

# UNDERSTANDING THE EMPLOYEE RETENTION CREDIT



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# EMPLOYEE RETENTION CREDIT: THE BASICS

- Refundable credit against payroll taxes, claimed on Form 941 (or 941-X)
- Can claim credit if received PPP but can't use same wages for forgiveness and ERC
- Employers with significant decline in gross receipts OR subject to full or partial government shutdown qualify
- Eligible entities include private-sector businesses and tax-exempt (501(c)) employers that carry on a trade or business
- Note: all items based on current guidance as of 5/20/21

# EMPLOYEE RETENTION CREDIT: THE BASICS

2020	2021
\$10,000/per employee wage limit for YEAR	\$10,000/per employee wage limit per QUARTER
50% credit	70% credit
50% drop in receipts versus same quarter in 2019 to qualify (unless gov't shutdown)	20% drop in receipts versus same quarter in 2019 to qualify (unless gov't shutdown)
Small employer: 100 full-time employees or less in 2019	Small employer: 500 full-time employees or less in 2019
Wages paid in a qualified period after 3/12/2020 are eligible	Wages paid on any date during the qualified period are eligible

# CREDIT ELIGIBILITY



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# EMPLOYEE RETENTION CREDIT: THE BASICS

Eligible employers must fall into one of two categories to qualify for the credit:

**1. Employer has a significant decline in gross receipts.**

- **2020:** eligible once gross receipts are down 50% versus the same quarter in 2019 – continue to qualify until the quarter AFTER receipts are more than 80% versus the same quarter in 2019
- **2021:** eligible if gross receipts are down 20% or more versus same quarter in 2019

**2. Employer's business is fully or partially suspended by government order due to COVID-19 during the calendar quarter.**

- You will only be eligible for the period of time business was fully or partially suspended

➤ Aggregation rules apply when making these determinations



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# 2020 SIGNIFICANT DECLINE

## 2020 Significant Decline Example

Employer A's receipts were down 55% in Q2 of 2020 vs Q2 of 2019. Employer A qualifies for the credit in Q2.

Employer A's receipts were only down 15% in Q3 of 2020 vs Q3 of 2019. Employer A qualifies for the credit in Q3, but will NOT qualify in Q4 unless they again experience a 50% drop in receipts vs Q4 of 2019.

If instead Employer A's receipts were down 25% in Q3 of 2020 vs Q3 of 2019, Employer A would qualify for the credit in Q3 and in Q4, regardless of Q4 gross receipts.



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# 2021 SIGNIFICANT DECLINE

## 2021 Significant Decline Details

1. Can elect to base your eligibility on the previous quarter's decline in gross receipts  
i.e. I can determine my eligibility in Q1 of 2021 based on Q4 of 2020 vs Q4 of 2019  
**NOTE: at this time it does NOT appear that you are required to use this method in all future quarters once the election is made**
2. If an employer did not exist in the beginning of the same quarter in 2019, the same quarter in 2020 is substituted



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# FULL OR PARTIAL GOVERNMENT SHUTDOWN

- Shutdown due to Federal, State or Local Government order that limits commerce, travel, or group meetings due to COVID-19 *and* that order impacts operations, hours, etc.
  - Examples: order to shutdown non-essential businesses, government imposed curfews, local health department mandate to close for cleaning/disinfecting
  - Not eligible if employer voluntarily suspends operation or reduces hours

# **PARTIAL SHUTDOWN - FACTORS TO CONSIDER *MORE THAN A NOMINAL EFFECT***

1. Does the employer have adequate teleworking capabilities?
2. Is the employee's work portable? I.e. can it be done at home.
3. Does the employee need to be in the physical workspace? (i.e. laboratories)
4. Was there a delay in getting your employees set up properly to telework?
5. Did your hours decrease due to a curfew?
6. Did you decrease your open hours in order to do a deep clean to comply?
7. Did you need to limit occupancy to provide for social distancing?
8. Did you require that business be performed only by appointment (previously had walk-in capability)
9. Did you change your format of service?
10. Were you unable to procure supplies from your suppliers due to supplier shut downs or border shut downs?

