

Publications

Client Alert: IRS Guidance Addresses the Impact of M&A Transactions Involving PPP Borrowers on Employee Retention Tax Credits

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On November 16, the IRS provided **guidance** clarifying the effect of M&A transactions involving target Paycheck Protection Program (PPP) borrowers on a business's eligibility for the Employee Retention Tax Credit (ERTC). The following summarizes this guidance.

Prior Guidance Failed to Address M&A Transactions

Prior IRS guidance emphasized two important points about the interplay between the ERTC and the PPP:

- The two programs are mutually exclusive. Generally, an eligible employer that receives a PPP loan, regardless of the date of the loan and regardless of whether the loan has been forgiven, **cannot** claim the ERTC. (An exception exists for PPP loans repaid in full prior to May 18, 2020 pursuant to Small Business Administration (SBA) guidance.)
- Aggregation rules apply. Under the ERTC rules, multiple affiliated entities with sufficient common ownership or control are treated as a single employer (Employer Group). The **entire** Employer Group is ineligible for ERTC if **just one** member receives a PPP loan.

This guidance did not address how these rules apply in the case of an M&A transaction where a target business with a PPP loan becomes a part of the acquirer's Employer Group.

Updated Guidance for Equity Acquisitions

The updated guidance provides that the acquirer's Employer Group remains eligible for the ERTC even if the target had been a PPP borrower.

Whether an ERTC can be claimed for post-closing amounts paid by target that had been a PPP borrower depends on actions taken by target before the transaction closing date:

- If, prior to the transaction closing date, the target entity either pays off its PPP loan or submits a forgiveness application and establishes an escrow account in accordance with the SBA's Oct. 12 Procedural Notice (more on that in this *Client Alert*), then there is no impact on the resulting Employer Group. An ERTC could be claimed in connection with wages paid to target's employees on and after the closing date.
- If, prior to the transaction closing date, the target entity **does not** pay off its PPP loan and **does not** submit a forgiveness application and establish an escrow account in accordance with the SBA's Oct. 12 Procedural Notice, then the target entity may not claim the ERTC for wages paid on or after the closing date.

Updated Guidance for Asset Acquisitions

Under the updated guidance, the following rules apply to transactions in which a PPP borrower's assets are acquired by an Employer Group that is otherwise eligible to claim the ERTC:

- If the acquiring entity does not assume target entity's PPP loan obligations, then there is no impact on the resulting Employer Group. Wages paid after closing to the target entity's former employees may be treated as qualifying wages for purposes of the ERTC. The other companies in acquirer's Employer Group remain eligible for the ERTC.
- If, as part of the transaction, the acquiring entity assumes the target entity's PPP loan, then the only impact on the resulting Employer Group is that wages paid to any of the target entity's former employees **may not** be treated as qualifying wages. The other companies in acquirer's Employer Group remain eligible for the ERTC.

Conclusion

The IRS's updated guidance provides welcome clarity for M&A transactions involving a target PPP borrower. The target entity's PPP loan generally will not affect the ERTC of the members of the acquiring group. In certain cases, the Employer Group may even be able to increase its qualifying wages for the ERTC by acquiring the target entity.

Eligibility for the ERTC is one of many tax considerations that should be considered when structuring an M&A transaction. If you have any questions about the ERTC, the PPP or this latest guidance, please contact your Vorys attorney.