

NOTICE – This article has not been updated to reflect new legislation passed by Congress on December 21, 2020. That legislation could significantly affect the content of this article. We plan to update this article during January 2021 to reflect the impact of the new legislation.

PPP Loan Not Right for Your Organization? The Employee Retention Credit Might Be – And It Could Be Improving

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Nonprofit organizations that have decided not to apply for a Paycheck Protection Program (PPP) loan or that have returned PPP loan funds should evaluate the Employee Retention Credit (ERC).

The ERC is a relief provision contained in the CARES Act passed into law on March 27, 2020, and under current law, it is not available to PPP loan borrowers. According to PPP loan guidance issued by the SBA on May 5, 2020 in the form of FAQ #45, a PPP borrower that returned its PPP loan funds prior to the SBA's safe harbor date of May 18 will be treated as though the borrower had not received a PPP loan for purposes of the Employee Retention Credit.

Following is our firm's summary of the Employee Retention Credit:

1. Provides eligible employers – including tax-exempt organizations – a refundable credit against the employer's share of payroll taxes. (As described below, the fact that it is a refundable credit means that it is simply money from the government – if the amount of the credit exceeds the employer's share of payroll taxes against which it is a credit, the organization receives a refund of the excess credit amount.)
 - a. Eligible employers must have carried on a trade or business during 2020 and satisfy one of two tests (for tax-exempt organizations described in Section 501(c) of the Internal Revenue Code, all operations of the organization are considered a trade or business for this purpose)
 - Have fully or partially suspended business operations during any calendar quarter of 2020 due to orders from a governmental entity limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes)
- or**
- Experience a reduction in gross receipts of at least of at least 50%:
 - In any calendar quarter of 2020 as compared to the same calendar quarter of 2019
 - And continuing through the end of the first subsequent calendar quarter of 2020 for which gross receipts exceed 80% of the amount for the corresponding quarter of 2019. (If, after declining by more than 50% in a

quarter, gross receipts do not increase for any subsequent quarter in 2020 to more than 80% of the amount for the corresponding quarter in 2019, the credit continues through the end of 2020.)

- Example: Employer A'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, Employer A's 2020 first, second, and third quarter gross receipts were approximately 48 percent, 83 percent, and 92 percent of its 2019 first, second, and third quarter gross receipts, respectively. Accordingly, Employer A 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 percent of the same quarter in 2019) and ending on the last day of the second calendar quarter of 2020 (the first subsequent quarter in 2020 for which the gross receipts were more than 80 percent of the amount in the same quarter in 2019). Thus, Employer A is entitled to a retention credit with respect to the first and second calendar quarters.
2. The credit is 50% of the first \$10,000 in wages per employee (including the value of qualified health plan benefits).
 - Note – wages for purposes of the ERC are generally FICA wages...clergy compensation is not ordinarily FICA wages.
 3. The credit is reduced by any credits claimed for emergency sick pay or emergency family leave pay under FFCRA ([see separate Alert on FFCRA](#)).
 4. To the extent the credit exceeds the employers' Social Security tax due, the excess is considered a refundable overpayment.
 5. For employers with an average of more than 100 full-time employees in 2019, only wages paid to employees for periods during which they are not currently providing services due to an economic hardship (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) are eligible for the credit. **For eligible employers with an average of 100 or fewer full-time employees in 2019, all wages paid to employees during a period of economic hardship (as defined above) are eligible for the credit.**
 - Aggregation of employee counts of affiliated entities may be required.
 - Employee counts are made using the methods applicable under the Affordable Care Act in determining whether an employer is an "applicable large employer." (Note that only the counting method is applicable...the employee count thresholds for the Employee Retention Credit are unrelated to the thresholds for the Affordable Care Act.)
 6. The employee retention credit is effective for wages paid after March 12, 2020, and before January 1, 2021.

7. An employer who obtains a Paycheck Protection Program loan is not eligible for this credit under current law.

The Internal Revenue Service provides an extensive list of FAQs related to the Employee Retention Credit – available [here](#).

Observations for Churches, Schools, and Other Organizations Subject to Mandatory Suspension of Group Meetings

Thankfully, few churches, schools, and charities have experienced revenue declines in a calendar quarter in excess of 50% - so that aspect of eligibility has limited application. We note, however, that churches, schools, and other organizations that were subject to mandatory full or partial suspension of operations or group meetings that did not obtain a PPP loan (or if they did, that returned the funds by May 18, 2020) seem to be eligible for the Employee Retention Credit regardless of whether they were able to continue carrying on certain of their activities via remote participation. While available IRS guidance does not specifically address this scenario, a straight reading of the law seems to support such an interpretation.

