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CARES Act Employee Retention Tax Credit Guide for Employers

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The Coronavirus Aid, Relief, and Economic Security (CARES) Act provides access to a tax credit for employers whose businesses have been impacted by COVID-19. Referred to as the Employee Retention Tax Credit (ERTC), the credit is available to businesses that either have had to partially or fully suspend their business operations in 2020 or have had a significant decline in gross receipts as compared with 2019. This guide outlines the general provisions in CARES regarding the ERTC tax credit, explains how businesses can claim the credit, sets out the limitations of using the ERTC when other relief has been claimed, and summarizes the seven pieces of ERTC guidance that have been released to date, all in a question and answer format.

For more information on any of these provisions, contact any of the Brownstein National Tax Policy Group attorneys listed on the last page.

As of May 8th, 2020, the following guidance has been provided:

- IRS FAQ
- IRS Notice 2020-22 (Relief from Penalty for Failure to Deposit Employment Taxes)
- IRS News Release IR-2020-62
- Department of Treasury Fact Sheet
- Department of Treasury Press Release
- U.S. Senate Committee on Finance FAQ
- JCT Description of Tax Provisions in CARES Act - Page 30
- IRS Coronavirus Tax Relief Homepage

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I. General Rules of the Employee Retention Tax Credit (ERTC)

A. What is the amount of the ERTC?

The CARES Act provides a refundable tax credit, capped at $5,000 per employee, for 50% of qualified wages up to $10,000 paid to employees from March 13, 2020, through Dec. 31, 2020.

> **Example:** Employer pays $10,000 in qualified wages to Employee A in Q2 2020. The ERTC available to Employer for the qualified wages paid to Employee A is $5,000.
>
> **Example:** Employer pays Employee B $8,000 in qualified wages in Q2 2020 and $8,000 in qualified wages in Q3 2020. The credit available to Employer for the qualified wages paid to Employee B is equal to $4,000 in Q2 and $1,000 in Q3 due to the overall limit of $10,000 on qualified wages per employee for all calendar quarters.

B. Who is eligible?

Traditionally, employee retention credits have been available to businesses that were inoperable as a result of damage caused by a natural disaster (e.g., floods, hurricanes, fires) to encourage employers to keep employees on their payroll. Employee retention credits have also been available to businesses that continued to employ uniformed service members when such service members were called up to active duty (e.g., Heroes Earnings Assistance and Relief Tax Act of 2008, Pub. L. No. 110-245).

As COVID-19 is unique from past situations, the eligibility for this credit has shifted from damaged/inoperable businesses and continued employment of active duty service members, to any employer carrying on a trade or business during calendar year 2020, which (i) was partially or fully suspended due to COVID-19 orders from an appropriate governmental authority, or (ii) experienced a significant decline in gross receipts.

In addition to affected trades and businesses, organizations exempt from tax under section 501(c) are eligible, but (1) government and state entities and political subdivisions thereof and (2) businesses that receive a forgivable Paycheck Protection Program loan are not. Self-employed individuals are also not eligible with respect to their own self-employment earnings (but may still receive the credit for their employees). We note that the Internal Revenue Service (IRS) has indicated it will provide additional guidance related to the nuanced question of whether a business is eligible for the retention credit if the business has *applied* for a Paycheck Protection Program loan but has *not* yet received a loan under that program.

C. What "orders from an appropriate governmental authority" may be taken into account for purposes of the credits?

Orders from the federal government, or any state or local government with jurisdiction over an employer, are counted if they limit commerce, travel or group meetings due to COVID-19 in a way that affects an employer's operation of its trade or business (e.g., hours of operation).

However, statements from a governmental official do not rise to the level of a governmental order for purposes of the Employee Retention Credit. Additionally, a declaration of a state of emergency is not sufficient to rise to the level of a governmental order if it does not limit commerce, travel, or group meetings in any manner. Further, such a declaration that limits commerce, travel, or group meetings, but does so in a manner that does not affect the employer's operation of its trade or business, does not rise to the level of a governmental order.

> **Example:** A state governor issues an order that all non-essential businesses must close from March 20, 2020 until April 30, 2020. The order provides a list of non-essential businesses. Employers that provide essential services may remain open. The governor's order is a governmental order limiting the operations

of non-essential businesses, entitling employers with non-essential businesses to claim the Employee Retention Credit for qualified wages.

