

## IRM PROCEDURAL UPDATE

**DATE:** 12/04/2024

**NUMBER:** ts-21-1224-1182

**SUBJECT:** Disallowance Actions for ERC Related Filtering Related Individuals;  
Correction Regarding Form 8974

**AFFECTED IRM(s)/SUBSECTION(s):** 21.7.2

**CHANGE(s):**

**IRM 21.7.2.5.21.1 (4)5 Changed "line 3" to "column c".**

(4) In addition to all other verification requirements applicable to the Form 94XX (or original tax return) to which a Form 8974 is attached, the following items are required to be verified on Form 8974 prior to processing:

1. Verify a name and EIN were entered in entity section of Form 8974.

**Note:** Companies filing aggregate employment tax returns (e.g., IRC 3504 agents, etc.) are required to file a Form 8974 for each client taking a QSB Research Credit. So, there may be multiple Forms 8974 attached to a single Form 94XX and these Forms 8974 may reflect the client's information in the entity section of Form 8974 rather than that of the company under whose EIN the QSB Research Credit is being claimed.

2. Verify the taxpayer claiming the QSB credit has filing requirements for the type of employment tax return identified on Form 8974. If the taxpayer does not have employment tax filing requirements, use Letter 4384C to reject the Form 94XX and Form 8974 and inform the taxpayer in the letter that we cannot consider the requested changes since our records indicate they do not file employment tax returns.
3. Verify the taxpayer filed an original employment tax return for the calendar year and quarter (if applicable) being corrected. If the taxpayer has employment tax filing requirements but no return is posted, see IRM 21.7.2.4.4.6, *Adjusted Employer's Tax Return or Claim for Refund Return Filed — No TC 150 Posted*, for handling guidance.

**Caution:** If the QSB Research Credit is being filed for an employment tax return period beginning earlier than April 1, 2017 for Form 941 or earlier than January 1, 2017 for Form 943 and Form 944, contact the IRM author through your management chain and the site P&A Staff for guidance on handling the case.

4. Verify the taxpayer filed the correct version of Form 8974 for the tax period under consideration.
  - Adjustment requests filed for tax periods 202212 and prior must be filed with Form 8974 having a revision date of December 2017.
  - Adjustment requests filed for tax periods 202303 and subsequent must be filed with a Form 8974 having a revision date of March 2023 or later.
  - If the taxpayer filed the adjustment request with an incorrect Form 8974 version, use Letter 4384C to reject the Form 94XX and Form 8974 and inform the taxpayer in the letter that we cannot consider the requested changes because the incorrect Form 8974 version was submitted.
5. Verify the taxpayer identified in Part 1 of Form 8974 has filed an original income tax return for the specified form type and tax period.

**Note: #**

a) If there is more than one Form 8974 attached to the Form 94XX, or if multiple EINs are listed in Part 1 of Form 8974, or if there is a single EIN listed in Part 1 of Form 8974 and it does not match the EIN on the Form 94XX,

# .

b) If more than one income tax return is listed in Part 1 of Form 8974 (all with the same EIN), #

# .

c) If the taxpayer identified in Part 1 of Form 8974 does not file Form 1040, Form 1065, Form 1120, Form 1120-F, or Form 1120S income tax returns, they are **not** eligible to claim the QSB Research Credit. If the taxpayer enters an income tax return other than one of those specified (or its corresponding amended income tax form), or research shows they file an income tax return other than one printed on Line 1 of Form 8974, reject the claim with Letter 916C. Advise the taxpayer in the letter that we cannot consider the amount claimed on their Form 8974 because our records show their organization type is not eligible to claim the QSB Research Credit.

d) If the income tax return has not posted and the date entered in column (c) of Form 8974 is less than 30 days prior to the received date of the Form 8974, suspend the case for 40 days and monitor for posting of the income tax return. If the return posts, continue to process as appropriate.

e) If the date entered is 30 days or more from the received date of the Form 8974, or the suspense period has passed and no income tax return is posted, follow the instructions in (5) below to reject the Form 94XX and Form 8974 with instructions to refile their QSB Research Credit claim after they file their income tax return.