Applying this interpretation would require the organization to evaluate whether it had “operations that were fully or partially suspended 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.” Such a determination may not be easy to make in every instance, since certain safety protocol communications made by government officials or agencies may not have reached the level of authority of “orders.” Additionally, language in the IRS FAQ document (FAQ #33) states that if the “employer is able to continue operations comparable to its operations prior to the closure by requiring its employees to telework, the employer’s operations are not considered to have been fully or partially suspended as a consequence of a governmental order.” While it may be tempting to assume that such language means that churches that offered virtual worship services were able to “continue operations comparable to its operation prior to the closure,” we would argue strongly that such is not the case. Not only are virtual worship services not comparable to regular in-person worship meetings, most churches stopped other significant aspects of their operations in addition to in-person worship services...such as children’s ministries, Sunday Schools, fellowship events, and more. Similarly, even though schools may have continued conducting classes online, many other school functions were stopped...including athletics and other extracurricular activities. Our firm believes that, until and unless additional official contrary guidance is published, the position we have described herein with respect to churches and schools is reasonable.

Assuming the IRS agrees with the interpretation described in the preceding paragraph, the Employee Retention Credit could represent a significant financial benefit to churches, schools, and other entities required to suspend group meetings – particularly those with 100 or fewer full-time employees in 2019. The reason is that for such organizations, the credit is half of the first \$10,000 in wages paid to all of their employees during the applicable period, regardless of whether such employees are providing services for the organization or not. That treatment contrasts dramatically with the treatment of organizations with more than 100 full-time employees in 2019. For those organizations, the credit is half of the first \$10,000 in wages paid during the applicable period only to employees while they are not currently providing services to the organization.

Example – Church with 85 Full-Time Employees in 2019 and 2020

Oak Church did not obtain a PPP loan. It had 85 full-time employees in 2019 and 2020 and no part-time employees. On March 15, 2020, Oak Church was ordered by government officials to stop holding in-person worship services. That mandate continued through May 31, 2020, at which time government officials permitted the church to hold limited-capacity worship services. The mandate for limited capacity worship services continued through December 31, 2020. Oak Church continued to pay all of its employees for the entire time during which in-person worship services were prohibited or limited. Ten of its employees (other than clergy) performed no services for Oak Church during the period from March 15 through May 31, 2020 (due to government orders to cease holding worship services), but were paid nonetheless. During the period from March 15, 2020 through December 31, 2020, Oak Church paid its 85 employees \$42,000 each in wages (including qualified health plan benefits). Half of the first \$10,000 of wages paid to each of its employees during the applicable period is \$5,000 per employee. Oak Church is entitled to an Employee Retention Credit of \$425,000 (85 x \$5,000). The credit is refundable. To the extent that the credit exceeds Oak Church's employer Social Security tax due on its Form 941s for the applicable quarters of 2020, Oak Church will receive a refund of the excess.

[Note that if Oak Church had an average of more than 100 employees in 2019, the credit would apply only with respect to the wages paid to the 10 employees who did not provide services and only during the period in which they were paid while not providing services. As mentioned above, we note that churches, schools, and other organizations that were subject to mandatory full or partial suspension of operations or group meetings seem to be eligible for the Employee Retention Credit regardless of whether they were able to continue carrying on certain of their activities via remote participation. While available IRS guidance does not specifically address this scenario, a straight reading of the law seems to support such an interpretation. Assuming the IRS agrees with the interpretation described in the preceding paragraph, the Employee Retention Credit could represent a significant financial benefit to churches, schools, and other entities required to suspend group meetings – particularly those with 100 or fewer full-time employees in 2019.]

Possible changes to the Employee Retention Credit

Congress is considering legislation that would both increase and broaden the Employee Retention Credit. Proposals under consideration include significantly increasing the amount of the credit and making it available to employers regardless of whether they obtained (or kept) a PPP loan. We will be closely monitoring these developments and will report any significant changes to this significant credit.

We're here to help!

If you would like assistance evaluating the Employee Retention Credit for your organization, please let us know. Our team of highly experienced tax professionals will be glad to help! You may contact us at C19taskforce@nonprofitcpa.com.

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