Alliance Partners Training

Part 3

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What is Payroll?

The word Payroll refers to a company's list of employees, along with employee information. It also is the total amount of money paid to all employees during each pay period. It can refer to the process of calculating and distributing wages and taxes and the records of salaries, wages, bonuses and withheld taxes. And finally, it refers the department within a company that processes and records the above.

Once upon a time an employer handed payment to his/her employees directly at some semi regular interval, daily, weekly, bi-weekly etc. The amount was not always correct or complete, but employees had no recourse other than to go find work elsewhere. Payment of wage has included room & board, food, livestock, land, gold silver, ownership, freedom and just about anything you can name.

Gradually over a period government intervention begin to safeguard employees and require employers to more equitably compensate employees. Cash and later checks became the standard. Employees began to demand better working conditions and pay. As some employers became larger and the skillsets of the employees grew the employee bargaining power became grater. Unions formed, federal and state laws were enacted. Employers begin to see that a better paid, happier work force was more productive and would even drive up demand for the employer goods or services.

And then came taxes!

Once the federal and state governments begin to take money from the employees and the employers they have never considered stopping. Government agencies at various levels, federal, state and even city require employers to withhold income taxes from employees' wages in trust until paid to the government. Failure to do so will result in fines and penalties. The government taxing agencies can even attach bank accounts without notice leaving the employer in a position where he or she must prove that the amount taken was greater than what was owed all the while scrambling to deal with empty bank accounts. An employer must withhold payroll taxes from an employee's check and hand them over to several tax agencies by law. Payroll taxes include the following:

1. Federal income tax withholding, based on withholding tables set by the Internal Revenue Service – IRS;
2. Social Security tax withholding. The employee pays a percent of the salary or wage, up to a set amount.
3. The employer also pays a percent in Social Security taxes. If you are self-employed, you pay the combined employee and employer amount of 12.4 percent in Social Security taxes on your net earnings;
4. Medicare tax. The employee pays a percent in Medicare taxes on the entire salary or wage. 0.9% is added for the salary portion bigger than $200,000 (only for the employee portion). The employer also pays a

matching percent in Medicare taxes (regardless if the amount is bigger than $200,000). If you are self-employed, you pay the combined employee and employer amount in Medicare taxes on your net earnings;
5. State income tax withholding;
6. Various local tax withholding, such as city taxes, county taxes, school taxes, state disability, and unemployment insurance.

Companies typically generate their payrolls at regular intervals, for the benefit of regular income to their employees. The regularity of the intervals varies from company to company, and sometimes between job grades within a given company. Common payroll frequencies include: daily, weekly, bi-weekly (once every two weeks), semi-monthly (twice per month), and monthly. Less common payroll frequencies include: 4-weekly (13 times per year), bi-monthly (once every two months), quarterly (once every 13 weeks), semi-annually (twice per year), and annually (yearly).

Before an employer can begin to process payroll, they will need to collect some information from the employees. Every employee must fill out Form W-4. This form will provide the payroll department with information about each employee's federal income tax withholding exemptions, along with their names, addresses, and Social Security numbers. All this information must be known to properly run and distribute payroll.

Time and attendance must be taken and recorded to know what to pay hourly employees and to protect the employer against employee generated litigation. Salaried employees are not necessarily exempted from overtime and recording their hours also is a measure of job performance.

Tracking time off for PTO, sick days, and vacation not only makes good business sense but is also now required for sick days given and taken in California as well as many other states.

If an employer has employees in multiple cities and or states all the additional jurisdictions may and probably will have different rules and regulations that must be kept up with and followed.

Salaries and wages

A salary is a fixed amount paid to an employee. Typically, an employee is given a yearly salary, which is then divided by the number of pay periods in the year.

For example, if an employee has a yearly salary of $28,600. The employer pays the employee every week, which means the weekly paycheck will be $550 before deductions ($28,600 / 52 weeks).

A wage is what is paid to an employee based on the hours worked. The employer will set a specific rate of pay for each hourly employee. To calculate an employee's total wages, you will multiply the rate of pay by the number of hours the employee works.

For example, an employee is paid $12 per hour. The employee worked 34 hours this week. The employee is owed $408 before deductions ($12 x 34 hours).

Overtime pay

All nonexempt employees must receive overtime pay in California for more than eight hours in a day or forty hours in a week. This includes both nonexempt hourly and salary workers. Again overtime varies state by state and changes from time to time.

Fringe benefits

Fringe benefits are a type of compensation. Benefits can include education assistance, health insurance, retirement plans, and employee discounts. Any benefits offered to an employee should be included in payroll. Some benefits are taxable and some are not. These tax calculations must also be done during the payroll processing.

Other pay

Employees could have additional sources of pay. Service workers may receive tips for example. Employees must report all tips to the employer, and there are payroll taxes on tips. If employees may also receive a commission or a bonus pay. You should include commissions and bonuses when you run payroll.

Deductions

A deduction is any money subtracted from an employee's total wages.

Payroll taxes

Every employer must deduct payroll taxes from the wages of every employee. The amount withheld from each employee will vary depending on total earnings and how many withholding allowances the employee claims on the W4 form. Marinating W4s and keeping them up to date is a joint responsibility of the employer and the employee.

Payroll taxes include federal income tax, state income tax, local income tax, federal unemployment tax, state unemployment tax, Medicare tax, and Social Security tax.

Garnishments

A garnishment is a court-ordered deduction post-tax deduction. A garnishment is used to pay off an employee's overdue debt. Employers could be instructed to deduct money from an employee's paycheck to pay for unpaid taxes, defaulted loans, and overdue child support. Garnishments are court orders to the employer and must be withheld and paid as directed in order to not face a bench warrant.

Net and gross pay

Employers need show an employee's net and gross pay on a pay stub. Gross pay is an employee's total pay. IRS forms typically ask for an employee's gross pay.

Net pay is an employee's pay after all deductions are subtracted. Net pay is an employee's take home pay. Banks and other loan providers typically want to know someone's net pay.

Options to run payroll

An employer has several payroll solutions when it comes to running payroll.

1. **Do payroll by hand.** The employer will have to learn how to do payroll. This option will be the most time-consuming. The IRS provides tax tables that can be used to calculate federal income tax withholding (found in IRS Publication 15). Also it is advisable to subscribe to all IRS publications and updates that effect payroll. State taxing agencies have additional tables, publications and subscription updates. Care should be taken here, errors can be costly today and years into the future.
2. **Use a payroll accountant.** Outsourcing payroll to a payroll accountant could free up some of your precious time. The account will take care of the entire payroll process. However, this option will most probably be the most expensive.
3. **Use a payroll software.** Most payroll software is inexpensive. Software for payroll automates a lot of a company's payroll program, meaning the employer will spend less time doing payroll. Payroll business software can calculate wages and taxes, and some will even turn in the taxes. The quality of payroll software varies and if an employer is not a payroll expert which software to place the financial future of your company can be a difficult decision. Additionally software is still just a tool. In the hands of an untrained person the results can be disastrous.

4. **Hire HR Ledger.** We do more payrolls in one day than most employers will do in a lifetime. Payroll is what we do, we don't have another business. We cover our employer clients against our errors with a $50,000,000 bond. Employers can then invest all the time and stress of other payroll methods into growing their own businesses.