

IRS Guidance on the Payroll Tax Deferral Program

Summary of the Payroll Tax Deferral

The payroll tax deferral initiative took effect September 1, 2020. This was not enacted via legislation, but rather was issued via a Presidential Memorandum (“PM”) on August 8, 2020. The PM announced a plan whereby the Secretary of the Treasury would defer the collection of Social Security payroll taxes from employees between September 1, 2020 and December 31, 2020. In short, employers may stop withholding the 6.2% Social Security portion of the payroll tax that employees pay each pay period for the rest of 2020. The deferral would apply only to the Social Security portion, not the Medicare portion. On August 28, 2020, the IRS issued Notice 2020-65 which provides guidance on how the deferral process will be administered.

Under this program, participating employers will defer withholding and depositing the employee share of Social Security tax on wages earned for employees who earn less than \$4,000 in any bi-weekly pay period between September 1, 2020 and December 31, 2020. The bi-weekly threshold of \$4,000 translates to an annualized salary of below \$104,000 a year based on 26 bi-weekly pay periods.

It is important to stress that at this time there are serious open issues regarding the operation of the payroll tax deferral program. Bolaños Lowe expects that additional guidance will need to be provided by the IRS before this program is fully operational.

Is the Program Mandatory or Optional?

The program appears to be optional. Notice 2020-65 establishes a general payroll tax deferral component but does not address whether employers or employees may choose to opt out of the tax deferral program. Prior to the issuance of the Notice, Treasury Secretary Mnuchin publicly announced that the deferral program would be optional. However, neither the PM nor the Notice explicitly confirm the mandatory or optional nature of the payroll tax deferral program.

Payment of Deferred Taxes Are Due in Early 2021

The deferral of the payroll tax collection obligations extends the employer’s withholding and payment deadlines—it does not forgive the tax obligations. Under the Notice, employers are responsible for withholding the deferred amounts from employee pay after the deferral period ends on December 31, 2020. The deferred amounts are to be paid with employee payroll deductions on a pro-rata basis during the period between January 1, 2021 and April 30, 2021. However, employers are permitted to make arrangements to collect the taxes from employees in some other matter in lieu of the payroll deductions. The Notice is clear that if an employer fails to withhold and pay the taxes ratably from wages and compensation over the recovery period, the employer will be subject to interest, penalties, and taxes on the uncollected deferred amounts as of May 1, 2021.

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While the President expressed his desire to have the deferred amounts forgiven by Congressional action, the program does not currently provide for such forgiveness. At this time, employers will have payment obligations in 2021 based on 2020 deferrals. Accordingly, employees will see reduced paychecks to account for what could amount to a double Social Security tax withholding amount for the first four months of 2021.

What Happens If an Employee Is Not Working in 2021?

A major concern for employers is their liability when the employee takes an unpaid leave of absence, quits, or is terminated before the deferred tax balance is recovered. Ultimately, employers are responsible to ensure that the deferred taxes are paid. Therefore, if an employee quits after deferring payroll taxes but before the deferred amount has been withheld, the employer will be responsible for the uncollected deferred tax amounts unless it makes “arrangements” otherwise to collect the sums from the employee and is able to do so.

What Should Employers Do?

- Determine if you will participate in the program.
- Determine whether you will treat the deferral of payroll tax withholding as optional or mandatory for all employees.
- If withholding is deferred, work with payroll to prepare a plan to withhold payroll taxes for all employees who earn \$4,000 or more in the

pay period (this will need to be assessed on a pay period by pay period basis according to the Notice).

- Defer withholding of the payroll taxes as applicable.
- Provide notice to the employees of the legal obligation to pay the amounts back, and ensure employees understand what they may be paying in January through April of 2021.
- Require employees who defer withholding of payroll taxes to sign a repayment arrangement that obligates the employee to repay the employee’s share of deferred payroll taxes that cannot be recouped via paycheck deduction because the employee is on unpaid leave, quits, or is terminated before the balance of the deferred amount can be satisfied by paycheck deductions.
- Ensure that any additional amounts deducted from an employee’s paycheck are timely deposited to satisfy the transmittal obligation of the PM and Notice.

Concerns

It seems that the program is optional, and most private employers are not opting to participate for a few reasons. Employers do not feel it is prudent to collect, essentially, double tax from employees in the first four months of 2021. Although the program could provide some relief to employees who are struggling at the moment, it could create a more significant hardship in 2021 if those individuals have to pay back the deferred taxes and do not have money to do so.



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Also, employers are worried about the burden of implementing a change to their payroll system for a few months; the Treasury did not even provide guidance until two days before the deferral period took effect. Employers are also worried about the additional risk of being liable for repayment even if they are unable to recoup the money from employees.