D. What constitutes fully or partially suspended operations?

The IRS's guidance provides that the operation of a business may be suspended if an appropriate governmental authority imposes restrictions upon the business operations by limiting commerce, travel, or group meetings (for commercial, social, religious or other purposes) due to COVID-19, such that the operation can still continue but not in all of its typical operations. For employers that operate in multiple jurisdictions, as well as for aggregated groups treated as a single employer, an order requiring the suspension of operations in one location is considered a suspension for all locations, regardless of whether such locations are subject to COVID-19 orders, and such employers, for purposes of operating the business in a consistent manner in all jurisdictions, can establish business operations policies that comply with local government orders, Center for Disease Control and Prevention (CDC) recommendations, and Department of Homeland Security (DHS) guidance to suspend its operations in certain jurisdictions.

However, if a government order causes customers of an essential business to stay home, that is not enough for the essential business to be considered partially suspended, but such an essential business may qualify for the credit if it has a significant decline in gross receipts. Further, if a COVID-19 order requires a business to close its workplace, but the business is still able to continue comparable operations by having its employees work online from home, such a business is not considered to have suspended operations.

> **Example:** A state governor issues an order closing all restaurants in the state in order to reduce the spread of COVID-19. However, the order allows the restaurants to continue food sales to the public on a carry-out, drive-through or delivery basis. This results in a partial suspension of the operations of the trade or business due to an order of an appropriate governmental authority with respect to any restaurants in the state that provided full sit-down service, a dining room or other on-site eating facilities for customers prior to the order.
>
> **Example**: Employer operates an auto parts manufacturing business that is considered essential under a governor's stay at home order. Employer's supplier of raw materials, however, is not essential and is required to shut down its operations due to the order. Employer is now unable to procure these raw materials from an alternate supplier, and therefore not able to perform its typical operations. Under these facts and circumstances, Employer would be considered an Eligible Employer because its operations have been suspended as a result of the governmental order that suspended operations of its supplier.
>
> **Example:** Employer, an automobile repair business, is an essential business and is not required to close its locations or suspend its operations. Due to a governmental order that requires people to stay at home except for certain essential travel, Employer's business has declined significantly. Employer is not considered to have a full or partial suspension of operations due to a governmental order.

E. What is a significant decline in gross receipts?

A significant decline in gross receipts means (i) any calendar quarter beginning Jan. 1, 2020, for which gross receipts are less than 50% of gross receipts for the same calendar quarter in 2019, and (ii) ending with the calendar quarter following the first calendar quarter beginning after a calendar quarter described in clause (i) for which gross receipts of such employer are greater than 80% of gross receipts for the same calendar quarter in the prior year. An employer does not need to establish that a significant decline in gross receipts is related to COVID-19 in order to be entitled to the retention credit based on a significant decline in gross receipts.

Example:

	2020 Gross Receipts	2019 Gross Receipts	% of Prior Year
Q1	$100,000	$210,000	48%
Q2	$190,000	$230,000	83%
Q3	$230,000	$250,000	92%

Using the above table, the Employer had a significant decline in gross receipts commencing on Jan. 1, 2020 (the calendar quarter in which gross receipts were less than 50% of the same quarter in 2019), and ending on July 1, 2020 (the quarter following the quarter for which the gross receipts were more than 80% of the same quarter in 2019). Thus, the Employer is entitled to a retention credit with respect to the first and second calendar quarters of 2020.

The IRS indicated that it will issue future guidance on how to determine whether a tax-exempt organization has had significant decline in gross receipts.

While an employer does not need to prove a significant decline in gross receipts is related to COVID-19, the IRS guidance provides that employers should retain records for the relevant calendar quarters in 2019 and 2020 to document that a significant decline in gross receipts occurred. Such records should be kept for at least four years for IRS review. We recommend that such documentation be created contemporaneously when the analysis is performed.

F. How are significant declines in gross receipts determined for new or acquired businesses?

Guidance issued by the IRS on April 30, 2020 provides specific rules for how businesses started or that acquire a business in 2019 should determine whether the business has a significant decline in gross receipts.

Business:	**Gross Receipts to Compare:**
Started Q1 2019	Compare 2019 quarters with applicable 2020 quarters
Started Q2 2019	Compare 2019 Q2 with Q1 and Q2 of 2020 Compare 2019 Q3 with Q3 of 2020 Compare 2019 Q4 with Q4 of 2020
Started Q3 2019	Compare 2019 Q3 with Q1, Q2 and Q3 of 2020 Compare 2019 Q4 with Q4 of 2020
Started Q4 2019	Compare 2019 Q4 with Q1, Q2, Q3 and Q4 of 2020
Started middle of any quarter	Estimate gross receipts the business would have had for that entire quarter based on the gross receipts for the portion of the quarter in operation, then apply the above cells in this table.
Acquired in 2020	An employer who acquires a business in 2020 may use a safe harbor method allowing the acquirer to include such business's 2019 gross receipts to determine whether there is a significant decline in gross receipts of the acquirer, but use of the safe harbor requires the acquirer to estimate the gross receipt that the acquirer would have had from the business for the entire calendar quarter in which the business was acquired.

