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Employee Retention Tax Credit: Qualified Health Plan Expenses FAQ Update

The Internal Revenue Service (IRS) updated its [COVID-19-Related Employee Retention Credits: Amount of Allocable Qualified Health Plan Expenses FAQs](#). The FAQs provide guidance on determining the amount of allocable qualified health plan expenses that may be treated as qualified wages for the employee retention tax credit (ERTC). The ERTC is a fully refundable tax credit for employers that is equal to 50 percent of qualified wages paid by employers to their employees after March 12, 2020, and before January 1, 2021, during any period in a calendar quarter in which the employer's business operations are fully or partially suspended due to a governmental order or a calendar quarter in which the employer experiences a significant decline in gross receipts, subject to the maximum of \$10,000 per employee for all calendar quarters. If the employer averaged 100 or fewer full-time employees in 2019, qualified wages are the wages paid to any employee during any period of economic hardship noted above. If the employer averaged more than 100 full-time employees in 2019, qualified wages are the wages paid to an employee for time that the employee is not providing services due to an economic hardship noted above.

Previously, the FAQs provided that employers could not treat qualified health plan expenses for employees as qualified wages unless the employer paid the employee other qualified wages. The IRS has modified the FAQs. For employers that averaged 100 or fewer full-time employees in 2019, the employer may treat health plan expenses as qualified wages even if the employees are not working and the employer does not pay the employees wages for the time they are not working. The FAQs provide two examples.

Example 1: Employer Y averaged 100 or fewer employees in 2019. Employer Y is subject to a governmental order that partially suspends the operation of its trade or business. In response to the governmental order, Employer Y reduces all employees' hours by 50 percent. It pays wages to the employees only for the time the employees are providing services, but Employer Y continues to provide the employees with full health care coverage. Employer Y's health plan expenses allocable to wages paid during the period its operations were partially suspended may be treated as qualified wages for purposes of the ERTC.



Example 2: Employer Z averaged 100 or fewer employees in 2019. Employer Z is subject to a governmental order that suspends the operation of its trade or business. In response to the governmental order, Employer Z lays off or furloughs all of its employees. It does not pay wages to its employees for the time they are laid off or furloughed and not working, but it continues the employees' health care coverage. Employer Z's health plan expenses allocable to the period its operations were partially suspended may be treated as qualified wages for purposes of the ERTC.

For employers that average more than 100 full-time employees in 2019, the employer may not treat health plan expenses as qualified wages for the time in which the employees are receiving wages for providing services; only the portion of health plan expenses allocable to the time that the employees are not providing services are treated as qualified wages. The FAQs provide three examples.

Example 1: Employer A averaged more than 100 full-time employees in 2019. Employer A is subject to a governmental order that partially suspends the operation of its trade or business. In response to the governmental order, Employer A reduces all employees' hours by 50 percent and pays wages to its employees only for the time that the employees are providing services, but Employer A continues to provide the employees with full health care coverage. Employer A's health plan expenses allocable to the time that employees are not providing services may be treated as qualified wages. However, Employer A may not treat health plan expenses allocable to the time for which the employees are receiving wages for providing services as qualified wages.

Example 2: Employer B averaged more than 100 full-time employees in 2019. Employer B is subject to a governmental order that partially suspends the operations of its trade or business. In response to the governmental order, Employer B reduces its employees' hours by 50 percent, but it reduces its employees' wages by only 40 percent, so that the employees receive 60 percent of their wages for 50 percent of their normal hours. Employer B continues to cover 100 percent of the employees' health plan expenses. In this case, Employer B may treat as qualified wages the 10 percent of the wages that it pays employees for time the employees are not providing services, plus 50 percent of the health plan expenses, because the health plan expenses are allocable to the time that employees were not providing services.

Example 3: Employer C is subject to a governmental order that fully suspends the operations of its trade or business. Employer C lays off or furloughs its employees and does not pay wages to the employees, but does continue to cover 100 percent of the employees' health plan expenses. In this case, Employer C may treat as qualified wages the health plan expenses that are allocable to the time that the employees are not providing services.

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