



# 10 Common Payroll Mistakes You Don't Want To Make

## Introduction

Running payroll can be time consuming. There are lots of steps, like reporting a new employee, calculating employee pay, and issuing Form W-2 at the end of the year. But the payroll process is not something you should rush through. Mistakes and skipped steps can come with penalties.

Here are 10 common payroll mistakes to watch out for. Each section includes why you should avoid the mistake, how to avoid it, and what to do if you've made the mistake.

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## Failing to Verify and Report New Employees

**You must verify the identity and legal work status of employees, have proper tax filing info, and follow new hire reporting laws.**

Possible consequences include incomplete or erroneous payroll records, fines, and increased scrutiny of your business. Get organized before your new employee starts, and follow laws in a timely manner.

### 1. Verify Name and Social Security Number

Record the employee's name and Social Security number (SSN) for Form W-2 reporting. See their card or use the Social Security Administration's Verification Service to verify the number.

### 2. Give New Employees Form W-4

Employees should complete Form W-4, which asks for SSN, contact info, and filing status. Keep the W-4 on file. It remains in effect until an employee completes a new one. Tax exempt employees must complete a new Form W-4 annually.

### 3. Follow New Hire Reporting Laws

New Hire Reporting laws ensure enforcement of child support orders. Each state has its own New Hire Reporting Center.

### 4. Complete Form I-9 and E-Verify

Within three days of starting, use Form I-9 to verify an employee's eligibility to work in the U.S.

- ✓ Have the employee complete Part 1 of Form I-9, Employment Eligibility Verification.
- ✓ Ask to see documents proving identity and work eligibility. Complete Section 2, stating the documents appear to be authentic.
- ✓ Use E-Verify to verify the employee's information on the Form I-9 (optional in most states).



## HELP! I'VE MADE THIS MISTAKE

If you fail to report or verify a new employee on time, you could face monetary and criminal penalties. File all forms and report your new employee as soon as possible. For state reporting, check with your state to see if there are additional steps to complete.



## Classifying Workers Improperly

**Misclassifying a worker as a contractor instead of an employee can be a costly mistake. If you are unsure whether a worker is a contractor or employee, you can file Form SS-8 to request an IRS determination of your worker's status.**

Many people classified as contractors should actually be classified as employees. This misclassification affects tax revenues. When you classify someone as a contractor, you don't deduct taxes from their wages or pay employer taxes. Governments miss out on valuable tax dollars.

Contractors don't benefit from FLSA rules on minimum wage and overtime pay. Misclassified workers might miss out on wages for their work.

If the IRS or U.S. Department of Labor (DOL) determines that you misclassified a worker, you will have to pay the employee and employer taxes, back wages, penalties, and interest. A misclassification audit can devastate a small business.

The DOL recommends using a six-part economic realities test to determine if someone is a contractor or an employee:

### 1. Is the work an integral part of the employer's business?

If the worker provides services that the company also provides, the worker is most likely an employee.

### 2. Does the worker's managerial skill affect the worker's opportunity for profit or loss?

If a worker can only increase profits by working overtime, the worker is probably an employee.

### 3. How does the worker's relative investment compare to the employer's investment?

If the worker relies on the employer for any special business skills, judgement or initiative, the worker might be an employee.

### 4. Does the work performed require special skill and initiative?

If the worker relies on the employer for any special business skills, judgement or initiative, the worker might be an employee.

### 5. Is the relationship between the worker and the employer permanent or indefinite?

If someone works long term or repeatedly for an employer, the worker might be an employee.

### 6. What is the nature and degree of the employer's control?

If the worker does not have significant control over meaningful aspects of the job, the worker is most likely an employee.



## HELP! I'VE MADE THIS MISTAKE

An IRS program allows employers to pay an amount equal to about 10% of their payroll tax liability for the past year—provided they properly classify workers going forward.



### Not Issuing Form W-2

**You paid your employees and withheld taxes throughout the year. That's all you had to do, right? Wrong.**

Send all your employees a Form W-2 after the year ends. They will use this to file their individual tax forms. You must also send a Form W-2 to the Social Security Administration (SSA) for each of your employees.

