

# Now & Next

## Tax Alert

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## End of Voluntary Disclosure Program for ERC looms

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What businesses need to know now and do next about Voluntary Disclosure Program deadline of March 22, 2024



### What's the impact?

- Every company that received an ERC refund should be assessing whether they actually may have been ineligible to claim the credit.
- The VDP is a valuable resource for companies that determine they did not qualify, especially those that worked with an ERC Promoter.
- Companies that have filed for the ERC should conduct a self-evaluation of their ERC situation and consider the VDP.

In late December 2023, the U.S. Internal Revenue Service (IRS) announced a Voluntary Disclosure Program (VDP) for those who received employee retention tax credit (ERC) refunds from the U.S. Treasury **before December 21, 2023**. While we will discuss qualification for the VDP, that is only

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<sup>1</sup> Mark Lytle (Partner—Government Investigations & White Collar Defense) assisted with the preparation of this alert.

part of the picture. To understand the importance of the looming deadline of March 22, 2024, the VDP must be put in proper context.

## Historic background

In response to COVID-19, Congress enacted several laws providing for the ERC, which essentially allowed a wide range of companies to qualify for cash refunds. While [eligibility for ERC funds](#) was straightforward in some cases, in many cases, it was not, due to ambiguous rules and questionable interpretations by the IRS, as well as taxpayers, accountants, lawyers, and ERC “Promoters.” Many ERC Promoters and others took advantage of these ambiguities and the result was a massive oversubscription to the ERC. Congress estimated the ERC would cost the government \$77 billion; as of the fall of 2023, the amount paid out was more than \$230 billion, with likely another one or two hundred billion dollars still in process.

## The IRS acts

The IRS saw this tidal wave coming in early 2023. It justifiably blamed most of the problem on ERC Promoters, who typically took a percentage of ERC funds obtained by a company. In March 2023, the IRS added ERC claims to its “Dirty Dozen” list of tax scams. In May 2023, the IRS issued a paper [warning taxpayers of ERC Promoters](#). On September 14, 2023, the IRS abruptly stopped processing ERC claims until no sooner than January 1, 2024, and listed “warning signs” of ERC Promoters. On December 21, 2023, to motivate taxpayers to voluntarily return ERC refunds they may not have been eligible for and to identify unsavory ERC Promoters, the IRS launched the VDP.

To apply for the VDP, a company completes a Form 15434, which requests information about any ERC Promoter used to obtain the ERC refunds. The IRS’s actions to date paint a clear picture: (a) The IRS warned taxpayers about ERC Promoters early and often; (b) the IRS described “red flags” taxpayers should look for regarding ERC Promoters; (c) the IRS has given taxpayers an “out” with the VDP in exchange for “outing” ERC Promoters; and (d) after all of this, if you don’t come clean, the IRS may be coming after you, not just ERC Promoters.

## VDP qualification and beyond

VDP allows qualifying companies to return 80% of the ERC refunds received, and in exchange, the IRS will allow the company to (i) keep 20% of the ERC refunds, (ii) keep any interest paid to the company by the IRS, (iii) reverse the reduction of the wage expense relating to the ERC, and (iv) avoid penalties.

Every company that received an ERC refund should be assessing whether they actually may have been ineligible to claim the credit. If so, the VDP is a no-brainer for companies that determine

they did not qualify, especially those that worked with an ERC Promoter. The information the IRS gathers via the VDP and Forms 15434 is likely to lead back to other companies that worked with these ERC Promoters. You want to be on the right side of that fence; otherwise, you could not only miss out on the benefits of the VDP listed above, but also face an IRS investigation, as well as civil and criminal penalties.

If you are not sure whether the ERC Promoter you worked with is a bad actor, you should look for the following “red flags” the IRS has identified:

- / Fees based on a percentage of the ERC claimed.
- / Unsolicited calls or advertisements mentioning an “easy application process.”
- / Statements that the promoter or company can determine ERC eligibility within minutes.
- / Large upfront fees to claim the credit.
- / Preparers seeking anonymity by refusing to sign the ERC return being filed by the business or supply their identifying information and a tax identification number. Like “ghost preparers,” this puts the risk on just the taxpayer claiming the credit.
- / Aggressive claims that your business qualifies before any discussion of your tax situation.

Even if you didn’t work with an ERC Promoter, if one or more of the above warning signs applies to the consultant you did work with, you should be concerned.

For example, if you applied for the ERC without written support of your basis for qualification, or if the consultant you worked with refuses to provide written support, that is a warning sign.

To qualify for the VDP, a company needs to meet various requirements, including:

- / ERC refund check was paid and cashed **before December 21, 2023**;
- / You are not entitled to *any* ERC (not even \$1);
- / You are not under employment tax examination (audit) by the IRS;
- / You have not received notice from the IRS about its intent to reverse your ERC and you have not reversed your ERC to zero (although exceptions may apply in the latter case);
- / The IRS has not been alerted by a third party about your ERC noncompliance; and
- / The IRS does not have information directly related to your ERC noncompliance from an enforcement action.

It is important to note that if you willfully filed an employment tax return that fraudulently claimed ERC, or if you assisted or conspired in such conduct, the VDP will not exempt you from potential criminal investigation and prosecution.

A number of these criteria are as vague and ambiguous as the ERC requirements themselves. Specifically, the requirement that you must be ineligible for even a \$1 of ERC is subjective under

many of the ERC rules. Still, pursuing the VDP, especially for those who used ERC Promoters, is likely to be the best course of action in most cases, for taxpayers ineligible for the ERC, despite any technical foot-faults.

The ERC rules are complicated and even the most seasoned accountants and tax professionals have struggled with the patchwork set of IRS guidance in this area. Now is the time to revisit your ERC situation:

- / If you received ERC, were you eligible in the first place?
- / Do you qualify for the VDP?
- / Do you have written support and backup documentation regarding your ERC qualification?
- / Did you have more than one tax professional assess your qualification?

## Takeaways

In light of increased scrutiny and enforcement activity, all ERC recipients need to re-evaluate their eligibility for the credit, regardless of whether they qualify for VDP. It would be a mistake for a company to conclude that not qualifying for the VDP means it does not need to re-evaluate its ERC status. The VDP is a tool for the IRS criminal division to seek out targets for prosecution, so it is a clarion call to action for all taxpayers who applied for the ERC. If the VDP is not an option, there is a regular withdrawal process that can be undertaken and should be considered. All companies that applied for the ERC should have robust written documentation supporting their basis for qualification.

Nixon Peabody has considerable experience with the ERC and IRS civil and criminal investigations, and we are recommending that companies that have filed for the ERC (whether or not ERC refunds have been received) conduct a self-evaluation of their ERC situation and consider the VDP, **which is scheduled to expire on March 22, 2024.**

For more information on the content of this alert, please contact your Nixon Peabody attorney or:

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