

Paycheck Administration Pitfalls: Steer Clear of these Common Mistakes and Avoid Costly Legal Risks

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What We're Going to Cover

- Employee classification
- Employment related forms
- Paying your employees
- Year end housekeeping
- Expense Reimbursements
- Awards, fringes & miscellaneous comp
- Supplemental withholding



Employee Classification

Most workers are classified as either:

1. An employee of someone else or
2. Self-employed/independent contractor



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Independent Contractors

- Various different tests from different agencies
 - IRS & state department of revenue
 - Equal Employment Opportunity Commission
 - National Labor Relations Board
 - Workers' compensation departments
 - Unemployment departments
- Economic realities test
- Behavioral control
- Financial control



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Basic Independent Contractor Test

- Who provides the tools?
- Does the individual bear the risk & reward for the work?
- Does the individual do the work of your organization?
- Does the individual determine how the work will get done?
- Does the individual determine when the work will get done?



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Common Law Employee Status

Employer becomes responsible for variety of employment related obligations:

- Required to withholding income taxes
- Required to
 - withhold and pay Social Security and Medicare taxes
 - pay unemployment taxes on wages paid to an employer
- Adherence to labor laws, overtime laws, etc.



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A 3rd Category of Workers?

Statutory Employee: The best of both worlds

Worker is treated as an employee by employer
&
Worker gets expense deduction treatment as an independent contractor

How Does It Work?

- Employer treats the worker as an employee by statute for tax withholdings and benefits
 - Employer withholds FICA/medicare & matches as a normal employee
 - Employer not required to withhold income taxes
 - Employee can participate in employer offered benefit plans
 - Employer does NOT have to pay unemployment taxes
- Worker reports employment related expenses on Schedule C
- Worker receives a W-2 that has marked Box 13, Stat Employee

Nice try. It's not open to interpretation.

- Statutory Employee Classification fall into one of 4 categories of job activities as defined in IRS Code Section 3121(d)(3)
- Only those classifications of employees listed in this code section qualify for statutory employee treatment
- Litigation in this area has the Tax Court ruling that the occupations listed were “not merely illustrations but were intended to be exhaustive”



I-9 Particulars

- New form as of January 2017
- Verify the ability of an individual to work in the US
- Download the new form, follow the instructions
- Check forms
- Debate whether to keep copies
- Maintain consistency
- Note: Trump Administration has hinted that they will review I-9 in every investigation, even those not related to immigration status



I-9, W-4 & Legal Ramifications

- Retain important documents
 - W-4 keep for 7 years
 - 1-9 keep for 3 years after separation
 - Hint – I-9s are separate from personnel files
- Based on statute of limitations



Form W-4 Withholding Tax

Form W-4 Employee's Withholding Allowance Certificate

Calculate federal
(& sometimes) state
income tax withholding

Form W-4 Withholding Tax

Pad your files – IRS doesn't want a copy

Old standard: W-4s with > 10 exemptions = send to IRS

New standard: Lock-in letter replaced this requirement

A Love Letter from the IRS

What is a Lock In Letter & why is the IRS sending this?

What is the employer required to do?

- Hard pass on using employee W-4
- Must implement within 60 days of receipt

What happens if the employer ignores the Lock In Letter directive?

- Employer will be liable for paying the additional amount of tax that should have been withheld



How Old Is That W-4?

Does a W-4 ever expire?

- There is no expiration date for W-4s so an original from a prior year is valid

How many times can an employee change their W-4?

- As often as they want – there is no min or max

A thumbnail image of the Form W-4 (2014) tax form, showing the header and the first section with checkboxes for filing status and number of dependents.

Valid W-4

The info a W-4 contains determines if it is valid

A W-4 can only contain:

- Employee demographic information
- Marital status
- Number of exemptions
- & area for *additional* withholding
- Box indicating employee is exempt from withholding



But That's Not Right...

Any alteration renders the W-4 invalid

- Set percentage
- Set dollar amount of withholding
- Crossed out language

An employer *can refuse* to accept a substitute or modified W-4



Because It's None of Your Business

Information you know to be incorrect *does not* make a W-4 invalid:

- Address is not address where you know employee to live
- Exemptions claimed are more than number of children

Employer should accept W-4 & withhold as the W-4 instructs



An Invalid Document

The W-4 is determined to be invalid – now what?

