Employee Retention Credit

Overview of Expanded and Extended Credit

CAA: Changes to the Employee Retention Credit

The latest legislation did two things:

1) **<u>Expanded</u>** the availability of the Employee Retention Credit (retroactive to 2020)
   - The provision that excluded taxpayers who took out a PPP loan from claiming the credit has been removed
     - For claiming these retroactive credits, you must file an amended payroll tax filing
     - Payroll costs can only be used for the Employee Retention Credit **<u>OR</u>** in applying for PPP loan forgiveness. We will need guidance on the coordination of these provisions – especially for those that have already filed and/or received forgiveness.
   - **<u>The same eligibility/criteria that were part of the CARES Act apply for 2020</u>**.

CAA: Changes to the Employee Retention Credit

2) **Extended** the availability of the Employee Retention Credit
   - Originally the credit was set to expire for wages paid beyond December 31, 2020; however, the latest legislation has expanded the credit to cover wages paid during the period beginning **January 1, 2021 through June 30, 2021**.
   - Included with this extension are **modifications** to the credit calculation.

Note: these modifications only apply to credits taken in 2021. For retroactive credits claimed for 2020 the "old" rules under the CARES Act still apply.

Overview of the Credit

Unless otherwise indicated, the information provided in these slides applies to both the 2020 and 2021 credits being claimed. Differences will be indicated in RED.

- Eligible employer's will receive a fully refundable credit against their payroll taxes equal to 50% for 2020 (for 2021, this amount is increased to 70%) of qualified wages paid to each employee during a calendar quarter.
  - Who is an "eligible employer"?
  - What are "qualified wages"?

What taxpayers are eligible?

- This credit is available to any size employer (i.e., not limited based on employer's size/# of employees, etc.).
- Available to tax-exempt organizations.
- However, this credit is **NOT** available to:
  - Governmental employers (for 2021 colleges, universities and entities whose principal purpose is to provide medical or hospital care are eligible for the credit)
  - Self-employed individuals.

Who is an “eligible employer”?

- An employer that is carrying on a trade or business during calendar year 2020 **and**
- The employer meets **one** of the following criteria:
  - during any calendar quarter the operation of such trade or business is fully or partially suspended due to government orders that limit commerce, travel or group meetings due to COVID-19, **or**
  - for a period beginning in any calendar quarter in which the gross receipts of such employer are less than 50% for 2020 (for 2021, this was changed to 80%) of the gross receipts for the same calendar quarter in the prior year and ending in the calendar quarter following the calendar quarter in which gross receipts exceed 80% of gross receipts for the same calendar quarter in the prior year.

** There are rules regarding how to make these determination where employers were not in business during the applicable 2019 periods.

What are “Gross Receipts”?

- “Gross Receipts”generally includes total sales (net of returns and allowances) and all amounts received for services. In addition, gross receipts include any income from investments, and from incidental or outside sources.

- Solely for purposes of determining eligibility for the Employee Retention Credit, gross receipts for a **tax-exempt employer** include gross receipts from all operations, not only from activities that constitute unrelated trades or businesses. For example, gross receipts for this purpose include amounts received by the organization from total sales (net of returns and allowances) and all amounts received for services, whether or not those sales or services are substantially related to the organization’s exercise or performance of the exempt purpose or function constituting the basis for its exemption. Gross receipts also include the organization’s investment income, including from dividends, rents, and royalties, as well as the gross amount received as contributions, gifts, grants, and similar amounts, and the gross amount received as dues or assessments from members or affiliated organizations.

- To determine whether there has been a significant decline in gross receipts, a tax-exempt employer computes its gross receipts received from all of its operations during the calendar quarter and compares those gross receipts to the same gross receipts received for the same calendar quarter in 2019.

What are “Gross Receipts”?

- For **<u>2021</u>**, employers may elect to determine to make gross receipts reduction determination based on the previous calendar quarter as compared to the corresponding “previous” 2019 calendar quarter. The law states that this election is to “be made at such time and in such manner as the Secretary shall prescribe.” More guidance on how to make such election.

Example: Reduction in Gross Receipts Calculation (For 2020 Credit)

- Employer's Gross Receipts in 2019: $200k (Q1); $210k (Q2); $230k (Q3); $250k (Q4)
- Employer's Gross Receipts in 2020: $190k (Q1); $100k (Q2); $190k (Q3); $230k (Q4)
- Employer's % of Gross Receipts: 95% (Q1); 48% (Q2); 83% (Q3); 92% (Q4)
  - Credit period begins in the first calendar quarter the employer has a > 50% decline in gross receipts: Second quarter decline = 52%; therefore; credit period begins in Q2.
  - Credit period ends in the first calendar quarter following the calendar quarter in which gross receipts exceed 80% when compared to prior year: Third quarter % when compared to prior year = 83%, therefore; credit period ends the following calendar quarter or Q4.

