

Pay Increases and Payroll Taxes



DECAL
Thriving Child Care
Business Academy

The influx of stimulus funds into child care businesses presents an opportunity to invest in and reward your hardworking staff, if you employ staff, through bonuses or pay increases. This guide will walk through ways you can offer these financial incentives and examine the long-term implications to consider in order to protect your business.

Introduction

As a child care business owner, you value your employees and want to compensate them for the essential services they provide. However, you also know that navigating pay increases for new and existing employees can be tricky. Ultimately, offering bonuses and pay increases can impact your business's bottom line. This guide will review ways you can offer pay increases and examine the tax implications as well.

Types of Pay Increases

There are a few different types of pay increases that you can consider for your program staff. Each type of pay increase will have a different impact on your business.

Bonuses

A bonus is a limited payment that temporarily increases your employee's income but there is no future obligation to award a bonus again. This type of pay increase can be useful when seeking out new staff members or as an incentive to current employees to stay with your program. You can choose to award a bonus to a new employee upon hiring or after they have successfully completed six months of employment. You could also choose to provide bonuses seasonally such as before the holidays or at the beginning of summer. Bonuses also can be used to recognize employees who have consistently exceeded expectations by working under unusual conditions or who have completed a certain number of professional development hours. Bonuses can boost overall staff morale and are worth consideration as this expense can have big benefits to your program.

Temporary Pay Increases

Temporary pay increases are just that, an increase to a person's pay rate for a temporary time. This type of pay increase is meant to last a short time, with a clear beginning and ending date. Perhaps you have an employee who you want to reward for their performance during a difficult time at your program. You could increase the employee's pay for the next six months but make sure the employee

knows that their pay will return to the original rate when the period ends. Clearly communicating, in writing, with your staff member is critical when choosing to use this type of pay increase. You would hate to lose a valuable employee over a temporary pay increase misunderstanding.

Long-Term Pay Increases

Long-term pay increases are most desirable, from an employee's perspective. This type of pay increase permanently raises the person's base level of pay, without any planned reduction. From an employer's point of view, a long-term pay increase can help you retain valuable employees and establish your program as a desirable place to work. However, raising employee pay must be a sustainable business practice.

Creating a Pay Scale

A pay scale helps to ensure that pay is fair and equitable across your program. Not only is a pay scale a useful business practice but it is especially helpful when considering pay increases. As you look at raising compensation for your employees, and especially when you are hiring new employees, it is important to review everyone's wages. You want to avoid wage compression, which can happen when employees who have been working with you for some time make less than the new employees just starting with your program in a similar type of position.

Sometimes wage compression happens when the demand for workers is greater than the supply of workers, which results in newly hired employees making higher wages than your current employees who are at the same level. This can happen because the criteria you use to set up your pay rates are outdated, unclear, or even too broad. Not only do you want to avoid wage compression because it's inequitable, but it can also cause challenges between your newly hired and current employees, resulting in your existing employees leaving your program.

Review your pay scale at least annually to make sure that it is comparable to current market rates. It's also a good idea to review your pay scale whenever you hire a new employee. One way to collect market rate information is to review up to ten job postings for similar positions from similar child care businesses in your community to learn how much they are paying. You can also look at some online job search sites where you can get a general idea of the salary by the position listed in your area, as well as compare it to other areas and communities across the country. As you create your pay scale, you should include the education level, qualifications, skill levels, and experience of your employees. Also, consider the variations in the roles and responsibilities of each position in your program.

To begin:

- Gather the job descriptions for each role in your program. Be sure to think about the key qualifications and responsibilities required for each role.
- Consider each position based on the required qualifications and/or certifications, the responsibilities, and the role, then rank these positions using this information.
- Group similar positions together and sort them into tiers
- Research salaries offered for similar positions in your area and find an average rate for each tier.
- Establish a range of pay within each tier and have the range span from an entry-level person (about 75-80% of the market average) to a highly skilled person (about 120-125% of the market average)
- Assess employees based on their skill level, seniority, experience, and education to decide if they should receive entry-level, average, or highly skilled level pay within their assigned tier.

Understanding Costs of Pay Increases

Be mindful of the associated costs when considering increasing employee pay, either short- or long-term, as you, the business manager, must be prepared to cover those costs. You will need to compare your current pay costs with your new pay costs and include both rates of pay and payroll taxes. Determining the increase in costs when considering employee pay helps you make the strongest decision for your business.

Calculating Current Costs

1. **Current Wages** – Use the following calculation to determine the current wages you pay your employee each week:

Total hours worked per week x current hourly rate = current wages per week

Let's practice by saying you have one full-time employee who currently earns \$10.00 per hour. Therefore,

40 hours per week x \$10.00 per hour = **\$400.00 (current weekly wages)**

- **Current Payroll Taxes** – Be aware of the increase in payroll taxes that will accompany an increase in pay that you, as the employer, will be required to pay. Federal Insurance Contributions Act (FICA) Taxes:
 - 6.2% Social Security Tax (check the [Social Security](#) website for current base earnings)
 - 1.45% Medicare Tax (withheld on all of an employee's wages)

Use the employee's wages multiplied by the tax percentage to calculate payroll taxes.

