NOTE: There are two subsequent acts of Congress that have impacted this topic. Information on those an be found here:
CARES Act--IRS Tax Credits (Employee Retention Credit)-2021 CAA Update
The American Rescue Plan Act of 2021 Further Extends COVID-19 Relief

COVID-19 Update

IRS Tax Credits (Employee Retention Credit)—Applies to Churches

As described in prior summaries provided by Wespath Benefits and Investments (Wespath) and the General Council on Finance and Administration (GCFA),[1] the **Coronavirus Aid, Relief and Economic Security Act (CARES Act)**[2] contains an incentive that encourages employers to retain—rather than terminate—employees despite current economic constraints due to COVID-19 impact. Recently, the Internal Revenue Service (IRS) announced the launch of this "*Employee Retention Credit*" and published **guidance** on related forms. *This credit is available for the tax year 2020 only.*

Eligibility

The Employee Retention Credit is available to large and small churches (and tax-exempt organizations generally)[3] if they have *either:*

- Suffered a decline in gross receipts of more than 50% (compared to the comparable quarter in 2019),[4] *or*
- Had to fully or partially suspend operations during a calendar quarter in 2020 "due to orders[5] from an appropriate governmental authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) due to the coronavirus disease 2019."

A local church will likely be eligible for this credit if it was subject to an order limiting group meetings. However, if a church-related organization does not rely on group meetings for its operations and is able to continue operating in a way that is *comparable to its operations prior to an applicable closure order* by requiring its employees to telework, it would not be eligible for the Employee Retention Credit on that basis and would instead need to show a decline in gross receipts of more than 50%.

[1] See the links provided at the end of this document.
[2] See CARES Act, Section 2301.
[3] The only exceptions to the program are state and local governments and organizations that received Paycheck Protection Program (PPP) loans.
[4] The IRS has not yet issued specific guidance about the meaning of this section for tax-exempt employers.
[5] Orders include state or local orders to shelter in place, as long as the organization is not one that was deemed essential. Statements from a governmental official do **not** rise to the level of an order. If an organization volunteers to shut down or slow operations, it must rely on a decline in gross receipts of more than 50% to be eligible for the Employee Retention Credit.

Calculating the Tax Credit

Applicable wages are capped at $10,000 per employee. Credit can be taken for 50% of the wages paid, meaning *a maximum credit of $5,000 per employee* is available to these employers.

For employers with *100 or fewer employees*, all wages,[6] including qualified health plan expenses[7] that are properly allocable to the wages, paid **after March 12, 2020 and before January 1, 2021** are eligible for the Employee Retention Credit. The credit can be taken for wages paid to all employees, regardless of whether they are able to work. For such an employer (with 100 or fewer employees), because qualified health plan expenses are considered "wages," such expenses are eligible for the credit even if the employer does not pay them any other wages.

For employers with *more than 100 employees*, the Employee Retention Credit is limited to *wages paid to employees for periods when they are not working*. For these employers, qualified health plan expenses are considered "wages" to the extent they can be allocated to periods when employees are not working but still being paid. (For example: if such an employer was subject to an order partially suspending its operations, and reduced employee hours by 50% while paying 100% of their health plan expenses, only the 50% of health expenses allocable to the time when employees were not working would be eligible for the credit.)

> ***IMPORTANT: The IRS has stated that wages paid (including any designated housing allowance) to clergy employees of a church do not qualify for the Employee Retention Credit.***

Applying for the Tax Credit

The easiest way to take the Employee Retention Credit is via the employer's IRS Form 941 (Employer's Quarterly Federal Tax Return). To the extent the employer paid qualifying wages **after March 12, 2020**, the employer can simply reduce the employment taxes[8] it would otherwise deposit via Form 941. (**IRS Guidance** provides that the first Form 941 that may be used for this Employee Retention Credit is the one for the second quarter, **due July 31, 2020**.)

> Example: An employer was due to deposit $8,000 in employment taxes on July 31, but it paid wages after March 12 that triggered a $5,000 Employee Retention Credit. Instead of depositing

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[6] This includes payment for paid time off (PTO) taken by employees under pre-existing policies, but not wages associated with paid leave provided by the FFCRA. Qualified sick or family leave wages paid under the FFCRA are eligible for a credit under the Families First Coronavirus Response Act (FFCRA), as opposed to the CARES Act's Employee Retention Credit. An employer may claim both types of credit, but not for the same wages. See IRS Instructions for Form 7200.

