The Coronavirus Aid, Relief and Economic Security (CARES) Act

Frequently Asked Questions (FAQ)
Regarding the Employee Retention Credit (ERC)

The Coronavirus Aid, Relief, and Economic Security (CARES) Act, which was signed into law on March 27, 2020, contains over $2 trillion for economic stimulus, including cash payments to individuals, expanded unemployment benefits, retirement distributions, payroll tax deferrals and tax credits, corporate relief, and economic support for the healthcare industry in order to combat the COVID-19 crisis. Included in the Act is an employee retention credit for employers impacted by the COVID-19 crisis.

1 What Is the Employee Retention Credit included in the CARES Act?

Section 2301 of the CARES Act provides that an eligible employer can claim a credit against applicable employment taxes for employees retained during the COVID-19 crisis.

2 How much is the credit?

The credit is 50% of qualified wages paid during the calendar quarter. The total amount of qualified wages (including allocable qualified health plan expenses) for all calendar quarters is limited to $10,000, with a maximum credit value of up to $5,000 per employee.

3 What is the effective date of the credit?

The credit applies to wages paid after March 12, 2020, and before January 1, 2021.

4 What are "applicable employment taxes"?

In short, "applicable employment taxes" is the employer's share of Social Security taxes on wages paid to an employee, determined without regard to the contribution and benefit base.

5 What if the credit exceeds the amount of applicable employment taxes?

The excess tax credits are refundable. The CARES Act states that if the amount of the employee retention credit for a calendar quarter exceeds the amount of "applicable employment taxes" for that quarter, the excess shall be treated as an overpayment of taxes that is refundable to the employer.

6 Who is an eligible employer?

An eligible employer is an employer who has been carrying on a trade or business during 2020 that meets one of the following two criteria:

- The employer's trade or business is fully or partially suspended during a calendar quarter due to orders from an appropriate government authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) as a result of COVID-19; or
- The employer experiences a significant decline in gross receipts. (See below for more details)

7 What constitutes "fully or partially suspended"?

The term is not defined by the CARES Act, so the determination will likely require a facts and circumstances test for each employer. The CARES Act gives examples of limits on commerce, travel, and group meetings as examples of suspended operations.

The IRS FAQs give examples of actions which, in the IRS's interpretation, will or will not constitute full or partial suspension of operations. Within these examples, the IRS makes a distinction between "essential businesses" and "non-essential businesses."

The IRS FAQs also provide that if an employer closes its workplace but continues operations comparable to its operations prior to closure by requiring employees to telework, the employer doesn't have a partial suspension of operations. The FAQs do not address what would be considered "comparable" with respect to remote operations.

8 What constitutes "orders from an appropriate government authority"?

An "appropriate government authority" isn't defined in the CARES Act but would likely include orders from a president, governor, mayor, sheriff, county commission, police department, fire department, or public health official.

Pursuant to the IRS FAQs, the following are included in government orders:

- An order from the city's mayor stating that all non-essential businesses must close for a specified period;
- A state's emergency proclamation that residents must shelter in place for a specified period, other than residents who are employed by an essential business and may travel to and work at the workplace location; and
- An order from a local official imposing a curfew on residents that impacts the operating hours of a trade or business for a specified period.
- An order from a local health department mandating a workplace close for cleaning and disinfecting.

The IRS FAQs state that comments from a government official in a press conference or a media interview do not rise to the level of a government order. Additionally, the declaration of a state of emergency by a government authority also does not constitute a government order.

Government will vary by jurisdiction, so an employer located in multiple jurisdiction should review all applicable government orders to determine the extent to which it is impacted by government orders.

9 What is an "essential business?"

The term "essential business" is not defined in the CARES Act. It first appears in a FAQ published by the Joint Committee on Taxation, and later appears in the IRS FAQs. An essential business is generally identified as such by a specific government order which allows the business to continue operations within the government's jurisdiction. What constitutes an "essential business" will vary from state to state.

