

Should I Stay or Should I Go? The IRS Makes the Decision Hard for Employers Who Filed For or Accepted Refunds Under the Employee Retention Tax Credit

Article By:

Alex H. Glaser

Timothy P. Brechtel

The Internal Revenue Service (IRS) recently announced two relief programs for employers that may have claimed credits under the employee retention credit (ERC) based on erroneous or specious eligibility standards. Owing in large part to what the IRS believes has been widespread abuse, the relief programs are aimed primarily at employers that may have been misled by third-party promoters into believing that they were eligible for the credit.

There are two bases for employers to claim the ERC. The first basis is a “decline in gross receipts” which is a mathematical calculation that compares income during eligible quarters of 2021 and 2022 to similar quarters during 2019 and 2020. Because the decline in gross receipts test is objectively determinable, the IRS has not scrutinized submissions under this standard to the same degree as those that filed under the second eligibility test, the “governmental order” test. Under the governmental order test, an employer has to experience a “suspension of operations” due to a qualifying governmental order. The test is based on relevant facts and circumstances and is intended to apply only if there is a more than nominal suspension of operations.

The IRS previously expressed its concern that employers are taking aggressive tax positions with respect to the governmental order test, often in reliance on advice from unscrupulous promoters and advisers. In response, the IRS halted processing new claims under the ERC program in the latter part of 2023 and warned employers that more aggressive scrutiny would be applied to pending claims.

The first relief program was announced in October 2023 for employers that filed an ERC claim but did not yet receive a refund or did not yet cash a refund check. Employers can withdraw their claim by filing a withdrawn tax return with the IRS, which the IRS will then accept or reject. If accepted, the returns are treated as never having been filed and therefore the employer will not face any potential interest or penalties associated with an ERC filing.

In December 2023, the IRS announced a voluntary disclosure program for employers that previously received ERC monetary refunds. Under the disclosure program, an employer can pay back 80% of the aggregate funds received from its ERC claim in exchange for a waiver of interest and penalties

and a certification from the IRS that it will not bring an enforcement action. The program is open to any employer that claimed the credit and received a monetary refund, except for employers under current criminal investigation or businesses that have been reported as being in noncompliance pursuant to a completed or pending enforcement action. Employers that participate in the program are asked to disclose any third-party promotor or adviser that they relied on to claim the credits. The voluntary disclosure program will remain open through **March 22, 2024**.

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