

Avoiding Payroll Pitfalls: What Every Nonprofit Needs to Know

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Mission of Pro Bono Partnership of Atlanta:

To maximize the impact of pro bono engagement by connecting a network of attorneys with nonprofits in need of free business legal services.

Pro Bono Partnership of Atlanta Eligibility & Other Information

- In order to be a client of Pro Bono Partnership of Atlanta, an organization must:
 - Be a 501(c)(3) nonprofit.
 - Be located in or serve the greater Atlanta area.
 - Serve low-income or disadvantaged individuals.
 - Be unable to afford legal services.
- Our website www.pbpatl.org includes our Request for Legal Assistance and informational articles
- We host free monthly webinars on legal topics for nonprofits
 - To view upcoming webinars or workshops, visit the [Workshops Page](#)
 - Join our mailing list by emailing rla@pbpatl.org
- This workshop presents general guidelines for Georgia nonprofit organizations and should not be construed as legal advice. Always consult an attorney to address your particular situation.

Real Life Payroll Problems

- Nonprofit ran its own payroll. IRS said Forms 941 didn't match W-2s and sent a bill for \$170,000.
- Executive Director of nonprofit that shut down had to pay \$1000 for the nonprofit's unpaid unemployment.
- Contractor let go by a nonprofit filed for unemployment which kicked off an investigation by DOL and IRS and almost shut down the nonprofit.
- Nonprofit treated Executive Director as a contractor. IRS sent a \$30,000 bill that nonprofit cannot pay because all funding is from Federal grants.

Before you pay anyone, ask “Is this person a...?”

- Volunteer
- Intern
- Contractor
- Employee

“Is this person a...?”

- Volunteer
 - ✓ Don't pay volunteers anything; reimbursement is okay
- Intern
 - ✓ Paying stipends is risky
- Contractor
 - ✓ Make sure they qualify
- Employee
 - ✓ Also ask whether they are exempt or non-exempt

Tax Treatment of Payments to Employees

- Employers must take out Federal and State payroll taxes from wages and report wages on appropriate forms
- Definition of “wages” is very broad
- Virtually any form of “remuneration for services” to employees constitutes “wages” for payroll tax purposes, whether paid in cash, property, non-cash benefits or any other form, including:
 - ✓ Cash or benefits provided to a former employee
 - ✓ A holiday bonus
 - ✓ Gift cards

Exclusions from “Wages”

- Certain forms of compensation are excluded from the employee’s taxable income
- If excludable, the value of the benefit is not subject to payroll tax and generally not reported on W-2. Examples include:
 - Accident and health insurance benefits, which can include employer contribution to a “cafeteria plan” under section 125
 - Certain de minimis fringes such as personal use of a company photocopier and cell phone
 - Working condition fringes such as use of employer-provided vehicles for business purposes
 - Meals and lodging while traveling overnight on business
 - Employee’s business expense reimbursements
 - Qualified parking reimbursements (up to \$245/month)
 - Training, professional and educational programs

Employer's Obligation to Withhold Payroll Taxes on Taxable Wages

- Employers must collect Federal and State income tax withholding and the employee's share of Federal Insurance Contributions Act (FICA) taxes from wages at the time of payment
 - ✓ Employer remains secondarily liable if it fails to withhold these taxes from the employee's wages
- The Employer is also liable for employer's share of Federal Insurance Contributions Act taxes and any state unemployment taxes

Federal Insurance Contributions Act (FICA)

- Matching shares for employers and employees:
 - ✓ For Social Security taxes, 6.2% of wages up to annual wage base (e.g., \$113,700 for 2013)
 - Combined employer and employee Social Security tax rate of 12.4%
 - Payroll tax holiday expired at end of 2012
 - ✓ For Medicare taxes, 1.45% of *all* wages
 - Combined employer and employee Medicare tax rate of 2.9%
 - Additional Medicare taxes of 0.9% must be withheld by the employer on wages exceeding \$200,000 for the calendar year
 - Employer is not required to match this additional 0.9% Medicare tax

