The Small Business
BEGINNER'S GUIDE TO PAYROLL

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When you think about **why you got into business** …

… a lot of reasons might come to mind: a great product or service concept, the ability to **be your own boss**, flexibility to **set your own work-life balance** (whether or not this became a reality is another question), a desire to support and contribute to the local economy … the list can go on and on. **What likely doesn't come to mind is payroll**.

While payroll might not have been a prominent consideration when you conceived your business, it has likely moved up the list of things you need to worry about as your small business becomes a reality. The truth is that payroll can take up a lot of time, can cause a lot of headaches, and, if not properly handled, can put your business at real risk of jeopardizing employee trust and financial stability. But that doesn't have to be the case.

SurePayroll's Small Business Beginner's Guide to Payroll will cover the basics that you need to know as you prepare to run your first payroll and/or bring on new employees.

This guide will serve as a starting point to help you get your payroll going, to set it up right from the start, and best avoid hiccups in the future. **We'll cover: the information you need to run a payroll, employee classifications, how to calculate FICA tax deductions, and common payroll missteps to avoid**. At the end of the guide you will find links to key resources, as well as a worksheet that you can use to get started and keep track of critical details.

"The truth is that payroll can take up a lot of time and cause a lot of headaches."

A note on **payroll taxes**

Payroll taxes consist of local, state, and federal taxes withheld from an employee's paycheck. The IRS provides an overview of employment taxes on its website, making note of:

- Federal Income Tax

- Social Security and Medicare Taxes

- Additional Medicare Tax

- Federal Unemployment Tax

Once you fully understand which taxes to withhold, as well as the rate associated with each one, you're in position to move forward. It's important to note that rates and requirements can differ from employee to employee, based on where they are located—an important detail if your small business uses a remote workforce, for example.

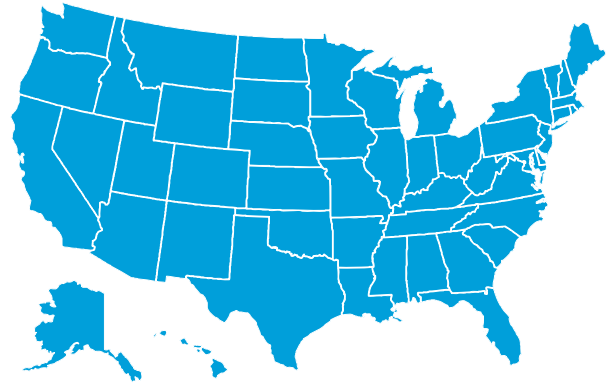*"rates and requirements can differ from employee to employee, based on where they are located."*

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What you need to **run a payroll**

There are several different ways to approach running payroll, whether you do it yourself, use an accountant, leverage an online payroll service, or invest in a payroll software. Regardless of the approach, in order to get your payroll set up and ready to run, there are certain pieces of information you'll need.

✓ **Employer Identification Number (EIN) and State Tax ID**

Much like you'll need to collect information from each of your employees (more to come on this shortly), you need to be prepared with identification information for your business. A business needs a unique identifier. For the purposes of federal filings, each business is required to have an Employer Identification Number (EIN) in order to process payroll and submit payroll taxes.

The IRS makes it simple to apply for an EIN online.

For some states, an EIN is all you'll need to file federal, state, and local taxes. For others, **you may also need a State Tax ID for your business**. To determine if you will need a State Tax ID as well, visit your state tax website.

✓ Employer Information

Request that each employee complete Form W-4. With this in hand, you can calculate how much federal income tax to withhold from your employee's paychecks. This documents the employee's allowances, as well as their filing status. Employees should also complete appropriate state withholding forms.

DID YOU KNOW?

Employment Eligibility: Your employees must also fill out section 1 of Form I-9 by their first day of work, Employment Eligibility Verification. Within three days of the employee's first day of work, the employer must review the employee's documentation of identity and work authorization and complete section 2 of Form I-9. This form must be retained for the longer of three years from hire or one year from termination. Employers must also comply with E-Verify requirements where applicable.

Employers are required to comply with federal and state new hire reporting requirements and must report newly hired employees within 20 calendar days of the date of hire. For each newly hired employee, the employer must provide the following to the state new hire directory (specific states may request additional information):

Employee: name, address, SSN, date employment began.
Employer: name, address, and EIN.

If you are outsourcing your payroll to an accountant, online payroll service, or using a software, ask if they handle new hire reporting for you, or if you will be responsible for completing this yourself.

