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## The Employee Retention Credit and Nonprofit Organizations

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## Agenda

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- Introduction
- Changes made by the Consolidated Appropriations Act
- Conceptual Framework and The Two Questions
- Eligible Employers: Significant Decline in Gross Receipts
- Eligible Employers: Full or Partial Suspension of Services
- Qualified Wages: Determining Average Number of Employees
- Qualified Wages: Determining Whether an Employee is Not Providing Services
- Claiming the Credit
- Examples and Explanations

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## Employee Retention Credit: The Act

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In the case of an **eligible employer**, there shall be allowed **as a credit against applicable employment taxes** for **each calendar quarter** an **amount equal to 50 percent** of the **qualified wages** with respect to **each employee of such employer** for such calendar quarter.

Section 2301(a)

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## Employee Retention Credit

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- Section 2301 of the Coronavirus Aid, Relief, and Economic Security (CARES) Act
- Meant to act as an incentive for distressed employers to maintain high levels of pre-pandemic employment
- Created a **refundable** payroll tax credit claimed against the employer's portion of the Social Security and Medicare taxes
- Up to \$5,000 for each employee who is paid up to \$10,000 of qualified wages on the payroll (50% credit)
- Changes made by the Consolidated Appropriations Act (CAA) in December 2020, as well as potential changes in latest House Bill

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## Employee Retention Credit

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- 2021 Consolidated Appropriations Act (CAA) extended the CARES Act program through the first two quarters of 2021
- Some changes only apply to Q1 and Q2 of 2021; major retroactive change for those who received PPP loans in 2020
- [IRS FAQ website](#) and IRS [Notice 2021-20](#) (released on March 1)
  - FAQs do not yet reflect impact of the CAA
  - Notice is for 2020 quarters; Notice for 2021 quarters is forthcoming
- Congress has not elected to include ministerial wages in the definition of qualified wages
  - Therefore, ministerial wages are not eligible for the employee retention credit
- Student employees' wages which are otherwise exempt from FICA **are** included

## Employee Retention Credit

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- PPP Loan Recipients: Organizations that received PPP loan proceeds in 2020 may now claim the credit for 2020 quarters
- **May not** claim the credit for wages that were paid for with PPP loan proceeds and forgiven
- **May** claim the credit for wages that were not paid with PPP loan proceeds and forgiven
- **May** claim the credit retroactively

## Employee Retention Credit CAA Changes

2020	2021
Qualified wages (up to \$10,000) paid after March 12, 2020 and before January 1, 2021	Qualified wages (up to \$10,000) paid after March 12, 2020 and before July 1, 2021
Had a full or partial suspension of services caused by a COVID-19 governmental order during the period, <i>or</i>  50% decline in gross receipts from the same quarter in 2019	<b>Beginning January 1, 2021:</b> Had a full or partial suspension of services caused by a COVID-19 governmental order during the period, <i>or</i> <b>20%</b> decline in gross receipts from the same quarter in 2019
100 or fewer full-time employees: eligible for the credit for every employee, regardless of whether they were able to work or not during the period	<b>500</b> or fewer full-time employees: eligible for the credit for every employee, regardless of whether they were able to work or not during the period
100 or more full-time employees: eligible for the credit for only those employees who were not able to provide services during the period	<b>500</b> or more full-time employees: eligible for the credit for only those employees who were not able to provide services during the period
Credit is 50% of qualified wages, with an annual cap of \$5,000	<b>Credit is 70% of qualified wages, with a <u>quarterly</u> cap of \$7,000</b>

