

NEW BUSINESS MINNESOTA

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Hiring Your First Employee

For Guidance on this Important Event, Turn to the Experts Who Wrote the Book on Preparing, Managing and Providing for Your First Employee: **Jessica White**, JW Employment Law Center; **Drew Davis**, Wells Fargo Business Payroll Services; **Bryan Cremeen**, AccountSource LLC; and **Michael Happe**, SFM Companies.

As You Consider Hiring Your First Employee, Avoid the Costly Missteps in Hiring, Managing and Meeting All Government Requirements. These Employment Experts Will Help You Get Up to Speed.



From the Publisher:

You started your venture with a solid plan to develop your niche and grow your business. If you're on track, you are going to grow and that means many of you are going to become employers...even in this harsh economy.

If you wait until your need to hire is so great that you need someone Monday, you haven't done your homework. It may be months more before you land that person who will join the effort. By preparing well in advance, studying and talking with experts, you will be ready when the time comes, when that opportunity is suddenly knocking at your door.

New Business Minnesota approached the experts on these pages to help write "the book" on *Hiring Your First Employee* as a primer for new business. Each has prepared a Chapter that will help lead you to a broader understanding of the downside as well as the upside in building your staff.

Whether you have already made that hire and need to be reminded that there are some steps you missed or are anticipating the approaching first employee, these Chapters will serve you well.

The authors will share more information in a free interactive workshop July 21 at the Airport Hilton, Bloomington. For more information and to register for this event, go to www.newstartupmeetup.com.



Chapter 1

Human Resources / Employment Law

**Preparation is
Key to Successful Hiring**
Review This Outline Before You
Make That First Hire; Avoid
Common Pitfalls.

By Jessica White

When you become an employer, you enter a new world with lots of responsibilities. I often say that in many ways, having employees is like having children – it's important to establish and clearly communicate rules, policies, expectations, rewards, and consequences.

While it is tempting to focus solely on sales and growth, employers, like parents, cannot ignore their responsibilities – in this case, complying with the many state and federal laws governing the employment relationship.

If you are planning on hiring employees, take some time to think through the issues addressed below.

Remember that there is a beginning and an ending to every employment relationship. If you fail to prepare up front, it will come back to haunt you, typically in the form of legal problems. If you take the time to prepare, you will fare much better when problems inevitably occur and protect yourself from liability.

After years of helping new and small businesses with their HR and Employment Law needs, I know that a surprising number don't have the necessary policies and procedures in place. Many businesses simply hire the employee and order business cards without any further planning. As you plan for your business to grow, make sure you establish policies and procedures and be aware of the key issues addressed here.

Classification Issues

While many employers classify workers as Independent Contractors to save money, the law defines Independent Contractors as well as the way in which they must be treated. Employers who misclassify workers as Independent Contractors will be responsible for unpaid taxes, Unemployment Insurance, and Workers' Compensation. In general, if a worker is receiving significant work direction from the employer, he/she is probably an employee and should be classified accordingly.

Employers must also decide whether an employee will be salaried (exempt from overtime

requirements) or hourly (entitled to overtime). The law restricts the types of employees who can be salaried, and employers who misclassify employees as salaried will be responsible for two to three years of back overtime. While there are exceptions, employees who lack the authority to hire and fire are typically entitled to overtime pay.

Job Descriptions

When preparing to hire employees, it is important to create written Job Descriptions for each position. Well-written Job Descriptions help you advertise the position, choose the right candidate, and evaluate the employee's performance once hired. Job descriptions should summarize the essential job duties; describe the work environment and physical requirements; and list the required experience, education, and technical skills.

Lawful Hiring Practices

Because hiring decisions can create liability for an employer, it is important to conduct and document your hiring process in a lawful manner. The hiring process includes advertising the job, the application process, the interview process, the hiring decisions, the offer, and pre-employment screening.

We always train our clients on how to conduct and document their hiring process to ensure that they are complying with the law, making the right hiring decisions, and documenting their process in a way that will protect them if a candidate files a claim against them.

Every step of the hiring process should be conducted with the goal of finding the candidate that is the most qualified and is the best fit for the position and the company. At each step, questions asked of the candidates and criteria used must be focused on the candidate's ability to do the job.

Offers should be made in writing and include the position, wage, and starting date. Because pre-employment screening such as criminal background checks, reference checks, and drug and alcohol screening cannot be completed until an offer has been made, offer

letters should also make it clear that the offer is contingent upon the successful completion of these checks.

