Employee Retention Credit Guidance Raises New Questions

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By Caitlin Mullaney

Employment tax practitioners facing an upcoming deadline still have several unanswered questions about the employee retention credit, despite new IRS guidance.

Justin Elanjian of Frost Law told *Tax Notes* that the recent guidance — a March 20 update to the ERC FAQ — "was much anticipated and long overdue." However, it "may be too little, too late and leaves much to be desired."

"This is sure to leave taxpayers and tax preparers scrambling in the weeks remaining" before the deadline, Elanjian added.

With the April 15 application deadline for the COVID-pandemic-era ERC near, the additional FAQ from the IRS addresses questions regarding interactions between the credit and income tax returns and reporting ERC fraud.

According to Elanjian, the FAQ may raise new questions, especially among taxpayers that have filed amended income tax returns and are still waiting for ERC payments.

Elanjian said the updated FAQ gives taxpayers the opportunity to account for the income tax effects of an ERC refund in the year of receipt. That's contrary to previous guidance (Notice 2021-20, 2021-11 IRB 922, and Notice 2021-49, 2021-34 IRB 316) and the statutes instructing taxpayers to follow rules similar to section 280C(a), which require a reduction of the wage deduction in the year for which the credit is determined, he said.

Risk of Reliance

Nathan Smith of CBIZ Advisors LLC asked what practitioners and businesses are supposed to do with this new guidance from the IRS.

"I know many taxpayers may want to follow these, but online FAQs are not authoritative," Smith said. "Online FAQs essentially are the same thing as a phone call with an agent: great for potential penalty relief but not substantial authority. So these FAQs cannot be used by themselves to support filing positions."

Smith noted, however, that the FAQ may be the best that that the IRS is able to offer given the regulatory freeze.

Matt Eddleman of Strategic Tax Planning said the guidance provided in the most recent FAQ "contradicts prior administrative guidance," and given its status as unpublished guidance, "it carries even less regulatory weight" than Notice 2021-20 regarding the income tax effects of claiming the ERC.

Issuing unpublished guidance shows the IRS knows it has fallen short on administering the ERC, according to Eddleman, who added that it appears the agency is attempting "to clean up a mess of its own making" by issuing the guidance that appears to have "a very tenuous statutory basis that the IRS has identified in the tax benefit rule."

Contradictions between the FAQ and previous notice guidance were also noted by Elanjian, who advised practitioners and businesses to be careful about relying on nonauthoritative guidance.

"It seems like the IRS has published these FAQs as a metaphorical punting of the decision on when to account for the income tax effects to taxpayers and tax preparers," Elanjian said.

Marvin A. Kirsner of Greenberg Traurig LLP had a positive reception to the FAQ additions, saying they resolve questions about the statute of limitations for amending income tax returns with deduction of wages accounting for ERC refunds.

The new guidance will be particularly beneficial for cases involving ERC refunds claimed for wages paid in 2020, for which the statute of limitations to file the required amended returns to reduce the deduction for wages has already expired, according to Kirsner.

But Kirsner also pointed to unanswered questions for the IRS regarding the aggregation rules for purposes of the employee count and the decline in gross receipts test.

"It is also unclear whether the IRS will assert the extended five-year statute of limitations to claw back an erroneous refund due to a misstatement of a material fact. These are complex issues that will need further time to be explained," Kirsner said.

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