



***PPP Loans 1 & 2 and the Stimulus  
Package: What You Need to Know***

**Thursday, January 21, 2020**

**3:00 pm PST**

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# Agenda for Today

- **PPP1** - what you need to know about applying for forgiveness and what you should be doing right now.
- **PPP2** - do you qualify and if so, how much will you get and what steps you should take right now.
- **The Employee Retention Credit** - how this can generate significant relief for your business.
- **A summary** of the major tax provisions of the year-end bill.
- **Q & A**

# PPP1 – Loan Forgiveness - Taxability

- Federal law - forgiveness is nontaxable, deductions are deductible, no tax attribute is reduced, and no basis increase denied.
- This result applies to both PPP1 and PPP2.

## PPP1 – Loan Forgiveness – Taxability, Continued

- California law – a whole different story.
- Forgiveness is nontaxable, but the deductions paid or incurred related to the forgiveness are NOT DEDUCTIBLE.
- California law (AB 1577) states that it is only applicable to “taxable years beginning on and after January 1, 2020”. This creates the following problems:
  - What do you do with fiscal year taxpayers?
  - What do you do when forgiveness occurs in 2021, but expenses are incurred/paid in 2020?



## PPP1 – Loan Forgiveness – Taxability, Continued

- California FTB solution: adopt IRS Rev. Rul. 2020-27 which reaffirmed nondeductibility of expenses under IRC section 265 and denied deduction of expense in 2020 if borrower “reasonably expected to receive forgiveness” in 2021.
- For fiscal year taxpayers:
  - If forgiveness received in 2019 fiscal year, amount of loan is taxable.
  - If forgiveness received in 2020 fiscal year, take deductions in 2019 fiscal year and then full loan amount taxable in 2020 under tax benefit rule.

## PPP1 – Loan Forgiveness – Taxability, Continued

- Problems with FTB positions:
  - Relies on a revoked IRS Revenue Ruling that was originally based on an entirely different statute and was expected to be challenged.
  - AB 1577 does NOT refer to IRC section 265 as authority.
  - Uses three different theories of taxation depending on whether taxpayer is fiscal year and when taxpayer files for forgiveness.
- Our recommendation: wait for more guidance, extend your 2020 tax return, and consider paying the California tax for 2020 by the due date of the return.



# PPP1 – Loan Forgiveness – New Eligible Expenditures

- The Act added new expenditures eligible for forgiveness - for BOTH PPP1 and PPP2
- These include covered operations expenditures such as software or cloud computing costs, covered property damage costs (from riots), covered supplier costs for goods that are essential to the operation of the borrower, and covered worker protection expenditures

## PPP1 – Loan Forgiveness – When to Apply

- The earliest that a PPP loan payment can be required is 10 months after the end of the 24-week covered period. This means most loan payments are not due until late summer.
- Forgiveness applications can be made up to 2 years after funding.
- The forgiveness process should become more streamlined and more certain over time.
- More guidance is needed regarding the interplay between PPP1 forgiveness and the Employee Retention Credit for 2020 – more on that later.

## PPP1 – Loan Forgiveness – When to Apply, Continued

- What does that add up to? WAIT.
- We recommend waiting until 2<sup>nd</sup> quarter 2021 to file – preferably May or June to give more time for simplification and clarification.

## PPP2 – Who Qualifies

- Reduction of gross receipts by 25% or more for any calendar quarter in 2020 as compared to the same calendar quarter in 2019.
- Test only needs to be met for one quarter in 2020.
- Ability to utilize 2020 total gross receipts versus 2019 total gross receipts.
- Have 300 or fewer employees - headcount average, not FTE, for preceding 12 months.

## PPP2 – Who Qualifies, Continued

- How do you calculate gross receipts? All revenue in whatever form received or accrued recorded under the method used by the business for its books and records.
- Does not include EIDL advances or PPP loan proceeds.
- Does not include gains or losses from sale of capital assets.
- Are interest, dividends and rents included? Yes per FAQ, perhaps no per SBA rules.

# PPP2 – Who Qualifies, Continued

- Documentation needed to qualify:
  - Loans less than \$150,000 – no documentation but must certify.
  - Loans greater than \$150,000 – quarterly financial statements, quarterly bank statements OR annual IRS income tax filings (if using annual reference period).
  - Key is to be consistent in 2020 quarter over 2019 quarter comparison.



## PPP2 – Who Qualifies, Continued

- Borrowers must certify that current economic uncertainty makes the loan necessary to support ongoing operations.
- Forward looking at the time of application vs backward looking at the time of forgiveness.
- Greater uncertainty now than last April? We think so.

## PPP2 – How Much?

- Payroll cost (defined the same as PPP1) is based on either 2019 costs or twelve trailing months before application date.
- Based on 2 ½ months payroll cost or 3 ½ months if in hospitality line of business.
- Loan terms are 1% interest with 5-year maturity.
- \$2,000,000 max; \$4,000,000 controlled group.

