



# IRS Notice 2020-65 Employee Social Security Tax Deferral: Too Little, Too Late?

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On August 28, 2020, the Department of Treasury (Treasury) and Internal Revenue Service (IRS) issued Notice 2020-65 (the Notice) providing long-awaited guidance to employers on the Presidential memorandum issued August 8, 2020, directing the Secretary of the Treasury to permit the *deferral* of the withholding, deposit, and payment of the employee portion of Social Security taxes for wages under the required dollar limit. The Notice, issued pursuant to the authority of section 7508A of the Internal Revenue Code (the Code), provides the basics for employers to implement the deferral. Unfortunately, there are significant employer and employee concerns with the program at this time. One of the primary concerns is the fact that, at this point, there are no guarantees that the government will ultimately allow *forgiveness* of the taxes deferred.

This blog discusses the following options for employers:

- “Ignore” the deferral opportunity and continue full social security tax withholding through year-end
- Same as above but provide a small amount of additional wages to those employees that would have been eligible for deferral
- Implement the deferral for all employees under the dollar limit
- Allow eligible employees to individually elect deferral

## THE BASICS

Notice 2020-65 authorizes the deferral of the 6.2% of employee-paid Social Security tax (and railroad retirement tax equivalent) on the first \$137,700 of wages for payroll tax obligations beginning September 1, 2020 through December 31, 2020 (Applicable Taxes). The amount deferred in 2020 must be withheld pro-rata from the 2021 wages paid beginning January 1 through April 30. The Notice applies to all employers (Applicable Taxpayer), including federal, state, and non-profit employers. The Notice does not provide any information for independent contractors or other self-employed individuals.

Importantly, the Social Security tax deferral can only be from “Applicable Wages,” which includes only those Applicable Wages that relate to a pay date occurring in the period beginning September 1, 2020 and ending

December 31, 2020. Applicable Wages are those defined in Code sections 3121(a) and 3231(e), which define Social Security and railroad retirement wages. Thus, for example, wages such as health insurance premiums not subject to Social Security tax would not be included as Applicable Wages.

The relief described in the Notice only applies if the employee's taxable wages are below \$4,000 during a bi-weekly pay period (or the equivalent threshold amount with respect to other pay periods; e.g., \$2,000 weekly or \$4,333 bi-monthly). This is an "all or nothing" provision. For example, if an employee's Code section 3121(a) wages are \$4,000 or more by even \$1.00 during a pay period, then no deferral may be made for that pay period. If wages are less than \$4,000 in a given pay period, then deferral of Social Security taxes from those wages may be made, even if the employee exceeds the threshold in a prior or subsequent pay period. For example, if an employee's bi-weekly wages for September 1 through December 15 are \$3,500 but the employee receives a \$1,000 year-end bonus (in addition to regular compensation) in the last pay period of December 2020, then no deferral may be made in that last pay period.

As mentioned earlier, payment of the deferred taxes is postponed until the period beginning January 1, 2021 and ending April 30, 2021. During this period, the employer must withhold and pay the deferred Social Security taxes (or make arrangements to otherwise collect the taxes). Payment of the deferred taxes will be in addition to any Social Security taxes that must be withheld beginning January 2021. If arrangements are not made to collect the deferred taxes, interest and penalties will begin to accrue May 1, 2021.

## MANDATORY OR OPTIONAL

The first question for employers is whether the implementation of the deferral is permissive or mandatory. The language of the Notice simply states that the due date for withholding and payment of "deferral pursuant to the Notice" is extended to 2021, at which point the deferred withholding is made up by a pro-rata withholding from wages from January 1, 2021 through April 30, 2021.

However, shortly after release of the Notice, Secretary of the Treasury Mnuchin commented that the delayed withholding and payment is *not* mandatory. Thus, although the original plan behind the deferral was to make it widespread to provide relief to employees in 2020, the ultimate guidance does not appear to force the employer to make a decision to defer or not to defer.

