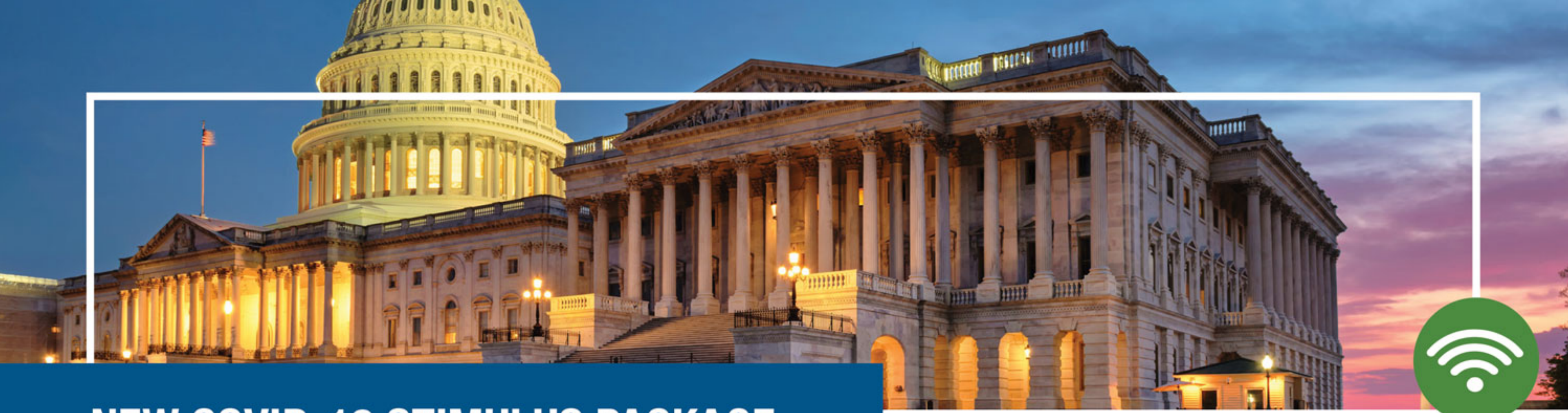

NEW COVID-19 STIMULUS PACKAGE

Key Areas Businesses Should Be Aware Of

February 10, 2021 | Presented By

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Updated Feb 8, 2021

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Learning Objectives

- Identify and understand the latest developments and major tax law provisions impacting businesses: **Consolidated Appropriations Act**
- Become familiar with new legislation impacting the Paycheck Protection Program (PPP2)
- Do so in a practical, not technical way

Agenda

- Second-Draw PPP
- Accounting for PPP
- PPP Tax Deductibility
- Payroll Taxes
- Employee Retention Credit
- Meal Deductions
- Stimulus Benefits
- Charitable Contributions
- Key Tax Extenders + Unemployment Benefits

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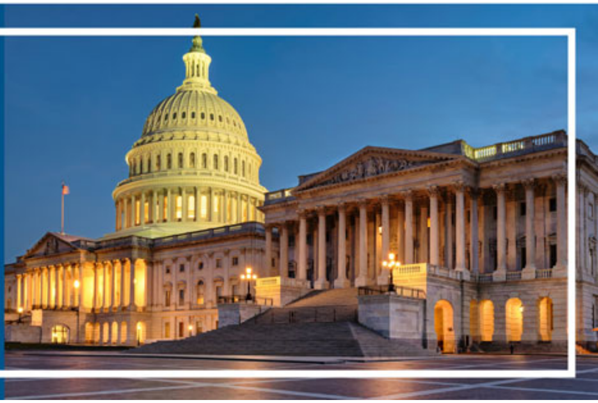
Second-Draw PPP



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Where We've Been

- **STIMULUS 1.0 – Mad scramble to apply**
  - How much can we get? Who can get if for us?
  - Oops, we ran out of money ($350B in 13 days)

- **STIMULUS 2.0 – Second wave of funding ($310B)**
  - Application deadline was June 30, 2020
  - Approximately $138B was left unclaimed

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New Legislation

- **STIMULUS 3.0 –** On again, off again, but finally enacted by the Consolidated Appropriations Act signed by President Trump on December 27, 2020
- $900B Stimulus package overall that includes additional $284B in funding for PPP
- Allows up to $2 million for borrowers that have used up original PPP funding or did not apply during the first round
- Through January 31st, 891,000 borrowers received a total of $72.7B from lenders = Approximately 26% of PPP2 funding.