6. Verify the Form 8974 has been filed for an employment tax period covering a calendar quarter that began **after** the income tax return identified in Part 1 of Form 8974 was filed. See (5) in IRM 21.7.2.5.21, *Form 8974, Qualified Small Business Payroll Tax Credit for Increasing Research Activities*, for guidance. If the Form 8974 was filed for an employment tax period before what is permitted based on when the identified income tax return was filed, follow procedures in IRM 21.5.3.4.6.3, *No Consideration Procedures* and instruct the taxpayer to refile their QSB Research Credit claim for the appropriate tax period.

**Reminder: #** [REDACTED]

[REDACTED] #

**Caution:** For timely filed returns, TXMOD and BMFOL return received dates fields reflect the associated return due date rather than the actual filing date. In some cases, it may be necessary to review MeF to verify the true filing date of the income tax return (if filed electronically) to verify the Form 8974 has been filed for a correct employment tax return period. # [REDACTED]

[REDACTED] #

7. Continue processing the Form 8974 as per instructions below in (5) or (6) based on the tax period for which the filing was made.

#### **IRM 21.7.2.7.8.10 Added new subsection to address related individuals.**

Disallowance of Form 94XX ERC Claims Meeting RAAS Filtering Criteria for Related Individuals

(1) Certain Form 94XX cases reflecting Employee Retention Credit (ERC) adjustment requests are being released to be worked by AM after having been analyzed by Research, Applied Analytics & Statistics (RAAS). These cases will be delivered to AM with instructions on how the ERC portion of the claim or adjustment is to be handled (i.e., additional handling required, assessment to be made, claim is allowable, disallowance criteria, or partial disallowance criteria).

**Caution:** RAAS analysis for these cases generally does not include consideration of non-ERC related tax items that may be reported on a Form 94XX, including those with a mix of ERC and non-ERC change items.

(2) This subsection provides handling guidance for Forms 94XX reporting ERC amounts which were identified by RAAS as being filed by employers who are claiming ERC credit for related individuals.

(3) The IRS has determined that Forms 94XX reporting new or increased ERC amounts (only) filed for accounts meeting the specified filtering criteria for related individuals will be formally disallowed.

(4) Cases identified by RAAS for disallowance handling per guidance in this subsection will be identified to AM as follows:

- IDRS Number: **0230281088**
- CII case notation: "**RiskedERC-Disallow**" and "**Related-Individuals**"

**Note:** CII case notes for these cases will also indicate the EIN and tax period that was identified during data transcription for RAAS analysis. This information is a factor in processing validation described in (5) below.

**Note:** CII case notes for these cases may indicate multiple filtering criteria as having been met. If so, the first case notation is deemed the **primary** indicator and controls handling. Additional filtering notes are deemed secondary indicators and are potentially a factor in handling as discussed in the last row of the table in (6) below.

(5) All other Form 94XX processing guidelines and requirements also apply to Forms 94XX reporting changes to ERC that have been identified to AM by RAAS as having been filed for accounts meeting the specified filtering criteria for related individuals. Forms 94XX so identified by RAAS have generally **not** been reviewed for completeness (e.g., presence of signature, certification block(s) marked, etc.) and processability (e.g., prior figures match, mathematically correct, etc.). As such, all preliminary reviews to ensure the Form 94XX is complete for processing **must** be conducted **before** taking action to disallow the Form 94XX on the basis of it having failed filtering analysis for related individuals. As usual:

- Review the Form 94XX for completeness and processability (e.g., for a Form 941-X claim, see (2) and (3) in IRM 21.7.2.4.5.6.2, *Form 941-X Tax Decrease — Claim*). Perfect or reject any unprocessable Forms 94XX as appropriate.

**Exception:** If there is no posted original return, **do not** follow guidance in IRM 21.7.2.4.4.6, *Adjusted Employer's Tax Return or Claim for Refund Return Filed — No TC 150 Posted* unless directed to do so per instructions in (7) below and **do not** follow procedures in IRM 21.7.2.7.8.4, *Form 94XX ERC Claims Meeting RAAS Filtering Criteria for Missing Original Returns (No TC 150)*. Continue processing as per guidance in this paragraph and then follow guidance in (7) below instead of (6).

**Caution:** The missing TC 150 condition will generally be identified by RAAS in the CII case notes. However, AM employees are responsible for reviewing the account for the presence of an original return when processing the released Form 941-X regardless of whether such a note is present and for applying (6) or (7) guidance below as appropriate.

