April 3, 2020

IRS Announces Penalty Relief for Employers Who Fail to Deposit Employment Taxes in Anticipation of COVID-19-Related Tax Credits

Notice 2020-22 (Notice) provides penalty relief for employers who fail to deposit employment taxes in anticipation of the allowance of the new tax credits provided under the Families First Coronavirus Response Act (FFCRA) and the Coronavirus Aid, Relief, and Economic Security Act (CARES Act).

The FFCRA requires employers with fewer than 500 employees to provide employees with paid family leave and paid sick leave if they (or their families) are affected by COVID-19. Employers providing paid leave pursuant to the FFCRA are entitled to refundable tax credits which are designed to immediately reimburse them for the cost of providing COVID-19-related leave and maintaining health insurance coverage for affected employees. These tax credits are available with respect to wages paid between April 1 and December 31, 2020. The Notice refers to wages paid during periods of paid family leave and paid sick leave under the FFCRA as "Qualified Leave Wages".

The CARES Act provides eligible employers with a credit against employment taxes equal to 50 percent of wages paid or incurred after March 12, 2020, and before January 1, 2021. An employer is eligible for this credit if (i) its operations are partially or fully suspended by a government order due to COVID-19, or (ii) its gross receipts for the calendar quarter declined by more than 50' year-over-year. The total credit is limited to $10,000 per employee. Wages that qualify for this credit are referred to as "Qualified Retention Wages" in the Notice.

Employers are required to withhold federal income, Social Security and Medicare taxes from their employees' wages. Normally, these withheld amounts must be deposited with the Internal Revenue Service (IRS) along with the employer's share of Social Security and Medicare taxes. Failure to deposit these employment taxes results in the imposition of a penalty under Section 6656 of the Internal Revenue Code of 1986, as amended (Code). The Notice provides that the penalty under Code Section 6656 will not apply to an employer's failure to deposit employment taxes for a calendar quarter if:

With respect to Qualified Leave Wages:

- Such wages were paid in the calendar quarter prior to the time of the required deposit;
- The amount of employment taxes not timely deposited does not exceed the amount of the employer's anticipated credits under the FFCRA; and
- The employer did not seek payment of an advance credit with respect to such anticipated credits.

With respect to Qualified Retention Wages:

- Such wages were paid in the calendar quarter prior to the time of the required deposit;
- The amount of employment taxes not timely deposited, reduced by the amount of employment taxes not timely deposited in anticipation of credits under the FFCRA, does not exceed the amount of the employer's anticipated credits under the CARES Act; and
- The employer did not seek payment of an advance credit with respect to such anticipated credits.

Accordingly, employers are able to pay Qualified Leave Wages and Qualified Retention Wages using employment taxes that they would otherwise deposit with the IRS without incurring a failure to deposit penalty.

If the amount of Qualified Leave Wages and Qualified Retention Wages exceeds the amount of employment taxes that would otherwise be deposited with the IRS, the employer may claim an accelerated refund from the IRS by filing Form 7200, Advance Payment of Employer Credits Due to COVID-19.

The IRS has also released a list of 66 frequently asked questions regarding COVID-19-related tax credits.

For more Day Pitney alerts and articles related to the impact of COVID-19, as well as information from other reliable sources, please visit our COVID-19 Resource Center.

COVID-19 DISCLAIMER: As you are aware, as a result of the COVID-19 pandemic, things are changing quickly and the effect, enforceability and interpretation of laws may be affected by future events. The material set forth in this document is not an unequivocal statement of law, but instead represents our best interpretation of where things stand as of the date of first publication. We have not attempted to address the potential impacts of all local, state and federal orders that may have been issued in response to the COVID-19 pandemic.

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