# NOMINAL EFFECT SAFE HARBOR

10% or more decrease in the ability to provide goods and services in the normal course of the employer's business considered partially shut down by a government order.

Exceptions:

1. if your business only decreased because customers were not out. Must have some sort of factor directly related to a government order.
2. Requiring someone to wear a mask or gloves will not have a nominal effect.

# MULTIPLE LOCATIONS OR AGGREGATED GROUPS UNDER DIFFERENT GOV'T ORDERS

Multiple Locations - If some of the locations are partially shut down due to a government order AND the business has a policy that the other locations (not shut down) will comply with CDC or Homeland Security guidance, ALL locations will be considered partially shut down.

Aggregated Group – If a trade or business is operated by multiple members of an aggregated group, and if the operations of one member of the aggregated group are suspended due to a governmental order, then all members of the aggregated group are considered to be partially suspended.



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# CREDIT CALCULATION



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# CREDIT CALCULATION

- 2020 credit is 50% of “qualified wages” paid during qualified period
  - Up to \$10,000 qualified wages per employee for the year – max credit of \$5,000 per employee in 2020
- 2021 credit is 70% of “qualified wages” paid during qualified period
  - Up to \$10,000 per employee PER quarter in which you are eligible – max credit of \$7,000 per employee each eligible quarter in 2021



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# QUALIFIED WAGES

- Gross wages
- Employer contributions to health insurance
- Doesn't include wages used for PPP or any other credit (i.e. FFCRA)
- Doesn't include wages paid to FORMER employees (i.e. severance)
- Doesn't include wages paid to owners' family members
  - Owners and spouses themselves unclear
- Qualified wages limited if considered large employer

# SMALL VS LARGE EMPLOYERS

- If you are a **SMALL** employer, wages paid during eligible period qualify for credit regardless of whether the employee is able to work
  - 2020 Small Employer = 100 or fewer FULL TIME EMPLOYEES
  - 2021 Small Employer = 500 or fewer FULL TIME EMPLOYEES
- If **LARGE** employer, only wages paid to those who are NOT working qualify
- Aggregation rules apply when making this determination

# SMALL VS LARGE EMPLOYERS

- Full time employees
  - Based on **2019** employees
  - Employee averaging 30+ hours/week or 130+ hours/month is full-time
  - **NOT** an FTE calculation – those under 30 hours/week not included in count

# QUALIFIED WAGES – LARGE EMPLOYERS

1. Partial Day of work/paid full day - The amount of wage attributable to the not working is a qualifying wage. Even if the employee is working a partial day, the portion that is related to the not working will be considered a qualifying wage.
2. Payment of vacation, sick, PTO, or severance is **not** a qualifying wage for LARGE employers only
3. Health insurance paid while an employee is out on furlough or only partially working is a qualifying wage. If partially working, then you allocate the amount of health insurance to qualified and nonqualified wage.

# PLANNING FOR ERC



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# PPP V. ERC

1. Can't use the same wages for both. Be Creative! Employers are not locked into a specific week or a specific employee for either program.
2. If haven't applied for forgiveness, then do the applications together in order to maximize the benefits of both programs. Make sure that you maximize the non-payroll costs up to the 40% number on the PPP application.
3. If you have applied already, the payroll included in the PPP application is disallowed from the ERC to the extent that it is needed to compute the forgiveness amount.



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# PPP V. ERC EXAMPLES

## *ASSUME FULL FORGIVENESS*

1. Example #1 – Loan amount - \$100,000. Application – used \$100,000 of payroll only (not health or retirement or other expenses). Could have included other expenses but didn't. Can't use any of the payroll for ERC.
2. Example #2 – Loan amount - \$100,000. Application – used \$150,000 of payroll only. \$100,000 is disallowed, can use \$50,000 for ERC.
3. Example #3 – Loan amount - \$200,000. Application – used \$130,000 of payroll and \$70,000 of other expenses. \$130,000 is disallowed.
4. Example #4 – Loan amount - \$200,000. Application – used \$200,000 of payroll and \$70,000 of other expenses for a total of \$270,000. \$130,000 is disallowed and \$70,000 is allowed. \$130,000 is the minimum amount of payroll costs needed to get full forgiveness.
5. Example #5 – Loan amount - \$200,000. Application – used \$200,000 of payroll costs and \$90,000 of other expenses for a total of \$290,000. \$120,000 is disallowed and \$80,000 is allowed.  $\$200k * 60\%$  minimum. Go to the minimum payroll costs needed.