10 Is it possible for an essential business to qualify for the CARES Act employee retention credit?

The IRS FAQs generally provide that an essential business that is exempted from the appropriate government order does not have a full or partial suspension of operations. The FAQs, however, do provide some pathways whereby employers with locations that are deemed "essential businesses" may still qualify for the credit:

- If a government order causes suppliers to an essential business to suspend operations, the essential business may be considered to have a partial suspension of operations.
- If a government order allows an essential business to continue operations, but at reduced hours, the essential business may be considered to have a partial suspension of operations.
- If an employer is required to suspend its business operations for certain purposes, but not for other purposes, it may be considered to have a partial suspension of operations. Examples given in the IRS FAQs include a hospital that suspends non-urgent procedures while still remaining open for emergency and intensive care purposes, and a retailer which closes its storefront but remains open for online orders and curbside pickup.
- If an employer has locations comprised of both essential businesses and non-essential businesses, and the non-essential businesses have a partial suspension of operations, then the employer is an eligible employer for purposes of the credit. In this case, the IRS FAQs state that the non-essential operations must constitute more than a nominal portion of the employer's business. All of the employer's locations are considered a single employer under the CARES Act employee retention credit aggregation rules.
- An essential business may still qualify for the CARES Act employee retention credit if it has a significant decline in gross receipts.

11 What is a "significant decline in gross receipts"?

A "significant decline in gross receipts" is a period of time that:

- Begins with the first calendar quarter in 2020 for which gross receipts are 50 percent less than the gross receipts for the same calendar quarter in the previous year, and

  Ends with the earlier of January 1, 2021, or the calendar quarter following the first calendar quarter beginning after the calendar quarter described above, for which gross receipts are greater than 80 percent of the gross receipts for the same calendar quarter in the previous year.

As an example, an employer's gross receipts drop below 50 percent of prior year in 2020 Quarter 2 and return to over 80 percent of prior year gross receipts in 2020 Quarter 3. The employer's period for "significant decline in gross receipts" is April 1, 2020 through September 30, 2020.

12 How are gross receipts defined for purposes of the "significant decline" test?

Regulations referenced by this section state that the term "gross receipts" includes, but is not limited to, total sales (net of returns and allowances), all amounts received for services, interest income, dividends, rents, royalties, annuities, and sales of property (net of basis in the asset sold).

13 Is the "significant decline" test applied on a location-by-location test?

No. The "significant decline" test is done at the employer level, so all locations which are included under the same employer identification number would be aggregated for purposes of the 50 percent and 80 percent tests. See also below for aggregation rules for consolidated groups and related entities.

14 In a consolidated group (parent and subsidiary companies), is the determination of an eligible employer done on a separate entity test?

No. Corporations that are related under common control (a parent entity) are treated as a single entity for purposes of the CARES Act employee retention credit.

15 Are tax-exempt organizations and public agencies eligible for the credit?

Yes. An organization that is exempt from income tax under Section 501(a) of the Code is eligible for the credit. However, the credit does not apply to the federal government, any state or local government, or any agency or instrumentality of such governments.

16 Who is an eligible employee for purposes of the credit?

All full and part-time employees of an eligible employer are potentially eligible for the credit. See below for limitations regarding "related party" employees and employees on whom the Work Opportunity Tax Credit, the Employer Credit for Paid Family and Medical Leave, or the Families First Coronavirus Response Act Emergency Sick Leave or Emergency Family Leave Credits have been claimed.

17 What is included in the definition of qualified wages?

Qualified wages are wages paid by an eligible employer with respect to which an employee is not providing services (see below for definition) due to either a full or partial suspension of operations, or a significant decline in gross receipts. A special rule for employers with 100 or fewer full-time employees is discussed below.

"Wages" are broadly defined as generally including all remuneration for employment, including cash value of all remuneration (including benefits) paid in any medium other than cash. Wages must be subject to Social Security and Medicare taxes in order to be treated as qualified wages.

18 To what extent can health plan expenses be included in qualified wages?

The CARES Act states that "qualified wages" shall include so much of the eligible employer's qualified health plan expenses as are properly allocable to such wages. "Qualified health plan expenses" are the amount paid by the employer to provide and maintain a group health plan, but only to the extent that the amounts are excluded from gross income of the employees.

Qualified health plan expenses are treated as properly allocable to qualified wages if made on the basis of being pro rata among employees and pro rata on the basis of periods of coverage.