Employee Handbook

The most important tool for an employer is the Employee Handbook, the requirements for which vary by state. Employee Handbooks include policies on many topics including attendance; vacation/PTO (paid time off); computer and internet usage; dress code; time reporting; leave; and much more.

Because every company has its own culture and needs, we customize every client's Handbook, making them more helpful, effective, and well received by employees compared to generic, "boiler-plate" Handbooks.

Performance Evaluations

A performance evaluation system is critical for all employers but can seem overwhelming. The most important thing about evaluations is to use as many objective, measurable criteria as possible so that employees receive specific feedback.

We routinely help our clients turn criteria that seem subjective and unmeasurable into objective, measurable criteria. Once the structure and evaluation criteria have been determined, performance evaluations become much less scary and overwhelming.

Terminations

If you hire employees, you will eventually need to terminate one. While terminations are stressful for everyone involved, there are things you can do to minimize both the stress and the potential legal risks associated with terminations.

The best advice is to document the reason for the termination, whether the reason is attendance, performance or behavior.

You should also know that in Minnesota, terminated employees are entitled to a copy of their personnel file and a written explanation of the reason for the termination. They are also entitled to their final paycheck, including any unused vacation/PTO, within 24 hours.

In order to minimize the employee's anger and make things easier for everyone, we always recommend having a copy of the personnel file, termination letter, and final paycheck ready to hand to the employee when the termination is communicated.

Conclusion

Even for established businesses, it's normal to feel overwhelmed by all the laws governing the employment relationship. These laws change routinely and continue to become more and more complex. As a result, it has become increasingly common for new and small businesses to utilize HR Consultants and Employment Attorneys to help them with their role as an employer.

One of the strengths of new and small businesses is their legendary nimbleness, the ability to react quickly to opportunities and chal-

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Chapter 4 Workers' Comp

Most Employers Are Required to Carry Workers' Compensation Insurance
State Law Demands You Protect Your Workers. Workers' Compensation Insurance Is Complicated to Figure Out for Novices. That's Why There Are Experts.

By Michael Happe, CPCU, SFM Companies

One of the most important things to consider when hiring your first employee is workers' compensation insurance. Required by state law, this insurance protects employees who are injured on the job by providing coverage for medical treatment and paying a portion of employees' lost wages if they are not able to work as a result of the injury.

All Minnesota employers, with limited exceptions, are subject to the Minnesota Workers' Compensation Act and are required to purchase workers' compensation insurance.

Under the Act, the term "employer" means any person who employs another to perform services for hire. This includes a corporation, limited liability company, partnership, sole proprietorship, association, the state and any governmental subdivision, such as counties, cities, towns and school districts. Any employer who has one or more employees is subject to the workers' compensation law.

Employees are generally defined as persons performing services for another, including minors and undocumented aliens. There is no minimum number of employees an employer must have before workers' compensation coverage is required: An employer with only one part-time employee generally must provide coverage.

There are some important, but notable, exceptions to these rules, which is why it's valuable to work with an agent experienced in

workers' compensation.

Exceptions to the Act

Family businesses – Small business owners and certain family members who work for them are exempt from workers' compensation coverage requirements. For example, a sole proprietor is not required to obtain coverage for himself or for his spouse, parents or children.

Similarly, a partnership is not required to provide coverage for its partners or for any partner's spouse, parent or child employed by the partnership.

Executive officers of closely held corporations and managers of limited liability companies are also excluded from coverage if certain conditions are met with respect to size of payroll and ownership interest.

Nonprofit organizations – A nonprofit organization, regardless of its purpose or cause, is subject to the workers' compensation laws and must maintain workers' compensation insurance if it pays more than \$1,000 in salaries or wages in any year. No nonprofit organizations are exempt from this requirement.

Independent contractors – Minnesota's law excludes independent contractors from workers' compensation coverage. The Minnesota Department of Labor and Industry has issued detailed rules to help employers determine whether a particular worker is exempted as an independent contractor. There are special, even more stringent statutory provisions regarding

independent contractors in the construction business.

The most important factor in determining whether a worker is an independent contractor is the amount of control the employer exerts over the manner in which the person performs his or her work. Employers should never assume that someone who represents himself as an independent contractor is not an employee for purposes of workers' compensation coverage.

Casual employees – Another category of worker not entitled to workers' compensation benefits is the casual employee. For this exception to apply, the employment relationship must be casual and not in the usual course of the employer's trade, business or occupation.

Courts have interpreted "casual" to mean work that is not performed on a regular basis and that is not permanent or continuous. For example, a man who was a property manager for a circus one week during the year was deemed a casual employee. This exception is rare and should be applied only with the advice of an attorney.

