PAYROLL ACCOUNTING

2016





Jeanette M. Landin Paulette Schirmer

Payroll Accounting 2016

Payroll Accounting 2016

Second Edition

Jeanette M. Landin

Landmark College

Paulette Schirmer

University of Phoenix





PAYROLL ACCOUNTING, SECOND EDITION

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Dedications

The authors dedicate this book to the following individuals:

For Chris, Kierstan, and Meaghan, who are the center of my universe.

—Jeanette Landin

For Royce and Elizabeth, who kept me grounded and reminded me to have fun.

—Paulette Schirmer

About the Authors



Jeanette Landin

Landmark College
Jeanette Landin is an Assistant Professor of Business and Accounting at Landmark College in Putney, Vermont, where she teaches undergrad-

nix, where she teaches composition and communications courses at the associate's level. Dr. Landin earned her B.A. degree from the University of California at Irvine before receiving her M.B.A. and Ed.D. from University of Phoenix, where she conducted research into college success strategies for at-risk students. She has earned Master's certificates in Accounting and Autism Spectrum Disorders. She is an active member of the Institute for Management Accountants (IMA), Teachers of Accounting Curriculum at Two-Year Colleges (TACTYC), and Vermont Women in Higher Education (VWHE), and previously served as an active member of the California Business Educators Association and the Western Business Educators Association. Dr. Landin currently serves on the IMA's Committee for Academic Relations and as a peer reviewer for the American Accounting Association. She is a peer reviewer for the Transnational Journal of Business and a member of the Business Editorial Board with the Multimedia Educational Resource for Learning and Online Teaching (MERLOT).

uate accounting and business courses to an at-risk student

population. She is the faculty advisor for the college's

Phi Beta Lambda chapter. Professor Landin is also a Cer-

tified Advanced Facilitator with the University of Phoe-



Paulette Schirmer

University of Phoenix
Paulette Schirmer is an accountant
with the Division of Finance for
the State of Alaska and a Certified
Advanced Facilitator for the Uni-

versity of Phoenix, where she teaches accounting courses at the bachelor's and master's level. Dr. Schirmer received her B.S. in Accounting from Metropolitan State College of Denver (now Metropolitan State University of Denver), her M.B.A. from Regis University, and her D.B.A. from University of Phoenix, where she conducted research on globalization strategies for small businesses.

Dr. Schirmer is active in the preparation of Alaska's Comprehensive Annual Financial Reports and that state's annual Compensation and Travel Report, as well as training state employees on the state's financial and reporting systems.

A light from the Authors

Businesses employ people, and part of employing people is compensating them for their labors. Labor costs often represent the largest company expenditure as well as the most complex one. Payroll accounting is very detailed, deadline driven, and of utmost importance for the successful functioning of a business. The changing, detailed nature of payroll accounting involves legal challenges, economic changes, technological advances, and-above all—governmental obligations. As we sought payroll accounting materials for study by our students, we realized that not many textbooks about the subject existed. We are passionate about college education. Our aim in Payroll Accounting 2016 is to provide instructors with a payroll accounting text that allows them to teach students how to navigate this highly specialized and extremely necessary aspect of accounting.

When we began updating the materials for *Payroll Accounting 2016*, we noticed how quickly payroll information changes and how much it mirrors societal evolution. We continue to rely on the guidance of our colleagues, instructor feedback from the first edition, and the information gained from our peers. Additions to the second edition reflect industry and student needs, and we continue to follow these trends to inform future updates.

Our approach to payroll accounting is different from other existing texts because we have chosen to include both the financial and managerial accounting pieces so that students can understand both the techniques involved and the importance of their work in the broader scope of business. We have worked very hard to present content that is concise, thorough, and easy to follow. We are excited to produce this work through McGraw-Hill because of the top-quality teaching and learning resources that the company makes available. Teaching traditional payroll accounting and Internet-based financial accounting via McGraw-Hill's Connect platform for several years has been a wonderful experience for both our students and ourselves.

Our text features many interesting real-world connections throughout. We've drawn examples from many different disciplines to help make payroll accounting come alive for teachers and students alike. Two discussions are unique: (1) the content in Chapter 5 that explores labor planning (Learning Objectives 5-5 and 5-6) and (2) the discussion in Chapter 6 about the function of labor costs in business and employee benefit reports as strategic tools (Learning Objective 6-7). We believe that this information contributes to a comprehensive understanding of

payroll accounting in the 21st century and that it will make accounting students more valuable to the organizations they work for in their careers.

Many payroll frauds and scandals occur in the real world. Payroll fraud continues to be a major source of loss for companies, and it is surprising to find how commonly it happens. We've included examples of the frauds that employees have perpetrated in recent years. One notable case that highlighted the scope of payroll fraud involved a \$700 million scheme that resulted in hundreds of jobs lost and for which the perpetrators remain at large. Students are interested in these stories, which enliven and enrich class discussion. We've also included a section in each chapter about ethics and internal controls to teach students how to prevent payroll fraud and to identify potential data breaches. We believe that this information about internal controls will become increasingly important as sensitive personnel information becomes more readily accessible with the inclusion of cloud-based payroll systems.

