Restaurant Taxation: Calculating Tips and FICA Tip Credit; Food Donations, Sales Tax, and Employer Retention Credit

WEDNESDAY, JANUARY 5, 2022, 1:00-2:50 pm Eastern

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Restaurant Taxation: Calculating Tips and FICA Tip Credit; Food Donations, Sales Tax, and Employer Retention Credit

January 5, 2022

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Restaurant Taxation

January 5, 2022

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- A dedicated National Restaurant practice serving all concepts across all segments of the Restaurant Industry
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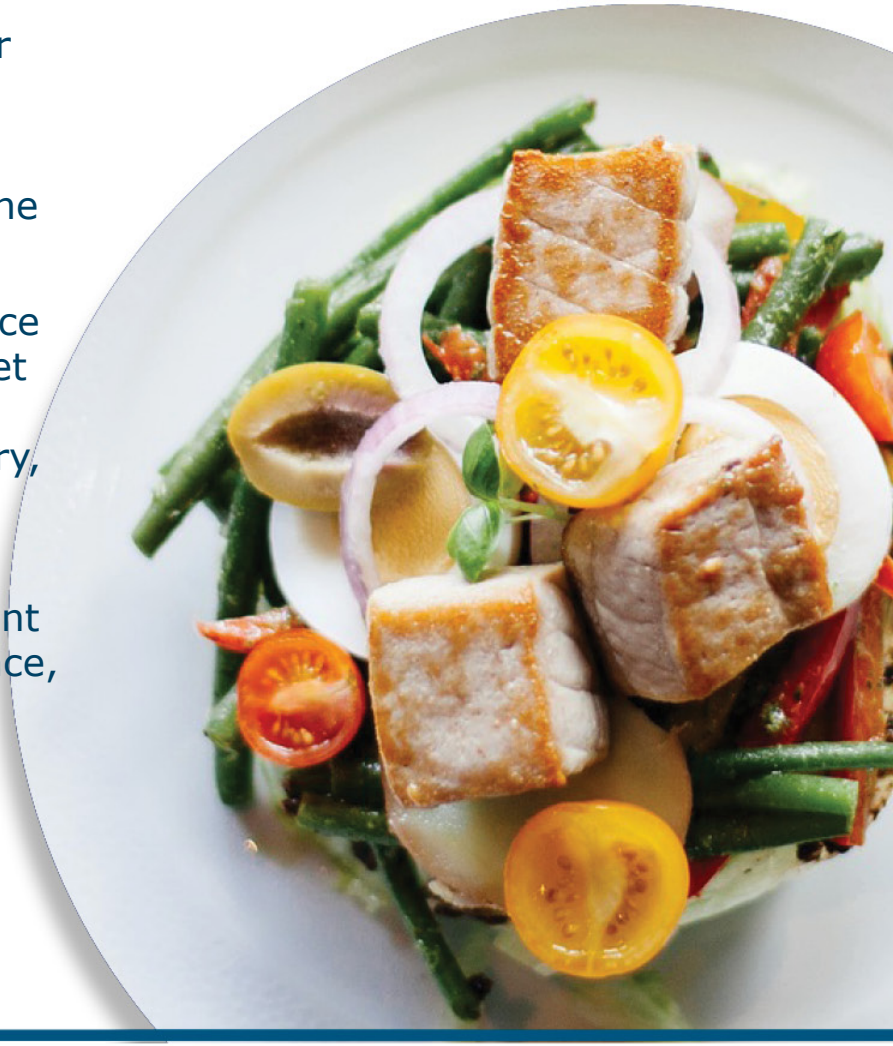
- GBQ is an active member of the Restaurant Industry in supporting the National Restaurant Association, Restaurant Leadership Conference, Restaurant Finance & Development Conference, Ohio Restaurant Association



Notes

This presentation is intended to make participants aware of tax issues that may apply to this audience.

Information presented herein is not intended to be tax advice.

Please consult with a qualified practitioner for tax advice related to specific transactions.

Agenda

- Restaurant Taxation: an Overview
- Reporting Tips
- FICA Tip Credit
- Food Donations
- Sales Tax
- Cost Segregation
- EIDLs, PPP Loans, RRF Status and Repayments
- Employee Retention Credit

Restaurant Taxation: An Overview

Restaurant Taxation: An Overview

The "3 Legged Stool" of Taxation

- **Income**
  - Defer – Accounting Methods, Gift Cards, etc.
- **Deductions**
  - Accelerate – Bonus/179 Dep, Smallwares, etc.
- **Credits**
  - Qualify – FICA Tip, WOTC

IRS Restaurants Tax Center

https://www.irs.gov/businesses/small-businesses-self-employed/restaurants-tax-center

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Restaurant Taxation: An Overview
(continued)

The "4 Legged Stool" of Taxation

- **Income**
  - Defer – Accounting Methods, Gift Cards, etc.
- **Deductions**
  - Accelerate – Bonus/179 Dep, Smallwares, etc.
- **Credits**
  - Qualify – FICA Tip, WOTC
- **Covid Considerations & Opportunities**
  - Qualified Improvement Property Fix
  - Paycheck Protection Program (PPP)
  - Employee Retention Credit (ERC)
  - Restaurant Revitalization Fund (RRF)
  - Sales/Use Tax Considerations

Reporting Tips

Navigating the Complex World of Gratuity

Reporting Tips

- Rev. Rul. 2012-18 provides guidance on determining whether a payment is a tip
- The Revenue Ruling provides that the absence of any of the following factors creates a doubt as to whether a payment is a tip and indicates that the payment may be a service charge:

  1) the payment must be made free from compulsion;
  2) the customer must have the unrestricted right to determine the amount;
  3) the payment should not be the subject of negotiation or dictated by employer policy; and
  4) generally, the customer has the right to determine who receives the payment.

