal receipts. A public awareness campaign will inform recipients about the transition and provide guidance on setting up digital payments. Exceptions will be made for individuals without access to electronic payment systems and certain special cases.

## GOP Committee Chair sets forth policy priorities for new Secretary of Labor

In a letter to newly confirmed Secretary of Labor Lori M. Chavez-DeRemer, Republican Committee Chair Tim Walberg outlined [several payroll-related policy priorities](#) and oversight concerns for the Department of Labor. The letter emphasizes the need for reform in wage and hour regulations.

Chairman Walberg urged the Secretary to reconsider several regulations enacted during the Biden-Harris administration. These include rules on overtime, minimum wage for federal contractors, and tip regulations under the Fair Labor Standards Act. The Committee advocates for a shift from the enforcement-heavy approach of the previous administration to one that emphasizes compliance assistance.

The letter also calls for the rescission or withdrawal of specific regulations, such as those related to the employment of workers with disabilities and changes to the Davis-Bacon Act and related acts. Additionally, the Committee expressed concerns over the efficient use of taxpayer money and the need for transparency in workforce data.

## Gold Card initiative: Opportunities and tax implications for US immigration reform

On February 26, 2025, President Trump introduced the “[Gold Card](#)” initiative, which would allow a foreign individual similar privileges as a green card, but much more quickly than the typical process. The Gold Card program is aimed at attracting wealthy individuals to the US in anticipation that the Gold Card holder would subsequently invest in the US economy. A US company may purchase a Gold Card, for example, for a highly skilled graduate who may not otherwise be legally allowed to work in the US after their student visa expires. The cost of a Gold Card is expected to be \$5 million.

When purchased by an employer for an employee, there are potential tax implications associated with the Gold Card that both employees and employers should consider. During a subsequent announcement on March 4, 2025, President Trump mentioned that Gold Card holders would not be taxed on income earned outside the United States. This potential tax benefit could serve as an incentive for attracting top talent, although the specifics of how this would be implemented remain unclear.

Employers contemplating the purchase of a Gold Card should be aware of possible additional tax liabilities. The \$5 million fee might not qualify as a tax-deductible business expense if it cannot be excluded from wages as a working condition fringe benefit, potentially making it taxable income for the employee. This could lead to further tax obligations, including the employer's share of payroll taxes and potential tax gross-ups if the employer chooses to offset the employee's tax burden.

While the President has suggested that the Gold Card may offer tax advantages not available to green card holders, the details of these benefits have not been fully clarified. See the KPMG GMS Flash Alert 2025-054 for additional insight. [United States – Trump's "Gold Card," tax implications](#)

### **Understanding potential penalties for employee retention credit claims**

Taxpayers who have submitted claims for the Employee Retention Credit may be subject to several penalties if found ineligible. The IRS has specified penalties such as failure-to-pay, ranging from 0.5 percent to 25 percent of the unpaid tax; failure-to-file penalties, ranging from 5 percent to 25 percent of the amount due; and failure-to-deposit penalties, ranging from 2 percent to 15 percent. Accuracy-related penalties include a 20 percent penalty for understatements due to negligence.

If the IRS determines there was fraud involved in claiming erroneous credits, a civil fraud penalty of 75 percent may be assessed. Fraudulent failure-to-file penalties, combined with failure-to-file penalties, range from 15 percent to 75 percent, and trust fund recovery penalties (TFRP) can be assessed against individuals responsible for collecting and paying over employment taxes. While most penalties apply to the employer entity, the TFRP can also target individual owners or employees responsible for the employer's tax obligations.

### **Reminder: Extended tax deadlines for 2024 disaster-affected regions**

IRS is reminding individuals and businesses in areas impacted by 2024 disaster declarations that automatic extensions for personal income tax returns and certain payments may be available. The extended deadline is October 15, 2025, for Los Angeles County, California, and November 3, 2025, for Kentucky and specific counties in West Virginia. Special relief is also available for taxpayers affected by terrorist attacks in Israel, with a filing and payment deadline of September 30, 2025.

The IRS automatically provides filing and penalty relief to taxpayers in disaster areas, eliminating the need for them to contact the agency. However, taxpayers outside these areas, whose records are located in affected regions, should reach out to the IRS for assistance. Those with uninsured or unreimbursed disaster-related losses may be able to claim them on either the return for the year the loss occurred or the prior year's return, as detailed in Publication 547, Casualties, Disasters, and Thefts.