Payroll accounting and the associated fields of economics and finance are continually evolving. As a result, the payroll industry contains an ever-changing array of rules and regulations, and the "Trends to Watch" box in each chapter will highlight the trends known at the time of publication. On the legal front, we are watching the ripple effects of the Supreme Court's legalization of same-sex marriages upon businesses and employees. The intersection of this legislation and the Affordable Care Act has affected employee benefits and tax reporting. Other trends we are watching include issues of cybersecurity that challenge the notion of secure electronic payroll deposits and cause internal control guidelines and new regulations to respond to the changing needs of the economy. In the "Internet Activities" sections at the end of each chapter, we provide Internet links for students who want to explore payroll topics in more depth.

In addition, we provide both a continuing problem, which is located at the end of each chapter, and a full-quarter additional comprehensive problem, located in Appendix A. Technological integration of the continuing problem and Appendix A within Connect provides a good tool for student learning. Smartbook, LearnSmart, and walk-through examples of tax forms are used to reinforce the questions and key terminology. A shortened version of Appendix A is another option for instructors who want a comprehensive problem with fewer payroll periods.

From our perspective, payroll accounting is complex enough to warrant specific attention in the curriculum.

ONE HUNDRED DOLLARS

Payroll Accounting 2016 is designed to fit the needs of terms as short as 3 weeks and as long as 15 weeks. The instructor may choose to assign the exercise sets found at the end of each chapter, the Continuing Payroll Project in each chapter, or the Comprehensive Project that encompasses an entire quarter of payroll accounting. We designed the content to give instructors curricular flexibility by offering many options for formative and summative assessments.

We are proud of what we have accomplished with this text and strongly believe that we have taken payroll accounting education to a higher level of rigor. The content of *Payroll Accounting 2016* is rich in its detail, yet readily understandable by students who may have little or no

prior accounting information. We have included materials to show the integration of payroll in other aspects of both managerial and financial accounting as well as business operations. Within Appendix E, we have provided materials that allow readers to learn about payroll within the context of their own state's legal framework and links to each state's revenue department to facilitate specific learning. We hope that you enjoy reading and learning from this text as much as we enjoyed writing it.

Jeanette Landin Paulette Schirmer



Based on feedback from our reviewers and users, we have made several changes to this second edition of *Payroll Accounting*. We appreciate all the feedback we have received and user recommendations because they have helped us create a stronger, more complete text. The changes we have made have added clarity, updated information, and additional opportunities for students to demonstrate their understanding of the concepts presented. For instructors, we have revised our learning objectives to incorporate Bloom's taxonomy verbs and have correlated the learning objectives with End-of-Chapter exercises. The answers for the Stop & Check sections are now included at the end of the chapters.

The following are specific changes to each chapter.

Chapter 1

In Chapter 1, we updated payroll-related legislation to reflect as many changes as possible prior to publication. We have included specific information about the effects of the Affordable Care Act on payroll management with regards to reporting requirements. We addressed guidance from the U.S. Department of Labor about payroll treatment of same-sex marriages, a topic that is continuing to evolve. We incorporated information about the changing nature of exempt worker classification and discussed cloud-based payroll accounting practices.

Chapter 2

In Chapter 2, we included highlights of upcoming guidance about employees that will be issued by the Equal Employment Opportunity Commission. We included some payroll-specific items about the current debate about minimum wage. We added information about applications available via smartphones and tablets that foster improved accuracy and increased employee involvement in time tracking and payroll file maintenance. We discussed proposed paycard legislation that would both facilitate employee access to compensation and guard employees against fraud. We included a graphic to clarify document retention requirements.

Chapter 3

Chapter 3 opens with updated minimum wage and tipped minimum wage information. We added depth and clarity to the discussion of overtime calculations, especially for piece-rate workers. We included statistical information about Incentive Stock Options and executive pay, topics that are becoming discussed more frequently by government officials. We added information to the discussion of special pay situations and exercises to for students to apply their learning.

Chapter 4

We extended our discussion of insurance coverage with details about employer mandates under the Affordable Care Act. We created a chart to help students understand the differences among employer-sponsored retirement plans and clarification about Section 125 (cafeteria) items. We included step-by-step guidance about using the wage-bracket tables in Publication 15 to determine federal income tax withholding amounts. The discussion of post-tax deductions includes more detail about mandated post-tax deductions and limits on amounts that may be withheld. We offered a detailed explanation about the computation of grossed-up pay and figure with explicit details about paper paychecks.

