

IRS Issues Payroll Tax Deferral Guidance to Clarify Employer Obligations

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The Department of Treasury recently released guidance, Notice 2020-65, to clarify President Trump's August 8 executive order deferring the employee's share of certain payroll taxes for the remainder of the 2020 calendar year (the "Order").[1] Notice 2020-65 provides clarity as to when employees are eligible for the deferral and the method of repayment of the deferred taxes.

The Order provides that the withholding, deposit, and payment of payroll taxes related to an employee's share of Social Security taxes ("Deferred Taxes") be deferred for the period of September 1, 2020 through December 31, 2020 ("Deferral Period"). The Order limits the availability of the deferral to taxpayers earning bi-weekly pay of less than $4,000 on a pre-tax basis ("Applicable Wages"). The Order also provides that the deferred tax will continue to accrue without penalty interest or any other addition to the tax.

Many employers initially expressed concern over the lack of guidance provided and the short time in which employers would have to implement the Order. The American Institute of CPAs[2] and the U.S. Chamber of Commerce[3] sent letters to the Treasury Department requesting guidance to address several concerns, including the following:

- Whether the deferral is voluntary and, if so, whether the employee is responsible for making an affirmative election to defer the taxes.
- How the $4,000 bi-weekly pay amount is determined and how to deal with fluctuating salaries, bonuses, and seasonal or short-term employees.
- How to deal with employees who leave employment before the end of the deferral period.
- The collection mechanism for the deferred taxes, the due date for the deferred taxes, and who bears the ultimate liability for

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the repayment of the deferred taxes.

Late on August 28, the Department of Treasury released Notice 2020-65, which provides employers guidance as to the implementation of the Order and addresses some of the questions stated above.

Voluntary or mandatory nature of the deferral of Deferred Taxes. On August 12, Treasury Secretary Steven Mnuchin stated that "[w]e can't force people to participate, but I think small businesses will, and pass on the benefits".[4] Based on this statement it appears that employers, not employees, have the option of whether or not to defer payment of the Deferred Taxes for eligible employees.

On August 21, a notice from the Agriculture Department's National Finance Center, which provides administrative services to federal agencies, stated that beginning with the first pay period after September 1, it will "eliminate the OASDI employee deductions" for employees earning less than $4,000 per pay period, while continuing to remit the employer portion of payroll taxes.[5] As such, it appears that certain federal agencies will be implementing the Order for payments made beginning on September 1.

Notice 2020-65 does not address whether eligible employees can opt out of the deferral of Deferred Taxes. However, the Order directs the Secretary of the Treasury to use his authority under Section 7508A to defer the payment of the Deferred Taxes. Section 7508A authorizes the IRS to postpone deadlines for various acts but does not permit the IRS to prohibit the timely withholding and payment of taxes. Therefore, the IRS does not have the authority under Section 7508A to prohibit employers from the withholding and payment of the Deferred Taxes, only the authority to postpone the deadlines for the timely withholding and payment of such taxes. Consistent with Section 7508A, the IRS and Department of Treasury press releases use language to describe the guidance as "allowing" deferral and "available" to employers,[6] further indicating that such deferral is not mandatory.

Calculation of wages for bi-weekly pay limitation. The Order limits the deferral of Deferred Taxes to employees with bi-weekly pay of less than the Applicable Wage threshold, $4,000. Notice

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2020-65 defines Applicable Wages as "wages" defined in Section 3121(a) of the Internal Revenue Code ("Code") or "compensation" defined in Section 3231(e) of the Code that is paid to an employee on a pay date between September 1, 2020 and December 31, 2020. Section 3121(a) "wages" and Section 3231(e) "compensation" include all renumeration from employment, with certain exclusions (e.g., payments related to insurance, medical, disability and annuity plans). An employee only has Applicable Wages for the deferral of Deferred Taxes if wages and compensation are less than $4,000 for the bi-weekly pay period. Notice 2020-65 provides that the determination of Applicable Wages is made on a pay period-by-pay period basis. Employees with fluctuating salaries and bonuses, may have Applicable Wages to defer payment of the Deferred Taxes for some bi-weekly pay periods but not others. For seasonal or short-term employees who may not have annual salaries that exceed the average of $4,000 bi-weekly pay ($104,000), they are also only eligible for the deferral if wages or compensation in a particular bi-weekly pay period are below the $4,000 threshold amount.

Payment of the Deferred Taxes. Notice 2020-65 provides that the payment of Deferred Taxes is postponed until the period beginning January 1, 2021. Starting January 1, 2021, employers must withhold and pay the Deferred Taxes ratably from wages and compensation until April 30, 2021 (the "Payment Period"). Interest, penalties, and additions to tax will begin to accrue on May 1, 2021, with respect to any Deferred Taxes. As such, employers electing to participate in the tax deferral will withhold an additional amount for each pay period during the Payment Period equal to the ratable amount of total Deferred Tax for each employee. In cases where employees have the same bi-weekly salary during the Payment Period as the Deferral Period, this will result in withholding for the Social Security portion of payroll taxes equal to two times the normal amount. Notice 2020-65 provides that employers may make arrangements to otherwise collect the total Deferred Taxes from employees but does not provide any examples or other guidance as to what appropriate arrangements may be made.

Liability for uncollected Deferred Taxes. Notice 2020-65 makes clear that the liability for the payment of the Deferred Taxes is on

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the employer, rather than the employee. Notice 2020-65 does not address how employers should treat the Deferred Taxes of employees who later leave employment before the Payment Period ends. However, tax practitioners have commented that the obligation to withhold tax on wages paid is a statutory obligation of the employer, therefore, even if the due date is deferred, the employer would have an obligation to pay over the required withholding amount even if the employee with respect to the wages paid in the Deferral Period no longer works for the employer.[7] Employers may have to pay the Deferred Taxes on behalf of employees who do not have wages or compensation during the Payment Period.

Potential relief from repayment of the Deferred Taxes. The Order directs the Secretary of Treasury to explore avenues, including legislation, to eliminate the obligation to pay the Deferred Taxes. Secretary Mnuchin has acknowledged that the Deferred Taxes cannot be forgiven without action from Congress.[8] There is considerable uncertainty as to whether any relief will be provided and whether employers electing not to defer the Deferred Taxes will cause their employees to miss out on a potential relief from payroll tax if legislation is passed to forgive any Deferred Taxes that remain unpaid.

Please contact any attorney in Frost Brown Todd's Tax practice if you have questions about compliance with the recent payroll tax deferral Order.

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[1] https://www.irs.gov/pub/irs-drop/n-20-65.pdf

[2] https://www.aicpa.org/content/dam/aicpa/advocacy/tax/downloadabledocume aicpa-comment-letter-pres-memo-payroll-tax-deferral.pdf

[3] https://www.uschamber.com/comment/us-chamber-letter-secretary-mnuchin-implementation-of-the-executive-order-deferring-payroll

[4] https://www.taxnotes.com/tax-notes-today-federal/employment-taxes/trumps-optional-payroll-tax-plan-may-not-pay-analysts-say/2020/08/13/2ctw5

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[5] https://nfc.usda.gov/ClientServices/HR_Payroll/Customer_Notifications/2020/0 OASDI.pdf (url is not active)

[6] See https://www.irs.gov/newsroom/guidance-issued-to-implement-presidential-memorandum-deferring-certain-employee-social-security-tax-withholding

[7] https://www.taxnotes.com/tax-notes-today-federal/employment-taxes/trumps-optional-payroll-tax-plan-may-not-pay-analysts-say/2020/08/13/2ctw5

[8] Id.

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