✓ ## Create Your Payroll Schedule

Payroll frequency determines how often you will run payroll, and subsequently how often your employees will be paid. General frequencies include weekly, bi-weekly, semi-monthly, and monthly. Note that pay frequency is often dependent on state law and/or industry requirements so you will want to make sure that your schedule is compliant with all applicable regulations for your business.

 DID YOU KNOW?

To provide clarity and manage your employees' expectations, we suggest creating a physical payroll calendar that you can share with them. We've rounded up some best practices for doing so here.

✓ ## Calculate and Withhold Taxes

This is when the payroll process really begins. With each paycheck, it's your responsibility to calculate and withhold the correct amount of taxes. Ensuring that your calculations are correct, and that employees understand how to read their paystubs, may go a long way toward gaining and maintaining employee trust.

In the next section, we will cover employee classifications and how to distinguish between exempt and non-exempt employees.

A bit later in this guide, we'll get into FICA calculations and deductions.

Quick link: Jump to FICA Tax Deductions

✓ Pay Taxes

There are due dates for each type of tax, so make sure you mark these on your calendar. Missing a due date can result in penalties and/or interest, not to mention lost time.

If you are outsourcing payroll, whether to an accountant, an online payroll service, or using a payroll software, you should inquire about their tax filing process and if they provide any sort of guarantee or remediation in the case of errors.

Now that you're armed with the information you'll need to get started with payroll, let's cover employee classifications and the difference between exempt and non-exempt employees.

Employee **classifications**

Whether it's hiring your first employee, or adding to your team, **bringing a new hire onboard is a big step**. As a small business, each new employee is not only a testament to the success and potential of your business, but a significant investment of time and financial resources.

There are important considerations to think through before you even get to the recruiting and interviewing stages, not the least of which is determining which employee classification type the role will be: **exempt** or **non-exempt**.

From a payroll perspective, you'll need to understand both types of employee classifications. Let's examine some of the characteristics of each.

✓ What It Means to Be an Exempt Employee

- At the federal level, overtime eligibility is determined by regulations which are part of the Fair Labor Standards Act (FLSA). **"Exempt" employees are those deemed exempt from some or all of the FLSA provisions, including requirements for minimum wage and overtime pay.**

📢 DID YOU KNOW?

It's important to note that the exemptions from overtime requirements under the FLSA are based on the specific job duties as well as the basis of pay for the position.

- The broadest category of exempt employees falls under "white-collar exemptions" for administrative, executive, and professional employees, certain computer professionals, and outside sales employees.

- Exempt employees are generally paid on a salary basis; that is, they receive the same amount of pay each pay period regardless of the quality or quantity of work performed. They are not eligible to receive overtime pay for hours worked over 40 in a workweek.

✓ What It Means to Be a Non-Exempt Employee

- Non-exempt employees must be paid minimum wage for all hours worked as well as overtime pay at a rate of one and one-half times their regular rate of pay for those hours worked over 40 in a workweek.

- Different states and localities may have stricter policies relating to the calculation and payment of overtime pay.

- **Under the FLSA, employees need only pay non-exempt employees for time worked**. For example, employers are not required to provide a different pay rate for holidays and are not required to pay non-exempt employees who do not work a holiday—unless there is an applicable state/local law or employment contract dictating a different rate of pay or paid holiday policy.

- Non-exempt employee classifications do often mean more work for you as the business owner and the person managing payroll. Why? Because you'll need to be tracking the hours worked by your non-exempt employees, and potentially calculate multiple pay rates per employee for a given pay period.

If you are using payroll services, such as a bookkeeper, accountant, or online payroll provider, you'll want to make sure that they can support the payroll requirements of your business. For non-exempt employees, for example, you will want to ask about timesheet software integrations, and multiple pay rate support.

Now that we're clear on exempt and non-exempt employees, let's touch on some of the most common payroll deductions you'll face, those associated with the Federal Insurance Contributions Act (FICA).

Calculating **FICA tax deductions**

As you prepare to process payroll, it's key that you understand the taxes associated with the Federal Insurance Contributions Act (FICA). These include:

- Social Security tax

- Medicare tax

DID YOU KNOW?

Current Rates

The current tax rate for the Social Security portion is 12.4 percent; while the rate for Medicare is significantly lower at 2.9 percent. The contribution for each is split between the employer and employee; for Social Security, this works out to 6.2 percent each, and for Medicare 1.45 percent each.

There is a wage base limit imposed on the Social Security tax. For 2017, the base is $127,200. This is the maximum wage subject to Social Security tax for the year.

Also, additional Medicare tax may apply if an employee earns in excess of the threshold amount for that tax year. Employers must withhold an additional 0.9 percent on any wages paid in excess of $200,000.

