# IRS Warns About Employee Retention Credit Schemes

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The IRS on October 19 issued IR-2022-183, warning employers to be wary of promotions for the employee retention credit (ERC) that sound too good to be true. According to the IRS, some third-party firms are taking aggressive or improper positions when it comes to determining eligibility for and calculating the credit. While accepting these offers to prepare ERC claims -- often on a contingent fee basis -- appears to be low risk to the employer, the IRS emphasized that taxpayers, not the promoter or consultant, are always responsible for the information reported on their tax returns.

**Insight**
Taking a position that is contrary to previously issued IRS guidance will likely result in the IRS denying the claim or pursuing repayment of the ERC, along with penalties and interest.

**Employee Retention Credit Eligibility**
The controversy regarding eligibility often stems from two questions: whether the employer was affected by orders from an appropriate governmental authority and which employees were able to perform services, even from a remote location. Some of the more aggressive positions seem to consider every business as being affected.

To be eligible for the ERC, employers must have:

- Sustained a full or partial suspension of operations due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings due to COVID-19 during 2020 or the first three quarters of 2021;
- Experienced a significant decline in gross receipts during 2020 or a decline in gross receipts during the first three quarters of 2021; or
- Qualified as a recovery startup business for the third or fourth quarters of 2021. As a reminder, only recovery startup businesses are eligible for the ERC in the fourth quarter of 2021.

**Insight**
Early Information Document Requests from the IRS requesting substantiation of ERC claims are requiring detailed records of the specific government order and proof of its impact on the taxpayer. Taxpayers' narratives about the impact, alone, are not sufficient proof to support the claim.

**Miscellaneous Reminders**
Remember that wage deductions claimed on the federal income tax return must be reduced by the amount of ERC. This reduction is required for the year the wages were paid, not the year in which the ERC

claim is filed or received. If the business filed an income tax return deducting qualified wages before it filed an employment tax return claiming the credit, the business should file an amended income tax return to correct any overstated wage deduction.

Also, the wages eligible for the ERC must be coordinated with wages that were reported as payroll costs in obtaining PPP loan forgiveness or that were used to claim certain other tax credits. While both ERC and PPP loan forgiveness can be obtained by the same taxpayer, the same wages cannot be used for both purposes.

**Insight**

The IRS has been harshly criticized by the Inspector General, Congress, the AICPA, and the general public for delays in processing pandemic relief benefits. Some reports state that additional manpower has been added to the task of processing ERC claims. Personnel have been specially trained to review and process the ERC claims. In some cases, the claim will be referred for examination and additional verification before the payment is made. Pursuant to the American Rescue Plan Act, the IRS has up to five years to make an assessment of any amount attributable to ERC for the third and fourth quarters of 2021 instead of the normal three-year statute of limitation.