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Employee Retention Credit Will Your Business Survive an IRS Audit?

Presented by
Joseph A. Peterson
Plunkett Cooney

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Today's Presenter



Joseph A. Peterson
(248) 433-7158
jpeterson@plunkettcooney.com

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Background

- What is the Employee Retention Credit or "ERC"?
- Pandemic Era program from CARES Act
 - Sister program with the Paycheck Protection Program (PPP)
 - Refundable tax credit
 - Covers 2020 and 2021 tax periods
 - Credit for qualified wages paid to employees
 - Very nuanced program with complex qualification rules

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IRS
 News Essentials | Issue Number: IR-2024-83
 "In the last year alone, we have opened nearly 700 new COVID fraud investigations that collectively add up to \$5 billion in potential fraud," said CI Chief Guy Ficco. "While COVID may no longer be top of mind to the average American when they wake up, the fraud committed through these different programs is very much top of mind to CI. Our special agents continue to seek out fraudsters who stole money from government loan programs for their personal gain."
 Facts & Figures: Investigation (CI) has investigated 1,644 tax and money laundering cases related to COVID fraud potentially totaling \$8.9 billion, with well over half that amount coming from cases opened in the last year.
 Around The Nation: ... fraud 9 billion ... mic-era law, ... Criminal ...

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Primary Qualifying Tests

- Full or partial shutdown due to mandatory executive order
 - Must be a mandatory order that suspended operations in non-nominal way
- Significant decline in gross receipts in 2020 or 2021
 - Decline of 50% for 2020 and 20% for 2021 when compared to similar quarters in 2019

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Maximum Credit

- Max credit is \$5,000 per employee for 2020 and \$7,000 per quarter per employee for 2021. The max credit per employee is \$26,000.
- ERC and the PPP
 - Prior to November 2021, businesses had to select one or the other.
 - After November 2021, both were available.
 - Can't use the same qualified wages for both programs

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ERC & PPP

- ERC and the PPP
 - Proper calculation allocates enough wages for full PPP forgiveness
 - The SBA and IRS have not indicated if they cross-report wage data

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ERC Qualification

- Determine qualification period and total qualified wages.
- Qualified wages are wages paid to W-2 employees.
- Employee paid health insurance and 401(k) contributions also apply.
- Aggregate any businesses that share 50% common ownership.
- Remove wages paid to owner(s) and their family members.
- Determine if business is a recovery start-up business.

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Claiming the ERC

- File amended 941X for qualifying quarters.
- IRS issues separate refund checks for each quarter.
- Historically, no due diligence was done by IRS before issuing refunds.
- Amend 2020 and 2021 income tax return to reduce payroll deduction.
- Deadlines to file:
 - 2020 Tax Year – April 15, 2024
 - 2021 Tax Year – April 15, 2025

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Rise of Third-Party Providers

- Following the change to allow businesses to claim the ERC and PPP, third-party providers began pursuing claims.
- These businesses began aggressive marketing campaigns targeting businesses through mail, phone, email and radio and TV ads.
- Many charged contingency fees as high as 50%.
- Many had little or no connection to tax preparation or tax law.
- Often, they did calculations without CPA or attorney input.

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False Claims

- Many encouraged businesses to make false claims based on the following:
 - Supply chain interruptions
 - Social distancing or other CDC/OSHA recommendations
 - Broad and overly general executive orders
 - Improperly allocated wages
 - Incorrect qualifications based on ownership

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7 Suspicious Signs

- According to the IRS, your ERC claim could be incorrect if:
 1. Too many quarters are claimed.
 2. Government orders don't qualify.
 3. Too many employees and wrong calculations
 4. Business citing supply chain issues.
 5. Business claiming ERC for too much of a tax period.
 6. Business didn't pay wages or didn't exist during eligibility period.
 7. Relying on promoters advising: "you have nothing to lose."

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Where do we Stand Now?

- Heavy IRS activity
 - #1 on 2020 Dirty Dozen List
 - Moratorium on processing new claims
 - Beginning in October 2023, no new claims were processed.
 - Moratorium in new claims extended indefinitely.
 - Heightened due diligence requirement on new claims

Continued

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IRS wraps up 2023 Dirty Dozen list; reminds taxpayers and tax pros to be wary of scams and schemes, even after tax season

Some items on this year's list were new and some made a return visit. While the list is not a legal document or a formal listing of agency enforcement priorities, it is intended to alert taxpayers and the tax professional community about various scams and schemes.

Many of these schemes peak during filing season as people prepare their tax returns. In reality, these scams can occur throughout the year as fraudsters look for ways to steal money, personal information, data and more.

To help people watch out for these scams, the IRS and the Security Summit partners are providing an overview recapping this year's Dirty Dozen scams.

"Scammers are coming up with new ways all the time to try to steal information from taxpayers," said IRS Commissioner Danny Werba. "People should be wary and avoid sharing sensitive personal data over the phone, email or social media to avoid getting caught up in these scams. And people should always remember to be wary if a tax deal sounds too good to be true."

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Where do we Stand Now?

- Increased processing time for new claims
- Voluntary Disclosure Program (VDP) through March 22, 2024
 - \$225 million returned with another 800 submissions in process
- \$1 billion in ERC claims denied by IRS during moratorium as of March 15, 2024
 - \$225 from VDP; \$251 from withdrawal process; \$572 from improper claim assessments
- \$3 billion in ERC claims in review by IRS criminal investigation

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Where do we Stand Now?

- Possible early sunset of ERC program
 - Bill working through Congress and a request from Commissioner Werfel to end program.
 - IRS request to extend audit period of 941s associated with ERC claims
 - Expected high levels of audit and criminal prosecution for businesses and promoters
 - Likely involvement of other federal agencies
 - Possible DOJ involvement with criminal cases

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Third-Party Prepared Claims

- If third party prepared claim, consider the following:
 - Gather and review contract from beginning of engagement.
 - Request detailed calculation information including wages and applicable ERC periods.
 - Request governmental orders and any narratives regarding how they apply to the business.

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Third-Party Prepared Claims

- Request narratives for any other criteria that was used to qualify the business.
- It is better to do these things before an audit and while the claim for the ERC is relatively recent.
 - It may be much harder to gather the documentation later.

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What can be Done Today?

- What can businesses and accountants do today?
 - Begin assembling package before potential audit.
 - Wages, 941 and 941X returns
 - Executive orders used to qualify
 - Any other supporting documentation

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What to Consider

- If you have any questions about whether a business qualifies, seek a second opinion from a third party with significant technical experience with the ERC program.
 - A second opinion can be done at a relatively low cost and will identify any issues in time to potentially resolve them with minimal or no penalties.
- Once the IRS begins an audit of an ERC claim, they will likely not waive penalties and interest if they deem the claim to be improper.
- A second opinion can help evaluate the claim to make correction before a potential IRS audit when less options will be available.

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Questions?




Joseph A. Peterson
 (248) 433-7158
 jpeterson@plunkettcooney.com

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Webinar Registration - Surviving an IRS Employee Retention Credit Audit

04/25/2024

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PRACTICE AREAS
Business Tax Controversy
Employee Retention Credit
Compliance
Tax Law



Date: April 25, 2024
Time: Noon to 1 p.m.
Cost: Complimentary

Since the start of the COVID-19 pandemic in 2020, businesses have applied for and received billions of


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