Mastering U.S. Federal Payroll Compliance

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Staying compliant with federal payroll mandates isn't just a best practice—it's crucial for your business's survival. Payroll mistakes can result in hefty fines, legal trouble, disrupted operations, and even loss of your business license. Remember Al Capone? He dodged many charges but was ultimately jailed for tax evasion.

The landscape of federal payroll tax laws is constantly evolving. Federal payroll tax laws and regulations constantly evolve, making it challenging to stay compliant. What was compliant yesterday may not be today, making it difficult to keep up. Whether you're new to payroll or an experienced professional, mastering federal payroll compliance is always a challenge. In this guide, we'll break down key regulations and show how the right payroll partner can help safeguard your operations.

Importance of Understanding Payroll Laws for Businesses

The federal government enforces payroll regulations to protect businesses and employees. These regulations exist to promote fair working conditions, prevent unethical practices, and combat discrimination.

Non-compliance can lead to significant penalties. Depending on the severity and frequency of non-compliance, failing to comply with these regulations can lead to fines, legal action, and/or even imprisonment. Whether

you're managing payroll internally or processing it for clients, it's your responsibility to adhere to all payroll laws and regulations.

But compliance isn't just about avoiding penalties – it also builds trust with your employees, showing that your business is committed to fairness and integrity.

Key Federal Payroll Laws You Need to Know

The U.S. Department of Labor (DOL) is responsible for enforcing various laws that affect payroll. While not all laws impact payroll directly, several key regulations are critical to ensure compliance.

Here's a quick overview of the federal laws you should prioritize:

• **The Fair Labor Standards Act (FLSA) -** Establishes minimum wages, overtime pay, and restricts child labor.

• **The Family Medical and Leave Act (FMLA) -** Allows employees to take unpaid job-protected leave for family and medical reasons.

• **The Employee Retirement Income Security Act (ERISA) -** Regulates pension and welfare benefit plans, which are often managed through payroll.

• **The Affordable Care Act (ACA) -** Provides all Americans access to affordable healthcare processed through payroll deductions and benefits.

• **The Consumer Credit Protection Act (CCPA) -** The majority of this law does not apply to payroll, but Title III establishes boundaries and restrictions around excessive wage garnishment.

These are five of the most common federal laws, but you should also stay current on state laws. For example, workers' compensation programs are covered by the state in which an employee lives or works and are not managed at the federal level.

Navigating The Fair Labor Standards Act (FLSA)

The Fair Labor Standards Act (FLSA) is one of the most comprehensive payroll laws in the U.S. It was enacted in 1938 to protect workers in the United States. It sets out crucial regulations regarding minimum wage, overtime pay, recordkeeping, and child labor. For payroll professionals, staying current with these rules is essential to ensure fair compensation and avoid legal pitfalls.

The Importance of Minimum Wage Compliance

One of the cornerstones of the FLSA is the federal minimum wage. Since its inception, the minimum wage has been adjusted numerous times to reflect economic conditions. Currently, the Federal minimum wage in the U.S. is $7.25 per hour.

Most states have additional legislation that establishes their minimum wage rate. Whether the state minimum wage is higher than the federal minimum wage (like in New York, where the minimum wage is $15.00) or the federal minimum wage is higher than the state minimum wage (like in Wyoming, where the minimum wage is $5.15), employers are required to provide the highest benefit for their employees.

Understanding Overtime Rules

Non-exempt employees who work more than 40 hours in a workweek must receive overtime pay at one and a half times their regular pay. This rule ensures fair compensation for additional hours worked and prevents exploitation. Miscalculating overtime is a common compliance issue.

Who is Exempt vs. Non-Exempt?

The most common exemption from the overtime standard is the executive, administrative, and professional employees (EAP) exemption. To qualify for the EAP exemption, an employee must be paid at least $684 a week ($35,547 annually). If an employee meets that standard and works over 40 hours a week, the employer is not required to pay time and a half for the additional hours worked.

The EAP exemption is being updated, and the salary range is increasing. This means that some employees that used to be EAP exempt will now qualify for overtime pay through the FLSA.

On July 1, 2024, the salary range was updated to $43,888, and on January 1, 2025, the salary range will be updated to $1128 per week, with it being scheduled to be updated on July 1, 2027, and every three years after. If you are a payroll processor, it is essential to correctly classify exempt and non-exempt employees as misclassification can lead to significant legal challenges.