- Tips are not wages

Reporting Tips

- The IRS has been aggressive in litigating tip-related issues and will likely become even more aggressive in this area.
- A gratuity charge automatically added to a customer's bill is a service charge that should be treated as wages, not a tip, if paid out to the wait staff and bartenders.
- Payments of service charges to employees must be paid through payroll as wages earned.
- Guests pay sales tax on a service charge, but not on a tip.
- Suggested gratuity calculations on Guest Checks are compliant.

Reporting Tips

- Employees must report tip income to the employer if they receive at least $20 per month in tips.
- This includes cash and charge tips collected by the employee, less any amounts paid to other employees.
- Employees must report their monthly tip income to the employer by the 10th day of the following month.
- Failure to report the tips may subject the employee to a penalty equal to 50% of the FICA taxes on the unreported tips.
- Restaurants are allowed to collect employee tip information electronically instead of on paper.

Reporting Tips

- The best way to record tips is to require employees to report their tips daily.
- Use of a point-of-sale computer system
- Form 4070A – *Employee's Daily Record of Tips* – and Form 4070 – *Employee's Report of Tips to Employer*
- The restaurant can create and use its own form for tip reporting as long as it includes the following:
  - Employee signature
  - Employee name, address and social security number
  - Employer's name and address
  - Time period covered and date reported
  - Total tips received

Reporting Tips

- **Large food and beverage establishments are required to allocate tips to employees whenever total reported tips fall below 8% of gross receipts from food and beverage sales.**
- Large food and beverage establishments have to test and potentially adjust the reported tips on an annual basis.
- Per Regs. 31.6053-3(i) and (j), a large food and beverage establishment is one that:
  - provides food and beverages for on-premises consumption,
  - where tipping is customary, and
  - that normally employed more than 10 employees on a typical business day during the preceding calendar year.

Reporting Tips

- The definition of a large food and beverage establishment specifically **excludes**:
  - Operations that have been open less than one month during any calendar year.
  - Fast food outlets and cafeterias where tipping is not customary.
  - Operations that derive at least 95% of their revenue from carryout service.
  - Establishments that enforce a service charge of at least 10%.

Reporting Tips

- Employers must file Form 8027 – *Employer's Annual Information Return of Tip Income and Allocated Tips* – and then report any allocated tips to the affected employees.

Form **8027**

Department of the Treasury
Internal Revenue Service

Employer's Annual Information Return of Tip Income and Allocated Tips

▶ See the separate instructions.
▶ Go to *www.irs.gov/Form8027* for instructions and the latest information.

OMB No. 1545-0714

2021

Check if:
Amended Return ☐
Final Return ☐

Name of establishment

Number and street (don't enter a P.O. box). See instructions.

City or town, state, and ZIP code

Employer identification number

Type of establishment (check only one box)
☐ 1 Evening meals only
☐ 2 Evening and other meals
☐ 3 Meals other than evening meals
☐ 4 Alcoholic beverages

Employer's name (see instructions)

Establishment number (see instructions)

Number and street (or P.O. box number, if mail isn't delivered to street address)

Apt. or suite no.

City, state, and ZIP code (if a foreign address, see instructions)

Does this establishment accept credit cards, debit cards, or other charges? ☐ Yes (lines 1 and 2 **must** be completed) ☐ No

1	Total charged tips for calendar year 2021	1	
2	Total charge receipts showing charged tips (see instructions)	2	
3	Total amount of service charges of less than 10% paid as wages to employees	3	
4a	Total tips reported by indirectly tipped employees	4a	

Reporting Tips

- If 8% of gross receipts exceeds the tips actually reported, the difference must be allocated among the tipped employees using one of the following methods:
  - good-faith agreement
  - gross receipts method
  - hours worked method (only available to restaurants that have fewer than the equivalent of 25 full-time employees during the period)
- Lastly, the employer reports the allocated tips on each employee's Form W-2.
- Remind all directly and indirectly tipped employees to report all tips.
- Audit your tip percentages and review if percentages are low.
- The IRS does offer two types of voluntary tip compliance agreements: Tip Rate Determination Agreements (TRDAs) and Tip Reporting Alternative Commitments (TRACs).

FICA Tip Credit

Navigating the Complex World of Gratuity

FICA Tip Credit

Who is eligible for the FICA Tip Credit? Under IRC §45B, a food and beverage establishment is allowed a credit for the amount of the employer's FICA tax obligation (7.65%) attributable to employee tips received for providing, delivering, or serving food or beverages.

However, no credit is given for tips used to meet the federal minimum wage rate.

- The Section 45B tax credit is determined on a minimum wage capped amount of $5.15 per hour, the rate in effect on January 1, 2007.

FICA Tip Credit

- The credit is claimed using Form 8846 - *Credit for Employer Social Security and Medicare Taxes Paid on Certain Employee Income* - and filed with your federal income tax return
- The credit is claimed as part of the General Business Credit under IRC §38 and is subject to the limitations of that code section.
- The FICA Tip Credit is non-refundable, which may reduce your regular income tax liability to zero, and is subject to the carryback and carryforward provisions for general business tax credits.

FICA Tip Credit

Form **8846**

Department of the Treasury
Internal Revenue Service

Credit for Employer Social Security and Medicare Taxes Paid on Certain Employee Tips

▶ Attach to your tax return.

▶ Go to *www.irs.gov/Form8846* for the latest information.

