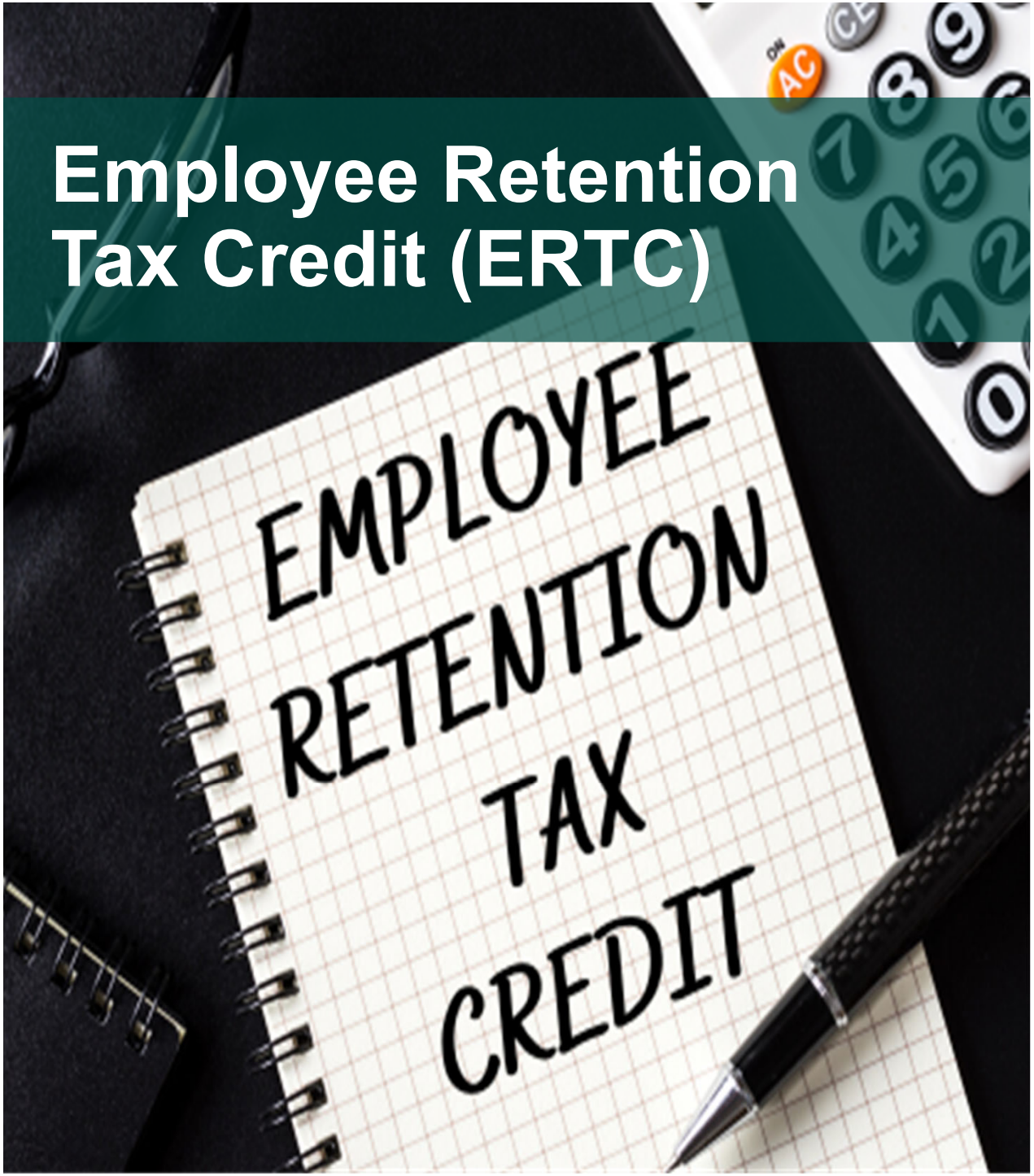
Employee Retention Tax Credit (ERTC)



Presenters:
Carlo Ferri
Director, Tax Strategies,
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John Dorsey
Partner,
Davis Bucco Makara & Dorsey

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Disclaimer

The information enclosed in the handout today is based on the guidance that has been published as of February 23, 2021. It is expected that additional guidance will be forthcoming from the IRS and SBA that could render some of this material inapplicable. This material should not be used as tax advice in making decisions in your business.