Recordkeeping Requirements Under the FLSA
Accurate recordkeeping is essential under the FLSA. Employers must maintain detailed records of employees' hours worked, wages paid, and other pertinent information for at least three years. Proper documentation helps verify compliance and defend against potential disputes.

Impact on Payroll Processing
For payroll professionals, understanding the FLSA is not just about compliance; it's about efficient payroll processing. Knowing the nuances of the law helps in accurate wage calculation, timely payroll disbursement, and proper record maintenance. This knowledge reduces errors and enhances overall payroll efficiency.

Avoiding Common Payroll Pitfalls
There are several common mistakes that employers and their payroll partners encounter when dealing with the FLSA. These include misclassifying employees, miscalculating overtime, and failing to maintain accurate records. Awareness of these issues and proactive measures can help avoid costly mistakes. Regular training and updates on FLSA regulations are crucial.

Leveraging Technology for Payroll Compliance
Payroll compliance is easier when you leverage technology. The right payroll software can automate complex payroll processing, including wage calculations, recordkeeping, and compliance checks. A good payroll partner will provide tools that can save time, reduce errors, and ensure adherence to FLSA regulations.

Practical Tips for Payroll Professionals

Here are some practical tips for payroll professionals to ensure FLSA compliance:

• Regular Audits: Conduct regular audits of payroll records to ensure accuracy and compliance.

• Training Programs: Implement training programs for HR and payroll staff on FLSA regulations.

• Software Solutions: Utilize payroll software that includes compliance features.

• Expert Advice: Seek advice from labor law experts when in doubt. IRIS has a full team of payroll compliance experts that ensure our payroll software is up to date with all new regulations

The Employee Retirement Income Security Act (ERISA)

The Employee Retirement Income Security Act (ERISA) is a key law affecting payroll professionals and accounting firms. Passed in 1974, ERISA sets basic rules for pension plans and health insurance benefits. While it doesn't require employers to offer these benefits, it does regulate those who do, ensuring transparency, accountability, and protection for workers.

Key ERISA Compliance Points:

Pension Plan Standards
ERISA establishes funding standards for employers offering pension plans. Payroll professionals must ensure compliance with these funding requirements and properly track benefit payments.

Health Insurance
Although ERISA doesn't mandate employers to provide health insurance, it does exempt employer-sponsored plans from certain state regulations, allowing for more consistent coverage across the country.

Reporting and Disclosure
ERISA demands strict reporting and disclosure. Employers must provide plan participants with detailed information about their benefits, funding status, and rights. Annual reports outlining the financial health and operations of benefit plans must be filed with the Department of Labor.

Fiduciary Responsibilities
Those managing benefit plan assets must act in the best interest of participants. They must focus on providing benefits and minimizing administrative costs.

Prohibited Transactions
ERISA bans certain actions that could lead to conflicts of interest or self-dealing. Fiduciaries must avoid these to ensure plan assets benefit the participants.

Enforcement and Penalties
ERISA has both civil and criminal penalties for non-compliance. The Department of Labor, IRS, and Pension Benefit Guaranty Corporation (PBGC) enforce its rules.

The Role of the PBGC
The PBGC is a federal agency set up by ERISA to protect private-sector pension benefits. It defines benefit plans, ensuring participants receive their promised benefits even if their employer's plan fails or is underfunded.

Why It Matters for Payroll
Managing employee benefits within the confines of ERISA requires payroll teams to monitor compliance closely and ensure that benefits are distributed appropriately. Non-compliance could lead to penalties or loss of employee trust.

Breakdown of the Patient Protection and Affordable Care Act (ACA)

The Patient Protection and Affordable Care Act, usually called the Affordable Care Act or ACA was signed into law in 2010. It aims to expand healthcare coverage, reduce costs, and improve healthcare quality. Understanding the ACA is crucial for ensuring compliance and avoiding penalties for payroll service bureaus and accounting firms.

ACA Compliance Essentials for Payroll:

Defining an Applicable Large Employer (ALE)
An applicable large employer (ALE) is a business that employed 50 or more full-time employees in the previous fiscal year. The ACA mandates that ALEs offer affordable health insurance to at least 95% of their full-time employees and their dependents. A full-time employee works (on average) 30 hours or more per week or 130 hours or more per month. Understanding whether the business qualifies as an ALE is the first step in ACA compliance.

Filing Forms 1094-C and 1095-C
ALEs must file forms 1094-C and 1095-C every tax year with the IRS and all applicable state agencies. These forms confirm that ACA-compliant coverage was offered to employees every month. Properly filing these forms is critical to avoid penalties and ensure compliance.

