

Taking Advantage of the Work Opportunity Tax Credit (WOTC)

Jennifer Shelton, CPA



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SWC (Steers, Walker & Company, LLP)
16875 W. Bernardo Drive, Ste. 290 | San Diego, CA 92127
p: (858) 487-4580 | f: (858) 487-8033 | e: admin@swc.cpa | w: SWC.cpa

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INTRODUCTION

Taking Advantage of the Work Opportunity Tax Credit (WOTC)

Need an incentive to hire a veteran or someone from an underserved demographic? You need to know about the Work Opportunity Tax Credit (WOTC) – a federal tax credit of up to \$9,600 for employers who hire people from specific groups facing significant barriers to employment. (Tax-exempt employers can claim the WOTC against their payroll taxes.)

The WOTC creates an incentive for business owners to increase workplace diversity while providing the unemployed and underemployed with access to good jobs. If you're a business owner or you manage a business for someone else, the WOTC provides you with the opportunity to grow your workforce at a discount as the economy recovers.

Jointly administered by the Internal Revenue Service (IRS) and the Department of Labor (DOL), the Work Opportunity Tax Credit is available for wages paid to certain individuals who begin work on or before Dec. 31, 2025. Under this program, participating companies receive a tax credit of between \$2,400 and \$9,600 per new qualifying hire.

Best of all, originally scheduled to expire at the end of 2020, the Consolidated Appropriation Act (CAA) extended the WOTC through December of 2025.

Screening Job Applicants

To take advantage of the Work Opportunity Tax Credit, you'll need to screen applicants to ensure that they qualify. To qualify, employees must meet the following criteria:

- Be a new hire, not an existing employee or previous employee being rehired
- Belong to one of the qualified groups (*see list below*)
- Perform at least 400 hours of service for the employer (employees who perform at least 120 hours of service may qualify for a partial credit)

Warning: Note that an employee's wages cannot be used for both the WOTC and the COVID-19 employee retention credit. The same wages cannot be counted twice.



To screen job applicants, create a WOTC questionnaire that they must complete and submit with their application. Your WOTC questionnaire needs to collect details that enable you to determine whether an applicant is a member of one of the qualifying groups:

- **Qualified ex-convict:** Individual was previously incarcerated or convicted of a felony and hired within one year after the conviction or release from prison.
- **Qualified Supplemental Nutrition Assistance Program (SNAP) recipient:** Individual is 18 to 39 years of age on the hire date and a member of a family that received SNAP benefits either for the six-month period ending on the hire date or for at least three of the five months ending on the hiring date in the case when a family member becomes no longer eligible for such assistance.
- **Qualified IV-A recipient:** The new hire is a member of a family that received Temporary Assistance for Needy Families (TANF) payments for any nine months during the 18-month period ending on the hire date.
- **Qualified Social Security Income (SSI) recipient:** The

new hire received SSI benefits for any month ending within 60 days of the hire date.

- **Vocational rehabilitation referral:** The new hire is considered mentally or physically disabled and was referred to your business after completion (or while receiving) rehabilitation services approved by your state, Department of Veterans' Affairs, or Social Security Administration.
- **Qualified veteran:** The new hire is a veteran of the United States armed forces who meets one or more of the following requirements:
 - Entitled to compensation for service-connected disability and is hired not more than one year after being discharged or released from active duty in the US Armed Forces
 - Member of a family that received SNAP benefits for at least a three-month period during the 12-month period ending on the hire date
 - Unemployed for a least four weeks but less than six months during the one-year period ending on the hire date
 - Unemployed for at least six months during the one-year period ending on the hire date
 - Entitled to compensation for a service-connected disability and was unemployed for at least six months during the one-year period ending on the hire date
- **Long-term assistance recipient:** The new hire is a member of a family that meets one or more of the following criteria:
 - Received TANF payments for at least 18 consecutive months ending on the hire date
 - Received TANF payments for any 18 months beginning after Aug. 5, 1997, and is hired not more than two years after the end of the earliest 18-month period
 - Stopped being eligible for TANF payments because state or federal law limited the maximum time those



payments could be made, and the individual is hired not more than two years after eligibility ended

- **Qualified summer youth employee:** The new hire is a 16- or 17-year-old who worked for your business between May 1 and Sept. 15 and lived in an empowerment zone, enterprise community, or renewal community.
- **Qualified long-term unemployment recipient:** The new hire is certified by a designated local agency as being in a period of unemployment not less than 27 consecutive weeks and includes a period during which the individual was receiving unemployment compensation under state or federal law.
- **Designated community resident:** The new hire is 18 to 39 years of age on the hire date who lives within an [empowerment zone](#), [renewal community](#), enterprise community, or a rural renewal county:
 - *An empowerment zone* is an economically distressed community eligible to receive tax incentives and grants from the federal government under the Empowerment Zones and Enterprise Communities Act of 1999.
 - *A renewal community* is a distressed urban community where qualifying businesses are eligible for billions of dollars in tax incentives.
 - *An enterprise community* is a federally designated geographic area characterized by high levels of poverty and economic distress, where businesses may be eligible to receive federal grants and tax incentives
 - *A rural renewal county* is one that's outside a metropolitan statistical area and has had a population loss during the five-year periods from 1990–1994 and 1995–1999.



Note: Employee who initially qualify your business for the Work Opportunity Tax Credit must continue living in a qualifying location for their wages to continue to qualify for the credit.