Certain state law prohibitions on wage deductions could be interpreted as *requiring* implementation of the deferral program by prohibiting deduction of Social Security taxes during the program period, but the most likely outcome is that the states will not get involved with the issue.

On a related note, the Notice did not address whether employees could be provided the choice of electing the deferral or electing out of the deferral should the employer choose to implement. It appears that the better answer is that employee elections would be permitted due to the absence of a prohibition in the Notice.

## EMPLOYER AND EMPLOYEE LIABILITY

As described, employees are liable for the Social Security taxes deferred, and those taxes must be withheld and paid in early 2021. However, the employer is also liable. Section 31.3202-1(e) of the Treasury Regulations, as well as Code section 3202(b), cause the employer to be liable for the employee Social Security tax whether or not withheld from the employee's wages. Unfortunately, this continues even after the employee has terminated. The bottom line is that the employer remains liable for the employee tax despite the deferred due-date provided by Notice 2020-65.

Note that some practitioners have expressed concerns regarding the "responsible party" liability of Code section 6672, which imposes liability on the individual responsible to "collect, truthfully account for, and pay over" employment taxes, including employee Social Security taxes. However, the section 6672 liability applies to the *withheld* tax. Thus, while the employer remains liable for non-withheld employee Social Security taxes, the individual responsible parties—which may include employees, directors, or agents—do not.

# NOTICE 2020-65 BEST PRACTICES

Because employers remain liable for the 2020 non-withheld taxes, many employers will understandably not wish to implement the deferral. Employees may be split on whether their employer should implement; some will want the immediate increase in paycheck for the remainder of 2020 while banking on a Congressional forgiveness of the amount deferred, whereas others may be concerned about the requirement to pay the taxes back in 2021 if there is not a legislative fix. Many believe that a legislative fix to include deferral forgiveness is imperative to making this program work.

For employers that are still exploring offering the deferral, the following actions must be considered:

- First and foremost, communicate with payroll and payroll vendors to determine the feasibility of implementing both the deferral, which may fluctuate for employees should their pay-date payments exceed \$4,000, as well as challenges regarding the payback of the deferred taxes through possible double deductions in 2021.
- If the deferral is feasible, consider whether to allow employees to opt in and opt out and communicate with payroll to determine whether such elections can also be administered.
- If, based on the preceding, the deferral is feasible, convey to employees the deferral opportunity coupled with the information that the “make-up” in 2021 will occur pro-rata over the first four months. Inform employees that this could result in approximately a double Social Security deduction at that time.
- Employees who have the deferral implemented should sign an agreement acknowledging the additional withholding (up to twice the normal amount of Social Security taxes) in the period from January 1 through April 30, 2021.
- Collectively bargained agreements and/or state law may limit the collection alternatives if there is no employee agreement in place.
- Such agreement should provide that the employer is authorized to withhold from other wages at a higher rate or request a check from the employee should the employee terminate prior to such a time when all deferred tax has been repaid.
- Similarly, be prepared for difficulties in executing the 2021 payback for employees whose salaries have decreased.

## WINSTON TAKEAWAY

The ability to defer withholding of the employee portion of the Social Security tax may or may not be welcome to many employers because of their continued liability for the employee Social Security tax, whether or not withheld from the employee’s wages. Employees whose wages fall under the \$4,000 threshold may also be split with respect to their desire for deferral. For employers and employees there are both pros and cons to this tax deferral.

Employers who are interested in taking advantage of this deferral will need to consult with their payroll vendors regarding how this change can be implemented, when this change can be implemented, whether there will be additional costs for programming and communications to employees, and how deferrals will be collected from employees who die, become disabled or terminate employment. In addition, employers will need to clarify with their vendor and clearly communicate with employees the method that will be used to repay the deferred taxes beginning in January 2021.

For employees, the consideration is whether having the increase in their paychecks from September to December of 2020 is worth the risk of having to pay up to double the regular rate of Social Security taxes in the first four months of 2021 if legislative forgiveness is not provided.

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