

## Payroll 101 – An Employer's Obligations

An employer has many obligations related to their payroll. Below are some basic payroll topics you need to understand in order to process a payroll.

- [FLSA](#)
- [Who are Employees?](#)
- [Wages and Other Compensation](#)
- [Pay Frequencies](#)
- [Employee-Paid Taxes](#)
- [Employer-Paid Taxes](#)
- [Payroll Tax Deposits and Returns](#)
- [New Hire Reporting](#)

### Other Products Of Interest

- [Payroll Services](#)
- [Tax Services](#)
- [State Unemployment Insurance](#)

### **FLSA**

An important task involves complying with regulations established by the Fair Labor Standards Act (FLSA), also known as the Federal Wage and Hour Law.

FLSA is designed to protect employee rights. Here are a few of the things it covers: the federal minimum wage requirement; definition of "what are wages?"; establishment of regulations on overtime pay and on equal pay for equal work; establishment of laws governing tips and tipped employees.

[Back to top](#)

### **Who are Employees?**

Generally, employees come under two categories — common law and statutory employees.

- **Common Law Employees**  
Anyone who performs services is an employee if you, as the employer, control what will be done and how it will be done. You have the legal right to control the method and result of the services, even when you give the employee freedom of action. Generally, people in business for themselves are not employees, such as doctors, lawyers, and construction contractors.
- **Statutory Employees**  
Someone who works for you and is not an employee under the common law rules for federal withholding.

[Back to top](#)

---

### ***Wages and Other Compensation***

Wages generally include all pay you give an employee for services performed. The pay may be in cash or other forms. It includes salaries, vacation pay, sick pay, commissions, bonuses, and fringe benefits. Wages and other compensation are generally subject to employment taxes.

Many benefits that an employer provides to employees are also subject to employment taxes such as cafeteria plans, pension and annuity plans, dependent care programs, stock options, and achievement awards.

[Back to top](#)

---

### ***Pay Frequencies***

A payroll is prepared at the end of an established pay period. An employer must establish how often the employees are to be paid. This could be anything from a daily frequency to annually. An employer may also elect to pay some of the staff weekly and some people semi-monthly, or with any other combination of pay frequencies.

At the end of each pay period, an employer must gather all information necessary to prepare a payroll for the pay period. This procedure may include (but isn't limited to) totaling each employee's timecard to find the hours worked for the pay period. It may also include other documents the employer establishes for rate changes, address changes, other types of pay, and other factors.

Today an employer has various methods they may use in the actual preparation of payrolls.

[Back to top](#)

---

### ***Employee-Paid Taxes***

Most employers are required to withhold specific employment taxes from an employee's pay, including:

- **Federal Income Tax**  
The IRS provides different withholding methods that an employer can choose from. The amount that an employer withholds is based on the employee's taxable compensation and information that an employee reports on Form W-4, Employee's Withholding Allowance Certificate for marital status, number of allowances, and exemptions.
- **Social Security and Medicare Taxes (FICA)**  
The Federal Insurance Contributions Act (FICA) provides a federal system for old-age, survivors, disability, and hospital insurance. Employees are required to contribute a percentage of their wages to support the financing of this system. These benefits, with the exception of hospital insurance, are supported by the social security tax. The Medicare tax supports the hospital insurance benefit. One amount may be deducted from an employee's pay to cover both portions. Each of these taxes are reported separately.
- **State and Local Income Tax**  
An employer must withhold income tax as specified by each state or locality requirement.
- **State Unemployment Insurance**  
Some states require that an amount be deducted from an employee's pay to cover the costs and benefits of the state's unemployment compensation program.

- **State Disability**  
Some states require an amount to be deducted from an employee's pay to cover the costs and benefits of the state's disability program.

