



# FAQs: Employee Retention Credit under the CARES Act

The Coronavirus Aid, Relief, and Economic Security Act (CARES Act), enacted on March 27, 2020, is designed to encourage Eligible Employers to keep employees on their payroll, despite experiencing economic hardship related to COVID-19, with an employee retention tax credit (Employee Retention Credit).

The Families First Coronavirus Relief Act (FFCRA) requires certain employers to pay sick or family leave wages to employees who are unable to work or telework due to certain circumstances related to COVID-19. Employers are entitled to a refundable tax credit for the required leave paid, up to specified limits. [See FAQs]. The same wages cannot be counted for both credits.

## Basic FAQs

### ▼ What is the Employee Retention Credit?

The Employee Retention Credit is a fully refundable tax credit for employers equal to 50 percent of qualified wages (including allocable qualified health plan expenses) that Eligible Employers pay their employees. This Employee Retention Credit applies to qualified wages paid after March 12, 2020, and before January 1, 2021. The maximum amount of qualified wages taken into account with respect to each employee for all calendar quarters is \$10,000, so that the maximum credit for an Eligible Employer for qualified wages paid to any employee is \$5,000.

### ▼ Who is an Eligible Employer?

Eligible Employers for the purposes of the Employee Retention Credit are those that carry on a trade or business during calendar year 2020, including a tax-exempt organization, that either:

- Fully or partially suspends operation during any calendar quarter in 2020 due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) due to COVID-19; or
- Experiences a significant decline in gross receipts during the calendar quarter.

**Note:** Governmental employers are not Eligible Employers for the Employee Retention Credit. Also, Self-employed individuals are not eligible for this credit for their self-employment services or earnings.

✓ **When is the operation of a trade or business partially suspended for the purposes of the Employee Retention Credit?**

The operation of a trade or business may be partially 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 to operate but not at its normal capacity.

**Example:** A state governor issues an executive order closing all restaurants, bars, and similar establishments in the state in order to reduce the spread of COVID-19. However, the executive order allows those establishments to continue food or beverage 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, bars, and similar establishments in the state that provided full sit-down service, a dining room, or other on-site eating facilities for customers prior to the executive order.

✓ **What is a “significant decline in gross receipts”?**

A significant decline in gross receipts begins with the first quarter in which an employer’s gross receipts for a calendar quarter in 2020 are less than 50 percent of its gross receipts for the same calendar quarter in 2019. The significant decline in gross receipts ends with the first calendar quarter that follows the first calendar quarter for which the employer’s 2020 gross receipts for the quarter are greater than 80 percent of its gross receipts for the same calendar quarter during 2019.

**Example:** An employer’s gross receipts were \$100,000, \$190,000, and \$230,000 in the first, second, and third calendar quarters of 2020, respectively. Its gross receipts were \$210,000, \$230,000, and \$250,000 in the first, second, and third calendar quarters of 2019, respectively. Thus, the employer’s 2020 first, second, and third quarter gross receipts were approximately 48%, 83%, and 92% of its 2019 first, second, and third quarter gross receipts, respectively. Accordingly, the employer had a significant decline in gross receipts commencing on the first day of the first calendar quarter of 2020 (the calendar quarter in which gross receipts were less than 50% of the same quarter in 2019) and ending on the first day of the third calendar quarter of 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.

### ✓ **How is the maximum amount of the Employee Retention Credit available to Eligible Employers determined?**

The credit equals 50 percent of the qualified wages (including qualified health plan expenses) that an Eligible Employer pays in a calendar quarter. The maximum amount of qualified wages taken into account with respect to each employee for all calendar quarters is \$10,000, so that the maximum credit for qualified wages paid to any employee is \$5,000.

**Example 1:** Eligible Employer pays \$10,000 in qualified wages to Employee A in Q2 2020. The Employee Retention Credit available to the Eligible Employer for the qualified wages paid to Employee A is \$5,000.

**Example 2:** Eligible 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 the Eligible 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.

### ✓ **What are “qualified wages”?**

Qualified wages are wages (as defined in section 3121(a) of the Internal Revenue Code (the “Code”)) and compensation (as defined in section 3231(e) of the Code) paid by an Eligible Employer to employees after March 12, 2020, and before January 1, 2021. Qualified wages include the Eligible Employer’s qualified health plan expenses that are properly allocable to the wages.

The definition of qualified wages depends, in part, on the average number of full-time employees (as defined in section 4980H of the Code) employed by the Eligible Employer during 2019.

If the Eligible Employer averaged more than 100 full-time employees in 2019, qualified wages are the wages paid to an employee for time that the employee is **not providing services** due to either (1) a full or partial suspension of operations by order of a governmental authority due to COVID-19, or (2) a significant decline in gross receipts. For these employers, qualified wages taken into account for an employee may not exceed what the employee would have been paid for working an equivalent duration during the 30 days immediately preceding the period of economic hardship.

