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WORK OPPORTUNITY TAX CREDIT

Introduction

The work opportunity tax credit (WOTC) is a federal income tax credit available to employers on hiring individuals from targeted groups that face certain employment barriers. Employers can claim up to \$9,600 per employee in tax credits per year under the WOTC program.

Applicability years

The Taxpayer Certainty and Disaster Tax Relief Act of 2020 extended the ability to claim the WOTC for members of targeted groups that begin working for the employer after 2020 and before 2026. Thus, the WOTC is in effect till December 31st, 2025.

Amount of credit available

The amount of the tax credit varies by target group. WOTC is available as a percentage of qualified first year wages paid to an employee from target group. Newly hired individuals from the following targeted groups qualify for WOTC:

1. A qualified veteran
2. A long-term family assistance recipient
3. A qualified summer youth employee
4. A qualified recipient of Temporary Assistance for Needy Families (TANF)
5. A qualified ex-felon
6. A designated community resident
7. A vocational rehabilitation referral
8. A qualified Supplemental Nutrition Assistance Program (SNAP) benefits (food stamps) recipient
9. A qualified Supplemental Security Income (SSI) recipient
10. A qualified long-term unemployment recipient

In addition to the general qualification, there are specific qualifications within each category of target group.

The qualified wages eligible for WOTC are limited from \$ 3,000 to \$ 24,000 per employee depending on the target group. There is no limit on number of employees eligible for WOTC.

The employee must work at least 120 hours to qualify for the credit and must not have worked for the taxpayer previously. Depending on the number of hours worked, 25% to 40% of the qualified wages is available as Work Opportunity Tax Credit to the employers.

In case of an employee certified as a long-term family assistance recipient, 50% of qualified second-year wages is available as WOTC.

Qualified wages exclude wages against which employee retention credit (ERC) or credit for qualified sick and family leave wages is claimed.

Certain restrictions

Following do not qualify for WOTC:

1. The wages for services of replacement employees during a strike or lockout are not qualified for WOTC.
2. The employee must not be your dependent or be related as per IRC section 51(i)(1).

Pre-screening and Certification

The taxpayer must obtain certification from the State Workforce Agency (SWA) of the state in which your business is located by submitting Form 8850: Pre-Screening Notice and Certification Request for the Work Opportunity Credit, that an individual is a targeted group member before WOTC is claimed.

The taxpayer must submit the signed form 8850 within 28 calendar days from the day the individual begins to work for the taxpayer. The SWA will issue determinations (certifications or denials) for individuals.

The taxpayer must obtain filled in page 1 of IRS Form 8850 from the employee and complete page 2 of the same form. The taxpayer can include this in their HR onboarding process.

Claiming the credit

Once taxable employers receive certification from SWA, WOTC can be claimed as general business credit on Form 3800 by filing Form 5884 along with the tax returns. This credit may be claimed only against business income tax liability and unutilized credit amount may be carried forward 20 years and carried back 1 year.

Qualified tax-exempt organizations can claim WOTC against the employer social security tax by separately filing Form 5884-C. The credit will not affect the employer's Social Security tax liability reported on the organization's employment tax return. Tax-exempt organizations may claim this credit only for qualified veterans certified by SWA.

What can KNAV help with?

- Assist the client in computation of credit and filing the credit claim along with the income tax return.
- Co-ordination with client's HR team/ payroll team for the purpose of above.

If you have any queries, please get in touch with us at tax@knavcpa.com

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