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Agenda

1. Overview of the ERTC
2. Evaluating eligibility
3. Discussion of shut-down orders
4. Calculation of the credit
5. Questions

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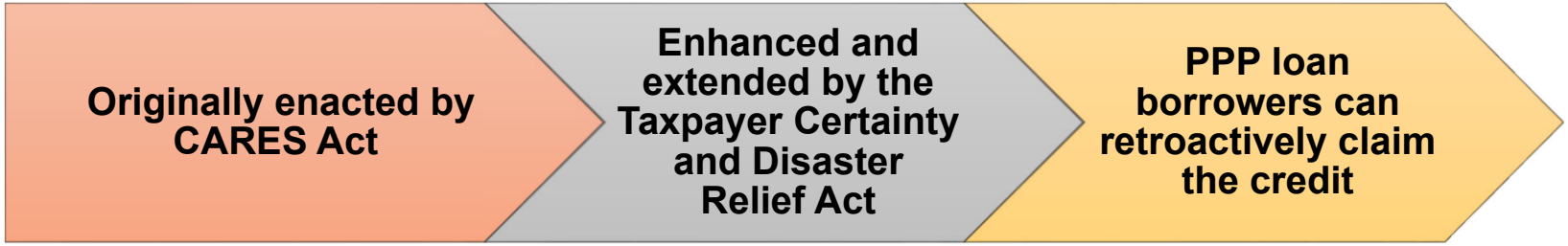
History of the ERTC



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What is the Employee Retention Tax Credit?

- The Employee Retention Credit is a **fully refundable payroll tax** credit for employers equal to 50 percent **(2020)** or 70 percent **(2021)** of **qualified wages** (up to a $10,000 cap) that **Eligible Employers** pay their employees.
- The maximum credit amount with respect to **EACH EMPLOYEE** is $5,000 **per year (2020)** or $7,000 **per quarter (2021)**
- Businesses qualify based on a decline in gross receipts or full/partial shutdown of their business.
- The credit is based on wages paid after March 12, 2020, and before July 1, 2021.
- For-profit and tax-exempt organizations qualify.

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Opportunities for Contractors

- Shut-Down Orders
- Cancelled or delayed jobs
- Reduction in backlog
- Decline in Gross Receipts

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What Every Business Needs to Evaluate

1. Did your business experience a 50% reduction in gross receipts in any quarter of 2020 compared to the same quarter in 2019?
2. Was your business required to be partially or fully shut down under a state or local order at any time from March 12 to the present?
3. How many full-time employees did your business have in 2019?
4. Did your business experience a 20% reduction in gross receipts in the 4th quarter of 2020 compared to the 4th quarter of 2019?
5. Does your business anticipate a 20% reduction in gross receipts in the 1st quarter of 2021 compared to the 1st quarter of 2019?
6. Does your business anticipate a 20% reduction in gross receipts in the 2nd quarter of 2021 compared to the 2nd quarter of 2019?

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***Aggregation rules apply to commonly owned businesses (revenue decline, operations suspension and total number of employees)**

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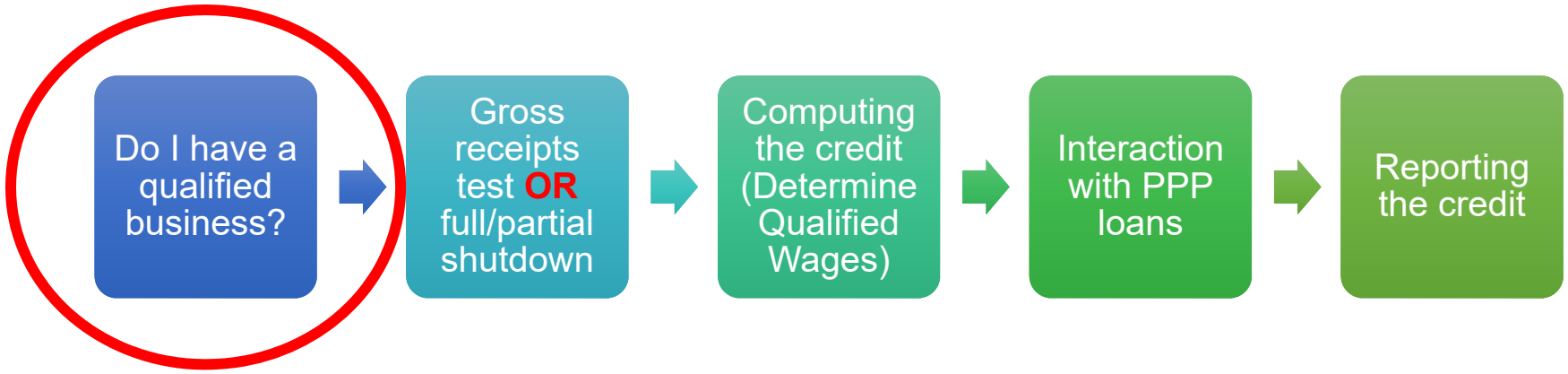
Steps in the Evaluation Process



*****Aggregation rules must be considered in determining:**
1. Gross receipts test
2. Full/partial shutdown
3. Total number of employees

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Do I Have a Qualified Business?