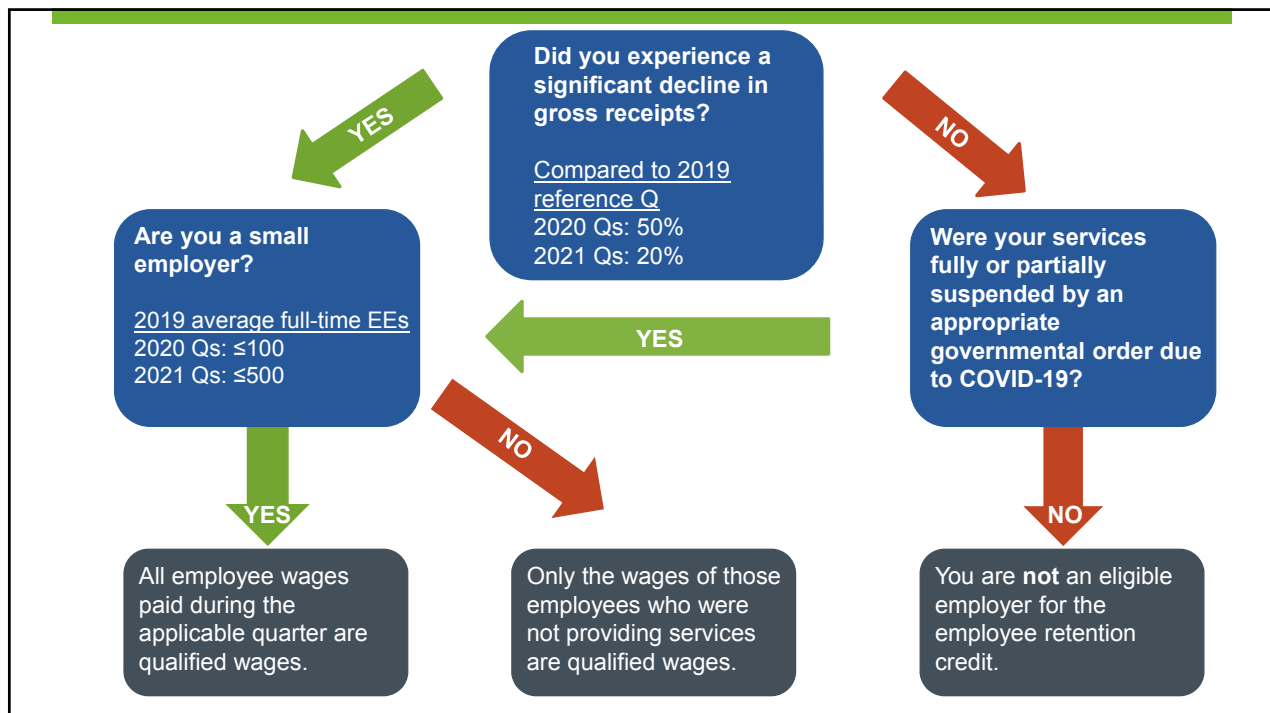
## Employee Retention Credit CAA Changes

2020	2021
Credit is 50% of qualified wages, with an annual cap of \$5,000  <i>e.g. \$10,000 in qualified wages * 50% for the entirety of 2020</i>	Credit is 70% of qualified wages, with a quarterly cap of \$7,000  <i>e.g. \$10,000 in qualified wages * 70% in Q1 \$10,000 in qualified wages * 70% in Q2</i>
<b>Total Credit for 2020:</b> \$5,000 for entire year	<b>Total Credit for 2021:</b> \$14,000 for Q1 and Q2 of 2021  <ul style="list-style-type: none"> <li>Can claim the 2021 credit even if received the maximum credit for the employee in 2020</li> </ul>

## Proposed Changes in House Bill

- \$1.9 trillion bill passed by the full House along (almost) strictly party lines on Saturday, February 27, 2021
- Contemplates extending the ERC through the end of 2021
- Faces a tough road in the Senate, but will most likely pass after minimum wage hike was eliminated
- Many hoping to pass before March 14, the expiration date of unemployment provisions

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## Employee Retention Credit

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Two salient questions:

- 1) Are you an “eligible employer”?
- 2) Did you pay any “qualified wages”?

