

APPENDIX I

Payroll Accounting

ASSIGNMENT CLASSIFICATION TABLE

<u>Learning Objectives</u>	<u>Questions</u>	<u>Brief Exercises</u>	<u>Exercises</u>	<u>A Problems</u>	<u>B Problems</u>
1. Compute and record the payroll for a pay period.	1, 2, 3, 5, 6, 7, 8	1, 2	1, 2, 3, 4	1A, 2A, 3A	1B, 2B, 3B
2. Describe and record employer payroll taxes.	2, 3, 4, 8	3	3, 5	1A, 2A, 3A	1B, 2B, 3B
3. Discuss the objectives of internal control for payroll.	9, 10	4		4A	4B

ASSIGNMENT CHARACTERISTICS TABLE

Problem Number	Description	Difficulty Level	Time Allotted (min.)
I-1A	Prepare payroll register and payroll entries.	Simple	30–40
I-2A	Journalize payroll transactions and adjusting entries.	Moderate	30–40
I-3A	Prepare entries for payroll and payroll taxes; prepare W-2 data.	Moderate	30–40
I-4A	Identify internal control weaknesses and make recommendations for improvement.	Simple	20–30
I-1B	Prepare payroll register and payroll entries.	Simple	30–40
I-2B	Journalize payroll transactions and adjusting entries.	Moderate	30–40
I-3B	Prepare entries for payroll and payroll taxes; prepare W-2 data.	Moderate	30–40
I-4B	Identify internal control weaknesses and make recommendations for improvement.	Simple	20–30

ANSWERS TO QUESTIONS

1. Gross pay is the amount an employee actually earns. Net pay, the amount an employee is paid, is gross pay reduced by both mandatory and voluntary deductions, such as FICA taxes, union dues, federal income taxes, etc. Gross pay should be recorded as wages or salaries expense.
2. Both employees and employers are required to pay FICA taxes.
3. No. When an employer withholds federal or state income taxes from employee paychecks, the employer is merely acting as a collection agent for the taxing body. Since the employer holds employees' funds, these withholdings are a liability for the employer until they are remitted to the government.
4. FICA stands for Federal Insurance Contribution Act; FUTA stands for Federal Unemployment Tax Act; and SUTA stands for State Unemployment Tax Act.
5. A W-4 statement shows the employee's name, address, social security number, marital status and the number of allowances claimed for income tax withholding purposes. A W-2 statement contains the employee's name, address, social security number, wages, tips, other compensation, social security taxes withheld, wages subject to social security taxes, and federal, state and local income taxes withheld.
6. Payroll deductions can be classified as either mandatory (required by law) or voluntary (not required by law). Mandatory deductions include FICA taxes and income taxes. Examples of voluntary deductions are health and life insurance premiums, pension contributions, union dues, and charitable contributions.
7. The employee earnings record is used in: (1) determining when an employee has earned the maximum earnings subject to FICA taxes, (2) filing state and federal tax returns, and (3) providing each employee with a statement of gross earnings and tax withholdings for the year.
8. (a) The three types of taxes are: (1) FICA, (2) federal unemployment, and (3) state unemployment.
(b) The tax liability accounts are classified as current liabilities in the balance sheet. Payroll tax expense is classified under operating expenses in the income statement.
9. The main internal control objectives associated with payrolls are: (1) to safeguard company assets from unauthorized payments of payrolls and (2) to assure the accuracy and reliability of the accounting records pertaining to payrolls.
10. The four functions associated with payroll are: (1) hiring employees, (2) timekeeping, (3) preparing the payroll, and (4) paying the payroll.