The IRS FAQs clarify that the definition of "qualified health plan expenses" includes both the portion of cost paid by the employer and the portion of the cost paid by the employee, provided that the employee's costs are paid with pre-tax dollars.

With respect to furloughed employees on whom the employer continues to pay health plan expenses, the Secretary of the Treasury has indicated in a letter to Congress that the FAQs will be revised to reflect Congressional intent, and will allow health plan expenses attributable to furloughed employees to be included in qualified wages.

19 What constitutes "not providing services" for purposes of the determination of qualified wages?

The CARES Act does not define "not providing services," so it is likely a facts and circumstances determination for each employer.

The IRS FAQs provide examples of circumstances where both exempt and non-exempt employees may be considered as "not providing services." Some of the statements in the FAQs include:

- If a non-exempt employee does not have a fixed schedule of work, the hours for which the employee is not providing services may be determined using any reasonable method.
- An employer may use any reasonable method to determine the number of hours that a salaried employees is not providing services, but for which the employee receives wages either at the employee's normal wage rate or at a reduced wage rate.
- Using the criteria for an employee entitled to intermittent leave under the paid sick leave or paid family leave provisions under the Families First Coronavirus Response Act is considered a reasonable method.
- The IRS FAQs provide that it is not reasonable for an employer to treat an employee's hours as having been reduced based on an assessment of the employee's productivity levels during the hours in which the employee is working.

20 Are vacation pay, sick leave, other personal leave or severance pay considered to be qualified wages for purposes of the employee retention credit?

The IRS FAQs provide that vacation pay, sick leave, and other personal leave is excluded from the definition of qualified wages to the extent that the leave was accrued in a period prior to the period in which the employee received wages and was not providing services. This interpretation doesn't exclude any leave accrued concurrent with the employee retention credit

The IRS FAQs provide that amounts paid to an employee following termination of employment does not constitute qualified wages for purposes of the employee retention credit.

21 What is the special rule for employers with 100 or fewer full-time employees?

In the case of an employer with 100 or fewer full-time employees, "qualified wages" include all wages paid to an employee during the eligibility period, regardless of whether or not the employee is not providing services.

For purposes of the credit, "full-time employee" is defined by Section 4980H of the Code as an employee who works 30 or more hours per week.

22 Can an employer claim the CARES Act employee retention credit on the same wages on which it qualifies for the Families First Coronavirus Response Act (FFCRA) emergency sick pay or family leave credits?

No. Any wages used for purposes of the Paid Sick Leave Credit (Section 7001 of the FFCRA) or the Paid Family Leave Credit (Section 7003 of the FFCRA) cannot be treated as qualified wages for purposes of the CARES Act employee retention credit. The FFCRA credits are limited to employers with fewer than 500 employees.

23 If the employer is eligible for the Employer Credit for Paid Family and Medical Leave on an employee, can the employer also claim the CARES Act employee retention credit on the employee on the same wages?

No. Any wages used for purposes of the Employer Credit for Paid Family and Medical Leave cannot be treated as qualified wages for purposes of the CARES Act employee retention credit.

24 Does the employer still have to add the amount of credit back to its wage deduction?

Yes. The CARES Act requires the employer to reduce its wage deduction by the amount of the CARES Act employer retention credit under Section 280C of the Code.

25 If a company files for the payroll tax deferral, can they also file for the advance refund claim on Form 7200?

Yes. An employer can request an advance payment on the refundable amounts of the retention credit (as well as the qualified sick and family leave credits under the FFCRA) after first reducing their current employment taxes to account for the credits. Any amount of credit that exceeds the reduced deposits can be requested in advance on a Form 7200. If an employer receives an advance payment, it will require a reconciliation on its employment tax return.

26 If an employee also owns an interest in the employer, can the employer still claim the credit?

The applicable attribution rules state that no wages will be taken into account with respect to the following individuals:

- An individual who owns 50 percent or more of the value of the stock of employer (if the employer is a corporation),
- An individual who owns 50 percent or more of the capital and profits interest of the employer (if the employer is another entity),
- A grantor, beneficiary, or fiduciary of the employer (if the employer is an estate or trust),
- A family relative of the employer (if the employer is an individual). Family relatives include children, siblings, step-siblings, parents, step-parents, nieces, nephews, aunts, uncles, and in-laws.

