Cash Flow, PPP Loans, and More: What Business Owners Need to Know Amid Covid-19

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Agenda

- Paycheck Protection Program forgiveness
- How do you request loan forgiveness?
- Recent tax law changes that impact business owners
- Income tax changes
- How to manage cash flow in the current environment

Paycheck Protection Program Forgiveness

Recent Legislation

- Part of the CARES Act, The Paycheck Protection Program ("PPP") authorized up to $349 billion in forgivable loans to small businesses to pay their employees during the COVID-19 crisis
- These funds ran out in just 13 days
- Round two, signed into law Friday, April 24th, gave an additional $310 billion to the PPP program

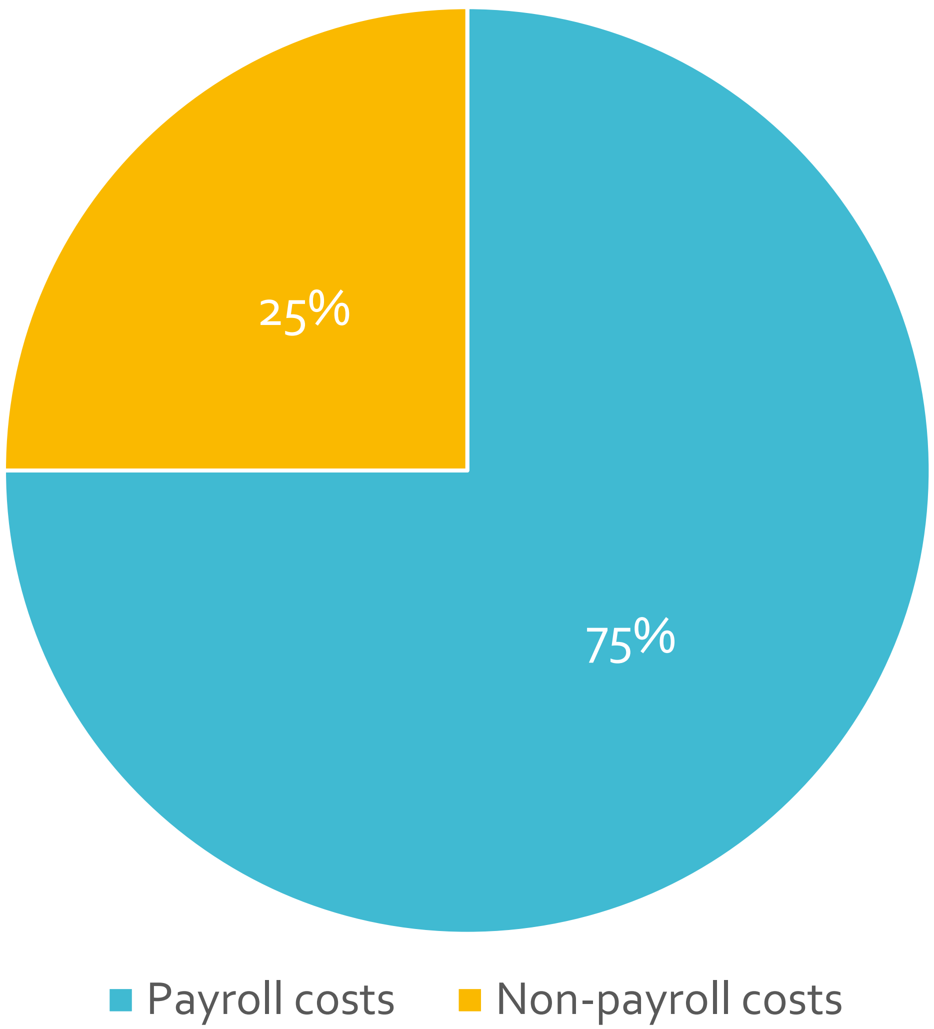
Paycheck Protection Program

- Small businesses that have been impacted by COVID-19 are eligible for the Paycheck Protection Program, which offers 100% forgivable loans if the funds are spent on qualifying costs
- The maximum amount of money a business can borrow is equal to 2.5 times their monthly payroll costs or $10 million, whichever is lower
- The borrower has an 8-week period to spend the loan funds on qualifying expenses beginning the day the borrower receives the funds

What If You're Self-Employed?

