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Chapter 14 – Payroll Compliance

14.1 Introduction

14.1.1 General

A significant percentage of the State of Delaware’s (State) annual operating budget is expended on Salaries and Other Employment Costs (OECs). Therefore, it is vital that the business processes associated with the administration of the State’s Payroll are grounded in strong policy with appropriate focus on regulatory requirements and internal controls.

The Division of Accounting (DOA) Payroll Compliance Group (PCG) provides information and guidance to State Organizations on how to properly administer Payroll functions while complying with applicable laws, rules, and regulations. Instructions in this chapter are in compliance with State of Delaware and Federal laws and regulations. State laws that apply to the administration of Payroll are found in Title 29 of the Delaware Code (Code). Specific Code references on a variety of topics may be found in PCG Bulletins accessible on the DOA website.

14.2 Payroll Expenditure Controls & Authorizations

14.2.1 Controls

DOA sets policies to ensure effective controls are in place governing all State financial activities including the expenditure of funds associated with the State’s Payroll process. For additional information about the payroll authorization process, refer to the PCG Payroll Policy: Payroll Expenditure Authorization (PCG-PRAUTH):

http://www.accounting.delaware.gov/payroll_comp/policies.shtml

Organizations are required to have in place and enforce effective internal controls to monitor Payroll-related transactions. These internal controls must be documented in a Payroll Internal Controls Plan on file with the Division of Accounting, Payroll Compliance Group. Controls must include, but are not limited to, the review and approval of all wage payments, preapproval of overtime, docking, and leave usage for employees.

Organizations should ensure an appropriate segregation of duties and monitoring throughout the payroll process. This includes establishing separate roles within the Organization for payroll approvers and payroll processors. Under no circumstances should an Organization’s payroll expenditures be approved by the individual who processes payroll transactions in the Payroll Human Resource Statewide Technology (PHRST) system for that pay period.

At a minimum, the following activities should be segregated:

- Segregate time-keeping and supervision functions from personnel, payroll processing, disbursement and general ledger functions.
- Individuals responsible for hiring, terminating and approving promotions should not be directly involved in preparing payroll transactions or inputting data.
- Individuals approving time sheets should not prepare or enter payroll transactions.
- Individuals performing payroll data entry should not have payroll approval authority.

Organizations that cannot segregate duties or implement appropriate controls must submit a written notice to the attention of the Director of Accounting acknowledging such control deficiencies. The memo must be signed by the Organization Head or Division Director.

14.2.2 Expenditures

Organizations have recurring biweekly funding expenditures related to the payment of salaries and premium pays (Shift, Hazard, Board Certified, etc.) owed to employees in authorized positions for time worked in the current pay period. These salary expenditures are approved in the annual Budget Appropriation Bill and by local School District authorities. Therefore, biweekly funding expenditures supporting these recurring payments are considered preapproved through those processes. All Organizations are expected to stay within their annual appropriations for salaries as well as authorized positions.

Organizations must use the **Confirm** version of the PHRST DocumentDirect report **DPR003 – Payroll Expenditures by Appropriation** to authorize payroll funding expenditures and certify that there are sufficient appropriated funds to cover the expenditures.

All payroll-related expenditures must be certified by an approving authority that the charges for the current pay period for the Organization meet all federal and state, legal and regulatory requirements and that the represented expenditures do not exceed the remaining balance of funds appropriated by the General Assembly.

Due to processes dependent upon the timely posting of the Payroll Journal to the General Ledger, the Director of the Division of Accounting, with the authority of the Secretary of Finance, approves and processes the Payroll Journal for the State of Delaware, through the State's financial management and accounting system, First State Financials (FSF), prior to the pay date on a biweekly basis with the expectation that Organizations follow the aforementioned laws and policies for the payment of salaries.

14.3 Payroll Signature Cards

Organizations submit new Payroll Signature Cards annually by July 1st. Organizations that fail to submit new Signature Cards by the July 1st deadline risk a negative finding in the annual CAFR audit. Cards are signed by all individuals authorized by the Organization Head to expend funds for the Department IDs listed on the card. The Organization Head is required to sign with a LIVE signature to indicate authorization of all signers to expend funds.

School Districts and Higher Education facilities must submit new signature cards any time new School Boards are organized.

Contact the Payroll Compliance Group for a blank signature card.

The Uniform Electronic Transactions Act, Title 6, Chapter 12A of the Delaware Code, allows for an electronic signature to authorize financial transactions. Authorized signers submit an electronic approval of biweekly payroll expenditures by sending an email to the PCG that includes the verbiage below with a list of the covered Department IDs:

To: PRFUND.AUTH@state.de.us

Subject: Payroll Funding Expenditures Authorization

I, _____ (Signer), certify that the associated charges for the Pay Period ending _____ (Pay Period End Date) for the Department IDs listed below meet all federal and state legal and regulatory requirements and that the represented expenditures **do not exceed** the remaining balance of funds appropriated by the General Assembly to this Organization.

