

Update: COVID-19 Related Tax Credits, Deferral of Payment of Employer Social Security Tax, Other Tax Issues

May 6, 2020

The Families First Coronavirus Relief Act (FFCRA) and the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) make two separate, but related, tax credits available to employers, including tax-exempt organizations, whose business is affected by the COVID-19 pandemic.

FFCRA Leave Credit. The FFCRA provides a tax credit to employers to cover the costs on a dollar-for-dollar basis of providing the FFCRA-required qualified sick leave and family leave wages. In addition, the tax credit includes health plan expenses paid by the employer in connection with the qualified leave wages. Eligible employers can claim these tax credits based on qualifying leave wages paid for the period between April 1, 2020, and December 31, 2020.

CARES Act Employee Retention Credit. The CARES Act provides a tax credit to employers whose operations are suspended or reduced due to COVID-19 equal to 50% of qualified wages (including certain health plan expenses) up to \$10,000 paid to employees after March 12, 2020, and before January 1, 2021. The maximum tax credit is capped at \$5,000 per employee. Employers who receive a Small Business Interruption Loan under the CARES Act cannot claim the Employee Retention Tax Credit.

Both tax credits are applied against the employer share of the Social Security tax imposed on the W-2 wages paid by the employer to all of its employees. If the total amount of the tax credits exceeds an employer's Social Security tax liability, the employer can receive a refund of the excess amount so the employer will get the benefit of the full amount of the tax credits.

Tax-exempt employers are eligible for the FFCRA Leave Credit and the Employee Retention Credit.

(This special report is based on the FAQs published and updated by the IRS through May 1, 2020.)

FFCRA Leave Credit

Businesses or tax-exempt organizations that (i) have fewer than 500 employees (as determined under the Department of Labor rules), and (ii) are required under the FFCRA to pay "qualified sick leave wages" and/or "qualified family leave wages" (Required Leave Wages), are entitled to claim the FFCRA Leave Credit.

An Eligible Employer is entitled to receive a tax credit equal to the total of the following:

1. 100% of the Required Leave Wages paid for leave taken during the *period beginning April 1, 2020, and ending December 31, 2020;*

plus

2. 100% of the "qualified health plan expenses" that are allocable to the Required Leave Wages paid to employees;

plus

3. 100% of the employer share of the Medicare tax that an employer is required to pay on the Required Leave Wages.

In addition, although Required Leave Wages are W-2 wages, the FFCRA provides that the employer share of the Social Security tax that normally applies to W-2 wages does *not* apply to Required Leave Wages.

CARES Act Employee Retention Credit

An employer is eligible for the tax credit if it carried on a trade or business during calendar year 2020 that

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either:

1. fully or partially suspends operations during any calendar quarter in 2020 due to “orders from an appropriate governmental authority” limiting commerce, travel, or group meetings due to COVID-19;

or

2. experience a “significant decline in gross receipts” during the calendar quarter (in comparison to the same calendar quarter in 2019).

(The IRS FAQs issued on April 29, 2020, provide additional guidance about: (i) what is an appropriate governmental order; and (ii) factors that indicate whether and when an employer’s operations are considered to be fully or partially suspended due to that order.)

The number of employees an employer has does *not* affect whether it is an eligible employer that can claim the credit.

- A “significant decline in gross receipts” *begins* on the first day of the first calendar quarter of 2020 in which an employer’s gross receipts for a calendar quarter in 2020 are *less than* 50% of its gross receipts for the same calendar quarter in 2019.
- The significant decline in gross receipts *ends* on the first day of the first calendar quarter following the calendar quarter in which the employer’s 2020 gross receipts *greater than* 80% of its gross receipts for the same calendar quarter during 2019.

The definition of “qualified wages” depends on the average number of employees an eligible employer had during 2019 (the average number of full-time employees is determined using the same rules for determining whether an employer is a large employer within the meaning of the health coverage requirements of the Affordable Care Act, as defined at Section 4980H of the Internal Revenue Code):

100 or Less. If the average number of full-time employees during 2019 was *100 or less*, then the employer may treat all wages (and qualified health plan expenses) paid to employees during the calendar quarter in which the employer’s business operations are fully or partially suspended due to COVID-19, or a calendar quarter in which the employer experiences a significant decline in gross receipts, as qualified wages *regardless of whether or not an employee is providing services* during that period.

More than 100. If the average number of full-time employees during 2019 was *greater than 100*, then only W-2 wages and qualified health plan expenses that are paid to employees for non-worked time during the calendar quarter in which the employer’s business operations are fully or partially suspended due to COVID-19, or a calendar quarter in which the employer experiences a significant decline in gross receipts, can be treated as qualified wages.

Notes –

- Employers may claim the tax credit for qualified wages that they pay *after March 12, 2020, and before January 1, 2021*. Accordingly, an employer may be able to claim the credit for qualified wages paid as early as March 13, 2020.
- The maximum amount of qualified wages taken into account with respect to each employee is \$10,000, so that the maximum credit for qualified wages paid to any employee from March 13, 2020, to December 31, 2020 is \$5,000.
- If an employer received tax credits for FFCRA leave wages, those same wages cannot be included as *qualified wages* for purposes of the Employee Retention Credit.
- An employer cannot receive the Employee Retention Credit if the employer receives a Small Business Interruption Loan under the CARES Act Paycheck Protection Program that is authorized under the CARES Act (PPP Loan), regardless of the date of the loan.