OMB No. 1545-0123

2021

Attachment Sequence No. **846**

Name(s) shown on return | **Identifying number**

Note: Claim this credit **only** for employer social security and Medicare taxes paid by a food or beverage employer where tipping is customary for providing food or beverages. See the instructions for line 1.

1	Tips received by employees for services on which you paid or incurred employer social security and Medicare taxes during the tax year (see instructions)	1	
2	Tips not subject to the credit provisions (see instructions)	2	
3	Creditable tips. Subtract line 2 from line 1	3	
4	Multiply line 3 by 7.65% (0.0765). If you had any tipped employees whose wages (including tips) exceeded $142,800, see instructions and check here ▶ ☐	4	
5	Credit for employer social security and Medicare taxes paid on certain employee tips from partnerships and S corporations	5	
6	Add lines 4 and 5. Partnerships and S corporations, report this amount on Schedule K. All others, report this amount on Form 3800, Part III, line 4f	6	

FICA Tip Credit

- Employers are responsible for withholding employee income tax and the employee's share of FICA taxes and paying the employer's share of FICA taxes on reported tips.
- The FICA Tip Credit allows employers to take a credit on a portion of the employer FICA taxes paid on the employee tips.
- Only tips received at establishments where tipping is a common practice qualify for the credit.
- **No "double-dipping"** - No deduction is allowed for any amounts used in computing the credit.

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Food Donation Deduction

Donation of Inventory

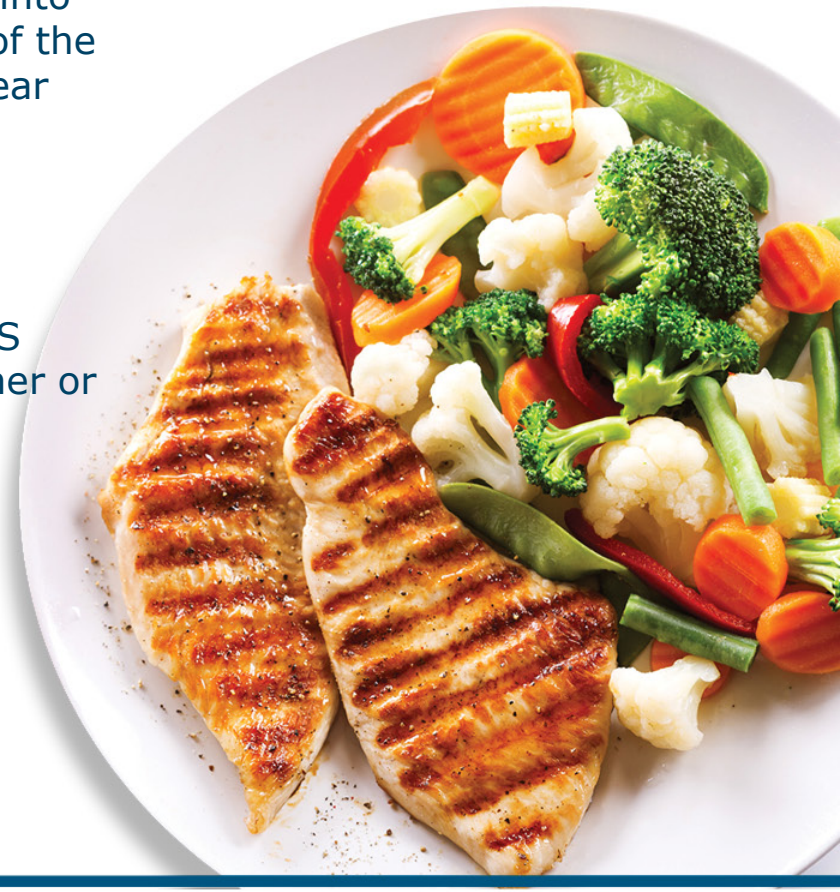
Food Donation Deduction

- A C-Corporation that makes a "qualified contribution" of inventory-type property to a charitable organization that uses it for the care of the ill, the needy, or infants in entitled to an enhanced, "above basis" deduction
- However, this qualified contribution rule applies to charitable contribution of food from any trade or business
  - Without regard to whether the contribution is made by a C Corporation, but
  - Only if the food is "apparently wholesome food"
- Thus, any trade or business, including S-Corporations, partnerships and sole proprietors, may make a donation of food inventory that will qualify for enhanced deductions

Food Donation Deduction
(continued)

Deduction Limit for *Non* C-Corporations

- The aggregate amount of contributions of apparently wholesome food that may be taken into account for the tax year may not exceed 15% of the taxpayer's aggregate net income for that tax year from all trades or businesses from which those contributions were made for that tax year, computed without regard to the charitable deduction for food inventory contributions
- In the case of contributions by partnerships or S corporations, the 15% limit applies at the partner or shareholder level, not at the partnership or corporate level



Food Donation Deduction
(continued)