Chapter 5

In Chapter 5, we have updated employer payroll tax information, especially as it pertains to FUTA and SUTA amounts. We have included guidance about employee compensation not subject to FUTA. All tax forms have been updated with the current year's editions. Figure 5-8 has been included to depict statistics about employer benefit costs to offer students a more complete picture of how payroll affects business profitability, reflecting payroll accounting's effect on managerial accounting. End-of-Chapter Exercise sections contain questions about Forms W-2 and W-3 so students may practice this skill.

Chapter 6

Chapter 6 opens with a discussion about employee retention and connects the payroll procedures discussed in the previous chapters to financial accounting concepts. We have updated the transactions to reflect current-year tax rates and have updated all accounting reports to match the presentation students will see in the End-of-Chapter Exercises.



Appendix A: Comprehensive Payroll Project

We have changed the location of Wayland Custom Woodworking to the state of Utah to facilitate computations of State Withholding Tax. We have included explicit instructions about the completion of employee paychecks.

Appendix D: State Income Tax Tables

We have included included tax rates for each state in Appendix D. This new information includes tax brackets, both married and single, and marginal tax rates.

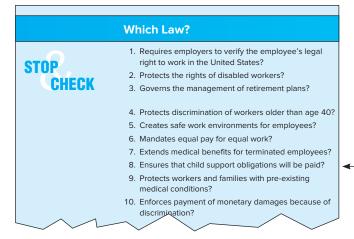
Appendix F: Payroll Certification Information

We have included information from the American Payroll Association about its Fundamental Payroll Certification (FPC). Upon completion of their payroll course, students could consider obtaining this certification to add to their career portfolio.



Chapter Opener

Each chapter opens by focusing on a payroll accounting topic related to a real-world company, to set the stage for the topic of the chapter.



Payroll Practices and System Fundamentals

The payroll system of a company is the backbone of its employees' records and serves many functions. The most obvious and visible role for a company's payroll department is the employee pay and benefits management function. However, a well-designed payroll system can do so much more. Payroll systems are an integral part of job planning and strategic human resource management, cost management for products and services, and benefits analysis for a company, in this chapter, we will explore the need for a payroll system, legal requirements, ethical guidelines, best practices, and variations in payroll practices among different-sized companies.

LEARNING OBJECTIVES

After studying Chapter 1, you should be able to:

L0 1-1 Understand the Purpose of Studying Payroll Accounting

L0 1-2 Discuss the Legal Framework for Payroll Accounting

L0 1-3 Discuss the Ethical Guidelines for Payroll Accounting

L0 1-4 Identify Contemporary Payroll Practices

Compare Payron Ssing Options for Different

Stop & Check

The Stop & Check feature allows students to review their understanding of the content just read. It also enables instructors to conduct formative assessments at multiple points throughout each chapter, testing the students' understanding informally as well as offering opportunities to expand on the material.

Repeal of the Defense of Marriage Act, which changed the definition of married couple

Trends to Watch

Each chapter contains a feature box that connects payroll-related recent events with industry trends that shape the future of the profession. These trends offer instructors more opportunities to expand upon chapter topics, fostering discussion and application.

Trends to Watch LEGAL ENVIRONMENT To say that the legal environment of payroll is continually evolving is an understatement. During the early part of the 2010s, we have witnessed the following legal challenges: Modification of language in employee handbooks to refine terminology and remove offensive wording. Official revisions to define the term supervisor as it pertains to employee discrimination. Employer liability for accidents following alcohol consumption at employer functions.

to include same-sex unions

End-of-Chapter Exercises

Students can demonstrate their understanding through exercises designed to complement the chapter's learning objectives. Each chapter has two alternative sets of exercises (A and B) to allow flexibility in classroom instruction and assessment.

★					
	Exercises Set A	1-1A. LO 1-6	Anya is a candidate for the position of sales manager with the foot- wear department of a major retail outlet. She is going to be required to supervise several employees and can determine the direction in which she will complete the assignments given to her. What classification of employee should she be, exempt or nonexempt? Explain.		
		1-2A. LO 1-6	John is the office manager for a small mortgage brokerage. Because it is a small معتصور he is required to keep track of all empayore records		

ONEHUNDRED DOLLARS

Critical Thinking Exercises

Want to challenge your students further? The Critical Thinking exercises require students to consider complex real-world situations that build confidence and turn learning into mastery. These exercises offer possibilities for team presentations or class debate.

In the Real World: Discussion

The Brinker Restaurant Group, owners of restaurant franchises such as Ch and Bar and Maggiano's Little Italy, was sued by its employees for not propadequate meal and rest breaks for employees. According to the Californi Code §512 and Wage Order no. 5, employees must be provided with rods—specifically, a 30-minute meal break—every five hours that they wo 10 hours of consecutive work, the employee must be given a second me The California Supreme Court ruled that the rest breaks had to be offered employer did not have to ensure that the employee actually rested.