## Eligible Employer Question

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Eligible employers are those who are able to demonstrate either:

- 1) A **significant decline in gross receipts**; or
- 2) A **full or partial suspension of services** due to orders from an appropriate governmental authority related to COVID-19

## Significant Decline in Gross Receipts

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- **For 2020 quarters:** the employer experienced more than a 50% decline in gross receipts from the reference calendar quarter in 2019

Nonprofits are told that gross receipts are those within the meaning of Internal Revenue Code 6033, without reduction for costs or expenses

[Q/A 25](#)

- **For 2021 quarters:** the employer experienced more than a 20% decline in gross receipts from the reference calendar quarter in 2019

## Significant Decline in Gross Receipts

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- **For 2021 quarters:** If not in existence in 2019, then the employer can substitute the same calendar quarter in 2020
- Alternatively, can use the immediately preceding calendar quarter
- If you answered “yes” to this eligibility pathway, then you move to the “qualified wages” questions
- Note: This does not appear to be a popular eligibility path



## Full or Partial Suspension of Services

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- What does “fully or partially suspended during the calendar quarter due to orders from an appropriate governmental authority... due to COVID-19” mean?
- Three questions here:
  1. Was there an “appropriate” governmental order?
  2. Was there a “full or partial suspension” of services?
  3. Was the suspension caused by the order?

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## Full or Partial Suspension of Services

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### 1. Was there an appropriate governmental order? [FAQ 28](#)

- Orders, proclamations, decrees from federal government
  - Same from state or local government
- That **limit** commerce, travel, or group meetings **due to** COVID-19 that **affects an employer’s operation** of its trade or business
- Statements at press conferences not enough
- States of emergency also not enough

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## Full or Partial Suspension of Services

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### 2. Was there a full or partial suspension of services?

- **Comparability:** Were you able to continue operations in a “comparable” manner even after the suspension?
  - What elements are lost due to the restrictions?
  - Were folks teleworking prior to the restrictions?
  - Were services widely available for live-streaming prior to the restrictions?
  - [See FAQ 33](#)
- **Modification:** What programs, elements, or portions of ministry have been modified, to the point that it has “more than a nominal effect on the business operations”?
  - [See FAQ 34](#)

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## Full or Partial Suspension of Services

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- Factors for determining **comparability** (non-exhaustive list)
  - [Question/Answer \(Q/A\) 16](#)
  - Employer’s telework capabilities
  - Portability of employee’s work
  - Need for presence in employee’s physical work space
    - Is it “so critical to its trade or business operations that tasks central to the trade or business’s operations are unable to be performed remotely”?
  - Transitioning to telework operations

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## Full or Partial Suspension of Services

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- Factors for determining **modification of services** that are allowed to remain open (non-exhaustive list) [Q/A 17,18](#)
  - Modification must be ordered as a precondition of reopening a physical space for business or service to the public
    - E.g., limiting occupancy for social distancing; requiring services on appointment-only basis; changing the format of a service; requiring employees and customers to wear face coverings
  - Mere fact of precondition is not enough; must also have more than nominal effect on business operations
  - “A governmental order that results in a reduction in an employer’s ability to provide goods or services in the normal course of the employer’s business of not less than 10 percent will be deemed to have more than a nominal effect on the employer’s business operations.”
    - Occupancy restriction at restaurant vs. occupancy restriction at big-box retailer
    - Face-covering orders for employees/customers not enough

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## Full or Partial Suspension of Services

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- Essential businesses that have other nonessential services?
  - “An employer that operates an essential business may be considered to have a partial suspension of operations if... more than a nominal portion of its business operations are suspended by a governmental order.” [Q/A 11](#)
    - More than nominal if either (i) gross receipts from that portion is not less than 10% of total gross receipts (use 2019 numbers), or (ii) hours of service by employees in that portion is not less than 10% of total number of hours performed by all employees
- Unable to get supplies?
  - May be able to demonstrate full or partial suspension if unable to “obtain critical goods or materials from suppliers because they were required to suspend operations” [Q/A 12](#)

