



# TaxNewsFlash

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## IRS offers clarifications in FAQs addressing interaction of ERC and PPP loans in acquisitions (COVID-19)

Parties engaging in transactions in 2020 have faced uncertainty regarding the intersection between the employee retention credit (ERC) and Paycheck Protection Program (PPP). There has been significant concern regarding the eligibility for an acquirer to claim the ERC in situations when a target has previously received a PPP loan.

The IRS this week updated a set of [“frequently asked questions” \(FAQs\)](#) that address this concern and clarify that, with certain limitations, an acquiring employer’s eligibility to claim the ERC will not be adversely affected by an acquisition with a target that had received a PPP loan. Read [TaxNewsFlash](#)

### Background

Eligible employers whose business has been affected by the coronavirus (COVID-19) pandemic may be entitled to an ERC—a refundable tax credit equal to 50% of qualified wages up to \$10,000 (i.e., up to a \$5,000 credit) per employee. However, there are additional limitations on determining ERC eligibility. If an otherwise eligible employer receives a loan under the PPP, the employer is generally not eligible for the ERC, and any prior ERC claims may be recaptured. Additionally, an aggregation rule applies under which all persons treated as a single employer under section 52(a) or (b) or section 414(m) or (o) of the Internal Revenue Code are treated as a single employer for ERC purposes.

Many larger acquisitive employer organizations (referred to here as “Acquirors”) have availed themselves of the relief provided in the form of the ERC or plan to do so before year-end. Many smaller employers that are likely to be on the sell-side of the acquisition (referred to here as “Targets”) have sought relief through PPP loans. However, the interaction between these two relief provisions caused concern and raised the following questions:

- *If both Acquiror and Target are treated as a single employer for ERC purposes post-transaction, can Target’s actions in the pre-close period “poison the well” for the Acquiror’s ERC eligibility going forward?*
- *Does the acquisition and resulting aggregation affect the Acquiror’s eligibility to claim the ERC for qualified wages paid prior to the transaction?*

- *Can the ERC be claimed for wages paid to Target employees post-transaction?*

The statutory language does not provide direct guidance on the nuanced application of the aggregation rule and PPP loan restrictions in the context of an acquisition, and this was not previously addressed in IRS guidance. While there was hope earlier in the year that these scenarios would be addressed through additional legislation, that is increasingly less likely.

## **New FAQ guidance**

The IRS has now provided guidance responding, at least in part, to these scenarios in the form of additions to its ERC “frequently asked questions” (FAQs). The new guidance, described below, generally results in favorable outcomes for employers engaging in either a stock or an asset acquisition, each addressed separately.

### **Stock acquisitions**

In a new Q/A 81a, the IRS addressed how ERC eligibility is affected if an Acquiror employer acquires the stock or other equity interests of a Target employer that had received a PPP loan and, under the aggregation rules, the employers are treated as a single employer as a result of the transaction.

Under this new Q/A, the outcome depends in large part on whether Target’s PPP loan is fully satisfied or an escrow to repay the loan is established prior to the transaction.

— **PPP loan fully satisfied or escrow established pre-transaction:** If, prior to the transaction closing date, the Target employer either (1) fully satisfied the PPP loan in accordance with the Small Business Administration Notice effective October 2, 2020 (the “SBA Notice”), or (2) submitted a forgiveness application to the PPP lender and established an interest-bearing escrow account in accordance with the SBA Notice, then after the closing date, the Acquiror’s aggregated employer group will not be treated as having received a PPP loan as a result of Target’s prior loan.

In this scenario, any aggregated employer that is otherwise eligible to claim the ERC can do so following the transaction, including with respect to wages paid to Target employees. In addition, the transaction would not give rise to recapture of any ERC amounts claimed by Acquiror prior to closing.

— **PPP loan not fully satisfied and no escrow established pre-transaction:** If, prior to the transaction closing date, the Target employer neither (1) fully satisfies the PPP loan, nor (2) submits a forgiveness application to the PPP lender and establishes an interest-bearing escrow account in accordance with the SBA Notice, then after the closing date, the Acquiror’s aggregated employer group will nevertheless generally not be treated as having received a PPP loan as a result of Target’s loan.

This scenario generally requires a bifurcation, post-transaction, between Target and Acquiror/other members of its aggregated employer group. As with the scenario above, any aggregated employer (other than Target) that is otherwise eligible to claim the ERC can do so following the transaction, and the transaction would not give rise to recapture of any ERC amounts claimed by Acquiror prior to closing. However, Target (that continues to be obligated on the PPP loan post-closing) is not eligible for the ERC for any wages paid to Target employees pre- or post-closing.

### **Asset acquisitions**

The asset acquisition scenarios described in a new Q/A 81b have similar outcomes to those described in the stock acquisition context. When acquiring Target's assets, the outcome is dependent upon whether Acquiror is assuming the PPP loan obligations.

- **No assumption of PPP loan obligations:** In an asset acquisition in which Target had received a PPP loan, Acquiror will not be treated as having received a PPP loan by virtue of the acquisition, provided that Acquiror does not assume Target's obligations under the loan.

In this scenario, Acquiror (and any member of its aggregated employer group) that is otherwise eligible to claim the ERC can do so following the transaction. In addition, the transaction would not give rise to recapture of any ERC amounts claimed by Acquiror prior to the acquisition.

- **Assumption of PPP loan obligations:** In an acquisition of the assets and liabilities of Target that had received a PPP loan, Acquiror will generally not be treated as having received a PPP loan by virtue of the acquisition; however, there will be limitations on what may be treated as "qualified wages" after the closing date.

This scenario generally requires a bifurcation, post-acquisition, to separately identify individuals who were employed by Target at the time of the transaction. As with the scenario above, Acquiror (and any member of its aggregated employer group) that is otherwise eligible to claim the ERC can do so following the transaction, and the transaction would not give rise to recapture of any ERC amounts claimed by Acquiror prior to closing. However, any wages paid by Acquiror after closing to an individual who was employed by Target on the closing date will not be treated as qualified wages.

Note that this scenario likely presents greater administrative challenges than the other scenarios in light of the bifurcation and segmenting of wages post-transaction.

## KPMG observation

Parties in a transaction need to consider how this new guidance may affect their current plans for claiming any COVID-19-related credits or other relief before 2020 comes to a close. In addition, parties need to consider if additional planning measures are warranted in advance of any impending transactions. Parties to previous transactions that may have discontinued claiming the ERC may need to revisit those positions.

Finally, whether an employer is otherwise eligible for the ERC, and what constitutes "qualified wages" for ERC purposes, need to be carefully considered and may be subject to requirements not addressed in this brief summary.

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