



Building a better working world



Helping Paycheck Protection Program (PPP) recipients and small to mid-sized employers capture the Employee Retention Credit (ERC)

On December 27, 2020, President Donald Trump signed the Consolidated Appropriations Act, 2021 (CAA), which amended the Coronavirus Aid, Relief, and Economic Security (CARES) Act and extended the ERC through June 30, 2021, while also modifying the credit both prospectively and retroactively.

Potential value of the ERC:

500	Employees
× \$19,000	Potential ERC/employee*
\$9,500,000	Total credit

*For wages paid in 2020 and 2021

Although this refundable credit will help businesses retain employees and offset economic loss, the underlying eligibility and qualified wage rules will require thorough analysis to capture the full benefit due.

Significant ERC modifications for PPP recipients and small to mid-sized employers:

- ▶ The CAA permits PPP recipients to claim the ERC retroactive to March 13, 2020. PPP recipients may take the ERC on qualified wages that are not paid for with forgiven PPP proceeds.
- ▶ The total ERC benefit per employee can be up to \$19,000 (\$5,000 in 2020 and \$14,000 in 2021).
- ▶ For Q1 and Q2 2021, eligible employers that had less than 500 full-time employees in 2019 may claim the ERC on 70% of all wages (up to \$10,000 per quarter) paid to employees, without regard to whether the employee provided services.
- ▶ The CAA adds several new categories of forgivable expenses (60% of PPP proceeds must still be used on payroll costs in order to receive full forgiveness).

Example: An employer obtains a PPP loan of \$1,000,000 and incurs \$1,000,000 in payroll costs and \$400,000 in other PPP-eligible expenses.

Expenses included in PPP forgiveness application:

- 60% payroll costs
- 40% other PPP covered expenses (rent, mortgage interest, etc.)

An eligible employer may be able to use the ERC to cover the remaining 40% of unforgiven payroll costs.

Summary of the key provisions – comparing the CARES Act to the CAA

The primary provisions of the CARES Act and the CAA are summarized below for reference.

	CARES Act key provisions	Changes under the CAA
Eligible employer definition	<p>Employers that carried on a trade or business during 2020 and:</p> <p>(1) Suspended operations fully or partially as a result of a COVID-19-related governmental order</p> <p>Or</p> <p>(2) Experienced at least a 50% year-over-year decline in calendar quarter gross receipts</p> <p>Tax-exempt organizations (excluding governmental employers) are eligible.</p> <p>An employer receiving a loan under the PPP is not eligible for the ERC.</p>	<p>Employers that receive PPP loans in 2020 and 2021 may claim the ERC as long as ERC wages are not paid with forgiven PPP loans.</p> <p>Eligible employers applying the gross receipts test only have to experience a 20% decline (reduced from 50%) in calendar quarter gross receipts starting January 1, 2021.</p> <p>Public colleges, universities and government entities providing medical or hospital care are now eligible for the ERC beginning January 1, 2021.</p>
Qualified wages	<p>For eligible employers that had an average number of full-time employees (within the meaning of Section 4980H) in 2019 greater than 100, wages paid to employees with respect to which an employee is not providing services due to reasons (1) or (2) above and not in excess of what the employee would have been paid for an equivalent amount of work in the 30 days immediately preceding the credit period.</p> <p>For eligible employers that had an average number of full-time employees in 2019 of 100 or fewer, wages paid to employees regardless of whether an employee provides services.</p> <p>Wages do not include wages taken into account under Sections 7001 and 7003 of the Families First Coronavirus Response Act (COVID-19 paid leave credits).</p>	<p>Eligible employers that had an average number of full-time employees in 2019 of 500 or fewer (increased from 100) can consider wages paid to employees regardless of whether an employee was providing services as qualified wages beginning on January 1, 2021.</p> <p>Qualified wages for the ERC are no longer limited to the amount of wages paid in the prior 30 days beginning on January 1, 2021.</p>
Refundable credit definition	<p>An eligible employer is entitled to a refundable credit equal to 50% of qualified wages paid from March 13, 2020 through December 31, 2020, plus qualified health plan expenses (up to \$10,000 per employee).</p>	<p>Beginning on January 1, 2021, an eligible employer is entitled to an increased credit percentage of 70% of qualified wages and increased qualified wage limitation to \$10,000 per employee per quarter. The credit now expires on June 30, 2021.</p>
Credit overlap and Section 280C(a) analysis	<p>The credit is not allowed for any employee for any period in which the Work Opportunity Tax Credit (WOTC) is claimed on such employee; wages used for the credit may not be used for the Section 45S credit. The deduction for wages and salaries must be reduced by the amount of the credit.</p>	<p>The credit is not allowed for any employee for any period in which the wages are also claimed on the WOTC, Section 41 (credit for increasing research activities), the Indian Employment Credit (IEC), 45P (active duty credit), Section 45S (paid family medical leave credit) or the Federal Empowerment Zone Credit.</p>

