

TO: U.S. Chamber of Commerce Members
FR: Neil Bradley, EVP and Chief Policy Officer and Caroline Harris, VP Tax Policy
DT: August 29, 2020
RE: IRS Notice on Payroll Tax Deferral Effective for September 1

On Friday evening, August 28, the IRS released its first notice regarding implementation of the president's executive order on payroll tax deferral. The document, which is just over two pages, can be found here: <https://www.irs.gov/pub/irs-drop/n-20-65.pdf>.

While the guidance leaves more questions unanswered than it answers, here is what we now know:

Short Summary:

As expected, employers may suspend the withholding of the 6.2% Social Security payroll tax normally deducted from an employee's pay.

The deferral only applies if the biweekly compensation (or equivalent amount for other pay periods) is less than \$4,000. The determination of whether the deferral applies is made on a paycheck to paycheck basis.

The deferral only applies to wages paid during the period beginning on September 1, 2020 and ending on December 31, 2020.

Employers are responsible for withholding and paying any deferred taxes. Specifically, employers "must withhold and pay the total Applicable Taxes that the [employer] deferred under this notice ratably from wages and compensation paid between January 1, 2021 and April 30, 2021 or interest, penalties, and additions to tax will begin to accrue on May 1, 2021, with respect to any unpaid Applicable Taxes."

FAQ:

Is the payroll tax deferral voluntary for the employer or employee?

The notice makes clear that the employer is the affected taxpayer.

While the notice does not explicitly say it is voluntary for the employer, it also does not make it mandatory. Based on our read and the analysis of others, it appears that it is voluntary for the employer.

The notice makes no mention of nor seems to contemplate the employee making the election to defer. Therefore, this would appear to be a decision left to the employer.

What happens if an employee's pay exceeds \$4,000 for one biweekly pay period, but is below it for another?

The notice makes clear that the deferral is made on a paycheck to paycheck basis. So, the full payroll tax would be withheld in any bi-week pay period where pay exceeds \$4,000 and would be deferred in any other pay period where it is below \$4,000.

What happens if an employee no longer works for an employer once the deferral is over? Is the employer responsible for the unpaid taxes?

This is murky. The notice implies that the employer is responsible for the deferred taxes but provides that the deferred taxes are to be withheld from employees beginning in January. The notice goes on to state, "If necessary, the [employer] may make arrangements to otherwise collect the total Applicable Taxes from the employee." But the notice provides no further guidance as to what this might mean. It also provides no guidance on what happens if the person is no longer an employee and the employer is unable to collect the unpaid taxes.

Must an employer decide by September 1 whether to defer withholding or not?

The notice is silent on whether an employer must defer the withholding for the entire deferral period (September 1 to December 31) or whether an employer can start deferring at any point during the deferral period. Presumably an employer could elect to implement the deferral after September 1.

Can an employer continue to withhold the tax, but suspend depositing it with the Treasury?

No, the notice indicates that the deposit obligation is linked to when the tax is withheld.

What might happen next?

Employers will have to make their own decision about how to proceed. But it seems like two possible scenarios might play out:

Scenario 1: Congress takes no action and events unfold as contemplated in the notice. Employers that suspend withholding payroll taxes this year will have to increase withholding (doubling the withholding to 12.4%) beginning in January to recoup and remit the deferred taxes. (It is unclear if employers would be responsible for any unpaid taxes they were unable to recoup from former employees.) Employers who do not suspend the withholding of taxes this year will operate as normal this year and next.

Scenario 2: Congress acts to forgive the deferred taxes or provides a substitute policy. It is possible that Congress could act to simply forgive the deferred taxes though that would create an inequity for employees whose employer elected to not suspend withholding (or didn't suspend withholding for the whole period). Congress might attempt to address this through some substitute policy (e.g. eliminating the tax for a four-month period but giving the employer the ability to decide when to begin that four-month period).

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