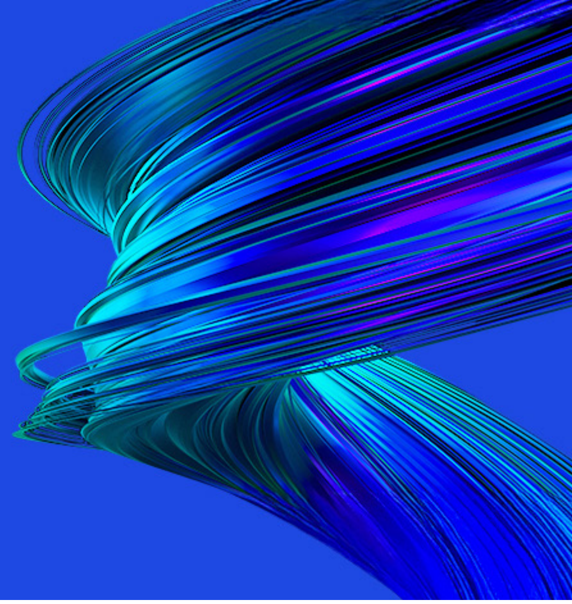

Payroll Insights

Employment tax news to guide you now and for the future

February 2026

This month's issue provides a summary of recent developments from the Internal Revenue Service (IRS) and state revenue departments that continue to shape the 2026 payroll landscape. Key items include the finalization of the 2026 Form W-2, *Wage and Tax Statement;* new standard mileage rates; and important state-level withholding and tax changes.

John's *fresh take:* Navigating W-2c requests and complex state wage allocations

Your 2025 Form W-2, *Wage and Tax Statement,* has just gone out the door, and your inbox is already full of requests for Form W-2c, *Corrected Wage and Tax Statement.* Employees expecting refunds with their personal income tax returns are eager to file, but something on their Form W-2 doesn't look right (to them!). Often, a simple email response to the employee resolves the confusion. However, we frequently receive questions, specifically about state wage allocations, that may not have a simple answer or may even require a Form W-2c. Every state is different, so every situation may require a separate analysis.

Some common situations that may require additional research or amendments include an employee who moved midyear and did not notify the employer, wage allocations to multiple states due to business travel, and the sum of all state wages not equaling total federal wages.

The basic concepts that underline these questions and potential amendments are that the employee is generally responsible for notifying the employer of their resident jurisdiction and the employer is generally responsible for knowing where the employee is performing services and sourcing the state and local wages according to the jurisdiction's laws.

This is general guidance to keep in mind as questions come flooding in. As mentioned above, each state and locality impose different rules, and each situation should be analyzed separately to determine if amendments should be made or if an explanation will suffice. As always, remind employees that they should speak with their personal tax advisers related to individual income tax advice.

Federal updates

IRS finalizes 2026 Form W-2 with key clarifications

On January 9, 2026, the IRS issued the final version of the 2026 Form W-2. The form includes important updates to the instructions for the reporting of tips, overtime compensation, and Trump account contributions for compliance with the One Big Beautiful Bill Act (OBBBA). The IRS also released the counterpart Forms W-2 for American Samoa and Guam.

Tip compensation

Box 12, Code TP, should be used by employers to report the total amount of qualified cash tips received by the employee. If cash tips are reported in Box 12 using Code TP, then the employer is required to report the Treasury Tipped Occupation Code in Box 14b. The Treasury Tipped Occupation Codes, are available on the IRS website. An employer may enter up to two codes based upon the occupations in which the tips were received.

The instructions clarify that if the tips were received in a nonqualifying occupation, then Code 000 should be reported as one of the occupation codes.

Qualified overtime compensation

Box 12 Code TT should be used by employers to report the total amount of qualified overtime compensation.

Trump account contributions

Box 12 Code TA should be used by employers to report contributions to Trump accounts.

Form 944 reporting continues in 2026

The IRS postponed the discontinuance of *Form 944, Employer's Annual Federal Tax Return*. In certain cases, Form 944 may be used by employers in lieu of Form 941, *Employer's Quarterly Federal Tax Return*, if approved by the IRS. Form 944 was originally scheduled to be discontinued for tax years after 2025 for employer reporting purposes. This would have then required employers to file quarterly Form 941 rather than the annual Form 944.

