PPP, EIDL & ERC

January 28, 2021

ARIZONA SMALL BUSINESS BOOT CAMP & COLLECTIVE

RESPOND → PLAN → RETURN STRONGER

the IDEA GARDENER®
Business Development & Strategy

BeachFleischman
collaborate forward

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Disclaimer

This presentation is based on relevant government guidance available as of January 27, 2021. Detailed transition guidance is not yet available for companies eligible for ERC who have already filed for or received forgiveness. We anticipate additional guidance from the IRS/SBA in the coming weeks. This presentation includes our best interpretation of the guidance available today.

The information provided here today is high level. Consult with your CPA for more detailed information on claiming the ERC.

PPP Loan Forgiveness

What's Next?

Math. Lots of math.

Changes to Loan Forgiveness

- The Consolidated Appropriations Act, 2021 (CAA) included a few changes to the loan forgiveness rules.
- On January 19, 2021 the SBA released revised loan forgiveness applications that incorporate the changes.
- Forms can be found here: https://home.treasury.gov/policy-issues/cares/assistance-for-small-businesses

Changes to Loan Forgiveness

- Form 3508S can now be used for loans up to $150,000
- HOWEVER, the breaks given to loans under $50,000 do not apply to loans between $50,001 and $150,000
- The latter must still comply with the FTE reduction rules and the wage rate reduction rules.

FTE Reduction Rules

- Borrowers who complete the 3508S, but who meet the requirements outlined in the instructions to 3508EZ (unable to operate at the same level due to COVID orders) may be exempt from the FTE reduction.
- Those who are not exempt must adjust their costs eligible for forgiveness by the ratio of employees during the covered period to employees during a selected base period.
- The rules are outlined in the instructions to Form 3508

FTEs

- Basic FTE Formula: Hours worked per week / 40

  Examples…
  Joe works 30 hours a week, he is a 0.75 FTE
  Mary works 20 hours a week, she is a 0.5 FTE
  Bob works 55 hours a week, he is a 1.0 FTE
  (can't be more than 1.0)

- For a payroll that includes the 3 employees above, the FTE count is: 0.75 + 0.5 + 1.0 = 2.25

FTEs

- The Application allows a simplified method of computing FTEs. Employees working 40 or more hours are 1.0, employees <40 are 0.5.

  Example using the simplified method…
  Joe works 30 hours a week, he is a 0.5 FTE
  Mary works 20 hours a week, she is a 0.5 FTE
  Bob works 55 hours a week, he is a 1.0 FTE

- For a payroll that includes the 3 employees above, the FTE count is: 0.5 + 0.5 + 1.0 = 2.0

FTEs

- For all periods that you have to compute FTEs, you need to pick one method (actual or simplified) and use it for all periods.
- Owners are EXCLUDED from all FTE computations.
- “Owner” has been defined as “an owner who is also an employee.” Assume any employee that has any stock ownership interest in a C-corp or S-corp is included.

FTEs

- The math for computing FTEs is based on the following paragraph in the Application:

Average FTE: This calculates the average full-time equivalency (FTE) during the Covered Period or the Alternative Payroll Covered Period. For each employee, enter the average number of hours paid per week, divide by 40, and round the total to the nearest tenth. The maximum for each employee is capped at 1.0. A simplified method that assigns a 1.0 for employees who work 40 hours or more per week and 0.5 for employees who work fewer hours may be used at the election of the Borrower.

- Step 1: Compute average number of hours paid per week
- Step 2: Divide by 40
- Step 3: Round to the nearest tenth

FTEs

- The FTE average during the covered period (or APCP) is then compared to the FTE average during the "base period"

- There are two options for the base period:
  - Option 1: 2/15/19 – 6/30/19
  - Option 2: 1/1/20 – 2/29/20

- Compute your FTE averages for both periods to determine which one is lower.

FTEs

- EXAMPLE: Compare the results:
  Option 1 average FTEs: 10.5
  Option 2 average FTEs: 6.8

- Select option 2 so that you are comparing your covered period to the smaller number.

FTEs

- Let's do the math…
  Average FTEs was 8.4 for the covered period
  Option 1 average FTEs: 10.5
  Option 2 average FTEs: 6.7

- Using Option 1, there would be a 20% reduction in the amount of costs eligible for forgiveness.
  (10.5 - 8.4) = 2.1   2.1 / 10.5=20%

- With Option 2, there's NO reduction.