So how do you calculate **FICA deductions?**

Here's the information you will need:

- The gross pay for each employee for the pay period

- The year-to-date gross pay for each employee

- The Social Security and Medicare withholding rates (see above)

- The amount of money deducted from an employee's paycheck for tax exempt benefits

Once you calculate FICA taxes for each employee, don't forget to set aside the same amount for your portion of the taxes.

"The contribution for each is split between the employer and employee."

Did you **deduct too much?**

It's easy to make a mistake when calculating FICA taxes. In the event that you deduct too much from an employee's paycheck, you may have to do one or all of the following:

- Refund the over withheld taxes to the employee

- File a new Form 941.

- You'll want to be sure to correct FICA withholding going forward, but also maintain the previous inaccurate record as a matter of data integrity.

Now that we've covered the basics of how to process payroll for your small business, let's discuss some common mistakes to avoid.

Payroll don'ts and how to avoid them

With everything else that goes into running a small business, it can be a challenge to focus the appropriate time, energy, and resources on the payroll process.

The bad news: even a small mistake can have major ripple effects.

The good news: most of the common small business payroll pitfalls can be avoided.

When it comes to payroll missteps, **common problems can be divided between setup and maintenance**.

Upfront Mistakes

Proper setup can be the difference between payroll success and failure. For this reason, it's imperative that you know exactly what's required of you, from a compliance perspective.

However, with so many regulations and nuances to understand and keep track of, it's easy to make a mistake. For example, you might forget to register your business for federal, state, and/or local tax withholdings. Or, it's possible that you misclassify employees, which is a red flag for the IRS or the Department of Labor.

DID YOU KNOW?

If you are looking to outsource payroll to a bookkeeper, accountant, or online payroll provider, you will want to ask how they stay up to date—and share updates with you, and whether they offer guarantees or protections when it comes to payroll, payroll tax compliance and audits.

SOLUTION: familiarize yourself with all the rules, regulations, and laws associated with payroll. Also, don't forget to stay current with any changes that could impact your company and/or your employees.

❌ Falling Behind

Just as important as setting things up right is setting up a payroll process that keeps you on top of deadlines, filings, and requirements on a continuous basis. As noted previously, small business owners are always pressed for time. Subsequently, it's easy to put payroll on the backburner as you focus on other areas of your business.

If you don't prioritize payroll, you will trigger an avalanche of problems, not least of which is that employees and the Department of Labor will not react well to missed pay days.

Also, if you don't pay your taxes on time, you could be subject to penalties on the federal, state, and local levels.

SOLUTION: create a payroll calendar to ensure that you never overlook a pay period or important tax related date. This can also be shared with employees so that everyone is aware of pay dates and any changes to standard schedules.

Is DIY payroll **right for you?**

Although it's always an option to do your own payroll, as our guide indicates, there is more to this than meets the eye.

Are you up to the task of collecting all the necessary information from your employees? Are you okay with the idea that it will take several hours each pay period to organize your payroll and issue paychecks? Are you familiar with the many taxes you're required to pay and withhold?

While this list of considerations can seem overwhelming, there are websites, agencies, and vendors that can help.

You didn't get into business to run payroll, **don't let payroll be the reason you go out of business**.

At the end of this guide we've rounded up some small business payroll resources, as well as a handy worksheet for recording key payroll details.

Small business **payroll resources**

▶ **IRS Small Business Resources**
https://www.irs.gov/businesses/small-businesses-self-employed
https://www.irs.gov/businesses/small-businesses-self-employed/understanding-employment-taxes

▶ **To apply for an EIN:**
https://www.irs.gov/businesses/small-businesses-self-employed/apply-for-an-employer-identification-number-ein-online

▶ **Key Forms**
https://www.irs.gov/uac/about-form-w4
https://www.uscis.gov/i-9
https://www.irs.gov/pub/irs-pdf/f941.pdf

▶ **For current FICA rates:**
https://www.irs.gov/taxtopics/tc751.html

▶ **Tips on creating a payroll schedule:**
https://www.surepayroll.com/resources/blog/the-payroll-schedule-how-to-create-one

▶ **Considerations for DIY Payroll:**
https://www.surepayroll.com/payroll/compare/diy-payroll

▶ **How to Run Payroll Checklist:**
https://www.surepayroll.com/docs/default-source/Blog-Guides/how-do-i-run-payroll-checklist.pdf?sfvrsn=6

Don't want the hassle of running payroll on your own?
Call **SurePayroll** to learn about your options:

800-900-0781

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