SOLUTIONS TO BRIEF EXERCISES

BRIEF EXERCISE I-1

Gross earnings:		
Regular pay (40 X \$16).....	\$640.00	
Overtime pay (7 X \$24)	<u>168.00</u>	<u>\$808.00</u>
Gross earnings		\$808.00
Less: FICA taxes payable (\$808 X 7.65%).....	\$ 61.81	
Federal income taxes payable.....	<u>95.00</u>	<u>156.81</u>
Net pay		<u>\$651.19</u>

BRIEF EXERCISE I-2

Jan. 15	Salaries and Wages Expense	808.00	
	FICA Taxes Payable (\$808 X 7.65%)		61.81
	Federal Income Taxes Payable		95.00
	Salaries and Wages Payable		651.19
Jan. 15	Salaries and Wages Payable.....	651.19	
	Cash.....		651.19

BRIEF EXERCISE I-3

Jan. 31	Payroll Tax Expense.....	10,941.50	
	FICA Taxes Payable (\$79,000 X 7.65%)		6,043.50
	Federal Unemployment Taxes Payable (\$79,000 X .8%).....		632.00
	State Unemployment Taxes Payable (\$79,000 X 5.4%)		4,266.00

BRIEF EXERCISE I-4

- | | |
|-----------------|---------------------------|
| (a) Timekeeping | (c) Preparing the payroll |
| (b) Hiring | (d) Paying the payroll |

SOLUTIONS TO EXERCISES

EXERCISE I-1

- (a) 1. Regular 40 X \$14.00 = \$560.00
Overtime 6 X \$21.00 = 126.00
Gross earnings \$686.00
2. FICA taxes—\$52.48 = (\$686 X 7.65%).
3. Federal income taxes \$29.
4. State income taxes \$13.72 = (\$686 X 2%).
5. Net pay \$560.80 = (\$686.00 – \$52.48 – \$29.00 – \$13.72 – \$30.00).

(b) Salaries and Wages Expense	686.00	
FICA Taxes Payable		52.48
Federal Income Taxes Payable		29.00
State Income Taxes Payable		13.72
Health Insurance Payable.....		30.00
Salaries and Wages Payable		560.80

EXERCISE I-2

- J. Seligman \$4,500 X 7.65% = \$344.25 Seligman's total gross earnings for the year are \$98,000 (\$93,500 + \$4,500), which is below the \$117,000 maximum for FICA taxes.
- R. Eby (\$3,400 X 6.2%) + (\$4,500 X 1.45%) = \$276.05. Eby's total gross earnings for the year are \$113,600. Thus, only \$3,400 of the gross earnings for this pay period are subject to Social Security taxes. In addition, \$4,500 is subject to Medicare (1.45%) taxes.
- L. Marshall (\$1,900 X 6.2%) + (\$4,500 X 1.45%) = \$183.05. Marshall's total gross earnings for the year are \$115,100. Thus, only \$1,900 of the gross earnings for this pay period are subject to Social Security taxes. In addition, \$4,500 is subject to Medicare taxes.

T. Olson

($\$4,500 \times 1.45\%$) = \$65.25 Olson's gross earnings prior to this pay period exceed the maximum amount subject to Social Security taxes. However, all of the gross earnings in the December 31 pay period are subject to Medicare taxes.

EXERCISE I-3

(a) See next page.

(b)	Jan. 31	Salaries and Wages Expense.....	1,688.00	
		FICA Taxes Payable		129.13
		Federal Income Taxes Payable		135.00
		Health Insurance Payable		53.00
		Salaries and Wages Payable		1,370.87

(a)

WELSTEAD COMPANY
Payroll Register
For the Week Ending January 31

<u>Employee</u>	<u>Total Hours</u>	<u>Earnings</u>		<u>Gross Pay</u>	<u>Deductions</u>				<u>Net Pay</u>
		<u>Regular</u>	<u>Overtime</u>		<u>FICA Taxes</u>	<u>Federal Income Taxes</u>	<u>Health Insurance</u>	<u>Total</u>	
W. Jeong	44	\$ 440.00	\$ 66.00	\$ 506.00	\$ 38.71	\$ 34.00	\$18.00	\$ 90.71	\$ 415.29
C. Garrison	42	520.00	39.00	559.00	42.76	43.00	15.00	100.76	458.24
J. Buss	43	560.00	63.00	623.00	47.66	58.00	20.00	125.66	497.34
Totals		<u>\$1,520.00</u>	<u>\$168.00</u>	<u>\$1,688.00</u>	<u>\$129.13</u>	<u>\$135.00</u>	<u>\$53.00</u>	<u>\$317.13</u>	<u>\$1,370.87</u>

EXERCISE I-3 (Continued)

(b)	Jan. 31	Payroll Tax Expense	233.78	
		FICA Taxes Payable.....		129.13
		Federal Unemployment Taxes Payable (\$1,688 X .8%)		13.50
		State Unemployment Taxes Payable (\$1,688 X 5.4%)		91.15

EXERCISE I-4

- (a) (1) \$1,100 [\$10,000 see (2) below – \$8,900].
(2) \$10,000 (FICA taxes \$765 ÷ 7.65%).
(3) \$400 (\$10,000 X 4%).
(4) \$2,660 (\$10,000 – \$7,340).
(5) \$6,000(\$10,000 – \$4,000).