Wage rates

- There is a second forgiveness reduction formula that needs to be considered.
- Concept: If wage rates decrease more than 25%, there is a reduction to costs eligible for forgiveness.

Wage rates

- Example: Joe is full-time and normally makes $1,000 per week, but you cut his salary to $650 per week (still full-time). If Joe was receiving the reduced salary for all eight weeks in the covered period, you would reduce eligible loan forgiveness by $800 for Joe.

  $1,000 * 25% = $250 is the allowed reduction
  Joe's reduction is $1,000 - $650 = $350
  Penalty is: ($350 - $250) * 8 weeks = $800

Wage rates

- Example: Mary makes $20 per hour but you cut her rate to $13 per hour. Mary averages 30 hours per week. The reduction to loan forgiveness for Mary is $480.

  $20 * 25% = $5 is the allowed reduction per hour
  Mary's reduction was $20 - $13 = $7
  Penalty is: ($7 - $5) * 30 hours * 8 weeks = $480

Wage rates

- The revised Application instructions indicate that wage rates (hourly rate or base salary) would be compared between *the most recent calendar quarter* and the covered period.

Covered Costs

- The amount of forgiveness is based on the amount of loan proceeds spent on covered costs during the Covered Period

- Covered costs:
  - Payroll costs
  - Rent
  - Interest
  - Utilities

Costs added by the CAA:
- Covered operations expenditures
- Covered property damage costs
- Covered supplier costs
- Covered worker protection expenditures

Covered Costs – Payroll Costs

- Payroll costs… this is the exact same definition that you used when you compiled your 2019 data to get your PPP loan.

  - Gross wages (salaries, wages, commissions, etc.)**
  - Cash tip or equivalent
  - Vacation, parental, family, medical or sick leave**
  - Group health insurance premiums, employer portion
  - Retirement contributions, employer portion
  - State unemployment taxes

Covered Costs – Payroll Costs

** The amount of wages claimed cannot include qualified sick leave wages for which a credit is allowed under the Families First Coronavirus Response Act (FFCRA)

The amount of wages claimed cannot include qualified family leave wages for which a credit is allowed under the FFCRA.

The benefits in FFCRA are separate from PPP, but you can't "double dip".

Covered Costs – Payroll Costs

** The amount of wages claimed cannot include wages that are used for the Employee Retention Credit.

The ERC program and the PPP are separate, but you can't "double dip".

Covered Costs – Nonpayroll Costs

- Rent… Includes rent for real or personal property under a leasing agreement in force (signed) before February 15, 2020.

- Real property = building, storage unit
  Personal property = equipment, vehicles

Covered Costs – Nonpayroll Costs

- Utilities... Includes services for the distribution of electricity, gas, water, sewer, transportation, telephone or internet access for which service began before February 15, 2020.

Covered Costs – Nonpayroll Costs

- Interest… Includes interest (not principal) on loans secured by real or personal property that were in effect before February 15, 2020.
- If you have any capital leases, they would <u>not</u> get counted as "rent" since they are a financing agreement. The monthly interest component would be considered a covered cost.

Covered Costs – Nonpayroll Costs

- Covered operations expenditures:

  Payments for any business software or cloud computing service that facilitates business operations, product or service delivery, the processing, payment or tracking of payroll expenses, human resources, sales and billing functions, or accounting of tracking of supplies, inventory, records and expenses.

Covered Costs – Nonpayroll Costs

- Covered property damage costs:

  Costs related to property damage and vandalism or looting due to public disturbances that occurred during 2020 that were not covered by insurance or other compensation.

Covered Costs – Nonpayroll Costs

- Covered supplier costs:

  Expenditures made to a supplier of goods for the supply of goods that are essential to the operations of the Borrower at the time at which the expenditure is made, and made pursuant to a contract, order or purchase order in effect prior to the beginning of the covered period (or for perishable goods, the contract order or PO may have been in effect before or at any time during the covered period)

Covered Costs – Nonpayroll Costs

- Covered worker protection expenditures:

  Operating or capital expenditures that facilitate the adaptation of the business activities of an entity to comply with the requirements established or guidance issued by the DHHS, CDC or OSHA or any equipvalent requirements established or guidance issued by a state or local government during the period starting 3/1/2020 and ending on the date on which the national emergency for COVID-19 expires....