G. What are qualified wages?

Greater Than 100 Employees. For businesses with an average of over 100 full-time equivalent employees during 2019, qualified wages means wages paid to an employee for the time the employee is not providing services when (1) the business is suspended for government orders related to COVID-19, or (2) there is a significant decline in gross receipts. Note, if an employee is performing services on a reduced schedule, wages paid to that

employee are treated as qualified wages only to the extent that those wages exceed what the employee would have otherwise been paid for the services performed; however, for these businesses, qualified wages for an employee may not exceed the amount such employee would have been paid for working an equivalent duration during the 30 days immediately prior to the period during which the business was suspended or experienced a significant decline in gross receipts, as applicable. The term "qualified wages" does not include required paid sick leave or required paid family leave under the FFCRA, or any wages for paid time off for vacations, holidays, sick days, and other days off pursuant to existing leave policies that represent benefits accrued during a prior period, but does include qualified health plan expenses properly allocated to the qualified wages.

100 or Fewer Employees. For businesses with an average of 100 or less full-time equivalent employees during 2019, qualified wages means all wages paid to an employee (whether or not providing services) when (1) the business is suspended under COVID-19 government orders, or (2) there is a significant decline in gross receipts. The term "qualified wages" includes include qualified health plan expenses properly allocated to the qualified wages and wages for paid time off for vacations, holidays, sick days, and other days off pursuant to existing leave policies, other than required paid sick leave or required paid family leave under the FFCRA.

The term "full-time employee" means an employee who, with respect to any calendar month in 2019, worked an average of at least 30 hours per week or 130 hours in the month, as determined in accordance with section 4980 of the Internal Revenue Code ("Code"). For purposes of determining the number of full-time employees, employers are treated as a single employer if they are aggregated as a controlled group of corporations under Code Section 52(a) or are partnerships, trusts, or sole proprietorships under common control under Code Section 52(b), or are entities aggregated under the Code Sections 414(m) or (o) (related to affiliated service groups).

Example: Pursuant to a state order, all restaurants in the state are required to close in order to reduce the spread of COVID-19. However, the order allows restaurants to continue food sales to the public on a carry-out, drive-through or delivery basis. To comply with the state order, Employee A typically works inside a restaurant as a manager, but has since been required to work from home remotely. Assuming that there are no sick leave, required paid family leave wages paid, will wages paid to Employee A be qualified wages? If Employee A (who is now required to work from home) receives 100% of his wages, but has his hours cut so that he is only working 75% of the time, does that change anything?

- If Employee A's restaurant averaged more than 100 full-time equivalent employees in 2019, wage payments to Employee A will not count as qualified wages, as he is still providing services. However, if Employee A's hours are reduced by 25% while his wages remain the same, 25% of the wages paid to Employee A will be considered qualified wages eligible toward the credit because Employee A is receiving 25% of his wages for not performing services while the restaurant's operations are partially suspended.

- If Employee A's restaurant averages 100 or less full-time equivalent employees in 2019, wage payments to Employee A would count as qualified wages, regardless of whether he is providing services, as the restaurant's operations are partially suspended due to COVID-19 orders. Reducing Employee A's hours does not affect the ability of the restaurant to take the credit.

Example: Pursuant to a state order, an employer is required to limit its store hours. In response, the employer reduces the hours its employees work. However, to incentivize the employees to continue working, the employer not only pays everyone 100% of their ordinary wages, but also increase s pay by $1 per hour. What is the outcome?

- If the business averaged more than 100 full-time equivalent employees in 2019, only the amounts paid to employees for time when they are not providing services, and at the rate of pay in effect prior to the increase, would be considered qualified wages.

- If the business averages 100 or less full-time equivalent employees in 2019, all amounts paid would be qualified wages.

There are also restrictions that prohibit (1) employee wages from being eligible for the credit if the employer is allowed a Work Opportunity Tax Credit with respect to the employee, (2) any wages taken into account for the credit being used to determine the Employer Credit for Paid Family and Medical Leave, (3) any severance payments to former employees from being included as qualified wages, (4) any wages paid to related individuals, as defined by section 51(i)(1) of the Code, from being included as qualified wages, and (5) wages exempt from the definition of wages under Code Section 3121(a) (wages for FICA tax purposes), other than qualified health plan expenses allocable to qualified wages.