## PPP2 – Applying

- When can I apply? NOW.
- Do I have to use the same lender as I did with PPP1? NO.
- Do I need to apply for forgiveness on PPP1 before applying for PPP2? NO.
- You must certify that you have already expended all your PPP1 funds on eligible expenditures (payroll, rent, etc.).

# New PPP1 Loans

- If a business didn't apply before, it can now.
- Generally the rules are the same as last spring.
- For most businesses, the employee limit is still 500.
- Unlike last spring, section 501(c)(6) organizations with 300 or less employees now qualify.
- Increased draw possibility for certain partnerships.

# The Employee Retention Credit (“ERC”)

- **Q:** So, why are we talking about this? I thought you said we could ignore it.
- **A:** Prior to December, you couldn’t take the ERC if you had a PPP loan.
- This is a big deal. Dave calls it the “sleeper.” It could be worth up to \$19,000 per employee.

# ERC – The Basics for 2020

- Which employers? 50% reduction in year over year gross receipts (tested by calendar quarter) **OR** a full or partial shutdown of operations. Does an occupancy restriction qualify?
- How much credit in 2020? up to \$5,000 per employee (50% of wages).
- All size employers qualify. If under 100 employees, they need not be idle.
- Aggregation rules are different and more stringent than PPP.
- Gross receipts are based on your tax return.



# ERC – Expansion to 2021

- A 20% reduction, not 50%, is required in gross receipts (tested by calendar quarter, compared to 2019) **OR** a full or partial shutdown of operations.
- Credit is increased to \$7,000 (70% of up to \$10,000 in wages/employee) for each of the first two quarters of 2021.
- Possible advance credits. May qualify based on prior quarter.
- 100 employee limit increased to 500.
- For both 2020 and 2021, raises and other special pay are now eligible for the credit.

# ERC – How to Claim the Credit

- Gross receipts vs partial shutdown. Which wages count?
- Coordination with the PPP. Wages can only be used once: sick leave credit, ERC, or PPP. Which comes first? Is a loan forgiveness application an election not to claim the credit?
- Any eligible wages in 2020 may be treated as paid in the fourth quarter.
- The credit may be claimed on an amended payroll tax return.

# Summary of Major Tax Provisions of the Stimulus Bill

- Tax Extenders
  - Made Permanent
    - Medical expense deduction floor of 7.5%
    - Section 179D deduction for energy-efficient buildings
  - 5 -year extension through 2025
    - Work Opportunity Credit.
    - Gross income exclusion for COD on a principal residence (\$750K)
    - Exclusion for certain employer payments of student loans

# Summary of Major Tax Provisions of the Stimulus Bill

- Tax Extenders, continued
  - 2-year extensions
    - Section 25D residential energy-efficient property credit (26%)
    - Section 48 energy investment tax credit for solar and residential energy-efficient property
  - 1-year extension
    - Section 25C credit for qualified nonbusiness energy property
    - Qualified mortgage interest premiums as qualified residence interest
    - Sections 30, 35, 40, 45 credits

# Summary of Major Tax Provisions of the Stimulus Bill

- Tax Extenders, continued
  - CARES Act extensions
    - Educator expenses include PPE.
    - Payroll tax credits for paid sick and family leave through March 2021.
    - Deferral of employees' portion of payroll tax. Employers' portion not extended.

# Summary of Major Tax Provisions of the Stimulus Bill

- Other Tax Provisions
  - Temporary allowance of full deduction for business meals
    - If provided by a restaurant.
    - Effective expenses incurred 1/1/2021 through 12/31/2022.
  - Certain charitable contributions for nonitemizers
    - Extended through 2021.
    - \$300 per person/\$600 for joint return.
    - Understatement penalty of 30% on these contributions.



# Summary of Major Tax Provisions of the Stimulus Bill

- Other Tax Provisions, continued
  - Education expenses
    - Repeals qualified tuition deduction.
    - Increases phaseout limits on the lifetime learning credit.
    - Effective for tax years after 12/31/20.
  - Modification of limitations on charitable contributions
    - Extends for one year (through 2021) the increased limit of 100% of AGI.
    - Extends for one year (through 2021) the corporate limit of 25% of income.
    - Corporate limit of 100% for qualified disaster relief contributions.

# Summary of Major Tax Provisions of the Stimulus Bill

- Non-Covid-19 Disaster Tax Relief
  - Use of retirement funds for disaster mitigation.
    - Up to \$100,000 of qualified distributions penalty free.
    - Income over 3 years or may be recontributed to plan.
    - For both qualified plans and IRAs.
  - Qualified disaster-related personal casualty losses.
    - Can increase standard deduction amount by the amount of loss.
    - Eliminates the \$100 and 10% of AGI limitation (replaced with \$500 floor).
    - COVID-19 is explicitly excluded from the definition of qualified disaster.

# Q & A

**Thank you from**



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