What do you think? Should employers ensure that employees on breaks form any work? Why or why not?



- 1-1. You have been hired as a consultant for a company facin accounting records. During your review, you notice and system involving overpayments of labor and payments to ees. What should you do?
- 1-2. Lee Chen is the accountant for a local nonprofit organi tasked with managing the costs of the payroll so that staffi the same even if funding levels change. He considers ou to a payroll processing company. What are some factors er in his decision? Why are these factors important?

←In the Real World: Scenarios for Discussion

Each chapter contains a discussion scenario that is drawn from real-world events. These scenarios encourage the expansion of chapter content and allow students to apply their learning to real situations.

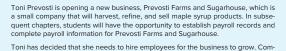
Internet Activities

The Internet Activities at the end of each chapter offer students the chance to use their Web navigation skills to expand on their learning. These exercises attract tech-savvy learners, allowing them to form their own understanding of payroll concepts on their own terms.

Internet Activities

- 1-1. Using the website www.istor.org, search for articles about payroll-related laws or relevant employment legislation. Once you find an article, summarize the article, and explain how the legislation influenced contemporary payroll practices.
- 1-2. Visit the website of the American Payroll Association at www.americanpayroll .org. On the right side of the Home page, you will find articles about recent developments in payroll practices and legislation. Choose an article and create a presentation to your class about how its content affects payroll practice

Continuing Payroll Project: Prevosti Farms and





Number (Form SS-4) with the following information: Prevosti Farms and Sugarhouse is located at 820 Westminster Road, Bridgewater, Vermont, 05520 (which is also Ms. Prevosti's home address), phone number 802-555-3456. Bridgewater is in Windsor County. Toni has decided that Prevosti

Farms and Sugarhouse, the responsible party for a sole proprietorship, will pay its

Continuing Problem: Prevosti Farms and Sugarhouse

Starting with Chapter 1, each chapter has an integrated, continuing problem—about fictional company Prevosti Farms and Sugarhouse—that matches the chapter content and affords students a macro-level understanding of how each piece of payroll fits together.



Comprehensive Payroll Project: Wayland Custom Woodworking

Comprehensive Problem

The Comprehensive Problem (Appendix A) allows students to track a quarter's worth of payroll transactions for a company. This Comprehensive Problem offers instructors increased flexibility in teaching and assessment by offering a simulation equivalent to a full quarter of a fictitious company's payroll activities, including payroll transactions, pay processing, and tax form completion. The Comprehensive Problem may be presented in different lengths—as short as one month or in its three-month entirety—to meet curricular needs.



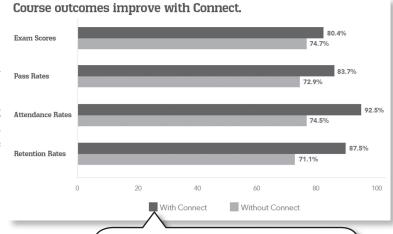
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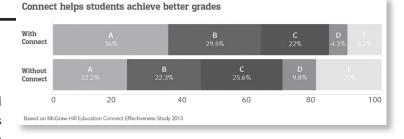
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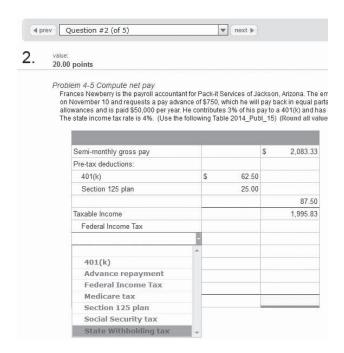


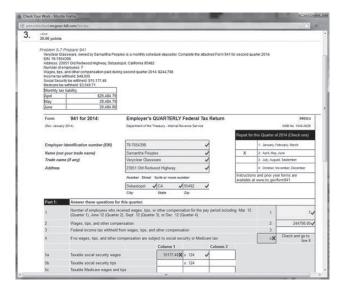
End-of-Chapter Content

End-of-Chapter Content is a robust offering of review and question material designed to aid and assess the student's retention of chapter content. The End-of-Chapter content is comprised of both static and algorithmic exercises, which are designed to challenge students using McGraw-Hill Education's state-of-the-art online homework technology. Instructors can also assign test bank questions to students in both static and algorithmic versions.

Payroll Form Problems

Templated payroll forms are integrated into *Connect* and are assignable. Students can complete the forms in these problems to gain a better understanding of how payroll forms are prepared in today's digital world.





