Deferring Payroll Tax—The Employer’s Dilemma

September 2, 2020

On August 13, 2020, President Trump issued a Presidential Memorandum directing the Secretary of the Treasury to use his authority to defer the withholding, deposit and payment of the employee portion of Social Security taxes (“SS Tax Deferral Program”). On August 28, 2020, the Secretary of the Treasury and IRS issued Notice 2020-65 (“Notice”) to implement the SS Tax Deferral Program. This FAQ-style alert addresses the key provisions of the Notice and the many remaining uncertainties about the SS Tax Deferral Program.

Are Employers Required to Implement the SS Tax Deferral Program? Although the Notice is silent on whether or not the SS Tax Deferral Program is mandatory or optional, the IRS press releases use permissive language to describe the guidance as “allowing” deferral and “available” to employers. The Notice and the Presidential Memorandum rely on Internal Revenue Code Section 7508A, which authorizes the IRS to postpone deadlines for various acts during a Presidentially declared disaster (including deferring withholding and payment of certain taxes), but that section does not specifically prohibit the timely withholding and payment of taxes during such postponed deadlines. Consistent with Section 7508A, the Notice does not apply to employees. Only “employers that are required to withhold and pay the employee share of social security tax” (and the equivalent Railroad Retirement Tax Act provisions) are designated as “Affected Taxpayers” for purposes of section 7508A. Meaning, it would be the employer’s decision, not employees, to implement or not implement the SS Tax Deferral Program. That said, the Presidential Memorandum itself states that “The deferral shall be made available with respect to any employee the amount of whose wages or compensation, as applicable, payable during any bi-weekly pay period generally is less than $4,000, calculated on a pre-tax basis, or the equivalent amount with respect to other pay periods.” Hence, there remains some confusion over the optional or mandatory nature of the SS Tax Deferral Program. We have requested the IRS to confirm that employers have the discretion to implement or not implement the SS Tax Deferral Program.

What Is the SS Tax Deferral Program? If implemented, an employer would cease withholding and depositing the payment of the employees’ portion of social security taxes on a pay date during the period beginning on September 1, 2020, through December 31, 2020. Although the Notice is silent, presumably an employer could implement the SS Deferral Program at any time during the deferral period, rather than for the entire deferral period of September 1 through December 31.

What Wages Are Eligible for the SS Tax Deferral Program? The deferral of social security tax withholding and payment only applies to employees’ bi-weekly paychecks that are less than $4,000 or the equivalent threshold amount with respect to other pay periods. This threshold is on a per-payroll basis; meaning that if an employee has less than $4,000 for some biweekly checks and $4,000 or more for others, then the employer can only defer social security tax withholding and payment for the biweekly paycheck that is less than $4000 and not from those of $4,000 or more.

When Are the Deferred Social Security Taxes Paid? The Notice clearly requires payment of any deferred social security taxes. Specifically, the Notice states that employers “must withhold and pay the total [deferred social security taxes that the employer] deferred under this notice ratably from wages and compensation paid between January 1, 2021, and April 30, 2021.” This means that the withholding of an employee’s portion of social security taxes will basically double from January 1, 2021, to April 30, 2021 (i.e., payment of the employee's deferred portion plus payment of the employee's then-current portion of social security taxes). If an employer fails to withhold and deposit the deferred social security tax by May 1, 2021, the IRS will assess the employer interest, penalties and additions to tax with respect to any unpaid deferred social security taxes.

Will the Payment of Deferred Social Security Taxes Be Forgiven? Unknown! The Presidential Memorandum states that the “Secretary of the Treasury shall explore avenues, including legislation, to eliminate the obligation to pay the taxes deferred pursuant to the implementation of this memorandum.” Neither the Secretary of the Treasury nor the President of the United States has the power to unilaterally forgive the delayed payroll taxes. That would require Congressional approval and action, which may not happen given the likely impact such forgiveness would have on social security funding.
What Are the Risks to Employers Who Implement the SS Tax Deferral Program? The number one concern for employers is the joint liability for withholding and payment of the employees’ share of social security taxes. The Notice makes clear that the employer is responsible for the payment of such deferred social security taxes, which can be done by ratably withholding the employees’ portion of the deferred social security taxes from paychecks issued from January 1, 2021, through April 30, 2021. The Notice also indicates that the employer may make arrangements to otherwise collect the deferred social security taxes and any failure to do so by May 1, 2021, will result in penalties, interest and additions to tax assessed to the employer. So, what happens when an employee is not receiving enough, if any, pay from the employer from January 1 to April 30, 2021? The Notice appears to hold the employer jointly accountable to pay the deferred social security taxes.

If an employer decides to implement the SS Tax Deferral Program, we strongly recommend a written agreement with each employee agreeing to pay his or her share of the social security taxes that are being deferred and agreeing in advance to have the full obligation deducted from the last paycheck issued to the employee in the event he or she terminates prior to April 30, 2021. However, it is likely that many employees will refuse to sign repayment agreements. We recommend that employers work with legal counsel to consider any state wage and hour laws that apply to payroll deductions and repayment agreements.

What Are Other Employers Doing? From discussions with our employer-clients and the numerous news articles on this subject, it appears an overwhelming majority of employers will not be implementing the SS Tax Deferral Program and will continue to withhold and pay the social security taxes as normal. The likely reasons for not implementing include payroll systems not being set up to determine qualifications for the deferral for each employee and tracking those deferrals, how to accommodate employees who do not wish to defer taxes, employees facing hardships in 2021 of not having sufficient funds to repay the deferred taxes, IT challenges to implement, concerns of how deferrals should be reported to the IRS so as to avoid penalties for failure to withhold and remit taxes, and concerns from many employers, especially those with high turnover or seasonal businesses, that they could be jointly liable to pay the deferred social security taxes for employees with little or no wages through April 30, 2021. So far, not ironically, it appears that the federal government is the major employer to announce implementing the SS Tax Deferral Program for its employees starting with the second paycheck in September.

If you have any further questions about the SS Tax Deferral Program or any of the information from this alert, please contact Amy Christen (248-203-0760 or achristen@dykema.com), Meg Hunter (313-568-6788 or mhunter@dykema.com), Mike Cumming (248-203-0740 or mcumming@dykema.com), or your Dykema relationship attorney.

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Deferring Payroll Tax—The Employer’s Dilemma (Cont.)

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