Employee Retention Tax Credit: Eligibility & Tax Benefit

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Key ERTC Concepts

- Full or partial operation suspension due to government shutdown:
  - Requires a full or partial cease of operations mandated by government order.
    - An employer who was required to close their workplace, but continued operations through remote working does not meet the requirement.
    - Businesses with customers affected by a stay-at-home order or curfew are not considered to cease operations for this reason alone.
  - Generally, essential business permitted to remain operational do not qualify unless:
    - If suppliers of the essential businesses had operations suspended, that business may be considered to fully or partially cease operations, depending on the severity of the impact.
    - Operations may be considered partially suspended if business is permitted to remain open for certain essential functions, but not all.
  - Notice 2021-20 – Guidance on the Employee Retention Credit

Key ERTC Concepts

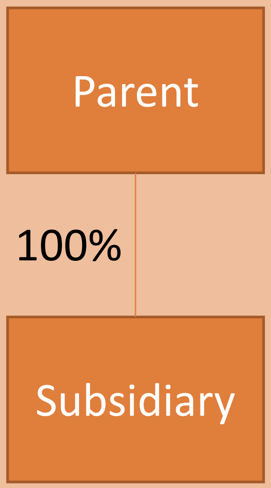
- Reduction in gross receipt factors:
  - The reduction must be tested at the controlled group level as determined by the ERTC aggregation rules.
  - General rule: compare gross receipts to same quarter of 2019.
    - In 2021, if business was not in existence during 2019 the business can use the corresponding quarter in 2020
  - Alternative Quarter Election: Allows businesses to use the immediately preceding quarter to determine gross receipts reduction qualification in current quarter.
- Number of Employees
  - Defined by section 4980H as an employee who during any calendar month during 2019 averaged at least 30 hours of service per week or 130 hours of service in the month.
- Qualified Wages
  - Employers need to determine whether they are considered a small or large employer, based on its number of employees during the credit period.
    - Small employers may include both wages and qualified health plan expenditures for all employees.
    - Large employers may only include wages and qualified health plan expenditures paid to employees not performing services.

Key ERTC Concepts

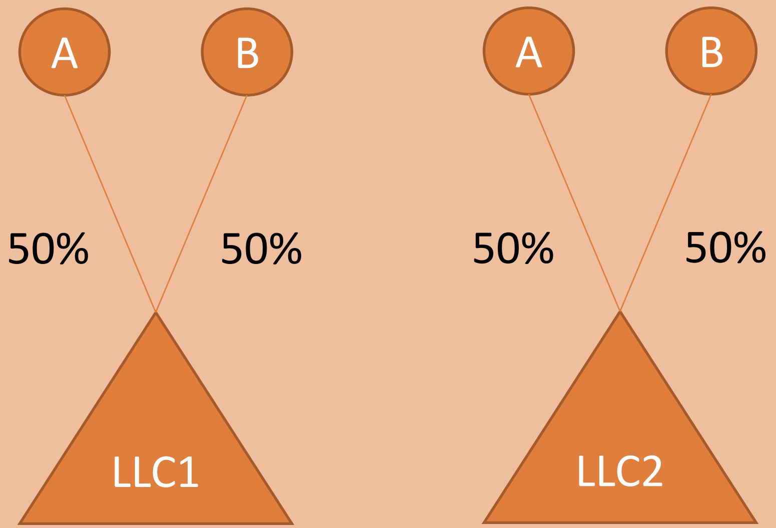
- Taxpayer Aggregation Rules
  - Both the gross receipts reduction and number of employee calculations need to include all business and taxpayers considered a single employer under Sec. 52(a) or (b) and Sec. 414(m) or (o).
    - Sec. 414 relates to affiliated service groups, while Sec. 52 covers a wider range of relationships including parent-subsidiary and brother-sister.
  - Sec. 52(a) provides rules for corporations.
    - A Parent-Subsidiary group exists when one corporation owns more than 50% of the voting power or value of a subsidiary corporation.
    - A Brother-Sister group exists when more than 80% of the voting power or value of two or more corporations is owned by five or fewer taxpayers. If more than 80% is owned by such a group, each shareholder's minimum ownership in all corporations is combined and must exceed 50%.
  - Sec. 52(b) provides similar rules for partnerships, trusts, estates and sole proprietorships.

