

Executive Action Permits Employers to Defer Employee Payroll Tax, but Uncertainties Remain

An Executive Memorandum from the White House dated August 11, 2020 directed the United States Secretary of the Treasury to use disaster-relief authority under Section 7508A of the Internal Revenue Code to permit deferral of the obligation to withhold and pay employee payroll taxes for the period from September 1, 2020 to December 31, 2020.

The Internal Revenue Service did not issue follow-up guidance until August 28, 2020, which was too late for many employers to take the option into account for the September 1 start date.

Moreover, while the guidance answers some questions, there are still unresolved issues for employers. As a result, although the intent of the executive action is to provide additional “take-home pay” by deferring payroll tax obligations, the “safe harbor” for employers may be to continue to withhold and pay the tax.

Option, Not Mandate. The executive actions do not *require* any employer to take any actions. The actions provide a means for employers to provide additional “take-home pay” for disaster relief by choosing not to withhold and pay from qualifying employees the employee obligation that would otherwise be withheld.

No employer is required to defer the withholding. The executive actions provide that no penalty will result if qualifying taxes are not withheld during the qualifying period. It is an option, not a mandate.

Deferral, Not Forgiveness. The guidance makes clear that the tax subject to the executive action is *deferred* and not forgiven. That is – unless there is subsequent congressional action to forgive the tax – the tax that is not withheld during the qualifying period must still be paid in the future.

The IRS guidance indicates that employers must withhold additional funds from employee payroll during the period from January 1, 2021 to April 30, 2021 to make up for the tax not withheld from the employee’s pay during 2020. Such additional withholding must be applied “ratably” according to the guidance.

Effectively, then, the additional “take-home pay” in 2020 would be offset by reduced “take-home pay” in 2021 – absent additional policy changes in the meantime.

Repayment Obligation. The guidance provides that if the deferred taxes are not paid from the “ratable” additional withholding during 2021, then the employer “may make arrangements to otherwise collect the total Applicable Taxes from the employee.”

There is no additional guidance as to what “arrangements” are required, but -- given the employer’s obligation to withhold and pay the payroll tax from the employee’s compensation – employers would appear to have few options beyond imposing a lump-sum payment on employees who leave employment or paying the additional tax themselves.

For employers likely to have employee turnover, the risk of interest or penalties on unpaid taxes could be significant if taxes are deferred but the employee is no longer receiving payroll in 2021 from which to withhold the required additional amounts.

Applicable Wages. The Executive Memorandum limited the deferral without penalty to employees receiving wages or compensation less than a threshold amount of \$4,000 per bi-weekly pay period or a comparable amount for other pay periods. On an annual basis, the limitation amounts to \$104,000 of annual compensation.

The guidance clarifies, however, that the limitation is to be applied for each pay period. So if an employee makes more than \$4,000 (or the equivalent amount) for the pay period, then the deferral is not allowed. If the employee makes less for the pay period then the deferral is allowed regardless of the employee's compensation in other pay periods.

In light of the complexities and the obligation to withhold additional amounts in 2021, many employers may choose the safest route is to decline the option to defer the tax.

Vandenack Weaver attorneys can assist with questions about the payroll tax deferral and other COVID-19 related employment issues by contacting us at 402-504-1300 or info@vwattys.com.