Documentation. While the CARES Act does not prescribe any particular form of documentation, taxpayers should develop a system to gather and maintain records of the following information:

- Documentation to show how the taxpayer figured the amount of the ERTC for an individual employee or group of similarly- situated employees;
- Documentation to show how the taxpayer figured the amount of qualified plan expenses that you allocated to wages; and
- Documentation to show the taxpayer's eligibility for the ERTC based on suspension of operations or a significant decline in gross receipts.

As mentioned above, the IRS has specifically stated that certain documentation must be available for IRS review for at least four years.

H. What are qualified health plan expenses?

Qualified health plan expenses are employer and pre-tax employee amounts paid or incurred by an eligible employer to provide and maintain a group health plan (as defined in §5000(b)(1) of the Code), but only to the extent such amounts are excluded from the employee's gross income by §106(a) of the Code.

Since qualified health plan expenses also increase the qualified sick and family leave credits under the FFCRA, such expenses must be properly allocated (so there is no double benefit) between qualified sick leave wages, qualified family leave wages, and qualified wages for purposes of the retention credit. In other words, qualified health plan expenses that are allocable to qualified sick and family leave wages cannot be used for purposes of determining the retention credit.

For purposes of the retention credit, qualified health plan expenses need to be allocated to the qualified wages. The IRS has provided guidance on how to determine the amount of the qualified health plan expenses and how those expenses can be allocated among employees, depending on whether the plan is fully-insured, self-insured, or a health reimbursement arrangement (HRA) or a flexible spending arrangement (health FSA) (for example, the average premium for all employees covered by a policy) and pro rata on the basis of period of coverage (relative to the time periods to which such wages relate). Where an employer maintains more than one type of plan, qualified health plan expenses are determined on a plan-by-plan basis.

> **Example:** An Employer sponsors a group health plan that covers 200 employees. Each employee is expected to work 250 days per year (five days a week for 50 weeks). The Employer and pre-tax employee amounts paid for the 200 employees are $2 million. The average for all employees covered by the plan is $2 million divided by 200, or $10,000. For each employee expected to work 250 days a year, this results in a daily rate equal to $40.
>
> That $40 is the amount of qualified health plan expenses, per employee, that can be allocated to each day of (1) paid sick leave, (2) paid family leave, and (3) qualified retention wages.

I. Are qualified health plan expenses included as qualified retention wages even if no other wages are paid?

The April 23 JCT pronouncement states that the secretary has authority to treat qualified health plan expenses as qualified wages in a situation where no other qualified wages are paid by the employer. However, in the IRS guidance released on April 29th, an employer may treat no portion of the health plan expenses as qualified wages for purposes of the ERTC because no portion of the health plan expenses would be allocable to wages paid to employees, but the IRS indicated that an employer could pay reduced wages to employees (for not providing services if over 100 average employees), and then allocate qualified health plan expenses to the qualified wages. On May 8th, the IRS released revised guidance that employers can treat health plan expenses as qualified wages even if no other wages are paid for the time they are not working.

> **Example:** Employer is subject to a governmental order that fully suspends the operations of its business. Employer furloughs its employees but continues to pay 25% of normal wages. Employer continues to cover 100 percent of the employees' health plan expenses. In this case, Employer may treat as qualified wages: (i) the 25% of wages that it pays its employees, plus (ii) the 100% of the health plan expenses that are allocable to the time that the employees are not providing services.
>
> **Example:** Employer Z averaged 100 or fewer employees in 2019. Employer Z is subject to a governmental order that suspends the operation of its trade or business. In response to the governmental order, Employer Z lays off or furloughs all of its employees. It does not pay wages to its employees for the time they are laid off or furloughed and not working, but it continues the employees' health care coverage. Employer Z's health plan expenses allocable to the period its operations were partially suspended may be treated as qualified wages for purposes of the Employee Retention Credit.
>
> **Example:** Employer C is subject to a governmental order that fully suspends the operations of its trade or business. Employer C lays off or furloughs its employees and does not pay wages to the employees, but does continue to cover 100 percent of the employees' health plan expenses. In this case, Employer C may treat as qualified wages the health plan expenses that are allocable to the time that the employees are not providing services

J. Which employers are aggregated and treated as a single employer for purposes of the credits?

All entities treated as a single employer under section 52(a) or (b) of the Code, or section 414(m) or (o) (related to affiliated service groups) of the Code, are treated as a single employer for purposes of:

- Determining whether the employer has a trade or business operation that was fully or partially suspended due to COVID-19 orders from an appropriate governmental entity;
- Determining whether the employer has a significant decline in gross receipts;
- Determining whether the employer has more than 100 full-time employees; and
- Determining the application of rules that preclude an employer from claiming the ERTC if any member of the aggregated group receives a Paycheck Protection Program loan.