- **Schedule C filers are eligible for PPP loans if they:**
  - Were in operation on February 15, 2020
  - Were an individual with self-employment income, such as an independent contractor or sole proprietor
  - Have a principal place of residence in the United States; and filed or will file an IRS Form 1040 Schedule C for 2019
- **Partners with self-employment income from partnerships are not eligible for PPP loans as self-employed individuals.** The self-employment income of a general active partner is reported as a payroll cost of the partnership. Partnerships are eligible for PPP loans, and the SBA has determined that limiting a partnership and its partners to one PPP loan is necessary to ensure that PPP loan proceeds reach as many eligible borrowers as possible and to avoid confusion.

Your Loan Will Be Forgivable If You Use at Least 75% on Payroll Costs



75% - Payroll Expenses

- Salary, wages, commissions or tips up to $100,000 gross pay per employee on an annualized basis
- Employee benefits such as:
  - Vacation, parental, family, medical, or sick leave
  - Costs for group health care benefits like insurance premiums
  - Payment of any retirement benefits
  - Allowance for separation or dismissal
- State and local taxes assessed on employee compensation
- For a sole proprietor or independent contractor: wages, commissions, income, or net earnings from self-employment, capped at $100,000 on an annualized basis for each worker

25% Non-Payroll Expenses

- Mortgage interest payments (but not mortgage prepayments or principal payments)
- Rent payments
- Utility payments
- Interest payments on any other debt obligations that were incurred before February 15, 2020
- Refinancing a SBA EIDL loan made between January 31, 2020 and April 3, 2020

Keep Your PPP Funds Separate

- Put your PPP funds in a separate account to make them easier to track
- Transfer from one account to another to cover PPP approved expenses such as payroll costs
- Document your transactions
- This is not a requirement, but will make it easier to prove how you used the funds

Increase Your Chances of Forgiveness

You will owe money if you do not maintain your staff and payroll

- **Number of Staff:** Your loan forgiveness will be reduced if you decrease your full-time employee headcount
- **Level of Payroll:** Your loan forgiveness will also be reduced if you decrease salaries and wages by more than 25% for any employee that made less than $100,000 annualized in 2019
- **Re-Hiring:** You have until June 30, 2020 to restore your full-time employment and salary levels for any changes made between February 15, 2020 and April 26, 2020

Client Questions

1. Do employers need to maintain the same head count as well as total payroll amount?

2. If someone was let go due to reasons NOT related to COVID-19, does their position need to be filled (& at the same salary?) or does just adding another employee satisfy the headcount requirement? Do we have to replace them at all?

3. How long does this headcount need to be maintained in order to satisfy loan forgiveness requirements?

Client Questions

- For employees earning greater than $100K/yr, is it possible to pay their salary up to the prorated $100K amount from the PPP loan, and the rest from your regular operating bank account?
- Can you give retention bonuses? Hazard pay?
- Are discretionary profit sharing or 401(k) contributions mid-year allowed & do they count?

Client Questions

In our office, we keep thinking of the fairness of an employee getting paid when he doesn't have PTO and another employee getting paid using PTO. Then the what-ifs come into play…what if employees take advantage of the paid without leave scenario.

PPP FAQ

Is the forgiven amount considered taxable income? No.

What if I do not spend 100% of the loan proceeds on covered costs? Repay the excess immediately and reduce the loan amount or keep the excess and repay it within the two-year loan period.

How does the remaining loan get repaid? No payments are due for six months; however, interest accrues during this deferral period.

What are the terms of the loan (the portion that is not forgiven)? 1% and the term is two years. No collateral, no personal guarantee required, and no prepayment penalties.

Issues That Need Further Clarification

- If a business spends less than 75% on payroll costs, does the entire loan become unforgivable, or does the forgivable amount become reduced? If so, how does that calculation work?
- For payroll and other qualifying expenses during the 8-week period, does this refer to "paid" or "incurred?"
- What happens if an employer's head count is not restored by June 30th? Will they receive no forgiveness or partial forgiveness?
- How will the SBA determine who was economically impacted by COVID-19 and thus eligible to receive the loans? Will there be a test?
- How does the SBA calculate and define the term "annualized"?