Employer is required to:

1. Use the last known valid W-4 on file
- OR
1. Use single marital status, with 0 exemptions



The States Want Their Say

The Form W-4 is a federal document & most states accept what is reported on the federal form

But *not all states* conform & have their own withholding form



The States Want Their Say

Red = Accepts Fed W-4

Green = Accepts Fed OR State W-4

*CA - 10 or + must be remitted

State	Form	State	Form
AL	A-4	MO	MO W-4
AK	No WH	MT	FED W-4
AZ	A-4	NE	FED W-4
AR	AR4EC	NV	N/A
CA	DE-4*	NJ	NJ W-4
CO	FED W-4	NM	FED W-4
CT	CT-2-4	NY	IT-2014
DE	FED W-4	NC	NC_4
DC	D-4	ND	FED W-4
FL	ND W/H	OH	IT-4
GA	G-4	OK	FED W-4
HI	HW-4	OR	FED W-4
ID	FED W-4	PA	NONE
IL	IL-W4	PR	.499-4.1
IN	WH-4	RI	FED W-4
IA	IA-W-4	SC	FED W-4
KS	K-4	TN	N/A
KY	K-4	TX	N/A
LA	L-4	UT	FED W-4
ME	W-4ME	VT	W-4VT
MD	MW-507	VA	VA-4
MA	M-4	WA	N/A
MI	MI-W4	WV	WV/IT_104
MN	W-4MN	WI	WT-4
MS	89-350	WY	N/A

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What About Chickens?

Paying your employees in other forms of payment does NOT exempt the employer from withholding obligations

- Compensating with property
 - Determine FMV of property or services
 - Needs to be added to W-2
 - Gross up
 - Run concurrent with another payroll that includes cash payment
- Payment of non-cash fringe benefits
 - Taxable or tax free fringes
 - IRS Publication 15-B "Employer's Tax Guide to Fringe Benefits"



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Pay Stubs as a Requirement

The Federal Labor Standards Act (FLSA) sets that standard at the federal level:

Employers are not required to provide pay stubs to employees

But not so fast!

Pay Stubs – The State Level

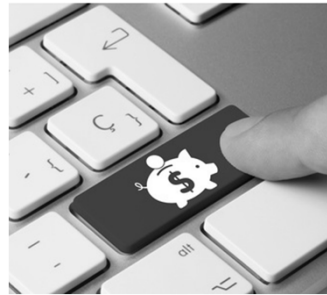
- State law can require employers to provide pay stubs:
 - Minimum amount of information reported on paystub
 - Employee name
 - SSN or some truncated version
 - Pay Rate
 - Pay Period
 - Deductions
- Allowed format of delivery of pay stub
 - Via paper
 - Via electronic method

My Company				Earning Statement			
Name		Address		City		State	
JOHN DOE		12345 Main St.		SEASIDE CITY		CA 94065	
Period		From		To		Total	
Starting Date		Ending Date		Gross Pay		Net Pay	
1/1/98		12/31/98		\$10,000.00		\$7,500.00	
Gross Pay		Deductions		Total		Net Pay	
\$10,000.00		\$2,500.00		\$7,500.00		\$7,500.00	
Gross Pay		Deductions		Total		Net Pay	
\$10,000.00		\$2,500.00		\$7,500.00		\$7,500.00	
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Gross Pay		Deductions		Total		Net Pay	

US DOL has links to every State Labor Office
www.dol.gov/whd/contacts/state_of.htm

Direct Deposit

- Preferred method for many employers & employees
- Concerns with direct deposit
 - Obtaining & storing bank info
 - Incorrect entry
 - Payroll vendors
 - Data security



Cannot Be Mandatory

- The “unbanked” workforce is unfairly positioned
 - Immigrants
 - Poor
 - Illiterate
- Employers are prohibited from using direct deposit as the *sole method* of compensating their employees



Pay Cards

- Pay cards or payroll cards – form of a prepaid card
- Still cheaper & safer than paper checks
- Pay cards are subject to significant regulation to protect the employee
- Federal & state regulations of pay cards make it a requirement that there are multiple access methods free of charge



Pay Cards

- State level requires employees receive full wages each pay period without discount i.e. limitation on fees
- Federal Reserve Regulation E requires disclosure of any fees that may be incurred as a result of using the pay card
- Disclosure requirements are very clear: no one should be surprised about the fees & how to avoid them



Year-End Forms – Who & When

1099s

- Due January 31st

W-2s

- The PATH Act of 2015 moved up the filing date of Employer Copies of information returns to IRS & SSA to January 31st

Thank you, Identity Thieves.

- 1095C – ACA Reporting



Reporting Forms for ACA

Forms 1094-C & 1095-C are used to report to the IRS the information about offers of health coverage & enrollment in health coverage for their employees

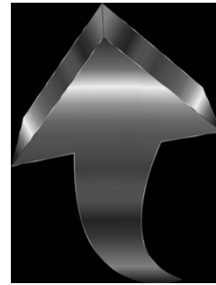
- Form 1094-C
 - *Transmittal of Employer-Provided Health Insurance Offer and Coverage Information Returns*
- Form 1095-C
 - *Employer-Provided Health Insurance Offer and Coverage*



Penalty Provisions

**It used to cost a little,
now it costs a lot!**

The Trade Preferences Extension Act of 2015 included a substantial increase in failure-to-file & late filing penalties for information returns such as Form 1099 & W-2 filed after December 31, 2015, effectively increasing the penalty by a very generous **150%**



Payroll Issues

How do you handle...

- The dead guy
- The guy that stole
- The guy that didn't pick up his paycheck
- The guy that disagrees with his W-2 or 1099



Expense Reimbursements

- Bad business decision
 - Affect on morale
 - Reputation as an employer
 - Sense of fairness employees expect of an employer



Must Employers Reimburse?