Loan Terms

- 2.5 times average monthly payroll costs or $2 million, whichever is less
  - Businesses in the hospitality sector, such as hotels, restaurant and other food service businesses can borrow up to 3.5 times
  - Can use the average of calendar year 2019, 2020 or the 12 months prior to application
- Five-year note on unforgiven portion
  - **1% interest with no collateral or personal recourse**
- Loan proceeds must be spent on payroll costs and other eligible expenses (to be eligible for forgiveness)
  - 60% of loan must be spent on payroll costs
  - Eligible expenses are expanded

Eligibility

- Meet the definition outlined as an eligible person or entity
- **Employ not more than 300 employees**
- Have used or will use the full amount of your original PPP, if applicable
- Demonstrate at least a **25% reduction in gross receipts** calculated based upon the first, second, third or fourth quarters of 2020 compared to 2019
    - Note, forgiven first-draw PPP loans should not be included in the 2020 gross receipts

Gross Receipts

- In general, gross receipts include all revenue in whatever form received or accrued (in accordance with the entity's accounting method) reduced by returns and allowances. Revenue sources include:
  - Sales of products or services
  - Interest
  - Dividends
  - Rents
  - Royalties
  - Fees or commissions

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Application Process

- Borrowers can apply for a second-draw PPP loan until Mar. 31, 2021
- Lenders' processes and timeline may vary for accepting applications
- Complete Second Draw Borrower Application with corresponding documentation
- Keep in mind that applying for a PPP2 loan is SEPARATE from applying for forgiveness

Forgiveness

- Employee and compensation levels need to maintained in the same manner as required for the first PPP draw for full forgiveness
- Loans less than $150K eligible for streamlined forgiveness
- Practical considerations: **"Current economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant"**
- **Don't forget about the dreaded F.A.Q. #31**

Forgiveness

- **F.A.Q. #31 :**
  - Question: Do businesses owned by large companies with adequate sources of liquidity to support the business's ongoing operations qualify for a PPP loan?

  - Answer: (abbreviated) "All borrowers must assess their economic need" *and* "…review carefully the required certification that current economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant."

Key Considerations

- Things to consider as you assess:
  - Getting a full-dollar PPP forgiven vs. a partial-dollar credit
  - Consider time periods
    - Which quarters might you have qualified for the payroll credit first – either from a shutdown or gross receipts decline – and use those periods for the ERC
  - You might have more than enough wages for PPP forgiveness even when using the same periods so modify forgiveness application accordingly

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Other Loan Opportunities

- Opportunities Beyond PPP:
  - **SBA is currently accepting new Economic Injury Disaster Loan (EIDL) applications from all qualified small businesses, including agricultural businesses, and private nonprofit organizations.**
  - EIDL $10,000 grant no longer subtracted from PPP forgiveness

Other Loan Opportunities

- Opportunities Beyond PPP:
  - EIDL Loan Terms:
    - Fixed rate of 3.75%
    - 30 year amortization
    - Payments deferred 1st year, interest still accrues
    - Collateral required for loans > $25K

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Other Loan Opportunities

- Opportunities Beyond PPP:
  - Payment relief for eligible SBA loans will be extended:
    - SBA will cover the payment on eligible SBA loans, including interest, for up to a total of $9,000 per payment for an additional 3 months

Key Considerations

- **MAKING INTERPRETATIONS - RESOURCES:**

- **Visit the U.S. Treasury's Website**
  https://home.treasury.gov/policy -issues/cares/assistance-for-small-businesses
  This is where you will find the "Frequently Asked Questions", Application Forms & Instructions

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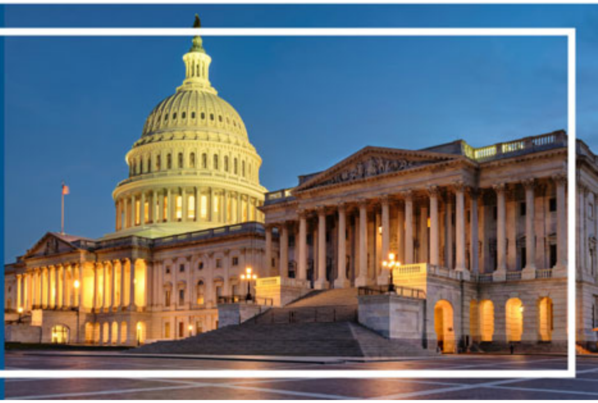
Accounting for PPP Loans & Forgiveness



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Accounting for PPP

- **Accounting for PPP has two dimensions that must be addressed:**

1. **GAAP Side** - How do I present PPP loan in my financial statements at year end?
2. **Tax Side** - How do I treat PPP funds for income tax purposes? (Tax Side)

Accounting for PPP

For either the GAAP or Tax Side:

Depends on whether you are applying for forgiveness or not!