If the Eligible Employer averaged 100 or fewer full-time employees in 2019, qualified wages are the wages paid to **any employee** during any period of economic hardship described in (1) and (2) above.

### ✓ **Is an Employer required to pay qualified wages to its employees under the CARES Act?**

No. The CARES Act does not require employers to pay qualified wages. In addition, Eligible Employers may elect to not claim the credit for the Employee Retention Credit. (The FFCRA does require certain employers to pay sick or family leave wages to employees who are unable to work or telework due to a COVID-19 circumstance. These employers may be entitled to a refundable tax credit for those wages paid, although the employers may elect not to claim the credit.)

✓ **Can Eligible Employers claim the Employee Retention Credit for qualified wages paid in March 2020?**

Eligible Employers may claim the Employee Retention Credit for qualified wages that they pay after March 12, 2020, and before January 1, 2021. Therefore, an Eligible Employer may be able to claim the credit for qualified wages paid as early as March 13, 2020.

✓ **May an Eligible Employer receive the Employee Retention Credit for periods after December 31, 2020?**

No. The Employee Retention Credit is only available with respect to wages paid after March 12, 2020, and before January 1, 2021.

✓ **Against what employment taxes does the Employee Retention Credit apply?**

The credit is allowed against the employer portion of social security taxes under section 3111(a) of the Internal Revenue Code (the “Code”), and the portion of taxes imposed on railroad employers under section 3221(a) of the Railroad Retirement Tax Act (RRTA) that corresponds to the social security taxes under section 3111(a) of the Code.

✓ **What makes the credit “fully refundable”?**

The credits are fully refundable because the Eligible Employer may get a refund if the amount of the credit is more than certain federal employment taxes the Eligible Employer owes. That is, if for any calendar quarter the amount of the credit the Eligible Employer is entitled to exceeds the employer portion of the social security tax on all wages (or on all compensation for employers subject to RRTA) paid to all employees, then the excess is treated as an overpayment and refunded to the employer under sections 6402(a) and 6413 (a) of the Code. Consistent with its treatment as an overpayment, the excess will be applied to offset any remaining tax liability on the employment tax return and the amount of any remaining excess will be reflected as an overpayment on the return. Like other overpayments of federal taxes, the overpayment will be subject to offset under section 6402(a) of the Code prior to being refunded to the employer.

**Example:** Eligible Employer pays \$10,000 in qualified wages to Employee A in Q2 2020. The Employee Retention Credit available to the Eligible 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 the Eligible Employer is liable for with respect to all employee wages paid in Q2 2020. Any excess over the employer's share of social security taxes is treated as an overpayment and refunded to the Eligible Employer after offsetting other tax liabilities on the employment tax return and subject to any other offsets under section 6402(a) of the Code.

✓ **How does an Eligible Employer claim the refundable tax credit for qualified wages?**

Eligible Employers will report their total qualified wages and the related credits for each calendar quarter on their federal employment tax returns, usually Form 941, Employer's Quarterly Federal Tax Return. 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, Eligible Employers can fund qualified wages by accessing federal employment taxes, including withheld taxes, that are required to be deposited with the IRS or by requesting an advance of the credit from the IRS.

✓ **Can an Eligible Employer paying qualified wages fund its payments of qualified wages before receiving the credits by reducing its federal employment tax deposits?**

Yes. An Eligible Employer may fund the qualified wages by accessing federal employment taxes, including those that the Eligible Employer already withheld, that are set aside for deposit with the IRS, for other wage payments made during the same quarter as the qualified wages.

That is, 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. The Eligible Employer must account for the reduction in deposits on the Form 941, Employer's Quarterly Federal Tax Return, for the quarter.

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

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

✓ **May an Eligible 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:

1. the Eligible Employer paid qualified wages to its employees in the calendar quarter before the required deposit,
2. the amount of federal employment taxes that the Eligible 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 Eligible Employer's anticipated Employee Retention Credit for the qualified wages for the calendar quarter as of the time of the required deposit, and
3. the Eligible 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.

For more information, about the relief from the penalty for failure to deposit federal employment taxes on account of qualified wages, see Notice 2020-22 (PDF).

✓ **How can an Eligible Employer that is paying qualified wages fund the payment of these wages if the Eligible Employer does not have sufficient federal employment taxes set aside for deposit to cover those payments? Can the employer get an advance of the credits?**

Yes. Because quarterly returns are not filed until after qualified wages are paid, some Eligible Employers may not have sufficient federal employment taxes set aside for deposit to the IRS to fund their qualified wages. Accordingly, the IRS has established a procedure for obtaining an advance of the refundable credits.