You must file a Form W-2 for all your employees, even if they were seasonal or quit after one day. Information needed on a Form W-2 includes:

- ✓ Employee Social Security number (SSN)
- ✓ Your employer identification number
- ✓ Your business name and address
- ✓ Employee's name and address
- ✓ Total compensation (including tips, bonuses, commissions, etc.)
- ✓ Total taxes withheld from the employee's wages

You can order Form W-2 on the **IRS website** or by calling 1-800-TAX-FORM. You cannot download and use a Form W-2 from the internet.

You must send a Form W-2 to each of your employees by January 31. You must also mail or electronically file the forms with the SSA and state governments by January 31. Form W-3 should accompany the forms you send to federal and state governments.



### HELP! I'VE MADE THIS MISTAKE

If you did not send out Form W-2 when you should have, do it as soon as possible. You can receive a penalty for each unsent form, and the penalties increase the longer you wait.



### Improperly Classifying Exempt Workers

**Exempt employees do not receive compensation for overtime hours; however, nonexempt employees do.**

If you misclassify an employee as exempt, they could potentially miss out on a lot of compensation and you could owe them back wages.

Just because you pay an employee a salary or you give them a certain job title, they are not automatically classified as exempt. An employee is exempt if they meet all three of the following Fair Labor Standards Act (FLSA) rules:

- ✓ they are paid on a salary basis,
- ✓ they make a minimum of \$23,600 per year (\$455 per week),
- ✓ and they have job duties that include great responsibilities that directly affect the company's operations.

For more specifics on classifying an employee as exempt vs. nonexempt, see the [\*\*FLSA guidelines\*\*](#).



### HELP! I'VE MADE THIS MISTAKE

If you discover that you misclassified an employee as exempt, reclassify them as nonexempt and begin paying them overtime wages. Also, pay the employee any back wages for overtime hours in the past that were not compensated. If the employee sues you, you may have to pay interest, damages, and other penalties.



# Miscalculating Overtime Wages

**Overtime is not as simple as time-and-a-half after forty hours.**

If you are not aware of all the overtime laws, your employees might get short-changed.

The basic Fair Standards Labor Act (FLSA) **rules** say employers must generally pay employees 1.5 times their regular rate of pay for any time worked beyond 40 hours in a workweek.

Some states also have their own overtime laws. You must follow whichever laws are more generous—either the federal or the state laws. Some states require overtime pay after only 8 or 12 hours in a workday. Doubletime may also be applicable in some situations. Make sure you're in compliance with your state's **minimum wage and overtime laws**.

Other things to consider:

- ✓ When calculating overtime, you must include wage augments, such as shift differentials.
- ✓ If your employees are paid biweekly, semimonthly, or monthly, you must still pay them overtime for time worked in excess of 40 hours for each workweek.
- ✓ Offering compensatory time off instead of paying overtime wages is almost always illegal.
- ✓ Neither the employer nor the employee can waive overtime pay.

For more specifics on classifying an employee as exempt vs. nonexempt, see the **FLSA guidelines**.



## HELP! I'VE MADE THIS MISTAKE

If you discover that you owe an employee compensation for overtime hours, pay them their owed back wages. As with misclassifying an employee as exempt, the employee can sue you, resulting in interest, damages, and penalties on top of the back wages.



## Not Applying for Payroll Tax

Before you hire your first employee, sign up for all tax accounts that apply to your company.

Failing to set up proper payroll tax accounts can mean fines, government audits, and paperwork nightmares.

Apply for all applicable tax account numbers as soon as possible. Here are the most common account numbers you will need:

- ✓ **Federal Employer Identification Number (EIN)**  
Use your EIN number for federal taxes, including federal unemployment (FUTA).  
**Apply online** or call the IRS at 1-800-829-4933.
- ✓ **State Income Tax**  
Apply for an income tax withholding account for your state.
- ✓ **State Unemployment (SUTA)**  
Apply for a SUTA account with your state.
- ✓ **Local income tax and school district tax**  
Some states have local income tax and other special taxes. If you withhold local tax as a courtesy, apply for account numbers in the employee's city of residence. For multiple worksites, be sure to apply for withholding accounts in those cities.

For more specifics on classifying an employee as exempt vs. nonexempt, see the **FLSA guidelines**.



## HELP! I'VE MADE THIS MISTAKE

Contact the agencies immediately to apply for withholding accounts and get up to date with your tax filing and payments.