Penalties

Failing to insure employees, regardless of whether an injury has occurred, can result in costly fines and potential lawsuits.

The Minnesota Department of Labor and Industry may order the employer to pay a penalty of up to \$1,000 per employee for each week the required insurance has not been in place.

If a work-related injury occurs, the employee is entitled to have the Minnesota Special Compensation Fund pay his or her workers' compensation benefits. The fund will then pursue reimbursement from the uninsured employer along with a penalty of 65 percent of the amount of the benefits.

Additionally, an injured employee may elect to sue the uninsured employer in a civil action often resulting in an amount awarded that's substantially higher than the workers' compensation benefits due.

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lenges. Nothing can knock a small business off balance faster than problems with employees, which often result in lost time, money, energy and opportunity.

Being aware of the suggestions above should give you a modest foundation as you prepare for that first hire. Just remember that like in many other areas of business, preparation is the key.

Jessica White, President of the JW Employment Law Center, spent seven years in corporate Human Resources in companies of all sizes, where she focused on staffing/recruiting, employee relations, and corporate training. With an undergraduate degree in Business Management with an emphasis in Human Resources, Jessica went on to become a licensed attorney

practicing in the area of Employment Law. Three years ago, Jessica started her own firm, where she helps small and start-up businesses by establishing customized policies and procedures and training Managers on their responsibilities as an employer. She can be reached at (612) 414-1999 or jessica@jwemploymentlawcenter.com. www.jwemploymentlawcenter.com.



Chapter 3 Payroll Services

Why Payroll Is Best Left to the Professionals
Expensive Penalties, Complex Regulations and the IRS Are Major Payroll Challenges.

By Drew Davis
Wells Fargo Business Payroll Services

Whether your business is a start-up or an established firm, you face an exacting yet essential challenge – payroll processing.

As if meeting the costs of each payroll weren't challenge enough, you also must meet strict deadlines, maintain meticulous records and obey the often confusing reporting and depository rules of federal, state, and increasingly often, local government agencies.

Employers must calculate, withhold and deposit their employees' share of income taxes, Social Security and Medicare payments accurately and on time with the appropriate agencies. And they must calculate their share of employment taxes – including Social Security and Medicare, federal unemployment insurance and state unemployment and disability insurance taxes.

One in three small businesses has been penalized at least once for missing payroll tax filing deadlines, and the penalties for incorrect withholding of income taxes can be severe.

Government agencies aren't your only taskmasters – your employees also expect to be paid on time – every time – and they assume that their federal and state income taxes, Social Security and Medicare payments will be calculated and deducted correctly from their gross pay. And that is just the beginning – deductions for health care benefits, pre-tax and after-tax 401(k) contributions, loan payments and other adjustments also must be accurate and timely.

Clearly, administering payroll is a complex job. It requires experienced profession-

als to keep abreast of ever-changing federal and state tax regulations and to process paychecks, deposit taxes and fill out the appropriate forms. While some large organizations with complex payroll processes may prefer to keep this function in-house, more and more small and medium-size companies are turning to independent payroll processors to get the job done.

A professional payroll service can help your company avoid penalties, provide the reliable pay processing your employees expect and deserve and – an important plus – allow you to focus on growing your business.

Outside payroll vendors provide a range of services including calculating and withholding employee tax payments, generating checks, depositing payments and preparing federal and state tax forms such as W-2s and 1099s. They also can calculate 401(k) and other deductions, produce employee earnings statements, develop payroll reports, calculate tax liabilities for various states and file required tax forms.

There are many advantages to outsourcing payroll processing to a qualified independent provider. For example, you can:

- Concentrate your resources on your core business.
- Count on accurate payroll tax liability calculations.
- Let payroll professionals do the time-consuming research needed to keep current on changing tax laws.
- Be assured your payroll function is in compliance with regulations.

When choosing a payroll vendor, look for

an experienced company with a strong reputation – a company that stands behind its work so you can be confident that your payroll tax deposits and filings will meet federal and state regulations. Look for a company that assumes complete responsibility for any errors on its part, and one that can answer inquiries from tax agencies on your behalf.

The organization also should have: the necessary security measures in place to keep your employees' personal information secure; electronic tax filing capability; a customer service call center that enables you to get answers about paychecks, earning statements and tax filings; and the capability to produce accurate and on-time W-2 and 1099 forms.

Another important consideration when choosing a payroll vendor is cash flow management. Ask the organization when they will debit the bank account funding your payroll to cover your payroll and tax liabilities, and how they will communicate with you and your bank should your bank account be improperly funded.