Matching Business Practices with ACA Requirements
Consistency between your business practices and the information on forms 1094-C and 1095-C is essential. Discrepancies can lead to penalties and compliance issues. Regular audits and updates to your payroll processes can help maintain alignment with ACA requirements.

The Financial Impact of ACA Penalties
Non-compliance with the ACA can result in significant financial penalties for ALEs. These penalties are calculated based on the number of full-time employees not offered affordable health insurance. Understanding these penalties can motivate organizations to prioritize compliance.

The Role of Technology in ACA Compliance
Modern payroll software can streamline ACA compliance by automating calculations, tracking employee hours, and accurately filing forms 1094-C and 1095-C. Investing in the right technology can significantly reduce the risk of errors and non-compliance.

Why It Matters for Payroll:
Compliance with the ACA is not just a legal obligation – it also ensures your business avoids costly penalties. Payroll professionals play a pivotal role in this, as they manage the reporting and ensure consistency with company practices.

The Consumer Credit Protection Act (CCPA)

Wage garnishments occur when a court orders deduction from an employee's paycheck to repay debts. Common reasons for wage garnishment include child support, student loans, and tax debts.

The Consumer Credit Protection Act (CCPA) is vital in regulating wage garnishment. It provides protections for employees and limits the amount that can be garnished from their disposable earnings. The CCPA is designed to balance the interests of creditors and employees' financial well-being.

Key CCPA Compliance Points:

Employee Protections Under the CCPA
One of the critical protections the CCPA offers is safeguarding employees from being terminated or discriminated against due to wage garnishments. Employers are prohibited from firing an employee because their wages are being garnished. This protection is limited to one wage garnishment, and additional garnishments could potentially alter this protection, depending on the State.

Limitations and Maximum Percentages
Most of the CCPA is implemented in the courtroom, where they establish how much of an employee's income must be garnished. Limitations and maximum percentages of disposable earnings may be garnished. Still, an employer should have no influence or access to those specific decisions. A payroll provider only needs to be aware of the amount that needs to be garnished from each paycheck.

Responsibilities of Payroll Processors
As a payroll provider, if you receive a wage garnishment order you should:

• Notify the employee: Inform employees of the garnishment, including where it was issued and the amount being withheld.

• Calculate withholdings: Calculate the correct amount to be withheld from their paycheck. This requires a thorough understanding of the CCPA and any state-specific laws that may affect the garnishment.

• Remit payments to the creditor or legal authority: After calculating the correct amount, it must be promptly sent to the appropriate creditor or legal authority. Timely remittance is crucial to maintaining compliance and avoiding penalties for late payments.

• Accurate recordkeeping: This should include the start date, the amount withheld, and the end date. This can also encompass all communication between you and the employee, including your initial conversations informing them of the garnishment.

• Handling changes in employment status: If the employee's employment status changes (e.g., termination or resignation), the payroll processor must inform the creditor or legal authority. Failure to do so can result in liability for the unpaid portion of the debt, along with potential fines and attorney fees.

Why it Matters for Payroll
Handling wage garnishments properly not only protects your organization from legal risks but also ensures employee satisfaction and trust.

Unlocking Federal Compliance for Payroll: What Every Employer Needs to Know

Employer Identification Number (EIN)

Every business processing payroll needs an Employer Identification Number (EIN). This nine-digit number, assigned by the IRS, is your company's identification for tax purposes, much like a social security number is for individuals. Applying for an EIN is straightforward and free, but maintaining it accurately is crucial for compliance.

Applying for an EIN can be done online through the IRS website. The business's legal name, type of organization, and other pertinent details must be provided. Once the application is submitted, the EIN typically takes two weeks to register.

Remember, an EIN is not just for payroll; it's also required for filing federal taxes, hiring employees, and applying for business licenses.

Tax Withholding

Payroll isn't just about paying employees – it's also about ensuring that taxes are withheld and remitted to the government properly. Here's are the two major components of tax withholding:

Federal Income Tax

Federal income tax withholdings are determined by the information provided on an employee's W-4 form. This includes their filing status, number of dependents, and any additional amount they wish to withhold. The withholding amount is then calculated based on their gross annual taxable income.

While it's possible to calculate these withholdings manually, using a payroll tool can significantly simplify the process. The IRS provides tax tables that outline the correct withholding amounts based on the information provided on the W-4 form. Payroll software can automatically apply these tables, reducing the risk of errors. Incorrect withholdings can lead to penalties and interest charges from the IRS. For employees, it can result in underpayment or overpayment of taxes, leading to an unpleasant surprise come tax season.

