

Employee Retention Credit Tax Strategy Planning Opportunities

baldwin
CPAs

Timeline of ERC

	CARES Act (3/27/20)	CAA (12/27/20)	ARPA (3/11/21)
Availability	<ul style="list-style-type: none"> Wages paid after March 12, 2020 and before January 1, 2021 PPP recipients cannot claim ERC 	<ul style="list-style-type: none"> Wages paid after December 31, 2020 and before July 1, 2021 PPP recipients can claim ERC retro to March 12, 2020 	<ul style="list-style-type: none"> Wages paid after June 30, 2021 and before January 1, 2022
Eligibility	<ul style="list-style-type: none"> 50% decline gross receipts for a calendar quarter in 2020 compared to the same in 2019 OR, Full or partial suspension in operations 	<ul style="list-style-type: none"> 20% decline gross receipts for a calendar quarter in 2021 compared to the same in 2019 OR, Full or partial suspension in operations 	<ul style="list-style-type: none"> No Change
Credit Value	<ul style="list-style-type: none"> 50% of up to \$10,000 of qualified wages per employee The \$10,000 is an annual cap for 2020 	<ul style="list-style-type: none"> 70% of up to \$10,000 of qualified wages per employee per quarter 	<ul style="list-style-type: none"> No Change

© 2021 Association of International Certified Professional Accountants. All rights reserved.

What We Know	2020	2021
Definition of Full-Time Employees	<p>For the purposes of the employee retention credit, a full-time employee is defined as one that, in any calendar month in 2019, worked at least 30 hours per week or 130 hours in a month (this is the monthly equivalent of 30 hours per week).</p> <p>Employers who were in business the entire calendar year in 2019 would take the sum of the number of full-time employees in each calendar month and divide by the number of months in business.</p> <p>An employer who started a business in 2020 determines the number of full-time employees by taking the sum of the number of full-time employees in each full calendar month in 2020 that the business operated, and dividing by that number of months.</p>	Same as 2020.
Retroactive Credit	<p>The Consolidated Appropriations Act, 2021, retroactively allows PPP recipients to take the ERTC for wages paid after March 12, 2020 and before Jan. 1, 2021.</p> <p>Employers may amend their tax returns to claim the credit.</p> <p>Note: The amended return process may be different for PEO.</p>	N/A

ERC: Back to the Basics

- Fully refundable payroll tax credit for qualifying wages starting March 13th, 2020 and extended to December 31st, 2021.
- Intended to provide liquidity to employers during the COVID-19 pandemic.
- Employers of **any size**, including tax-exempt organizations engaged in a trade or business are eligible for the credit.

ERC: Qualifying Employer

- Fully or partially suspended operations during any calendar quarter in 2020 or 2021 due to a government order limiting commerce, travel or group meetings due to COVID-19.

OR

- Experience a significant decline in Gross Receipts. The cause of decline is **not** required to be related to COVID-19

ERC: Decline in Gross Receipts

2020	2021
50% quarterly decline in Gross Receipts compared to same quarter in 2019.	20% quarterly decline in Gross Receipts compared to same quarter in 2019.

ERC: Fully or Partially Suspended

Fully or partially suspended due to “orders from an appropriate governmental authority limiting commerce, travel or group meetings due to COVID-19”

- Government orders include:
 - An order from the City’s Mayor stating that all non-essential business must close for a specified period.
 - Shelter in place order
 - An order imposing a curfew that impacts operating hours of a trade of business.

Partial suspensions (caused by government order)

- Auto parts store, part shortage from suppliers – **Yes.**
- Auto dealership (nonessential) with a service dept. (essential) – **Yes, *if* dealership > 10% of gross receipts or hours.**
- Restaurant, take out only – **Yes.**
- Restaurant, dining-in limited to 50% capacity – **Yes.**
- Hospital, elective surgeries delayed by government order – **Yes, *if* more than nominal (10%).**

Partial suspensions (caused by government order)

- Grocery store (essential), but salad bar closed (nominal part of business) – **No.**
- Hardware store, but customers not coming in – **No.**
- Attorney office, workplace closed, but business continues remotely at comparable level as before COVID – **No.**
- Clothing store, density in store limited and short wait outside for customers – **No.**

ERC: Qualifying Wages

- Definition depends in part on the average number of full-time employees employed during 2019.

