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Internal Revenue Service
memorandum**

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subject: Whether an Employer Experienced a Full or Partial Suspension of the Operation of a Trade or Business under Section 2301 of the Coronavirus Aid, Relief, and Economic Security Act or Section 3134 of the Internal Revenue Code due to a Supply Chain Disruption

This Generic Legal Advice Memorandum (GLAM) responds to your request for assistance. This GLAM may not be used or cited as precedent.

ISSUES:

Whether, under the scenarios involving supply chain disruptions described below, the operation of an employer's trade or business was fully or partially suspended during a calendar quarter due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) due to the coronavirus disease 2019 (COVID-19) (also referred to as the "suspension test") such that the employer satisfies the definition of an "eligible employer" under section 2301(c)(2)(A)(ii)(I) of the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), Pub. L. No. 116-136, 134 Stat. 281 (March 27, 2020), and section 3134(c)(2)(A)(ii)(I) of the Internal Revenue Code (Code).

FACTS:Scenario 1

Employer A was not subject to any governmental orders limiting commerce, travel, or group meetings due to COVID-19 at any time. However, during 2020 and 2021, Employer A experienced several delays in receiving critical goods from Supplier 1. At all times during 2020 and 2021, Employer A continued to operate because Employer A had a surplus of the critical goods normally provided by Supplier 1. Employer A assumed that Supplier 1's delay in delivering critical goods was caused by COVID-19. Employer A inquired and Supplier 1 vaguely confirmed that the delay was due to COVID-19. Supplier 1 did not provide a governmental order from an appropriate governmental authority and Employer A was unable to locate one.

Scenario 2

Employer B was not subject to any governmental orders limiting commerce, travel, or group meetings due to COVID-19 at any time. However, certain critical goods from Supplier 2 were stuck at port in State X. Employer B assumed the bottleneck at the port was a result of COVID-19. Employer B could not identify any specific governmental order applicable to Supplier 2 or any specific governmental order that caused the bottleneck at the port. Some news sources stated that COVID-19 was the reason for the bottleneck, while others cited reasons such as increases in consumer spending and aging infrastructure. In addition, Supplier 2 mentioned to Employer B that other critical goods that were not stuck at port would be delayed due to a truck driver shortage. Employer B saw some discussion on social media that the truck driver shortage was because drivers were out sick due to COVID-19.

Scenario 3

Employer C and Supplier 3 are located in a jurisdiction that issued governmental orders suspending both of their business operations for the duration of April 2020. Employer C and Supplier 3's jurisdiction lifted all orders related to COVID in May 2020. For the remainder of 2020 and 2021, Employer C experienced a delay in receiving critical goods from Supplier 3. Supplier 3 does not provide a reason for the delay, but Employer C assumes the delay is due to the governmental order in place in April 2020.

Scenario 4

Employer D was not subject to any governmental orders limiting commerce, travel, or group meetings due to COVID-19 at any time. During 2020 and 2021, Employer D could not obtain critical goods from Supplier 4. However, Employer D was able to obtain the goods from an alternate supplier. The critical goods from the alternate supplier cost 35% more than those from Supplier 4. Employer D could continue to operate its trade or business even though it was not as profitable as in 2019.

Scenario 5

Employer E operates a large retail business selling a wide variety of products. Employer E was not subject to any governmental orders limiting commerce, travel, or group meetings due to COVID-19 in 2021. Due to various supply chain disruptions, Employer E was not able to stock a limited number of products and was forced to raise prices on other products that were in limited supply. However, at no time did the product shortage prevent Employer E from continuing to fully operate as a retail business during 2021.

LAW:

Section 2301 of the CARES Act, as amended by section 206 of the Taxpayer Certainty and Disaster Tax Relief Act of 2020 (Relief Act) (enacted as Division EE of the Consolidated Appropriations Act, 2021, Pub. L. No. 116-260, 134 Stat. 1182 (December 27, 2020)), provides an employee retention credit for employers subject to closure due to COVID-19.

Section 2301(a) of the CARES Act, as amended by section 206 of the Relief Act, provides that in the case of an eligible employer, there shall be allowed as a credit against applicable employment taxes for each calendar quarter an amount equal to 50 percent of the qualified wages with respect to each employee of such employer for such calendar quarter.

Section 2301(m) of the CARES Act, as amended by section 206 of the Relief Act, limits the employee retention credit under section 2301 of the CARES Act to wages paid after March 12, 2020, and before January 1, 2021.

Section 2301(a) of the CARES Act, as amended by section 207 of the Relief Act, provides that in the case of an eligible employer, there shall be allowed as a credit against applicable employment taxes for each calendar quarter an amount equal to 70 percent of the qualified wages with respect to each employee of such employer for such calendar quarter.

Section 2301(m) of the CARES Act, as amended by section 207 of the Relief Act, limits the employee retention credit under section 2301 of the CARES Act to wages paid after March 12, 2020, and before July 1, 2021.