- First and foremost, these funds are loan proceeds. Most companies' initial accounting entry was to record a loan payable on their balance sheet.
- Why? Because isn't a "loan a loan" until it is either paid off or forgiven? (*More on this concept later*)

Accounting for PPP

GAAP Side: For-Profit Entity

In June of 2020, the American Institute of Certified Public Accountants published an update to their Q & A document consistent with SEC guidance which allows for-profit businesses to account for the PPP loan in one of two ways:

- **As Debt, or**
- **As a Grant**

Accounting for PPP

GAAP Side: Debt Approach

When accounting for a PPP loan as debt, one should accrue interest (at 1%) and the loan should remain on the balance sheet until the loan is forgiven. **At the point the debt is forgiven** (possibly next year) a gain is recorded on extinguishment of debt.

- **For most companies, this would have the impact of more debt on the books at 12/31/20 and deferring gain until next year.**

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Accounting for PPP

GAAP Side: Grant Approach (Theoretical)

If company thinks it is probable that PPP loan will be forgiven, it can be accounted for as a grant. (*Apparently, a loan is not always a loan until it is forgiven!*)

- **Grants are recorded first on the balance sheet as deferred income and later ratably moved to the income statement as eligible expenses are incurred.**
- **Conclusion: Forgiveness is not the "trigger"**

Accounting for PPP

GAAP Side: Grant Approach (Practical)

Note: Most companies did not have this guidance in mind and did NOT ratably recognize income during 2020.

- **Guidance provides the two choices in recognizing the credit to the income statement:**

  1. **Report as Other Income**
  2. **Report as a credit to expenses that were eligible for forgiveness (i.e., Expense recovered)**

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Accounting for PPP

GAAP Side: Grant Approach (Practical)

I am recommending the "grant approach" and reporting as "Other Income" for the following reasons:

1. **All eligible expense likely incurred before 12/31/20.**
2. **Income is recognized in same period as eligible expenses – so no mismatch**
3. **Deferral of gain results in no tax benefit**
4. **No impact on ratios such as GP, Debt:Equity**
5. **Keeps PPP a 2020 issue only**

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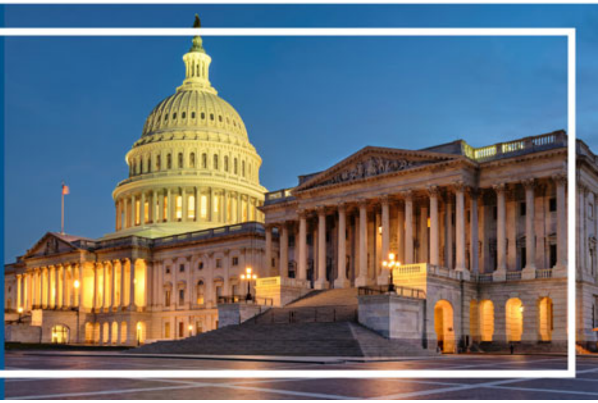
Tax Deductibility



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PPP Tax Deductions

- The CARES Act created the PPP, but did not address deductibility of expenses paid with loans
- The CARES Act specifically said forgiven PPP debt is not taxable
- IRS Notice 2020-32 and 2020-07 stated deductions would not be allowed for expenses paid with forgiven PPP proceeds because the proceeds are tax exempt
    - Per IRC Section 265, expenses paid with tax-exempt income are not deductible

PPP Tax Deductions (Old Slide) Appreciate what you escaped !

Tax Side: For-Profit Entity - Conclusions

- Forgiveness itself is not taxable – Banks will NOT be sending 1099s to those granted forgiveness
- There is NO tax benefit to delaying your application for forgiveness since it is your EXPENSES that are non-deductible…and those were paid in 2020
- Assuming 100% forgiveness, your tax planning for 2020 should include the amount you received for PPP as part of taxable income
- Dig deep – the tax dollars will have to come from other resources since all of your PPP funds are spent

- Thankfully, red language above no longer applies

PPP Tax Deductions

- Congress original intent: "tax nothing" and drafted CARES Act with assumption deduction would be allowed
- The COVID-Related Tax Relief Act Section 276 clarifies taxpayers whose PPP loans are forgiven are allowed to take deductions for otherwise deductible expenses paid with the proceeds of a PPP loan and retroactively allows businesses to take tax deductions for expenses paid with forgiven PPP proceeds to tax years ending after Mar. 27, 2020
- IRS Notice 2021-02 obsoletes Notices 2020-32 and 2020-07

