MEMORANDUM

DATE: November 28, 2023
TO: All
FROM: Wendy J. Manson, CPA, and William J. Palazzolo, Esq.
RE: Employee retention credit temporary hold

On September 14, 2023, the Internal Revenue Service ("IRS") placed a temporary hold on its Employee Retention Credit ("ERC") review process through at least year-end 2023. In a press release, the IRS cited that the main reason for the temporary hold is that the IRS is concerned that many new ERC claims are ineligible and may even be fraudulent. During this moratorium, the IRS will review outstanding ERC claims more closely and take more time to review the claims before processing the credit. Also, any newly filed claims will not be processed until the temporary hold is lifted.

The IRS is placing a moratorium on new ERC claims because, over the past few years, many ERC mills have aggressively pushed small businesses to claim credits to which the small businesses may not be entitled. Specifically, the IRS has seen many improper ERC claims by companies citing eligibility for the ERC due to alleged supply chain issues.

If your business submitted a claim and has yet to receive an ERC refund, please note that the IRS still had 637,000 unprocessed ERC claims as of September 6, 2023. The IRS has been reviewing returns and approving credits at its own pace. While the IRS has stated that its review process typically takes four months, the review can and often does take longer and, in some cases, can take well over a year. With the stricter compliance reviews in place during the moratorium, existing ERC claims will go from a standard processing goal of 90 days to a goal of 180 days – and much longer if the claim faces further review or audit. The IRS may also seek additional documentation from the taxpayer to ensure it is a legitimate ERC claim.

The IRS noted that the enhanced compliance review of existing claims submitted before the moratorium is critical to protect against fraud, but also to protect small businesses from facing penalties or interest payments stemming from bad claims pushed by unscrupulous ERC promoters.

The IRS's moratorium on processing of new ERC claims through at least the end of 2023 will allow the IRS to add more safeguards to prevent future abuse and protect businesses from predatory tactics. Also, the IRS is working with the Justice Department to pursue fraud fueled by aggressive marketing for improper ERC claims.

For both 2020 and 2021 ERC claims, the employer must have experienced a significant decline in gross receipts. However, the significant decline in gross receipts is calculated differently for each year.

For 2020, a significant decline in gross receipts begins when gross receipts were less than 50% of gross receipts for the same calendar quarter in 2019. Employers with these claims have until the extended deadline of April 15, 2024, to file the claim for the 2020 year.

For the first, second and third quarters of 2021, a significant decline in gross receipts was a quarter where gross receipts were less than 80% of the same quarter in 2019, or alternatively, comparing the preceding quarter in 2021 to the same quarter in 2019 (i.e., to qualify for the second quarter of 2021, comparing the first quarter of 2021 to the second quarter in 2019). Employers with these claims have until April 15, 2025, to file the claim for the 2021 year.

For 2020, the percent of qualified wages paid that were eligible for the credit is 50% ($10,000 per employee including certain health care expenses) for qualified wages paid for the year. Thus, the maximum credit is $5,000 per employee for 2020.

For 2021, the percent of qualified wages paid that were eligible for the credit is 70% ($10,000 per employee per calendar quarter including certain health care expenses) for qualified wages paid between January 1 and September 30, 2021. Thus, the maximum credit is $7,000 per employee per quarter in 2021.

Qualified wages include the wages of the majority shareholder when there are no other employees with a family relationship to the majority shareholder. If any wages were paid to a family member, that would make the wages paid to a majority shareholder ineligible for the credit as well as the wages paid to the other family members. When the wages are qualified, they are treated the same way as wages paid to any other employee. Thus, limited to $10,000 per year in 2020 with a 50% credit, and limited to $10,000 per quarter in 2021 with a 70% credit per quarter.

Lastly, any wages used in qualifying for the Paycheck Protection Program ("PPP") forgiveness, cannot also be used as qualifying wages to calculate the ERC credit.