

Employee retention credit: Fact or fiction?

Given COVID-19's wide-reaching effects, many small businesses will qualify for an employee retention credit (ERC).

FICTION. Determining whether a business is eligible for the ERC can be pretty complex. Your business must meet the gross receipts test (50% or more reduction for 2020 or a 20% or more decline for 2021 qualifying quarters when compared to 2019 quarters) or experience a full or partial suspension of operations because of a government order. Whether a business experienced a partial suspension is a facts and circumstances determination and will vary depending on the location of the business and the government orders.

My business did not have a significant revenue decline in a calendar quarter compared to 2019 (50% or more for 2020 or 20% or more for 2021), but I can still qualify for an ERC.

FACT. However, as noted above, there must have been a full or partial suspension of operations **BECAUSE OF A GOVERNMENT ORDER** that limited commerce, travel or group meetings due to COVID-19. A partial suspension is based on the facts and circumstances of what government orders are in place for the location. The orders would need to have a more than a nominal impact on the business to qualify for the ERC.

All safety recommendations or guidelines a government agency issues should be considered government orders to suspend operation requirements.

FICTION. Government orders are defined as orders, proclamations and decrees from federal, state or local governments that have jurisdiction over the business operations. No federal order during 2020 or 2021 would qualify businesses for the ERC, so it is important to review the state and local orders.

My business experienced supply chain disruption, which means it qualifies for the ERC.

FICTION. Experiencing supply chain issues stemming from the pandemic does not guarantee ERC eligibility. The supply chain issues must result from a government order that affects its supplier, and **ALL** these requirements must be met:

- ▶ Supplier cannot make deliveries of critical goods due to a government order.
- ▶ Business can't purchase those critical goods from another supplier.
- ▶ Business must experience a more than nominal effect as a result.

My business qualifies for ERC because employees and clients had to wear masks.

FICTION. The requirement to wear a mask alone does not automatically mean there was a full or partial suspension of business operations that had a more than nominal impact on the business.

My business was in a location where there was a stay-at-home order, and I adjusted operations based on this. This automatically means I can claim the ERC.

FICTION. The IRS clearly states that voluntary reductions of hours or closing based on service demand do not create a full or partial suspension of its operations due to a government order.

As an owner, my salary and family members' salaries are qualifying salaries for calculating the ERC.

FICTION. Salaries of majority owners and their families cannot be included in the ERC calculation. Family attribution rules apply; if the business owner has any living relatives, then none of the salaries are eligible.

My business received my Form 941-X refund from a 2021 quarter in 2022, so I should amend my 2021 income tax return to reflect the adjustment for wages.

FACT. The wage reduction used to calculate the ERC must happen in the tax year in which the wages were paid or incurred, so you would amend your 2021 income tax return to adjust the wages.

My business received a Paycheck Protection Program (PPP) loan, but it can still qualify for the ERC.

FACT. Legislation passed at the end of 2020 allows businesses that received PPP to apply for the ERC for qualifying quarters as long as the same salaries are not used and the business meets one of the qualifications for the ERC.

The ERC applied to payroll tax returns in 2020 and 2021, so my business cannot claim the credit now.

FICTION. Form 941-X can be used to amend a previously filed payroll tax return for the ERC qualifying quarters. For determining the three-year statute of limitations, Forms 941 for a calendar year are considered filed on April 15 of the succeeding year if filed before that date. Therefore, for each quarter of 2020, Form 941-X will be due by April 15, 2024. For each quarter in 2021, Form 941-X will be due by April 15, 2025.

There were so many claims for the ERC that the IRS is unlikely to audit my business' return.

FICTION. While there is no guarantee that the IRS will examine your business' ERC claim, they are aware of the potential for abuse related to this credit and scrutiny of COVID-19 relief funds are high in general.

If my business must pay back the ERC, the penalties will be large.

FACT. The amount of the penalty (and interest) on the unpaid payroll taxes could be substantial, especially if the IRS imposes fraud and negligence penalties upon examination.

I have heard about new companies that guarantee large refunds but charge a high contingent fee for assistance claiming the ERC. It seems anyone can process ERC claims.

FICTION. There may be companies that are not well versed in all the complexities of the rules and regulations required for eligibility determination and ERC calculations. You are responsible for ensuring that you are working with a reputable company. One consideration is to determine whether the company has experience working with the IRS and can provide support to your business in the case of audits or examinations.

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