Loan Forgiveness Example

Loan amount	$250,000.00
Payroll costs for the covered period	$180,000.00
Mortgage interest, rent & utilities	$70,000.00 Up to 25% of forgiveness $60,000.00
Estimated amount for forgiveness prior to full-time equivalent (FTE) and/or wage/salary calculation	$240,000.00
Average FTEs per month during the covered period	5
Average FTEs per month for comparison	5
Percent of loan principal that must be paid back due to FTE reduction	0%
Decrease in wages greater than 25%	$0.00
Amount of loan principal that may be forgiven	$240,000.00
Amount of loan principal that may be paid back	$10,000.00

How Do You Request Loan Forgiveness?

How Do You Request Loan Forgiveness?

SUBMIT A REQUEST TO YOUR LENDER

SUBMIT DOCUMENTS TO VERIFY YOU QUALIFY FOR FORGIVENESS

LENDER WILL DECIDE IN 60 DAYS

Salaries and Wages

Documentation needed:

- Copies of payroll processing reports, tax or other reports during the 8-week period
- Related payments like vacation, sick and other paid time off for employees during the 8-week period

Healthcare Benefits

Documentation needed:

- Documents reflecting the health insurance premiums paid by the company under a group healthcare plan, including owners of the company during the 8-week period
- Copies of the monthly invoices should be acceptable

Retirement Plan Funding

Retirement plan contributions made during the 8-week qualified period are eligible PPP expenses, including employer contributions funded to Defined Benefit Plans, Defined Contribution Plans and SEP IRAs.

Documentation needed:

- Documentation of retirement plan funding by the employer during the 8-week period following the origination of the loan
- Copies of statements, funding schedules and remittances from the retirement plan administrator

Rent Expenses

Documentation needed:

- Signed lease agreement
- Proof of rental payments (checks, bank statements, ACHs, or wires) along with the invoice if applicable

Mortgage and Other Loan Interest

Interest on mortgage obligations and loans secured by any business personal property are qualified expenses if these loans were incurred before February 15, 2020.

Documentation needed:

- Copies of all statements of interest paid on loans and mortgages, such as a bank statement showing principal and interest or a loan invoice, along with payment

Utilities

The SBA defines qualified utilities as phone, gas, internet, electricity, water. Service contract agreements must predate February 15, 2020.

Documentation needed:

- Copies of proof of payment (cancelled checks, bank statements, ACHs or wires)
- Other evidence of utilities paid

Check in With Your Lender Regularly

- Your lender will be able to provide additional guidance on documentation required
- Information is changing frequently; check the SBA's website for updates

Recent Tax Law Changes That Impact Business Owners

Employee Retention Tax Credit Eligibility

- In order to qualify to receive this credit you must carry on a trade or business in 2020 and:
  - Had your operations fully or partially suspended during a 2020 calendar quarter as a result of an order from an appropriate governmental authority that limits commerce, travel or group meetings due to COVID-19; or
  - Experienced a greater than 50% decline in gross receipts for a 2020 calendar quarter compared to the corresponding 2019 calendar quarter
- Self-employed individuals, government employers, or any small business that receives a Paycheck Protection Program (PPP) are <u>not</u> eligible for this credit
- The Employee Retention Credit applies to full-time workers only

Employee Retention Tax Credit

- The credit amount equals 50% of eligible employee wages paid by an eligible employer for all eligible calendar quarters beginning March 13 and ending December 31, 2020
- It's subject to an overall quarterly wage cap of $10,000 per eligible employee (employers can receive up to $5,000 credit per employee per quarter)
- The credit is applied to your portion of the employee's Social Security taxes and is fully refundable
- You can claim your credit immediately by reducing payroll taxes sent to the IRS
- If your credits exceed payroll taxes, you can request a direct refund from the IRS

Employee Retention Tax Credit Cont.

Wages considered “eligible”:

- Credit is available to cover eligible wages paid between March 13, 2020, and December 31, 2020
- 100 or fewer full-time employees in 2019 - all employee wages are eligible
- Over 100 full-time employees in 2019 - only wages of employees who are furloughed or given reduced hours due to the employer’s closure or reduced gross receipts are eligible for the credit
- Eligible wages are increased to include qualified health plan expenses allocable to those wages

Payroll Tax Deferral

- Only applicable to the employer portion of Social Security Wages (6.2% of wages) paid from Mar. 27 thru Dec. 31, 2020
- All businesses are eligible, regardless of whether they are impacted by COVID-19 or not