- It depends...
- Under certain circumstances
 1. Under the FLSA requirement to meet minimum wage and OT rules of non-exempt employees
 2. Under certain state law – some states *expressly* require employers to reimburse employees for certain expenses
- Expense reimbursements: Discretionary
 - It is a best practice to reimburse all employees for any reasonable business expenses they incur



What is Reimbursable?

- Any ordinary and necessary expense
 - *Bona fide* business use
 - Used in connection with performance of services as an employee
 - Within reasonable limits as set by an employer
 - For example, what type of lodging or transportation is eligible for reimbursement
- Ordinary
 - Considered normal for a taxpayer in a similar trade or business to incur the same expense
- Necessary
 - Need not be *vital*, only need be appropriate or helpful



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What is Reimbursable?

- Examples
 - Tools
 - Equipment
 - Business use of a personally owned vehicle
 - Mobile devices
 - Travel
 - Meals & entertainment
- Some limitations

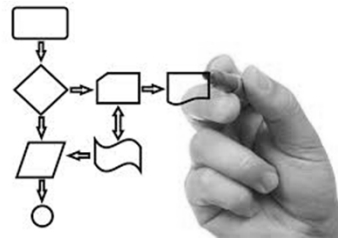


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How To Do It

- Expense reimbursements
 - Payroll
 - Separate expense checks (generally processed via Accounts Payable)
- Per diems
- Allowances



Two Options

- Accountable plan
 - Direct expenses
 - Sets an amount to reimburse
- Not an accountable plan
 - No receipt tracking
 - No reimbursement
 - Taxable income to employee
 - Employees generally not fond of this



Accountable Plan

- IRS definition:

- An accountable plan is any reimbursement or other expense allowance arrangement that meets all of the following requirements:
 - Business connection
 - Substantiation
 - Return of excess amounts



Supplemental Wage Rates

- Any non-periodic payment to an employee outside of regular salary:
 - Commissions
 - Bonus
 - Sick leave
 - Any severance
 - Taxable prizes
 - Retroactive pay increases
 - Taxable fringe benefits
- Increased withholding ensures the employee doesn't spend their bonus before they get a chance to pay their taxes on it



The \$1 Million Dollar Question

- Federal supplemental withholding rates depend upon whether or not the payment is greater than \$1 million
- Supplemental wages of more than \$1 million
 - Withhold tax on the amount OVER \$1m at the highest income tax rate
- Supplemental wages of less than \$1 million
 - It depends



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\$ 1 Million Choice

- If the payment is included in regular wages, withhold as normal
 - If the supplemental wages are identified separately from salary or regular pay,
 - Withhold at 25%
- OR
- Combine regular + supplemental wages and withhold as if it were regular wages



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State Supplemental Wage Rates

- States may vary on their supplemental wage/bonus rate
 - None/No provision
 - Flat rate
 - Combined tax table rate
- Review on state Department of Revenue website – rates may change annually



Takeaways

- Payroll rules are designed to limit surprises to employees
- Clear policies & procedures are critically important
- Don't skimp on training on these issues
- All the agencies involved (IRS, state departments of revenue, Labor) all have their own rules
- Pay is sacred



Questions

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An enthusiastic management-side attorney and SHRM-SCP/SPHR-certified human resources professional, Kate Bischoff advises organizations in a wide range of industries on employment law and employment decisions, from recruitment and workplace culture to terminations. Her strengths include ensuring human resources policies and practices are compliant with federal and state laws, training employees and managers on equal employment opportunity and other supervisory topics, and handling investigations into employee grievances and complaints. Ms. Bischoff is passionate about improving company culture and using technology (social media and big data) in the workplace. Ms. Bischoff also litigates employment cases, including discrimination, harassment, wage and hour, and contract matters. After several employment law trials, she speaks from experience when advising clients when administrative and court matters commence. Prior to founding tHRive Law & Consulting, Ms. Bischoff worked as an attorney at Zelle LLP and served as a human resources officer for the United States Department of State at the U.S. Embassy Lusaka, Zambia and for the U.S. Consulate General Jerusalem.



Elizabeth Bystrom

Elizabeth Bystrom CPA, Ltd. is a small business built on relationships. Ms. Bystrom's technical specialties include small business consulting and individual income tax. Before building her own business, Ms. Bystrom worked for some of the brightest minds available at Redpath & Co. During her ten years with Redpath & Co, she worked in widely various departments, including: compilation and review, sales tax and payroll tax compliance, payroll research, and management of bookkeeping and accounting staff. Working in the corporate tax department brought Ms. Bystrom to both accounting consulting with

corporate tax clients, as well as corporate income tax. Her final five years with Redpath & Co. were spent in the individual income tax department, working closely experienced tax partners.

Ms. Bystrom built her own business to enable her to achieve a work/life balance that suited her family. She is licensed as a Certified Public Accountant in the state of Minnesota, and spokesperson for the MNCPA.