Employee Payroll Tax Deferral:

WHAT WE KNOW, WHAT'S STILL UNCLEAR & WHAT IT MEANS FOR YOUR ORGANIZATION

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How We Got Here

- Quick refresher:
  - Failed Stimulus 4.0 talks led to President Trump taking executive action in an attempt to provide additional relief by targeting evictions, unemployment, student loans and payroll taxes.
  - Actions consisted of one executive order and three presidential memorandums issued on Saturday, August 8, 2020.
  - Temporary payroll tax deferral received the most attention; however, the president's memorandum provided little detail regarding mechanics of how this would work and directed Treasury to issue additional guidance.
  - Notice 2020-65: 2 ½ pages of guidance issued August 28 addresses some of the practical considerations but still leaves some open unanswered questions.

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Memorandum on Deferring Payroll Tax Obligations in Light of the Ongoing COVID-19 Disaster

Memorandum provides for the deferral of employee Social Security on:

> "…wages or compensation, as applicable, paid during the period of September 1, 2020, through December 31, 2020, subject to the following conditions:
>
> > (a) 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.
> >
> > (b) Amounts deferred pursuant to the implementation of this memorandum shall be deferred without any penalties, interest, additional amount, or addition to the tax."

***Different from the employer Social Security deferral allowed under the CARES Act**

Additional Guidance Provided

On August 28, 2020, Treasury released Notice 2020-65:

Optional for employer and employee:

- With the guidance released on August 28, employers officially have the option of not providing this deferral.

- “The guidance allows employers to defer withholding and paying the employee’s portion of the Social Security payroll tax if the employee’s wages are below a certain amount.”
  - The wording “allows” (as opposed to “requires”) provides the option.

Additional Guidance Provided

- Deferral based on bi-weekly taxable Social Security wages of less than $4,000 (weekly less than $2,000). An employee could be eligible one pay and not eligible the next, since each pay is looked at separately.
  - Note: The maximum deduction for 2020 is $8,537.40.

- Any tax deferred must be deposited by employers no later than April 30, 2021 (penalties and interest begin to accrue on May 1).

- “If necessary, the Affected Taxpayer may make arrangements to otherwise collect the total Applicable Taxes from the employee.”
  - The “Affected Taxpayer” has been identified as the employer – the employer is responsible for collecting and paying these deferred taxes.

- This liability will remain the employer’s regardless of if, when or how the money is collected from the employee.

Additional Considerations and Unknowns

Considerations

- This remains a deferral, not a waiver
- A new Form 941 and W-2 format will likely be created to report the deferrals
- If an employer must pay the employee's deferred tax for them in 2021, this tax payment then becomes taxable wages to the employee (with additional tax requirements paid by the employer)
  - For example:

    Employer pays the employee's deferred tax of $1,000
    Employee taxable wages to cover the tax = $1,082.84
    Social Security tax for employer and employee = $134.27
    Medicare tax for employer and employee = $31.40

    Total employer liability = $1,165.67

Unknowns

- Would a separate Social Security tax "code" be set up to track the deferral that is then "paid down"?
- How does this deferral apply to the self-employed?

Next Steps

1. Prepare a communication to employees – are you as the employer opting in or out?

2. If opting in, prepare a form for the employee to sign outlining:
   - This is a deferral not a waiver
   - The deferred tax limitations (the $4,000 per bi-weekly pay)
   - The money must be collected from them, to be deposited by you, no later than April 30, 2021 and provide the details of the repayment (for example, collected back over the first four pays in 2021)
   - They will be required to sign a document agreeing to the payback terms
   - They will be responsible for paying the balance (provide due date) of any unpaid taxes if their employment terminates before April 30

3. Regularly check in with your payroll provider or payroll software company on their process for managing this deferral (both with the deferral in 2020 and the payback in 2021)

Q: There seems to be some amount of flexibility with how organizations can approach this issue – can you summarize some of the approaches you are seeing?

This will continue to evolve as time passes but here are a few approaches we are hearing about:

- Opt out – Elect not to defer and simply continue to withhold and deposit the employee's payroll tax obligation
- Permit deferrals only at the employee's election
- Require deferral for all employees
- Continue withholding and depositing, but offer employees a nominal bonus to acknowledge the lack of deferral benefit, while easing the organization's own administrative burden of a short-term implementation

Q: Should my organization offer this deferral option to employees?

This is an individual decision for each and every organization.

We are hearing that many organizations are planning to opt-out and continue withholding and depositing taxes as normal; however, each employer must weigh the administrative burden and risk of potentially having to pay for employees who are no longer employed with the potential for employee legal action if the deferred tax is later forgiven.

Q: What are some of the pros vs. cons of opting-in to this deferral?

Pros

- Payroll tax holiday for employees – basically it's a short-term, interest-free loan that provides a little extra cash to employees for the next four months.

Cons

- Administrative burden for employers
- Deferral, not forgiveness: Absent legislative changes forgiving the tax, employees will be required to **repay** through payroll deductions from January through April 2021
- **Employers** are responsible for paying the deferred taxes, even if the money has not been collected, no later than April 30, 2021
- Could result in additional taxes and payroll related benefits if the taxes are paid without collection

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Q: What else should my organization be thinking about as it relates to opting-in to this deferral?

- Consider the need to record a liability for the deferred taxes on year-end balance sheet
- Budgeting and preparing to pay the deferral if it is not collected from the employee
- Is there any impact on PPP loan/forgiveness calculations? No
- Confirm retirement plan impact to the wage calculation for 2021 for those taxes paid by the employer
  - Are these grossed-up wages eligible for retirement plan deferral? If so, consider that cost.

THANK YOU

Questions?

- Contact your RKL advisor
- Visit RKL's Business Recovery Resource Center for more updates and guidance

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