PPP Tax Deductions

- New Statutory Language

1) No amount shall be included in the gross income of the eligible recipient by reason of forgiveness of indebtedness described in subsection (b)
2) No deduction shall be denied, no tax attribute shall be reduced, **and no basis increase shall be denied**, by reason of the exclusion from gross income provided by paragraph (1)
3) In the case of an eligible recipient that is a partnership or S corporation
   - A) Any amount excluded from income by reason of paragraph (1) shall be treated as tax exempt income for purposes of sections 705 and 1366 of the Internal Revenue Code of 1986
   - B) Except as provided by the Secretary of the Treasury (or the Secretary's delegate), any increase in the adjusted basis of a partner's interest in a partnership under section 705 of the Internal Revenue Code of 1986 with respect to any amount described in subparagraph (A) shall equal the partner's distributive share of deductions resulting from costs giving rise to forgiveness described in subsection (b)

PPP Loan Forgiveness & S-Corp Basis

- CARES Act - PPP loans specifically excluded from federal income tax
- CAA, 2021 - deductions are allowed for expenses paid with PPP loan and forgiveness will not reduce tax basis
- Gitlitz V. Commissioner, 531 U.S. 206 (2001)
  - Shareholders increased stock basis with discharged debt
  - IRS challenged
  - Supreme Court agreed with shareholders
  - Amendment of Code Sec. 108 - special rules for S-corp to close loophole
  - PPP loans forgiven under CARES Act, not Sec. 108
- Loan forgiveness will increase the other adjustment and accumulated adjustment account
  - May limit distributions restricted by the accumulated adjustment account
- **Important: Watch out for timing issues related to date of forgiveness**
- AICPA is analyzing legislation and has not confirmed a position.

S-Corp Basis Example

CARES Facts:

- Tom maintains a low basis in his S-corporation, ABC Roofing, by withdrawing income as distributions at year-end. Basis at beginning of 2020 is $0.
- ABC Roofing received a PPP loan of $400,000, used the entire amount, and Tom expects the loan to be fully forgiven.
- Finished 2020 with a loss of $100,000 (exclusive of $400,000 PPP loan forgiveness).
- In a perfect world, Tom would increase basis by tax-exempt income of $400,000 and be able to take the $100,000 loss on his 2020 tax return. BUT…

S-Corp Basis Timing Issue

CARES Facts:

- When will the loan be forgiven? Most likely, majority of PPP loans will be forgiven in 2021.
- Result: Tom's $100,000 loss from ABC Roofing may be suspended until forgiveness triggers increase in basis in 2021 (or will it be 2020?).
- Can argument be made that PPP funds, if sure of forgiveness, are not a loan but instead, tax-exempt income? Will need more guidance.

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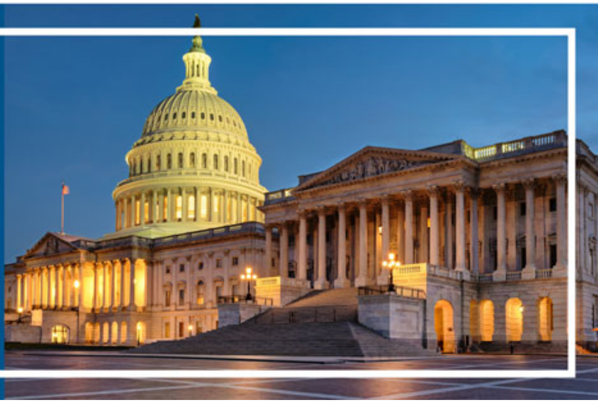
Payroll Taxes



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Extension of Paid Leave Tax Credits

- Under FFCRA, employers with 500 or fewer FTEs were required to provide paid leave to certain individuals impacted by COVID-19 and were eligible for a 100% payroll tax credit
- The CCA expands this program through Mar. 31, 2021
  - 100% credit remains in effect
  - Per-employee daily and maximum amounts of required leave remain the same

Deferral of Payroll Taxes

- CAA provides for an extended repayment period for any deferred payroll taxes under Notice 2020-65
  - **Employees** who deferred 6.2% SS tax on wages paid between Sept. 1, 2020 and Dec. 31, 2020 now have the full calendar year to repay the deferred amounts
  - Almost no one took advantage of this. Why? Because if employee left the business for any reason, EMPLOYER would be liable for tax.