- Review for account conditions that require special handling (i.e., open CAT-A or AIMS status, RICS/RIVO/IDT, etc.) which must be addressed prior to taking further action on the Form 94XX. Suspend, route, or otherwise address the account condition encountered as appropriate.
- **In addition**, compare the EIN and tax period entered on the Form 941-X to the EIN and tax period specified in CII case notes releasing the case to be worked.

**Caution:** If the tax period or EIN shown on the form do not match CII case controls **or** the tax period or EIN specified in CII case notes releasing the case to be worked do not match CII case controls, the case **must** be returned to RAAS for additional analysis. Take the following actions to refer such a case for further RAAS consideration:

- 1) Correct case controls as necessary and appropriate.
- 2) Enter/update the case with **Priority Code 6**.
- 3) Enter the appropriate case note as follows: "EIN mismatch" or "Tax Period mismatch" or "EIN and Tax Period mismatch"
- 4) Reassign the case to IDRS number **0230281416**.

**Note:** Procedures found in (6) below do not apply to Form 94XX cases rejected or "no-considered" as the result of following guidance in (5) above and such cases **do not** require further RAAS consideration.

**Caution:** Form 94XX cases released to be worked by AM after RAAS analysis may include assessment cases in addition to claims, including net credit/refund or zero balance cases reporting tax increase items along with refundable credit changes. Although suspended inventory was reviewed for statute imminent 2020 account situations prior to normal ASER expiration on April 15, 2024, there is heightened risk of encountering statute barred assessments in this work. Consider guidance in (2) of IRM 25.6.1.13.2.6, *Routing and Controlling Form 9355*, if such cases are identified.

(6) **For accounts with a posted TC 150 original return:** After applying the guidance in (5) above, continue handling **processable** Forms 94XX identified to AM by RAAS as having been filed for accounts meeting the specified filtering criteria related individuals as follows:

If	And	Then
The Form 94XX reports <b>only</b> changes to ERC		<p><b>Disallow the claim:</b></p> <ol style="list-style-type: none"> <li>1. Complete a TC 290 .00 adjustment in Blocking Series 98 or 99 as appropriate (see (1) in IRM 21.5.3.4.6.1, <i>Disallowance and Partial Disallowance Procedures</i>) to record a full disallowance of the claim.</li> <li>2. Send Letter 105C as per</li> </ol>

		<p>instructions in IRM 21.5.3.4.6.1, <i>Disallowance and Partial Disallowance Procedures</i> and insert the following text in two open paragraphs:  "Wages paid to related individuals are not qualified wages for purposes of computing the ERC. Related individuals include, among other categories, a corporation's majority owner or constructive majority owner, and their spouse, children, siblings, or other specified relatives"  "For more information on Employee Retention Credit (ERC) eligibility requirements and how to respond to this letter if you disagree, please see <a href="https://irs.gov/erc105c">irs.gov/erc105c</a>."</p>
<p>The Form 94XX reports other tax or credit changes <b>in addition to</b> ERC changes</p>	<p>The other changes <b>do not</b> meet CAT-A criteria when considered separately from the ERC changes reported</p>	<p><b>Partially disallow the claim:</b></p> <ol style="list-style-type: none"> <li>1. Complete a TC 29X adjustment in Blocking Series 18 or 00 as appropriate (see (2) in IRM 21.5.3.4.6.1, <i>Disallowance and Partial Disallowance Procedures</i>) with appropriate IRNs/CRNs to record the allowable portion of the correction requested on the Form 94XX.</li> <li>2. Send Letter 106C as per instructions in IRM 21.5.3.4.6.1, <i>Disallowance and Partial Disallowance Procedures</i> and insert the following text in two open paragraphs:  "Wages paid to related individuals aren't qualified wages for the ERC. Related individuals include, among other categories, a corporation's majority owner, and their spouse, parents, children, siblings, or other relatives as described in the FAQs about ERC on <a href="https://irs.gov">irs.gov</a>."</li> </ol>