Employers that carry on a trade or business during calendar year 2020, including tax-exempt organizations, that **EITHER**:

Experience a **significant decline** in gross receipts during the calendar quarter;

OR

Fully or partially suspended their 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.

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Aggregation Rules

- Aggregated employers are treated as a single employer for purposes of:
  - Gross receipts test
  - Determining a full or partial shutdown
  - Total number of employees
- Aggregated under:
  - IRC Section 52(a)
    - Controlled group corporations (generally requires 50% common ownership)
    - Parent-sub, brother-sister, combined group
  - IRC Section 52(b)
    - Sole proprietorship, partnership, trust, or an estate
  - IRC Section 414(m) or (o)
    - Related entities for purposes of qualified retirement plans & other employee benefits
    - Includes A-Org, B-Org & management groups

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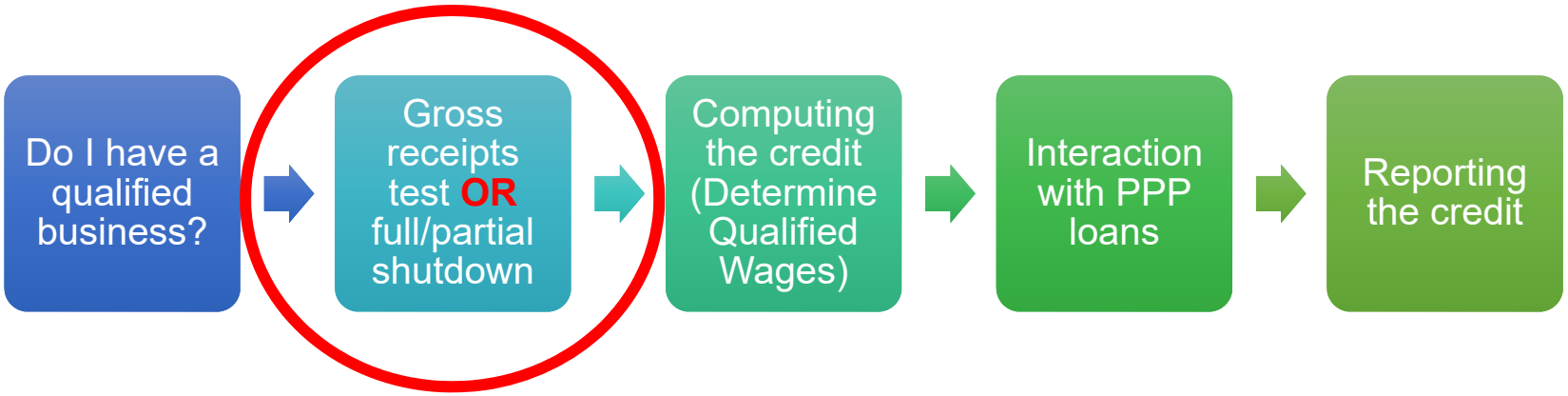

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What is Gross Receipts?

- Follows your **TAX reporting, not book**
- For-Profit Entity
  - Total sales (less returns and allowances)
  - Investment Income
    - Interest
    - Dividends
    - Rents
    - Royalties
    - Annuities
    - Capital transactions (less: adjusted basis in the assets sold)

Form **1120-S** — **U.S. Income Tax Return for an S Corporation** — OMB No. 1545-0123 — **2020**

Department of the Treasury
Internal Revenue Service

▶ Do not file this form unless the corporation has filed or is attaching Form 2553 to elect to be an S corporation.
▶ Go to *www.irs.gov/Form1120S* for instructions and the latest information.

For calendar year 2020 or tax year beginning , 2020, ending , 20

A S election effective date	TYPE OR PRINT — Name	D Employer identification number
B Business activity code number (see instructions)	Number, street, and room or suite no. If a P.O. box, see instructions.	E Date incorporated
C Check if Sch. M-3 attached ☐	City or town, state or province, country, and ZIP or foreign postal code	F Total assets (see instructions) $

G Is the corporation electing to be an S corporation beginning with this tax year? ☐ Yes ☐ No If "Yes," attach Form 2553 if not already filed
H Check if: (1) ☐ Final return (2) ☐ Name change (3) ☐ Address change (4) ☐ Amended return (5) ☐ S election termination or revocation
I Enter the number of shareholders who were shareholders during any part of the tax year ▶
J Check if corporation: (1) ☐ Aggregated activities for section 465 at-risk purposes (2) ☐ Grouped activities for section 469 passive activity purposes

Caution: Include **only** trade or business income and expenses on lines 1a through 21. See the instructions for more information.