[7] Qualified health plan expenses include premiums, including both the cost paid by the employer and the cost paid by the employee with pre-tax salary reduction contributions. Qualified health plan expenses also include employer contributions to a health reimbursement arrangement (HRA) and a health flexible spending arrangement (FSA). They do not include employer contributions to a health savings account (HSA) or a qualified small employer health reimbursement arrangement (QSEHRA).

[8] The Employee Retention Credit may be taken against both income taxes withheld and the employer and employee shares of Social Security and Medicare taxes.

the full $8,000, the employer would need to deposit only $3,000, and could use the other $5,000 to reimburse itself immediately for half of the eligible wages it paid to its employees.

If an employer can claim a credit that exceeds the amount of employment taxes it was due to deposit with Form 941, the employer can request an *advance*, i.e., a "refund" of this amount even where it exceeds taxes owed, of the difference by filing IRS Form 7200. Alternatively, the employer can request a refund of the overpayment when it files Form 941.

UMC Example 1

A qualifying local church with one non-clergy[9] employee paid $10,000 in wages to that employee prior to June 30, 2020, with $5,900 of the total being paid after March 12. If the employment taxes withheld for this employee for the second quarter total $1,000 (i.e., the withheld federal income tax plus the employee and employer shares of Social Security and Medicare taxes), then on the Form 941 the local church files, it can use its $2,950 Employee Retention Credit (50% of the $5,900 qualifying wages paid after March 12) to repay itself $1,000, and seek an *advance refund* for the remaining $1,950 (i.e., the remaining balance of the 50% of qualifying wages).

UMC Example 2

A qualifying local church has three non-clergy employees. Assume it paid qualifying wages after March 12 and through the end of June of $11,000 to Employee One and $9,000 each to Employees Two and Three. It could anticipate an Employee Retention Credit of $5,000 for Employee One (the maximum for the year) and $4,500 *each* for Employees Two and Three.

- For second-quarter filing: If the church was due to deposit $5,000 in employment taxes with its second-quarter Form 941, it could keep the $5,000, and seek a refund for the additional $9,000 ($4,500 each for Employees Two and Three) in employee retention credits.
- For third-quarter filing: Assuming the church kept its payroll the same in the third quarter and continued to qualify, it would only have another $500 *each* in credits for wages paid to Employees Two and Three, bringing each employee wage reimbursement to the maximum of $5,000 in employment retention credits. The church could reduce its deposit for the third quarter from $5,000 to $4,000 to account for the remaining credit.
- For the fourth quarter, the church would have no additional employee retention credits to claim.

Limitations

The CARES Act has other provisions that support employers and employees impacted by the COVID-19/coronavirus pandemic. The Act includes measures to prevent double-counting or redundancy of benefits. For example, if the employer was required to pay emergency sick leave or expanded family

[9] *If a church's only employee is its pastor, the church would not be able to claim any amount as an Employee Retention Credit.* The IRS has stated that credit cannot be taken against wages paid to clergy employees.

leave wages under the Families First Coronavirus Response Act (FFCRA), it should subtract those amounts from wages paid after March 12 in calculating its Employee Retention Credit.[10]

In addition, the CARES Act created a new loan support program for small businesses called the Paycheck Protection Program (PPP). PPP loans are administered through the Small Business Administration (SBA)—and are available to nonprofits and churches.

> ***IMPORTANT: Employers, including local churches and annual conferences, that received PPP loan funds are not eligible for Employee Retention Credits.***

The Department of Treasury recently clarified through its **FAQs** (#43 and #45) that an organization that returns PPP funds by the **May 14, 2020** safe harbor deadline will be treated as if it did not receive a PPP loan and will thus be eligible for the Employee Retention Credit.

Additional Resources

CARES Act, including Paycheck Protection Program

- **CARES Act Summary**
- **CARES Act Q&A**
- **PPP Application Form and Guidance**
- **FAQs about PPP Loans**

FFCRA

- **FFCRA Summary**
- **FFCRA Q&A**

More Information Related to COVID-19

- **General Council on Finance and Administration**
- **Wespath Benefits and Investments**

The information above should not be considered legal or tax advice. Plan participants, annual conferences, local churches, or other employers or parties affiliated with The United Methodist Church should consult with counsel in considering the application of the coronavirus-related laws and guidance to their circumstances.

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[10] The IRS has published a general summary of the different types of employer credits available.