Unemployment Taxes

- 501(c)(3) nonprofit organizations are not required to pay federal unemployment taxes, but nonprofits may still be subject to state unemployment tax
- Georgia nonprofits are responsible for unemployment insurance coverage if they employ four or more workers in each of 20 different weeks during a calendar year
- Nonprofits can pay for unemployment coverage through:
 - ✓ Georgia's unemployment tax system (State Unemployment Tax Act), **OR**
 - ✓ The "reimbursable" method under which the organization chooses to self-insure unemployment claims and reimburses the Georgia Department of Labor for the actual costs of those benefits that were paid by the State
- Nonprofits must notify Georgia Department of Labor of which method it chooses as soon as it reaches four employees

Payroll Tax Deadlines

- Withheld payroll taxes must be deposited promptly (sometimes by the close of the next business day!)
- Penalties for late filings.
 - ✓ Note: IRS can forgive late deposit penalties for “reasonable cause”

Failing to Treat Taxable Benefits as Wages

- Employer is secondarily liable for failing to pay income tax withholding and for employee's share of Federal Insurance Contributions Act taxes
- Employer is liable for failing to pay its share of Federal Insurance Contributions Act taxes and unemployment taxes
- Significant penalties can be assessed

Failing to Treat Taxable Benefits as Wages (cont'd)

- Potential personal liability of “responsible persons” for 100% of withheld payroll taxes.
 - ✓ Can include compensated Executive Directors and board members if they are connected to the nonprofit’s payroll tax procedures
 - ✓ Limited protection for uncompensated board members of exempt organizations
 - ✓ Note that officers can also have personal liability for unpaid unemployment taxes.

Payroll Tax Forms

- State forms
- Forms 941 – Employer’s Quarterly Return
- Form W-2, Wage and Tax Statement
- Aggregate Forms 941 for the year must reconcile with aggregate Form W-2 data filed with the Social Security Administration
- IRS has begun comparing Forms 941 against Forms 990
- Forms are very difficult to correct after filing
- Penalties for failing to file or filing late, or for filing incomplete or inaccurate statements

Best Practices: Review of Payroll Processes

- Compile list of benefits provided to employees and determine whether excluded from wages
- Review payroll processes (timing of deposits, filing of forms)
- Review reconciliation of Forms W-2 with Forms 941 and with Form 990
- Good documentation of procedures for administration of payroll and benefits is important “first line of defense” in IRS employment tax examination

Best Practices (cont'd)

- Consider using a payroll service
 - ✓ But remember employer is ultimately responsible
 - Double check filings with EFTPS
- Review worker classifications (employees vs. contractors)
 - ✓ Seek legal advice if there is any question about the classification

Who Are Your Employees?

- Employer is not responsible for payroll taxes if worker is a true independent contractor
- “Employee” defined
 - ✓ The ***right to direct and control*** a worker determines status for employment tax purposes
- Revenue Ruling 87-41 sets forth the 20 factors that the IRS takes into account when determining whether an employer/employee relationship exists or whether worker is an independent contractor

PBPA Resources

- [“Nuts and Bolts of Paying Employees”](#) article
- [“Classifying Employees as Workers or Independent Contractors”](#) article
- [“Wage and Hour Law for the Nonprofit Organization”](#) article
- [“Unemployment Insurance for Nonprofit Organizations”](#) article
- [“Employment Law 101: Classifying Workers”](#) webcast
- [“Employment Law 102: Employees and the Fair Labor Standards Act”](#) webcast
- [“Does Your Nonprofit Employ Four or More? Know Your Unemployment Obligations”](#) article
- [“Payroll Taxes: A Webinar to Help Your Nonprofit Understand What It Needs to Know About FICA Taxes and Income Tax Withholding”](#)

IRS Resources

- [IRS Pub. 15 – Circular E, Employer’s Tax Guide](#)
- [IRS Pub. 15-A – Employer’s Supplemental Tax Guide](#)
- [IRS Pub. 15-B – Employer’s Guide to Fringe Benefits](#)
- [“Independent Contractor or Employee? Training Materials,” IRS Training 3320-102 \(Rev. 10-96, TPDS 842381\)](#)
- [IRS website](#)

For More Information:

If you would like more information about the services of Pro Bono Partnership of Atlanta, contact us at:

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