Federal Insurance Contributions Act (FICA) Tax

FICA tax supports Social Security and Medicare contributions. Both employees and employers share the responsibility of paying FICA tax, making it essential to calculate these withholdings accurately.

• Social Security tax is calculated at 6.2% of an employee's gross income up to a certain wage limit. Employers are responsible for matching this contribution, resulting in a total Social Security tax rate of 12.4%.

• Medicare tax is 1.45% of an employee's gross income, with no wage limit. Like Social Security tax, employers must match this contribution, bringing the total Medicare tax rate to 2.9%.

For most employees, the combined FICA withholding rate is 7.65%. Payroll providers must ensure these withholdings are calculated and reported accurately. Failure to do so can result in penalties and interest charges from the IRS.

Employee Classifications

Correctly classifying employees is more than just an administrative task – it's fundamental to determining tax obligations, benefits, and compliance with federal laws like the Fair Labor Standards Act (FLSA). Misclassification can lead to costly fines and legal issues, so it's crucial to understand the different types of employee classifications.

The seven common employee classification types are:

1. Full-time: These employees work a set number of hours each week, usually receiving a salary rather than an hourly wage. The FLSA does not specify a minimum number of hours for full-time status; employers set these parameters. Therefore, an employee can work 31 hours per week and still be classified as full-time.

2. Part-time: These employees are paid hourly and usually do not receive additional benefits. They are non-exempt from overtime pay since they generally work less than 40 hours per week and earn below the FLSA minimum rate.

3. Contract: Contract employees are hired for a specific duration as outlined in a professional contract and appear on the company's payroll. The contract specifies job duties, compensation, and work expectations. They can qualify for FLSA benefits if their compensation exceeds the annual minimum limit through multiple contracts within the same fiscal year.

4. Independent Contractor: Contractors perform similar roles to contract employees but are not on the company's payroll. They work flexibly, often beyond 40 hours per week, and have varying compensation structures. They are not considered employees and do not receive FLSA or other employment benefits.

5. Temporary: These employees are hired for short-term or seasonal work. Their classification as exempt or non-exempt depends on their job duties, wage structure, and employer specifics.

6. On-Call: On-call employees must be available during specified hours but are not required to work continuously during these times. They may need to be on-premise, especially in healthcare roles, but often must be easily reachable for remote positions. Pay for on-call time is calculated case-by-case.

7. Volunteer: Volunteers do not receive compensation; therefore, tax and employment laws do not apply to them.

Why It's Important for Payroll
Employee misclassification is one of the leading causes of payroll compliance issues. Partnering with the right payroll partner can save your business from hefty penalties.

The Crucial Role of Your Payroll Software Partner in Ensuring Federal Compliance

In today's rapidly evolving business landscape maintaining federal compliance in payroll processing is more critical – and more challenging – than ever. Payroll service bureaus and accounting firms face increasing pressure to keep up with evolving legislation, complex tax codes, and stringent reporting requirements. Partnering with a reliable payroll software provider is essential to meet these demands. But what exactly should you expect from your payroll partner to ensure compliance? Here, we break down the key roles and features your payroll software or service partner should offer to keep you federally compliant.

Automatic Tax Filing and Payments

One of the most significant advantages of a top-tier payroll solution is the automation of tax filings and payments. This feature saves time and minimizes the risk of human error, which can lead to costly penalties and interest. With IRIS Payroll, you can count on:

• **Automated Tax Management:** Once a payroll is approved, tax liabilities are scheduled automatically for payment on the due date, and for users of our advanced electronic services, all tax payments and forms are processed automatically - with the flexibility to specify different terms for any tax payment as needed.

• **Easy Electronic Services:** Submit a single application for all electronic services, including federal and state electronic payments, e-filing, direct deposit, and more.

• **Comprehensive Electronic Filing:** Electronic filing of federal and most state forms, including forms W-2, W-3, 1099-MISC, and 1096, with automatic e-filing option.

• **Signature-Ready Forms:** Access signature-ready tax forms for federal and all 50 states, including filing status summary.

Dedicated Compliance Team

Navigating the complex landscape of payroll regulations can be daunting. Non-compliance leads to fines, penalties, potential lawsuits, legal repercussions, and a serious disruption to your business operations. That's why you need a payroll partner with a dedicated compliance team that ensures your business stays up-to-date with all relevant payroll regulations.

