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EMPLOYEE RETENTION TAX CREDIT (ERTC)

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Every Y should talk to their account/auditor/CFO, etc. about the potentially significant positive financial impact of the Employee Retention Tax Credit (ERTC) on their Y. Y-USA is awaiting additional guidance from the IRS on the ERTC and will disseminate it when it is released.

BACKGROUND

The ERTC was originally enacted under the Coronavirus Aid, Relief, and Economic Security (CARES) Act, and later expanded and extended to Q1 and Q2 of 2021 under the Consolidated Appropriations Act of 2020 (CAA) in December.

Additionally, a key change under the December law now allows those employers eligible for the Paycheck Protection Program (PPP) to also claim the ERTC, including retroactive 2020 claims for borrowers from the initial round of PPP who originally were ineligible. (Please note that the credit can only be taken on wages that are not forgiven or expected to be forgiven under PPP.)

The recent American Rescue Plan Act of 2021 (ARPA), enacted in March of 2021, also made some material changes to the ERTC. In response to the ongoing impact of the COVID-19 pandemic, eligible employers—including nonprofits—may now also be eligible to claim the expanded ERTC benefits on qualified wages through Dec. 31, 2021.

WHAT IS THE ERTC?

The ERTC is a vehicle designed to deliver cash relief to eligible employers. The mechanism to deliver the funds is done through a credit that can be claimed against a Y's "qualified wages" when filing quarterly payroll taxes. The credit is both "advanceable" (employers may request an advance in a given quarter) and "refundable" (any amount in excess of payroll taxes owed will be refunded).

ELIGIBILITY:

Shutdown/Reduction Orders "Or" Gross Receipts Reductions

Eligible Employers that are entitled to claim the ERTC are private-sector businesses and tax-exempt organizations that during calendar year 2020 and either:

- *Have operations that were fully or partially suspended due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) due to COVID-19;(See IRS FAQ link below for details).* ***Or***

- *Experienced a significant decline in gross receipts during the calendar quarter. (50% in a 2020 quarter compared to same quarter in 2019; only 20% to qualify for 2021 credits)*

Number of Employees*
The new law significantly expanded eligibility—based on number of employees in 2019—for full ERTC benefits.

- For full benefits in 2021 under the new law, a YMCA association can have up to **500 full-time employees in 2019** (According to IRS Notice 2021-49, the term "full-time employee" means an employee who, with respect to any calendar month in 2019, had an average of at least 30 hours of service per week or 130 hours of service in the month (130 hours of service in a month is treated as the monthly equivalent of at least 30 hours of service per week), as determined in accordance with section 4980H of the Code. See also Q/A-31 of Notice 2021-20 and section III.E. of Notice 2021-23. (Employers in 2021 with over 500 employees in 2019 may be eligible for ERTC on wages and/or health benefits paid to employees who were retained on the payroll but "were not providing services.")
- For **retroactive** 2020 full credit, you must be under 100 full-time employees in 2019. (Employers in 2020 with over 100 employees in 2019 may be eligible for ERTC on wages and/or health benefits paid to employees who were retained on the payroll but "were not providing services."

* *For purposes of determining whether an eligible employer is a large eligible employer or a small eligible employer, eligible employers are not required to include full-time equivalents when determining the average number of full-time employees. Please be aware that the employee calculation used for the PPP is not calculated the same way as this more favorable method of counting full-time employees for the ERTC noted above.*

VALUE OF ERTC**

Changes in the law also significantly increased the value through changes in the ERTC benefit formula.

- For wages paid after January 1, 2021, and before July 1, 2021, the ERTC can be applied to 70% of qualifying wages of up to $10,000 per quarter. **This means companies could receive a maximum of up to $14,000 per employee through June 30, 2021.**
- For wages paid after March 12, 2020, and before January 1, 2021, the ERTC can be applied to 50% of qualifying wages up to $10,000. **This means a maximum of $5,000 per employee could be credited back to your company if it qualifies for 2020.**

****** *For purposes of identifying qualified wages, an employee's status as a full-time employee is irrelevant and wages paid to an employee who is not full-time may be treated as qualified wages if all other requirements to treat the amounts as qualified wages are satisfied.*

Talk to your accounting saff/auditor/payroll firm, etc. about how to best leverage ERTC benefits for your Y. Please be aware of three key IRS Forms associated with the ERTC: the usual **Form 941** for filing quarterly payroll taxes, **Form 7200** to request and advance credit, and **Form 941-X** to file an amended report (used for the retroactive claims).

For more detailed guidance on the Employee Retention Credit for qualified wages paid during these dates:

- *After March 12, 2020 and before January 1, 2021* - Notice 2021-20 PDF
- *After December 31, 2020 and before July 1, 2021* - Notice 2021-23 PDF
- *After June 30, 2021 and before January 1, 2022* – Notice 2021-49 PDF

Note that IRS Notice 2021-20 specifies rules for retroactive 2020 ERTC claims for those who also had PPP. IRS Notice 2021-23 specifies rules regarding the expansion of the program for Q1 and Q2 of 2021. Notice 2021-49 addresses changes made by the American Rescue Plan Act of 2021 (ARP) to the employee retention credit that are applicable to the third and fourth quarters of 2021.