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## Full or Partial Suspension of Services

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- Shutdown due to lack of demand?
  - This is not enough [Q/A 13](#)
- Multiple sites?
  - If only some of the sites are under a governmental order leading to full or partial suspension, that will be a partial suspension of services for the entire organization [Q/A 20](#)

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## Full or Partial Suspension of Services

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### **3. Was the full or partial suspension caused by the order?**

- The order must actually affect your operations
- The suspension must not have been due to causes other than the COVID-19 order
- The order must be one that limited commerce, travel, or gatherings
- Voluntary closures do not qualify. [FAQ 29](#)
- If people customers/service recipients stop coming, that does not qualify. [FAQ 32](#)

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## Decision Tree on Full or Partial Suspension

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- **First:** Were your overall services fully suspended by the order?
- **Second:** If not, were your overall services partially suspended by the order?
- **Third:** If not, were there departments, service offerings, or programs that were fully suspended by the order?
- **Fourth:** If not, were there departments, services offerings, or programs that were partially suspended by the order?
- **And fifth:** Was the full or partial suspension caused by the order?
  - Not voluntary and not due to some other cause
- Use the Comparability and Modification questions at each stage

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## Qualified Wages

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- This requires you to examine two things:
  1. **First**, are you a “small” employer for the purposes of claiming the credit?
  2. **If not**, do you have any employees who were (a) paid and (b) were “not providing services” during the applicable quarter(s)?

## Calculating the Average Number of Employees

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- See [FAQ 49](#), [Q/A 31](#)
- Use 2019 numbers
- “Full-time employee” is defined as an employee who had an average of 30 hours of service per week or 130 hours of service per month
- Calculate the sum of full-time employees for each month, add them all together, then divide by 12
- If your organization began operations in the middle of 2019, divide the total number by the applicable number of months in 2019 that you were in existence
  - Same idea applies if you started in 2020

## Calculating the Average Number of Employees

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- **For 2020 quarters:** If you have more than 100 full-time employees on average in 2019, then only “wages paid to employees... for the time they are not providing services during a calendar quarter in which the... business operations are fully or partially suspended” are qualified wages. [FAQ 52](#)

If **less than** 100 full-time employees, then you “may treat all wages paid to [your] employees... as qualified wages” [FAQ 51](#)
- **For 2021 quarters:** The number changes to more than 500 full-time employees on average in 2019

## What does “not providing services” mean?

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- What about wages paid to employees who performed work different from their normal job?

**FAQ 52:** No, that is not sufficient. In an example, a restaurant was ordered to shut down indoor dining, but was allowed to carry on take-out and drive-thru services. Wages to workers who were repurposed to those tasks were not qualified wages.

- What about wages paid to hourly or non-exempt workers who may not have a set schedule of work?

**FAQ 54, Q/A 36:** Perhaps. You would need to use a “reasonable method” for determining the hours that are not being worked. You may **not** determine that hours have been reduced based on assessment of the employee’s productivity level.

## What does “not providing services” mean?

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- What about wages paid to employees who are exempt salaried employees?

**FAQ 55, Q/A 37:** Perhaps. Again, an employer may use “any reasonable method to determine the number of hours that a salaried employee is not providing services,” **except** for the productivity levels assessment.

The example provided references a fitness club business, all of whose sites have been closed. Their managerial staff continues to be paid their respective salaries, but they only perform some admin and accounting functions. The employer demonstrated through time records that they were only performing 10% of their typical work hours.

