



# IRS Nationwide Tax Forum | 2023

## Employee Retention Credit Positions and Audits

# Learning Objectives

Today our presentation will cover:

- Qualification Requirements Refresher
- Information Document Requests
- Preaudit Considerations
- Interaction with PPP Loans
- Amended Return Considerations



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# Qualification Requirements Refresher

## The Basics

- Refundable payroll tax credit
- Help businesses keep employees on payroll, even if not working
- Available to eligible employers of any size

# Timeline of Legislation & Related Guidance

## Coronavirus Aid, Relief, and Economic Security (CARES) Act (3/2020)

- Originally set to expire 12/31/2020
- IRS Notice 2021-20: authoritative guidance on wages paid 3/13 –12/31/2020,
  - Retroactive changes made by Taxpayer Certainty & Disaster Relief Act of 2020 (e.g., eligibility for PPP recipients)
  - Interplay of qualified wages with wages reported on PPP loan forgiveness applications
  - Form 941 / Form 941-X filing rules for PPP loan borrowers

## Taxpayer Certainty and Disaster Relief Act of 2020 (12/2020)

- Enhanced rules and extended credit to 6/30/2021
- IRS Notice 2021-23: authoritative guidance on wages paid 1/1/2021 – 6/30/2021 and on the election to use alternative quarter to calculate gross receipts

## American Rescue Plan Act of 2021 (3/2021)

- Enhanced rules and extended credit to 12/31/2021
- IRS Notice 2021-49: authoritative guidance on wages paid 7/1/2021 -12/31/2021
  - Example of application of related party rules

## Infrastructure Investment and Jobs Act (11/2021)

- Retroactively terminated ERC as of 9/30/21, except for Recovery Startup Business

# Eligible Employer

- Employers of any size
- Engaged in a trade or business
- Pays wages in a calendar quarter in which:
  - Business operations fully or partially suspended due to certain COVID-19-related government orders; **or**
  - Business has significant decline in gross receipts

2020

- ✓ Includes tax-exempt orgs
- ✓ Excludes government entities

2021

- ✓ Includes tax-exempt orgs
- ✓ Includes certain government entities that are colleges, universities hospitals and medical care providers

# Aggregation Rules for Related Employers

- Aggregated employers treated as single employer for all aspects of ERC
- Aggregated group rules:
  - Section 52(a) – parent-sub or brother-sister controlled group, or combined group corporation rules generally based on > 50% ownership
  - Section 52(b) – similar aggregation rules to partnerships, trusts, estates, sole-proprietorships operating a trade or business
  - Section 414(m) or (o) – normally used to determine related entities for purposes of qualified retirement plans & other employee benefits based on service relationships or management control

# Full or Partial Suspension of Business Operations

- Partial suspension: eligible employer continues some -- but not all trade -- or business operations
  - A supply concept, not a demand concept
  - If able to telework comparably, no suspension
  - Operations not able to be continued “in manner comparable to operations before COVID”
  - Modifications to operations must have (a) more than a nominal effect (10% impact on ability to provide goods or services) on (b) more than nominal portion of business operations (Safe harbor: 10% of revenue or hours in 2019)
- All members of aggregated group are eligible employers if one member of the group has business operations fully or partially suspended due to government order



## A Government Order Is...

- Order from city mayor requiring non-essential businesses to close
- State emergency proclamation that residents must shelter in place, other than those working for essential business that must travel to & from work, so workers cannot come to work
- Order from local official imposing curfew on residents that impact the operating hours of a business
- Order from local health dept. mandating workplace closure for cleaning or disinfecting

## A Government Order Is Not...

- Following OSHA requirements
- CDC recommendation as to health, distancing, & quarantining
- Following state or local orders that recommended measures but did not require them by law
- Declaration of State Emergency

