Don't Be Fooled: Employee Retention Credit Scams

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The Employee Retention Credit (ERC) is a valuable tax credit provided by the U.S. government to offer financial assistance to businesses that were negatively impacted by the pandemic. Many companies in the transportation industry were able to take advantage of this credit due to the negative impact that certain government orders had on their business. Through February 2023, it has been estimated that over $50 billion in ERC funds have been paid to hundreds of thousands of businesses. With applications tied only to the submission of timely amended payroll tax returns, ERC funds will continue to be applied for and paid through April 2025.

We've written in great detail about the opportunities relating to the ERC. However, we've also seen an increase in deceptive communications relating to the ERC that are troubling – not just to us, but also to the IRS, which named claims regarding the ERC as #1 on its 2023 Dirty Dozen list of tax scams.

Backdrop

The ERC is a payroll tax credit, initially made available as part of the CARES Act in March 2020 and extended and changed over a number of relief bills in 2020 and 2021.

There are limited ways that a business could qualify for the ERC:

- Suspension of operations – If business operations were fully or partially suspended due to orders relating to COVID-19 mandated by an appropriate government authority in 2020, which was particularly relevant to the public-school bus industry, or the first three quarters of 2021, or
- Significant decline in gross receipts – If a business experienced at least a 50% decline in gross receipts in a 2020 calendar quarter compared to the same 2019 calendar quarter or at least a 20% decline in gross receipts in a 2021 calendar quarter compared to the same 2019 calendar quarter, or
- Qualified as a recovery startup business for the third or fourth quarters of 2021.

The qualification most at issue is the "suspension of operations" – that's where the IRS is seeing most of the aggressive positions and outright fraud rooted.

Buyer Beware

The seemingly unlimited amount of ERC monies, combined with complex rules and eligibility criteria, have recently spawned an explosion of marketing campaigns that you likely have seen, heard, or read through various communication platforms (email blasts, letters, radio and TV ads) … many which seem "too good to be true." So aggressive and misleading are their tactics that in March 2023, promotion claims regarding ERC services topped the "2023 Dirty Dozen," an annual list compiled by the IRS of the "worst of the worst" tax scams. The IRS indicated concerns with "blatant attempts by promoters to con ineligible people to claim the credit."

While difficult to recognize by businesses genuinely seeking professional guidance, some of what we have seen firsthand include:

- False or exaggerated claims that a business might qualify, or the likelihood of success in claiming the credit. Many of these ads will indicate a "success rate" with the credit, which is currently meaningless when the IRS audit process is just beginning to ramp up.
- Falsification of documentation or manipulation of data to increase the credit, or to give the appearance the business is eligible when it is not. We have seen clients receive documents manipulated to look like an IRS notice stating that a company is "due" a credit.

- Calculations of the credit that do not factor in other government funding sources (PPP Loans, Shuttered Venue Grants, Restaurant Revitalization Funding), or omission of the fact that the credit must be reflected as a reduction in wages on an amended income tax return.
- Excessive fees or ones that are based on a percentage of the calculated or expected credit. A business claiming a contingent fee based on the credit amount has a significant conflict of interest and incentive to claim eligibility over a longer period.
- Identity theft and other frauds perpetrated using information sent by unsuspecting business owners.
- The lack of asking pertinent questions. Common ownership rules require businesses to be aggregated in certain circumstances, before assessing whether the aggregated group of companies would be eligible for the ERC. Similarly, depending on the company's average full time equivalent employees, the credit could be limited to those employees being paid to not work, as opposed to including all employees in the calculation. Simply looking at a company in isolation and asking limited questions as if to assume that all companies qualify, is not the proper way to assess whether or not the company is eligible for the ERC.

Our best recommendation remains to work with an organization with a history of providing tax advice and one not charging a contingent fee.

Closing

Businesses should be careful when using others to calculate their Employee Retention Credit to ensure accuracy, compliance, confidentiality and clear communication throughout the process. Ultimately, the responsibility for an incorrect ERC calculation falls on the business claiming the credit. With the IRS having the ability to audit ERC claims for five years after filing, expect the IRS to hold businesses accountable, assessing significant penalties and interest in addition to having to repay the excess credit and, in some cases, pay additional fines or apply criminal prosecution, or both.

Contact Us

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