



**EmPower HR**

# **A Guide To Employer Payroll Taxes**



## Oh Taxes, The Necessary Evil

Payroll taxes can be a pain to understand and wrap your head around. And as employees, we always cry a little inside when we see the amount they deduct from our final paychecks.

But as employers, we often scratch our heads and ask,

- ▶ What are these amounts for?
- ▶ Who decided these percentages?
- ▶ Why is it so much?

Although we may have mixed feelings about them, they do serve a purpose.

Our handy guide will help you navigate this foreign land a little better by walking you through common types of employer payroll taxes.

# Let's Start From The Top

Payroll taxes are taken out of an employee's paycheck every time payroll is run, including federal, state and local taxes.

Here is a high-level view of the taxes taken out:

- ▶ **Withholding taxes:** the employer withholds a percentage of the employee's income for federal, state and local income taxes.
- ▶ **Employer taxes:** are payroll taxes that are paid by the employer only. However, some payroll taxes, like Medicare and social security, are shared taxes and split between the employer and employee.

Although we may have mixed feelings about them, they do serve a purpose.

Special note: Employers are responsible for payroll taxes for their employees; however, that is not the case for contractors. Contractors will need to be responsible for taking out their own withholding taxes to ensure they do not owe come tax season.

Most of us are aware of the more obvious business income taxes, as they're more readily talked about and 'in your face.'

But payroll taxes seem to be catching more business owners by surprise and can often go overlooked or unnoted.

It's beneficial to note that payroll taxes are pretty complex and leave absolutely no room for mistakes.

Over the years, there have been various instances where entrepreneurs faced extreme consequences because they failed to strategize and stay organized with their payroll taxes during the year.

While it seems more convenient to procrastinate, there's a high likelihood of running into serious problems down the line.

Instead, consider enrolling the services of payroll professionals to take this administrative burden away and ensure it is well handled.

Did you know that businesses pay more in payroll taxes than income taxes, according to the

**\$2 trillion +**

was collected in payroll taxes in 2017 representing about

**70%**

of all federal revenue.

The penalties incurred every year by businesses are so great they could fund defense equipment!

Small businesses are actually the greatest offenders when it comes to noncompliance in taxes.

# Collecting And Reporting Payroll Taxes

On withholding or remitting a payroll tax amount, the employer must ensure the funds are paid:

To the appropriate tax authority:

- On the federal level, payroll taxes are remitted to the Internal Revenue Service (IRS).
- On the state level, the appropriate tax authority is the department of revenue for income taxes and the department of labor for unemployment taxes.
- For local taxes, the relevant authorities will depend on the type of tax.

- ▶ Payments to tax authorities work with a schedule that is typically set by the size of your company and the amount of tax you pay.

You get your own payment schedule when you register your business with the IRS. If there's any change, you should receive a notification.

- ▶ It's also on the employer to file regular reports of the payroll tax amounts collected from payroll and paid to the IRS, state and local tax authorities.
- ▶ Employers need to report income tax, Medicare, social security and tips quarterly on a federal level basis using Form 941.

- ▶ The Federal Unemployment Tax Act (FUTA) needs to be reported annually using Form 940.

- ▶ Speaking of the state level, wage detail reports are used to report payroll taxes, and the requirements are based on the state.

- ▶ Local tax agencies handle local reporting.

- ▶ W-2s must be provided to employees and the appropriate tax agencies at the end of the year. The deadline is 31st January of the following year.

# How Are Payroll Tax Rates Regulated?

There are different factors involved in calculating and deciding the rates for payroll taxes. Here's how it works:

- ▶ Every year, the IRS has the duty of updating Publication 15 (Circular E). This document holds the most current withholding tables and tax rates for federal income tax, Medicare, social security and federal unemployment tax act.
  - ▶ In some states, you will find transportation taxes as well as school board taxes.
  - ▶ It's important to note these taxes early on in addition to understanding how they affect payroll and the business.
  - ▶ You should get a statement when you register your company with the IRS and other tax authorities. You will also be informed about which rates apply to your company as well as which payment and reporting schedules apply to you.
  - ▶ It's normal and absolutely fine to be unsure, and when you are, the appropriate tax authorities are reachable by phone. In addition, you can liaise with a professional bookkeeper, accountant, or payroll professional to get the correct information.
- ▶ The lawmakers work together with the IRS, Social Security Administration and Department of Labor to set the rates.
- In the company, employees' gross wages, bonuses and W-4 determine what is withheld for federal income tax.
- In regards to Medicare, the employer contributes 1.45% for 2.9% in total. The same applies to the employee.
- For employees earning more than \$200,000, there's an additional 0.9% for them to pay in overall taxes given their earnings.
- There's no cap to the maximum amount for employees' additional payments. Employers are also not responsible for any of their contributions.
- For example, if an employee ends up earning more and their contributions don't increase that period, it can increase the next period by how much more their gross pay is.
- Regarding social security, both the employer and employee contribute 6.2% each for a total of 12.4%. In this case, the maximum cap for taxable earnings is updated annually.

With FUTA, 6.0% is set with a \$7000 maximum taxable earning.

The individual states determine the state income tax and SUTA rates.

It's a different ball game with local taxes, as each tax is peculiar to each locality.

In some states, you will find transportation taxes as well as school board taxes.