14.3.1 Future Expenditures Considerations

Any State of Delaware Organization paying employees from authorized funding sources (general, local, federal funds or capital improvement debt appropriations) are required by Delaware Code to monitor expenditures against these funding sources to ensure balances do not go into a negative condition.

Authorizers must consider the remaining pay periods in the fiscal year to ensure anticipated expenditures will not exceed appropriated balances.

14.4 Direct Deposit Compliance

Method of payment of State officials and employees:

(f)(1) Notwithstanding any other provision of law, all state wage and salary payments shall be paid to employees who begin to receive such payments on or after January 1, 1996, and recipients of

state retirement payments who begin to receive such retirement payments on or after January 1, 1996, by electronic funds transfer, unless another method has been determined by the Secretary of Finance to be appropriate.

- (2) Each recipient of state wage, salary or retirement payments shall designate 1 financial institution and associated account and provide the payment authorizing information necessary for the recipient to receive electronic funds transfer payments through each institution so designated.
- (3) The Secretary of Finance may waive the requirements of paragraph (f)(1) of this section for any state employee upon request by the head of an agency or school district under standards prescribed by the Secretary of Finance.

(29 Del. C. § 2712)

14.4.1 Components of Direct Deposit Compliance

- Participation in Direct Deposit is a mandatory condition of employment with the State of Delaware.
- New employees must participate in Direct Deposit within 3 pay periods of their hire date.
- Direct Deposit exemptions: Grandfathered employees, attachés, student workers, tutors, aides, substitutes or casual/seasonal employees (term not to exceed two months).
- All other employees must participate in Direct Deposit or submit a request to waive the requirement which must be approved by both the Head of the employing Department and the Secretary of Finance, refer to the PCG Payroll Policy: Direct Deposit Waiver – PCG-DDWVR:
http://www.accounting.delaware.gov/payroll_comp/policies.shtml.
- Organization Human Resources/Payroll representatives are responsible for ensuring employees adhere to the Direct Deposit rule.
- The Payroll Compliance Group (PCG) monitors a master list of all direct deposit non-participants and reviews it for any new entries. The PCG contacts the Organization regarding any employee who is not in compliance with the law, refer to the PCG Payroll Policy: Mandatory Direct Deposit Participation Enforcement & Escalation Process – PCG-DDMPE:
http://www.accounting.delaware.gov/payroll_comp/policies.shtml.

14.5 Non-Resident Employment

The US Department of State administers the J1 Exchange Program under the provisions of the Mutual Educational and Cultural Exchange Act of 1961. The State of Delaware participates in this program by employing teachers and professors who are residents of other countries and are in the United States on a J-1 Visa.

The U.S. has income tax treaties with a number of foreign countries. Under these treaties, pay of professors and teachers who are residents of certain countries is generally exempt from U.S. income tax for 2 or 3 years if the employee temporarily visits the U.S. to teach or do research. These reduced rates and exemptions vary among countries and specific items of income. If there is no treaty between a country and the U.S., employees must pay income tax on the wages.

For detailed information on the exchange program and guidance on employment taxes and OECs for residents of China, France, or Spain, refer to PCG Bulletin #2012_001 – Non-Resident Alien Teachers: http://www.accounting.delaware.gov/payroll_comp/comm/bulletins_archive.shtml.

Contact the PCG for guidance on foreign employees who are residents of other countries.

14.6 Fringe Benefits

Fringe benefits include any compensation other than cash wages. The general rule is that the compensation is taxable; however, the Internal Revenue Code provides exclusions for numerous forms of noncash compensation provided to employees. Taxation rules vary according to the circumstances and business process associated with a specific fringe benefit.

Federal laws and regulations take precedence over any State regulations or employment or union contracts in determining if fringe benefits are taxable income.

Reference: Publication 15-B – Employer’s Tax Guide To Fringe Benefits:
<http://www.irs.gov/publications/p15b/ar02.html>

14.6.1 Clothing/Uniform/Footwear

Some Organizations employ individuals whose specialized job requirements include issuance and/or care and upkeep of uniforms, clothing, or footwear, or cash allowances for the purchase of these items.

- Periodic allowance payments made to employees for the purchase and maintenance of specific articles of employer-required uniforms are not taxable to the employees provided the uniforms are not adaptable to general use, and are not worn for general use. In addition, the employees must substantiate the expenses. If the employer does not

require substantiation, the allowance is taxable as wages and subject to withholding when paid.

