Actions on Payroll Taxes and Unemployment Benefits Promise Relief, Raise Questions

Payroll managers should be prepared to make withholding changes by Sept. 1

By Stephen Miller, CEBS August 10, 2020 SHRM.org

On Aug. 8, President Donald Trump signed a series of executive orders and memorandums intended to provide financial relief to employees and those who have lost their jobs due to the COVID-19 pandemic.

These declarations included a Memorandum on Deferring Payroll Tax Obligations in Light of the Ongoing COVID-19 Disaster, which directed the Treasury Department to defer collection of the employee portion of Social Security FICA taxes—part of required payroll tax withholding—from Sept. 1 through the end of 2020. The deferred taxes may have to be subsequently repaid unless Congress enacts legislation stating otherwise.

Trump cited his authority to postpone certain tax deadlines by reason of a presidentially declared disaster. Democrats, however, are expected to challenge that claim in court. Nevertheless, it is prudent for employers and payroll managers to stay aware of developments and prepare to move quickly if the directive and upcoming guidance are not blocked or superseded by enactment of a comprehensive relief bill.

Payroll tax relief, as outlined in the president's directive, would require employers to take steps to ensure compliance, including working with their payroll administrators to adjust their systems by Sept. 1. Employers would also need to explain to employees that while their take-home pay may go up in the short term, they may be required to repay these deferred taxes at a future date.

Details on employer requirements, however, would depend on Treasury Department guidance, expected to be issued shortly.

The other presidential actions called on regulators to allow a weekly supplemental unemployment benefit of up to $400, with $300 to be paid by the federal government and an option for states to add an additional $100. That amount would be down from the $600 weekly supplement that expired July 31. The president also called for continued student loan payment relief and for measures to prevent residential evictions and foreclosures resulting from financial hardships due to COVID-19.

Reduced Unemployment Insurance Supplement

Republicans in Congress argued that the initial $600 federal supplemental payment disincentivized recipients from seeking jobs, since many were collecting more money unemployed than employed. Some wanted the program reduced to $200 per week, while Democrats argued the program should be renewed at the original $600 per week.

Questions were raised about funding for the $400 unemployment insurance boost, which would pull from FEMA's Disaster Relief Fund to pay for a portion of the supplemental benefits while asking states to fund the remainder. Because states may not use the unemployment program to pay benefits unless they are authorized by Congress, they may have to set up a new system to pay their portion of the supplement.

Unemployment experts were also unsure about how funds will be distributed, who will qualify for benefits and how long the benefits will last, pending regulatory guidance.

FICA Taxes

Social Security and Medicare payroll taxes are collected together as the Federal Insurance Contributions Act (FICA) tax. FICA tax rates are statutorily set and are not adjusted for inflation.

Social Security is financed by a 12.4 percent payroll tax on wages up to employees' taxable earnings cap—$137,700 for 2020—with half (6.2 percent) paid by workers and the other half paid by employers. There is no earnings cap on the Medicare portion of FICA, for which employers and employees separately pay a 1.45 percent wage tax.

The COVID-19-related payroll tax relief only applies to the Social Security portion of FICA.

The Payroll Tax Directive

Section 2302 of the Coronavirus Aid, Relief, and Economic Security (CARES) Act, enacted in March and implemented through IRS Notice 2020-22 and a series of IRS FAQs, allows eligible employers to defer the deposit and payment of the *employer's* share of Social Security FICA taxes for the period beginning March 27, 2020, through Dec. 31, 2020. The deferral also applies to 50 percent of the equivalent taxes incurred by self-employed persons. The deferred payments must subsequently be paid to the Treasury Department, with half due by Dec. 31, 2021, and the other half by Dec. 31, 2022.

The CARES Act provision and related guidance did not apply to *employees'* share of the Social Security tax.

Under the new presidential directive:

- The secretary of the treasury is authorized to defer the withholding, deposit and payment to the Treasury of employees' portion of Social Security payroll taxes on applicable wages or compensation paid from Sept. 1, 2020, through Dec. 31, 2020. This provision does not apply to the Medicare portion of FICA taxes.
- The deferral is to be made available to employees whose earnings during any biweekly pay period is generally less than $4,000, calculated on a pretax basis, which would cover salaried employees earning $104,000 or less per year.
- Social Security taxes for these employees will be deferred without any penalties, interest, additional amount or addition to the tax.
- The secretary of the treasury is directed to issue guidance to implement the president's memorandum and to explore avenues, including legislation, to eliminate the obligation to pay the taxes deferred under the implementation of the memorandum.

