

IRS Reverses Course on Employee Retention Credit for Qualified Health Plan Expenses

Health plan expenses are treated as qualified wages, even for furloughed employees with no wages

By William Hays Weissman © Littler

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The IRS has changed its position and will allow employers to receive a tax credit for paying health care plan premiums for employees on furlough.

Background

The Coronavirus Aid, Relief and Economic Security (CARES) Act creates an employee retention credit (ERC) that allows employers to claim a credit against up to \$10,000 it pays in "qualified wages." Under the CARES Act, "qualified wages" include:

- Cash compensation paid between March 13, 2020 and Dec. 31, 2020.
- Qualified health plan expenses.

The CARES Act defines "qualified health plan expenses" as amounts paid or incurred by the employer to provide and maintain a group health plan, but only to the extent that those amounts are excluded from the gross income of employees.

On April 29, 2020, the IRS issued numerous FAQs on the ERC (<https://www.irs.gov/newsroom/covid-19-related-employee-retention-credits-determining-qualified-wages-faqs>). While the FAQs do not have the force and effect of law and cannot be relied upon, they are among the most common methods by which the IRS has provided guidance on its views about the CARES Act.

Under those FAQs—numbers 58, 64 and 65—the IRS explained that an employer could not claim the ERC unless some amount of cash compensation subject to Social Security and Medicare tax was also paid. This meant that employers that furloughed employees, paid no cash wages but continued to pay their employees' health plan premiums, could not claim the ERC. The IRS reiterated this position during a webinar hosted by the American Bar Association Taxation Committee on April 30, 2020.

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(www.shrm.org/resourcesandtools/tools-and-samples/hr-qa/pages/how-does-the-families-first-coronavirus-response-act-hr-6201-impact-employers.aspx)

Position Reversed

On May 4, 2020, Senator Chuck Grassley, Chair of the Senate Finance Committee, Congressperson Richard Mean, Chair of the Ways and Means Committee, and Senator Ron Wyden, Ranking Member of the Senate Finance Committee, sent a letter

(<https://www.finance.senate.gov/imo/media/doc/050420%20Letter%20to%20Treasury%20on%20ERTC%20health%20benefits.pdf>) to

Treasury Secretary Steven Mnuchin questioning the IRS's position. On May 7, 2020, the Treasury Department responded (<https://www.finance.senate.gov/imo/media/doc/2020-05-07%20UST%20Response%20to%20Grassley%2005-04%20letter.pdf>) that it has "taken your views under consideration and would be revising the applicable guidance."

On May 11, the IRS updated FAQs 64 and 65 and added new FAQ 79 (<https://www.irs.gov/newsroom/covid-19-related-employee-retention-credits-amount-of-allocable-qualified-health-plan-expenses-faqs>). Q&As 64 and 65 now state that employers can claim the ERC for qualified health care expenses regardless of whether the employee is paid qualified wages.

The revised Q&As clarify this new interpretation with five examples in which qualified health care expenses paid to furloughed employees are considered qualified wages for purposes of the employee retention credit.

This is welcome news for employers and will encourage them to continue paying health plan expenses for employees on furlough.

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