Ryan, Swanson & Cleveland, PLLC
1201 Third Avenue, Suite 3400
Seattle, WA 98101-3034

www.ryanswansonlaw.com

Understanding Employee Paycheck Deductions

By Britenae Pierce
Ryan, Swanson & Cleveland, PLLC

Many employers face the question of how to handle making deductions from employee paychecks. Below are the basic rules and some additional tips for navigating the laws for employee paycheck deductions.

Employee Deductions Generally

A number of circumstances exist where employers may deduct an employee's wages either from ongoing paychecks or from the employee's final paycheck. In some circumstances, employers may make deductions causing the rate of pay to be below the minimum wage. While these circumstances exist, they are limited. Best practice is to limit deductions for each paycheck so that the employee still receives minimum wage for the hours worked. One exception is for deductions required by state or federal law or for court-ordered deductions such as child support. For any deduction, the employer must identify and record all wage deductions openly and clearly in each employee's payroll records.

Appropriate Paycheck Deductions

During an ongoing employment relationship, standard deductions are as follows: 1) as required by state or federal law, including for taxes; 2) for medical surgical, or hospital care or service; or 3) to satisfy a court order, judgment, child support payments, or other court-ordered deductions. Medical, surgical, or hospital services are not those related to job-related injuries. Instead, those are for when a company elects to pay a worker's medical costs for non-work related injury or care.

While the employee is employed, an employer may deduct wages from the employee's paycheck when the employee agrees to such deductions in advance and in writing. The purpose behind the deduction must be lawful and be for the employee's benefit.

A common example of these types of employee-agreed deductions are for employee premiums for health and benefit plans. Employees can elect to participate in their company's health or dental plan, or even life insurance or other benefit plans, and to have the employer deduct the necessary premiums for the employee. This is a benefit to the company so that it can keep track of its plan participants and also a benefit to the employee so that the employee does not handle multiple premium payments per month.

Another example of these types of deductions is when the employee purchases goods or services from the employer and instead of paying directly, opts to make payments through paycheck deductions. For any goods or services sold to an employee, such goods and services must be provided to the employee at the same or better rate than given to the public.

Another example is a loan. Some companies offer loans to their employees, whether to tide them over to payday or for more significant purposes. The employer can charge interest on employee loans but the rate must be reasonable.

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All of these types of deductions work best if the employer and employee can agree to a schedule of deductions in advance. As a practical matter, the employer and employee reaching agreement over all aspects of paycheck deductions in advance reduces the likelihood of future problems.

Final Paycheck Deductions

Employers and employees should have an agreement in advance that if the employee's employment terminates (whether voluntarily or involuntarily) prior to the end of the scheduled deductions, then the remainder owed may be deducted from the final paycheck. For example, if the employee has a $500 loan and $50 is taken out per paycheck, but at the time of the employment ending the employee still owes $300 on the loan, then the employer may deduct the entire $300 from the final paycheck based on the written agreement.

There are a number of circumstances where the deductions are allowed from the final paycheck, even though such deductions are not allowed from regular paychecks. These circumstances include deductions for breakage, loss, or damage to equipment but only if it was caused by the employee's dishonest or willful act, for employee theft if the theft was dishonest or willful and if the company files a police report, and for failure to return a company uniform if the parties agreed to the uniform deduction in advance. Additionally, employers and employees can make their own agreements for deductions from the final paycheck at the time of termination. But if the employee does not agree to a voluntary deduction, then the employer may not deduct.

Final paychecks are due to employees on the next regularly scheduled payday. Paychecks may not be withheld until the employee turns in company property. To avoid any issues, best practice is to require employees to turn in all company property at the time of termination.

Practical Approach

The above list is not exhaustive of all allowed and disallowed deductions, but it covers some of the most frequently asked questions about deductions. The most basic rules for paycheck deductions to avoid running into trouble are to deduct only when agreed by the employee in advance and in writing and to limit deductions so that the resulting paycheck is at or above minimum wage. When considering payroll deductions beyond these rules, consult your employment attorney for more detailed assistance.

Britenae Pierce is a partner practicing in Ryan, Swanson & Cleveland, PLLC's Employment Rights, Benefits and Labor Group. She can be reached at 206.654.2289 or pierce@ryanlaw.com.