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**LEGAL ALERT****Executive Memo on Payroll Tax Deferral**

On August 8th, 2020, President Trump signed an Executive Memorandum (“Memo”) directing the Secretary of the Treasury to defer the withholding, deposit, and payment of employee payroll/Social Security taxes. Under 26 U.S.C. 3101(a), that tax is 6.2% of an employee’s wages (up to \$137,700). This deferral would only be available for employees who make \$4,000 or less on a biweekly basis, or \$104,000 annually. The deferral would be effective beginning September 1, 2020, and run through December 31, 2020.

The Memo instructed the Secretary of the Treasury to release further guidance, to supplement the known details, and on Friday, August 28th, the IRS released guidance in Notice 2020-65.

First, It should be noted that the President does not have the authority to provide for tax forgiveness, so this deferral is essentially a loan. If utilized, the deferral would stop the withholding of the 6.2% payroll tax, which may mean more money in an employee’s pocket with each paycheck. However, because the deferral is only effective through the end of 2020, the Memo currently contemplates employees being required to pay this deferred tax beginning with the first paychecks of 2021. The IRS’ guidance clarified this point. As predicted, the deferral will be effective from the beginning of September, through the end of December of 2020. Beginning January 1, 2021, the repayment period is to begin and employees who had their payroll tax withholding deferred will begin repaying those deferred taxes. In effect, this results in increased tax withholding for the first four months of 2021. For employees with a fixed salary, this translates to a doubling of their payroll tax withholdings from January through April of 2021. The Administration is hopeful that Congress will allow for a forgiveness of the deferred payroll taxes, but that idea has not been well-received by Congress to this point. Many businesses, as well as the U.S. Chamber of Commerce have taken the position that this deferral would do more harm than good, as it would leave employees with a burdensome tax bill in 2021.

In addition to the burden created for employees, there appears to be

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substantial burden for employers as well. The Memo and the guidance released by the IRS both implicate employers as being responsible for withholding and remitting any deferred taxes in 2021. However, this raises issues if an employee leaves the business before he or she has fully repaid the deferred taxes. Currently, neither the Memo nor the IRS has provided any clarity as to how an employer is to collect deferred taxes from an employee who is no longer with the company.

Adding to the list of unknowns, neither the Memo nor the IRS appears to affirmatively require that employers take any particular action, whether that is to utilize the deferral or not. As mentioned, many businesses have stated they will not utilize the deferral, but it is unclear what latitude an employer would actually have in this regard.

Another consideration for employers is the resources that would be involved in altering their existing payroll tax withholding protocols. For many employers, the withholding process is done by software, and it is unclear whether any popular software programs, or accounting departments generally, are currently equipped to make changes that would be on a temporary basis, and that would only apply to employees that make earn below a certain amount of wages. Further, it can be expected that Form 941, the form used by an employer to report payroll taxes, will be modified this year, but to what extent is unknown.

As pointed out, the deferral will likely incur a cost of both time and resources to implement, and employers may determine that the benefit to employees is not substantial enough to incur that cost. The decision on whether to utilize the deferral period is ultimately up to the employer. However, given our current understanding, KTJ is hesitant to advise using the deferral due to the relatively limited benefit it provides to employees and the responsibility it creates for employees to modify their withholding procedures and collect payroll taxes in 2021 from employees that may or may not be with the business at that point.

KTJ will continue to monitor the situation and will review any further guidance that is to come. In the meantime, please do not hesitate to contact us with any questions that may not have been covered here.