Therefore, in this example the employer could claim a credit for qualified wages paid in Q2 and Q3 of **2020**.

Example: Reduction in Gross Receipts Calculation (For 2021 Credit)

Reminder: As of the enactment of the CAA, these provisions are only applicable for the first and second quarters of 2021.

- Employer's Gross Receipts in 2019: $200k (Q1); $210k (Q2)
- Employer's Gross Receipts in 2021: $150k (Q1); $189k (Q2)
- Employer's % of Gross Receipts: 75% (Q1); 90% (Q2)

  - Credit period begins in the first calendar quarter the employer has a > 20% decline in gross receipts: First quarter decline = 25%; therefore; credit period begins in Q1.
  - Credit period ends in the first calendar quarter following the calendar quarter in which gross receipts exceed 80% when compared to prior year: Second quarter % when compared to prior year = 90%, therefore; credit period ends the following calendar quarter (in this case the credit expires 6/30/2021 employer would qualify through the expiration date of the credit).

Therefore, in this example the employer could claim a credit for qualified wages paid in Q1 and Q2 of **2021**.

What are "qualified wages"?

- For eligible employers with > **100 for 2020 (for 2021, this increased to 500) employees :
  - Wages paid to an employee that is **<u>not providing services</u>** during the eligible credit period (ex., this would be those employees that were furloughed but were still being paid/benefits covered but not working).

- For eligible employers with < **100 for 2020 (for 2021, this increased to 500) employees:
  - Wages paid to all eligible employees (whether they are being paid to work or are not working) during the eligible credit period.

** average number of full-time employees during 2019 (taking into account full-time equivalent rules under IRC 4980H) – must include "related employers" when making this determination.

- **For more details, see the IRS FAQs - Determining Which Entities are Considered a Single Employer Under the Aggregation Rules**

What are “qualified wages”?

- For **2020**, only wages paid from March 13, 2020 through December 31, 2020 are eligible for the credit.
- For **2021**, only wages paid from January 1, 2021 through June 30, 2021 are eligible for the credit.
- Qualified wages include costs incurred by the employer for qualified health plan expenses allocable to such eligible wages (this was clarified in the latest legislation and applies to both 2020 and 2021 credits).

What are "qualified wages"?

- For **2020**, the maximum amount of qualified wages that may be considered for each employee for **all** calendar quarters during 2020 is $10,000, so the maximum credit for qualified wages to any one employee during 2020 is capped at $5,000 ($10,000 qualified wages x 50% credit limitation).
- For **2021**, this cap is expanded to $10,000 per calendar quarter, so the maximum credit for qualified wages to any one employee is capped at $7,000 per quarter for 1st and 2nd quarters of 2021.
- This means for a taxpayer that is eligible for this credit they could received up to a maximum of $19,000 per employee ($5,000 cap in 2020 +$14,000 cap in 2021).
- Qualified wages **exclude** the following amounts:
  - Wages required to be paid under the "Sick Leave" and "Family and Medical Leave" provisions of the Families First Coronavirus Relief Act (FFCRA)
  - Wages for which a Work Opportunity Tax Credit (WOTC) are claimed.
  - Wages for which a Family and Medical Leave Credit are claimed.
  - Wages paid to anyone owning more than 50% of the stock of a corporation or more than 50% of the capital or profits of a partnership (after applying IRC 267 attribution rules).
  - **Wages that are used to qualify for PPP loan forgiveness.**

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ERC: Other Highlights

- The credit is refundable to the extent it exceeds the employer's payroll tax liability.
- Employers can reduce the amount of their otherwise required federal employment tax deposit (including amounts withheld from employees for federal income taxes, employees and employers share of Social Security and Medicare taxes) by the amount of anticipated credit under this provision.
- If the anticipated credit exceeds the otherwise required federal employment tax deposit, an employer may request an advance of their excess anticipated credit using IRS Form 7200
- Amounts not deposited and/or received through an advanced credit request will have to be considered when filing Form(s) 941.
- Wage deductions of the employer must be reduced by an amount equal to the credit claimed. This will impact deductions allowed to be claimed on 2020 returns.

Example: Federal Tax Deposits Withheld/Advanced Payment Request

- An eligible employer pays $20,000 in qualified wages to 4 employees, therefore; they are eligible for a $10,000 ‘Employee Retention Credit’.
- They are required to make a $8,000 federal tax deposit which includes all taxes withheld from its employees as well as their share of payroll taxes.
- The employer has not paid sick or family leave credits available under the FFCRA provisions.
- The employer can keep the entire $8,000 of taxes it would have otherwise been required to deposit without any penalties.
- The employer can file IRS Form 7200 to request an advance of the remaining $2,000 credit.
- The employer will have to reconcile these amounts when filing their Form 941.

Questions?

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