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Client Alert: IRS Releases Guidance on Payroll Tax Deferral

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On August 28, 2020, the IRS published Notice 2020-65 (the "Notice") to provide guidance on the deferral of payroll tax withholdings, as directed by President Trump's previously issued Executive Order. Whereas the CARES Act previously provided for the deferral of *employers'* shares of payroll taxes, the current guidance provides employers with the option to defer the withholding and payment of *employees'* shares of the Social Security portion of Federal Insurance Contributions Act ("FICA") (6.2 percent), on wages paid from September 1, 2020 through December 31, 2020. (Note that there is no option to defer the Medicare portion (1.45 percent) of the FICA due on these wages). The Notice only allows deferral for an employee's pay period if the employee's wages paid for a bi-weekly pay period are less than \$4,000. Employers that choose deferral must make the determination in respect to each employee for each payroll period, so it is possible that a certain employee's wages may qualify for deferral in one period, but not another.

The Notice explicitly delays the due date for the withholding and depositing of employees' shares of Social Security. It is up to the employer as to whether the employer wants to withhold and deposit as per usual, or wait to withhold and deposit by the deferred due date. Since the Notice fails to provide a specific method to elect deferral, employers presumably make the election simply by not withholding Social Security from employees' paychecks.

The Notice requires employers to recover deferred amounts from the affected employee's wages and compensation paid from January 1, 2021 through April 30, 2021. This means that for each affected employee, the employer will have to determine an adjusted withholding rate that will recover the deferred amounts in equal installments over the designated timeframe. Employers must remit all deferred amounts to the IRS by May 1, 2021.

The Notice provides only limited guidance on what an employer should do when it defers withholding payroll tax amounts for a particular employee but that employee is subsequently terminated or leaves employment. The Notice states "[I]f necessary, the Affected Taxpayer may make arrangements to otherwise collect the total Applicable Taxes from the employee." Since the employee share of FICA is a "trust fund tax," ultimate liability for payment of the deferred payroll tax rests with the employer. We therefore advise employers to come to terms for repayment with employees before deferral, possibly with a written commitment from the employees, to avoid having to negotiate to recover the deferred amounts from an employee upon departure.

The Executive Order asked the Secretary of Treasury to explore ways to eliminate the obligation to pay back deferred amounts, but it appears such relief would require Congress to pass the necessary legislation.

We expect the IRS to issue further guidance and a revised Form 941 in the coming months.