- If it is determined that the clothing qualifies as a taxable fringe benefit, then the IRS requires that the fair market value be included on the employee's W-2 and withholdings be deducted.
- **PCG Bulletin 2013_002 – Uniform & Clothing Allowance Fringe Benefits** includes guidance on determining if the Uniform/Clothing is a taxable fringe benefit or a working condition fringe benefit.
http://www.accounting.delaware.gov/payroll_comp/comm/bulletins_archive.shtml
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14.6.2 Commuting Use of a State Provided Vehicle

- Commuting is the only authorized “personal use” of State-owned vehicles, pursuant to the State Policies, Procedures, and Standards, issued by the Government Support Services (GSS), Office of Fleet Management. Delaware Code provides for fines for any violations of this policy.
- Organizations must maintain current and accurate records of employees who are provided a State vehicle. For any part of a vehicle's usage to be considered non-taxable, Organizations should only provide vehicles to those employees whose job duties require the use of a vehicle. If the vehicle is used for both business and personal travel, the employee must account for the business use to the employer.
- Commuting and all other personal use of a State-provided vehicle is a taxable fringe benefit. All passengers commuting in a State vehicle, with the exception of vanpools, are subject to all the same taxable income rules. The IRS requires that the calculated value of commuting use of a State-provided vehicle be included on the employee's W-2 and withholdings be deducted.
- The State uses the Special Accounting Period Rule which makes November 1 - October 31 the taxable year for reporting commuting use.
- For detailed information on Vehicle Usage and guidance on associated employment taxes and OECs, refer to PCG Payroll Policy: Vehicle Usage – PCG-VEHUSE:
http://www.accounting.delaware.gov/payroll_comp/policies.shtml
- For detailed information on entering Vehicle Usage imputed income in the PHRST system, refer to PHRST Payroll Policy: Vehicle Usage – PRU-VEH-01.
<http://extranet.phrst.state.de.us/production/procedures.shtml>

14.6.3 Meal Provisions

To determine if a meal is allowable, Organizations should refer to **Chapter 7 – Purchasing and Disbursements, Section 7.6.6.2**. If the Organization determines the meal or meal reimbursement is allowable, the following must be considered to determine if there are tax implications to the employee.

- To determine if meal reimbursements are excludable from gross income, employers must consider general fringe benefit rules as well as regulations included in several sections of the Internal Revenue Code.
- Provision of infrequent meals of minimal value may be excluded as de minimis fringe benefits if it is unreasonable or impractical to account for the food.
- The value of occasional meals provided during employer-required overtime is excludable from wages. Refer to the Office of Management and Budget (OMB) Meal Reimbursement Policy for guidelines for the reimbursement of meals when working overtime. <http://intranet.omb.state.de.us/policies/index.shtml>
- The value of meals provided for the convenience of the employer is generally excludable from wages.
- Meal expense reimbursements or allowances must meet the accountable plan rules in order to be excludable from wages.
- For detailed information on Meal provisions and guidance on associated taxes and OECs, refer to PCG Bulletin # 2012_004 – Meal Provisions. http://www.accounting.delaware.gov/payroll_comp/comm/bulletins.shtml
- Refer to **Chapter 11 - Travel Policy**, for the policy on reimbursement of meal expenses incurred during out-of-state travel.

14.6.4 Tuition Reimbursement

- Internal Revenue Code (IRC) §132(d) (Education as Working Condition Fringe Benefit) provides an exclusion from gross income of reimbursements of expenses for job-related courses.
- IRC §127 (Qualified Educational Assistance Program) provides an exclusion of up to \$5,250 per calendar year for amounts paid by an employer through a sponsored educational assistance program. Qualified education expenses include tuition, fees, books, and supplies for both undergraduate and graduate education.

- The IRS requires that §127 Education Assistance Programs have a separate written plan. In the absence of a written plan, reimbursements for non-job-related courses are taxable.
- As a benefit to State employees, Organizations may provide Educational Assistance and/or Tuition Reimbursement, provided the funds are available in the budget.
- **PCG Bulletin 2013_001 – Education Assistance/Tuition Reimbursement** includes guidance on determining if the education assistance is a taxable fringe benefit or a [working condition fringe benefit](http://www.accounting.delaware.gov/payroll_comp/comm/bulletins.shtml).
http://www.accounting.delaware.gov/payroll_comp/comm/bulletins.shtml

14.6.5 Definitions

- **De Minimis Fringe Benefit** – any property or service with a value so small it is unreasonable or impractical to account for it.
- **Accountable Plan** – meets the IRS requirements that reimbursed expenses are business related and substantiated with receipts.
- **Nonaccountable Plan** – reimbursements for nonbusiness-related expenses or expenses not substantiated with receipts. These reimbursements are taxable income.
- **In-Kind** – payments made in something other than cash.
- **Working Condition Fringe Benefit** – employer-provided items that would be deductible by an employee as a business expense if they had incurred the cost. These types of benefits are excludable from income per IRC §132(d). The general rules are that the benefit must be provided so the employee can perform his or her job and the allowances and reimbursed expenses must be substantiated with reports and/or receipts.