Tax Notes

Didn't Get the PPP? Think About the Employee Retention Credit

By Sandy Weinberg, JD, Principal, and Christopher Migliaccio, JD, Senior Manager

By far, the most discussed aspect of the CARES Act has been the Paycheck Protection Program (PPP) loans. And with good reason. The PPP loans provide a powerful benefit of up to 2.5 times monthly payroll costs, and the possibility that the entire loan will be forgiven. The Employee Retention Credit (ERC), also introduced under the CARES Act, received comparatively less press. This was understandable as the Act explicitly states that a business could not obtain both and the ERC, limited to $5,000 per employee, is almost certainly a smaller benefit than the PPP loan.

But as businesses now determine that they are not eligible for the PPP loan, or are perhaps unable to secure the funds, they should consider whether and to what extent they qualify for the Employee Retention Credit, and the best method to go about claiming it. Answers to a few questions may dictate whether and how to pursue the credit.

Question 1 – Did Your Business Receive a PPP loan?

As noted, employers that receive the PPP cannot receive an Employee Retention Credit. The IRS has also confirmed that an employer that is treated as a single employer under the aggregation rules, cannot receive the ERC if any member of the employer's aggregated group [determined under IRC §52(a) and (b) and IRC §414(m) and (o)] receives a PPP loan. The IRS has confirmed, though, that if an employer repays its PPP loan by the May deadline, then it will be treated as though it had not received a PPP loan for purposes of determining ERC eligibility.

However, your business can still take advantage of the employment tax deferral, as discussed here. Even if you received the PPP loan, you can still defer employment taxes until the date the loan is forgiven. The amount deferred before that date can be deferred as follows: 50% until December 31, 2021, and the remainder until December 31, 2022.

Question 2 – Has Your Business Been Significantly Affected by COVID-19?

To be eligible for the Employee Retention Credit, your business (including a tax-exempt organization) must carry on a trade or business where:

- Operations were fully or partially suspended on orders from a governmental authority due to COVID-19 (COVID-19 Shutdown). You no longer qualify when the relevant order is lifted.

or

- Your business experienced a 50% reduction in gross receipts for a calendar quarter in 2020 as compared to the same calendar quarter in 2019 (Gross Receipts Decline). The period ends when your gross receipts for a calendar quarter in 2020 are 80% of the gross receipts in the same calendar quarter in 2019. This test requires you to analyze gross receipts across all entities treated as one employer under the aggregation rules.

Whether your business is subject to a partial suspension can be a difficult question to answer. While a business that has clearly had one piece of its business suspended qualifies (e.g., a restaurant that cannot provide sit-down service). A business with an office that has been closed but which can continue comparable operations via telework does not qualify.

Question 3 – How Many Full-time Employees Did Your Business Have in 2019?

While employers of all sizes qualify for the credit, it applies differently depending on the number of full-time employees the business averaged in 2019 (computed on a monthly basis).

If you employed more than 100 employees on average in 2019, qualified wages are wages paid to your employees who are not providing services due to a COVID-19 Shutdown or Gross Receipts Decline. If an employee is providing part-time services, the credit is available for wages paid above the amount of services provided (i.e., if an employee is working 50% of their prior number of hours, but being paid 75% of their prior salaries, 25% of their salary is qualified wages).

Wages cannot exceed the amount paid to an employee in the 30-day period immediately preceding the period in which the employee is paid. The aggregation rules discussed above apply in determining an employer's total number of employees.

If you averaged in 2019, 100 or fewer employees, the calculation is simpler. Qualified wages are wages paid to any employee without regard to whether the employee is providing services.

Question 4 – How Do You Calculate the Credit for Your Business?

The Employee Retention Credit equals 50% of each employee's qualified wages, up to a maximum of $10,000 of wages. As such the credit is capped at $5,000 per employee.

The earliest date qualified wages could have been paid is March 13, 2020, and the latest date will be December 31, 2020 (although qualified wages must be paid during the time the business is affected by COVID-19). While health plan expenses may be included in determining qualified wages, credits cannot be claimed for employees who have been furloughed and are receiving no wages other than health plan benefits.

To the extent the credit amount exceeds the amount of Social Security tax due on the wages paid, it is refundable to the employer.

While the ERC can be claimed on a taxpayer's quarterly employment tax return (Form 941 or similar), taxpayers will be able to file a Form 7200 to receive an advanced credit any time before 30 days after the end of a quarter (i.e., before the due date of the taxpayer's quarterly employment tax return, which is 30 days after the end of a quarter). For more information, see our recent *Tax Notes* here.

If the employer was eligible for the credit for wages paid in the first quarter, but did not claim the credit on Form 941, an amended Form 941-X can be filed to claim the credit.

Question 5 – Should You Use a CPA Firm to Assist?

The IRS has noted that numerous common errors have occurred when taxpayers have sought advance payments of the Employer Retention Credit. It recommends using a CPA or tax return preparer. Further, many payroll tax providers have stated that they will not be completing Form 7200 for their clients. Finally, fact-specific issues may require guidance. As a result, in many instances, it is recommended that employers work with a CPA firm to assist in obtaining the credit.

While it may not match the PPP loan program, the Employer Retention Credit has the potential to provide significant and immediate benefit to eligible employers. Your business should consider taking advantage of this opportunity if you are not part of the PPP loan program and you qualify for the credit.

Contact Us

PKF O'Connor Davies is monitoring the situation with regard to the CARES Act. If you have any questions about the payroll tax provisions, specifically the payroll tax deferral and the employee retention credit, please contact your client services partner or:

Sandy Weinberg, JD
Principal
sweinberg@pkfod.com | 203.705.4170

Christopher Migliaccio, JD
Senior Manager
cmigliaccio@pkfod.com | 646.699.2890

About PKF O'Connor Davies

PKF O'Connor Davies, LLP is a full-service certified public accounting and advisory firm with a long history of serving clients both domestically and internationally. With roots tracing to 1891, twelve offices in New York, New Jersey, Connecticut, Maryland and Rhode Island, and more than 800 professionals, the Firm provides a complete range of accounting, auditing, tax and management advisory services. PKF O'Connor Davies is ranked 27th on *Accounting Today'*s 2020 "Top 100 Firms" list and is recognized as one of the "Top 10 Fastest-Growing Firms." PKF O'Connor Davies is also recognized as a "Leader in Audit and Accounting" and is ranked among the "Top Firms in the Mid-Atlantic," by *Accounting Today.* In 2020, PKF O'Connor Davies was named one of the 50 best accounting employers to work for in North America, by *Vault*.

PKF O'Connor Davies is the lead North American representative in PKF International, a global network of legally independent accounting and advisory firms located in over 400 locations, in 150 countries around the world.