(b)	Feb. 28	Salaries and Wages Expense.....	10,000	
		FICA Taxes Payable		765
		Federal Income Taxes Payable.....		1,395
		State Income Taxes Payable.....		400
		Union Dues Payable		100
		Salaries and Wages Payable		7,340
	28	Salaries and Wages Payable	7,340	
		Cash		7,340

EXERCISE I-5

(a)	FICA tax (\$789,000 X 6.2%) + (\$850,000 X 1.45%) ...	\$61,243
	SUTA tax (\$70,000 X 5.4%).....	3,780
	FUTA tax (\$70,000 X 0.8%).....	560
	Total payroll tax	<u>\$65,583</u>
(b)	Payroll Tax Expense	65,583
	FICA Taxes Payable.....	61,243
	State Unemployment Taxes Payable.....	3,780
	Federal Unemployment Taxes Payable.....	560

SOLUTIONS TO PROBLEMS

PROBLEM I-1A

(a)

ETHRIDGE DRUG STORE
Payroll Register
For the Week Ended February 15, 2017

		Earnings			Deductions					Net Pay
		Regular	Over-time	Gross Pay	FICA	Fed.	State	U.F.	Total	
<u>Employee</u>	<u>Hours</u>									
A. Joseph	38	532.00	0	532.00	40.70	22.00	15.96	0	78.66	453.34
J. Wilgus	42	520.00	39.00	559.00	42.76	9.00	16.77	5.00	73.53	485.47
P. Kirk	44	480.00	72.00	552.00	42.23	57.00	16.56	7.50	123.29	428.71
L. Zhang	48	480.00	144.00	624.00	47.74	52.00	18.72	5.00	123.46	500.54
Totals		<u>2,012.00</u>	<u>255.00</u>	<u>2,267.00</u>	<u>173.43</u>	<u>140.00</u>	<u>68.01</u>	<u>17.50</u>	<u>398.94</u>	<u>1,868.06</u>

PROBLEM I-1A (Continued)

(b)	Feb. 15	Salaries and Wages Expense.....	2,267.00	
		FICA Taxes Payable		173.43
		Federal Income Taxes Payable		140.00
		State Income Taxes Payable		68.01
		United Fund Contributions Payable		17.50
		Salaries and Wages Payable		1,868.06
15		Payroll Tax Expense	313.99	
		FICA Taxes Payable (\$2,267 X 7.65%)		173.43
		Federal Unemployment Taxes Payable (\$2,267 X .8%)		18.14
		State Unemployment Taxes Payable (\$2,267 X 5.4%)		122.42
(c)	Feb. 16	Salaries and Wages Payable.....	1,868.06	
		Cash		1,868.06
(d)	Feb. 28	FICA Taxes Payable (\$173.43+ \$173.43)	346.86	
		Federal Income Taxes Payable	140.00	
		Cash		486.86

PROBLEM I-2A

(a)	Jan. 10	Union Dues Payable	250.00	
		Cash		250.00
12		FICA Taxes Payable	662.20	
		Federal Income Taxes Payable	1,254.60	
		Cash		1,916.80
15		U.S. Savings Bonds Payable	350.00	
		Cash		350.00
17		State Income Taxes Payable	102.15	
		Cash		102.15
20		Federal Unemployment Taxes Payable	312.00	
		State Unemployment Taxes Payable	1,954.40	
		Cash		2,266.40
31		Salaries and Wages Expense	46,200.00	
		FICA Taxes Payable		3,534.30
		Federal Income Taxes Payable		1,770.00
		State Income Taxes Payable		360.00
		Union Dues Payable		400.00
		United Fund Contributions Payable		1,800.00
		Salaries and Wages Payable .		38,335.70
31		Salaries and Wages Payable	38,335.70	
		Cash		38,335.70

