

Penalty for Failure to Deposit Employment Taxes

Cross References

- Notice 2020-22

The IRS recently announced penalty relief for certain employment tax deposits of FICA, RRTA, and federal income tax withholding. The relief applies to employers entitled to the new refundable tax credit provisions under the Families First Coronavirus Response Act (Families First Act, Public Law 116-127) and the Coronavirus Aid, Relief, and Economic Security Act (CARES Act, Public Law 116-136).

The CARES Act provides for a refundable tax credit up to 50% of the qualified retention wages paid, including allocable qualified health expenses, limited to \$10,000 per employee, if such wages are paid by an employer experiencing a full or partial business suspension due to orders from a governmental authority due to the coronavirus disease 2019 (COVID-19), or experiencing a statutorily specified decline in business.

Under the CARES Act, the payment and deposit of the employer's share of the Social Security portion of FICA tax and the employer's share of the Social Security portion of RRTA tax for deposits that are due to be made during the period beginning on March 27, 2020, and ending before January 1, 2021, is not due until December 31, 2021 for the first 50% of the liability, and December 31, 2022 for the remaining 50% of the liability. Under this provision, an employer is treated as having timely made these required deposits of FICA and RRTA taxes if all such deposits are made no later than these applicable due dates. This deferral does not apply to employers that have had indebtedness forgiven under other provisions of the CARES Act.

Although Form 941 is due quarterly and payment and deposit of the above described employment taxes is deferred, the Internal Revenue Code generally requires deposits of employment taxes to be made on a monthly or bi-weekly basis. A penalty applies when the employer fails to deposit employment taxes on a timely basis. Notice 2020-22 provides relief from this penalty under circumstances describe below.

The Families First Act generally requires employers of fewer than 500 employees to provide paid sick leave and expanded family and medical leave for employees unable to work or telework due to certain circumstances related to COVID-19. Employers that are required to pay qualified leave wages are entitled to a refundable tax credit. This refundable tax credit may be claimed against the employer's share of the Social Security portion of FICA or RRTA tax in an amount equal to 100% of the qualified leave wages paid plus qualified health plan expenses allocated to such wages. Qualified leave wages for purposes of the refundable tax credit are those wages paid for the period starting April 1, 2020 and ending on December 31, 2020 that are required to be paid under the Families First Act.

Qualified leave wages are not subject to the Social Security portion of FICA or RRTA, so if the employer claims the credit on Form 941, it is taken against FICA tax imposed on other wages that are subject to FICA, the employer's share of Medicare tax imposed on qualified leave wages, plus any federal income tax withholding. If the credit exceeds the total employment tax liability for that quarter, the credit may be claimed as an overpayment on Form 941.

The employer also has the option to claim an advance payment of the refundable tax credit by filing Form 7200, *Advance Payment of Employer Credits Due to COVID-19*.

The CARES Act also provides for a refundable tax credit against an employer's creditable employment taxes for each calendar quarter for qualified retention wages paid by the employer. This refundable tax credit may also be claimed on Form 941 or Form 7200.

Relief From Failure to Make a Deposit of Taxes

Notice 2020-22 states an employer will not be subject to a penalty under IRC section 6656 for failing to deposit employment taxes relating to qualified leave wages in a calendar quarter if:

- 1) The employer paid qualified leave wages to its employees in the calendar quarter prior to the time of the required deposit,
- 2) The amount of employment taxes that the employer does not timely deposit is less than or equal to the amount of the employer's anticipated credits under the Families First Act for the calendar quarter as of the time of the required deposit, and
- 3) The employer did not seek payment of an advance credit by filing Form 7200 with respect to the anticipated credits it relied upon to reduce its deposits.

Thus, an employer may reduce, without a penalty, the amount of a deposit of employment taxes by the amount of qualified leave wages and qualified health plan expenses paid during the calendar quarter prior to the required deposit, plus the amount of the employer's share of Medicare tax on such qualified leave wages, as long as the employer does not also seek an advance credit with regard to the same amount.

The total amount of any reduction in any required deposit may not exceed the total amount of qualified leave wages and qualified health plan expenses and the employer's share of Medicare tax on the qualified leave wages in the calendar quarter, minus any amount of qualified leave wages, qualified health plan expenses, and employer's share of Medicare tax that had been previously used:

- 1) To reduce a prior required deposit in the calendar quarter and obtain the relief provided by Notice 2020-22, or
- 2) To seek payment of an advance credit.

Notice 2020-22 also states an eligible employer will not be subject to a penalty under IRC section 6656 for failing to deposit employment taxes relating to qualified retention wages in a calendar quarter if:

- 1) The employer paid qualified retention wages to its employees in the calendar quarter prior to the time of the required deposit,

- 2) The amount of employment taxes the employer does not timely deposit, reduced by the amount of employment taxes not deposited in anticipation of the credits claimed for qualified leave wages, qualified health plan expenses, and the employer's share of Medicare tax on the qualified leave wages, is less than or equal to the amount of the employer's anticipated credits under the CARES Act of the calendar quarter as of the time of the required deposit, and
- 3) The employer did not seek payment of an advance credit by filing Form 7200 with respect to the anticipated credits if relied upon to reduce its deposits.

Thus, after a reduction, if any, of a deposit of employment taxes by the amount of credits anticipated on qualified leave wages, an employer may further reduce, without penalty, the amount of the deposit of employment taxes by the amount of qualified retention wages paid in the calendar quarter prior to the required deposit, as long as the employer does not also seek an advance credit for the same amount.

The total amount of any reduction in any required deposit may not exceed the total amount of qualified retention wages in the calendar quarter, minus any amount of qualified retention wages that had been previously used:

- 1) To reduce a prior required deposit in the calendar quarter and obtain the relief provided by Notice 2020-22, or
- 2) To seek payment of an advance credit.