

PAYMENTS TO CORPORATE OFFICERS

The purpose of this information sheet is to clarify whether payments made by a corporation to a corporate officer who is an employee under Sections 621(a) and 13004 of the California Unemployment Insurance Code (CUIC) should be classified as a loan or as wages.

WHAT ARE WAGES?

Wages are payments made to an employee for his or her personal services, including commissions, bonuses, and the reasonable cash value of all remuneration paid to an employee in any medium other than cash (for example, lodging and meals).

FACTORS INDICATING LOANS OR WAGES

Section 926-6 of Title 22, California Code of Regulations, defines a "loan" as a payment made by an employer to an employee in consideration of an oral or a written agreement between the parties for repayment in full, irrespective of earnings in the employ of the employer. Wages does not include a loan made by an employer to an employee, but earnings for services in employment applied to reduce the debt under the loan are "wages" at the time they are actually or constructively paid.

The following factors, when available, are used by the Employment Development Department (EDD) to determine if a specified payment made to a corporate officer constitutes a loan or wages. These factors were established in tax decisions issued by the California Unemployment Insurance Appeals Board (CUIAB).

Loans

1. A pre-incorporation agreement exists calling for assumption of the liability owed to a corporate officer by the predecessor corporation to be paid by the successor corporation.
2. The loan was acknowledged in the Articles of Incorporation.
3. The loan was recorded in the corporate minutes.
4. There exists a corporate resolution stating that the loan was bona fide.

5. The loan was so named in company books, which include the general ledger, and show the appropriate increase and decrease in the loan balances.
6. The loan was secured by a note.
7. Income tax returns report the loan.

Wages

1. It is not possible by examining accounting or payment records to determine whether the payments received by the corporate officer are acknowledged wages or a loan.
2. There is no written evidence of a loan.
3. There is no record of any meeting by officers or directors of the corporation authorizing payment to be for the loan.
4. There is no effort made to collect the loan money by the corporation.
5. The payments made to a corporate officer in order to allow him or her to meet living expenses will be considered wages where evidence is insufficient to establish that such payments are a bona fide loan.
6. The loan agreement had a low interest rate, only payable on demand, and was unsecured.

In considering each of these available factors, a determination of whether payments are a loan or wages will depend upon a grouping of factors that are significant in relation to the service being performed by the corporate officer. There is no single controlling factor.

Examples

Tax decisions by the CUIAB provide some guidance as to whether payments to corporate officers constitute loans or wages.

1. A corporate officer loaned money to the corporation. The corporate officer raised the money through personal loans from banks. The pre-incorporation

agreement called for the corporation to assume the liability owed the corporate officer. The corporation's board of directors passed a resolution affirming all liabilities. The corporation was repaying the corporate officer. These payments were held to be repayment of a loan.

2. The recipient of the loan was a corporate officer. The loan was given to the corporate officer for his convenience when his salary was being garnished. The loan agreement was drafted by the corporate officer and contained terms entirely favorable to him; it was an open-ended agreement providing a favorable rate of interest and payable only on demand. It was unsecured. The corporation has made no demand for payment, and the payment was listed as compensation in the corporate accounting system. The money received by the corporate officer was held to be wages.

By no means do the above-mentioned cases encompass the entire set of factors used by the CUIAB in establishing the classification of payments made to corporate officers. They are presented here as examples only. The EDD and the CUIAB will determine status of payments on a case-by-case basis by applying the CUIC to the specific facts.

REPORTING REQUIREMENTS

If payments received by corporate officers are wages, they are taxable for Unemployment Insurance, Employment Training Tax, State Disability Insurance,* and California Personal Income Tax (PIT) purposes. The PIT should be withheld based on the federal Employee's Withholding Allowance Certificate (Form W-4) or the EDD's *Employee's Withholding Allowance Certificate* (DE 4) completed by the corporate officer.

ADDITIONAL INFORMATION

For further assistance, please contact the Taxpayer Assistance Center at 888-745-3886 or visit the nearest Employment Tax Office listed in the *California Employer's Guide* (DE 44) and on the EDD's website at www.edd.ca.gov/Office_Locator/. Additional information is also available through the EDD's no-fee payroll tax seminars and online courses. View the in-person and online course offerings on the EDD's website at www.edd.ca.gov/Payroll_Tax_Seminars/.

The EDD is an equal opportunity employer/program. Auxiliary aids and services are available upon request to individuals with disabilities. Requests for services, aids, and/or alternate formats need to be made by calling 888-745-3886 (voice) or TTY 800-547-9565.

*Includes Paid Family Leave (PFL).

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