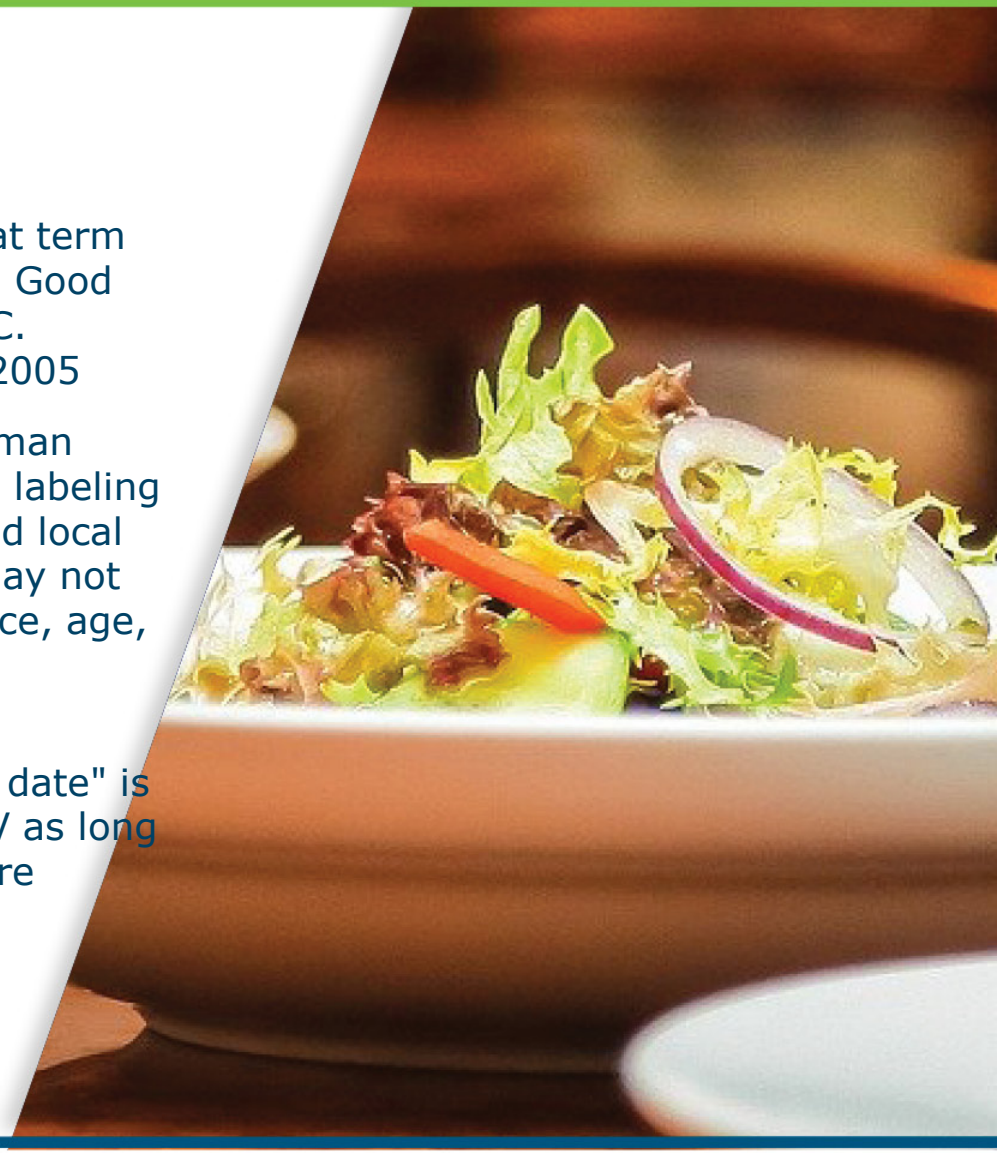
Deduction Limit for C-Corporations

- A C-Corporation's charitable deduction for contributions of food inventory is limited to 15% of its taxable income determined without regard to the deductions for charitable contributions
- For other corporate charitable deductions the 10%of taxable income limitation is reduced (but not below zero) by the contributions subject to the 15% limit

Food Donation Deduction
(continued)

Apparently Wholesome Food

- "Apparently Whole Food" was given that term by section 22(b)(2) of the Bill Emerson Good Samaritan Food Donation Act (42 U.S.C. 1791(b)(2)), as in effect on Sept. 23, 2005
- It must be food that is intended for human consumption that meets all quality and labeling standards imposed by federal, state and local laws and regulations, even though it may not be readily marketable due to appearance, age, freshness, grade, size surplus or other conditions
- Note: The food's "pull date" or "sell-by date" is therefore irrelevant in determining FMV as long as the quality and labeling standards are otherwise met.



Food Donation Deduction
(continued)

Enhanced Deduction

- A deduction is allowed equal to the lower of
  - The basis of the contributed property plus ½ of the ordinary income that would have been recognized if the property were sold for fair market value on the contribution date, or
  - Twice the basis of the property
- In order to qualify for the deduction, the organization may not transfer the food for money or other property or services and must provide a written statement that the donation complies with all requirements

Food Donation Deduction
(continued)

Non-Qualified Organizations

- In the event the donation is made to an organization that does not qualify under IRC §501(c)(3), the donation does not qualify for deduction under IRC §170
- Instead, such donation should be input into the restaurant's POS system as a "complimentary sale," which would reduce your gross sales but would not impact your net income
- The result is effectively an expense for the cost of the food that is donated

Sales Tax Update

Sales Tax Update

Economic Nexus

- All states (plus DC and AK localities) are enforcing some form of economic nexus on sales tax
  - Florida effective July 1, 2021
  - Missouri effective January 1, 2023
- Trends
  - Retroactivity – Trend is toward prospective enforcement
  - Movement away from transactional thresholds
  - Use tax notification requirements
  - Movement away from physical presence – Does economic nexus truly replace the physical presence test?
- Adjustment of nexus thresholds since initial legislation
- Restaurants should pay close attention to invoices from out of state vendors to confirm that sales tax is properly being charged

Sales Tax Update
(continued)