# Gross Receipts Test

## 2020

- Decline of at least 50% of gross receipts comparing a 2020 calendar quarter to the same 2019 quarter for the controlled group
- Credit ends in quarter following quarter in which gross receipts reach 80% comparing a 2020 calendar quarter to the same 2019 quarter for the controlled group

## 2021

- Decline of at least 20% of gross receipts for the controlled group
- Compare a 2021 calendar quarter to the same 2019 quarter
- Compare the preceding calendar quarter to the same 2019 quarter

# Gross Receipts

## For-Profit Entity

- Total sales (less returns & allowances)
- Plus: Investment income
  - Interest
  - Dividends
  - Rents
  - Royalties
  - Annuities
- Less:
  - Adjusted basis in assets sold

## Not-for-Profit Entity

- Total sales\*\* (less returns & allowances)
- Plus: Investment & Other income
  - Sales Proceeds
  - Interest
  - Dividends
  - Rents
  - Royalties
  - Annuities
  - Contributions
  - Gifts
  - Grants
  - Member dues

\*\* Include all activities not only those related to exempt org. status

# Gross Receipts for an Employer Not in Business for All of 2019

Alternative measurement periods for employers commencing business in 2019:

- If business started in the 2nd, 3rd, or 4th quarter of 2019, use that quarter as the base period to determine whether it experienced a significant decline in gross receipts.
- If the employer commenced business in the middle of a quarter in 2019, the employer should estimate the gross receipts it would have had for the entire quarter based on the gross receipts for the portion of the quarter that the business was in operation.

# Qualified Wages & Credit Rate

Gross wages subject to Social Security taxes (disregarding wage base) & allocable group health care benefits incl. HDHPs, HRAs, FSAs; excluding HSAs & QSEHRAs

2020

- \$10,000 annual limit per employee
- Employer with 100 or fewer full-time employees, all wages
- Other employers, wages paid to individuals not rendering services
- Credit rate of 50% of qualified wages
- Max credit of \$5,000 per employee

2021

- \$10,000 per quarter limit per employee
- Employer with 500 or fewer full-time employees, all wages
- Other employers, wages paid to individuals not rendering services
- Credit rate of 70% of qualified wages
- Max credit of \$21,000 per employee

## Qualified Wages

- Allocable health plan expenses for employees paid by the employer, determined actuarially, by premiums paid or by using COBRA applicable premium
- Excludes wages for which an FFCRA credit was claimed and, for 2021 if an R&D credit was claimed
- For 2020, at the wage rate paid in 30 days immediately preceding suspension of operations or decline in gross receipt

# Number of Full-Time Employees

- A full-time employee is one who in 2019 averaged at least 30 hours of service per week or 130 hours of service in a month
- Average number of full-time employees determined by taking number of FTEs in each calendar month in 2019 divided by 12
- Special rules apply if employer was not in business for all of 2019 or started business in 2020



## Summary of 2021 Credit Enhancements

- PPP loan borrowers can claim the credit in 2020 & 2021
- Public colleges, universities, and health care entities can claim the credit
- Credit extended through December 31, 2021, with 4th quarter later repealed
- Qualified wages per employee increased from \$10K for the year to \$10K per qtr.
- Eliminate 30-day look-back period that limits qualified wages
- Credit calculation increased from 50% to 70% of qualified wages
- Significant decline in gross receipts based on 20% versus 50% of 2019 gross receipts
- Election to use prior qtr. gross receipts to determine eligibility (e.g., use Q4 2020)
- All wages qualify if employer < 500 employees. For employers > 500 employees only wages paid to employees not rendering services. In 2020 test was 100 employees
- Employers not in existence in 2019 can claim the credit



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# Information Document Requests Issued in ERC Examinations

