

Voluntary Disclosure Program for the Employee Retention Credit

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The COVID-19 pandemic disrupted the lives and operations of individuals and businesses across the globe. To help combat these disruptions, various bills were passed and government actions were taken throughout the pandemic, including a business tax credit known as the Employee Retention Credit (ERC), which was first made available under the Coronavirus Aid, Relief and Economic Security Act, Pub. L. No. 116-136, 134 Stat. 281 (March 27, 2020).

Throughout the existence of the ERC program, there have been businesses that have rightfully taken the credit — a credit that helped them keep needed employees on the payroll during some of their toughest times — but, unfortunately, there have also been businesses that (knowingly or unknowingly) took the ERC when they weren't, in fact, eligible for it.

Generally, when a taxpayer takes a tax credit that shouldn't have been taken, they potentially expose themselves to a variety of consequences, not least of which is paying interest and penalties (such as failure-to-pay penalties, accuracy-related penalties and even civil fraud penalties). However, the IRS has come out with a novel program, called the Voluntary Disclosure Program (VDP), specifically for purposes of the ERC, which may help taxpayers not only avoid these consequences if they qualify (and fully follow the requirements of) the program, but also retain a portion of the credit taken.

Before the VDP is explored in more detail, a general understanding of the ERC may be helpful.

"Just the Basics" of the Employee Retention Credit

There are generally three ways for a business to qualify for the ERC:

1. The business suffered a significant decline in gross receipts;
2. The business was fully or partially suspended by a governmental order; and/or
3. The business qualifies as a "recovery startup business."

These three qualification methods will only be briefly touched upon in this article. There are a lot of nuances to the ERC (for example, aggregation rules, PPP interplay, full-time employee counts, just to name a few), and it has gone through a lot of changes since its inception and is subject to various IRS guidance. It is highly recommended that any business that has previously claimed the ERC without the help of a tax professional, or any business that would like to apply for the ERC, seek the help of a tax professional as soon as possible.

Significant Decline in Gross Receipts

Generally speaking, a business experienced a significant decline in gross receipts (i) if their 2020 gross receipts were less than 50% of

their 2019 gross receipts (measured by corresponding calendar quarters), or (ii) if their 2021 gross receipts were less than 80% of their 2019 gross receipts (measured by corresponding calendar quarters).

If a business qualifies under subsection (i), their qualification continues until the calendar quarter *after* the first calendar quarter for which the gross receipts are greater than 80% of the gross receipts of the corresponding 2019 calendar quarter.

Governmental Order Test

A business can qualify under the so-called "governmental order test" if their operations were either fully or partially suspended by a governmental order related to the pandemic. A full suspension means the business was fully shutdown and could not operate at all (other than perhaps performing minimum basic operations to keep the business intact during the shutdown, such as maintenance, cleaning, payroll duties, etc.).

A partial suspension means either (i) a more than nominal portion of the business was fully shut down or (ii) the business was subject to such modifications and restrictions under governmental order that its normal operations were more than nominally impacted. The IRS established a "more than nominal" threshold of 10% as a safe harbor. In other words, if at least 10% of a business was impacted by governmental order, then such business is *deemed* to have experienced a qualifying shutdown.

Specifically, to be considered a "more than nominal" portion of a business, such portion must comprise at least 10% of the business' total operations measured by either the total gross receipts or total employee service hours for such portion (by using 2019 calendar quarter numbers). For example, 12% of a limited-service restaurant's gross receipts in 2019 Q1 came from indoor dining. This portion of the business (i.e., indoor dining) was fully shut down in 2020 Q1 due to governmental order. This would satisfy the IRS's safe harbor under the governmental order test for 2020 Q1.

To be considered to have experienced a "more than nominal" impact to normal operations, a business must have been subject to modifications under governmental order that resulted in a reduction by at least 10% of its ability to provide its goods or services. The IRS did not provide specific metrics to use in order to satisfy this test, but did provide some examples



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(such as a business being subject to a 50% capacity limit under governmental order, or a business being required to follow strict social distancing measures which had the direct effect of reducing one's normal customer base by 25%).

Being subject to a governmental order by itself isn't enough; there must be the requisite "more than nominal" impact to qualify.

Recovery Startup

A recovery startup business is a business that began operating after February 15, 2020, and had average annual gross receipts of \$1,000,000 or less for the 3-year period preceding the calendar quarter for which the ERC is claimed. A recovery startup business can only claim the ERC for the third and fourth quarters of 2021 and may claim a maximum ERC of \$50,000 per quarter.

Understanding the Importance of the Voluntary Disclosure Program

In December 2023, the IRS released Announcement 2024-3 (which can be located here: <https://www.irs.gov/pub/irs-drop/a-24-03.pdf>), which detailed the VDP, a repayment program for those businesses "that filed for and erroneously received the ERC" in order to "resolve their civil tax liabilities... and avoid potential civil litigation, penalties, and interest."

The VDP not only helps the taxpayer to avoid these consequences, but it also allows the taxpayer to keep 20% of the ERC erroneously claimed. In other words, a taxpayer that enters into the VDP will only need to repay 80% of the credit claimed, and thus comes out on top by participating in this program.

To be eligible for the VDP, (i) the taxpayer cannot be under criminal investigation, (ii) the IRS cannot have information about the taxpayer's noncompliance, (iii) the taxpayer cannot be under an employment tax examination and (iv) the taxpayer cannot have previously received notice and demand for repayment of its ERC.

Time is of the essence for the VDP since its deadline is **March 22, 2024**. Not only that, but the IRS has announced it will soon be sending out 20,000 ERC disallowance letters to taxpayers who have already claimed the ERC. If a taxpayer receives one of these letters, such taxpayer will no longer be eligible for the VDP.

Though time may not be on a taxpayer's side when it comes to the VDP, it is never too late to get with a tax professional who can assist a taxpayer with this program. This program, like any IRS program, has its nuances, which are best navigated by an expert. If a taxpayer goes into the program blind, they risk providing the IRS with more information than is necessary, which leaves them exposed. By entering into the VDP, a taxpayer does not make itself immune from criminal prosecution for fraud, nor does the IRS waive any of its rights to judicial review. If a business is interested in the VDP and learning more about it, it is imperative to reach out to a trusted tax professional — and sooner rather than later.

Caitlin Grimes Rieser began her career as a tax and corporate attorney with Dentons Bingham Greenebaum based in Louisville. She has since transitioned in-house to serve as Senior Legal Counsel for Figure Financial, Inc., a specialty tax firm located in Orem, Utah with a national reach. Currently, her primary focus is on business tax credits. Rieser earned her J.D. from the University of Louisville Brandeis School of Law in 2018, and her LL.M. in Taxation from Boston University in 2020. ■



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