Importantly, since an employer is not entitled to the retention credit if the employer has a Paycheck Protection Program loan, it is important for an employer to understand whether it is part of a group of entities that is treated as a single employer and whether *any* member of that group has received a Paycheck Protection Program loan.

II. Administration of the ERTC

K. How are the credits refundable?

Pursuant to the text of the statute, the CARES Act provides that the credit is allowed against the employer's share of (1) old-age, survivors, and disability insurance (OASDI) taxes, and (2) Social Security and hospital insurance (Medicare) portions under the Railroad Retirement Tax Act (after taking into account any credits allowed for the employment of qualified veterans and for research expenditures of a qualified small business as well as the credits allowed for required paid sick or family leave under the FFCRA, and further reduced by the credits for (i) employment of qualified veterans, (ii) research expenditures of a qualified small business, and (iii) qualified sick and family leave under the FFCRA). To the extent that the retention credit for a calendar quarter exceeds the employer's share of the old-age, survivors, and disability insurance (OASDI) taxes for that quarter (or Social Security and hospital insurance (Medicare) portions under the Railroad Retirement Tax Act), the excess is refundable to the employer.

Through Notice 2020-22, FAQs, and the instructions to Form 7200 (Advance Payment of Employer Credits Due to COVID-19), the IRS provided guidance that amounts that are withheld by an employer from employees' wages for (1) the employees' share of OASDI taxes, (2) the employees' share of Medicare, and (3) federal income taxes as well as the employer's share of hospital insurance (Medicare) taxes that are required to be deposited can be retained by the employee as an advance payment of the refundable portion of the retention credit, provided that, to the extent such amounts exceed the refundable portion of the retention credit, the excess amount ,must be timely deposited by the employer in order to avoid any late deposit penalties.

The credit will be applied to offset any remaining tax liability on the employment tax return payable by the employer and the amount of any remaining excess retention credit will be reflected as an overpayment on the return. The overpayment will be subject to offset under section 6402(a) of the Code prior to being refunded to the employer. Notably, during any applicable calendar quarter, the employer can file for an advance payment of any remaining refundable portion of the retention credit by filing IRS Form 7200 (Advance Payment of Employer Credits Due to COVID-19), and multiple Form 7200s can be filed during any applicable calendar quarter (for example, after each payroll period).

> **Example:** Employer pays $10,000 in qualified wages to Employee A in Q2 2020, with the resulting tax obligations set forth in the below table:
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> | | |
> |---|---|
> | ER Share OASDI | $620 |
> | EE Share OASDI | $620 |
> | ER Share HI | $145 |
> | EE Share HI | $145 |
> | EE Fed Income Tax WH | $1,470 |
> | **Total** | **$3,000** |
>
> In this case, if Employee A was the only employee, Employer would not send in any of these taxes. The ERTC available to Employer for the qualified wages paid to Employee A is $5,000. This amount may be applied against the employer share of Social Security taxes that Employer is liable for with respect to all employee wages paid in Q2 2020 (the $620), leaving a refundable retention credit of $4,380. The employer can retain the employer's share of FICA taxes and the FICA and federal income taxes withheld from the employee's wages that otherwise would be required to be deposited as an advance payment of the refundable retention credit ($2,280 = 620 + 145 + 145 + 1,470), leaving a refundable credit of $2,000, for which the employer can request advance payment by filing the IRS Form 7200.

L. Can eligible employers claim the credit for qualified wages paid in March 2020?

Yes, an eligible employer can claim the credit for qualified wages paid as early as March 13, 2020. Credits claimed for March may be claimed on Form 941 (or other applicable employment tax return) for the second quarter of 2020 or through a request for advance payment on Form 7200.

M. How does an employer claim the credit?

Employers will report their total qualified wages and the related credits for each calendar quarter on their federal employment tax returns, usually quarterly on Form 941 (though §6302 of the Code generally requires deposits of employment taxes to be made on a monthly or biweekly basis).

Form 941 is used to report income and Social Security and Medicare taxes withheld by the employer from employee wages, as well as the employer's portion of Social Security and Medicare tax.

In anticipation of receiving the credits, employers can fund the credits in advance with federal employment taxes, including taxes withheld from employees' wages that are required to be deposited with the IRS or by requesting an advance of the credit from the IRS on Form 7200.