Acknowledgments

This second edition of *Payroll Accounting* would not have been possible without the patience, guidance, and encouragement of Steve Schuetz, Brand Manager; the diligence and commitment of Jonathan Thornton, Product Developer; the support and leadership of Dana Pauley and Brian Nacik, Content Project Managers; the incredible form templates designed by Kitty O'Donnell; and the amazing artwork of Srdjan Savanovic, Designer. We further want to thank Michelle Nolte, Marketing Manager; Melissa Homer and Lorraine Buczek, Content Licensing Specialists; Patricia Plumb, Director of Digital Content Development; Xin Lin, Digital Product Analyst; Kevin Moran, Digital Product Developer; and the compositing team at SPi Global. Special thanks goes to Anna Hoppmann, Digital Asset Librarian, and to Connie Schleisman and the Technical Support team for facilitating our online access and asset location needs. Thanks go to our project development team who handled every formatting request with professionalism.

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Chapter

Payroll Practices and System Fundamentals

The payroll system of a company is the backbone of its employees' records and serves many functions. The most obvious and visible role for a company's payroll department is the employee pay and benefits management function. However, a well-designed payroll system can do so much more. Payroll systems are an integral part of job planning and strategic human resource management, cost management for products and services, and benefits analysis for a company. In this chapter, we will explore the need for a payroll system, legal requirements, ethical guidelines, best practices, and variations in payroll practices among different-sized companies.

LEARNING OBJECTIVES

After studying Chapter 1, you should be able to:

- LO 1-1 Understand the Purpose of Studying Payroll Accounting
- LO 1-2 Discuss the Legal Framework for Payroll Accounting
- LO 1-3 Discuss the Ethical Guidelines for Payroll Accounting
- LO 1-4 Identify Contemporary Payroll Practices
- LO 1-5 Compare Payroll Processing Options for Different Businesses
- LO 1-6 Differentiate between Exempt and Nonexempt Workers



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Payroll Challenges for the World's Largest Employer

Walmart, based in Bentonville, Arkansas, is the largest American employer according to 24/7 Wall Street. As of fiscal year 2014, Wal-Mart Stores, Inc., (d.b.a. Wal-Mart) employed 2.2 million workers, making it the largest private employer in the world. More than 1.4 million of Wal-Mart Stores' employees work in the United States. As of February 2015, Wal-Mart Stores announced that it would increase the minimum starting wage to \$9.00 per hour for more than 500,000 employees due to long-standing pressure from labor organizations, and that the average wage for full-time workers will rise to \$13.00 per hour. This wage increase represents an additional \$1 billion in personnel costs to the company. As of 2014, Walmart retained its top spot in the Fortune 500 ranking of companies with the largest revenue, \$476.3 billion, and more than \$16 billion in profits. (Sources: Reuters, Fortune Magazine, 24/7 Wall Street)

The need for organized payroll practices grows in proportion to the business size. Companies have many options for their payroll management, depending on the firm's structure and size. In Chapter 1, we will explore the basics of payroll systems, including legal and ethical issues involved with employee pay.

LO 1-1 Understand the Purpose of Studying Payroll Accounting

Unlike many other types of accounting, payroll affects most (if not all) members of an organization. Payroll errors could lead to serious internal and external problems. Internal errors may cause a company to pay excessive wages for unneeded overtime, forego profits, or employ the wrong number of workers during seasonal or other workflow changes. Managers use internal reports about labor usage, staffing levels, and employee compensation trends to ensure operational effectiveness. Organizational decision makers use these reports to control labor costs, hire additional employees to meet surge demands, and manage the cost of goods sold. Payroll errors can result in governmental fines, taxes, or legal charges related to the violation of labor laws. External reports are provided to the Internal Revenue Service (IRS), state government tax departments, and many more agencies, depending upon the nature of the company.

According to the United States Bureau of Labor Statistics in 2015, the accounting industry is expected to increase 13% through 2022. Salaries can range between \$34,960 for financial clerks and \$63,550 for accountants with bachelor's degrees. (Source: www.bls.gov/ooh)

The legislative framework governing employers' payroll systems is very complex. These laws reflect societal evolution over time. Note how some of these laws have been challenged or changed since their inception.

The Equal Pay Act of 1963 mandated that males and females be paid equally for equal work. If an employee feels that they have been paid unequally and the only clear delineation is based upon gender, the employee has legal options to rectify the situation.

- First, they should gather documentation regarding the differential and determine if the other employee in question is willing to substantiate the difference.
- Second, they should speak with their supervisor to question the pay differential.
- Should the supervisor be unwilling to discuss or adjust, an attorney may become a necessary third step.

This Act was modified by the **Lilly Ledbetter Fair Pay Act of 2009**, which removed the 180-day statute of limitations on claims of unequal treatment.