2020	2021
>100 employees = qualified wages paid for the time employee is not providing services	>500 employees = qualified wages paid for the time employee is not providing services
<100 employees = qualified wages paid to any employee during the period employer qualifies	<500 employees = qualified wages paid to any employee during the period employer qualified

How to Claim the Credit

- Credit is claimed on quarterly 941's
- Claiming credit retroactive to 2020
 - Must amend Form 941's by filing 941X for applicable quarter
 - 941X will request a refund (cannot apply to a future quarter)

ERC: PPP Loan and ERC

- Employers who received a PPP loan are now eligible for the ERC and should evaluate if they qualify.
- May not use the same wages for ERC used for the following:
 - PPP Loan, RRF, SVOG
 - Paid Sick Leave and Family Leave Credits
 - Work Opportunity Credit, R&D Credit and others
- **Carve out wages used in completing the PPP Loan Forgiveness Application.**

Major Questions Answered by the IRS

- **Are wages paid to Majority Shareholder (> 50%) & Spouse qualified wages?**
 - It depends on complicated family attribution rules.
 - Wages are not taken into account if an individual has any of the following relationships to:
 - The Taxpayer
 - If the taxpayer is a corporation, the majority owner of the corporation
 - If the taxpayer is a non-corporate entity; the majority owner of the noncorporate entity

Major Questions Answered by the IRS

- Relations:
 - A. Child or descendant of a child
 - B. Brother, sister, stepbrother, stepsister
 - C. Father, mother or ancestor of either
 - D. Stepfather or stepmother
 - E. Niece or nephew
 - F. Aunt or uncle
 - G. Son-in-law, daughter-in-law, father-in-law, mother-in-law, brother-in-law, sister-in-law
 - H. Individual with same principal place of abode as the taxpayer

Major Questions (continued)

- In addition to the last slide, constructive ownership rules to determine who is considered a majority owner of a corporation
 - If the majority owner of a corporation has living ancestors (parents, grandparents, siblings, children or grandchildren), regardless if they are employed by the entity, meaning they merely have to exist, then the wages of the majority owner & spouse don't qualify for the credit.
 - If they don't have these particular living relatives, their wages do qualify.

Major Questions (continued)

- **Tips are qualifying wages**
 - Cash Tips over \$20 which are reported as wages are qualified wages for the ERC
 - The wages qualify for both ERC and Tip Credit
- Employer Size based on **Full-time employees** not Full-time equivalents (Good News!)
 - Full Time employee is defined as an employee who worked at least an average of 30 hours per week or 130 hours per month in 2019.

Major Questions (continued)

- **Income Tax Consequences of Claiming ERC:**

- Reduce deduction for wages, including health plan expenses, on federal income tax return in the amount of the ERC in the tax year in which the qualified wages were paid or incurred.
- Example: Employer A, a PPP loan borrower, files an amended Form 941-X in June 2021 to retroactively claim a \$100,000 ERC for Q3 and Q4 of 2020. Employer A files their 2020 federal income tax return in March 2021, which included a previous deduction for the \$100,000 of ERC Wages. An amended federal income tax return must be filed in order to reduce the previous deduction for wages by \$100,000.

Major Questions (continued)

- **Excludable Gross Receipts**

- IRS issued a safe harbor that allows an employer to exclude certain amounts received from other coronavirus economic relief programs in determining whether it qualifies for the ERC based on a decline in gross receipts.
 - Amount that can be excluded in calculated gross receipts are:
 - PPP Loan Forgiveness (First and Second Draw Loans)
 - Shuttered Venue Operators Grant
 - Restaurant revitalization grant
 - Must consistently apply the safe harbor to the calculation across all quarters.

Major Questions (continued)

- **Recovery Start-up Business – New category of eligible employer for 3Q & 4Q 2021**

- Criteria to qualify:

- Began carrying on a trade or business after February 15, 2020
- Average annual gross receipts of \$1M or less
- And is not otherwise an eligible employer due to gov't test or decline in gross receipts

- A Recovery Start-up business will receive small employer treatment – all employee wages are considered qualified wages. The wages are not limited to the wages paid when employees are not providing services.

- Credit limited to \$50,000 for each 3rd & 4th Qtr.

What information is needed to determine ERC Eligibility and estimate the credit

- Does the business have substantially common ownership with any other company (commonly controlled entity)?
- How many average full-time employees in 2019?
- Income Statement or Profit & Loss by quarter for 2019 – 2021. (Gross Receipts Test)
- Did the business fully or partially suspend operation during any calendar quarter in 2020 or 2021 due to orders from an appropriate governmental authority?

What information is needed to determine ERC Eligibility and estimate the credit (continued)

- Payroll reports
- Employer share of health plan expense by employee
- PPP1 & PPP2 loan information
- Does the business employ family members of the majority shareholder?

Keep in Mind

- **Senate passed bipartisan infrastructure bill August 10th, which includes a provision that would end the ERC early on September 30, 2021. We are watching this closely.**

Questions? Contact Us.

Beth Overbey

beth.overbey@baldwincpas.com

502.736.9161

Ross Vanoli

ross.vanoli@baldwincpas.com

859.626.4983

