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Tax Notes

Form 941 Deadline Approaching: There Is Still Time for Not-for-Profits to Take Advantage of Payroll Tax Relief

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With the second quarter employment tax return filing date approaching, it is not too late for not-for-profit organizations to explore their eligibility for the Employee Retention Tax Credit (ERTC) and/or the Employer Payroll Tax Deferral provisions under the Coronavirus Aid, Relief, and Economic Security (CARES) Act, discussed below.

"Nothing is more expensive than a missed opportunity." – H. Jackson Brown, Jr.

Employee Retention Tax Credit (ERTC)

Not-for-profit organizations that either did not receive a Paycheck Protection Program (PPP) loan or have repaid their PPP loan in a timely manner are eligible for the ERTC – a refundable credit. Like the PPP loan program, the ERTC was designed to encourage eligible employers to continue to pay employees during the pandemic.

To qualify, the not-for-profit organization must have experienced:

- a suspension or partial suspension of their operations due to a government order limiting travel, commerce or group meetings due to COVID-19, **or**
- a significant decline in gross receipts during a calendar quarter.

A not-for-profit organization is considered to have a significant decline in gross receipts for the period beginning with the first calendar quarter in 2020 for which its gross receipts are less than 50 percent of gross receipts from the same calendar quarter in 2019.

The credit ends on the earlier of January 1, 2021 or the first calendar quarter after the quarter for which gross receipts are greater than 80 percent of gross receipts for the same calendar quarter in 2019.

Qualifying wages are those wages subject to Medicare tax and paid to an employee after March 12, 2020 and before January 1, 2021. Qualified wages are increased by the employer's and the employees' pre-tax share of group health plan costs incurred during the same period of eligibility. The refundable tax credit – which offsets employment taxes – is equal to 50% of qualified wages (not to exceed $10,000 in wages per employee); thus, the maximum credit for an eligible employer for qualified wages paid to any employee is $5,000.

For employers averaging **100 or fewer full-time employees** in 2019, ***all*** qualifying wages paid during any period in which the business operations are fully or partially suspended due to a governmental order or any quarter the business is experiencing a significant decline in gross receipts are eligible for the credit.

If an employer averaged **more than 100 full-time employees** in 2019, qualified wages are ***only*** amounts paid when an employee is not providing services due to the full or partial suspension of the business or during a quarter in which there is a significant decline in gross receipts.

An eligible business can claim the ERTC by reducing its federal employment tax deposit – without penalty – in any qualifying calendar quarter by the amount of its expected employee retention credit. The credit for qualifying wages paid since March 13, 2020 should be claimed on the second quarter employment tax return.

If a not-for-profit organization subsequently determines in 2021 that it had a significant decline in receipts that occurred during a calendar quarter of 2020 where they would have been eligible for the credit, the not-for-profit organization can claim the credit by filing an amended return (Form 941-X) in 2021. Furthermore, in the event the payroll tax credits exceed payroll deposits, a not-for-profit organization may choose to have its refundable payroll tax credit expedited – instead of claiming the refund on its upcoming quarterly payroll tax return – by filing Form 7200, Advance Payment of Employer Credits Due to COVID-19 at any time during the quarter.

For more information, please refer to the IRS FAQs.

Employer Payroll Tax Deferral

The ability to defer payment of the employer share of payroll taxes is yet another particularly helpful relief measure for nonprofit organizations offered by the CARES Act. Under this relief provision, not-for-profit organizations may defer deposits of their share of Social Security taxes due on or after March 27, 2020 and through December 31, 2020. Not-for-profit organizations can utilize the payroll tax deferral as a tool to improve current cash flow and have more cash on hand to fund operations during the pandemic.

The deferrable portion of employer payroll taxes is limited to the 6.2% Social Security tax and does not apply to the 1.45% Medicare tax or to any amounts withheld from employees' wages. The deferred tax is permitted to be paid over a two-year period, with half of the deferred amount due December 31, 2021, and the remaining half due December 31, 2022.

As originally enacted, the CARES Act required employers who received a Paycheck Protection Program (PPP) loan to stop deferring the Social Security tax after receiving notification of loan forgiveness. However, the Paycheck Protection Program Flexibility Act (PPFA) enacted on June 5, 2020 fortunately eliminated this restriction. Advantageously, loan forgiveness recipients can continue to defer payment of the employer share of the Social Security tax.

There is no election, application form, or approval procedure required to take advantage of this generous deferral. Rather, not-for-profit organizations may simply reduce their deposit amounts. For informational purposes only, the revised Form 941 now has added Line 13b to report the deferred amount of the employer's share of Social Security taxes during the calendar quarter.

It is also noteworthy that the second draft of the Form 941 instructions states that an employer may treat prior deposits during the quarter as first being deposited for employment taxes other than the employer share of Social Security tax. Therefore, employers who have previously deposited employer Social Security tax may choose to reduce their deposits of other employment taxes (federal income tax withholding, employee Social Security tax, and employee and employer shares of Medicare taxes) by the amount of employer Social Security tax deposited for the quarter.

For more information, please refer to the IRS FAQs.

PKFOD Observations

The IRS recently released the final version of the revised Form 941, Employer's Quarterly Federal Tax Return*,* and a second draft of the instructions. The revised Form 941 is to be used starting with the second quarter of 2020 (April 1 to June 30). The form includes 18 new lines for reporting data on coronavirus-related employment tax relief.

It is important for not-profit-organizations utilizing a third-party payroll provider or a Professional Employer Organization (PEO) to work closely in tandem with each other.

We recommend not-for-profit organizations begin to compile pertinent documentation necessary for payroll reporting now and provide advance notification to their third-party providers as to their specific circumstances.

Contact Us

For more information on these payroll tax provisions, please contact a member of your tax-exempt client service team at PKF O'Connor Davies, LLP or Garrett M. Higgins, CPA, Partner at ghiggins@pkfod.com.

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