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Deferral of Payroll Taxes

- The original CARES Act provided employers could defer depositing employer's portion of SS tax on wages paid from March 27, 2020 to December 31, 2020.
  - 50% of the amount deferred is payable 12/31/2021
  - Remaining 50% of amount deferred is payable 12/31/2022
  - **Here's the kicker:** Although this tax is included in expenses for 2020…the expense WILL NOT be tax deductible until tax year paid if above due dates are followed

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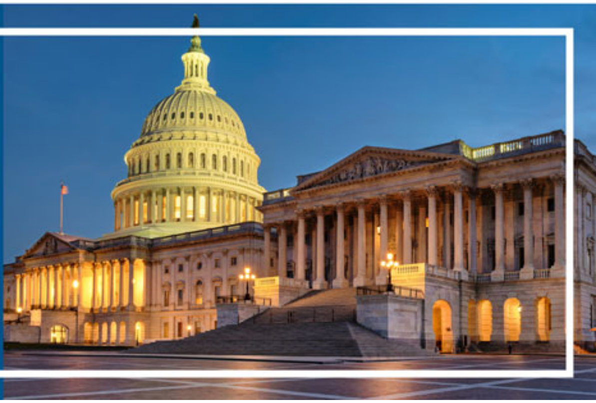
Deferral of Payroll Taxes

- Do I have to postpone the tax deduction?
  - No. If employer pays the first 50% by extended due date of corporate tax return (9/15/21), then employer can deduct 50% in 2020.
  - Under the same rule, if employer pays the second 50% by extended due date of corporate tax return (9/15/22), then employer can deduct second 50% in 2021 tax year

Employee Retention Credit



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About the Credit & Recent Changes

- Employee retention credit (ERC) was originally created by CARES Act to encourage businesses to keep employees on payroll
- The CCA now allows companies that received PPP loans to also benefit from the ERC
  - CARES Act did not allow both benefits

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Changes to the Rules

- Changes to the rules
  - Extends the credit to cover qualified wages paid through June 30, 2021 (instead of Dec. 31, 2020)
    - With this extension, employers can apply for advance payments of their expected future credits
  - The credit is increased to 70% of qualified wages per employee, up to $10,000 per quarter (previously 50% per employee for all of 2020)
    - Meaning first two quarters of 2021 allows for a maximum credit of $7,000 per employee per calendar quarter (potential credit of $14,000)

Changes to the Rules

- Changes to the rules (continued)
  - Reduction in gross receipts for employers who experienced a significant decline due to the government shutdown order is reduced to 20% (previously 50%)
  - Qualified wages taken into account in calculating the 2021 credits are no longer limited to what employer paid to employees in any specific period

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Changes to the Rules

- Changes to the rules (continued)
  - Employers averaging 500 or fewer full-time equivalents (FTEs) now eligible for the full credit (was previously at 100 or fewer)
  - Qualified wages applicable to the tax credit may not also be counted as forgivable payroll costs under the PPP (although employer has the option to do either)
    - New rules are retroactive to the passing of the CARES Act
    - An analysis can reveal PPP borrowers can still claim 2020 credits by amending payroll tax filings

Meals Deductibility

- Temporary provision allows 100% deduction for business meals incurred after Dec. 31, 2020 through Dec. 31, 2022
  - Previously, was set at 50% under the Tax Cuts and Jobs Act
  - Note, not for 2020 tax year
- Meant to spur business for the restaurant industry hit hard by pandemic
- Entertainment expenses remain non-deductible
  - Separate charts of accounts for meals versus entertainment is best for tracking purposes

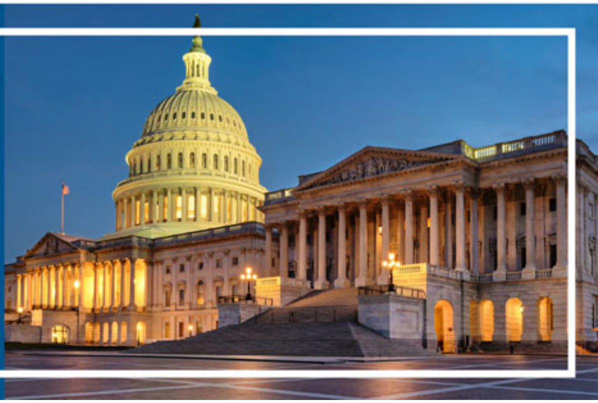
Stimulus Payments

- A second round of stimulus payments has been issued:
  - $600 per individual (prior stimulus payment was $1,200)
  - Dependents also get $600
  - 17 years old age restriction continues to apply
  - Phaseouts are the same
  - $75,000 for single or married filing separate
  - $112,500 for head of household
  - $150,000 for married filing jointly
  - Phaseout is $5 for every $100 above the phaseout threshold
- Considered an advance on a 2020 tax credit
- Payment amount is based on 2019 income
- All stimulus payments will be reconciled on the 2020 return