In 1979, Lilly Ledbetter, an employee of Goodyear Tire and Rubber Company, started at the same rate of pay as males in the same position. Over time, she was declined raises by management, which based its decisions on negative reviews that Ms. Ledbetter later claimed were discriminatory. Under the provisions of the 1963 Equal Pay Act, the claimant had 180 days to file a complaint. Although the U.S. Supreme Court agreed with her discrimination claims, it ruled in favor of Goodyear because of the lack of timeliness of Ms. Ledbetter's filing. This ruling ultimately led to the Lilly Ledbetter Fair Pay Act of 2009. (Source: www.govtrack.us)

The Civil Rights Act of 1964 prohibited discrimination based on race, creed, color, gender, or national origin. Since 1964, this Act has been extended by Executive Order 11478 to protect people with AIDS, pregnant workers, people with different sexual orientations, and people with disabilities. In 2015, discussions about LGBT employees' rights and workplace treatment have sparked debates about equal treatment based on sexual orientation and gender identity. (Source: www.eeoc.gov)

The Age Discrimination in Employment Act of 1967 (ADEA) prevents mandatory retirement of older employees (older than age 40) and prohibits age-based discrimination in hiring.

Several landmark cases followed ADEA enactment. Some of the most notable cases involved commercial airline pilots who were discriminated against based on their age, not their ability to pilot an airline. In the case of *Trans World Airlines v. Thurston* (1985), the defendant disputed the FAA's mandatory retirement age for pilots, claiming that older pilots should be given the same rights as disabled pilots, which involves reassigning these individuals as flight engineers. The U.S. Supreme Court upheld Thurston's claim but denied the double damages that Thurston sought. (Source: legal-dictionary.thefreedictionary.com)

The Occupational Safety and Health Act of 1970 (OSHA) defined and enforced healthy and safe working environments for employees. Employee safety programs and personal protective equipment represent an additional cost to the employer, but fines for noncompliance and payments made following workplace injuries are often far more costly.



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The Employee Retirement Income Security Act of 1974 (ERISA) regulates the management of retirement and pension plans. ERISA has been extended by the Consolidated Omnibus Budget Reformation Act of 1986. During the recession of 2007–2009, the value of some employee retirement funds decreased, causing employees to postpone retirement. The Internal Revenue Service imposes limitations on retirement plan contributions, and those limits have shifted to reflect the need for employees to recoup losses sustained during the recession.

In CIGNA v. Amara (2011), the U.S. Supreme Court ruled on communications issued by retirement plan administrators. CIGNA was found in violation of ERISA because of its misleading and incomplete communications to plan participants that resulted in misunderstandings about the benefit level due to the participant. The Court ruled that the benefit level accrued under the plan needed to be commensurate with the benefits received upon the participant's retirement. (Source: www.nixonpeabody.com)

The Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) extended medical benefits for terminated employees at the employee's expense. The federal government, in response to the high unemployment rates at the start of 2010, briefly subsidized COBRA insurance. The temporary reduction in COBRA remains available, but only for employees who were terminated between September 1, 2008, and March 31, 2010. The repeal of the Defense of Marriage Act (DOMA) in 2013 forced employers to offer COBRA coverage to same-sex spouses. (Sources: U.S. Department of Labor, SHRM)

The Immigration Reform and Control Act of 1986 (IRCA) requires employers to verify that employees are legally able to work in the United States. The form I-9 is the most common payroll-related application of this law. Immigration and citizenship laws require the collection of information within an I-9, and retention is three years from date of hire or one year from date of termination (whichever is longer).



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H.R. 399, Secure Our Borders First Act of 2015–2016, would strengthen immigration restrictions, affecting the number of immigrant workers available. Agribusiness is a \$374 billion industry that is heavily dependent on immigrant workers. (Sources: www.congress.gov, immigrationimpact.com)

The Americans with Disabilities Act of 1990 (ADA) extended the provisions of the Civil Rights Act of 1964 by ensuring that people with disabilities have the same opportunities

as those without mental or physical impairment. This law applies to employers with 15 or more employees on the payroll, including full-time and part-time workers.

The Civil Rights Act of 1991 granted employees who have been discriminated against the chance to be paid monetary damages through legal proceedings. This act applies to American employers and American-controlled employers with internationally based operations.

In the case of *Pollard v. DuPont* (2000), Sharon Pollard sued DuPont for her managers' knowledge of a hostile work environment created by sexual harassment. Under Section VII of the Civil Rights Act of 1964, Ms. Pollard would not have received compensation for her complaint. However, the 1991 revision of the Civil Rights Act allowed her to receive \$300,000 in compensation for damages. (Source: www.oyez.org)

The Family and Medical Leave Act of 1993 (FMLA) granted employees the right to take medical leave under reasonable circumstances without fear of job loss. The employee may have to take unpaid leave, but medical benefits must continue under FMLA provisions. Upon return from family leave, the employer must provide an equivalent position with equivalent pay, benefits, and terms of employment. The employer has many responsibilities under the FMLA that involve employee notification of benefits and processes while on leave. The repeal of DOMA provoked the need to clarify the term "family member." In 2015, the U.S. Department of Labor updated the definition of spouse to include same-sex marriages, regardless of where they live. (Source: U.S. Department of Labor)

In the case of *Young v. Wackenhut*, the plaintiff was on unpaid leave according to FMLA provisions. Ms. Young had completed all forms provided by Wackenhut, her employer; however, Wackenhut neglected to issue a specific, individual notice about requirements involved with her return to work. The New Jersey District Court ruled in favor of Ms. Young because Wackenhut did not satisfy all stipulated notification requirements of FMLA. (Source: www.lexology.com)



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The Uniformed Services Employment and Reemployment Rights Act of 1994 (USERRA) governs the rights of military service members in terms of length of military service, return to work, and accommodations for injured veterans. USERRA was amended as to service members' rights in 2005. In 2011, USERRA was further amended by the Veterans Opportunity to Work, which allowed USERRA to recognize claims of a hostile work environment resulting from an individual's military status.