*Also see IRS ERTC FAQ page (note menu of topic links). **Please be aware that this site has an alert noting that it these FAQs do not reflect the changes made by the Taxpayer Certainty and Disaster Tax Relief Act of 2020 (Relief Act), enacted December 27, 2020, or the American Rescue Plan Act of 2021 (ARP Act), enacted March 11, 2021**, but it does have general information about the ERTC from 2020, much of which has been affirmed in the recent cited IRS Notices and may still be helpful.* https://www.irs.gov/newsroom/faqs-employee-retention-credit-under-the-cares-act

ERTC Eligibility	2020	2021
Business size	100 Full-time employees or less in 2019* (partial eligibility for over 100 - limited to those retained on payroll but "were not providing services."	500 Full-time employees or less in 2019*
Full or partial Shutdown	An employer whose operations are fully or partially suspended during a calendar quarter due to a governmental order may be entitled to the ERTC.	An employer whose operations are fully or partially suspended during a calendar quarter due to a governmental order may be entitled to the ERTC.
Revenue Loss**	>50% revenue loss, 2019 quarter vs. the same 2020 quarter	>20% revenue loss, 2019 quarter vs. the same 2021 quarter or Q4 2020 vs. Q4 2019 (for Q1 2021). **Also, <u>for any quarter in 2021</u>, according to recent IRS Notice 2021-23 and Notice 2021-49, you can use an "alternative" test by using the prior quarter comparison test for eligibility** (for example, for Q2, you can use Q2 of 2021 compared to Q2 of 2019 ***or*** Q1 of 2021 compared to Q1 of 2019)
Amount of Credit	50% of the first $10,000 of salary per employee for the year (a total of up to $5000 for 2020)	70% of the first $10,000 of salary per employee per quarter through June 30, 2021 (total of up to $7000 per quarter/$14,000 in 2021)
Am I Eligible If I Received PPP?	Yes; you can now retroactively apply for ERTC for 2020 if you received PPP. File an amended form 941 (941-X). Different wages must be used for ERTC and PPP (you can't "double dip")	Yes; Different wages must be used for PPP and ERTC (you can't "double dip")

Gross Receipts Test and Forgiven PPP Loans

The IRS released new guidance on August 10, 2021 that made a favorable ruling on how forgiven PPP loans impact the gross receipts test for ERTC eligibility. The new guidance Revenue Procedure 2021-33 *allows a "safe harbor" where an organization does not have to count PPP forgiven PPP loan amounts in the ERTC gross receipts eligibility test (see especially pages 9-11 in RP 2021-33). Initially, forgiven PPP funds may have counted toward gross receipts, depending on forgiveness of the PPP loan and the timing of forgiveness. Also, please note that if the PPP is not forgiven and remains a loan it does not affect the gross receipts test.*

Gross Receipts Test and ERTC Credits

Some Ys have been receiving conflicting information when asking their auditors if funds from surplus ERTC credits (amounts more than the payroll taxes owed) count toward the gross receipts test for subsequent ERTC eligibility? The answer is unclear at the time of this update: Crowe LLP, Y-USA's national tax consulting firm, recently held a panel discussion with various tax-exempt practitioners from around the country and this issue was raised. While some practitioners believe that the Q&A numbers 60 and 61 from IRS Notice 2021-20 (see below) support an argument that a tax-exempt organization does not have to count receipt of ERTC in the gross receipts test for determining eligibility for the "next quarter," other practitioners assert that the Q&As are not specific to exempt organizations which must rely on the definition of "gross receipts" under section 6033. It is unclear whether the IRS will be issuing clarification on this issue for exempt organizations; however, an effort is underway to urge the IRS to clarify the issue with a favorable ruling.

> ***<u>IRS Notice 2021-20, p. 92:</u>***
> ***Question 60****: Does the employee retention credit reduce the expenses that an eligible employer could otherwise deduct on its federal income tax return?*
> ***Answer 60:*** *Yes. Section 2301(e) of the CARES Act provides that rules similar to section 280C(a) of the Code shall apply for purposes of applying the employee retention credit. Section 280C(a) generally disallows a deduction for the portion of wages or salaries paid or incurred equal to the sum of certain credits determined for the taxable year. Accordingly, a similar deduction disallowance applies under section 2301(e) of the CARES Act with regard*

to the employee retention credit, such that an employer's deduction for qualified wages, including qualified health plan expenses, is reduced by the amount of the employee retention credit. (An employer does not, however, reduce its deduction for the employer's share of social security and Medicare taxes by any portion of the credit).

Question 61*: Does an eligible employer receiving an employee retention credit for qualified wages need to include any portion of the credit in income?*
Answer 61*: No. An employer receiving a tax credit for qualified wages, including allocable qualified health plan expenses, does not include the credit in gross income for federal income tax purposes. Neither the portion of the credit that reduces the employer's applicable employment taxes, nor the refundable portion of the credit, is included in the employer's gross income.*

ERTC Claims and Other Federal Pass-through Grants
The American Rescue Plan Act of 2021 only specifically mentions coordination of the ERTC with PPP loans, grants under the Economic Aid to Hard-Hit Small Businesses, Non-Profits and Venues Act, and restaurant revitalization grants. As noted above, ERTC cannot be applied to any funds that were used as qualified wages for any First or Second Draw PPP loans, or any of these other noted relief programs. There is no specific language in the ERTC guidance excluding the use of other federal pass-through grants common to YMCAs, although it is certainly possible that state or local governments may include a "no double dip" provision in their pass-through contracts; therefore, each agreement should be reviewed to determine whether claiming the ERTC on wages paid from funding under the grant is prohibited. Some claim that wages paid with another grant with no prohibitions is acceptable given the grant is paying for a service (as opposed to the clearly excluded funds like PPP that are purely relief that provides revenue without an expected service/cost to the organization), but, again, this should be discussed with your auditor to ensure there are no prohibitions or conflicting language in the pass-through contracts.

Please note that any of the information in this document should be vetted by each of the Y organizations counsel and tax advisors as it is subject to interpretation and organizational books and records. Also, be aware further changes may be made due to legislative action from Congress and/or rulemaking decisions by the IRS.

Updated as of 8/20/2021