### **Streamlining state income tax for mobile workers: The Mobile Workforce State Income Tax Simplification Act of 2025**

Senators John Thune (R., SD) and Catherine Cortez Masto (D., NV) introduced the [Mobile Workforce State Income Tax Simplification Act of 2025](#) (the Act), a legislative proposal aimed at regulating state income tax obligations for employees who work in multiple states. The Act seeks to limit the authority of states to impose income taxes on wages earned by employees performing duties across state lines. Under the Act, employees would only be subject to state income tax in their state of residence and in any state where they work for more than 30 days within a calendar year.

The Act outlines specific rules for determining tax obligations, including the reliance on employee records for time spent working in different states, unless an employer maintains a precise time and attendance system. If passed, the Act would take effect on January 1 of the second calendar year following its enactment and would not apply to tax obligations accruing before its effective date. Note that similar proposals have been submitted during numerous legislative sessions in the past without sufficient agreement to pass.

### Alabama H.B. 379

Ala. H.B. 379 adds language to Alabama Code Section 40-18-2.2, which excludes certain nonresident income from Alabama state income tax (SIT) withholding. If signed into law, then effective January 1, 2026, Alabama nonresidents should not be subject to Alabama SIT withholding from wages paid for services performed in Alabama if all four of the following criteria apply:

1. Compensation paid for employment duties performed by the nonresident individual in the state on 30 or fewer days in a calendar year;
2. The nonresident individual performed employment duties in more than one state during the calendar year;
3. Compensation is not paid for employment duties by the nonresident individual in their capacity as a professional athlete, professional entertainer, or public figure; and
4. The nonresident individual's state of residence:
  - o Provides a substantially similar exclusion (i.e., a de minimis threshold);
  - o Does not impose an individual income tax; or
  - o The individual's income is exempt from taxation by this state under the United States Constitution or federal statute.

If any of these criteria are not satisfied, then a nonresident employee should be subject to Alabama SIT on the first day that wages are paid for services performed in the state. Further, if all four criteria are satisfied but the employee performs services in Alabama for more than 30 days during the calendar year, then the employer should be required to withhold and remit Alabama SIT on all wages paid during the calendar year (i.e., retroactive to wages paid for days one through 30 during the calendar year).

### Arkansas and Utah regulate earned wage access

Arkansas and Utah have recently introduced laws to regulate earned wage access (EWA) providers, joining other states in establishing guidelines for this financial service. Arkansas Code, Section 23-52-202 defines an EWA provider a person or business offering and providing EWA services to a consumer.

In Arkansas, effective June 18, 2025, EWA providers are not required to register with the state or obtain a special license to operate. They should adhere to specific rules, such as not charging employees late fees or interest for failing to repay any outstanding amounts.

In Utah, effective May 7, 2025, EWA providers should register annually with the Utah Division of Consumer Protection and pay a registration fee. Providers already operating as of May 7, 2025, can continue their activities but should comply with the new law and submit a registration application by October 6, 2025.

Pursuant to Arizona H.B.1517 and Utah H.B. 279, employees and independent contractors are protected since EWA providers are now restricted from imposing fees, interest, or penalties for unpaid debts. However, providers can restrict users from accessing earned wage services if they have unpaid balances from prior transactions.

### Iowa introduces bill that significantly changes the state's unemployment taxable wage base

The recently signed Iowa bill, Senate File (SF) 603, introduces significant changes to the state's unemployment taxable wage base, effective July 1, 2025. This legislation includes amending the definition of "taxable wages," for purposes of determining the amount of wages subject to unemployment taxes. Previously, Iowa employers could receive a taxable wage credit for wages paid to out-of-state employees who, subsequently, became covered employees in Iowa, but SF 603 eliminates this credit. As such, the Iowa unemployment insurance trust fund is projected to see an annual revenue increase of \$394,000, impacting approximately 2.5 percent of Iowa employers who utilized the credit. For 2025, the taxable wage base is set at \$39,500.

## Seattle, Washington, retroactive Social Housing Tax

During an election held in February, Seattle voters approved the Seattle Social Housing Tax, which has now been codified as Chapter 5.37, Social Housing Tax, and is effective retroactively to January 1, 2025. The new chapter imposes a 5 percent tax on compensation exceeding \$1 million paid to an employee in Seattle. This tax is paid by employers and cannot be deducted from employee wages. For 2025, affected Seattle employers should file returns and pay the tax by January 31, 2026. Starting in 2026, tax returns and payments will be due quarterly.

This new tax is an addition to the existing Seattle payroll expense tax, which also requires employers to pay taxes based on the compensation paid to employees in Seattle. Both taxes are part of Seattle's efforts to address housing affordability through employer contributions.

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