With the postponement, Form 944 may continue to be used by smaller employers who have an estimated annual liability of federal employment tax of $1,000 or less and have been approved by the IRS to file Form 944. Note that an employer's request to file Form 944 must be made by March 16 (if made in writing) or April 1 (if made by phone).

IRS finalizes publication 15-B and releases 2026 standard mileage rates

The IRS released the final version of the 2026 Publication 15-B, *Employer's Tax Guide to Fringe Benefits*, including the numerous fringe benefit updates and limits that were discussed as part of the draft Publication 15-B in last month's edition of *Payroll Insights*. The 2026 IRS Publication 15-B was published before the business mileage rates for 2026 having been finalized. These rates can be found in Notice 2026-10.

As stated in Notice 2026-10, effective for the 2026 calendar year, the standard mileage rate for the business use of an automobile will increase to 72.5 cents per mile, up from 70 cents in 2025.

For medical or moving purposes, the 2026 standard mileage rate will decrease slightly to 20.5 cents per mile from 21 cents in 2025. The rate for charitable use, which is set by statute, remains unchanged at 14 cents per mile.

Additionally, Notice 2026-10 increased the maximum standard automobile cost for calculating allowances under a fixed and variable rate plan to $61,700 for 2026.

Employer contributions to Trump accounts

The final 2026 IRS Publication 15-A, *Employer's Supplemental Tax Guide*, provides that beginning July 4, 2026, employers may contribute up to $2,500 per year to a Trump account, which should be indexed for inflation after 2027, until it reaches the annual $5,000 contribution that can be made to a Trump account (as established by PL 119-21). The contribution can be made to the account of an employee (if under the age of 18) or of a dependent of an employee (if the dependent is under the age of 18), and the amount should be excluded from the gross income of the employee if paid pursuant to a Trump account contribution program. The Treasury Department and the IRS previously released guidance on Trump accounts in Notice 2025-68 that also clarified that employer contribution limits are per employee and not per dependent of the employee and that contribution programs can be offered via salary reduction under a Section 125 cafeteria plan.

Employers should partner with their benefits and legal teams to confirm that any new or revised company policies are compliant with federal regulations before making contributions to Trump accounts. In addition, state and local tax laws should be reviewed to identify if such contributions should be recognized as supplemental taxable wages at the state or local level.

Wage garnishment on student debt delayed

On January 16, 2026, the US Department of Education announced further delays to restarting wage garnishments for student loan debt in default.

IRS Advisory Council issues annual public report

The IRS Advisory Council (IRSAC) issues an annual report of observations and recommendations to the commissioner of the IRS. The report also analyzes the IRS's actions in response to IRSAC's prior-year report.

The IRSAC recommended several updates to the IRS voluntary disclosure programs in recent years, and the 2026 report, issued on January 14, 2026, notes that they have not seen many improvements. The recommendations to improve voluntary disclosure programs listed in the 2026 report include the following:

a. Allow domestic, nonwillful taxpayers without reasonable cause for the error to participate in the programs.

b. Revise penalties to be "modest, predictable, and proportionate."

c. Improve transparency by publishing participation and outcome data.

Employment tax–related voluntary disclosure programs, including the Voluntary Closing Agreement Process for Employment Tax, the Voluntary Classification Settlement Program (for worker misclassification), and the Tip Rate Determination Agreement, are specifically included in the report as programs that would benefit from these recommendations.

US Department of Labor issues four opinion letters

On January 5, 2026, the US Department of Labor (DOL) issued four opinion letters to clarify FLSA rules, as follows:

FLSA2026-1: clarification on the learned professional exemption

FLSA2026-2: treatment of certain bonus payments in regular rate of pay

FLSA2026-3: if "roll call" time pursuant to a collective bargaining agreement is includable for overtime hours

FLSA2026-4: minimum pay standard for exemption for commission employee.

These opinion letters are interpretations of the FLSA by the current federal administration and *are not binding in any other circumstances*. However, they can be an important tool for an employer when reviewing current FLSA practices and calculations. Because the OBBBA qualified overtime compensation reporting requirements are based on FLSA rules, all employers with overtime-eligible employees, including those who pay overtime more generously than the FLSA requires, should review their calculations in line with DOL guidance to make sure overtime premiums are paid and reported correctly.

