

insight

The 10 Biggest Myths of the Employee Retention Credit

Debunk the misunderstandings surrounding the Employee Retention Credit to help your business clients receive a much-needed cash infusion. **By Rick Meyer, CPA, MBA, MST | Digital Exclusive - 2021**



The Employee Retention Credit (ERC) is huge! In March 2021, this credit was extended through Dec. 31, 2021 and then expanded as part of the American Rescue Plan Act of 2021.

But let's face it ... many of us CPAs—the highly trusted, value-adding professionals—are blowing it. We're not fully grasping the nuances and complexities of this expanded law. As a result, we're not properly educating and helping our clients with this large, refundable credit—yikes!

So, what are we misunderstanding about this credit? Let's review.

The ERC is a tax credit first put in place last year as a temporary coronavirus relief provision to assist businesses in keeping employees on payroll. It definitely helped. Tens of thousands of businesses have already received more than \$1 billion in tax credits through the ERC just this year, according to the White House. This boatload of cash flow has provided a night-and-day difference for those companies struggling to keep employees on payroll and their doors open.

However, we've also seen many companies close their doors. I wonder, did we help them get the ERC and the maximum amount possible? Did we help them with the proper documentation to pass muster with the IRS? Were we there to help educate them about the new enhancements of the ERC?

Maybe not—and maybe that's because of our own misunderstandings. Here are the top 10 misunderstandings and myths surrounding the ERC—and how to correct them.

1. My client can't claim the ERC if they've already claimed Paycheck Protection Program (PPP) funds or gotten their PPP loans forgiven.

Now you can claim both! Congress removed such limitations in the Consolidated Appropriations Act (CAA) of 2021. What's more, PPP funds will only account for 2.5 times your monthly payroll expenses and is meant to be spread out over six months. This leaves plenty of uncovered wage expenses for claiming the ERC.

2. My client's business didn't have a drop in gross receipts of 50 percent or more.

The CAA reduced this qualification to a drop of 20 percent or more. Also keep in mind that a business may qualify for the ERC if it was subject to a partial or full suspension due to a government order.

3. My client's business wasn't shut down during the pandemic.

Even a partial suspension order by the government (federal, state, or local) of your client's business could potentially qualify. For instance, a partial shutdown, a disruption in their business, inability to access equipment, having limited capacity, shutdowns of their supply chain or vendors, reduction in services offered, reduction in hours to accommodate sanitation, shutdown of some locations and not others, and shutdowns of some members of a business are all scenarios that still potentially qualify your client for the ERC. The key question is: Due to a government-ordered suspension is/was your client's business not able to continue its activities in a comparable manner, and did that result in a more than nominal impact on their business operations? Remember, the partial or full suspension is an alternative way to qualify for the ERC that is separate from the reduction in gross receipts test.

4. My client's company was deemed an essential business, so they don't qualify due to business suspension.

Even if your client's business is deemed essential, an impact to or change in their business may still qualify them. For example, if they were open but their vendors were closed or they couldn't go to their client's job site, they may still qualify. Alternatively, if part of their business was considered non-essential and was impacted by a government-ordered suspension, they may also qualify. The scenarios discussed above could apply here as well.

5. My client's company has grown during the pandemic, so this isn't something they should take.

Great news! If your client's company has grown during the pandemic, but experienced a full or partial suspension, there are still expenses that may qualify for the ERC.

6. Sales have rebounded for my client in the first quarter of 2021, so they can't qualify for this credit.

The CAA allows you to look at one quarter prior to determine qualification. This means we can still potentially determine eligibility based on lost revenue in 2020. Also, your client may still qualify if their business was subject to a full or partial suspension.

7. My client was generating losses, or they don't have any tax liability.

This ERC is a refundable credit. In practice, this means that any credit above tax liability is sent to the taxpayer/business owner as a refund.

8. My client's company has grown to more than 500 employees, so they're not eligible for the ERC.

The employee count restriction is based on full-time equivalent (FTE) employees, which is a more involved calculation than just counting everyone on payroll. For example, the FTE calculation recognized less than 500 employees at a business we helped when they employ 640 individuals. Further, if your client paid any employees to not work, or to work fewer hours for which they were paid, then the employee count restriction would not apply to those employees.

9. My client is a charity and the ERC is only for businesses.

The ERC also may provide significant benefit to charities—churches, nonprofit hospitals, museums, etc. Charities can be particularly good candidates for the ERC.

10. The IRS is too busy to properly check documents.

There are still many tax advisors who think they can just create their own simple form. They check a few boxes, give a few sentences of explanation, and expect the IRS to hand over thousands of dollars. Guess again.

We've spoken with former senior IRS officials. It's clear that the best practice is for businesses to provide contemporaneous documentation from counsel that will properly and fully document how they qualify for the ERC.

Let's face it ... many businesses are still struggling to stay open. There's still so much economic uncertainty due to COVID-19 and its variants. What affect will this have on your client's business? Do they have enough cash to make it another month, quarter, or year? You can ensure they do by educating them about the ERC and helping them get the cash infusion they need. Let's do our best to be that trusted strategic business advisor that gives them a chance to survive!

Rick Meyer, CPA, MBA, MST is a long-time member of the Illinois CPA Society.