PROBLEM I-2A (Continued)

(b)	Jan. 31	Payroll Tax Expense	6,398.70
		FICA Taxes Payable	
		(\$46,200 X 7.65%)	3,534.30
		Federal Unemployment Taxes	
		Payable (\$46,200 X .8%)	369.60
		State Unemployment Taxes	
		Payable (\$46,200 X 5.4%)	2,494.80

PROBLEM I-3A

(a) Salaries and Wages Expense.....	490,000	
FICA Taxes Payable		35,005*
Federal Income Taxes Payable.....		108,000
State Income Taxes Payable		12,740
United Fund Contributions Payable.....		25,000
Health Insurance Payable		26,800
Salaries and Wages Payable		282,445

(b) Payroll Tax Expense	38,635	
FICA Taxes Payable		35,005*
Federal Unemployment Taxes Payable		
(\$110,000 X .8%)		880
State Unemployment Taxes Payable		
(\$110,000 X 2.5%)		2,750

***(\$45,000 X 6.2%) + (\$490,000 X 1.45%)**

(c)					
	Wages, Tips, Other Compensation	Federal Income Tax Withheld	State Income Tax Withheld	FICA Wages	FICA Tax Withheld
Employee					
S. Brand	\$56,000	\$18,500	\$1,456 (1)	\$56,000	\$4,284
R. Morin	27,000	11,000	702 (2)	27,000	2,066

(1) \$56,000 X 2.6%.

(2) \$27,000 X 2.6%.

PROBLEM I-4A

(a) <u>Weaknesses</u>	(b) <u>Recommended Procedures</u>
<p>1. ▶ Hours worked are marked on time card by employee.</p> <p> ▶ Employees give the approved cards to payroll.</p>	<p>▶ Time cards should be punched by a time clock and the punching of the clock by employees should be supervised so that one employee cannot punch more than one card.</p> <p>▶ The manager should deliver the cards to payroll in order to prevent possible alterations by employees during delivery.</p>
<p>2. ▶ Department manager indicates the rates of pay.</p> <p> ▶ The department manager pays the employees.</p> <p> ▶ Payment is in cash.</p>	<p>▶ Rates of pay should be authorized in writing by the human resources department.</p> <p>▶ The treasurer's department should pay employees.</p> <p>▶ Payment should be made by check.</p>
<p>3. ▶ Manager prepares payroll register which is sent to the payroll department.</p> <p> ▶ A payroll supervisor pays each employee by check.</p>	<p>▶ The payroll department should prepare the payroll register on the basis of the clock cards approved by the manager.</p> <p>▶ Payment to employees should be made by the treasurer's department.</p>

(a)

RALPH'S HARDWARE
Payroll Register
For the Week Ending March 15, 2017

		Earnings			Deductions					Net Pay
		Regular	Over-time	Gross Pay	FICA	Fed.	State	U.F.	Total	
Employee	Hours									
K. Litwack	40	600.00	0	600.00	45.90	38.00	27.00	5.00	115.90	484.10
E. Burgess	46	520.00	117.00	637.00	48.73	24.00	28.67	5.00	106.40	530.60
R. Perez	44	520.00	78.00	598.00	45.75	60.00	26.91	8.00	140.66	457.34
H. Hosseini	48	520.00	156.00	676.00	51.71	67.00	30.42	5.00	154.13	521.87
Totals		<u>2,160.00</u>	<u>351.00</u>	<u>2,511.00</u>	<u>192.09</u>	<u>189.00</u>	<u>113.00</u>	<u>23.00</u>	<u>517.09</u>	<u>1,993.91</u>

PROBLEM I-1B (Continued)

(b)	Mar. 15	Salaries and Wages Expense.....	2,511.00	
		FICA Taxes Payable		192.09
		Federal Income Taxes Payable		189.00
		State Income Taxes Payable		113.00
		United Fund Contributions Payable		23.00
		Salaries and Wages Payable		1,993.91
	15	Payroll Tax Expense	347.77	
		FICA Taxes Payable (\$2,511 X 7.65%)		192.09
		Federal Unemployment Taxes Payable (\$2,511 X .8%)		20.09
		State Unemployment Taxes Payable (\$2,511 X 5.4%)		135.59
(c)	Mar. 16	Salaries and Wages Payable.....	1,993.91	
		Cash		1,993.91
(d)	Mar. 31	FICA Taxes Payable (\$192.09 + \$192.09)	384.18	
		Federal Income Taxes Payable	189.00	
		Cash		573.18