# Information Document Request Sample

1. Forms 941 for quarters ending Dec. 31, 2020, March 31, 2021, June 30, 2021, Sept. 30, 2021
2. Worksheet 1 or similar worksheet(s) used to compute the ERC included on the amended returns for the 4<sup>th</sup> quarter of 2020 and 1<sup>st</sup>, 2<sup>nd</sup>, and 3<sup>rd</sup> quarters of 2021.
3. Payroll journal for months of Oct. - Dec. of 2020 and Jan. - Sept. of 2021
4. List of employees paid sick and/or family leave
5. The dates employees were paid sick and/or family leave
6. The amounts paid to each employee for sick and/or family leave
7. Statements required to be provided by the employees of the COVID-19 related reason the employee is requesting leave and written support for that reason
8. Statements required to be provided by the employees that the employee is unable to work, including by means of telework, for that reason

# Information Document Request (Cont'd)

9. Documentation to show how the amount of qualified sick and family leave wages paid to employees that are eligible for the credit was determined, including records of work, telework and qualified sick leave and qualified family leave
10. Documentation to show how the amount of qualified health plan expenses that the employer allocated to wages (if applicable) was determined
11. Forms 2020 and 2021 Forms W-2
12. Business income tax returns for 2020 and 2021 (for review only if available)
13. List of employees who were paid wages for which the ERC was claimed
14. Are there any individuals related to a shareholder owning 50% of the capital and profits interests in the entity who are employed by the company? If so, provide a list and description of relationship

# Information Document Request (Cont'd)

15. Wages paid to each employee for which the ERC was claimed
16. Documentation that operations were fully or partially suspended due to orders from appropriate governmental authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) due to COVID-19, OR documentation that the taxpayer experience a significant decline in gross receipts during the calendar qtr. ERC claimed
17. Documentation to show how the taxpayer determined the amount of qualified health plan expenses that the employer allocated to the ERC
18. Documentation related to PPP loans and related forgiveness including wages included on the loan application
19. Spreadsheet or breakdown of gross receipts. A reconciliation to yearly gross receipts for tax years 2019, 2020, 2021 - either a monthly or quarterly
20. Analysis or break down of how wages were allocated between the ERC credit and the PPP loans. Specifically for the 1<sup>st</sup>, 2<sup>nd</sup>, and 3<sup>rd</sup>, quarters of 2021



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# Proactive Audit Considerations

# Documentation

- Determination of an eligible employer that paid qualified wages, including:
  - Governmental order suspending employer's business operations
  - Records to determine whether more than a nominal portion of its operations were suspended due to a governmental order or whether a governmental order had more than a nominal effect on its business operations
  - Records to determine employer had a significant decline in gross receipts
  - Large eligible employers; work records and documentation showing that wages were paid for time an employee was not providing services
- Determination of amount of allocable qualified health plan expenses
- Determination of whether employer is a member of an aggregated group treated as a single employer and, if so, how the aggregation affects the determination and allocation of the credit

## Documentation

- Forms 7200 employer submitted to the IRS.
- Federal employment tax returns employer submitted to the IRS
- For employers that use third-party payers for employment tax obligations, records provided to the third-party payer regarding employer's entitlement to ERC claimed on federal employment tax return



# Client Communication & Education

***IR-2023-65: IRS Commissioner Danny Werfel warns:***

*"The IRS remains concerned about abusive tax arrangements, and they remain a focal point for our enforcement efforts," "Taxpayers should beware of potentially abusive arrangements and promoters pushing them. People should seek out trusted, reputable tax advice and not be fooled by aggressive advertising and sales pitches."*



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# Client Communication & Education

**IR-2023-105:** IRS alerts businesses, tax-exempt groups of warning signs for misleading ERC scams; simple steps can avoid improperly filing claims.

WASHINGTON – As aggressive marketing continues; the Internal Revenue Service today renewed an alert for businesses to watch out for tell-tale signs of misleading claims involving the Employee Retention Credit.

The IRS and tax professionals continue to see a barrage of aggressive broadcast advertising, direct mail solicitations and online promotions involving the Employee Retention Credit. While the credit is real, aggressive promoters are wildly misrepresenting and exaggerating who can qualify for the credits.