		<p>"For more information on Employee Retention Credit (ERC) eligibility requirements and how to respond to this letter if you disagree, please see <a href="https://irs.gov/erc105c">irs.gov/erc105c</a>".</p>
<p>The Form 94XX reports other tax or credit changes <b>in addition to</b> ERC changes</p>	<p>The other changes <b>do meet</b> CAT-A criteria when considered separately from the ERC changes reported</p>	<p>The ERC Math Verification Worksheet <b>must</b> be executed <b>before</b> the CAT-A referral is completed:</p> <ol style="list-style-type: none"> <li>1. Follow handling guidance in (13) and (14) of IRM 21.7.2.7.6.3, <i>Form 94XX — Employee Retention Credit (ERC) — Claims and Adjustments Cleared for Processing (Accepted) by RAAS and Forms 94XX Reporting Tax Increases or Credit Decreases</i>, to execute the worksheet and to document the results.</li> <li>2. Complete the CAT-A referral as usual.</li> <li>3. Take action to complete processing of the Form 94XX based on instructions received from Exam Classification when the case is returned including (as appropriate): <ul style="list-style-type: none"> <li>• Completing the ERC Math Verification Worksheet again.</li> <li>• Completing an adjustment as per guidance in other rows of this table to record a full or partial disallowance.</li> <li>• Issuing an appropriate 105C or 106C full/partial disallowance letter with text as per guidance in other rows of this table or as instructed by Exam Classification.</li> </ul> </li> </ol>
<p>The CII case notes indicate <b>multiple</b> RAAS disallowance filters were met</p>		<p><b>Each</b> failed filter must be considered:</p> <ol style="list-style-type: none"> <li>1. As appropriate, consider handling guidance provided in this subsection as well as any applicable guidance in other subsections based on the</li> </ol>

		<p>identified failed filters.</p> <ol style="list-style-type: none"> <li>2. If the Form 94XX is deemed processable after all applicable guidance has been considered (i.e., did not meet rejection or "no consideration" criteria), then take action as appropriate to fully or partially disallow the Form 94XX.</li> <li>3. When issuing the appropriate 105C or 106C disallowance letter, insert text into the letter as described in the previous rows of this table as well as any text provided in other subsections applicable to the other failed filter(s).</li> </ol>
--	--	---

(7) **For accounts with no posted TC 150 original return:** After applying the guidance in (5) above, continue handling **otherwise processable** Forms 94XX identified to AM by RAAS as having been filed for accounts meeting the specified filtering criteria for related individuals as follows:

If	Then
The Form 94XX reports <b>only</b> changes to ERC	<p><b>Disallow the claim:</b></p> <ol style="list-style-type: none"> <li>1. Input a TC 971 AC 002 to release the E- freeze if a TC 971 AC 010 was previously input.</li> <li>2. Send Letter 105C as per instructions in IRM 21.5.3.4.6.1, <i>Disallowance and Partial Disallowance Procedures</i> and insert the following text in two open paragraphs:  "Wages paid to related individuals aren't qualified wages for the ERC. Related individuals include, among other categories, a corporation's majority owner, and their spouse, parents, children, siblings, or other relatives as described in the FAQs about ERC on irs.gov."  "For more information on Employee Retention Credit (ERC) eligibility requirements and how to respond to this letter if you disagree, please see IRS.gov/erc105c."</li> </ol>
The Form 94XX reports other tax or credit changes <b>in addition to</b> ERC changes	<ul style="list-style-type: none"> <li>• Follow guidance in IRM 21.7.2.4.4.6, <i>Adjusted Employer's Tax Return or Claim for Refund Return Filed — No TC 150 Posted</i></li> <li>• If an original return is secured, complete processing of the Form 941-X as per guidance</li> </ul>



	in (6) above <b>after</b> the original return is posted.
The CII case notes indicate <b>multiple</b> RAAS disallowance filters were met	<p><b>Each</b> failed filter must be considered:</p> <ol style="list-style-type: none"> <li>1. As appropriate, consider handling guidance provided in this subsection as well as any applicable guidance in other subsections based on the identified failed filters.</li> <li>2. If the Form 94XX is deemed processable after all applicable guidance has been considered (i.e., did not meet rejection or "no consideration" criteria), then take action as appropriate to fully or partially disallow the Form 94XX.</li> <li>3. When issuing the appropriate 105C or 106C disallowance letter, insert text into the letter as described in the previous rows of this table as well as any text provided in other subsections applicable to the other failed filter(s).</li> </ol>