The U.S. Department of Labor investigates many cases involving service members' rights. A notable case involved an Army reservist, Colonel Scott Harrison, who served multiple tours in the Middle East, during which he received many rank promotions for his military work. His civilian employer denied him promotions, stating that his military service detracted from his work performance. USERRA states that a service member must receive the same promotions and compensation that they would have received if they had not been absent for military purposes. Colonel Harrison received a promotion plus \$96,000 in lost wages because of USERRA. (Source: U.S. Department of Labor)

The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWOR) mandated that employers file a new hire reporting form within 20 days after an employee initially commences work. This act protected children and needy families

by enforcing child support obligations. The child support provisions of PRWOR were strengthened by the passage of the **Personal Responsibility**, **Work and Family Promotion Act of 2002**.

The Health Insurance Portability and Accountability Act of 1996 (HIPAA) protects workers and their families who have pre-existing medical conditions from discrimination based on those conditions. The Ebola outbreak in 2014 led to additional guidance about HIPAA rights and notifications to interested parties, including employers, during emergency situations,

In Equal Employment Opportunity Commission v. Boston Market (2004), the plaintiff claimed that Boston Market, an employer, sought access to employees' private psychological and medical records. Although the Supreme Court ultimately found that state law was more stringent than HIPAA legislation, Boston Market was found in violation of patient privacy law by seeking communication with medical professionals without prior specific authorization. (Source: www.americanbar.org)

The Sarbanes—Oxley Act of 2002 (SOX) provided criminal penalties for violations of ERISA. SOX provides protections for whistleblowers and mandates the rotation of auditors among publicly owned companies. Costs of SOX compliance have sparked discussion about the Act's effectiveness, especially following the 2008 financial crisis.

An employee of Countrywide Mortgage, a Bank of America subsidiary, alerted OSHA officials to fraud in the company's financial records. This employee led internal investigations that revealed significant fraud in monetary transactions, as well as a history of retaliation against other whistleblowers. In 2011, the U.S. Department of Labor found Bank of America to be in violation of the Sarbanes—Oxley Act's whistleblower provision and awarded \$930,000 to the employee. (Source: www.osha.gov)

The American Recovery and Reinvestment Act of 2009 (ARRA) provided tax credits for employers and employees through the Making Work Pay provisions. Changes in withholding allowances reduced the amount of taxes collected from workers, and unemployed individuals received between \$400 and \$800 on their tax return based upon specific qualifications within the act. Although ARRA's provisions have expired, parts of it were reinstated through the *American Taxpayer Relief Act of 2012 (ATRA)*. Many of the ATRA provisions were extended through 2015 by the extension of the Work Opportunity Tax Credit.

The Defense of Marriage Act of 1996 (DOMA) restricted payroll-related taxes and benefits to include only traditionally married couples, denying married status to people in same-sex unions. The U.S. Supreme Court overturned DOMA in its ruling in *U.S. v. Windsor* on September 6, 2013; the Internal Revenue Service subsequently mandated that all married same-sex couples must be treated as married for all tax purposes. The repeal of DOMA had a ripple effect throughout all phases of payroll because of the need to amend business and personal tax return filings back to 2011, owing to the three-year amendment rule. The effects of DOMA's repeal have had a ripple effect on employee rights, highlighting the need for additional legislative clarification.

In *U.S. v. Windsor*, Ms. Windsor and her wife were recognized as a married couple by the State of New York and her compensation was taxed accordingly. *(continued)*

(concluded)

However, the IRS sued Windsor for unpaid taxes because her same-sex marriage violated DOMA. The U.S. Supreme Court found that DOMA violated Windsor's Fifth Amendment right to liberty and overturned DOMA. The IRS subsequently dropped its lawsuit. (Source: www.supremecourt.gov)

As times change, new legislation will be enacted, and existing laws are sometimes repealed and amended. For example, Vermont Governor Peter Shumlin proposed an additional 0.7% payroll tax effective in 2016 to offset employee healthcare costs related to the Affordable Care Act.

The payroll accountant's job is one of consistent and continual learning and research to ensure that the company is complying with all current regulations and reporting requirements. Many states, but not all, have additional payroll tax laws.