The Eligible Employer should first reduce its remaining federal employment tax deposits for wages paid in the same calendar quarter by the maximum allowable amount. If the anticipated credit for the qualified wages exceeds the remaining federal employment tax deposits for that quarter, the Eligible Employer can file a Form 7200, Advance Payment of Employer Credits Due to COVID-19, to claim an advance refund for the full amount of the anticipated credit for which it did not have sufficient federal employment tax deposits.

If an Eligible Employer fully reduces its required deposits of federal employment taxes otherwise due on wages paid in the same calendar quarter to its employees in anticipation of receiving the credits, and it has not paid qualified wages in excess of this amount, it

should not file the Form 7200. If it files the Form 7200, it will need to reconcile this advance credit and its deposits with the qualified wages on Form 941 (or other applicable federal employment tax return such as Form 944 or Form CT-1), and it may have an underpayment of federal employment taxes for the quarter.

**Example:** An Eligible Employer paid \$20,000 in qualified wages, and is therefore entitled to a credit of \$10,000, and is otherwise required to deposit \$8,000 in federal employment taxes, including taxes withheld from all of its employees, on wage payments made during the same calendar quarter. The Eligible Employer has no paid sick or family leave credits under the FFCRA. The Eligible Employer can keep the entire \$8,000 of taxes that the Eligible Employer was otherwise required to deposit without penalties as a portion of the credits it is otherwise entitled to claim on the Form 941. The Eligible Employer may file a request for an advance credit for the remaining \$2,000 by completing Form 7200.

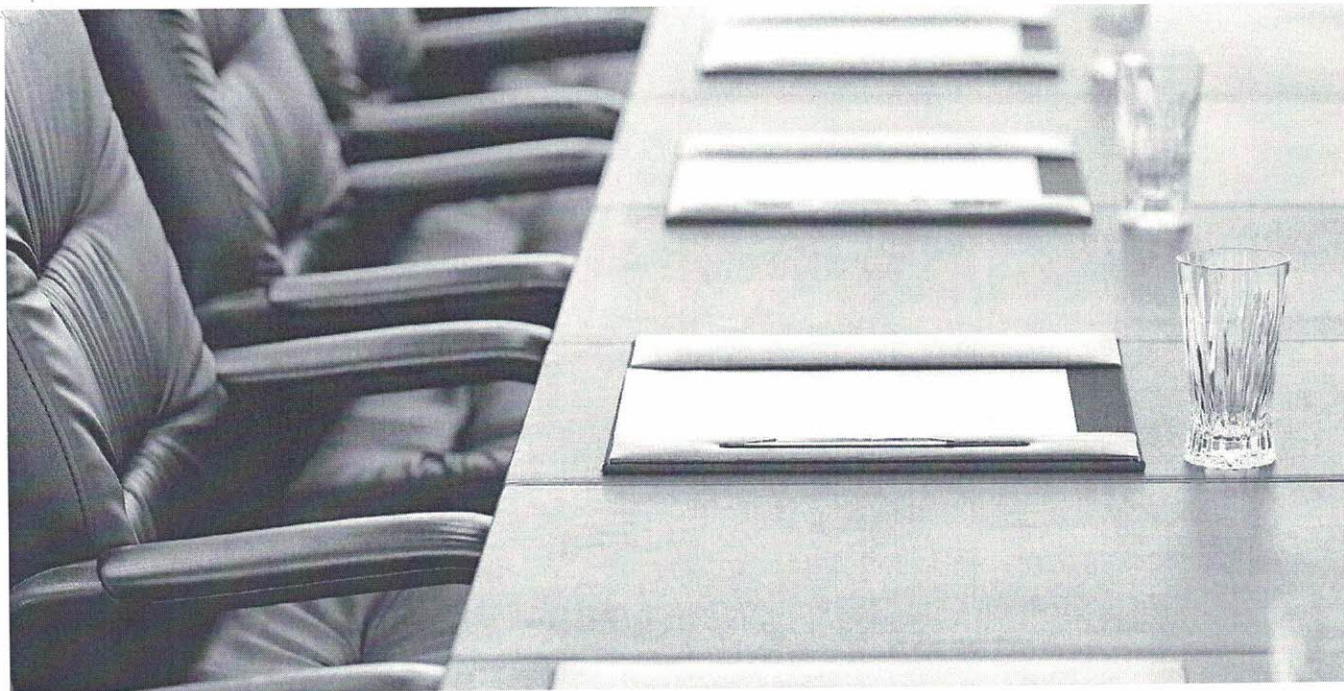
✓ **May an Eligible Employer receive both the tax credits for the qualified leave wages under the FFCRA and the Employee Retention Credit under the CARES Act?**

Yes, but not for the same wages. The amount of qualified wages for which an Eligible Employer may claim the Employee Retention Credit does not include the amount of qualified sick and family leave wages for which the employer received tax credits under the FFCRA.