Practical Note: Employers could stop depositing employment taxes to the extent they can claim a retention credit that exceeds the amount of the payroll and federal income taxes required to be deposited.

N. How do I receive my credit?

Employers can be immediately reimbursed for the credit by reducing their required deposits of employment taxes that are required to be deposited, including employment and federal income taxes withheld from the employees' wages up to the amount of the retention credit.

Eligible employers will report their total qualified wages and the related health insurance costs for each quarter on their (quarterly) employment tax returns beginning in the second quarter. If the employer's employment tax deposits are not sufficient to cover the credit, the employer may receive an advance payment from the IRS by submitting Form 7200, Advance Payment of Employer Credits Due to COVID-19.

O. With respect to the ERTC, what is Form 7200 and how does it work?

Form 7200, Advance Payment of Employer Credits Due to COVID-19, is used to request an advance payment of the ERTC that a taxpayer will claim on its quarterly (or annual) federal payroll tax return.

When employers pay their employees, they are required to withhold federal income taxes and the employees' share of Social Security and Medicare taxes. Employers are required to deposit those taxes, along with the employer's share of Social Security and Medicare taxes, with the IRS and file employment tax returns (Forms 941, 943, 944 or CT-1, as applicable).

The employment taxes available for the credit are the employer's share of (1) old-age, survivors, and disability insurance (OASDI) taxes, and (2) Social Security and hospital insurance (Medicare) portions under the Railroad Retirement Tax Act (after taking into account any credits allowed for the employment of qualified veterans and for research expenditures of a qualified small business as well as the credits allowed for required paid sick or family leave under the FFCRA, and further reduced by the credits for (i) employment of qualified veterans, (ii) research expenditures of a qualified small business, and (iii) qualified sick and family leave under the FFCRA). To the extent that the retention credit exceeds those taxes, it is refundable to the employer and the employer can reduce its required payroll tax deposits as an advance payment of the refundable portion of the retention credit. If there remains a refundable portion of the retention credit after payroll tax deposits are reduced, the employer can request an advance payment of that remaining refundable retention credit by filing the Form 7200; however, no employer is required to file Form 7200. Instead of filing Form 7200, an employer can wait to get a refund when the employer claims its credits on the employment tax return. Please note, employers should not reduce

their deposits and request advance credit payments for the same expected credit. Employers will need to reconcile any advance credit payments and reduced deposits on their employment tax returns filed for 2020.

> **Example:** If an employer is entitled to an ERTC of $5,000 and is otherwise required to deposit $8,000 in employment taxes, the employer could reduce its federal employment tax deposits by $5,000. The employer would be required to deposit only the remaining $3,000 on the applicable required deposit date.
>
> **Example:** If an employer is entitled to an ERTC of $10,000 and was required to deposit $8,000 in employment taxes, the employer could retain the entire $8,000 of taxes as an advance payment of the refundable tax credit to which it is entitled and file a request for an advance payment for the remaining $2,000 using Form 7200.

P. How does an employer report qualified wages paid in Q1?

For employers that paid qualified wages between March 13, 2020, and March 31, 2020, such employers will include those wages together with the qualified wages paid during the second quarter of 2020 on their second quarter Form 941 to claim the ERTC. Do not include the credit on your first quarter Form 941 for 2020.

Q. With respect to the ERTC, when can an employer file Form 7200?

The ERTC for qualified wages applies to those wages paid between March 13, 2020, and Dec. 31, 2020.

An employer can file Form 7200 for an advance payment of the credits anticipated for a quarter at any time before the end of the month following the quarter in which it paid the qualified wages.

If necessary, an employer can file Form 7200 several times during each quarter. However, an employer should not file Form 7200 after it files Form 941 for the fourth quarter of 2020, and should not file Form 7200 to request an advance payment for any anticipated credit for which that employer has already reduced deposits.

R. How do I fill out Part II of Form 7200?

Line 1. Enter 50% of the amount of the qualified wages you paid to your employees so far in the current quarter. If you paid any qualified wages between March 13, 2020, and March 31, 2020, include 50% of those wages together with 50% of any qualified wages paid during the second quarter for the second-quarter total to enter on line 1.

Qualified wages don't include wages included on line 2 or line 3 for a credit for paid sick or paid family leave. Finally, you can't include wages paid to employees for whom you will take a work opportunity tax credit during this quarter.

Line 2. Enter the qualified sick leave wages you paid so far in the current quarter.

Line 3. Enter the qualified family leave wages you paid so far in the current quarter.

Line 4. Add lines 1, 2 and 3 and enter the result on line 4.