Department of Employee Retention Credit  
Tax Notice

<b>Notice</b>	<b>ERTC Employee Retention Credit</b>
Notice Date	April 27, 2023
[REDACTED]	
To contact us	(202) 949-4201
Your Caller ID	E31022-45970
Page 1 of 1	

T36 P1 158314-1-1-1 10951



Contact us (202) 949-4201  
(Mon-Fri 8am-5pm EST)  
Please visit us at  
[www.YourERCTeam.com](http://www.YourERCTeam.com)

Your notice of pending Employee Retention Tax Credit  
**Amount of estimated Tax Credit: \$1,332,000**

We are attempting to provide you with an ERC refund estimate that has been issued by Congress to compensate your business affected by the COVID-19 pandemic. Please call us immediately to verify your ERC fund estimate.

- Eligibility for all business that were affected by COVID-19
- Estimated Tax Credit of up to \$26,000 per employee
- No restrictions on use of tax refund
- Past PPP loan does not affect ERC tax refund

**ERC Estimate Summary**

[REDACTED]	
Estimated tax refund	PENDING
Estimated employee count	74
<b>Total estimated tax refund due</b>	<b>\$1,332,000</b>

## IRS Action to Combat Fraud

- Special processing of Forms 941-X > certain dollar amount
- Audits of Forms 941 and 941-X
- Public acknowledgement, communication and vehicle to report illegal ERC activities
- Report bad actors on Form 3949-A – information referral
- Report suspected abusive tax promotions or preparers on Form 14242
- 2023 “Dirty Dozen” list of tax scams



Employers warned to beware of third parties promoting improper Employee Retention Credit claims

**Issue Number: IR-2022-183**

WASHINGTON -- The Internal Revenue Service today warned employers to be wary of third parties who are advising them to claim the Employee Retention Credit (ERC) when they may not qualify. Some third parties are taking improper positions related to taxpayer eligibility for and computation of the credit.

# IRS Resources on ERC Scams

## News releases:

- **NEW:** IRS alerts businesses, tax-exempt groups of warning signs for misleading Employee Retention scams; simple steps can avoid improperly filing claims [English](#), [Spanish](#) & [Chinese](#)
- Employee Retention Credit: Beware of too-good-to-be-true offers [English](#), [Spanish](#) & [Chinese](#)

## e-Poster/flier to share electronically or post in your office or community:

- Publication 5792, Small Businesses & Tax-Exempt Organizations: Beware of Tax Credit Scams! [English](#) & [Spanish](#)

## ERC videos on YouTube you can share on your social media platforms or in other content:

- Don't Fall for Employee Retention Credit Scams [English](#) & [Spanish](#)

## ERC video shorts on YouTube with captions (multilingual) you can share on your social media platforms:

- Avoid schemes promoting the Employee Retention Credit [English](#) & [Spanish](#)
- Beware of adds that promise big money by claiming the Employee Retention Credit. (Note: this caption in English is for reference only) Two video shorts in 6 languages: [Spanish video #1](#) & [video #2](#)

## IRS Tax Tip for newsletters, emails or web content:

- Employers: Watch out for Employee Retention Credit scheme [English](#) & [Spanish](#)

## Ready-to-use article for newsletters, emails or web content:

- [Beware of Employee Retention Credit scammers](#)

# IRS Resources on ERC Scams

## Social media messages:

### Employee Retention Credit scams alert:

- #IRS alerts businesses and tax-exempt groups of the warning signs for misleading Employee Retention scams. Follow these simple steps to avoid improperly filing claims: <http://ow.ly/JHTA50Ox0hx> #ERC #ERTC
- Business owners: Learn the signs and steps to avoid improperly filing claims involving misleading Employee Retention Credit scams. <http://ow.ly/JHTA50Ox0hx>. #ERC #ERTC
- #IRS and #TaxPros continue to see a high volume of aggressive broadcast advertising, direct mail solicitations and online promotions involving the ERC. Find out more: <http://ow.ly/JHTA50Ox0hx> #ERC #ERTC
- #IRS warns of wildly misleading claims and scams regarding the Employee Retention Credit. "The aggressive marketing of the #ERC continues preying on innocent businesses and others," said IRS Commissioner Danny Werfel. Read more: <http://ow.ly/JHTA50Ox0hx> #ERTC
- Help #IRS spread the word about misleading Employee Retention Credit scams aimed at businesses and tax-exempt groups. Learn more: <http://ow.ly/JHTA50Ox0hx> #ERC #ERTC

