



## IRS Gets Favorable Result in Bankruptcy Court Opinion: What Is an Order? What Is a Suspension? And Who Decides?

By Zachary Lyda, Esq.

The Internal Revenue Service (“IRS”) got a highly favorable result for its positions on what constitutes a governmental order and partial suspension of operations in the Employee Retention Credit (“ERC” or the “Credit”) context. On August 7, 2025, Judge Joseph N. Callaway of the United States Bankruptcy Court for the Eastern District of North Carolina issued a decision granting the government summary judgement in JSmith Civil LLC v. United States of America, Adv. Proc. No. 24-00004-5-JNC, (Bankr. E.D.N.C Aug. 7, 2025). This decision marked the first instance of a court wrestling with the idea of what qualifies as a governmental order and what actions by a business result in a partial suspension of operations.

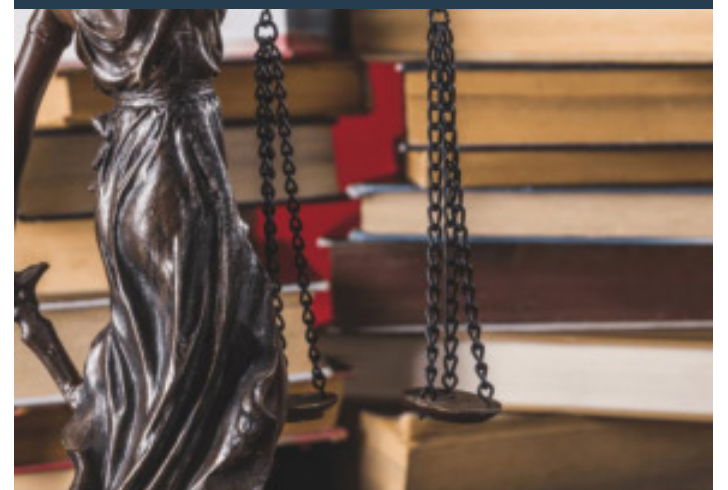
### Background

JSmith Civil LLC (“JSmith”) filed for bankruptcy in September of 2023. During the pandemic it provided construction related activities in North Carolina. At issue in this case are its claims for the Credit for the second quarters of 2020 and 2021. In total it sought over \$1 million in refunds between those two claims. In support of its position, it indicated that it was required to follow orders from the governor of North Carolina, Occupational Safety and Health Administration (“OSHA”), North Carolina Department of Labor (“NCDOL”), and the Centers for Disease Control and Prevention (“CDC”) which it argued resulted in a partial suspension of operations.

### The Opinion

The Court draws a distinction between COVID-era government support programs. It describes some programs as being “presumption-in” and others being “presumption-out.” A “presumption-in” program is one that generally allows broad access to the program with specific groups exempted from access, such as the stimulus payments during the pandemic. The Court, in contrast, describes the ERC program as being a “presumption-out” program that requires businesses to meet “. . . more traditional and onerous eligibility criteria” to be eligible for the Credit. After providing a recitation of requirements to be an eligible employer

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for purposes of the Credit, the Court points out that the terms “partial,” “suspension,” and “orders from an appropriate governmental authority” are not defined in the statute. The Court then cites *Loper Bright Enters. v. Raimondo*, 603 U.S. 369 (2024), for the proposition that it is now up to the Court to use canons of statutory construction to define these crucial terms.

The Court defines a partial suspension as “. . . a temporary stoppage of a portion of operations” and appears to give deference to the IRS’s idea that such suspension must involve a more than nominal portion of the business’s operations. The Court next turns to what constitutes a governmental order. According to the Court, “. . . an order must be compulsory.” Furthermore, it must “. . . impose binding requirements or repercussions for noncompliance.” Put together the Court indicates that three elements must be satisfied for a business to qualify as an eligible employer for purposes of ERC:

1. The business was subject to a compulsory governmental mandate limiting commerce, travel, or group meetings that was issued because of the pandemic.
2. The business stopped a meaningful portion of its operations during the relevant quarter. (Emphasis added).
3. The reason the business stopped operating was that the governmental mandate directly required it.

The Court then proceeds to walk through the orders cited by JSmith but does not find any as supporting eligibility for the Credit. Because construction activities were exempted from the governor’s orders, the Court said they were inapplicable to JSmith, even if it chose to follow

them. The other orders cited by JSmith such as those by OSHA, NCDOL, and the CDC, the Court said were not really mandates. Even when NCDOL cited JSmith for failure to have a proper infection control policy, the Court said it was not an order.

The Court further indicated that general disruptions to business activities are not sufficient to rise to a level of partial suspension of business operations. The Court stated “. . . while there is no doubt various delays, quarantines, sicknesses, and other disruptions occurred, general pandemic conditions caused those closures, not shut down orders.” Because the Court indicates that, in its opinion, JSmith was not required to follow the governmental orders it cited, it found the impacts to the business were immaterial.

### Takeaways

This decision, while well written and well-reasoned, did not include the analysis that businesses and their representatives wanted to see. It appears to create a more onerous eligibility path for businesses than what appeared to be intended by Congress when it put money into advertising this broad-based COVID support program.

One element of the decision that has caught tax practitioners’ eyes is the definition of “partial.” The Court takes the time to outline the Black’s Law Dictionary’s definition of partial: “Not complete; of, relating to, or involving only a part rather than the whole.” However, in the test the Court derives it refers the suspension as having to affect a “meaningful” portion of the business’s operations. The Court appears to make this determination





considering the IRS’s “more than a nominal portion” standard; however, it seems to be a sizable leap to go from “more than nominal” to “meaningful.” This rhetorical leap is also compounded by the fact that the “more than nominal” standard created by the IRS is not in the law. In fact, as discussed above, nothing more than a “partial” suspension is necessary under the text of the law.

Another key takeaway that the IRS appears to now be overlooking, is that this is but one judge’s opinion. This decision, and its reasoning, carries zero precedential weight. The IRS, in recent matters, has cited this decision as if its definitions and pronouncements on orders and suspension are binding on the entire country. This is wrong. Many businesses and their representatives would likely disagree with some of the analysis of this Court. Those businesses may ultimately get the opportunity to persuade a different court that a different definition of partial suspension or governmental order is superior or more in line with the spirit of the law when it was drafted to provide support for businesses across the country.

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