Key ERTC Concepts – Taxpayer Aggregation Examples

AGGREGATED TAXPAYERS

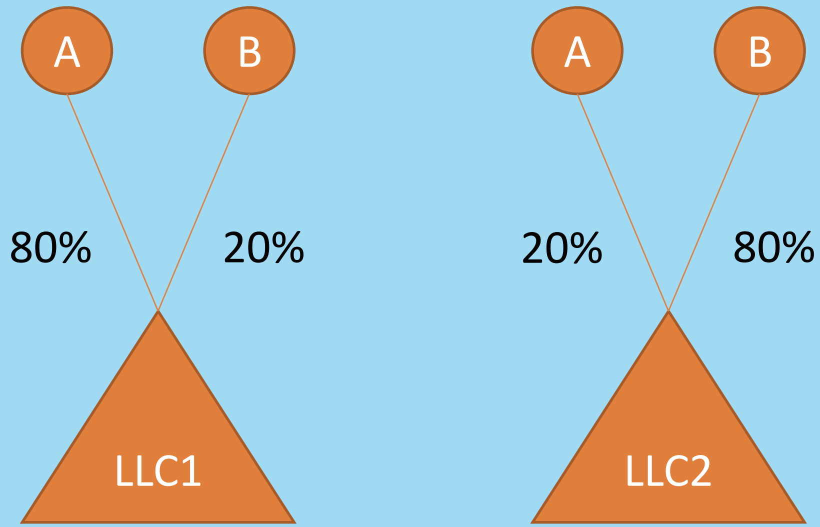


Parent owns 100% of Subsidiary



A & B each own 50% of both LLC1 and LLC2

NON-AGGREGATED TAXPAYERS



A owns 80% of LLC1 and 20% of LLC2 while B owns 20% of LLC1 and 80% of LLC2. While this meets the 80% test, it does not meet 50% test.

Key ERTC Concepts – Aggregation Cont.

- Aggregation may be a positive or negative
  - May result in a business which qualified under the reduction in gross receipts test on a stand-alone basis to be included in a group without a sufficient reduction.
    - Alternatively, a stand-alone business which does not qualify for the gross receipts test may be included in a group, which, when aggregated, has a sufficient reduction.
  - May require a business to be treated as a large taxpayer (over the employee threshold) when combined with aggregated entities.
- Aggregation for private equity structures
  - Additional factors need to be considered including whether the parent operates its own trade or business and its relationship to its investments.

Employee Retention Tax Credit (ERTC) History

- Originally implemented by the Coronavirus Aid, Relief and Economic Security Act (CARES Act) in March 2020.
  - The credit was to provide economic stimulus to employers continuing to pay wages during operational and economic difficulties caused by COVID-19.
  - 2020 Qualifying factors included:
    - A greater than 50% reduction in gross receipts or governmental shutdown
    - Excluded recipients of Payroll Protection Program (PPP) loans.
  - The amount of the 2020 credit was limited to the following amounts:
    - Maximum of $10,000 of qualified wages per employee for the period of 3/13/2020 – 12/31/2020.
      - For small employers (100 employees or less in 2020), all wages may be considered qualified.
      - For large employers (over 100 employees in 2020), only wages paid to employees not performing services may be considered qualified.
    - Employers are entitled to a tax credit of 50% of qualified wages.

Employee Retention Tax Credit (ERTC) History

- The Consolidated Appropriations and American Rescue Plan Acts of 2021 extended the credit through December 31, 2021. The eligibility for the credit in 2021 was adjusted from the CARES Act version in several ways.
  - Qualifying factors in 2021 included:
    - A greater than 20% reduction in gross receipts or governmental shutdown
    - Removed the exclusion of PPP loan recipients
  - The amount of the 2021 credit was limited to the following amounts:
    - Maximum of $10,000 of qualified wages per employee, per quarter for each quarter of 2021.
      - For small employers (500 employees or less in 2021), all wages may be considered qualified.
      - For large employers (over 500 employees in 2021), only wages paid to employees not performing services may be considered qualified.
    - Employers entitled to a tax credit of 70% of qualified wages.
  - Other changes included:
    - Retroactively allowed employers who received PPP loans to qualify for the credit in both 2020 & 2021 – provided that the same wages are not used to both qualify for PPP forgiveness and claim the ERTC.
    - IRS Statue of Limitation extended from 3 to 5 years for ERTC related items.

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	2020	2021
Covered Periods	**March 13, 2020 - December 31, 2020**	**January 1, 2021 – December 31, 2021**
Eligible Employer	1) Gov't Orders resulting in full or partial suspension of business operations during any calendar quarter 2) Significant decline in gross receipts for the calendar quarter compared to the same calendar quarter in 2019*	
Significant Decline	Greater than 50% decline	Greater than 20% decline
Qualified Wages	**Small Employer** (defined below): Wages paid to all employees **Large Employer:** Wages paid to employees not performing services	
Small Employer	100 or fewer employees	500 or fewer employees
Credit Amount	50% of qualified wages	70% of qualified wages
Maximum Credit	$5K per employee per year	$7K per employee per quarter
Claiming the Credit	Refundable Credit	

* For the 2021 credit a business that was not open in 2019 can compare gross receipts for the 2021 calendar quarter to the same calendar quarter in 2020.