Section 207(k) of the Relief Act provides that the amendments made by section 207 of the Relief Act shall apply to quarters beginning after December 31, 2020. Therefore, the employee retention credit under section 2301 of the CARES Act is equal to 50 percent of the qualified wages with respect to each employee of an eligible employer for calendar quarters in 2020 and 70 percent of the qualified wages with respect to each employee of an eligible employer for the first and second calendar quarters in 2021.

Section 9651 of the American Rescue Plan Act of 2021 (ARP), Pub. L. 117-2, 135 Stat. 4, enacted section 3134 of the Code. Section 3134 of the Code provides an employee retention credit for employers subject to closure due to COVID-19 that is substantially similar in structure to that of section 2301 of the CARES Act, as amended by section 207 of the Relief Act, with certain changes.

Section 3134(a) of the Code provides that in the case of an eligible employer, there shall be allowed as a credit against applicable employment taxes for each calendar quarter an amount equal to 70 percent of the qualified wages with respect to each employee of such employer for such calendar quarter.

Section 3134(n) of the Code, as amended by section 80604 of the Infrastructure Investment and Jobs Act, Pub. L. 117-58, 135 Stat. 429 (2021), limits the employee retention credit under section 3134 of the Code to wages paid after June 30, 2021, and before October 1, 2021 (or, in the case of wages paid by an eligible employer which is a recovery startup business, January 1, 2022).

Section 2301(c)(2)(A)(ii)(I) of the CARES Act defines the term “eligible employer,” in part, as any employer which was carrying on a trade or business during the calendar quarter for which the credit is determined under section 2301(a) of the CARES Act, and with respect to any calendar quarter, for which the operation of the trade or business is fully or partially suspended during the calendar quarter due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) due to COVID-19.

Section 3134(c)(2)(A)(ii)(I) of the Code similarly defines the term “eligible employer,” in part, as any employer which was carrying on a trade or business during the calendar quarter for which the credit is determined under section 3134(a) of the Code, and with respect to any calendar quarter, for which the operation of the trade or business is fully or partially suspended during the calendar quarter due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings (for commercial, social, religious, or other purposes) due to COVID-19.

Notice 2021-20, 2021-11 I.R.B. 922, provides guidance on the employee retention credit under section 2301 of the CARES Act, as amended by section 206 of the Relief Act.

Section III.C. of Notice 2021-20 provides specific guidance on orders from an appropriate governmental authority (also referred to as governmental orders).

Section III.D. of Notice 2021-20 provides specific guidance on when the operation of an employer’s trade or business is fully or partially suspended for purposes of the employee retention credit under section 2301 of the CARES Act.

Notice 2021-23, 2021-16 IRB 1113, provides guidance on the employee retention credit under section 2301 of the CARES Act, as amended by section 207 of the Relief Act.

Notice 2021-23 amplified Notice 2021-20; under Notice 2021-23, the provisions of section III.D. of Notice 2021-20 continued to apply to section 2301 of the CARES Act, as amended by section 207 of the Relief Act.

Notice 2021-49, 2021-34 IRB 316, provides guidance on the employee retention credit under section 3134 of the Code. Notice 2021-49 amplified Notice 2021-20 and Notice 2021-23; under Notice 2021-49, the provisions of section III.D. of Notice 2021-20 continued to apply to the third and fourth calendar quarters of 2021 for purposes of the employee retention credit under section 3134 of the Code.

Notice 2021-65, 2021-51 IRB 880, modified Notice 2021-49 to implement statutory changes made by the Infrastructure Act. Under Notice 2021-65, section III.D. of Notice 2021-20 no longer applied to the fourth calendar quarter of 2021 for purposes of the employee retention credit under section 3134 of the Code.

Section III.D., Q&A 12 of Notice 2021-20 provides that an employer may be considered to have a full or partial suspension of operations due to a governmental order if, under the facts and circumstances, the business's suppliers are unable to make deliveries of critical goods or materials due to a governmental order that causes the supplier to suspend its operations. If the facts and circumstances indicate that the business's operations are fully or partially suspended as a result of the inability to obtain critical goods or materials from its suppliers because the suppliers were required to suspend operations, then the business would be considered an eligible employer for calendar quarters during which its operations are fully or partially suspended and may be eligible to receive the employee retention credit.

Section III.N., Q&A 70 of Notice 2021-20 provides guidance on the records an eligible employer should maintain to substantiate eligibility for the employee retention credit.

ANALYSIS:

The statutory language in section 2301(c)(2)(A)(ii)(I) of the CARES Act and section 3134(c)(2)(A)(ii)(I) of the Code does not include supply chain disruptions. Instead, section III.D., Q/A-12 of Notice 2021-20 provides a narrow, limited exception for employers that had to fully or partially suspend their business operations because the employers' suppliers who provided critical goods or materials to the employer were fully or partially suspended during the calendar quarter due to orders from an appropriate governmental authority. This limited exception provides that "[a]n employer may be considered to have a full or partial suspension of operations due to a governmental order if, under the facts and circumstances, the business's suppliers are unable to make deliveries of critical goods or materials due to a governmental order that causes the supplier to suspend its operations."