State Enforcement

- **General Information Letters / Technical Memoranda**
  - Administrative notice informing taxpayers of nexus thresholds and filing requirements
  - May provide information on registration and/or voluntary compliance
- **Nexus Questionnaires**
  - Provided directly to specific taxpayers
  - Use caution when completing
  - Non-response may trigger an audit or further inquiry
- **Desk Audits**
- **Lookback Period**
  - Economic nexus is prospective in majority of states
  - Measurement period for transaction/gross receipts thresholds
    - Current or prior calendar year
    - Trailing twelve months
    - "Expected" to reach threshold

Sales Tax Update
(continued)

Registrations

- Additional registrations required
- Carefully consider registrations where no taxable sales exist
  - Taxable sales vs. gross sales analysis
- "Business State Date" for registrations
- Registering as of a date in the future
- Beware of questions related to other tax types
  - Withholding
  - Income/Franchise Tax

Sales Tax Update
(continued)

Registrations (continued)

- Secretary of State Requirements
- Certificates of good standing
- Hard copy mailings with account numbers or access codes
- Beware of business start dates driving past due returns
- Member/Officer personal information
- Responsible party ramifications

Sales Tax Update
(continued)

Marketplace Facilitators

- Many states have enacted statutes requiring marketplace facilitators to collect and remit tax on behalf of sellers
- Applies whether facilitator takes title and makes sale or not
- Many large marketplace facilitators were collecting tax prior to or shortly after *Wayfair* decision
- Broad definition of "marketplace facilitator" reaching beyond traditional facilitators (Amazon, eBay, etc.)
- Opt-out clauses

Sales Tax Update
(continued)

Restaurant Industry Specific Issues:

- Third-party delivery services (Uber Eats, GrubHub, DoorDash)
  - Review contracts to understand marketplace facilitator responsibilities
  - Review state law to handle administration
  - Review with internal and external service providers
- Taxability of Prepared Food / Meals
- Food / Beverage / Alcohol / Meals taxes
- Tax base / "Price"
  - Delivery charges
  - Service fees / COVID surcharges
  - Discounts
  - Gratuities

Additional Considerations – Real Property

- **Real Property Construction Contracts**
  - Repairs, construction, or additions to real property
  - Contractor liable for sales or use tax on cost of materials incorporated into real property (does not charge sales tax to end customer)
- **Contracts to install tangible property / business fixtures**
  - Items that are attached or affixed to land, building, structure or land improvements that primarily benefits the business conducted on premises
  - Contractor will not pay sales tax or use tax when purchasing materials (purchases are for resale)
  - Contractor should charge and collect sales tax on invoice to customer calculated on materials, labor/installation, profit, mark-up and overhead

Sales Tax Update
(continued)

Additional Considerations – Real Property

- **Restaurant-Specific Real Property Issues**
  - Exhaust Hoods
  - Grease Traps
  - Walk-In Coolers/Freezers
  - Signage
  - Drive-Thru Window
  - Menu Boards
  - Security cameras (internal)
  - Specialty indoor and outdoor lighting
  - Window treatments
  - Repairs and maintenance (real property vs. equipment)

Sales Tax Update
(continued)

Additional Considerations – Restaurant Purchase Exemptions

- **State specific sales tax exemption include:**
  - Food preparation or preservation
  - Items used to clean food preparation or preservation equipment
  - Manufacturing
  - Utilities (e.g. electricity, gas and water used to prepare meals)
  - Repairs and maintenance on exempt equipment
  - Packaging
  - Items to comply with public health / pollution control (e.g. hair nets, gloves, etc.)
  - Resale
    - Non-reusable items (e.g. napkins; plastic eating utensils, etc.)
    - May includes items that may not leave restaurant with taxpayer (i.e. plates, silverware, tables, chairs)

Sales Tax Update
(continued)

Developing a Multistate Compliance Process

- Consider return compliance software vs. versus manual spreadsheet method
- Compliance/payment outsourcing
- Importance of filing calendars
- Consider local sales/use tax, especially in home-rule states

Sales Tax Update
(continued)

Accounting Groups and Tax Departments

- Increased cost of compliance
  - Assess current system capabilities to handle food service-specific taxes
- Increased internal resource requirements
- Possible need for increased headcounts and specific sales/use tax roles
- Tax Departments are not just for large companies anymore
- Interfacing with outsourced professionals
  - Data requirements and timing
  - Timely approvals
- Utilization of contractors

Cost Segregation

Accelerating fixed asset deductions

Cost Segregation

What is it?

- Cost Segregation is a strategic tax savings tool that allows companies and individuals who have constructed, purchased, expanded, or remodeled any kind of real estate to increase cash flow by accelerating depreciation deductions and deferring federal and state income taxes.
    - Acquired Property
    - New Construction
    - Remodeled Property
    - Build-outs
- Identify all construction-related costs that can be depreciated over shorter lives (Section 1245 property)

Cost Segregation
(continued)

Study Example

- $5 million Quick Service Restaurant
- Without a Cost Segregation Study, the building would be depreciated straight line over 39 years

With a Cost Segregation Study

$5M recovered over asset class lives

of $5 Million:
$750k over 5 Years
$500k over 15 Years
$3.75M over 39 Years

Increased Depreciation Deduction in the first year:
$1.25M
Projected NPV Benefits: $330k

Cost Segregation
(continued)

For Restaurants

- Different types of facilities yield different types of re-allocation results depending on what type of facility it is and what types of functions are being performed.
- Restaurant-type buildings provide an average re-allocation of 20-45%
- Section 1245 property
  - Decorative lights
  - Counters
  - Cabinets
  - Canopies & awnings
  - Plumbing fixtures, special piping
  - Special electrical wiring
  - Soft costs (architecture fees, permitting fees)

Cost Segregation
(continued)