Covered Costs – Nonpayroll Costs

- Covered worker protection expenditures (continued):

  … related to maintenance standards for sanitation, social distancing, or any other worker or customer safety requirement related to COVID-19, but does not include residential real property or intangible property.

Covered Costs

IMPORTANT DISTINCTION:

All eligible payroll and nonpayroll costs must be paid or incurred during the covered period.

Covered Costs

- Once you have all of your covered costs captured for the covered period, you have to evaluate the total and the components.
- At least 60% of total costs incurred must be payroll costs.
- There is a reduction in forgiveness if you don’t reach 60% or if you don’t spend all of the money.

Covered Costs

- Example: You receive a $100,000 PPP loan. You spend $80,000 on payroll costs and $15,000 on other covered costs.
- Total spent = $95,000
- Payroll costs = 84% ($80,000 / $95,000)
- Reduction is $5,000. You met the 60% test, but you didn't spend all of the proceeds on covered costs.

Covered Costs

- Example: You receive a $100,000 PPP loan. You spend $55,000 on payroll costs and $45,000 on other covered costs.

- Total spent = $100,000

- Payroll costs = 55% ($55,000 / $100,000)

- Reduction is $8,333. Maximum forgiveness is a function of the amount spent on payroll costs: $55,000/60% = $91,667 maximum forgiveness

Summary of the Forgiveness Formula

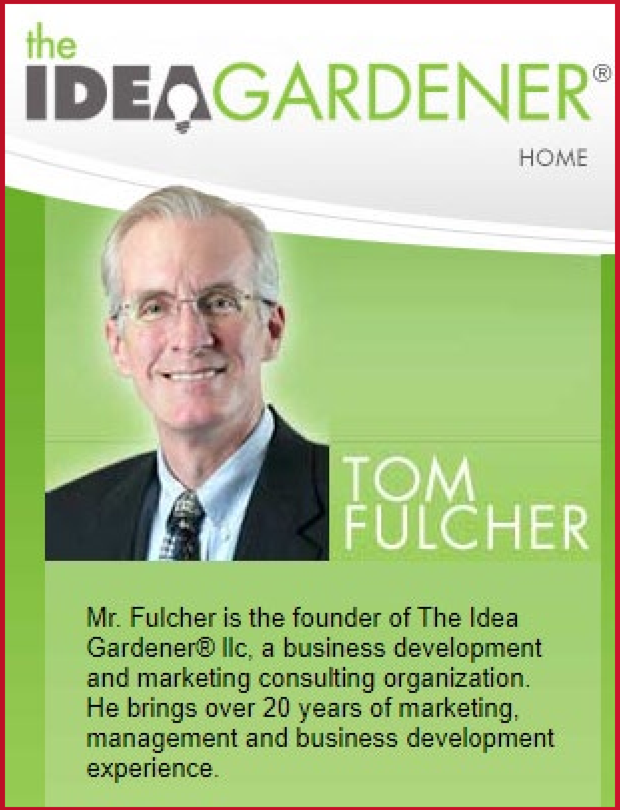
- Forgiveness amount is the lesser of the following 3 numbers:

  ~ (Total spent – wage reduction) * FTE Reduction Quotient

  ~ PPP Loan Amount

  ~ Total payroll costs incurred divided by 0.6

EIDL Advances



EIDL Advances

- CARES Act Program
- EIDL: Economic Injury Disaster Loan – this is a longstanding SBA program
- Businesses could apply for an emergency advance equal to $1,000 per employee, up to a maximum of $10,000
- Application was very short, done online

EIDL Advances

- These advances do not have to be repaid
- Prior to the CAA, a company with a PPP loan had to reduce the amount of forgiveness by their EIDL advance
- The CAA repealed that provision, retroactively
- Any business who had their forgiveness reduced already will be made whole in 2021

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EIDL Advances

- It is not taxable (clarified in CAA)
- Costs it was used for are deductible (clarified in CAA)

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EIDL Loans

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EIDL Loans

- EIDL Loans are <u>totally separate</u> from the EIDL Advances
- Companies that applied for and received an EIDL loan in 2020 received up to $150,000
- Terms are statutory:
  - 3.75% interest rate (2.75% for nonprofits)
  - 12 month delay in repayment
  - Up to 30 year amortization
  - No collateral required