Section 2301(c)(2)(A)(ii)(I) of the CARES Act and section 3134(c)(2)(A)(ii)(I) of the Code require that the operation of the employer's trade or business be fully or partially

suspended due to orders from an appropriate governmental authority. A supply chain disruption, by itself, does not rise to the level of a full or partial suspension primarily because no governmental order applies to the employer's operations. In addition, the goods or materials that are disrupted may not have had an impact on the employer's operations that rises to the level of a full or partial suspension, or the employer may have been able to obtain the goods or materials from an alternate supplier.

The guidance provided by section III.D., Q/A-12 of Notice 2021-20 allows the employer to "step into the shoes" of its supplier for purposes of the suspension test. To meet the terms of this exception, as explained in Q/A-12, the supplier must have been subject to a governmental order that causes the supplier to suspend its operations. In addition to having a governmental order, the employer must substantiate its eligibility for the credit by providing records or documentation demonstrating that (i) the governmental order caused the supplier to suspend operations, (ii) the inability to obtain the supplier's goods or materials caused a full or partial suspension of the employer's business operations, and (iii) the employer was not able to obtain these critical goods or materials from an alternate supplier. See Section III.N., Q&A 70 of Notice 2021-20; see also Treas. Reg. § 31.6001-1 and Treas. Reg. § 1.6001-1. If the facts and circumstances dictate that the employer's operations are fully or partially suspended because of the governmental order suspending the supplier from providing the critical goods or materials, then the employer may be considered an eligible employer under the guidance provided by Q/A-12.

CONCLUSION:

Scenario 1

Employer A does not meet the definition of eligible employer provided under section III.D., Q/A-12 of Notice 2021-20 because Employer A cannot demonstrate that a governmental order applicable to Supplier 1 fully or partially suspended Supplier 1's trade or business operations.

Even if Employer A received or could locate the governmental orders applicable to Supplier 1, Employer A did not have to cease operations because Employer A had a reserve of critical goods allowing Employer A to continue operations; thus, Employer A did not experience a full or partial suspension of operations due to an inability to obtain Supplier 1's critical goods. The relevant inquiry is whether Employer A's trade or business operations could continue; since Employer A was able to continue its own business operations despite the supply chain disruption, it was not subject to a full or partial suspension of operations.

Scenario 2

Employer B does not meet the definition of an eligible employer under section III.D., Q/A-12 of Notice 2021-20 because Employer B cannot demonstrate that a

governmental order applicable to Supplier 2 fully or partially suspended Supplier 2's trade or business operations. In addition, while COVID-19 may have been a contributing factor to the bottleneck at the port or the truck driver shortage, Employer B could not substantiate that any specific governmental order caused a bottleneck at the port. Even if Employer B could identify governmental orders applicable to the bottleneck, Employer B must substantiate that the bottleneck and thus the suspension of Supplier 2 was due to the orders.

Scenario 3

Employer C is an eligible employer in the second calendar quarter of 2020 because its business operations were fully or partially suspended due to a governmental order. However, only wages paid with respect to the period during which Employer C is fully or partially suspended due to a governmental order may be considered qualified wages. See section III.D., Q/A-22 of Notice 2021-20.

Employer C does not meet the definition of an eligible employer under section III.D., Q/A-12 of Notice 2021-20 for any subsequent calendar quarter in 2020 or 2021 because Employer C cannot demonstrate that a governmental order applicable to Supplier 3 fully or partially suspended Supplier 3's trade or business operations. The residual delays caused by a governmental order in place during a prior calendar quarter will not constitute a governmental order in subsequent calendar quarters once the order has been lifted.

Scenario 4

Employer D does not meet the definition of an eligible employer under section III.D., Q/A-12 of Notice 2021-20 because Employer D could continue to operate its trade or business. Employer D was not prevented from operating its trade or business at any point during 2020 or 2021. Incurring a higher cost for critical goods does not result in a full or partial suspension of operations.

Scenario 5

Employer E does not meet the definition of an eligible employer under section III.D., Q/A-12 of Notice 2021-20 during calendar year 2021 because Employer E cannot demonstrate that a governmental order applicable to a supplier of critical goods or materials caused the supplier to suspend operations and that Employer E was unable to obtain critical goods and materials causing a full or partial suspension of Employer E's business operations. At all points during 2021, Employer E was able to operate its retail business. While a limited number of products were not available, Employer E was still able to offer a wide variety of products to its customers and Employer E was not forced to partially suspend operations.

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Please call Matthew Leiwant (202) 317-4774 if you have any further questions.