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**Attachments:** 1. 20-0011333 Resolution, 2. Optional Payroll Tax Deferral Program Power Point Final.pdf

Date	Ver.	Action By	Action	Result
10/15/2020	1	City Council	continued	Pass

**REPORT TO THE CITY COUNCIL**

**October 15, 2020**

**FROM:** MICHAEL LIMA, Controller/Finance Director  
Finance Department

**SUBJECT**

\*\*\*RESOLUTION - Authorizing and directing Finance to decline City participation in the optional federal payroll tax deferral program (Subject to Mayor's veto).

**RECOMMENDATION**

Staff recommends that Council approve the accompanying Resolution authorizing and directing the Finance Department to decline City participation in the optional federal payroll tax deferral program.

**EXECUTIVE SUMMARY**

By executive order, the federal government has established a payroll tax deferral program. The program would allow employers to defer certain payroll tax obligations, specifically the Social Security payroll tax, from September 1, 2020 to December 31, 2020. Any employee who deferred taxes would need to repay them by May 1, 2021 to avoid penalties and interest. The program is voluntary for employers. Both the Finance Department and the City Attorney's Office have analyzed the program. It is the opinion of the Finance Department that City participation in this program would produce significant operational impacts, numerous legal issues, and greater financial liability. Thus,

staff recommends that the Council approve a resolution declining City participation in this program.

## **BACKGROUND**

President Donald Trump signed an Executive Order (85 FR 49587) on August 8, 2020. Under this order, employers can defer certain payroll tax obligations (specifically, the Social Security payroll tax) incurred between September 1, 2020 and December 31, 2020. The deferred taxes would need to be repaid by May 1, 2021, or penalties and interest will be assessed against the unpaid taxes. Participation in the program is optional.

There are approximately 400 City employees that currently have Social Security payroll tax deducted from their paychecks; and, thus would have these taxes deferred should the City choose to participate in the program. If participation is chosen, the City would be responsible for collecting and remitting the deferred tax in addition to the usual tax.

The Finance Department and the City Attorney's Office have jointly reviewed the program's requirements and analyzed its potential impact on the City. Both offices have concluded the following:

- The process to track and remit the payroll tax deferred from 400 employees on a bi-weekly basis would be manual, and not automated. The current payroll system does not have functionality to support this payroll deferral program. Additionally, such functionality would not be developed before the December 31, 2020 end of the program.
- A manual calculation and monitoring program would likely produce errors, which could result in the City incurring liability if the tax is incorrectly calculated.
- Employees participating in the program would likely not understand that the tax is deferred, not forgiven. Thus, they would likely not realize that the City will be deducting both the usual 6.5% tax and an additional 6.5% tax to repay the deferral from their paychecks between January 1, 2021 and May 1, 2021. The surprise additional deduction may result in impacted employees filing claims with the State Department of Labor alleging the City is unilaterally taking deductions from their paychecks in violation of California Labor Code. While the City would be shielded from liability in these claims, adjudicating these claims would take up staff time and resources that could be spent on other initiatives.
- There is no clear guidance on how an employer collects deferred taxes from an employee who separates from the employer between when the deferral starts and when the taxes are due. As the vast majority of City employees impacted by this program (should the City choose to participate) would be temporary employees, there is a strong likelihood that there will be at least some employees who leave City service before the deferred tax is recouped. There is a possibility that the employer could be liable for the un-recouped deferred tax, which cannot be determined at this time.

Given these issues, it is the recommendation of the Finance Department that the City not participate in the payroll tax deferral program, and that Council adopt the accompanying resolution codifying that recommendation. The City Attorney's Office confirmed participation in this program is optional and a policy decision.

## **ENVIRONMENTAL FINDINGS**

By the definition provided in the California Environmental Quality Act Guidelines Section 15378 this

item does not qualify as a “project” and is therefore exempt from the California Environmental Quality Act requirements.

### **LOCAL PREFERENCE**

Local preference was not considered because this Resolution does not include a bid or award of a construction or service contract.

### **FISCAL IMPACT**

Adopting this resolution will have no impact to the City’s finances. Not adopting this resolution will result in additional cost (unquantifiable at this time), and possibly create a future tax liability for the City.

Attachment: Resolution