EIDL Loans

- The EIDL Loan is a real loan, it has to be repaid, there are no forgiveness provisions on this one

EIDL and Targeted EIDL Advance

- ***Extended through12/31/21 or while funds last***
  - ***Do not expect to get a second EIDL***

We are still awaiting new guidance from the SBA

Information provided herein sourced from U.S. SBA and Treasury Dept –
Nothing herein intended as guarantee of loan forgiveness or accuracy due to continually changing situation

Targeted EIDL Advances/Grants

- *Priority One*
  - *Received an EIDL Loan*
  - *Located in Low Income Community*
  - *30% Reduction in Gross Receipts (8-week period March 2 or later)*
- ✓ *Grant when combined with Advance totals $10K*
- *Priority Two*
  - *Received an EIDL Loan prior to 12/27/20 but no Advance*
    - *$1,000/employee up to $10,000 max*

SBA Outreach ***Unclear on new EIDLs***

Information provided herein sourced from U.S. SBA and Treasury Dept –
Nothing herein intended as guarantee of loan forgiveness or accuracy due to continually changing situation

SBA Debt Relief

Extended & Enhanced

7a, 504, microloans

- Already received debt relief
  - Three more months
  - Eight more months
- Loan approved 9/28/20-1/31/21?
  - 0, 6 or 9 months
- New Loan 2/1/21-
  - 6 months (+?)

We have new guidance from the SBA but seeking clarifications

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SBA Debt Relief

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Shuttered Venue Operator Grants

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Shuttered Venue Operator Grants

NAICS 71-Arts, Entertainment and Recreation

- Live venue operators or promoters
- Theatrical producers
- Live performing arts organization operators
- Relevant museum operators, zoos and aquariums who meet specific criteria
- Motion picture theater operators
- Talent representatives, and
- Each business entity owned by an eligible entity that also meets the eligibility requirements

Other requirements of note:

- Must have been in operation as of February 29, 2020
- Venue or promoter must not have received a PPP loan on or after December 27, 2020

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Shuttered Venue Operator Grants

NAICS 71-Arts, Entertainment and Recreation

- In operation on January 1, 2019
  - 45% of their 2019 gross earned revenue OR $10 million, whichever is less.

- Began operation after January 1, 2019
  - The average monthly gross revenue for each full month in operation during 2019 multiplied by six (6) OR $10 million, whichever is less.

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Shuttered Venue Operator Grants

NAICS 71-Arts, Entertainment and Recreation

- Priorities
  1. 90%+ reduction in gross earned revenues 4/2/20-12/31/20
     - First 14 days
  2. 70%+ reduction in gross earned revenues 4/2/20-12/31/20
     - Next 14 days
  3. 25%+ reduction in gross earned revenues 4/2/20-12/31/20
     - Next
  4. Supplemental Funding
     - 70% or greater loss in most recent quarter (starts 4/1/21)

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Shuttered Venue Operator Grants

NAICS 71-Arts, Entertainment and Recreation

- Other
  1. Allowable Use of Funds rules (and prohibited)
  2. No application yet
  3. Open Questions
     - Many. eg: Earned vs Contributed Revenues

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Employee Retention Credit

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Employee Retention Credit (ERC)

The Consolidated Appropriations Act 2021 (CAA), which was passed in late 2020 did two things:

- Removed the prohibition against companies who receive a PPP loan from taking the ERC
- Extended the ERC through June 30, 2021 with some modifications to the rules for 2021

Employee Retention Credit (ERC)

The ERC is computed using eligible wages and allocable health care costs:

- Eligible wages are generally gross wages paid during the relevant period
- Allocable health care costs are costs for insurance that are related to the relevant period (could be paid earlier or later)

Eligibility

- The credit is available for March 12, 2020 – December 31, 2020 as well as January 1, 2021 – June 30, 2021
- The eligibility and credit computations are different for 2020 and 2021
- We will address each year individually

2020

The following slides are related to the ERC for 2020, and 2020 only.

Before we start talking about 2021, you will see another blue slide like this.

Do not confuse the rules for each year.