**Now, if an employer speeds it up and pays the SUTA tax promptly, they get 'rewarded' with a deduction of up to 5.4%, reducing the rate to 0.6%.**

## Common Payroll Tax Areas Worth Noting

- ▶ Payroll taxes affect take-home pay in the sense that the amount on an employee's paycheck before taxes is the gross pay. The amount after payroll taxes and other deductions, like payroll taxes, is the net pay and, in theory, the take-home pay.
- ▶ Bonus wages are not left out, including bonuses, commissions, overtime pay, back pay, and accumulated sick pay. Bonus wages are subject to income taxes at a federal, state, and local level sometimes.  
  
As an employer, you must not forget to withhold the appropriate amounts for these types of incomes coupled with the withholding amounts for standard wages.
- ▶ The frequency of salary payment has a direct effect on your payroll taxes. So, if you run your payroll more frequently, you'll just need to calculate your taxes more often.
- ▶ You'll need to invest in good payroll software to automatically calculate, deduct, pay and report your payroll taxes. This will save time, limit errors, and create room for strategizing on growing the business.
- ▶ You can learn more about payroll taxes from a bookkeeper, an accountant, IRS publication, or payroll specialist.



Mistakes happen every now and then. In fact, they're pretty commonplace. Mistakes can be classified as minor or major. In the case of a little mistake, they are usually administrative in nature and don't intend to deceive. That being said, they're easier to correct.

### Minor Tax Mistakes:

- ▶ Incorrect or temporary employer identification numbers which are usually typos or used in states that require a permanent ID number.
- ▶ The wrong payroll tax payment schedule during setup or just failing to update new information in the payroll software.
- ▶ Not posting payment correctly or posting to the wrong business ID.

### Major Tax Mistakes:

- ▶ They are frequently paying or filing late, which ultimately leads to fines.
- ▶ Frequent mistakes, including any form of underreporting or using the wrong tax tables.
- ▶ Misclassifying employees which makes you liable for all back taxes.
- ▶ Failure to remit payroll taxes to the tax authorities which is against the law. In mild cases, the business will get a heavy fine, and in nasty instances, it can be sentenced or permanently closed.
- ▶ Avoiding payroll taxes all together which is never a good option.

Unfortunately, the government doesn't hold back when it comes to teaching tax offenders a lesson. You can get in big trouble and the consequences start to multiply rapidly.

## Tax Mistake Consequences

Falling behind on reporting comes with its own baggage too. The fine is a minimum of 5% and a maximum of 25%.

If you try to play a fast one by dismissing your fines, you can add another 0.5% per month and another 1% after your notice. This can increase to as much as 25%.

As if this is not enough, the fines are subject to quarterly interest ranging from 3-6%, take-home pay in theory, which creep in pretty quickly and require you to keep paying until you've paid the full amount.

## There's Help Out There

As an employer, seeing all these numbers can make your head spin...and for a good reason.

Ensuring you're making the correct payroll deductions is paramount to properly running your business.

You want to make sure that you and the government are in good standing at the end of the year.

Knowing the basics is key but understanding how to build these into your business strategy is of the utmost importance.

**“Enlisting the service of payroll experts such as those at EmPower HR can help you make sure nothing slips through the cracks.”**

Lateness in paying payroll taxes to the IRS leads to the following fines:

5 days or less warrants  
2% of what is owed.

Over 5 days to a maximum of 15 days warrants 5% of the amount owed.

After 16 days, you'll need to pay 10% of the amount you owe.

More than 16 days, you receive your first notice (showing you've really crossed the line). You'll need 15% of the amount owed, unsurprisingly.

# Payroll Year End Checklist

Before your last payroll of the calendar year, make sure to do the following:

## 1. Check Employee And Employer Data

- Verify the employer and employee data that is used in processing your quarterly tax reports and W-2s.
- To which employees does the “retirement plan” indicator in Box 13 of Form W-2 apply.
- Confirm that employee names and Social Security numbers are in the correct format.
- The IRS may impose a penalty for each Form W-2 with a missing or incorrect Social Security number or employee name.
- Ensure that deceased employees are correctly coded.

## 2. Check Wage, Tax And Benefits Data

- Confirm that the deferred compensation plan type is correct and verify employee contribution data amounts.
- Verify that withholding has been made accurately or withhold from the final paycheck for taxable fringe benefits.

These may include:

- Group-term life insurance above \$50,000
- Third-party sick pay (is the third party issuing a W-2?)
- Personal use of company vehicle
- Non-qualified moving expense reimbursements
- Company-provided transportation or parking
- Employer-paid education is related to the employee’s job
- Non-accountable business expense reimbursements or allowances
- Bonuses
- Non-cash payments

# Payroll Year End Checklist Continued...

- Check that Group-Term Life Insurance adjustments have been updated and submitted.
- Ensure that other special tax items have been updated and submitted, such as Other Compensation, Third-Party Sick Pay, Employee Business Expense Reimbursements, Taxable Fringe Benefits, Tip Allocation information, and Dependent Care Benefits.
- Verify the employer state unemployment insurance tax rate and taxable wage limit for each state to avoid errors.
- Compute uncollected Social Security and Medicare taxes for retirees and former employees for their paperwork.

## 3. Check For Special Procedures

- Schedule any special bonus payrolls.
- Request any special reports.
- Determine whether all adjustments are applied or that an adjustment payroll has been scheduled.
- Remind employees to fill out a new Form W-4 if their situation has changed.
- Obtain new Forms W-5 for Advance Earned Income Credit (EIC) for the new year.
- Confirm that all checks written during the year have been accounted for and updated in the system.
- Determine that all voided or reversed paychecks have been accounted for in the system.



## How EmPower HR Can Help?

EmPower HR offers a variety of human resource services tailored to your business needs. Let us handle the HR administrative tasks so you can focus on your business and employees.

**Learn more at [empowerhr.com](https://empowerhr.com)**

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