Qualified Health Plan Expenses

Both the FFCRA and the CARES Act define *qualified health plan expenses* as amounts paid or incurred by an eligible employer to provide group health plan coverage to eligible employees on a tax-free basis.

Qualified health plan expenses include both the portion of the cost paid by the employer *and* the portion of the cost paid by the employee through pre-tax salary reduction contributions.

The IRS FAQs provide rules for allocating the qualified health plan expenses to eligible employees for purposes of determining the amount of the tax credits.

How to Claim the Tax Credits

Under the IRS FAQs, the procedures for claiming the FFCRA Leave Credit and Employee Retention Credit are the same.

Employers will report their total Required Leave Wages and the FFCRA Leave Credits, and total Qualified Wages for purposes of the Employee Retention Credit for each quarter on IRS Form 941, *Employer’s Quarterly Federal Tax Return* — the regular form 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. (On May 1, 2020, the IRS issued a draft version of Form 941 revised to take into account the COVID-19 tax credits.)

An employer that pays Qualified Sick Leave or Family Leave Wages and/or 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 the amount of:

1. the Qualified Sick Leave or Family Leave Wages (and allocable qualified health plan expenses and the Employer's share of Medicare tax on the Qualified Sick Leave or Family Leave Wages) paid in that calendar quarter, and
2. the Qualified Wages paid in the calendar quarter.

An employer that pays Required Leave Wages and/or 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 — including taxes withheld from employees — it deposits for that quarter by the amount of:

- the Required Leave Wages (and allocable qualified health plan expenses and the employers share of Medicare tax on the Required Leave Wages) paid in that calendar quarter, and
- the Qualified Wages paid in the calendar quarter.

The total amount of the FFCRA Leave Credit and the Employee Retention Credit in excess of the Social Security tax the Eligible Employer owes for the quarter is refundable. If the amount of the tax credits for a calendar quarter exceeds the Social Security tax the Eligible Employer owes for the quarter, then the excess is treated as an overpayment that can be applied to offset any remaining tax liability on the Form 941 prior to being refunded to the employer.

Alternatively, instead of waiting on the regular refund procedures, an employer can request an advance payment of the refund by filing IRS Form 7200, *Advance Payments of Employer Credits due to COVID-19*.

Deferral of Payment of Employer Portion of 2020 Social Security Tax

The CARES Act permits any employer to defer payment of the employer portion of Social Security taxes *regardless* of whether the employer is affected by COVID-19. The statute does *not* impose any terms and conditions for the deferral and does have any employer size requirements. *All* employers are eligible to use the deferral. The deferral can apply to the employer Social Security tax payable at any time beginning as March 27, 2020 (date of enactment of the CARES Act) and ending before January 1, 2021.

The deferral applies only to the employer portion of Social Security taxes. The deferral does *not* apply to the employer portion of Medicare taxes.

The deferred employer Social Security taxes must be paid in two installments by the following dates (the “applicable dates”):

- 50% by December 31, 2021.
- Remaining 50% by December 31, 2022.

No interest or penalties apply to the deferred Social Security tax payments.

Limitation – Employers who have received a PPP Loan may defer payment of the employer's share of Social Security tax that otherwise would be required to be made beginning on March 27, 2020, through the date the lender issues a decision to forgive the loan. Once an employer receives a decision from its lender that its PPP loan is forgiven, the employer is no longer eligible to defer payment of the employer's share of Social Security tax *due after that date*. However, the amount of the deposit and payment of the employer's share of Social Security tax that was deferred through the date that the PPP loan is forgiven continues to be deferred and will be due on the “applicable dates,” described below.

How FFCRA Qualified Leave Wages and CARES Act Qualified Wages are Treated for Tax and Benefit Purposes

FFCRA Qualified Leave Wages and CARES Act *qualified wages* are taxable as W-2 wages to employees and subject to FICA (Social Security and Medicare) tax withholding and federal income tax withholding. The FFCRA did *not* add any special exceptions.

The same rules that generally apply to an employee's regular wages also apply to FFCRA Qualified Leave Wages and CARES Act *qualified wages*. That means — subject to the terms and conditions of the particular benefit plan — that

- To the extent an employee has a salary reduction agreement in place with the Eligible Employer, the FFCRA does not include any provisions that expressly prohibit taking salary reduction contributions for any plan from FFCRA Qualified Leave Wages and CARES Act *qualified wages*.
- FFCRA Qualified Leave Wages and CARES Act *qualified wages* also are considered wages for purposes of other benefits that the Eligible Employer provides, such as contributions to 401(k)

plans.

Special Tax Issues for Employers

The economic benefit of the tax credits is reduced for taxable employers by the income tax treatment of the credits:

- *FFCRA Leave Credit.* An employer receiving the FFCRA Leave Credit must include the amount of the credit in gross income on its income tax return.
- *Employee Retention Credit.* In contrast, an employer receiving the Employee Retention Credit is not required to include the credit in gross income, but instead reduce the amount that the employer can claim as a compensation deduction on its income tax return by the amount of the credit.

For additional guidance, please contact a Jackson Lewis attorney.

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