How to Claim the ERTC

- Employers who qualify for the ERTC must report their qualified wages on their quarterly payroll return, generally Form 941.
  - Form 941 may be amended if qualified wages were incorrectly omitted, or for purposes of PPP loan recipients claiming the credit in 2020 after the CAA changes.
- The employer's share of social security tax due with the return will be reduced by the amount of the credit. Any excess credit is refundable.
  - Rather than receiving a refund, employers may opt to retain other employment taxes that would generally be deposited, such as payroll taxes and employee's share of social security tax.
- Small employers may request and advance of the ERTC by filing Form 7200 Advance Payment of Employer Credits Due to COVID-19
  - Advance payments cannot exceed 70% of the average quarterly wages paid by the employer in 2019. Special rules apply if the employer was not in existence in 2019.
- **The amount of any credit received reduces the employer's wages/employee benefits deduction for income tax purposes for that period.**

ERTC vs. PPP Forgiveness

- PPP loan recipients may qualify for the ERTC. However, the same wages cannot be used for both PPP loan forgiveness and the ERTC.
  - An employer may elect not to claim qualified wages for the ERTC so that such wages can be used in PPP forgiveness. The election is made by not claiming the credit on such wages.
- Of wages included on a PPP loan forgiveness application, an employer is only considered to have applied the minimum amount of payroll costs required for forgiveness.
  - At least 60% of qualified expenses used to claim PPP forgiveness must be payroll costs.
  - The remaining qualified expenditures may be made up of other qualifying expenditures as well as additional payroll costs.

ERTC vs. PPP Forgiveness

- Notice 2021-20, Example 3
  - Employer C received a PPP loan of $200,000
  - During the covered period, Employer C incurred $200,000 of qualified wages and $70,000 of other eligible expenses.
  - Employer C submitted a PPP loan forgiveness application and reported $200,000 of qualified wages but did not report the other eligible expenses of $70,000.
  - The entire $200,000 of payroll costs included in the application submission may not be treated as qualified wages for ERTC purposes.
    - Although the employer has sufficient other expenses to only require $130,000 of wages used towards forgiveness, the other expenses were not included on application so cannot be used.

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ERTC vs. PPP Forgiveness

- Notice 2021-20, Example 4
  - Employer C received a PPP loan of $200,000
  - During the covered period, Employer C incurred $200,000 of qualified wages and $70,000 of other eligible expenses.
  - Employer C submitted a PPP loan forgiveness application and reported $200,000 of qualified wages and other eligible expenses of $70,000.
  - Only $130,000 of payroll costs included in the application submission may not be treated as qualified wages for ERTC purposes.
    - This is the minimum amount of wages required for full PPP forgiveness.

ERTC vs. PPP Forgiveness

- Additional Example
  - Employer A received a PPP2 loan of $60,000
  - During the covered period, Employer A has wages equal to the chart to the right. Additionally, employer A has $50,000 of other qualified expenses.
  - Employer A must use $36,000 of wages toward PPP forgiveness – the remaining $24,000 can include other qualified expenses.
  - Employer A should first apply wages for each employee over the $10,000 qualified threshold limit toward the $36,000.
    - Employees C, D & E each of wages in excess of this limit either in Q1, Q2, or both.
    - If either Q1 or Q2 are not eligible for the ERTC, wages in those quarters can be considered applicable toward PPP forgiveness.

Employee	Q1	Q2	Total
A	$8,000	$8,000	$16,000
B	$10,000	$10,000	$20,000
C	$12,000	$12,000	$24,000
D	$15,000	$5,000	$20,000
E	$20,000	$20,000	$40,000