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# HOW TO MAXIMIZE THE ERC WITH PPP

1. Owners' relatives can't get ERC – Put all of their wages to PPP, subject to PPP limits.
2. Schedule C or Partners with Self Employment (debate is still out on the owner/employees) can't get ERC – Put all of their self employment to PPP, subject to PPP limits
3. Consider timing. If the shut down occurs in 2<sup>nd</sup> quarter, use all of the eligible 3<sup>rd</sup> and 4<sup>th</sup> quarter wages toward the PPP and use the 2<sup>nd</sup> quarter wages for the ERC.
4. Consider vacation/severance pay – may not be eligible for ERC so put toward PPP.

# INCOME TAX CONSEQUENCES

## Deductibility of wages:

- The amount of the credit reduces the total wage deduction, and thus reduces wages for other purposes, such as the R&D credit, or 199A
- NYS allows a subtraction modification to deduct the wages

# CLAIMING THE ERC



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# CLAIMING THE ERC

1. Form 941 (or 941-X if previous quarter)
2. No penalty imposed if don't pay in required social security taxes to the extent you qualify for ERC
  - i.e. if Employer A owes \$20,000 in social security taxes but knows they will qualify for \$12,000 in ERC credits in that quarter, they can choose to only pay in \$8,000 and will not face penalties for underpayment – will claim the \$12,000 credit on that quarter's Form 941
3. Form 7200 – Advance Payment of Employer Credits
  - i.e. if Employer A owes \$20,000 in social security taxes but knows they will qualify for a \$25,000 in ERC credits in that quarter, they can choose not to pay in the SS taxes and can file a form 7200 to collect the remaining \$5,000 in advance



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Employer identification number (EIN)

Name (not your trade name)

Trade name (if any)

Address

Number Street Suite or room number

City State ZIP code

Foreign country name Foreign province/county Foreign postal code

**Return You're Correcting...**

Check the type of return you're correcting.

941

941-SS

Check the ONE quarter you're correcting.

1: January, February, March

2: April, May, June

3: July, August, September

4: October, November, December

Enter the calendar year of the quarter you're correcting.

(YYYY)

Read the separate instructions before completing this form. Use this form to correct errors you made on Form 941 or 941-SS. Use a separate Form 941-X for each quarter that needs correction. Type or print within the boxes. You MUST complete all four pages. Don't attach this form to Form 941 or 941-SS unless you're reclassifying workers; see the instructions for line 36.

**Part 1: Select ONLY one process. See page 5 for additional guidance.**

1. **Adjusted employment tax return.** Check this box if you underreported amounts. Also check this box if you overreported amounts and you would like to use the adjustment process to correct the errors. You must check this box if you're correcting both underreported and overreported amounts on this form. The amount shown on line 27, if less than zero, may only be applied as a credit to your Form 941, Form 941-SS, or Form 944 for the tax period in which you're filing this form.
2. **Claim.** Check this box if you overreported amounts only and you would like to use the claim process to ask for a refund or abatement of the amount shown on line 27. Don't check this box if you're correcting ANY underreported amounts on this form.

**Enter the date you discovered errors.**

/  /

(MM / DD / YYYY)

**Part 2: Complete the certifications.**

3. **I certify that I've filed or will file Forms W-2, Wage and Tax Statement, or Forms W-2c, Corrected Wage and Tax Statement, as required.**

**Note:** If you're correcting underreported amounts only, go to Part 3 on page 2 and skip lines 4 and 5. If you're correcting overreported amounts, for purposes of the certifications on lines 4 and 5, Medicare tax doesn't include Additional Medicare Tax. Form 941-X can't be used to correct overreported amounts of Additional Medicare Tax unless the amounts weren't withheld from employee wages or an adjustment is being made for the current year.