Payroll Tax Deferral Eligibility

- If your PPP loan is forgiven, you are not eligible, however you can defer payment if you have applied for or received a loan, as long as the loan has not been forgiven
- As an employer, you are liable for timely payment of employment taxes even if you designate an agent to deposit those taxes for you
- You must deposit 50% of deferred taxes by Dec. 31, 2021, and the remainder by Dec. 31, 2022, or face significant failure-to-deposit penalties

Employee Retention Tax Credit Vs. Payroll Tax Deferral

Terms	Employee Retention Credit	Payroll Tax Deferral
Program description	Refundable payroll tax credit	Deferral of employer share of 6.2% social security tax or half of self-employment tax
Maximum available	50% of up to $10k in wages (including health care costs) per employee, paid 3/12/20-12/31/20	Applies to tax on wages paid 3/27/20-12/31/20
Staff size limitations	-More than 100: only wages of furloughed or reduced-hours employees eligible -100 or fewer: no furlough or reduced-hours limitations	N/A
Taxes affected	Employer portion of qualified SS taxes	Employer portion of SS taxes
Taxes due	None + potential refund	50% 12/31/21; 50% 12/31/22
Exclusivity	Ineligible if receiving PPP loan	-No longer eligible for deferral of new amounts as of date PPP loan is forgiven -Apply Employee Retention Credit first
Impact on Families First Coronavirus Response Act	No credit for FFCRA credits	None
Other terms	Penalty relief for related payroll tax deposits and advanced payment procedure available	N/A

Income Tax Changes

Carrybacks Allowed for Certain NOLs

- NOLs that arise in tax years beginning in 2018 through 2020 can be carried back for five years.
- For example, a taxpayer could carry back an NOL arising in 2020 to 2015 and recover federal income tax paid for that year. That could be very beneficial, because the federal income tax rates for both individuals and corporations were higher before the TCJA rate cuts took effect in 2018.
- When advantageous, taxpayers can elect to waive the carryback privilege for an NOL and, instead, carry the NOL *forward* to future tax years.

Excess Business Loss Disallowance Rule for Noncorporate Taxpayers Is Postponed

- TCJA disallowed current deductions for "excess business losses" incurred by individuals and other noncorporate taxpayers in tax years beginning in 2018 through 2025.
- An excess business loss is one that exceeds $250,000 ($500,000 for a married joint-filing couple). These limits are adjusted annually for inflation.
- The CARES Act temporarily removes the excess business loss disallowance rule for losses arising in tax years beginning in 2018 through 2020.
- The excess business loss disallowance rule will come back into play for losses that arise in tax years beginning in 2021 through 2025. Any disallowed excess business loss for one of those years will be carried forward to the following year and can be deducted under the rules for NOL carryovers.

How to Manage Cash Flow in the Current Environment

Extend Your Lines of Credit

- Actively engage with your financing partners to make sure your lines of credit remain available and explore additional options for financing in case you need it
- Do some scenario planning to determine how much cash you will need and for how long
- Identify critical short, intermediate and long-term cash needs and loan uses

Negotiate With Vendors and Suppliers

- Reach out to all vendors and suppliers to discuss the terms of your payments
- If you need to extend your payments, have a plan that will satisfy all parties

Speed up Customer Payments

- Offer a discount for early payment
- Check outstanding invoices and increase collections activity
- Consider accepting credit card payments if you don’t already

Reduce Variable Costs

- Place restrictions on discretionary spending such as entertainment and training
- Avoid layoffs by finding opportunities to reduce outside contract labor and redistribute the work to your W-2 employees
- If necessary, consider offering voluntary (or involuntary) leave without pay to conserve cash

Focus on Inventory Management

- Businesses will have to balance the demand for more cash flow and buffer inventory
- Sustainable savings with likely require fundamental improvements in:
  - Demand planning
  - End-to-end supply chain inventory visibility
  - Production planning and scheduling
  - Inventory and safety stock policies
  - Lead-time compression
  - SKU (stock keeping unit) rationalization
  - Network-wide available-to-promise

Audit Payables and Receivables Transactions

- Ensure you're collecting the right amount for the goods and services you sell and paying the right amount for the goods and services you procure

Check Your Business Interruption Insurance

- As it stands currently, there's much disagreement regarding whether business interruption insurance policies should cover loss of income triggered by the pandemic
- While courts and lawmakers are addressing these issues, companies that have a business interruption policy in place should consider taking the following steps:
  - Review your policy in detail
  - Determine the notification period
  - Build your case

Thank You!

We'd love your feedback

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