ERC 2020 - Eligibility

Two different ways to be eligible for the 2020 credit:

- Business had operations that were fully or partially suspended during any calendar quarter in 2020 due to government COVID-related orders. The credit only applies to wages paid during the portion of the quarter that the business is suspended, not the entire quarter, OR
- Business experienced a significant decline in gross receipts during any quarter in 2020. An employer is considered to have a significant decline in gross receipts for the period beginning with the first quarter in 2020 for which its gross receipts are less than 50 percent of gross receipts from the same quarter in 2019 and ending with the earlier of January 1, 2021 or the first quarter after the quarter for which gross receipts are greater than 80 percent of gross receipts for the same quarter in 2019.

ERC 2020 - Eligibility

- For the first bullet, the company should document the specific government orders that caused them to be fully or partially shut down
- Only wages and allocable health costs during the shut down period are eligible for the ERC

ERC 2020 - Eligibility

- For the second bullet, the company will have to look at 2020 and 2019 gross receipts
- Use the accounting method that the company uses for internal accounting or their income tax method of accounting
- If a company does not maintain quarterly records, they can compute annual gross receipts to meet the 50% test

ERC 2020 - Eligibility

EXAMPLE 1				
2019				
Q1	Q2	Q3	Q4	Total
50,000	60,000	70,000	80,000	260,000
2020				
Q1	Q2	Q3	Q4	Total
75,000	25,000	35,000	60,000	195,000
Relationship of 2020 to 2019				
Q1	Q2	Q3	Q4	Total
150%	42%	50%	75%	75%
NOT ELIGIBLE	Eligible Qtr	Eligible Qtr	Eligible Qtr	

EXAMPLE 2				
2019				
Q1	Q2	Q3	Q4	Total
50,000	60,000	70,000	80,000	260,000
2020				
Q1	Q2	Q3	Q4	Total
75,000	25,000	58,000	75,000	233,000
Relationship of 2020 to 2019				
Q1	Q2	Q3	Q4	Total
150%	42%	83%	94%	90%
NOT ELIGIBLE	Eligible Qtr	Eligible Qtr	NOT ELIGIBLE	

ERC 2020 – Compute the Credit

Wages/costs eligible for the credit is dependent on how many employees (EEs) you had in 2019.

Compute the number of full-time EEs you had in 2019.

Only include EEs who average more than 30 hrs/wk

Formula:

$$\frac{\text{Number of full-time EEs in each calendar month in 2019}}{12}$$

ERC 2020 – Compute the Credit

For more information on computing the number of employees, you can read the IRS FAQ:

https://www.irs.gov/newsroom/covid-19-related-employee-retention-credits-determining-qualified-wages-faqs

ERC 2020 – Compute the Credit

- Employers with 100 or fewer full-time EEs in 2019 can use all wages (including health care costs) paid: during the affected period/quarter and after March 12, 2020, minus any FFCRA wages.

- Employers with more than 100 employees can only take the credit on wages and health care costs paid to/for employees who were not working (literally paid while staying home and not providing services).

ERC 2020 – Compute the Credit

The credit is the first 50% of the first $10,000 in wages and allocable health care costs paid during the affected period/quarter to each eligible employee

Maximum credit for 2020 is $5,000 per employee

ERC 2020 – Compute the Credit

Important restriction #1:

Wages do not include wages paid under the family and/or sick leave provisions of FFCRA, the Families First Coronavirus Response Act. In addition, wages claimed for employees under the Work Opportunity Credit do not qualify as wages that may increase this credit. Wages paid to relatives or family members generally do not qualify. With entities, one applies these relationship rules depending on a particular level of ownership.

ERC 2020 – Compute the Credit

Important restriction #2:

Any wages used in the computation of the ERC are not eligible covered costs on the application for forgiveness of a PPP loan.

You can see how retroactively claiming the credit for 2020 gets interesting if you have already filed for or received forgiveness.

ERC 2020 – Compute the Credit

Important restriction #3:

There are aggregation rules that can affect parent-subsidiary or brother-sister groups, or a combined group of corporations. These complex rules can also reach partnerships, trusts and estates. Aggregation can affect qualification in such areas as to whether there is a full or partial shutdown as well as measuring the decline in gross receipts.

ERC 2020 – Claim the Credit

- Claim the credit on the quarterly Form 941

- Credits in excess of the quarterly employment tax deposits, you can request an advanced payment from the IRS on Form 7200

https://www.irs.gov/newsroom/how-to-claim-the-credits

ERC 2020 – Claim the Credit

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https://www.irs.gov/newsroom/how-to-claim-the-credits

ERC 2020

- For more details on the ERC 2020, there is an article on our website:

  https://beachfleischman.com/tax-bites/2020/04/employee-retention-credit/

- The IRS also has extensive FAQs on the ERC:

  https://www.irs.gov/newsroom/faqs-employee-retention-credit-under-the-cares-act

SWITCHING GEARS TO 2021

Please note that the slides from this point forward are related to the ERC for 2021.