Certifying Qualified Employees

To qualify for the Work Opportunity Tax Credit, be sure to complete Form 8850 (Pre-Screening Notice and Certification Request for the Work Opportunity Credit) on or before the day you offer the applicant employment. You and your new employee must sign Form 8850 and submit it to your state workforce agency (SWA) no later than the 28th day after the employee begins work.

Other forms you must complete and file with a SWA include the following:

- ETA Form 9061 Individual Characteristics Form (ICF)
- ETA Form 9062 Conditional Certification
- ETA Form 9175 Long-Term Unemployment Recipient Self-Attestation Form (only if the new hire is a long-term unemployment recipient)

You're not permitted to claim the WOTC for an employee until you receive certification from your state workforce agency that the individual qualifies. If you receive the certification after filing your tax return, you have two options for claiming the credit later:

- File an amended tax return for the year the qualified wages were paid
- Claim the credit on the return you file the year you receive the certification



Computing the Tax Credit for Each Qualified Employee

The Work Opportunity Tax Credit generally equals 40 percent of eligible wages paid, up to a maximum of \$6,000 per employee wages during first year of employment, which results in a maximum tax credit of \$2,400 per employee.

The WOTC for a long-term family assistance recipient equals 40 percent of qualified first year wages paid, up to maximum of \$10,000 per employee wages, (which results in a maximum tax credit of \$4,000 per employee), and 50 percent of qualified

second year wages paid, up to a maximum of \$10,000 per employee wages (resulting in a maximum tax credit of \$5,000 per employee).

No credit is available until the eligible employee completes at least 120 hours of work. The credit is reduced to 25 percent of eligible wages if the employee works at least 120 hours but less than 400 hours.

For qualified veterans, the maximum per employee wages and resulting tax credits are higher:

- \$12,000 per employee for qualified veteran certified as being entitled to compensation for a service-connected disability and hired not more than one year after being discharged or released from active duty in the U.S. Armed Forces (maximum credit of \$4,800 per employee)
- \$14,000 per employee for a qualified veteran certified as being unemployed for at least six months during the one-year period ending on the hire date (maximum credit of \$5,600 per employee)
- \$24,000 per employee for a qualified veteran certified as being entitled to compensation for a service-connected disability and who was unemployed for at least six months during the one-year period ending on the hire date (maximum credit of \$9,600 per employee)

Wages qualify only if more than half of those wages are for services performed in the trade or business of the employer.

The following wages don't qualify:

- Wages paid to an individual who was previously employed by the employer at any time
- Wages paid under a federally funded on-the-job training or work supplementation program
- Wages paid to an employee in a strike replacement position



If you're not working with a tax planning and financial strategy firm like SWC, be sure to reduce your wage deduction by the allowable credit when filing your tax return yourself, even if all the credit isn't used because it exceeds the allowable general business credit for the year. If you capitalize wages instead of deducting them, reduce the capitalization amount by the allowable credit.



Recognizing the Credit Restrictions and Limitations

The following limits apply to the Work Opportunity Tax Credit:

- The credit isn't allowed for wages paid to an employee who is related to the employer.
- The carryback period for unused credit is one year and carryforward is 20 years. If any of the credit remains after Year 20, it's allowed as a deduction in the 21st year.

For up-to-date guidance on credit restrictions and limitations, see IRS Form 3800.

Claiming Your WOTC

You claim your Work Opportunity Tax Credit on IRS Form 5884 (Work Opportunity Credit). For all taxpayers except pass-through entities (partnerships, S Corporations, cooperatives, estates and trusts), the credit from Form 5884 is carried to Part III of Form 3800 General Business Credit, where it's combined with other credits, and the tax liability limit is calculated.

Taxpayers whose only source of the credit is from pass-through entities are not required to file Form 5884. Instead, report it directly on Part III of Form 3800.

Claiming Your WOTC as a Tax-Exempt Organization

Section 501(c) organizations (e.g., nonprofits) are exempt from income tax and generally ineligible for the Work Opportunity Tax Credit, but if yours is a tax-exempt organization and you hire a qualified veteran who begins work before Jan. 1, 2026, you can claim a payroll tax credit of 26 percent of that employee's qualified wages paid during the one-year period

beginning on the day the veteran begins working for your organization. You can carry forward credit claimed against your share of social security taxes and any unused credits to future calendar quarters.

Credit is reduced to 16.25 percent for any veteran who works at least 120 hours but less than 400 hours. No credit is available for a veteran who works fewer than 120 hours, and the work must be in furtherance of the organization's tax-exempt purpose or function.

To claim the credit, file Form 941 Employers Quarterly Federal Tax Return and then Form 5884-C Work Opportunity Credit for Qualified Tax-Exempt Organizations. Your organization reduces its deposits by the credit amount.

Getting Help with the Work Opportunity Tax Credit

If your head is spinning, don't worry. Taxes are complicated, which is why many people outsource them to tax planning firms like ours. Whether you need assistance creating a WOTC questionnaire for screening applicants, filing forms to certify new hires, or strategizing to maximize your WOTC, we're here to help. We can provide the guidance you need and address your questions and concerns or manage the entire process – or parts of it – for you.

About the author: Jennifer Shelton, CPA, is an accountant at SWC – a San Diego, Calif.-based tax planning and financial strategy advisory firm for small-business owners, real estate investors, and high-net-worth individuals. A graduate of Kansas State University and a member of the Kansas Society of Certified Public Accountants (KSCPA) and the American Institute of Certified Public Accountants (AICPA), Jennifer has more than 15 years of experience in public accounting with a background in taxation and accounting.

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