27 If the employer has claimed the Work Opportunity Tax Credit (WOTC) on the employee, can the employer also claim the CARES Act employee retention credit on the employee?

Yes, with some limitations. The CARES Act states that an employee cannot be included in the employee retention credit if the employer has also claimed WOTC on that employee in the same period.

28 If the employer has claimed disaster area employee retention credits on the employee for 2017-2019 disasters, can the employer also claim the CARES Act employee retention credit on the employee?

Yes. There are no restrictions in the CARES Act that would prohibit an employer from claiming the employee retention credit on an employee if the employer previously claimed disaster-related employee retention credits in 2017 through 2019.

29 Can the employer claim the CARES Act employee retention credit on an employee if the employer is also claiming the Federal Empowerment Zone Employment Credit or the Indian Employment Credit on the same employee?

There are no restrictions in the CARES Act that would prohibit an employer from claiming the employee retention credit on an employee if the employer also claimed the Federal Empowerment Zone Employment Credit or the Indian Employment Credit.

30 If the employer has outsourced its employment functions to a certified professional employer organization, is it still eligible for the CARES Act employee retention credit?

Yes. The CARES Act states that the employee retention credit is a credit described in Section 3511 (d)(2) of the Code. As such, credit with respect to a work site employee performing services for the customer applies to the customer, and not the certified professional employer organization.

31 If the employer is pursuing a Paycheck Protection Program (PPP) loan as provided by the CARES Act, is it still eligible for the CARES Act employee retention credit?

No. The CARES Act prohibits an employer from claiming the employee retention credit if the employer also receives a covered loan under Section 1102 of the CARES Act ("Paycheck Protection Program"), unless it was repaid by May 18, 2020, per IRS FAQ, Question 79. The May 18 deadline is the date defined by the Small Business Administration as being the safe harbor deadline for repaying a PPP loan without having to certify a need for the loan in good faith. The Secretary of the Treasury is also authorized to issue guidance regarding recapture provisions if the employer receives a covered loan after initially claiming the employee retention credit.

32 Will the credit be available for advance payment if the company will have a refund?

Yes. The IRS has issued Form 7200 on which an employer can claim an advance payment of the employee retention credit that would be due for the quarter. Form 7200 may be filed at any time prior to the due date of Form 941 for the applicable quarter and may be able to be filed multiple times during the course of the quarter. Form 7200 advance payments will be available for the 2nd through 4th quarters of 2020.

33 The CARES Act also allows an employer to defer the payment of the employer portion of Social Security taxes to 2021 and 2022. How does this affect the credit?

The CARES Act employee retention credit is a permanent reduction in the amount of employer Social Security taxes. The delay of the payment of the employer portion of Social Security taxes is strictly a deferral. If the employer plans to take advantage of the deferral, the retention credit reduces the amount of employer Social Security taxes ultimately due.

34 What government forms and interpretations have been published with respect to the CARES Act employee retention credit?

The IRS has released two new forms with respect to the credit:

- Form 7200 – Advance Payment of Employer Credits Due to COVID-19
- Revised Form 941 – Employer's Quarterly Federal Tax Return (still in draft form)

Additionally, interpretations in the form of Frequently Asked Questions have been published by the following:

- Internal Revenue Service (https://www.irs.gov/newsroom/faqs-employee-retention-credit-under-the-cares-act)
- Senate Finance Committee (https://www.finance.senate.gov/chairmans-news/cares-act-employee-retention-credit-faq)
- Joint Committee on Taxation (https://www.jct.gov/publications.html?func=startdown&id=5256)

35 What types of information should an employer be gathering to properly calculate the CARES Act employee retention credit?

Examples of items needed to calculate the credit include payroll information and documentation of how COVID-19 has impacted your workforce at each of your locations. ADP can assist you with the credit calculation with mapping tools showing general areas of government-mandated restrictions, survey methodologies for capturing employee-level information, and best practices across the country.

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