## What does “not providing services” mean?

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- Bottom line: If you are not a small employer, then you should have documentation that demonstrates the drop in services provided by **each employee whose wages you will argue are qualified wages**

## Claiming the Credit

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- **For 2021 quarters (prospective application)**
  - [Form 941](#) (Employer’s Quarterly Federal Tax Return)
    - Should reduce the deposit by the amount of the credit
    - Then, if applicable, may claim advance payment through Form 7200
  - [Form 7200](#) (Advance Payment of Employer Credits Due to COVID-19)
    - For small employers
    - For use if applying for 2021 quarters
    - Could be a delay – stopped processing payments from late December through January 21, 2021
    - Letter 6312 (delay due to mistake) or letter 6313 (delay due to address verification)



## Claiming the Credit

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- **For 2020 quarters (retrospective application)**
  - [Form 941-X](#) (Adjusted Employer's Quarterly Federal Tax Return)
  - May use this method for sick leave and family leave credits as well
  - Speak to your payroll provider

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## Interaction with PPP Loan Forgiveness

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- May **not** claim as ERC qualified wages amounts that were included in the payroll costs reported on the PPP loan forgiveness application up to (but not exceeding) the **minimum amount of payroll costs, together with any other eligible expenses reported on the forgiveness application**, sufficient to support the amount forgiven. [Q/A 49](#)
- Remember: employers needed to hit the 60% payroll costs threshold to achieve full forgiveness

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## Interaction with PPP Loan Forgiveness

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- **Example 1:** Employer receives PPP loan of \$100,000 and had \$100,000 in qualified wages for the ERC
  - They were required to report a total of \$100,000 of payroll costs + other eligible expenses (at least \$60,000 in payroll costs)
  - They reported \$100,000 in payroll costs to support forgiveness
  - **Result:** They may not take \$100,000 of the qualified wages into account

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## Interaction with PPP Loan Forgiveness

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- **Example 2:** Employer receives PPP loan of \$200,000 and reports \$200,000 of payroll costs **as well as** \$70,000 of other eligible expenses in support of forgiveness application
  - **Result:** They may not take \$130,000 of qualified wages into account for the ERC
- **Example 3:** Same as above, except they report \$200,000 of payroll costs **as well as** \$90,000 of other eligible expenses
  - **Result:** They may not take into account \$120,000 of qualified wages into account
- Remember the 60% payroll costs forgiveness threshold

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## Interaction with PPP Loan Forgiveness

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- This guidance will be detrimental to those organizations that only provided payroll costs to substantiate forgiveness
- If you would like to comment on this or other provisions of the Notice, you should contact Ms. Dixie Pond and/or Mr. Danchai Mekadenaumporn, Office of the Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes), at 202-317-6798

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## Substantiation Requirements

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- [Q/A 70](#)
- Documentation to show that you are an eligible employer
  - Governmental order
  - Records relied upon to demonstrate more than nominal portion of business was suspended
  - Records demonstrating significant decline in gross receipts, payment of qualified wages, and (for large employers) work records and documentation showing that wages were paid for time an employee was not providing services
- Form(s) 941, 941-X, 7200

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## Example 1: Church

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- First Congregational Church of Chattanooga (FCCC) is wondering if it is eligible to claim the ERC. It has not experienced a significant decline in gross receipts. The governor of Tennessee did institute a COVID-19-related series of orders, one of which related to capacity limitations in gathering spaces.
- However, the governor did say that the order did not apply to religious organizations. FCCC, in the name of loving their neighbor, decided to abide by the guidelines anyway. Is this a suspension due to a governmental order?
- **Answer:** No. Voluntary choice. See [FAQ 29](#).

## Example 1: Church

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- Same facts as before. However, in this case the order applies to churches but exempts them from whatever penalties they would have otherwise faced. Is this a suspension due to a governmental order?
- **Answer:** Maybe. [FAQ 28](#) notes that the governmental order qualifies the employer “without regard to the level of enforcement.”
- **FYI:** Examine the orders. Worship gatherings may be exempted by the order, but what about other elements? Youth groups? Sports leagues? Child care? Food bank?