Income				
1a	Gross receipts or sales	1a		
b	Returns and allowances	1b		
c	Balance. Subtract line 1b from line 1a		1c	
2	Cost of goods sold (attach Form 1125-A)		2	
3	Gross profit. Subtract line 2 from line 1c		3	
4	Net gain (loss) from Form 4797, line 17 (attach Form 4797)		4	
5	Other income (loss) (see instructions—attach statement)		5	
6	**Total income (loss).** Add lines 3 through 5 ▶		6	

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What is a Significant Decline in Gross Receipts?

•**2020 ERTC** – all of 2020

•**START**: The first calendar quarter in **2020** in which an employer's gross receipts are *less than* **50 percent of its gross receipts for the same calendar quarter in 2019**.

•**END**: The significant decline in gross receipts ends with **the first** calendar quarter following the calendar quarter where 2020 quarterly gross receipts are greater than 80 percent of its gross receipts for the same calendar quarter in 2019.

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DOES NOT have to be COVID-19 related

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Significant Decline in Gross Receipts – Example

2020 ERTC

Start: 50% decline comparable quarters 2020 to 2019

Stop: The quarter that follows the first calendar quarter in which a greater then 80% comparable quarter 2020 vs 2019

	2020 Gross Receipts	2019 Gross Receipts	Decline in Gross Receipts	
1st Quarter	500,000	550,000	9%	Does not qualify
2nd Quarter	265,000	555,000	52%	QUALIFY
3rd Quarter	500,000	565,000	12%	QUALIFY
4th Quarter	450,000	575,000	22%	Does not qualify

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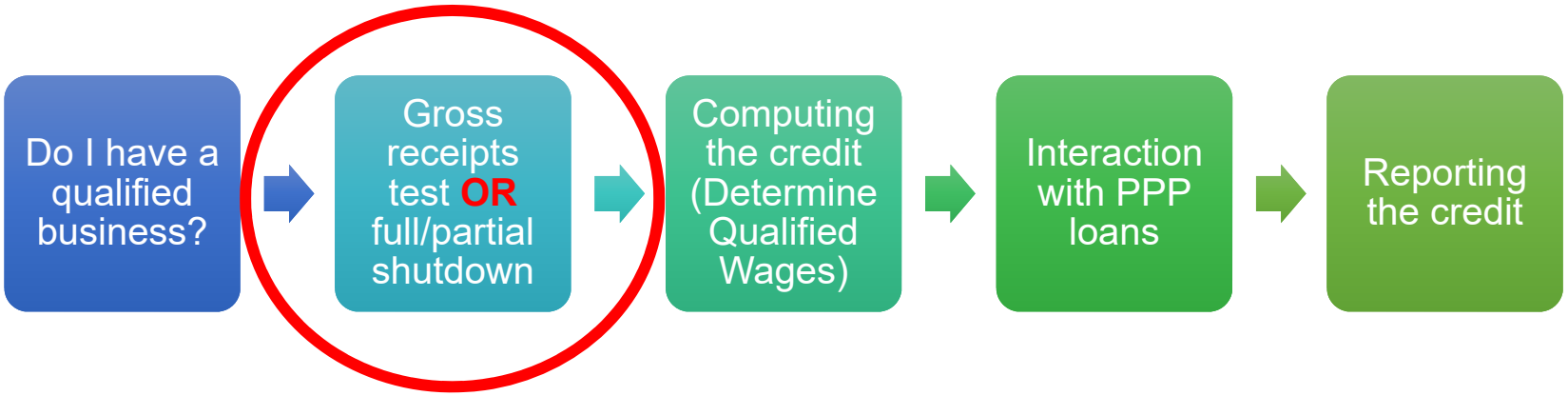

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1. Gross receipts test
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Who is an "Eligible Employer"

Businesses who:

1) Experience a **significant decline** in gross receipts during the calendar quarter; **OR**

2) **Fully or partially suspended** their 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.

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Orders That Trigger Partial or Full "Suspension"

"***orders from an appropriate government authority***"

- State Orders and Proclamations
- Municipals Orders
  - Closures for cleaning
  - Closure via curfew
  - Closure via 'stay at home order'

ARE THEY LAWFUL AND VALID?

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THE EVOLUTION OF THE "SHUTDOWN"

Pennsylvania

Effective March 23, 2020 – May 8, 2020 shutdown for "non-life sustaining" business shutdown subject to a "waiver" process.

PARTIAL OR FULL SUSPENSION

Depends on what you do

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Partial Shutdowns…more than nominal impact

- **New Jersey**
  - Effective March 24, 2020, construction projects may continue so long as businesses "***reduce staff on site to the minimal number necessary to ensure that essential operations can continue [. . .].".***
- **Pennsylvania**
  - Effective May 8, 2020 return to work subject to site staffing limitations.
- **Delaware**
  - Effective March 24, 2020 "life sustaining business" authorized to proceed.