Do not confuse the rules for each year.

ERC 2021 - Eligibility

Two different ways to be eligible for the 2020 credit:

- Business had operations that were fully or partially suspended during the 1st or 2nd quarter in 2021 due to government COVID-related orders. The credit only applies to wages paid during the portion of the quarter that the business is suspended, not the entire quarter, OR

- Business experienced a significant decline in gross receipts during the 1st or 2nd quarter of 2021. An employer is considered to have a significant decline in gross receipts only for the quarters for which its gross receipts are less than 80 percent of gross receipts from the same quarter in 2019.

ERC 2021 - Eligibility

- For the first bullet, the company should document the specific government orders that caused them to be fully or partially shut down
- Only wages and allocable health costs during the shut down period are eligible for the ERC

ERC 2021 - Eligibility

- For the second bullet, the company will have to look at 2021, 2020 and 2019 gross receipts
- Use the accounting method that the company uses for internal accounting or their income tax method of accounting
- There is a lookback rule, that says if you don’t meet the test for a quarter you can look at the immediately preceding quarter

ERC 2021 - Eligibility

EXAMPLE 1	
2019	
Q1	Q2
50,000	60,000
2021	
Q1	Q2
35,000	45,000
Relationship of 2021 to 2019	
Q1	Q2
70%	75%
Eligible Qtr	Eligible Qtr

The example at right is a demonstration of the allowable lookback rule.

EXAMPLE 2		
2019		
Q4 2019	Q1 2019	Q2 2019
80,000	50,000	60,000
2020	2021	2021
Q4 2020	Q1 2021	Q2 2021
60,000	45,000	45,000
Relationships		
Q4	Q1 2021	Q2 2021
75%	90%	75%
	Eligible Qtr	Eligible Qtr

ERC 2021 – Compute the Credit

Wages/costs eligible for the credit is dependent on how many employees (EEs) you had in 2019.

Compute the number of full-time EEs you had in 2019.

Only include EEs who average more than 30 hrs/wk

Formula:

$$\frac{\text{Number of full-time EEs in each calendar month in 2019}}{12}$$

ERC 2021 – Compute the Credit

- Employers with 500 or fewer full-time EEs in 2019 can use all wages (including health care costs) paid: during the affected period/quarter, minus any FFCRA wages.

- Employers with more than 500 employees can only take the credit on wages and health care costs paid to/for employees who were not working (literally paid while staying home and not providing services).

ERC 2021 – Compute the Credit

The credit is the first 70% of the first $10,000 in wages and allocable health care costs paid during the affected period/quarter to each eligible employee

Credit is computed independently for Q1 and Q2 of 2021

Maximum credit for 2021 is $14,000 per employee

ERC 2021 – Compute the Credit

Important restriction #1:

Wages do not include wages paid under the family and/or sick leave provisions of FFCRA, the Families First Coronavirus Response Act. In addition, wages claimed for employees under the Work Opportunity Credit do not qualify as wages that may increase this credit. Wages paid to relatives or family members generally do not qualify. With entities, one applies these relationship rules depending on a particular level of ownership.

ERC 2021 – Compute the Credit

Important restriction #2:

Any wages used in the computation of the ERC are not eligible covered costs on the application for forgiveness of a PPP loan.

For entities who are applying for a PPP2 loan, they have time to plan and allocate wages between FFCRA, ERC and PPP.

ERC 2021 – Compute the Credit

Important restriction #3:

There are aggregation rules that can affect parent-subsidiary or brother-sister groups, or a combined group of corporations. These complex rules can also reach partnerships, trusts and estates. Aggregation can affect qualification in such areas as to whether there is a full or partial shutdown as well as measuring the decline in gross receipts.

ERC 2021 – Claim the Credit

- Claim the credit on the quarterly Form 941
- Credits in excess of the quarterly employment tax deposits, you can request an advanced payment from the IRS on Form 7200

https://www.irs.gov/newsroom/how-to-claim-the-credits

Q&A