4. **If you checked line 1 because you're adjusting overreported federal income tax, social security tax, Medicare tax, or Additional Medicare Tax, check all that apply.** You must check at least one box.

I certify that:

- a. I repaid or reimbursed each affected employee for the overcollected federal income tax or Additional Medicare Tax for the current year and the overcollected social security tax and Medicare tax for current and prior years. For adjustments of employee social security tax and Medicare tax overcollected in prior years, I have a written statement from each affected employee stating that he or she hasn't claimed (or the claim was rejected) and won't claim a refund or credit for the overcollection.
- b. The adjustments of social security tax and Medicare tax are for the employer's share only. I couldn't find the affected employees or each affected employee didn't give me a written statement that he or she hasn't claimed (or the claim was rejected) and won't claim a refund or credit for the overcollection.
- c. The adjustment is for federal income tax, social security tax, Medicare tax, or Additional Medicare Tax that I didn't withhold from employee wages.

5. **If you checked line 2 because you're claiming a refund or abatement of overreported federal income tax, social security tax, Medicare tax, or Additional Medicare Tax, check all that apply.** You must check at least one box.

I certify that:

- a. I repaid or reimbursed each affected employee for the overcollected social security tax and Medicare tax. For claims of employee social security tax and Medicare tax overcollected in prior years, I have a written statement from each affected employee stating that he or she hasn't claimed (or the claim was rejected) and won't claim a refund or credit for the overcollection.
- b. I have a written consent from each affected employee stating that I may file this claim for the employee's share of social security tax and Medicare tax. For refunds of employee social security tax and Medicare tax overcollected in prior years, I also have a written statement from each affected employee stating that he or she hasn't claimed (or the claim was rejected) and won't claim a refund or credit for the overcollection.
- c. The claim for social security tax and Medicare tax is for the employer's share only. I couldn't find the affected employees, or each affected employee didn't give me a written consent to file a claim for the employee's share of social security tax and Medicare tax, or each affected employee didn't give me a written statement that he or she hasn't claimed (or the claim was rejected) and won't claim a refund or credit for the overcollection.
- d. **The claim is for federal income tax, social security tax, Medicare tax, or Additional Medicare Tax that I didn't withhold from employee wages.**

Next ▶



**Part 3:** Enter the corrections for this quarter. If any line doesn't apply, leave it blank.

	Column 1 Total corrected amount (for ALL employees)	Column 2 Amount originally reported or as previously corrected (for ALL employees)	Column 3 Difference (If this amount is a negative number, use a minus sign.)	Column 4 Tax correction
6. Wages, tips, and other compensation (Form 941, line 2)				Use the amount in Column 1 when you prepare your Forms W-2 or Forms W-2c.
7. Federal income tax withheld from wages, tips, and other compensation (Form 941, line 3)				Copy Column 3 here ▶
8. Taxable social security wages (Form 941 or 941-SS, line 5a, Column 1)				$\times 0.124^* =$
9. Qualified sick leave wages (Form 941 or 941-SS, line 5a(i), Column 1)				$\times 0.062 =$
10. Qualified family leave wages (Form 941 or 941-SS, line 5a(ii), Column 1)				$\times 0.062 =$
11. Taxable social security tips (Form 941 or 941-SS, line 5b, Column 1)				$\times 0.124^* =$
12. Taxable Medicare wages & tips (Form 941 or 941-SS, line 5c, Column 1)				$\times 0.029^* =$
13. Taxable wages & tips subject to Additional Medicare Tax withholding (Form 941 or 941-SS, line 5d)				$\times 0.009^* =$
14. Section 3121(q) Notice and Demand—Tax due on unreported tips (Form 941 or 941-SS, line 5f)				Copy Column 3 here ▶
15. Tax adjustments (Form 941 or 941-SS, lines 7 through 9)				Copy Column 3 here ▶
16. Qualified small business payroll tax credit for increasing research activities (Form 941 or 941-SS, line 11a; you must attach Form 8974)				See instructions
17. Nonrefundable portion of credit for qualified sick and family leave wages (Form 941 or 941-SS, line 11b)				See instructions
18. Nonrefundable portion of employee retention credit (Form 941 or 941-SS, line 11c)	10,000 .	0 .	10,000 .	See instructions (10,000) .
19. Special addition to wages for federal income tax				See instructions
20. Special addition to wages for social security taxes				See instructions
21. Special addition to wages for Medicare taxes				See instructions
22. Special addition to wages for Additional Medicare Tax				See instructions
23. Combine the amounts on lines 7 through 22 of Column 4				(10,000) .
24. Deferred amount of social security tax* (Form 941 or 941-SS, line 13b)				See instructions
25. Refundable portion of credit for qualified sick and family leave wages (Form 941 or 941-SS, line 13c)				See instructions

