CLIENT ALERTS

Federal Tax Update: Expanded Tax Credit Opportunity and New IRS Rules Regarding PPP Loans

1.8.2021

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Tax

TAX CREDIT OPPORTUNITY – EMPLOYEE RETENTION CREDIT

Businesses financially impacted by the COVID-19 pandemic may be eligible for the Employee Retention Credit (the "Credit" or "ERC"). This Credit, a refundable tax credit intended to provide economic relief, was originally enacted as part of the CARES Act and recently modified by the Consolidated Appropriations Act, 2021 ("2021 Appropriations Act") (H.R. 133) signed into law on December 27, 2020.

Eligibility and Calculation

In general, a business must satisfy either of the two requirements below to qualify for the Credit:

- the business fully or partially[1] suspended operations during at least one quarter of 2020 due to governmental orders related to the COVID-19 pandemic; or
- the business realized a *significant* decline in its gross receipts for a calendar quarter compared to the same quarter in 2019. A significant decline is defined as 50% for 2020 or 20% for 2021.[2]

The Credit, available for wages paid through June 30, 2021, is calculated based on 50% of the qualified wages (including qualified health plan expenses) paid to an employee in 2020 and 70% of the qualified wages paid in each of the first two calendar quarters of 2021. The Credit is capped at $5,000 per employee in 2020 (50% of the first $10,000 of qualified wages) and $14,000 per employee in 2021 (70% of the first $10,000 of qualified wages in each of the first and second quarters). The calculation of qualified wages depends, in part, on the number of full-time employees employed during 2019. For 2020, the calculation of qualified wages depend on whether employers averaged more than 100 full-time employees in 2019; for 2021, this threshold is increased to 500.

Claiming the Credit

To claim the Credit, the employer can directly reduce its deposits of payroll taxes withheld from employees' wages by the amount of the Credit as determined by the employer and account for the taxes retained as the Credit upon filing Form 941 (Employer's Quarterly Federal Tax Return), which is generally due by the last day of the month following the end of the quarter. For employers who may have been eligible but did not take advantage of the Credit, the Credit may be retroactively claimed within the appropriate timeframe by filing Form 941-X adjustment, requesting a refund. In addition, some employers may be eligible to claim an advance of the credit before the qualified wages are paid.

Coordination between the PPP and the ERC

In addition to the modifications discussed above, the 2021 Appropriations Act allows recipients of PPP funds to claim the Credit. Previously, under the CARES Act, the Credit was available to businesses that did not receive funds under the PPP program. Additional guidance from the Internal Revenue Service ("IRS") is anticipated with regard to the interplay between the PPP and the ERC.

IRS ISSUES REVENUE RULING RELATED TO PAYROLL PROTECTION PROGRAM LOANS

The IRS released Revenue Ruling 2021-2 on January 6, 2021 which declares Notice 2020-32 and Revenue Ruling 2020-27 related to guidance disallowing deductions of expenses paid for with Payroll Protection Program (PPP) loan money obsolete due to the enactment of the COVID-19 Economic Relief Bill. This legislation made critical changes to the Payroll Protection Program established under the CARES Act (see here for our Client Alert on this bill). One of the critical changes provides that taxpayers may deduct otherwise eligible expenses paid with the proceeds of PPP loans, even if those loan amounts are forgiven. This legislation has resulted in the reversal of the position previously taken by the IRS.

Please contact a Butzel Long attorney listed on this Client Alert for further information on the updates discussed above or for general assistance.

CORONAVIRUS (COVID-19) RESOURCE PAGE

Please visit the Butzel Long Coronavirus (COVID-19) Resource Center for the latest information for businesses and individuals on the legal, regulatory, and commercial implications of the COVID-19 virus.

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[1] The IRS has provided guidance interpreting what it considers partially suspended. Among the guidance provided is the IRS FAQ on the Credit, available at https://www.irs.gov/newsroom/faqs-employee-retention-credit-under-the-cares-act

[2] For 2020, a business' eligibility lasts through the end of the quarter for which its gross receipts for the quarter exceed 80% of the gross receipts for the same calendar quarter in the prior year. For 2021, if a business did not exist at the beginning of the same quarter of 2019, the same quarter in 2020 is substituted.