

IRS Issues Limited Guidance on Payroll Tax Deferral Option

Labor & Employment Law Update

By Kelly Haab-Tallitsch on August 31, 2020

On August 28, the IRS issued Notice 2020-65 providing brief guidance on the payroll tax deferral announced in a Presidential Memorandum issued on August 8th. The Memorandum directed the Treasury Department to issue guidance for a deferral of the withholding and payment of the employee portion of Social Security taxes to be “made available” to employers. The IRS Notice, with very limited details, establishes the ability of an employer to defer the payroll tax, but leaves many questions unanswered.

Is it Required or Voluntary?

Under the Presidential Memorandum and IRS Notice, the deferral of payroll taxes is optional for employers. There is no penalty for employers that choose not to take advantage of the deferral. The Presidential Memorandum also specifies that the Memorandum does not create an enforceable legal right to a benefit. In other words, an employee does not have the right to initiate legal action to force an employer to permit the payroll tax deferral.

Which Employees Can Be Eligible for Deferral?

Employers may defer the withholding and payment of the employee portion of Social Security taxes from September 1 through December 31, 2020 for employees that are paid less than \$4,000 in a bi-weekly pay period (or the equivalent amount with respect to other pay periods). Eligibility for the deferral must be determined on a pay-period by pay-period basis. No deferral is available for any bi-weekly pay period in which an employee earns \$4,000 or more.

“Deferral” Does Not Mean the Tax Liability is Eliminated

Employers must withhold and pay any deferred taxes ratably between January 1 and April 30, 2021. This means employees would be subject to withholding of the deferred taxes (from the last four months of 2020) on top of regular tax withholding during the first four months of 2021. The Notice provides that an employer may make “other arrangements” to collect the deferred taxes from an employee if necessary, although it is unclear what this means.

Employer Liability

It is important to note that the Memorandum and Notice do not relieve an employer of the obligation to ultimately pay the relevant payroll taxes. Employers remain liable for the payment of deferred taxes regardless of whether an employer is able to collect the deferred taxes from an employee. For example, no specific relief is provided under the Notice to an employer in the event an employee is not employed in the first quarter of 2021 and the employer is unable to withhold the deferred taxes at that time. Interest and penalties will begin to accrue to the employer on any unpaid taxes beginning May 1, 2021.

The Bottom Line

Without additional clarification and guidance, employers deferring payroll taxes this fall run the risk of having to impose what will seem like an additional tax on employees or potentially face other liability next spring. Furthermore, employers should consider the administrative complexity of reviewing employee eligibility on a pay-period basis and the communication required to ensure employees understand they will be subject to additional withholdings before moving forward.

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