\* Use this line to correct the employer deferral for the second quarter of 2020 and the employer and employee deferral for the third and fourth quarters of 2020.

Next ▶



Name (not your trade name)	Employer identification number (EIN)	Correcting quarter (1, 2, 3, 4)
		Correcting calendar year (YYYY)

**Part 3: Enter the corrections for this quarter. If any line doesn't apply, leave it blank. (continued)**

	Column 1 Total corrected amount (for ALL employees)	Column 2 Amount originally reported or as previously corrected (for ALL employees)	Column 3 Difference (if this amount is a negative number, use a minus sign.)	Column 4 Tax correction
26. Refundable portion of employee retention credit (Form 941 or 941-SS, line 13d)	40,000	0	40,000	(40,000)
27. Total. Combine the amounts on lines 23 through 26 of Column 4				(50,000)
<p><b>If line 27 is less than zero:</b></p> <ul style="list-style-type: none"> <li>If you checked line 1, this is the amount you want applied as a credit to your Form 941 or 941-SS for the tax period in which you're filing this form. (If you're currently filing a Form 944, Employer's ANNUAL Federal Tax Return, see the instructions.)</li> <li>If you checked line 2, this is the amount you want refunded or abated.</li> </ul> <p><b>If line 27 is more than zero, this is the amount you owe.</b> Pay this amount by the time you file this return. For information on how to pay, see Amount you owe in the instructions.</p>				
28. Qualified health plan expenses allocable to qualified sick leave wages (Form 941 or 941-SS, line 19)				
29. Qualified health plan expenses allocable to qualified family leave wages (Form 941 or 941-SS, line 20)				
30. Qualified wages for the employee retention credit (Form 941 or 941-SS, line 21)	95,000	0	95,000	
31. Qualified health plan expenses allocable to wages reported on Form 941 or 941-SS, line 21 (Form 941 or 941-SS, line 22)	5,000	0	5,000	
32. Credit from Form 5884-C, line 11, for this quarter (Form 941 or 941-SS, line 23)				
33a. Qualified wages paid March 13 through March 31, 2020, for the employee retention credit (use this line to correct only the second quarter of 2020) (Form 941 or 941-SS, line 24)				
33b. Deferred amount of the employee share of social security tax included on Form 941 or 941-SS, line 13b (use this line to correct only the third and fourth quarters of 2020) (Form 941 or 941-SS, line 24)				
34. Qualified health plan expenses allocable to wages reported on Form 941 or 941-SS, line 24 (use this line to correct only the second quarter of 2020) (Form 941 or 941-SS, line 25)				





**QUESTIONS?**



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# **RESOURCES**

**IRS FAQs** [HTTPS://WWW.IRS.GOV/NEWSROOM/FAQS-EMPLOYEE-RETENTION-CREDIT-UNDER-THE-CARES-ACT](https://www.irs.gov/newsroom/faqs-employee-retention-credit-under-the-cares-act)

**IRS NOTICE 2021-20** [HTTPS://WWW.IRS.GOV/PUB/IRS-DROP/N-21-20.PDF](https://www.irs.gov/pub/irs-drop/n-21-20.pdf)

**IRS NOTICE 2021-23** [HTTPS://WWW.IRS.GOV/PUB/IRS-DROP/N-21-23.PDF](https://www.irs.gov/pub/irs-drop/n-21-23.pdf)



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