State and local updates

Illinois updates withholding allowance for 2026

Illinois updated its [2026 state income tax] withholding methods, increasing the value of a standard withholding allowance to $2,925 (up from $2,850). The additional allowance for age or blindness remains at $1,000, and the state's flat income tax rate is unchanged at 4.95 percent.

Louisiana updates withholding method for 2026

Louisiana updated its 2026 state income tax withholding methods, as announced in a Declaration of Emergency released by the Department of Revenue Tax Policy and Planning Division. The rule provides an update to the standard deduction ($12,875, up from $12,500 in 2025) and confirms the tax rate of 3.09 percent to be used by employers in 2026.

Louisiana emergency rules are valid for 180 days. An extension or other legislation must pass before the expiration for the updates to be valid for the second half of 2026.

Massachusetts releases the final 2026 tax tables

Massachusetts released the final 2026 Circular M, *Income Tax Withholding Tables,* which includes the 4 percent surtax on wages in excess of $1,107,750 annually. The flat tax rate of 5 percent is generally applicable to all taxable wages in 2026.

Minnesota releases guidance on worker classification

On December 4, 2025, the Minnesota Department of Revenue released an updated tax factsheet providing guidance on classifying workers as employees or independent contractors. The factsheet outlines criteria for proper classification and highlights key differences between employees and independent contractors for state tax withholding purposes.

Summary of updates

- Clarified classification criteria: The factsheet provides updated guidance on determining whether a worker should be classified as an employee or an independent contractor for Minnesota withholding tax purposes. It emphasizes the importance of evaluating behavioral control, financial control, and the relationship between the parties.
- Expanded examples and scenarios: New examples illustrate common situations, helping employers understand how to apply the classification criteria in practice.
- Updated compliance requirements: Employers are reminded that misclassification can result in penalties and additional tax liabilities. The factsheet outlines steps to correct misclassification and comply with withholding requirements.

Minnesota paid leave enacted

As reported in prior issues of Payroll Insights, employer contributions and paid leave benefits went into effect on January 1, 2026, with the first report and contribution payments due on April 30, 2026. Impacted employers without a Minnesota unemployment insurance account should register for a paid leave account. Employers with an existing Minnesota unemployment insurance account will pay and report the contributions with their current returns, if applicable.

Mississippi reduces withholding tax rate for 2026

As a reminder of Mississippi House Bill 1, the Mississippi state income tax withholding rate on taxable income in excess of $10,000 has decreased to 4 percent for 2026. The rate is currently set to be reduced to 3.75 percent in 2027.

Nebraska lowers withholding tax rates for 2026

The Nebraska Department of Revenue released its 2026 withholding methods, reflecting several decreases in income tax rates for the upcoming year.

The top four income tax rates used in the state's percentage method have been reduced, with the new rates ranging from 2.26 percent to 4.6 percent, down from a top rate of 5.37 percent in 2025. Additionally, the value of a state allowance increased from $2,360 to $2,440 annually.

Notably for payroll processing, the flat withholding rate for supplemental wages paid separately from regular pay has been lowered from 5 percent to 3.5 percent. This new rate also applies to nonperiodic pensions and annuities.

North Dakota adjusts 2026 withholding brackets

North Dakota adjusted its 2026 tax brackets, including an increase in the zero-tax bracket's upper threshold. The tax rates, however, remain unchanged from 2025, with the supplemental wage rate holding at 1.5 percent.

Oregon updates 2026 withholding formula

For 2026, the Oregon Department of Revenue updated its income tax withholding formula with increased values for deductions and allowances.

The standard deduction used in the formula rose to $2,910 for single employees (up from $2,835) and $5,820 for married employees (up from $5,670). Additionally, the value of a state withholding allowance increased from $256 to $263.

The maximum amount of federal tax that can be subtracted from taxable wages also increased to $8,750. However, the department confirmed on its website that the rates for the local TriMet (0.8237 percent) and Lane County (0.8 percent) transit district taxes will remain unchanged for 2026.

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