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“Eligible Employer” Based On “Partial Suspension”

- An “Essential Service” may also be deemed “partially suspended” and therefore an “Eligible Employer” if:
  - Materials, supplies or equipment are unavailable to the “Essential” business do COVID-19 shutdown order;
  - Clients of “Essential” business are unable to access to services due to a shutdown order
  - One division provides “Essential” service, other does not

What if my workers are ‘shutdown’ due to CDC or DPH Orders?

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Partial Suspension – Multi-Location Employer

- Pennsylvania – “Non-life sustaining” – shutdown
- Maryland – Construction deemed “essential” – not shutdown
- New Jersey – Not shutdown but subject to limitations

PROJECTS IN DIFFERENT JURISDICTIONS CAN CREATE “ELIGIBLE EMPLOYER” STATUS

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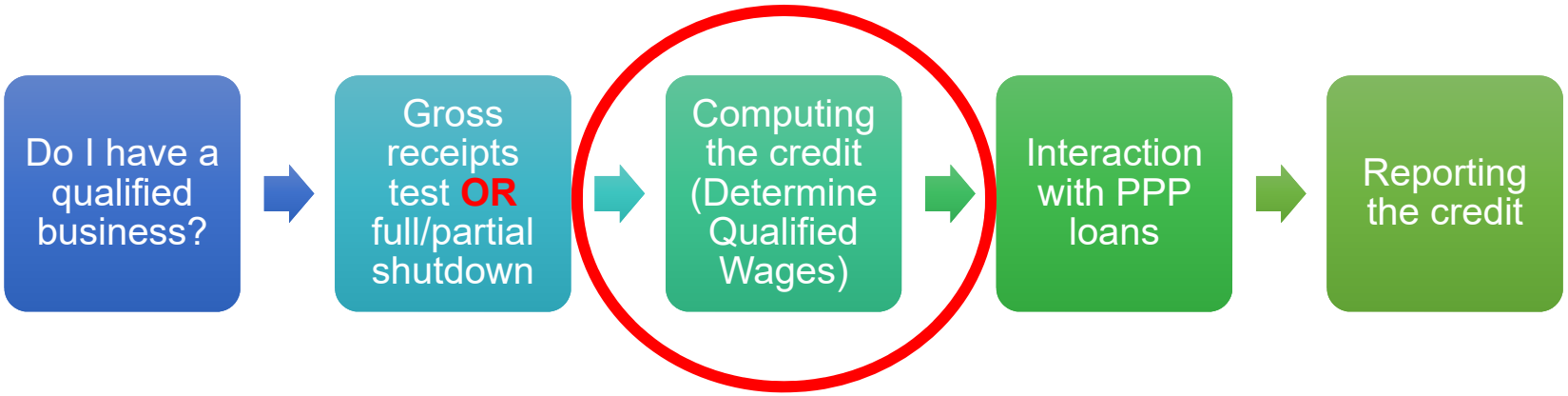

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What Are Qualified Wages?

- **2020 ERTC** – all of 2020
  - 100 or **FEWER** employees – **ALL** qualified wages paid to an employee
  - 100 or **MORE** employees – **ONLY** qualified wages paid to an employee for **NOT** providing services
- Computation of full-time employee is based on a monthly average of **2019 employees**
- The term "full-time employee" means an employee who, with respect to any calendar month in **2019**, worked an average of at least 30 hours per week or 130 hours in the month
- Generally, it is compensation paid by an eligible employer after March 12, 2020 and before July 1, 2021. Qualified wages also includes the Eligible **Employer's qualified health plan expenses** that are properly allocable to the wages.
- Related party compensation is excluded from qualified wages

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CANNOT use the same wages utilized in the PPP Loan forgiveness, FFCRA tax credits and WOTC Credits

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How to Calculate the Credit- EXAMPLE

- **2020 ERTC** – March 12, 2020 thru December 31, 2020
  - Employer N has two employees, Employee A and Employee B;
  - Employer N pays each employee $10,000 in qualified wages in the second quarter 2020; and
  - Employer N pays each employee $10,000 in qualified wages in the third quarter 2020

2020

	2020 Qualified Wages ***	2020 Credit
2nd Quarter	20,000	10,000
3rd Quarter	20,000	0

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*** Includes qualified health plan costs

What are “Services” Creating “Qualified Wages”

- Employers < 100 employees – All wages paid to employees are eligible
- Employers > 100 employees – Wages paid only to employees NOT providing services
- “Services” being considered “Qualified Wages” should consider:
  - Rules and policies applicable to payment for on-call, travel, and waiting time
  - ‘Donning and Doffing’
  - Be Consistent with what you treat as ‘payable’ wages in determining “Qualified Wages”