PROBLEM I-2B

(a)	Jan. 10	Union Dues Payable	740.00	
		Cash		740.00
12		FICA Taxes Payable	760.00	
		Federal Income Taxes Payable	1,204.60	
		Cash		1,964.60
15		U.S. Savings Bonds Payable	360.00	
		Cash		360.00
17		State Income Taxes Payable	108.95	
		Cash		108.95
20		Federal Unemployment Taxes Payable	288.95	
		State Unemployment Taxes Payable	1,954.40	
		Cash		2,243.35
31		Salaries and Wages Expense	50,600.00	
		FICA Taxes Payable		3,871.00
		Federal Income Taxes Payable		1,958.00
		State Income Taxes Payable		414.00
		United Fund Contributions Payable		1,888.00
		Union Dues Payable		400.00
		Salaries and Wages Payable .		42,069.00
31		Salaries and Wages Payable	42,069.00	
		Cash		42,069.00

PROBLEM I-2B (Continued)

(b)	1. Jan.	31	Payroll Tax Expense	7,008.20	
			FICA Taxes Payable		
			(\$50,600 X 7.65%)		3,871.00
			Federal Unemployment Taxes		
			Payable (\$50,600 X .8%)		404.80
			State Unemployment Taxes		
			Payable (\$50,600 X 5.4%)		2,732.40

PROBLEM I-3B

(a) Salaries and Wages Expense.....	570,000	
FICA Taxes Payable		37,405
Federal Income Taxes Payable.....		168,000
State Income Taxes Payable		18,240
United Fund Contributions Payable.....		27,500
Health Insurance Premiums Payable		32,200
Salaries and Wages Payable		286,655
 (b) Payroll Tax Expense	 41,530	
FICA Taxes Payable		37,405*
Federal Unemployment Taxes Payable		
(\$125,000 X .8%)		1,000
State Unemployment Taxes Payable		
(\$125,000 X 2.5%)		3,125

*($\$470,000 \times 6.2\%$) + ($\$570,000 \times 1.45\%$)

(c)					
	Wages, Tips, Other Compensation	Federal Income Tax Withheld	State Income Tax Withheld	FICA Wages	FICA Tax Withheld
Employee					
Jin Chien	\$59,000	\$19,500	\$1,888 (1)	\$59,000	\$4,514
Nina Harris	28,000	7,200	896 (2)	28,000	2,142

(1) $\$59,000 \times 3.2\%$.

(2) $\$28,000 \times 3.2\%$.

PROBLEM I-4B

(a) <u>Weaknesses</u>	(b) <u>Recommended Procedures</u>
1. <ul style="list-style-type: none">▶ Department managers have too much authority in hiring.▶ An interview should not be the sole basis for hiring or rejecting an applicant.▶ The pay rate should not be manually written on the W-4 form.	<ul style="list-style-type: none">▶ The human resources department should do the hiring.▶ The qualifications of each applicant should be determined and letters of recommendation should be obtained.▶ The human resources department should notify the payroll department of new hires through a hiring authorization form.
2. <ul style="list-style-type: none">▶ The chief accountant manually signs the payroll checks.▶ The department managers distribute the payroll checks.▶ The department managers retain custody of unclaimed checks.	<ul style="list-style-type: none">▶ The treasurer should sign the payroll checks.▶ A representative of the treasurer's department should distribute the payroll checks.▶ A representative of the treasurer's department should have custody of unclaimed checks.

PROBLEM I-4B (Continued)

(a) Weaknesses

3. ▶ The assignment of duties among the payroll clerks does not result in any independent internal verification.

(b) Recommended Procedures

- ▶ The duties of the payroll clerks should be assigned so that one clerk computes gross earnings for all employees. Then the computations made should be verified by the clerk that did not make the initial determination of the data. Each month the duties of the clerks should be reversed.