Charitable Contributions

- Above-the-line charitable contribution deduction allowed for non-itemizers in 2021:
  - $600 for married filing jointly
  - $300 for all other filing statuses
- NOTE: Above-the-line charitable contribution deduction for 2020 is $300, regardless of filing status
- Also allows a charitable deduction of 100% of adjusted gross income for both 2020 and 2021, if itemizing

Key Tax Extenders



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Key Tax Extenders

- Bill included over $100 million in extensions and enhancements of expiring tax extenders
- Extensions were made in one-year and five-year increments, as well as permanent

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Key Tax Extenders

- Provisions made permanent include:
  - 7.5% adjusted gross income limitation for medical expenses
  - Deduction for energy efficient commercial buildings under Section 179D
  - Exclusion from gross income under Section 139B(d) for certain benefits provided to volunteer and emergency responders, as included in the SECURE Act of 2019
  - Craft beverage lower excise tax rates on small brewers, vintners and distillers under Sections 5001, 5041 and 5051
  - Lifetime learning credit under Section 25A(d)(2)
  - Railroad track maintenance credit; however, the credit rate is reduced from 50% to 40%

Key Tax Extenders

- Provisions extended to Dec. 31, 2025 include:
  - Employer credit for paid family and medical leave
  - Exclusion from taxation of mortgage forgiveness on a principal residence
  - Work Opportunity Tax Credit
  - Expanded exclusion for employer-provided educational assistance, including student loan repayment benefits as enacted as part of the CARES Act
  - Seven-year recovery period for motorsports entertainment complexes
  - Special expensing rules for certain film, television and live theatrical productions
  - Empowerment zone designation (empowerment zone tax-exempt bonds and employment credit were NOT extended)
  - Look-through rule for related controlled foreign corporations

Key Tax Extenders

- Provisions extended to Dec. 31, 2021 include:
  - Credit for qualified nonbusiness energy property
  - Health coverage tax credit
  - Energy-efficient homes credit
  - Treatment of qualified mortgage insurance premiums as qualified residence interest

Unemployment Benefits

- Additional unemployment benefits have been reinstated:
  - $300 per week through Mar. 14, 2021
  - $100 per week for workers who have both wage and self-employment income, but whose usual unemployment calculation doesn't consider the self-employment income

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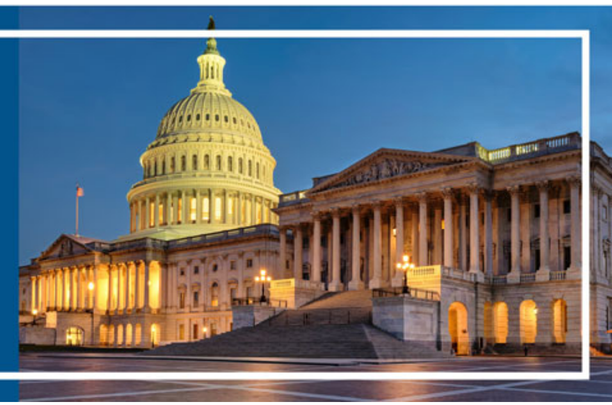
Thank You!



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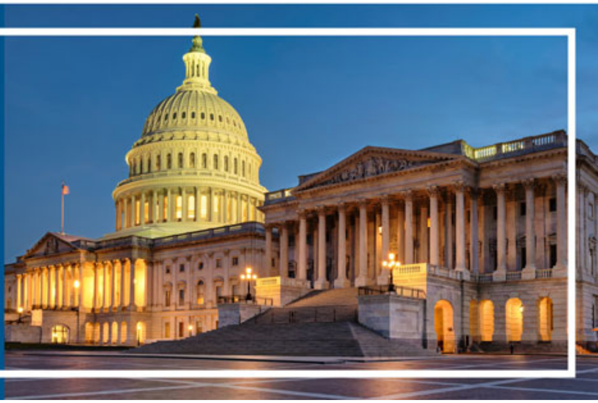
Questions?



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