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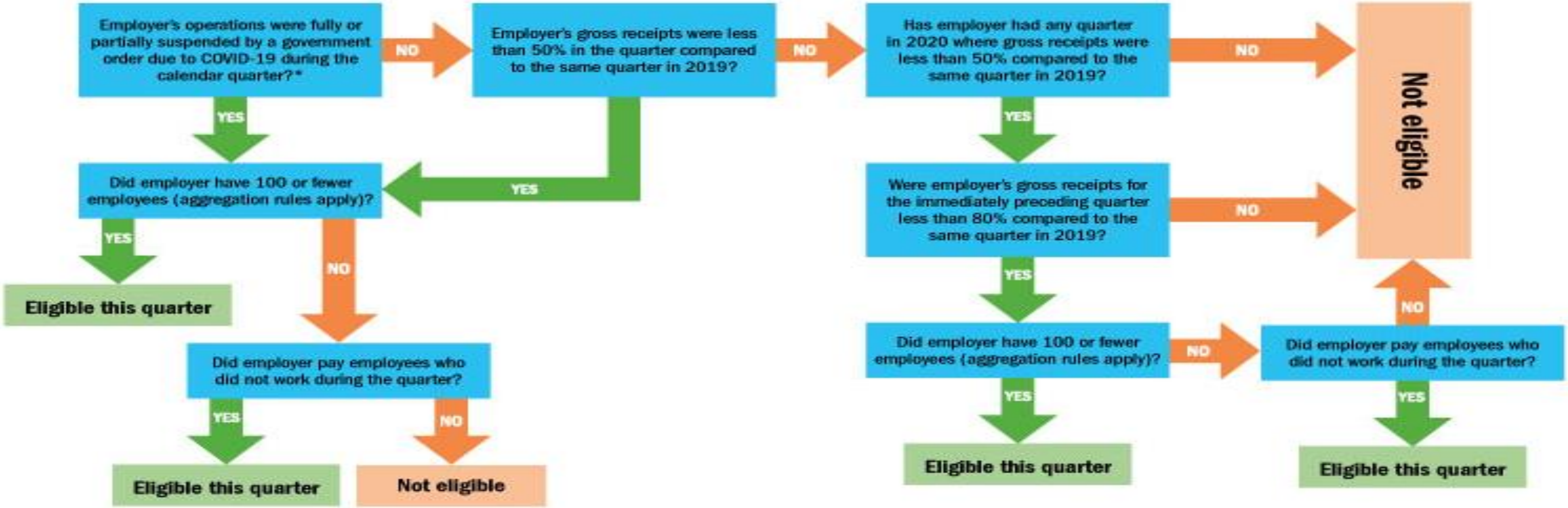
Employee Retention Tax Credit Flow Chart for 2020 Quarters



*Essential businesses may still qualify as fully or partial shutdown in certain instances. Please consult an appropriate member of the tax department.

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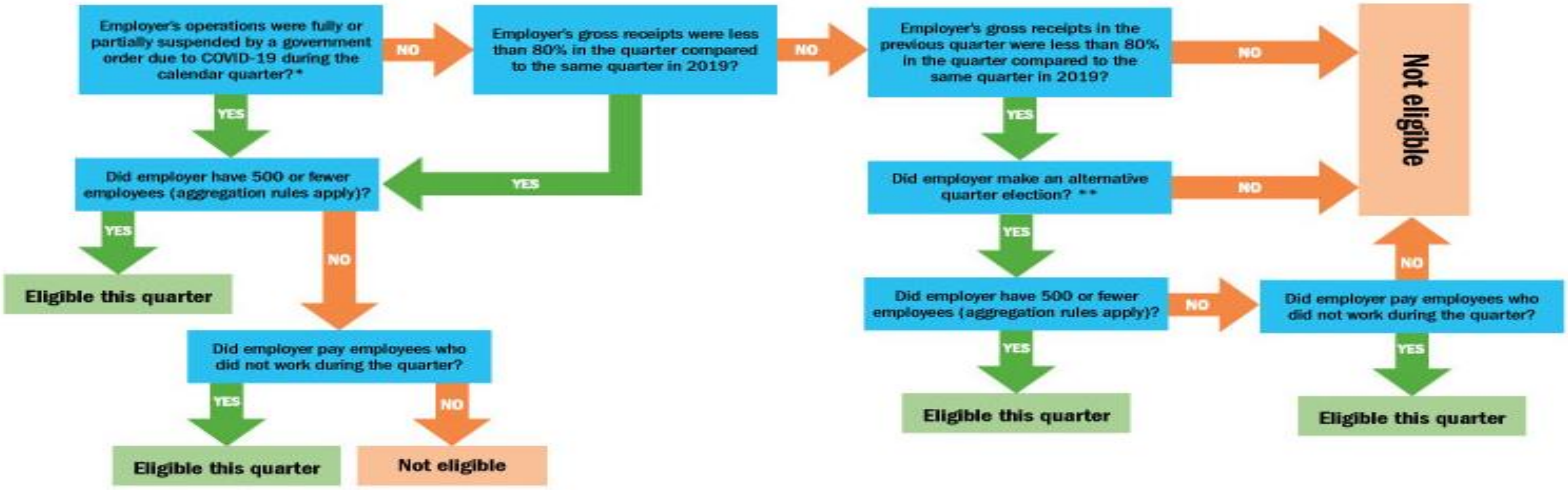
Employee Retention Tax Credit Flow Chart for 2021 Quarters



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**Employer's gross receipts in the immediately preceding quarter are less than 80%

Questions:

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