For Restaurants (continued)

- Tenant improvements
- Build-outs
- Remodeling, Reimaging, Scrape & Build
- Cost Segregation studies can be done the year the assets are placed in service or in a later year
- If in a later year, Form 3115, Application for Change in Accounting Method, is filed to address the cost segregation
- Good Rule of Thumb: viable if building/improvement basis is > $500k (excluding land)

Cost Segregation
(continued)

For Restaurants (continued)

- Bonus depreciation can apply to reclassified items in a cost segregation study which augments the benefit
- Unused deductions carry forward
- When a building is sold, the taxpayer must recapture depreciation taken on personal property
  - Personal Property (Sec 1245) recapture is at ordinary tax rates
  - Therefore the hold period should be > 3 to 5 years
  - NOTE: Recapture can be avoid if classified as a Repair & Maintenance item

Cost Segregation
(continued)

Tax Cuts & Jobs Act – Bonus Depreciation

- Temporary 100% bonus depreciation is applicable for certain assets acquired and placed in service after Sept. 27, 2017 and before Jan. 1, 2023.
  - Rate phases down by 20% each year after that through 2026
  - Bonus is now available for used property
- Cost Seg Studies – personal property and land improvements are fully depreciated even for acquired buildings
- Consolidation of Qualified Leasehold Improvements, Qualified Restaurant Property, Qualified Retail Property
  - All replaced with Qualified Improvement Property "QIP" (beginning 1/1/2018)

Cost Segregation
(continued)

Tax Cuts & Jobs Act – Bonus Depreciation
(continued)

- **Qualified Improvement Property is defined as**
  - Sec. 1250 interior improvements to a non-residential property,
  - "Made by the taxpayer" after the building was originally placed in service
  - Non-structural in nature (internal structural framework)
  - Not an elevator or an escalator
  - Not an expansion of the building

Cost Segregation
(continued)

Tax Cuts & Jobs Act – Bonus Depreciation (continued)

- **CARES Act:**
  - Qualified Improvement Property technical correction "Restaurant/Retail Glitch"
    - 15-year class life, 100% bonus eligible
  - Net Operating Loss carryback provisions
    - 2018, 2019, or 2020 losses can be carried back five years
    - NOL limit of 80% Adjusted Taxable Income suspended to fully offset income
    - Can create larger NOLs using Form 3115, thus generating refunds
  - Planning Opportunities for Restaurants
    - Cost-benefit analysis of a cost seg study on any improvements placed in service
    - File Form 3115 and take the 481(a) adjustment in 2021
    - Results in a potentially large decrease in taxable income and generate NOL
    - Carryback the NOL going as far back as 2014 – only for years 2018, 2019 and 2020
    - Plan ahead

Update on EIDL, PPP and RRF

Update on EIDL, PPP and RRF

Economic Injury Disaster Loan (EIDL)

- First form of aid when COVID pandemic hit
- Latest program had a maximum loan amount of $2M fixed over 30 years at 3.75% for businesses and 2.75% for private non-profit organizations
- COVID-19 EIDL loan applications were accepted until December 31, 2021
- Borrowers can request increases up to their maximum eligible loan amount ***for up to two years after their loan origination date***, or until the funds are exhausted, whichever is soonest 11/19/21 SBA Release Number 21-110
- No new COVID related SBA loan programs at this time

Update on EIDL, PPL and RRF
(continued)

Paycheck Protection Program (PPP)

- PPP ended on May 31, 2021
- Existing borrowers may seek forgiveness
- Borrowers can seek forgiveness through term of their loan (2 or 5 years)
- Coordinate PPP and ERC to maximize both benefits

Update on EIDL, PPL and RRF
(continued)

Restaurant Revitalization Fund (RRF)

- Tax free grant to qualifying entities in the restaurant industry
- $28.6 billion in funds were exhausted
- Eligible expenses are broad: payroll, principal or interest on debt, rent, utilities, COGS, etc.
- Recipients are not required to repay the funding as long as funds are used for eligible uses no later than March 11, 2023
- Per IRS Notice 2021-49 "double dipping" permitted on wages for RRF and ERC for 2020 and Q1 & Q2 of 2021.
- Any organization that expends more than $750,000 in federal funds required to have a Single Audit performed – included is RRF and EIDL funds

Employee Retention Credit

Expanded Opportunities for the Restaurant Industry

Employee Retention Credit

- **What is it**? The ERC is a fully refundable payroll tax credit designed to encourage businesses to retain and compensate employees during periods in which businesses are not fully operational.

- **Why have I not taken advantage of this or heard of this?** Under the CARES Act, businesses could take advantage of either the PPP or the ERC, but not both and virtually all restaurants took advantage of the PPP. The Consolidated Appropriations Act, enacted on December 27, 2020, retroactively changed those rules and expanded it.

- **Who is eligible for the ERC?** To claim the ERC in any given calendar quarter, restaurants must meet one of the following criteria during that quarter:

  - They experienced a significant decline in gross receipts during the calendar quarter compared to 2019; ***OR***

  - Their operations were fully or partially suspended as a result of orders from a governmental authority limiting commerce, travel or group meetings due to COVID-19

Employee Retention Credit
(continued)

Who is eligible for the ERC?

Question: My restaurant was required to close at an earlier hour than its regular closing time due to a statewide government curfew. Is my restaurant considered partially shut down for purposes of determining eligibility for the ERC?

Question: Under a government order, my restaurant was required to reduce the seating capacity of our indoor dining room to accommodate for social distancing. However, the indoor dining room is open, and we are still able to offer delivery and carry-out. Is my restaurant considered partially shut down for purposes of determining eligibility for the ERC?

