



**March 16, 2011**

## **Worcester Pays up \$356,000 in Taxes**

The city of Worcester owed the IRS \$356,570 because it failed to classify certain job-related allowances paid to employees as part of their reported incomes, made errors in Medicare withholdings for some of its employees and did not report vendor payments in its 1099 Form. In addition, the city allowed 11 of its municipal workers 24 hour use of city vehicles for emergencies but they were not assessed \$3 per day on their W-2 Forms.

And employees who were claiming full exemption from IRS withholdings of income taxes did not supply annual W-4 filings with the city as required.

These issues were discovered when the IRS conducted an audit on the city's 1099 and W-2 filings for 2007. During the audit, the IRS reviewed more than \$500 million paid by the city in wages, employee reimbursements and vendor payments that year.

In total, the city owes \$356,570 made up of \$293,755 in federal income taxes, \$42,815 in Medicare taxes and was fined \$20,000 for failure to issue 1099 Forms to outside legal counsels and medical services. The city council voted unanimously to transfer the funds and pay off this debt after its manager, Michael V. O'Brien informed the council of this matter.

O'Brien also gave the assurance to the council that the necessary measures

have been taken by the city treasurer, chief financial officer and auditor to satisfy IRS requirements. As such the IRS found no reason to audit submissions from any other financial year.

The job-related allowances paid to the city's employees which the IRS said should have been classified as income were reimbursements for these employees who are required to purchase certain tools, clothes and equipment for their jobs. They include firemen, police officers, School Department custodial and trade employees. Their purchases of the items they require for their work are reimbursed by the city under collective bargaining contracts the city has with these employee groups.

Starting from July 1, 2008, the city has classified these reimbursements as employee wages on employee W-2 Forms. However, the IRS noted that the city needs to provide a more thorough substantiation to back up those payments, even though the amounts are clearly set by collective bargaining agreements. Therefore, the city has implemented measures that require more detailed receipts before reimbursements can be made.

As for the Medicare issue, the city did not withhold Medicare taxes for employees who quit their jobs but were re-hired because the Worcester financial system at that time recognized their original start date.