

Now & Next

Tax Alert

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Employee Retention Tax Credit—January 2025 Update

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The current status of the ERC and the next steps to support your businesses.



What's the impact?

- For taxpayers that have made ERC claims and received Denial Letters, immediate consideration is required.
- Strategy for appeals and litigation vary from taxpayer to taxpayer.
- Taxpayers should reconsider their posture given the incoming administration.

Taxpayers who have filed ERC claims are generally in one of three positions.

- / They received their ERC refund.
- / They received a denial letter in the form of Letter 105C (Denial Letter) (or a partial denial letter (Letter 106C)).
- / They have received nothing.

What happens when an ERC refund is received?

In early December 2024, IRS Commissioner, Danny Werfel, announced that the IRS would be ramping up the approval of ERC claims. Similar statements have been made in the past (like in summer 2024), but the IRS fell short then and it is not entirely clear whether anything will change now, although we have seen some uptick in ERC refunds. That said, it seems unlikely that all of the estimated 1.4 million claims will be processed in the next couple of months.

As a practical matter, taxpayers who have received an ERC refund need only worry about an attempt by the IRS to clawback the refund prior to the expiration of the statute of limitations. The IRS notifies taxpayers of a clawback by issuing a Letter 6577-C, Employee Retention Credit (ERC) Recapture. The statute of limitations generally expired on April 15, 2024, for ERC 2020 claims and will expire on April 15, 2025, for ERC 2021 claims. The statute of limitations would be longer if the circumstances involved fraud.

What happens when a Denial Letter is received?—*Time is of the essence*

The IRS has been sending out tens of thousands of Denial Letters in the past several months. For taxpayers that have made ERC claims and received Denial Letters, immediate action is needed, as generally a reply is required within 30 days to preserve all appeal rights. The IRS will not extend this 30-day period.

Denial Letters are often not clear about the reasons for a denial or recourse available to the taxpayer. The IRS appears to have fixed some of the problems [we previously discussed](#) and admitted in I.R. 2024-203 (August 8, 2024) that Denial Letters were short and deficient in multiple respects including by omitting information regarding appellate rights. Now, the pendulum has swung in the other direction, and Denial Letters contain the proverbial kitchen sink and seemingly inapplicable information that needs to be carefully parsed to understand what is relevant and important.

It is important for taxpayers to know what they need to do, if anything, within the 30-day deadline. Taxpayers have two options: (a) appeal by making a submission to the Appeals Office or (b) do nothing. An appeal is made via a written submission to the Appeals Office and the instructions should be in the Denial Letter, including the address where the submission should be mailed by certified mail, return receipt requested. The submission should include the basis upon which the taxpayer qualified for the ERC. For taxpayers who did a thorough analysis of their basis for qualification prior to submitting their Forms 941-X (ERC refund requests), this should be straightforward. If this work was not previously completed, a lot of work is required and

complying with the 30-day deadline may be challenging. Taxpayers should contact their tax counsel or accountant to determine the best way to complete this submission.

Taxpayers may decide to do nothing. Failure to act within the 30-day period forfeits your right to administrative appeal, but it does not forfeit your right to file a federal suit to attempt to force the IRS to pay the ERC refund, pursuant to Section 7422¹, as discussed below. Of course, some taxpayers may decide to do nothing and simply let the process end. For these taxpayers it is important to note that the right to file a suit under Section 7422 ends two years after the date of the Denial Letter and can only be extended by the consent of the IRS. This is done on Form 907.

What happens if no ERC refund is received?

Millions of taxpayers have submitted ERC claims and have heard nothing from the IRS. These taxpayers should consider checking their tax transcripts with the IRS to make sure ERC refund checks or Denial Letters were not lost in the mail or otherwise missed.

Assuming nothing was missed and the IRS is simply still processing your amended payroll tax returns (Form 941-X), if six months have passed since you submitted the Form 941-X, you have a statutory right under Section 7422 to file a federal suit in a federal district court of competent jurisdiction (“District Court”) or the Court of Federal Claims (“Claims Court”) to force the IRS to pay substantiated ERC refund claims.

Until the IRS denies a taxpayer’s ERC refund, there is no statute of limitations on the time for filing suit under Section 7422. In theory, it could be filed decades from now, and interest would continue to accrue in favor of any legitimate ERC refund (currently the rate is 7%). However, once the IRS formally denies the ERC refund claim, the two-year period begins, and the taxpayer must file suit within this time period unless an extension is granted (Form 907). It is important to note that the administrative appeals process (discussed above) does not extend this two-year period. We understand that in many cases the administrative appeals process has been taking between 12 and 18 months to complete; however, this is not always the case, and we are also aware of matters being resolved in 30 days or less. Lengthy administrative appeals that end in denials of claims means that the window to prepare a Section 7422 may be small.

In determining whether to file a Section 7422 action, there are many strategic litigation considerations, including choosing which court to file in (District Court or the Claims Court), and whether to opt for a jury trial or a bench trial. Strategy will vary depending on each taxpayer’s situation and the basis under which they qualify for the ERC (the “suspension test” or the “gross receipts” test). Taxpayers should consult litigation counsel for advice regarding optimal strategy for filing a Section 7422 claim depending on the unique facts of their case.

¹ All references to “Section” are to the Internal Revenue Code of 1986, as amended

The number of Section 7422 complaints has increased about ten-fold since summer 2024, rising from 8 to nearly eighty, with many more in the wings. It is not clear whether this wave of lawsuits, which need to be handled by the Department of Justice (with help from the IRS), will influence the processing of the outstanding ERC claims and whether the new administration will handle things differently.

ERC under the Trump administration

President Trump's nominee for IRS Commissioner, Billy Long, has experience with the ERC. Therefore, it is important to follow his nomination process and, if confirmed, his role as IRS Commissioner. If confirmed, there is speculation that ERC processing and approval will be expedited, but that is yet to be seen. As of the date of this article, Mr. Long's confirmation hearing has yet to be scheduled, but Sen. Elizabeth Warren (D-MA) has submitted a [list of questions](#) and asked that they be provided by January 26, 2025. The prior Commissioner, Danny Werfel, announced that he was stepping down, effective January 20, 2025, which means the position is currently vacant.

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