• **Stay ahead of legislative changes:** Our compliance experts constantly monitor updates in payroll laws, ensuring your business adapts smoothly to any changes. You can trust us to keep you informed of critical deadlines and updates.

• **Timely software updates:** Legislative changes are seamlessly integrated into our software. Our compliance team works closely with product development to provide nearly real-time updates, so your payroll processes remain compliant and efficient.

• **Expertise You Can Trust:** Our Director of Compliance is an active member of the Reporting Agents Forum for the IRS and serves on the Citizens Bank Treasury Advisor Board. This expertise is a full-time commitment to staying on top of U.S. payroll tax rules and regulations.

Streamlined Client Communications

Communication and transparency are essential for your success. Your payroll partner should make it easy to communicate with your clients and include being able to schedule automatic communications.

With IRIS, you can schedule automatic emails to remind employers about important deadlines, strengthening client relationships while reducing your workload.

Comprehensive ACA Compliance Assistance

Ensuring compliance with the Affordable Care Act (ACA) is non-negotiable. Your payroll service should offer robust support for tracking employee eligibility and managing necessary forms. Unlike other solutions, we feature an ACA tool that reduces administrative burdens and mitigates IRS penalties. This tool allows you to:

• Connect directly to your payroll data, expanding your ability to monitor, report, and conduct affordability checks

• Track when employees are due offers of coverage

• Monitor full-time status for variable-hour employees

• Manage health plan coverage information

• Electronically file forms 1094-C and 1095-C

• Measure period cycles down to child companies

• Automate tracking of coverage based on defining factors

Streamlined and Integrated Services

Payroll is not a standalone service; it's part of an ecosystem of many services like HR, Time & Attendance, accounting, and data mining.

IRIS Payroll provides an open set of APIs that enables other applications to set up and modify employees, send time data, and read paystubs.

API integration also enables IRIS Payroll to send payroll data automatically to your accounting system.

Consistent and Reliable Feature and Functionality Updates

Payroll is an essential service that needs to be accurate and consistent every pay period. Just like you go to the dentist for checkups to ensure your teeth are healthy, your payroll solution should frequently run self-diagnosis and updates. IRIS technology is consistently updated to ensure compliance with all monthly, quarterly, and annual federal, state, and local payroll tax changes without disrupting your day-to-day processes.

Ensure Your Payroll Compliance with Unmatched Security

In an age where data breaches are a significant concern, protecting sensitive payroll information is paramount. Accounting firms and payroll service bureaus need robust systems that comply with U.S. Federal Payroll regulations and guarantee the utmost security for client data.

The integrity and confidentiality of payroll data are paramount. A breach can lead to severe consequences, including financial losses, legal penalties, and damage to your reputation. That's why it's essential to ensure that your system is secure and reliable.

At IRIS, we host your and your clients' data on Amazon Web Servers (AWS), the same industry-leading infrastructure used by Amazon.com. AWS is renowned for its state-of-the-art security features and has earned leading industry certifications, including:

• **ISO 27001 –** Demonstrates our commitment to keeping information assets secure.

• **SAS70 Type II Audits –** Shows our compliance with stringent security standards and controls.

Download the IRIS Payroll Software brochure for more specific compliance functionality such as advanced e-services, critical compliance push notifications, and report generation.

Take the Next Step to Ensure Federal Compliance for Your Firm and Clients

Federal payroll compliance is a complex and evolving challenge, but it doesn't have to be overwhelming. By leveraging the automation and expertise offered by a reliable payroll software or service partner like IRIS, you can ensure timely and accurate compliance, freeing up time to focus on growing your business.

If you're ready to take the next step in streamlining your payroll processes and ensuring federal compliance, consider partnering with IRIS. Learn more about how our solutions can benefit your business and connect with a specialist today.

Contact now

IRIS Americas is part of IRIS Software Group. IRIS payroll solutions exist to take the pain out of processes and enable professionals working in CPA firms and payroll service bureaus businesses comply with regulations, improve efficiency and drive growth. IRIS Americas brands include IRIS Star Practice Management, IRIS Global Workforce, IRIS Innervision, IRIS Practice Engine, Doc.It, PSI Payroll, IRIS HCM, Apex, AccountantsWorld, Senta and Conarc.

IRIS partners with thousands of CPA firms, payroll service bureaus and small to midsize businesses across North America, including 52 of the top 100 US CPA firms. We offer innovative Payroll and HR solutions, making us the preferred partner in the region. Globally, IRIS serves over 100,000 customers, with 80% having tenure of five or more years.