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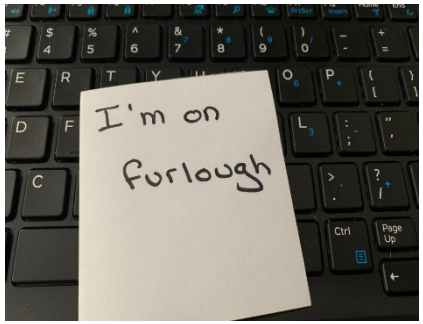
Employees Not Providing Services

- Furloughed Employees – only paying health insurance costs
- Stand-by labor
- Reduce pay but not providing services
- No change in pay but limited amount of services being provided



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2021 Enhancements

- Revise definition of significant decline in gross receipts
  - **20% reduction for 2021 vs 50% reduction for 2020**
- Credit increased to **70% for 2021 vs 50% for 2020**
- Qualified wages per employee increased
  - **$10,000 per quarter for 2021 vs $10,000 per year for 2020**
- Revise definition of qualified wages
  - **500 employees for 2021 vs 100 employees for 2020**
- Election to use prior quarter gross receipts to determine eligibility
- Extended credit through June 30, 2021

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What is a Significant Decline in Gross Receipts? – ENHANCEMENT

- **2020 ERTC** – all of 2020
  - Gross receipts decline by at least 50%

- **2021 ERTC** – 1/1/2021 thru 6/30/2021
  - Gross receipts decline by at least 20%
  - Compare Q1 2021 to Q1 2019
  - Compare Q2 2021 to Q2 2019

  - Special rule - Eligible Employers can elect to use the preceding quarter's gross receipts
    - Example – Compare Q4 2020 to Q4 2019 to determine Q1 2021 eligibility

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Significant Decline in Gross Receipts – EXAMPLE & ENHANCEMENT

2021 ERTC – Start: 20% decline; Stop: 20% decline

EXAMPLE 1

	2021 Gross Receipts	2019 Gross Receipts	% Decline in Gross Receipts	
2021 1st Quarter	400,000	555,000	28%	QUALIFY
2021 2nd Quarter	545,000	555,000	2%	QUALIFY (Lookback Election)

EXAMPLE 2

	Gross Receipts	2019 Gross Receipts	Percentage of Prior Year	
4th quarter 2020	400,000	555,000	28%	
1st quarter 2021	555,000	555,000	0%	QUALIFY (Lookback Election)

What Are Qualified Wages? – ENHANCEMENT

- **2020 ERTC** – all of 2020
  - **100** or FEWER employees - **ALL** wages paid to an employee
  - **100** or MORE employees - **ONLY** wages paid to an employee for **NOT** providing services
- **2021 ERTC** – 1/1/2021 thru 6/30/2021
  - **500** or FEWER employees - **ALL** wages paid to an employee
  - **500** or MORE employees - **ONLY** wages paid to an employee for **NOT** providing services

  - Based on **2019** headcount

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What is the Employee Retention Tax Credit? - EXAMPLE & ENHANCEMENT

- **2021 ERTC** – 1/1/2021 thru 6/30/2021
  - Employer N has two employees, Employee A and Employee B;
  - Employer N pays each employee $10,000 in qualified wages in the first quarter 2021; and
  - Employer N pays each employee $10,000 in qualified wages in the second quarter 2021

2020

	2020 Qualified Wages ***	2020 Credit
2nd Quarter	20,000	10,000
3rd Quarter	20,000	0

2021

	2021 Qualified Wages ***	2021 Credit
1st Quarter	20,000	14,000
2nd Quarter	20,000	14,000

*** Includes qualified health plan costs

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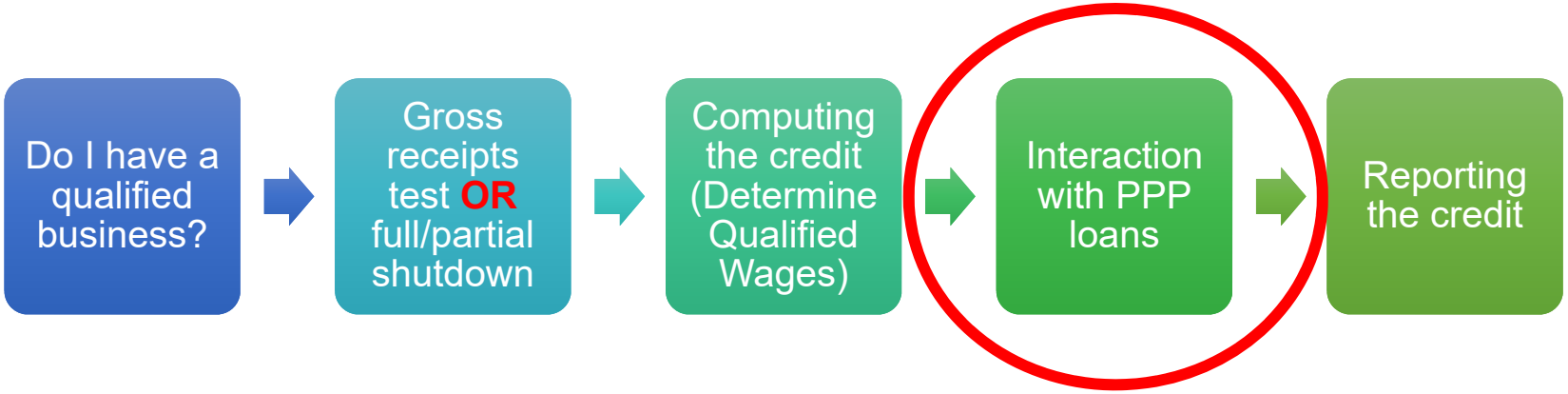