✓ **May an Eligible Employer receive both the Employee Retention Credit and a Small Business Interruption Loan under the Paycheck Protection Program that is authorized under the CARES Act?**

No. An Eligible Employer may not receive the Employee Retention Credit if the Eligible Employer receives a Small Business Interruption Loan under the Paycheck Protection Program that is authorized under the CARES Act (“Paycheck Protection Loan”). An Eligible Employer that receives a paycheck protection loan should not claim Employee Retention Credits.

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## Alert

Our attorneys stay on top of changes in legislation, agency regulations, case law, and industry trends—then craft timely legal alerts to keep clients up to date on legal developments important to their business.

March 27, 2020

# COVID-19: US Economic Stimulus Law Includes Employee Retention Credit for Employers

On Friday, President Trump signed the Coronavirus Aid, Relief, and Economic Security (CARES) Act into law, which includes a significant tax incentive to keep employees on payroll in the form of a new “employee retention credit.”

The employee retention credit is a payroll tax credit equal to 50 percent of “qualified wages” paid by “eligible employers” to certain employees during the COVID-19 crisis. The credit applies against the employer’s share of FICA (social security) tax. The credit is capped at \$10,000 per employee.

To the extent that the credit exceeds the employer’s share of FICA taxes for the quarter, the excess will be refunded to the employer. The CARES Act grants the Internal Revenue Service the authority to advance tax credit payments to eligible employers and to waive failure to



deposit penalties for employers that do not make payroll tax deposits in anticipation of receiving the credit. The credit will apply to wages paid between March 12 and December 31.

### Eligible Employer

An “eligible employer” means any employer conducting a trade or business in 2020—including tax-exempt entities—the operations of which have been fully or partially suspended as a result of a government order limiting commerce, travel, or group meetings, or that have experienced a reduction over 50 percent in quarterly receipts measured against the same quarter last year.

### Qualified Wages

The CARES Act defines “qualified wages” differently for employers who employed more than 100 full-time employees in 2019 (eligible large employers) and employers who employed 100 or fewer full-time employees in 2019 (eligible small employers). For eligible large employers, “qualified wages” means wages paid to an employee who is not performing services for the employer (e.g., a furloughed employee remaining on the employer’s payroll). For eligible small employers, “qualified wages” include all wages paid by the employer regardless of whether the employee is performing services for the employer. The number of an employer’s full-time employees in 2019 is determined under the methodology established under the Affordable Care Act.

For both eligible large employers and eligible small employers, “wages” has the meaning used for FICA tax purposes. Qualified wages also include the employer-paid portion of the employee’s group health plan premiums.

### Coordination With Tax Credit for Coronavirus-Related Mandatory Paid Leave

Signed into law on March 18, the Families First Coronavirus Response Act (FFCRA) requires most employers to provide up to 80 hours of paid sick leave of up to \$511 per week to employees quarantined due to COVID-19 or self-quarantined while seeking a medical diagnosis. The FFCRA also requires employers to provide up to 80 hours of paid leave of up to \$200 per day to employees who take leave to care for a family member or child whose school or daycare center is closed. The FFCRA includes a mandatory paid leave credit against payroll tax for 100 percent of the mandatory paid leave.

For purposes of the employee retention credit, qualified wages do not include wages taken into account for purposes of the mandatory paid leave credit. An employer that claims both credits must apply the mandatory paid leave credit first, followed by the employer retention credit.

### Coordination With Other Employer Tax Credits

The employer retention credit is not available with respect to an employee for any period for which the employer is allowed a work opportunity credit with respect to the employee. Wages taken into account for the employer credit for paid family and medical leave (Internal Revenue Code Section 45S) are not eligible for the employee retention credit.

### Other Limitations

The credit is not available to employers receiving small business interruption loans under the CARES Act.

*If you have any questions regarding the content of this alert, please contact Ray McCabe, partner, at [rmccabe@barclaydamon.com](mailto:rmccabe@barclaydamon.com) or another member of the Tax Practice Areas.*

*We have a specific team of Barclay Damon attorneys who are actively working on assessing regulatory, legislative, and other governmental updates related to COVID-19 and who are prepared to assist clients. Please contact Yvonne Hennessey, COVID-19 Response Team leader, at [yhennessey@barclaydamon.com](mailto:yhennessey@barclaydamon.com) or any member of the COVID-19 Response Team at [COVID-19ResponseTeam@barclaydamon.com](mailto:COVID-19ResponseTeam@barclaydamon.com).*

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## Related Practices

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## Related Industries

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