

Expansion and Changes to the Employee Retention Credit – Posted January 18, 2021

Welcome News for Businesses with PPP Loans

The new stimulus package signed into law in late December brings billions more in aid to American businesses. Among the provisions of the nearly 5700-page law: an extension of the Employee Retention Credit (ERC), which is designed to support businesses that keep employees on payroll during the pandemic. The ERC has been extended through June of 2021 and is now available to businesses with Paycheck Protection Program (PPP) loans.

What is ERC and how does it work?

The ERC is a refundable payroll tax credit that was included in the CARES Act of 2020 with the intent to keep employees on staff throughout the Covid-19 pandemic. For the period March 12, 2020 through year-end, businesses that met one of two tests could claim a credit of up to \$5,000 of wages paid per employee. The eligibility tests were either:

- 1) At least 50% reduction in gross receipts for any quarter in 2020 as compared to the same quarter in 2019 or
- 2) Full or partial business closure due to a government shutdown in any quarter in 2020

One major note from the CARES Act: Employers that applied for a forgivable Payroll Protection Program (PPP) loan through the SBA were *not* eligible for the ERC.

Now let's fast-forward to the impact of the Consolidated Appropriations Act, 2021. Under Act Section 206, **businesses can now receive both forgivable PPP loans and remain eligible for ERC**. This appears to be retroactive back to March 2020, but there are some unknowns. Here are some things we *do* know about changes to the ERC:

- The same wages cannot be used to qualify for both PPP forgiveness and Employee Retention Credits
- If utilizing both the PPP and ERC, employers are supposed to treat wages as qualified for ERC purposes before PPP loan forgiveness

So, what do those employers do who have already filed for PPP round one forgiveness? We will have to keep apprised for guidance on this nuance, as it likely affects many businesses.

Some more welcome news for businesses Under Act Section 207: the ERC is now extended through June 30, 2021. The first eligibility test related to the 2021 credits has been eased to only a 20% reduction in gross receipts. Note, this is still in reference to a quarter-over-quarter comparison to 2019 gross receipts. Employers are now eligible for a credit of up to 70% employee wages rather than the 50% eligibility that remains for 2020 credits, and rather than limiting wages per employee to \$10,000 per year, this limit is applied per quarter in 2021. This equates to a maximum of \$14,000 in credits per employee for 2021 as compared to the 2020 cap of \$5,000 per employee.

The last major benefit for 2021 ERC calculations is the increase on allowable company size when determining qualified wages. For 2020, employers with 100 or fewer employees could include all wages paid to employees towards this credit.

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For 2021, this limit is adjusted to 500 or fewer. Keep in mind, employers with more than 500 employees may still be eligible for a credit; their definition of qualified wages is just limited.

It is important to acknowledge the impact of both PPP and ERC being made available for businesses. Here's a very simple example of how a company may benefit from both during 2021:

Company A, a manufacturer, has 60 employees, each earning a \$50,000 annual salary. Company A meets the gross receipts test for Q1 & Q2 2021 for ERC and for a second round of PPP funding, receiving in January 2021.

The ERC calculation should be addressed first, as wages are qualified for this credit prior to PPP forgiveness eligibility.

Company A's 2021 ERC would be:

$70\% \times \$10,000 \text{ qualified wages} \times 60 \text{ employees} \times 2 \text{ eligible quarters} = \$840,000 \text{ ERC}$

Company A also received PPP round two funding of \$605,000. The \$1,200,000 wages (\$10,000 per employee x 60 employees x 2 quarters) used to calculate the Employee Retention Credits cannot be included in wages paid for Company A's PPP forgiveness application. This means the ERC may limit PPP forgiveness.

Company A will likely spend over \$1.3M in wages over their 24-week PPP forgiveness period, meaning only the wages in excess of \$1.2M will be eligible for PPP forgiveness purposes. Since PPP loans must be at least 60% spent on payroll, you may have to pay back a portion of the loan.

Moral of the story: Many businesses who qualify for PPP and ERC can benefit from both, so don't overlook ERC available to you. Just keep in mind the credits you may receive when filing your 941's could limit your total PPP forgiveness.

In Summary

Overall, the 2020 and 2021 ERC changes are positive for employers and their employees. Businesses just have to keep in mind the computational changes are only effective for the first half of 2021 and forward. There's still a lot to learn and interpret as we apply these changes in practice in the coming months. I would encourage you to stay in close contact with your GJM tax advisory team as you make decisions for your business in the days and weeks to come. You can also find further resources in the [GJM online Covid-19 Resource Center](#).



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