Employee Retention Credit
(continued)

Who is eligible for the ERC? (continued)

Question: Our company owns restaurants located in California, North Dakota and Utah. The restaurant locations in California were required to shut down due to government order. The ones in North Dakota and Utah were not. Is our company considered to have a suspension of operations due to a government order?

Employee Retention Credit
(continued)

2020 ERC Provisions

- **Maximum Creditable Wages Per Employee:** $10,000 per year from March 13, 2020 – December 31, 2020
- **Maximum Credit:** 50% of eligible wages up to $5,000 per employee for the year
- **Threshold to be considered a Large Employer:** over 100 FTEs
- **Revenue decline threshold:** Experienced more than 50% decline in gross receipts during a calendar quarter in 2020 as compared to the same quarter in 2019

Employee Retention Credit
(continued)

2021 ERC Provisions

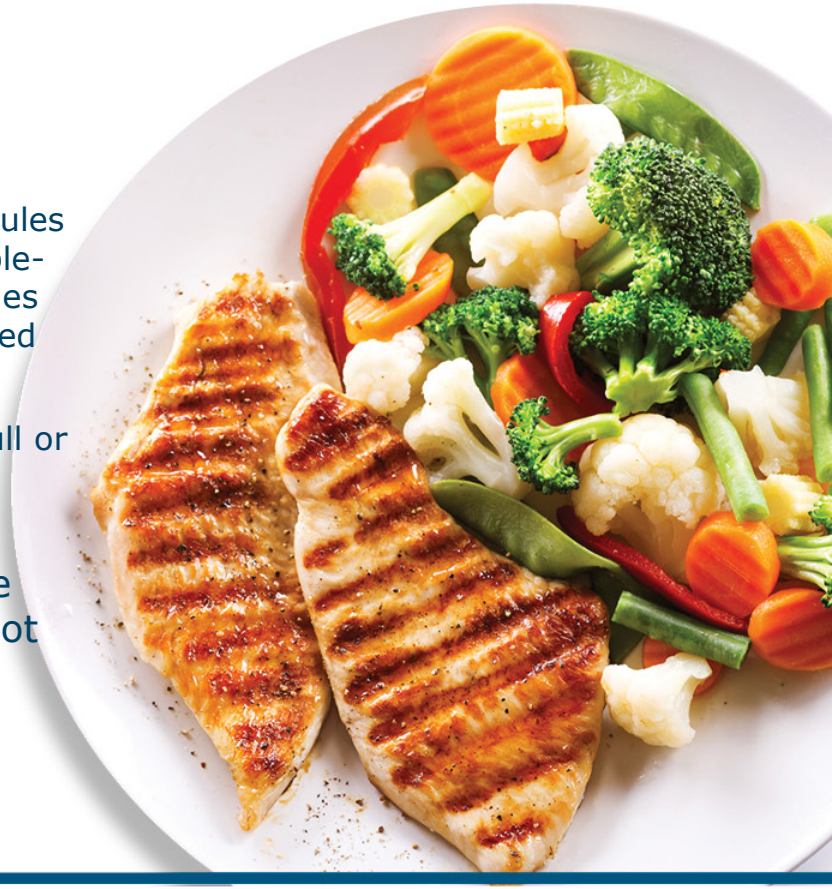
- **Maximum Creditable Wages Per Employee:** $10,000 per quarter from January 1, 2021 - September 30, 2021
- **Maximum Credit:** 70% of eligible wages up to $7,000 *per employee per quarter*
- **Threshold to be considered a Large Employer:** over 500 FTEs
- **Revenue decline threshold:** Experienced more than 20% decline in gross receipts during a calendar quarter in 2021 as compared to the same quarter in 2019.
- There is also an alternative quarter election that allows companies to look at the immediately preceding quarter to determine eligibility.

NOTE: Potential total refundable credit per employee over both 2020 and 2021 is $26,000

Employee Retention Credit
(continued)

2021 ERC Provisions (continued)

- **Recovery Startup Business:** Section 3134(c)(5) of the Code defines a "recovery startup business" as an employer
  - that began carrying on any trade or business after February 15, 2020
  - for which the average annual gross receipts of the employer (as determined under rules similar to the rules under section 448(c)(3) of the Code) for the 3-taxable-year period ending with the taxable year that precedes the calendar quarter for which the credit is determined does not exceed $1,000,000, and
  - that is not otherwise an eligible employer due to a full or partial suspension of operations or a decline in gross receipts.
- The amount of the credit allowed for each of the third and fourth calendar quarters of 2021 cannot exceed $50,000.
- ***Only business eligible for the ERC in the fourth quarter of 2021.***



Significant Decline in Gross Receipts

- **For 2020, a significant decline in gross receipts begins:**
  - the first calendar quarter in 2020 (if any)
  - in which an employer's gross receipts are less than 50% of its gross receipts
  - for the same calendar quarter in 2019
- **For 2020, the significant decline in gross receipts ends with the earlier of January 1, 2021, or:**
  - the calendar quarter that *follows* the first calendar quarter
  - in which gross receipts are greater than 80% of its gross receipts
  - for the same calendar quarter in 2019
- **For 2021, a significant decline in gross receipts:**
  - is made separately for each calendar quarter
  - and is based on an 80% threshold

Employee Retention Credit
(continued)

Significant Decline in Gross Receipts
(continued)

- For 2021, Section 2301(c)(2)(B) of the CARES Act, as amended by section 207(d)(2) of the Relief Act, permits an employer to elect to use an alternative quarter to calculate gross receipts.
- An election to use an alternative quarter to calculate gross receipts is made by claiming the employee retention credit for the quarter using the alternative quarter to calculate gross receipts.
- Under this election, an employer may generally determine if the decline in gross receipts test is met for a calendar quarter in 2021 by comparing its gross receipts for the immediately preceding calendar quarter with those for the corresponding calendar quarter in 2019 (substituting 2020 for 2019 if the employer did not exist as of the beginning of that quarter in 2019).