# Paying the Wrong Tax Rates

**Tax rates can change. Make sure you're using the right rates for your company.**

Use the wrong tax rate, and you may pay more in the long run with penalties and interest piling up.

Do the following to keep current with federal, state, and local tax rates:

- ✓ **Choose a payroll processing method**, like G&D Integrated's online payroll software, that automatically updates universal rate changes and tax tables.
- ✓ **Watch the mail for business specific rate changes**. For example, your state should annually notify you of your business's state unemployment tax rate.



## HELP! I'VE MADE THIS MISTAKE

When you realize you've paid a wrong tax rate, contact the tax agency immediately, and they can tell you how to proceed.



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# Missing Employment Tax Deadlines

It's easy to get so busy with your business that you don't realize you've missed a tax deadline. Tax agencies don't mail forms anymore. And, most federal tax payments are now due through the **Electronic Federal Tax Payment Service (EFTPS)**, which must be initiated several days ahead of the due date.

Missing employment tax deadlines can quickly land employers in hot water. Missed or late tax payments can result in hefty late charges, penalties, or legal trouble.

Apply for all applicable tax account numbers as soon as possible. Here are the most common account numbers you will need:

- ✓ **Federal Employer Identification Number (EIN).** The IRS has a tool called Calendar Connector to help you remember federal tax deadlines.
- ✓ **Register for EFTPS** when you start your business at [www.eftps.gov](http://www.eftps.gov).
- ✓ **Initiate your tax payments through EFTPS** well ahead of the due date.
- ✓ **Indicate the proper tax period** when paying taxes. If you select the wrong tax period, the government may apply your payment to the wrong quarter.
- ✓ **Double-check mailing addresses** for tax payments, and opt for a return receipt so you know your payment has safely arrived.
- ✓ **Consider using a payroll tax filing service** so you don't have to worry about deadlines.

For more specifics on classifying an employee as exempt vs. nonexempt, see the **FLSA guidelines**.



## HELP! I'VE MADE THIS MISTAKE

If you miss a payment, contact the tax agency. Sooner is better. Late charges can pile up quickly.



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### Not Running Payroll on Time

You should consistently run your payroll, whether it is weekly, biweekly, semimonthly, or monthly.

Your employees rely on knowing when their wages will be available to them. They have bills to pay too. If you fail to run your payroll on time, you may lose your staff's trust. Also, most states have **pay frequency requirements**.

Set a schedule for yourself. Decide how frequently you will pay your employees. From there, figure out which day you will pay your employees and how soon before that you need to run your payroll. If you give your employees written or printed checks, you may be able to run payroll and pay your employees on the same day. If you pay your employees with direct deposit, you may need to run your payroll a few days ahead of when your employees should receive their pay.



### HELP! I'VE MADE THIS MISTAKE

If you do not run your payroll on time, run it as soon as possible; your employees are waiting on their money. Be transparent with your employees and explain to them that their pay will be late. Try to avoid combining pay periods as this can complicate taxes and withholdings.



# Using an Inefficient Payroll Process

**Payroll errors are all too easy to make—especially if you figure payroll by hand or use outdated software.**

- ✓ Changing laws, tax tables, and filing requirements are complicated and confusing.
- ✓ Payroll is time consuming, whether you have two employees or 50.
- ✓ Payroll errors can be costly and difficult to correct.

More than ever, it's vital to have an accurate, efficient way to handle payroll for your business. Luckily, you have options. You can:

- ✓ **Outsource your payroll** to an accountant or a payroll service provider. This hands-off method can be time-saving but costly, and you may have to wait for paycheck delivery.
- ✓ **Buy off-the-shelf payroll software** for effective payroll calculations. You will need to download costly updates to keep up with software and tax changes, and you will have to file your own taxes.
- ✓ **Choose online payroll software.** You can log into a secure website to run payroll anytime or anywhere you have an internet connection. The software updates automatically for free, and if your computer crashes, your data is securely saved. With online payroll, you can file your own taxes or sign up for an optional payroll tax filing service.



## HELP! I'VE MADE THIS MISTAKE

It's never too late to choose a more efficient, reliable payroll process for your business. When you're choosing a payroll method, look for guaranteed accuracy, security, ease of use, affordable cost, and reliable customer support. With TransNational Payments' **Full Payroll Service**, you will receive all of this and more!



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