(See www.americanpayroll.org/weblink/statelocal-wider/ for more information)

Which Law? 1. Requires employers to verify the employee's legal a. COBRA right to work in the United States? STOP 2. Protects the rights of disabled workers? b. ERISA 3. Governs the management of retirement plans? c. Civil Rights Act of 1991 4. Protects discrimination of workers older than age 40? d. PRWOR 5. Creates safe work environments for employees? e. IRCA 6. Mandates equal pay for equal work? f. ADEA 7. Extends medical benefits for terminated employees? g. HIPAA 8. Ensures that child support obligations will be paid? h. ADA 9. Protects workers and families with pre-existing i. OSHA medical conditions? 10. Enforces payment of monetary damages because of j. Equal Pay discrimination? Act of 1963

LO 1-2 Discuss the Legal Framework for Payroll Accounting



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Why did businesses start withholding taxes from people's paychecks? Federal income tax withholding was temporarily instituted in 1861 as a way to recover from the high costs of the Civil War; this tax was repealed in 1872. Throughout the 19th century, cities were growing in the wake of the Industrial Revolution, as factories and companies increased automation and institutionalized mass production. People were moving from rural to urban areas in unprecedented numbers, and the need for infrastructure and civil services grew. Roads needed to be built, law enforcement personnel needed to be increased, and outbreaks of disease prompted a need for sanitation systems. Therefore, the U.S. Congress formalized the permanent continuation of the federal income tax instituted during the Civil War as a means to fund the infrastructure improvements of the booming cities. After many failed attempts to reinstate a federal income tax, Congress passed the **Sixteenth Amendment to the U.S. Constitution** in 1913. This version incorporated a tiered income tax including exemptions and deductions to limit the tax imposed on wages earned (see Figure 1-1).

Payroll Regulations Timeline

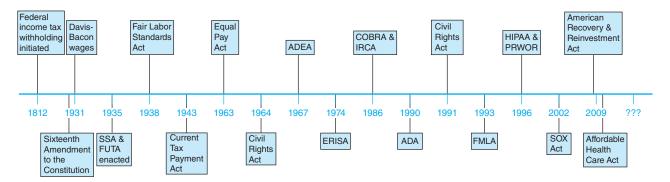


FIGURE 1-1
Timeline of Payroll Legislation.

During the Great Depression of the 1930s, the stock market collapsed, financial institutions went bankrupt, and companies released workers or ceased business operations. The government needed money to fund programs that would stimulate economic recovery. Additionally, the need for a social welfare system emerged as the number of displaced workers increased. The 1930s became a decade of landmark employment legislation that defined the legal environment for employers and employees, most of which remains enforced in 2015.

In 1931, Congress passed the *Davis-Bacon Act*, creating a standard of wages for governmental contracts more than \$2,000. The higher standard wages created under the Davis-Bacon Act brought additional revenue to small businesses and the communities where the workers on the contracts lived, bought groceries, and purchased other services or goods. The Davis-Bacon Act combined more than 60 different federal statutes, providing a prevailing wage and wage classification strategy to guide employers and contractors.

In 1935, the **Social Security Act** (**SSA**), also known as the **Federal Insurance Contributions Act** (**FICA**), established a contribution-driven fund that would help the average U.S. worker achieve a level of financial stability when he or she became too old or infirm to work. A contribution-driven fund's employees and employers pay a percentage of gross earnings into the Social Security fund. Originally, the fund was designed to be earmarked for a specific individual upon retirement, but it now also provides assistance for families who experience diminished wages and working situations because of infirmity of the worker or a family member. Social Security is synonymous with **Old-Age**, **Survivors**, **and Disability Insurance** (**OASDI**).

Medicare tax, a government-mandated health insurance program for individuals older than 62 years of age, was also included in the SSA legislation. The viability of the Social Security and Medicare system has been debated in recent years because of changes in eligible recipients that are beyond the scope of the program's original purpose.

The *Walsh-Healey Public Contracts Act* of 1936 affected governmental contractors providing goods or services exceeding \$10,000. This act required companies to pay workers a minimum wage for all hours worked under 40 per week and time and a half (regular pay times 1.5) per hour for any hours over 40 per week. The Walsh-Healey Act also prohibited the employment of individuals younger than 16 years of age. Compliance with this act is enforced through the Employment Standards Administration Wage and Hour Division of the Department of Labor. These standards also apply to workers within the District of Columbia.

As another part of its social welfare legislation, the U.S. Congress passed the *Federal Unemployment Tax Act (FUTA)* along with the **Social Security Insurance (SSI) Act** as a way to help displaced workers, individuals from the workforce who find themselves unemployed and meet certain state or federal qualifications. FUTA and its state counterpart, *SUTA*, are based upon the wages earned by the employees. Unlike Social Security taxes, only employers pay FUTA. Some states require employers and employees to



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