Line 5. Enter the amount by which you have already reduced your federal employment tax deposits for the credit for qualified leave wages (and certain health expenses and the employer's share of Medicare tax on the qualified leave wages) and the ERTC for this quarter.

Line 6. Enter the amount of any advances that you applied for on previous filings of this form for this quarter.

Line 7. Add lines 5 and 6 and enter the result on line 7.

Line 8. Subtract line 7 from line 4 and enter the amount on line 8. If the amount is zero or less, don't file this form; you're not eligible to receive an advance. You will need to report the amount of the advance that you request on your employment tax return for the return period, as well as the amounts that you requested on line 8.

The amounts entered on lines 1, 2, 3, 5 and 6 are cumulative totals for the quarter.

Example:

- Employer files Form 7200 on April 24, 2020, because it has a $7,000 ERTC to report on line 1 and reduced deposits of $4,000 (line 5).
- Employer also previously filed a Form 7200 on April 10, 2020, that reported $5,000 on line 1 and reduced deposits of $3,500 on line 5.
- The Form 7200 filed on April 24, 2020, will report $12,000 on line 1, $7,500 on line 5, and $1,500 on line 6 (5,000 – 3,500 advance from Form 7200 filed April 10).
- The advance payment requested (line 8) on April 24 is $3,000 (line 4–line 7).

S. May an employer reduce its federal employment tax deposit by the qualified wages that it has paid without incurring a failure to deposit penalty?

Yes, an eligible employer will not be subject to a penalty under section 6656 of the Code for failing to deposit federal employment taxes relating to qualified wages in a calendar quarter if:

- the employer paid qualified wages to its employees in the calendar quarter before the required deposit;
- the amount of federal employment taxes that the employer does not timely deposit, reduced by any amount of federal employment taxes not deposited in anticipation of the paid sick or family leave credits claimed under the FFCRA, is less than or equal to the amount of the employer's anticipated ERTC for the qualified wages for the calendar quarter as of the time of the required deposit; and
- the employer did not seek payment of an advance credit by filing Form 7200, Advance Payment of Employer Credits Due to COVID-19, with respect to any portion of the anticipated credits it relied upon to reduce its deposits.

The point of these rules is that an employer cannot retain taxes that it would otherwise be required to deposit as an advance payment of the refundable portion of the retention credit *and* file a Form 7200 for an advance payment of the same refundable retention credit.

T. Can an employer paying qualified wages fund its payments of qualified wages before receiving the credits by reducing its federal employment tax deposits?

Pursuant to Notice 2020-22, an eligible employer may fund qualified wages by accessing federal employment tax deposits. An eligible employer that pays qualified wages to its employees in a calendar quarter before it is required to deposit federal employment taxes with the IRS for that quarter may reduce the amount of federal employment taxes it deposits for that quarter by half of the amount of the qualified wages paid in that calendar quarter (up to the retention credit amount). The eligible employer must account for the reduction in deposits on the Form 941, Employer's Quarterly Federal Tax Return, for the quarter.

Example: Employer paid $10,000 in qualified wages (including qualified health plan expenses) and is therefore entitled to a $5,000 retention credit, and is otherwise required to deposit $8,000 in federal employment taxes for wage payments made during the same quarter as the $10,000 in qualified wages. Employer has no paid sick or family leave credits under the FFCRA. Employer may keep up to $5,000 of the $8,000 of taxes Employer was going to deposit, and it will not owe a penalty for keeping the $5,000.

Employer is required to deposit only the remaining $3,000 on its required deposit date. Employer will later account for the $5,000 it retained when it files Form 941, Employer's Quarterly Federal Tax Return, for the quarter.

III. Interaction of the ERTC with Other Provisions

U. May an employer receive both the tax credits for the qualified leave wages under the FFCRA and the ERTC under the CARES Act?

Yes, but not for the same wages. The amount of qualified wages for which an eligible employer may claim the ERTC does not include the amount of qualified sick and family leave wages for which the employer received tax credits under the FFCRA. This is because the FFCRA credits are refundable against employment taxes as well, and a double benefit is not permitted.

Example: Employer reports its employment tax liability quarterly on Form 941, Employer's QUARTERLY Federal Tax Return. Employer is not required to make any deposits or payments with respect to its employment tax liability except at the end of each quarter when it files Form 941.

Employer sponsors a group health plan that covers 200 employees. Each employee is expected to work 250 days per year (five days a week for 50 weeks). The Employer and pre-tax employee amounts paid for the 200 employees are $1 million. The average for all employees covered by the plan is $1 million divided by 200, or $5,000. For each employee expected to work 250 days a year, this results in a daily rate equal to $20. This is the amount of qualified health plan expenses that can be allocated to each day of paid sick leave, paid family leave, and qualified retention wages.