### You can find more IRS social media content on these platforms:

- **Instagram:** Access IRSNews at [Instagram.com/irsnews](https://www.instagram.com/irsnews) or the Instagram app.
- **YouTube:** Find video tips in [English](#), [Spanish](#) and [American Sign Language](#).
- **Twitter:** Follow [@IRSsmallbiz](#) information for small businesses, [@IRSnews](#) for tax announcements, [@IRStaxpros](#) tweets news for tax professionals, [@IRSenEspanol](#) for information in Spanish, and [@IRStaxsecurity](#) for posts on scam alerts.
- **Facebook:** Get news and information for [taxpayers](#) and [tax return preparers](#); also in [Spanish](#).
- **LinkedIn:** Find agency [updates and job opportunities](#).



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# ERC Interaction with PPP Loans



# Interaction of ERC and PPP Loan

Identical wages cannot be used for both PPP loan forgiveness and ERC

- Forgiveness applications often include payroll costs and other expenses in excess of what is needed for loan forgiveness
- PPP forgiveness applications that listed only wages cannot be amended

Example: Timeline for 2020 Wages





## Example 2 from IRS Notice 2021-20

### Facts

- PPP loan of \$200,000
- Q3 & Q4 2020 ERC qualified wages paid of \$250,000
- Other loan forgiveness eligible expenses paid \$50,000
- Loan forgiveness application reported \$250,000 in payroll costs and not other expenses

### \$50,000 in qualified wages reported on loan forgiveness application eligible for ERC

- No other wages can be used as no other eligible expenses were reported on loan forgiveness application.
- If \$50,000 in other expenses had been claimed on the forgiveness application, then \$100,000 in payroll costs could be claimed for ERC as loan forgiveness could rely on \$150,000 of wages and \$50,000 of other costs

# ERC for Unforgiven PPP Loan Proceeds

Rejected forgiveness of PPP loans might free up compensation that is now eligible for ERC. If you received a PPP loan during the pandemic and have portions that are unforgiven, you're still able to claim the ERC retroactively:

- ERC credits can still be claimed on compensation not used for PPP loan forgiveness
- File Form 941-X within three years of filing or two years of paying the taxes
- Some adjustments may be required
- Shutdown or gross income decrease of 50% in 2020 and 20% in 2021 compared to same quarter in 2019 still apply



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# Amended Return Considerations

# Amended Payroll Tax Returns

To claim ERC for all quarters in:

- 2020, amend payroll tax returns by April 15, 2024
- 2021, amend payroll tax returns by April 15, 2025

*Note: The IRS has an additional two years from issuance of any refund to seek repayment , even if the statute of limitations has expired.*

# Amended Federal Income Tax Returns

- Qualified Wages Deduction Disallowance
  - Employer's deduction for qualified wages, including qualified health plan expenses must be reduced by the amount of the ERC (Section 2301(e) of the CARES Act, Notice 2021- 20, and section 3134(e) of the IRC)
- Timing of Wage Addback
  - Tax year in which the qualified wages were paid or incurred (Notice 2021-49)
  - Partnerships which have not elected out of the partnership audit regime adjust the current year return, paying tax at the partnership or partner level

## Other IRS ERC Resources

<https://www.irs.gov/coronavirus/employee-retention-credit>

<https://www.irs.gov/newsroom/employee-retention-credit-2020-vs-2021-comparison-chart>