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*****Aggregation rules must be considered in determining:**
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Interaction with PPP Loan Forgiveness

Limitations
• Payroll costs funded by forgiven PPP loans are not eligible for the ERC • ERC qualified wages cannot be considered payroll costs that are eligible for PPP forgiveness

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Interaction with PPP Loan Forgiveness

- Due to CAA changes, an employer can support the PPP Loan using any period of time within the PPP period (April 1 – December 31, 2020), not just 8 or 24 weeks

- Most borrows received PPP funds in April (Round 1) or May (Round 2), while the most government shut-down orders were issued starting mid-March through May; so, there may be a period of time when operations were partially/fully shut down before the PPP loan “covered period”

- If total wages are significantly higher than the PPP loan amount, there is likely still an ERC benefit during the PPP timeframe

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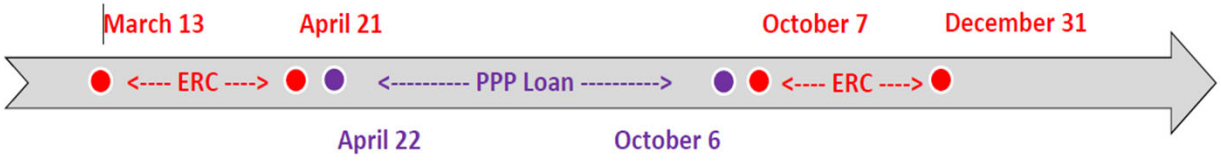

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Interaction with PPP Loan Forgiveness

- If a borrower has not yet applied for forgiveness for PPP loan forgiveness, borrowers may want to allocate the maximum permissible amount of non-payroll costs for PPP loan forgiveness. Up to 40% of PPP funds can be used for non-payroll costs.

- Consider the forgiveness period (8 weeks vs 24 weeks or anything in between) and the impact on eligible wages.

- Documentation is needed to show that a company is not using the same wages for both PPP forgiveness and the ERC.

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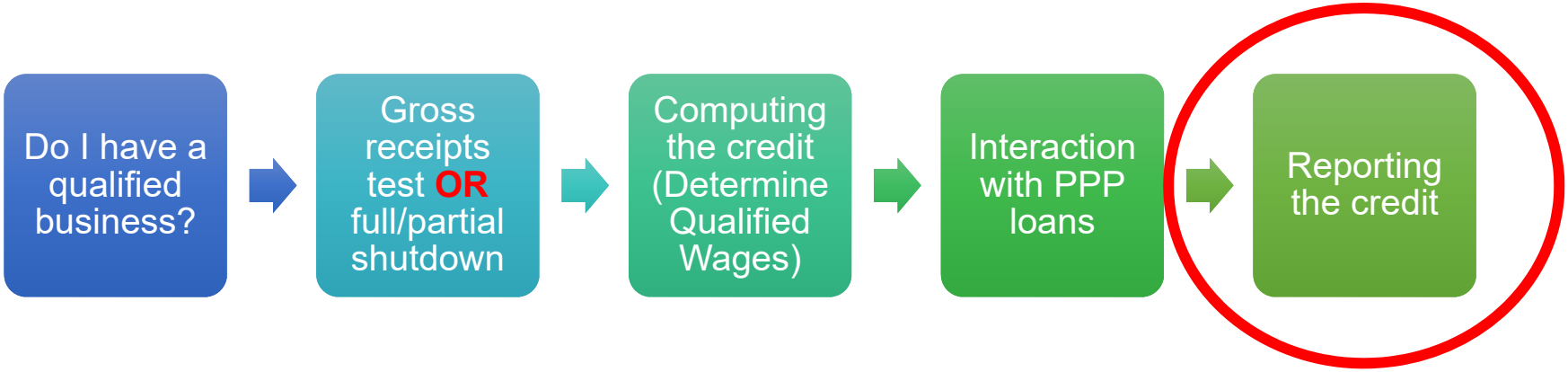