## Example 2: Nonprofit

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- Central Detroit Food Bank (CDFB) had more than an average of 100 employees during 2019. They did, however, experience a partial suspension of services due to a Michigan governor's order in 2020. In this case, CDFB had to send home much of its workforce to comply with the governor's orders on occupancy. CDFB did not have a "Zoom-friendly" culture before the order. They are unable to do much of the work that they used to. Is the suspension due to the order?
- **Answer:** Most likely. If they can demonstrate the work the employees do is not "comparable" to the pre-order days, and/or they had to make more than nominal "modifications," then it should qualify. See [FAQ 33 and 34](#).

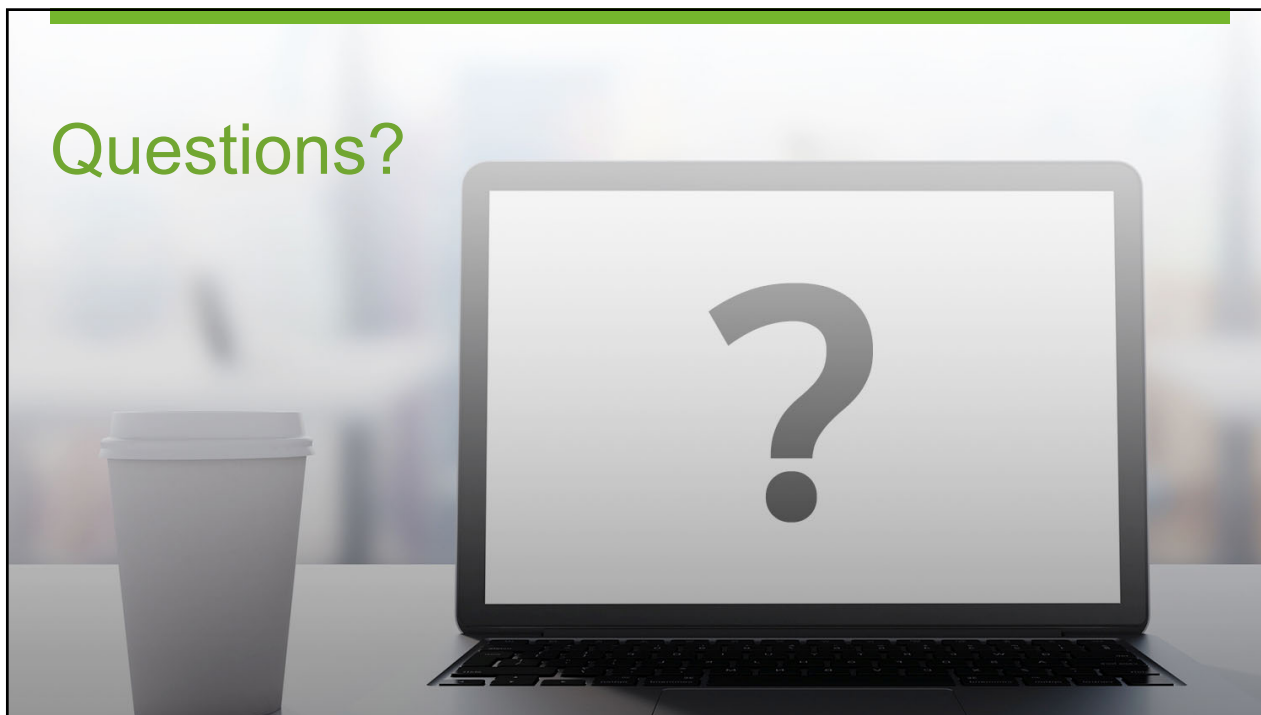
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## Example 2: Nonprofit

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- Same facts as above. There were very few folks coming to the food bank during Q1 – Q2 of 2020, so many employees were repurposed to other activities in the organization where they weren't nearly as productive (think: *Undercover Boss*). Are wages paid to them qualified wages?
- **Answer:** No. CDFB should analyze the duties of the employees and how much actual downtime they had. See [FAQ 54 and 55](#).

# Questions?



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