Employee Retention Credit
(continued)

Significant Decline in Gross Receipts
(continued)

- Gross receipts for purposes of the ERC for an employer has the same meaning as when used under Section 448(c) of the Internal Revenue Code
  - Under Section 448(c) regulations, "gross receipts" means gross receipts of the taxable year and generally includes total sales (net of returns and allowances) and all amounts received for services
  - In addition, gross receipts include any income from investments, and from incidental or outside sources

Employee Retention Credit
(continued)

Full or Partial Suspension of Operations

- The operation of a trade or business is considered partially suspended if an appropriate governmental authority imposes restrictions on the employer's operations by limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) due to COVID-19 such that the employer can still continue some, but not all of its typical operations.
- Partial closure of operations (e.g., restaurant that continues pickup/delivery services) may qualify for the credit under the partial closure rules.
- An employer that operates an essential business may be considered to have a partial suspension of operations if, under the facts and circumstances, more than a *nominal* portion of its business operations are suspended by a governmental order.

Employee Retention Credit
(continued)

Aggregation Rules

- Each employer must apply the aggregation rules of IRC Section 414(m) and (o) as well as IRC section 52(a) or (b)
- Under IRC section 414(m) an affiliated service group is treated as a common employer based on rules on the performance of services by one entity for the benefit of another entity
- Under Section 52, corporate employers must aggregate the number of employees if:
  - It is included in a parent-subsidiary group where a common parent owns more than 50% of the subsidiaries
  - It is included in a brother-sister combined group where a group of 5 or fewer people own 80% or more of each corporation
  - It is a combined group which is a group of three or more corporations each of which is either a parent-subsidiary group or a brother-sister controlled group

Employee Retention Credit
(continued)

Aggregation Rules (continued)

- Section 52b also applies similar rules to partnerships, trusts, estates, etc.
- All members of an aggregated group are treated as a single employer for purposes of the ERC.
- As a result, these employers must be aggregated for purposes of the following rules applicable to the ERC:
  - Determining whether the employer has a trade or business operation that was fully or partially suspended due to orders related to COVID-19 from an appropriate governmental authority.
  - Determining whether the employer has a significant decline in gross receipts.
  - Determining whether the employer has more than 100/500 full-time employees.
  - Determining the maximum credit per employee.

Employee Retention Credit
(continued)

Number of Full-Time Employees

- **The term "full-time employee" means an employee who, with respect to any calendar month in 2019, had an average of at least 30 hours of service per week or 130 hours of service in the month**
  - 130 hours of service in a month is treated as the monthly equivalent of at least 30 hours of service per week
- **If in business for the entire 2019 calendar year**
  - The sum of the number of full-time employees in each calendar month in 2019 and dividing that number by 12
- **If started business in 2019**
  - The sum of the number of full-time employees in each full calendar month in 2019 in which the employer operated its business and dividing by that number of months
- **If started business in 2020**
  - The sum of the number of full-time employees in each full calendar month in 2020 in which the employer operated its business and dividing by that number of months

Employee Retention Credit
(continued)

Qualified Wages

- Qualified wages are wages (as defined in section 3121(a) of the IRC) and compensation (as defined in section 3231(e) of the IRC) paid by an Eligible Employer to some or all employees between March 13th, 2020, and September 30, 2021
- Qualified wages include the Eligible Employer's qualified health plan expenses that are properly allocable to the wages
- The definition of qualified wages depends on how many employees an eligible employer has

Employee Retention Credit
(continued)

Qualified Wages (continued)

- The calculation of Qualified Wages depends on whether the employer has 100 (2020) / 500 (2021) or less employees or more than 100 (2020) / 500 (2021) employees
- 100 (2020) / 500 (2021) or less employees:
  - Qualified wages are all wages paid to employees within the applicable period
  - Plus all qualified health care costs
- More than 100 (2020) / 500 (2021) employees:
  - Qualified wages include only wages paid to employees for the time the employee *did not work* due to economic hardship as a result of COVID-19
  - Plus qualified health care costs prorated to qualified wages

Employee Retention Credit
(continued)

Qualified Wages (continued)

- **Question:** Is my restaurant required to include part-time employees in the calculation of employees to determine if we are a large employer for calculating qualified wages?

- **Question:** When calculating qualified wages, should we include the wages of only the full-time employees or all employees?

- **Question:** Are tips included in the calculation of qualified wages?

Employee Retention Credit
(continued)

Other Considerations

- Taxpayers that received PPP loan in 2020 and/or 2021 can claim ERC, but no "double dipping"
- The American Rescue Plan Act of 2021 extended the limitation on the time period for assessment from 3 years to 5 years
- IRS issued ERC guidance in Notices 2021-20, 2021-23 and 2021-49

Employee Retention Credit
(continued)

Other Considerations (continued)

- **Question:** My restaurant currently claims the Work Opportunity Tax Credit (WOTC). If we claim the ERC, will that impact the calculation of the WOTC?

- **Question:** My restaurant utilizes a PEO to report our payroll. Can we still claim the ERC?

- **Question:** Is the ERC subject to federal and state income tax?

GBQ

Thank you!

Contact Information

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