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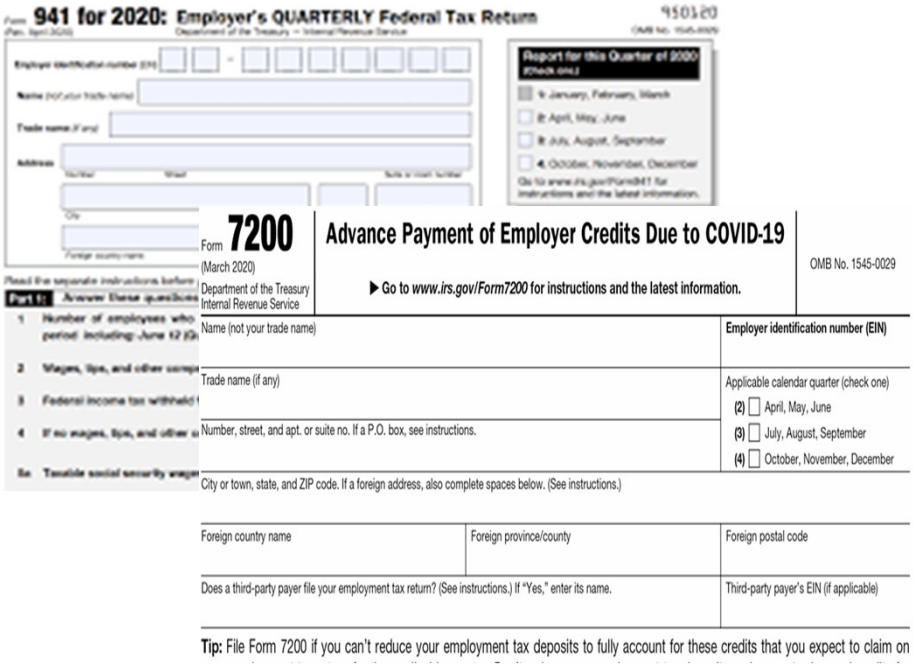
How Do I Receive My Credit?

- Employers can reduce deposits of employment taxes for federal income tax withheld from employees, Social Security and Medicare taxes of employees and employer
- Claim on form 941
- File form 7200
- Guidance forthcoming on Advance Credit-Draft Form 7200


941 for 2020: Employer's QUARTERLY Federal Tax Return

Form 7200 (March 2020) Department of the Treasury Internal Revenue Service

Advance Payment of Employer Credits Due to COVID-19

▶ Go to www.irs.gov/Form7200 for instructions and the latest information.

OMB No. 1545-0029

Name (not your trade name) | Employer identification number (EIN)

Trade name (if any) | Applicable calendar quarter (check one)

(2) ☐ April, May, June

Number, street, and apt. or suite no. If a P.O. box, see instructions. | (3) ☐ July, August, September

(4) ☐ October, November, December

City or town, state, and ZIP code. If a foreign address, also complete spaces below. (See instructions.)

Foreign country name | Foreign province/county | Foreign postal code

Does a third-party payer file your employment tax return? (See instructions.) If "Yes," enter its name. | Third-party payer's EIN (if applicable)

Tip: File Form 7200 if you can't reduce your employment tax deposits to fully account for these credits that you expect to claim on

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QUESTIONS?

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Contact the Presenters

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Carlo has a wide range of experience providing tax and business advisory services to privately-held companies in various industries including manufacturing, distribution, and construction. He advises owners and key executives through the various cycles of their business related to corporate and individual tax matters (i.e., growth, maturity, exit) and represents them in front of the IRS.

Carlo specializes in tax compliance and strategic planning. As the firm's Construction Industry Group Co-Leader, he forms relationships with and educates construction companies and trade organizations in the region on tax matters that impact the industry and their businesses. Carlo's extensive experience in business and tax-related topics has earned him the opportunity to present at external industry events on a regular basis. He also oversees the firm's internal tax training programs.

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Contact the Presenters

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John is a partner of Davis Bucco Makara & Dorsey, with nearly twenty years of litigation and transactional experience in Pennsylvania, New Jersey and Massachusetts. His practice focuses on construction, real estate and commercial matters. John comes to Davis Bucco after previously serving as in-house counsel at the Keating Building Company and the Tutor Perini Corporation where he managed over $1 billion in subcontractor procurement as well as owner-contractor agreement negotiations, public procurement, litigation and corporate matters.

John, in addition to construction litigation and transactional experience, has a background in zoning and land use as both a former public official and attorney. He has also represented clients on corporate formation and operation matters, including entities providing medical and other professional services. Additionally, John has extensive labor relations experience in negotiating project labor agreements, litigating ERISA/fringe benefit audit disputes, Unfair Trade Practices and other labor issues.

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