Josh Blackman, a constitutional law professor at the South Texas College of Law Houston, blogged that HR lawyers will have until Sept. 1 "to figure out the details." Because the policy terminates on Dec. 31, 2020, "President Trump, or President Biden, will be forced to decide whether to continue this program," he wrote.

A Controversial Move

"By providing this tax relief, American families will have more cash on hand during these critical next few months," according to a White House statement.

White House economic advisor Larry Kudlow said that "we will take any steps possible to forgive this deferral," so employees will not be required to pay back the amounts deferred through Dec. 31, *The Hill* reported. However, doing so would require new legislation by Congress.

Presumptive Democratic presidential nominee Joe Biden charged that Trump would try to make the cuts permanent if re-elected and said doing so would "undermine the entire financial footing of Social Security."

Prepare to Adjust Systems and Notify Employees

For now, HR payroll managers should:

- Discuss with their payroll administrators steps to adjust their payroll systems to exclude employees' share of FICA Social Security taxes beginning Sept. 1, if that becomes necessary, pending the issuance of Treasury guidance.
- Prepare to notify employees that possibly less of their pay will be subject to payroll withholding, although the reduction in payroll taxes may have to be paid back in the future, possibly when filing their 2020 income tax return.
- Expect questions from employees who may be confused about paycheck adjustments.

A Wait and See Approach

Melissa Ostrower and Robert Perry, principals in the New York City office of law firm Jackson Lewis, "recommend that employers continue to monitor applicable guidance, but not make any changes to their payroll withholding processes at this time."

They added, "We realize that changes to payroll systems require lead time, but given the uncertainty surrounding how the deferral will be implemented and whether it actually will become effective, we think this is the most prudent course at this time."

UPDATE:

Payroll Providers Weigh In

On Aug. 14, the American Payroll Association and the National Payroll Reporting Consortium submitted a letter to the U.S. Treasury and IRS regarding the guidance being crafted to help employers defer employees' Social Security payroll taxes. The letter outlines six employer priorities for the regulators' consideration regarding initial guidance:

- Any requirement that employees opt in or out of the deferral could result in employers having to manage informational notices and election forms of potentially over 100 million employees in coming weeks. Regardless of whether any election is required, the guidance should permit it to be electronic.

- Clarify that employers will not be held liable for employee Social Security taxes deferred. Employees should pay any deferred amount with the 2020 income tax return, IRS Form 1040.

- Minimize related reporting requirements. Optimally, there should be no new entry boxes on Forms W-2 or 941. Qualifying Social Security wages paid from Sept. 1 through Dec. 31, and/or Social Security tax deferred, could be a coded entry I Box 12 of Form W-2.

- Clarify that employers should apply only a per-day period amount (e.g., $4,000 biweekly) to determine eligibility. Each payment of wages should be evaluated in isolation.

- There should be no phase-out formula for employees near the $4,000 biweekly level.

- If an employer implements the deferral program after September, there should be no adjustment for prior payrolls.

Employers' Questions Await Guidance

The president's executive memorandum "leaves open a number of questions and issues, some of which will likely be addressed by guidance from Treasury," according to an Aug. 9 legal alert by Adam Cohen, Mary Monahan and Robert Neis, partners at law firm Eversheds Sutherland in Washington, D.C. Issues to be addressed, they said, include:

- Whether the deferral is voluntary on the part of employers, and whether an employer may deposit and pay employees' deferred taxes at any time prior to the applicable due date.

- Whether employers will be required to withhold all of the deferred amounts from the first paycheck on or after January 2021, or if there be an extended time for collection and deposit? "A lump sum repayment could cause significant financial hardship for some employees, particularly if it is required right after the holiday season," Cohen, Monahan and Neis noted.

- What to do with respect to employees who terminate employment before Jan. 1, 2021. "To the extent the employee portion of [Social Security payroll taxes] was deferred, an employer may want to withhold it from paychecks prior to termination of employment, unless there is guidance permitting the employee to pay the deferred portion on their federal income tax return or by other means," the attorneys explained. "For lower-paid employees, this may eliminate one or more paychecks at the end of their tenure. In some situations, the employer may end up bearing the cost of the taxes as a practical matter."

- Whether an employer can use the deferral with respect to some groups of qualifying employees, but not others, where that may be desirable for payroll administration or other reasons.

- How overtime pay or other variable pay, such as commissions and bonuses, should be taken into account in calculating the $4,000 threshold. "It appears that base pay or wages may be the proper metric in most cases, but further elaboration by Treasury is needed," Cohen, Monahan and Neis said.

SHRM Senior Legal Editor Lisa Nagele-Piazza contributed to this article.