



# TOP TIPS: EMPLOYEE WITHHOLDING TAXES EXPLAINED

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# EMPLOYEE WITHHOLDING TAXES EXPLAINED

Whether you have a part-time job after school or you're entering the job market for the first time, you don't get to keep all of what you earn. The difference is mostly due to deductions taken out of your pay check by your employer for income taxes. Generally speaking, the amount withheld from your paycheck is based on your expected yearly earnings, marital status (single or married) and the number of allowances you're claiming (family size). This information is submitted to your employer when you complete a W-4 form (Employee's Withholding Certificate) which your employer is responsible to give you when you start a new job. The more allowances you claim the less income taxes will be withheld from your pay check; the less you claim, the more taxes will be withheld. If you don't submit a W-4 form your employer can place you in the highest tax bracket. Which means you may have to pay more taxes than you otherwise would.

Employers are required by law to withhold income taxes from your pay check. They must also report and submit the taxes withheld to the government. This is because the United States system of taxation is based on a pay-as-you go system. This means that you must pay your taxes throughout the year. For most people who earn a salary this is accomplished through automatic withholdings for each pay period. In addition, the United States tax system is progressive which means that the more money you earn the more taxes you will pay.

Below you will find the various types of taxes that are withheld from your paycheck and what the taxes are used for by the various governmental agencies.

## FEDERAL INCOME TAXES

Your employer will submit this type of income tax to the Federal government. The amount withheld from your paycheck will depend on your yearly earnings, marital status and how many allowances you claim. The Federal government collects this type of tax in order to provide its citizens with interstate highway systems, health services, national parks, military and social services such as food stamps and housing.

## STATE INCOME TAXES

Depending on where you live, you may not have state withholding or you might have withholding for more than one state. That means the state you live in and the state you work in. Similar to the Federal income tax, the amount withheld from your pay check will depend on your yearly earnings, marital status and how many allowances you claim. The state government collects these taxes to pay for highway construction and upkeep, public colleges and law enforcement.

## LOCAL INCOME TAXES

This type of tax maybe withheld on earnings inside city, county, and school district boundaries. If you live or work in a jurisdiction that imposes such a tax, earnings will be taxed by that jurisdiction. Similar to the Federal and State income taxes, the amount withheld from your paycheck will

depend on your yearly earnings, marital status and how many allowances you claim. At the local level, these taxes support spending for public schools, roads, libraries, athletic facilities and the salaries of county and municipal employees.

## SOCIAL SECURITY TAXES

This tax is one component of the Federal Insurance Contribution Act (FICA). It is also known as the Old Age, Survivors, and Disability Insurance tax (OASDI). Your employer will typically withhold a flat rate of 6.2% of your gross earnings up to a maximum dollar limit which generally changes every year. If you reach the maximum payment you do not pay any more Social Security tax until the next calendar year. This type of tax is used to provide benefits for retirees, surviving family members and for the disabled and their dependents.

## MEDICARE TAXES

This tax is the other part of the Federal Insurance Contribution Act (FICA). Your employer will typically withhold a flat tax rate of 1.45%. This tax has no maximum dollar limit which means the rate is applied to all of your gross earnings. This tax is used to provide government regulated health care to qualified employees, retirees and their spouse when they reach age 65.

The various types of income taxes withheld by your employer are sent to the appropriate governmental agency which credits the amount to your tax account. When you file your income

tax return it provides an opportunity to settle up your tax bill with the government. If you paid too much tax you will receive a refund from the government. If you didn't pay enough tax you will owe money to the government.

The taxes that are withheld from your paycheck are one of several ways in which the Federal, State and Local governmental agencies are able to raise money. The taxes collected are used to pay for public services such as schools, roads, military, medical services and so forth. These are the things that citizens need, want and demand. If we didn't have the governmental agencies providing public services, each person would have to pay full value for them. Many people may not be able to afford to pay for them.

Even though your take home pay is smaller than what you expected, you now know the various types of taxes withheld and why they are withheld.



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