In addition, a payroll vendor should demonstrate flexibility and an ability to adapt to meet your company's changing needs. For example, as your company grows and adds employees, you may need additional services such as workers' compensation insurance, 401(k) plans, human resources and benefits services. And the provider should offer you a variety of options that will meet your business needs such as, how you transmit payroll information – by phone, fax, e-mail or the Internet, and who prints your paychecks and payroll reports – you or your payroll vendor.

Selecting the right vendor is vital, because it requires sharing of confidential company information. And look for a company with an established track record of excellence – someone you can trust as a long-term partner. Once you've made this important decision and handed over payroll processing to the pros, you can focus on what matters most – growing your core business.

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Chapter 2 Accounting

Start Planning Early for Your New Employee Know the True Cost of Hiring and the Regulations You Must Comply With.

By Bryan Cremeen
AccountSource LLC

Hiring your first employee brings many new challenges and opportunities to you and your business.

If you're hiring sales or marketing person, there is the prospect of increased revenue coming your way. If it is an administrative person hired in response to growing demand for your product or services, it means you are building a foundation that will support that growth.

Although hiring is always a good sign, especially in the current economy, it can easily become a nightmare if you're not prepared.

Planning for the New Hire

It's surprising how many new entrepreneurs fail to plan for the full costs and administrative burdens – not to mention complying with the numerous reporting requirements – associated with hiring an employee.

That's why we highly recommend new business owners consult with their professional business advisors well in advance to make sure they address all the administrative and financial issues. Don't wait until the last minute.

Federal and state governments each have their own requirements for the hiring of an employee. Before you hire your first employee, you are required to obtain a Federal Employer Identification Number (FEIN) and a Minnesota taxpayer identification number.

The employee will also need to fill out a W-4 to determine their tax withholding and an I-9 to verify they are allowed to work in the United States.

Minnesota also requires that you register the new employee with the Department of Human Services and the MN Department of

Employment and Economic Development (DEED) for the unemployment insurance program.

The Actual Cost of an Employee

Financially, the cost of hiring an employee extends beyond the paycheck your employee will receive. As the employer, you are responsible for the employer's share of social security and Medicare taxes (FICA), unemployment insurance for both the federal and state, and workers compensation insurance.

There are also costs for finding the employee, office space, supplies and equipment that the employee will need to perform their job.

Wages that are subject to these taxes may include salaries, vacation benefits, bonuses, commission and fringe benefits. They may also include non-cash payments such as property, lodging, food, clothing, or vehicle allowances.

As you are planning your hire, make sure to include all these additional costs to your budget to ensure that your cost-benefit is sufficient. Too many new owners forget to include the complete costs. They put in a \$24,000 salary because that's what they are planning to offer. That kind of thinking will get your business into a lot of trouble.

In order to reduce your tax liability, you may want to consider hiring your minor child. If your business is a sole proprietorship or partnership, you are not subject to Social Security or Medicare taxes on any wages paid to your child who is under the age of 18.

As long as the child works in your business, for your business, and is paid by your business, you may deduct your child's wages from your income. This is an opportunity to

reduce the amount of self-employment tax that you may have to pay at the end of the year.

Reporting and Remittance Requirements

Every employer is required to withhold income and FICA taxes every pay period from their employees. Depending on the amount of the withholding, you must remit the withheld taxes to the appropriate government agency based on their payment schedule.

At the end of each quarter, you must report the amount of wages you paid your employees and any withholding to the IRS using Form 941 and the State of Minnesota using their online reporting system.

You are also required to report Minnesota unemployment on a quarterly basis using a separate system run by MN DEED. FUTA is reported on an annual basis to the IRS using Form 940.

By January 31 of each year, employers are required to send out W-2s to every employee that earned income in the prior year. They are also required to submit the W2s to both the State of Minnesota and the Social Security Administration.

Failure to file the required forms by their due dates may result in penalties and interest being charged to your company.

There are many government agencies involved in reporting income to employees and many employers get "stung" by not planning for all the costs and reporting burdens required of them.

Conclusion

Obviously this column is a brief overview of some of the challenges you'll have to consider. I strongly recommend you work with a qualified accountant who can assist you in the planning of your new hire in order to reduce the chance of getting "stung."

Bryan Cremeen is the founder and partner of AccountSource LLC. AccountSource LLC was established in 2004 to provide small businesses with tax, payroll, and bookkeeping solutions. He has a B.S. degree in Accounting and is currently an Enrolled Agent, Enrolled to Represent Taxpayers before the IRS. He is also currently a member of the National Association of Tax Professionals. He can be reached at (763) 786-1112. bcremeen@acctsource.com. www.acctsource.com.