- Current wages x 6.2% (0.062) = Social Security Tax

- Current wages x 1.45% (0.0145) = Medicare Tax

Let's practice by using our previous example. Here's how to calculate payroll taxes for a full-time employee making \$10.00 per hour:

- $\$400.00 \times 6.2\% (0.062) = \24.80
- $\$400.00 \times 1.45\% (0.0145) = \5.80

Total: \$30.60 taxes per week

2. **Total Current Costs** – You now need to combine the total wages paid to your employee with the total payroll taxes owed on those wages. By continuing with our example, the total current cost is \$430.60 per week:

$$\$400.00 \text{ (total wages)} + \$30.60 \text{ (total payroll taxes)} = \$430.60 \text{ (total cost)}$$

Calculating Increase in Costs

After you've calculated your current costs, then you need to calculate the new costs after you've increased your employee's rates of pay.

Let's practice by saying you want to give your full-time employee an increase from \$10.00 per hour to \$12.00 per hour. You've already calculated the total weekly cost associated with \$10.00 per hour, so you need to make the same calculations using \$12.00 per hour as your rate of pay:

Calculating New Costs

New Wages:

$$40 \text{ hours per week} \times \$12.00 \text{ per hour} = \mathbf{\$480.00 \text{ total wages per week}}$$

New Taxes:

- $\$480.00 \times 6.2\% \text{ Social Security Tax } (0.062) = \29.76
- $\$480.00 \times 1.45\% \text{ Medicare Tax } (0.0145) = \6.96

Total: \$36.72 taxes per week

Total New Cost: \$516.72

$$\$480.00 \text{ (new wages)} + \$36.72 \text{ (new taxes)} = \$516.72 \text{ (new cost)}$$

Difference in Old vs. New Costs

Let's find the difference between the total current cost (\$430.60) and the total new cost (\$516.72). To learn your total increase in weekly costs to raise one full-

time employee from \$10.00 per hour to \$12.00 per hour, subtract the total current cost from the total new cost:

$$\$516.72 \text{ (total new cost)} - \$430.60 \text{ (total current cost)} = \$86.12 \text{ (increase in cost)}$$

In this example, the total employer cost per week increases by \$86.12 when giving this employee a \$2.00 per hour raise, or \$4,478.24 per year (multiplying the weekly cost by 52 weeks in a year).

Bonuses or Short-Term Pay Increases

Increasing employee pay, through either bonuses or short-term pay increases, requires that you are prepared to handle the costs. You must make sure that you have the funds available for either wage increases or one-time bonuses. To decide how much tax to withhold for bonuses, there are two ways to consider it. One, you can calculate the taxes owed on your employee's bonus by using a flat percentage of 22% for supplemental pay, regardless of your employee's income tax withholding rate. This method is easiest when you choose to pay your employee apart from their normal wages.

For example, \$1,000.00 (bonus) x 22% = \$220.00

Or two, you can add their bonus to their regular pay. You can treat the total amount as one payment and then calculate the payroll taxes just as you normally do.

For example, \$1,000.00 (bonus) + \$1,200.00 (regular paycheck) = \$2,200.00 combined amount

Payroll Taxes:

- \$2,200.00 x Social Security Tax 6.2% (0.06) = \$136.40
- \$2,200.00 x Medicare Tax 1.45% (0.0145) = \$31.90
- TOTAL payroll taxes on combined amount = \$168.30

To determine the payroll taxes owed on just the \$1,000.00 bonus, follow the same calculations but use \$1,000.00 as the total wages:

- \$1000 x Social Security Tax 6.2% (0.062) = \$62.00
- \$1000 wages x Medicare Tax 1.45% (0.0145) = \$14.50
- TOTAL payroll taxes on just the bonus portion of payment = \$76.50

Combine the payroll tax amounts with the federal income tax withholdings per your employee's withholding rate to calculate the withholding amounts for bonuses combined with regular pay.

Knowing the amount you will owe in payroll taxes will help you determine how much you will need to put aside so that you have funds available when you need them. You can take the amount that you estimate you will owe and divide it over the time period that the wage increase will cover. For example, from our previous exercise, if you were to raise an employee's pay rate by \$2.00 per hour, you would have a new weekly cost of \$516.72, which would be \$26,869.44 per year. To cover the total costs of this employee's new salary, you would need to have \$2,239.12 per month. This might feel like a lot in total, but the actual increase was just \$373.19 per month, or a 20% increase. From our example, plan to set aside at least an additional \$373.19 per month to cover the additional costs for this employee.

To learn more about your budgeting, cash flow, and other business practices, check out these resources:

- [Create a monthly budget](#)
- [Determine your cash flow](#)
- [Make sure you are paying yourself](#)
- [Consider adjustment in your rates](#)
- Consider the [Child Care Subsidy program](#)
- Participate in the [Child and Adult Care Food Program](#)

These resources can help you create a solid financial plan to support your business now and in the future.

Additional Resources

If you have questions or need help, assistance is available.

[GaPDS Website](#)

[DECAL Thriving Child Care Business Academy Website](#)

[Georgia Licensing Rules and Regulations](#)

To Find Other Study Guides: Click on [Resources](#) on the Academy home page

To Find Training: Click on [Trainings](#) on the Academy home page

To Register for Training: Click on [Schedules & Registration](#) on the Academy home page

To Sign Up for Study Groups: Fill out the [Intake Assessment](#)

For questions about coaching or study groups: Email GAcoaching@civstrat.com

To Find Other ECE Resources: Visit the [DECAL Website](#)

For General Questions about the Academy: Email thriving@decals.ga.gov

For More Information:

[Family Child Care Learning Home Rules and Regulations](#)

[Child Care Learning Center Rules and Regulations](#)