Key data points a business needs to examine to validate its ERC opportunity



For 2020 PPP recipients:

- ▶ Has the business already filed for loan forgiveness? If no, an ERC evaluation is recommended prior to filing for forgiveness. Even if a business has filed for forgiveness, it may still qualify for the ERC and have qualified wages depending on its facts and circumstances.
- ▶ Was the business an eligible employer under the CARES Act (i.e., partially suspended due to governmental orders or experienced a drop in gross receipts of more than 50%)?
 - ▶ If yes, determine which quarters were impacted
 - ▶ If yes, determine the full-time employee count for 2019 under IRC Section 4980H
- ▶ Did the business have 100 or less full-time employees?
 - ▶ If yes, then all wages paid to employees can qualify regardless of whether employees provided services
 - ▶ If the business has more than 100 full-time employees, then evaluate which employees were not providing services

For 2021 PPP recipients:






- ▶ Has the business already applied for a PPP loan in 2021?
 - ▶ If no, evaluate the timing and eligible expenses of the PPP loan together with ERC eligibility to determine amounts available under both programs
 - ▶ If yes, evaluate whether the business is eligible for the ERC in Q1 2021 either due to new or existing governmental order restrictions or a drop in gross receipts of 20% or more (vs. Q1 2019 or Q4 2020 vs. Q4 2019).
- ▶ Under the CAA, the 2021 ERC may be claimed on all 300 employees regardless of whether or not they are providing services.

Does your business have non-payroll, forgivable PPP expenses that would permit you to reduce the amount of payroll costs included in your forgiveness application and still meet the 60% test? If yes, consider the ERC as an option to offset payroll costs.

- ▶ If an employer has more than one legal entity, all entities must be aggregated under rules in IRC Sections 52 and 414. This rule applies for purposes of determining the number of full-time employees and determining if the employer experienced a significant decline in gross receipts.
- ▶ If the aggregated group includes non-US entities, the gross receipts test may require a global analysis.

How Ernst & Young LLP (EY US) can help

During 2020, we helped hundreds of employers in virtually all sectors, including essential businesses, capture the ERC. We have developed a process and technology to assist employers with the requirements and opportunities of the ERC in an efficient and accurate manner. Our services include the following:

-  **1. ERC feasibility (preliminary eligibility determination and value proposition):** we have developed a streamlined feasibility study that analyzes ERC and PPP eligibility and models potential ERC and PPP value under various scenarios.
-  **2. Substantiating ERC eligibility and capturing qualified wages:** to determine eligibility for the ERC, employers should review governmental orders from March 2020 through June 2021 and consider eligibility under the gross receipts test, then verify that all qualified wages are identified and captured. EY US professionals have extensive experience determining eligibility and analyzing payroll.
-  **3. Secure data collection:** data security is paramount, especially when dealing with payroll data. EY US professionals have deep experience securely receiving and tracking sensitive employee data.
-  **4. Credit computation and overlap analysis:** We can assist with computing the refundable credits for each qualified employee, including completing overlap analysis for the WOTC, Section 45S, Section 41, the IEC, Section 45P and the Federal Empowerment Zone Credit and ensuring ERC qualified wages are not paid for with forgiven PPP proceeds.
-  **5. Forms 941 and 941-X support:** the refundable credit is claimed on the quarterly IRS Forms 941 and 941-X or Form 7200. Any excess credit can be refundable as a cash refund or can be applied against future liability. Employers have three years to file amended Forms 941-X and claim the ERC. We can assist the business by preparing the necessary forms to claim the refundable credit. Conversely, with client authorization, EY US professionals can work directly with an external payroll provider to support claiming the credit, which would include confirming that all necessary forms are prepared and filed properly.

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Why EY US

We have the technical know-how, subject-matter resources and digital platforms to quickly help employers determine eligibility for the ERC and compute and claim the credit. We bring the multifunctional tax technical capabilities of our Employment Tax, Tax Credits, and Compensation & Benefits practices to assist our clients. Our experience includes:

- ▶ Hundreds of 2020 ERC eligibility analyses, utilizing our national database of governmental orders and knowledge of accounting methods
- ▶ PPP First Draw Loan modeling, compliance and assistance with forgiveness
- ▶ Significant knowledge of IRC Section 4980H full-time employee determinations since the enactment of the Affordable Care Act
- ▶ Application of complex compensation and benefit rules, including aggregation rules under IRC Sections 52 and 414