

EMPLOYEE RETENTION CREDIT: CALCULATIONS, WAGES, PPP FORGIVENESS AND MORE - GUIDANCE FOR Q3 AND BEYOND



The IRS released [Notice 2021-49](#) on August 4, which amplifies and clarifies guidance from the two previous Employee Retention Credit (ERC) Notices (see [here](#), and [here](#)) and provides additional guidance on the American Rescue Plan (ARP) extension of the ERC for the 3rd and 4th quarters of 2021. These clarifications include, among other things:

1. making the credit available to eligible employers that pay qualified wages after June 30, 2021, and before January 1, 2022,
2. expanding the definition of eligible employer to include "recovery startup businesses,"
3. modifying the definition of qualified wages for "severely financially distressed employers," and
4. providing that the ERC does not apply to wages considered as payroll costs in connection with a shuttered venue grant under section 324 of the Economic Aid to Hard-Hit Small Businesses, Non-Profits, and Venues Act, or a restaurant revitalization grant under section 5003 of the ARP.

We've summarized the key items included in the notice for claiming the credit in the 3rd and 4th quarters of 2021.

Q3 and Q4 Guidance

Qualified Employers

Employers that experience a 20% decline in gross receipts, have a full or partial suspension of business due to a governmental order, **or**, are a recovery start-up business are eligible. The credit is still limited to 70% of \$10,000 in qualified wages per employee for each calendar quarter. This credit is limited to a maximum credit of \$50,000 per calendar quarter for a recovery start-up business.

Recovery Start-Up Business

Businesses that began operating after February 15, 2020, and have an average annual gross receipt below \$1,000,000 qualify as recovery start-up businesses. The Notice clarifies the date a business began operations is when the business has begun to function as a going concern and performs the activities for which it is organized. The determination of whether an employer is a recovery startup business is made separately for each quarter. This means the business could qualify for the ERC under the 20% decline in receipts for the 4th quarter and as a recovery start-up business in the 3rd quarter.

Severely Financially Distressed Employer

Employers who have more than a 90% decline in gross receipts compared to the same calendar quarter in 2019 qualify as severely financially distressed employers. The Notice clarifies that the alternative quarter election is available for severely financially distressed employers. For example, if a company had a 95% decrease in the 2nd quarter of 2021, it would qualify in the 3rd quarter of 2021 as a severely financially distressed employer. A severely distressed employer may treat all wages paid to its employees during the quarter as qualified wages. Large employers are not limited to wages paid to employees who did not perform services.

PPP Loan Forgiveness and Other Programs

The ERC does not apply to qualified wages considered as payroll costs in

connection with a shuttered-venue-operators grant, restaurant-revitalization grant, paycheck protection program or other similar programs.

Miscellaneous Issues for 2020 and 2021

Notice 2021-49 also provides guidance on several miscellaneous issues with respect to the employee retention credit for both 2020 and 2021. This guidance responds to various questions that the Treasury Department and the IRS have been asked about the employee retention credit, including:

- The definition of a full-time employee and whether that definition includes full-time equivalents,
- The treatment of tips as qualified wages and the interaction with the section 45B credit,
- The timing of the qualified wages deduction disallowance and whether taxpayers that already filed an income tax return must amend that return after claiming the credit on an adjusted employment tax return, and
- Whether wages paid to majority owners and their spouses may be treated as qualified wages.

Full-Time Employees vs. Full-Time Equivalents

When an employer is determining their average number of employees in 2019 to determine if they are a large eligible employer or a small eligible employer, full-time equivalents are not required to be included in the analysis when determining the full-time employees. Employees who are not full-time are still included in determining qualified wages if all other requirements to treat the amounts as qualified wages are satisfied.

Tips as Qualified Wages

The Notice confirmed that cash tips received by an employee are included in the definition of "wages" when they exceed \$20. Tips are paid by the employer when the employee received them in the course of their employment. The Notice also clarified that an employer may still claim the ERC and section 45B credit for excess employer social security tax on the tips on the same wages.

Timing of Qualified Wage Deductions

Guidance was received on the timing of the qualified wages deduction disallowance from the ERC. A reduction in the amount of the deduction allowed for qualified wages caused by the receipt of the ERC occurs in the tax year the wages were paid or incurred. This confirms that a taxpayer should file an amended Federal income tax return or Administrative Adjustment Request if they have already filed an original return that deducted the wages that were later included in an Amended payroll tax return to claim the credit.

Exclusion of Related Individuals' Wages

The Notice clarifies the wages of majority owners and their spouses do not qualify for the ERC if either the owner or the spouse has any living relative. The Notice provides additional examples and clarification on whether wages paid to majority owners, their spouses and other family members may or may not be qualified wages. Under the existing guidance, wages paid to employees with the following relationships to a majority owner of a corporation or partnership are not Qualified Wages:

- Child or descendant of a child
- Brother, sister, stepbrother, or stepsister
- Father, mother, or ancestor of either
- Stepfather or stepmother
- Niece or nephew
- Aunt or uncle
- Son-in-law, daughter-in-law, father-in-law, mother-in-law, brother-in-law, or sister-in-law
- An individual (other than a spouse) who has the same principal place of abode and is a member of the household

The Department of Treasury and IRS have stated in this Notice that they will continue to monitor potential legislation related to the ERC that may impact this notice and ERC guidelines. Additional guidance may follow.

Your [BMF Advisor](#) can help you determine the applicability of your unique

situation. Contact us if you have questions about these changes or how your tax status could be affected.