DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, DC 20224

OFFICE OF THE CHIEF COUNSEL

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The Honorable Matt Cartwright
Member, U.S. House of Representatives
20 North Pennsylvania Avenue, Suite 213
Wilkes-Barre, PA 18711

Attention:

Dear Representative Cartwright:

I am responding to your May 9, 2023, inquiry on behalf of your constituent, . He asked for clarification about income tax filing rules related to the employee retention credit (ERC). He explained his business was eligible for the credit in 2021, but the business did not receive its refund until 2022.

I believe question relates to the timing under the general rule that an employer's deduction for qualified wages must be reduced by the amount of the ERC. I can provide a general explanation of the law concerning the timing of this reduction.

Section 2301 of the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) provides an ERC for the first and second quarters of 2021. Section 3134 of the Internal Revenue Code (Code) provides an ERC for the third and fourth quarters of 2021. Section III.L. of Notice 2021-20 provides that:

(1) the ERC is not included in an employer's income, and

(2) the ERC, even though it is an employment tax credit, does not reduce the income tax deduction for the employer's share of Social Security and Medicare taxes. Instead, the ERC reduces the income tax deduction for qualified wages. This is because of special rules in Section 2301(e) of the CARES Act and Section 3134(e) of the Code, which provide that rules similar to Section 280C(a) of the Code apply to the ERC.

Section 280C(a) generally disallows a deduction for the portion of wages or salaries paid or incurred equal to the sum of certain credits determined for the taxable year. Accordingly, a similar deduction disallowance applies to the ERC. This means that an employer's deduction for qualified wages is reduced by the amount of the ERC. Section IV.C. of Notice 2021-49 explains that Section 280C(a) requires tracing to the specific wages generating the applicable credit. Because of this tracing requirement, the timing of the reduction in the employer’s deduction occurs in the tax year in which the qualified wages were paid or incurred, not the year the ERC is received.

The outcome we described above is the result of our applying the principles of existing law incorporated in Section 2301 of the CARES Act and Section 3134 of the Code.

Again, I have provided certain general principles of the law in this letter. It is intended for informational purposes only and does not constitute a ruling. See Revenue Procedure 2023-1, Section 2.04, 2023-1 IRB 1 (January 3, 2023).

I hope this information is helpful. If you have questions, please contact me at , or a member of your staff may contact , general attorney, at .

Sincerely,

Danchai Mekadenaumporn
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(Employee Benefits, Exempt Organizations,
and Employment Taxes)