[Back to top](#)

---

### ***Employer-Paid Taxes***

An employer is required to pay the following employment taxes:

- **Social Security and Medicare (FICA)**  
Employers also contribute a segment of the social security and Medicare taxes to be paid to the IRS (the concept of employers simply "matching" employee contributions is a fallacy). A business is liable for the entire tax due, regardless of the amount actually withheld from employees. So, the total liability is calculated, the amount collected from employees is subtracted, and the remaining amount is the employer's portion.
- **Federal Unemployment Insurance**  
The Federal Unemployment Tax Act (FUTA), in conjunction with state unemployment insurance programs, provides payments to workers who lose their jobs. An employer is required to pay a federal unemployment tax as well as a separate state unemployment tax. The federal unemployment tax is strictly an employer paid tax to help finance administrative costs and state programs as needed.
- **State Unemployment Insurance**  
The state unemployment insurance program pays the actual benefits to unemployed workers. An employer is required to pay a state unemployment insurance tax. If the state fund is depleted, the state may borrow from the federal government (hence, FUTA tax).
- **State Disability**  
A few states require that an employer contribute to a state mandated disability program. These contributions are normally paid quarterly with a state return.

[Back to top](#)

---

### ***Payroll Tax Deposits and Returns***

Employers must deposit taxes and file many returns and reports. Payroll reporting requirements are often complex and confusing and employers must be alert to the different rules. The timely deposit of taxes and the accurate and thorough preparation of returns is essential to an employer's compliance procedures. Otherwise, an employer can easily incur a costly penalty.

#### **Tax Deposits**

An employer is responsible for depositing taxes deducted from an employee's pay and employer paid taxes based on deposit schedules.

Federal taxes, which include federal income tax and both the employer and employee social security and Medicare tax amounts, must be deposited into authorized financial institutions or a Federal Reserve Bank.

Federal unemployment and state unemployment taxes (both employer and employee amounts) are typically paid quarterly.

State and local income tax amounts are usually paid directly to the state or local taxing agency. State disability amounts can be paid to the state agency in conjunction with either the state income tax or state unemployment tax, depending on the state's requirements.

## Tax Returns

- *Federal Income Withholding, Social Security and Medicare taxes*  
Employers are required to report these taxes and wages separately on Forms 941 (Employer's Quarterly Federal Tax Return) and Form W-2 (Wage and Tax Statement).
- *Federal Unemployment tax*  
Employers must report FUTA taxes and wages on Form 940 (Employer's Annual Federal Unemployment Tax Return).
- *State Unemployment Insurance Tax*  
Employers are required to report state unemployment taxes and wages on the state-specific form.

[Back to top](#)

---

## New Hire Reporting

Since October 1, 1997, all employers are required to report information about their newly hired and rehired employees to the appropriate state agency within 20 days of the date of hire. (This is per federal regulations. States may establish more stringent reporting requirements.) For business owners, this means more paperwork and time-consuming reports to complete and file with the appropriate state agencies.

The New Hire Reporting regulations were passed as part of the Personal Responsibility and Work Opportunity Reconciliation Act (PRWORA) of 1996 to help enforce child support rulings and reduce welfare payments. States can use the new hire reports to match against child support records to locate parents, establish an order, or enforce existing orders. State agencies will also be able to use the new hire information to find and prevent fraudulent workers' compensation and unemployment claims.

New hire reports must be accurate and legible. They must contain the employee's name, address, social security number, and date of hire. They must also include the name, address, and federal identification number of the employer. (Again, states may request additional information and faster compliance.) To comply, employers may file a Form W-4 or an equivalent form created by the employer. Penalties for non-compliance can be up to \$25 per employee, and up to \$500 per employee in the case of a conspiracy between employer and employee.

New hire reports can be sent by first class mail, by magnetic media, or electronically. Businesses with employees in multiple states may select a single state (in which the employer has employees) to report all new hires. In this case, reporting must be done by magnetic tape or electronically. Failure to transmit the reports within the deadline will result in a penalty, which varies by state.

Paychex handles all the new hire reporting requirements by reporting all your new employees, when they are hired, to the correct agency for a modest fee.

[Back to top](#)