In Q2 2020, Employer pays $10,000 of wages to Employee, of which, $2,000 are for 30 days of qualified wages for purposes of the employee retention credit, $1,000 are for 3 days paid sick leave, and $200 are for 1 day of paid family leave. The three days of paid sick leave and one day of paid family leave overlapped with four of the 30 days where qualified retention wages were paid.

Qualified health plan expenses can be allocated amongst the employee retention credit, paid sick leave credit, and paid family leave credit:

- $2,000 + $600 qualified health plan expenses = $2,600 qualified retention wages
- $1,000 + $60 qualified health plan expenses = $1,060 paid sick leave wages
- $200 + $20 qualified health plan expenses = $220 paid family leave wages

While Employer can receive tax credits for qualified leave wages under the FFCRA and qualified retention wages under the CARES Act, it cannot be for the same wages. Thus, the $2,600 qualified retention wages are reduced by the $1,060 paid sick leave wages and $220 paid family leave wages.

Employer will then have an anticipated $1,060 paid sick leave credit, $220 paid family leave credit, and $660 retention tax credit ($1,320 qualified retention wages divided by two).

Generally, the $10,000 of wages paid to Employee in Q2 2020 would result in the following tax obligations for Employer:

ER Share OASDI	$620
EE Share OASDI	$620
ER Share HI	$145
EE Share HI	$145
EE Fed Income Tax WH	$1,470

Total	**$3,000**

However, paid sick leave wages and paid family leave wages (plus allocable qualified health plan expenses) are not subject to the employer share of OASDI on such wages, so the tax obligations for Employer would actually be:

ER Share OASDI	~~$620~~ $540.64 ($8,720 x 0.062)
EE Share OASDI	$620
ER Share HI	$145
EE Share HI	$145
EE Fed Income Tax WH	$1,470
Total	**~~$3,000~~ $2920.64**

Pursuant to Section 2302 of the CARES Act, Employer is not required to deposit its share of OASDI at the end of Q2 when it files Form 941. Instead, Employer is permitted to defer paying 50% of the $540.64 until December 31, 2021, and the remaining 50% until December 31, 2022.

With respect to the remaining $2,380 of employment tax liability, Notice 2020-22 allows Employer to reduce such liability by the $1,060 paid sick leave wages and $220 paid family leave wages. Employer would then reduce the remaining $1,100 employment tax liability by the $660 employee retention credit leaving a $440 liability, due and to be paid when Employer files its Q2 Form 941.

The IRS has released guidance that Form 941 will be revised for Q2 2020 to instruct employers how to reflect the deferred deposits and payments otherwise due.

In the example above, Employer still has to pay an amount when filing its Form 941. However, if Employer instead had enough paid sick leave wages, paid family leave wages, and qualified retention wages to cover the Q2 employment tax liabilities, it could retain the entire $2,920.64 of employment taxes as a portion of the refundable credit to which it is entitled, and file a request for an advance payment for the remaining amounts using Form 7200, Advance Payment of Employer Credits Due to COVID-19.

V. How does the ERTC interact with the deferral of payroll taxes (Section 2302 of CARES Act) and the Paycheck Protection Program loans (Section 1102 of CARES Act)?

Section 2302 of the CARES Act provides that the payment and deposit of an employer's share of the Social Security portion of FICA tax and the employer's share of the Social Security portion of the Railroad Retirement Tax Act for deposits that are due to be made from March 27, 2020, through Dec. 31, 2020, is not due before Dec. 31, 2021 (for the first 50% of the liability), and Dec. 31, 2022 (for the remaining 50% of the liability).

A taxpayer who receives a loan under the Paycheck Protection Program described in Section 1102 of the CARES Act is not eligible for the ERTC, unless the loan is paid back by May 14, 2020. However, unless and until a taxpayer is approved for a Paycheck Protection Program loan, it can claim the ERTC (subject to future guidance from the IRS regarding whether an application for a Paycheck Protection Program loan precludes an employer from being eligible for the ERTC). If a taxpayer claims the ERTC and later receives a Paycheck Protection Program loan, the taxpayer must cease claiming the ERTC on such date (not on the date of Paycheck Protection Program loan forgiveness), and the ERTC taken prior to receiving the Paycheck Protection Program loan will be recaptured, again subject to future IRS guidance.

W. Will there be additional guidance forthcoming?

Additional guidance is expected is expected with respect to qualified health plan expenses that are paid under a variety of different plans.

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