



CARES Act – Paycheck Protection Program (PPP) UPDATE

How to manage your PPP funds for maximum loan forgiveness

Based on the latest information available on 5/15/20 and subject to change. Additional information can be found on our Avitus Group COVID-19 Resources page at <https://avitusgroup.com/covid-19/>

You have received PPP loan funds, now what?

If your business has received approval for a loan from the Paycheck Protection Program (PPP), congratulations on obtaining aid to help get your business and your employees through the shutdown measures needed to stop the spread of COVID-19. However, you need to use the loan carefully. First, you want to maximize the feature that makes the PPP loan forgivable. Second, you want to use the loan properly so that you stay out of legal trouble for any potential abuse of the program.

- Best practice is to set up a separate bank account to deposit the PPP funds so they are not comingled with other accounts. This way you can track the use of the funds precisely, even if it means transferring them from one account to another, for example, to fund payroll. To be clear, this is not required, but you want to make sure spending is tracked with the same level of detail as if you were under the assumption the IRS was going to audit your accounting records.
- To the extent possible, use this separate bank account to pay qualified expenses (see below), and ONLY for qualified expenses.
- Be sure to track everything. Set up a file to track all transactions in detail. For example, copies of pay stubs, health insurance invoices, and entries in a check register for expenses related to payroll, commissions, healthcare benefit and premium payments, mortgage statements, rent and utility invoices, etc.
- If your accounting software system is capable, consider flagging these type of transactions with a class or coding of “PPP Loan”, or something similar. This will make it easier to provide supporting documentation when applying for loan forgiveness at the end of the 8 week period.

What expenses qualify for forgiveness?

Loan amounts spent on the below in the 8-week period after the loan was originated are eligible for forgiveness:

- Payroll costs (see further description below), including benefits (see Payroll exceptions below).
- Interest (but only interest) on existing mortgages or other debt obligations, incurred before February 15, 2020.
- Rent, under lease agreements in force before February 15, 2020.
- Utilities, for which service began before February 15, 2020.

Note: No more than 25% of the forgiven amount may be for non-payroll costs.

Payroll exceptions-

- Salaries in excess of \$100k/year (you can deduct up to \$8,333/month).
- Any compensation of an employee whose principal place of residence is outside of the United States.
- If you cut headcount the forgiveness will be reduced by the difference in average headcount. The comparison is with headcount between 2/15/19 and 6/30/19 OR 1/1/2020 and 2/29/2020 (at your choosing). Headcount is determined by calculating a full-time equivalent (“FTE”) number of employees, not raw



headcount. Using the most common definition, which commentators agree is the only one available now, the total number of hours worked in any payroll period, divided by 40, will result in a count of FTE for this purpose.

- If you cut salaries > 25%, based on the most recent full calendar quarter, the forgiveness will be reduced by the amount in excess of the 25%.
- Employer's share of federal unemployment taxes, FICA (Federal Insurance Contributions Act), and Railroad Retirement Act taxes.
- Exemption for Re-Hires/Salary Reductions:
 - o If you already laid off staff or reduced salaries below 25%, you have until June 30, 2020 to undo those to still get the forgiveness credit. However only those layoffs through April 26, 2020 qualify for the re-hire benefit. Based on current guidance a replacement for an employee who was laid off and does not want to return to work will count as a re-hire.

What is included in payroll costs?

- Salary, wages, commissions, or tips (capped at \$100,000 on an annualized basis for each employee). A partnership will also include any active partners' allocable share of net income that is subject to self-employment tax as part of the loan amount and forgiveness portion.
- Employee benefits including costs for vacation, parental, family, medical, or sick leave; allowance for separation or dismissal; payments required for the provisions of group health care benefits including insurance premiums; and payment of company portion of retirement benefit.
- State and local taxes assessed on 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 employee. Partner allocable share of net income, see above, is also capped at \$100,000.
- Are Social Security taxes included in "payroll costs"? No. Payroll costs are calculated on a gross basis, without subtracting the employee's federal taxes which are withheld by the employer. The employer's portion of federal payroll taxes (such as Social Security and Medicare) are also not included in "payroll costs," and similarly, PPP loan funds cannot be used to pay the employer's portion of federal payroll taxes. Employers are still required to submit the employer's portion of federal payroll taxes to the IRS.
- Does the PPP cover paid sick leave? Yes, the PPP covers payroll costs, which include employee benefits such as costs for parental, family, medical, or sick leave. However, it is worth noting that the CARES Act expressly excludes qualified sick and family leave wages for which a credit is allowed under sections 7001 and 7003 of the Families First Coronavirus Response Act (FFCRA) (Public Law 116-127). Learn more about the FFCRA's Paid Sick Leave Refundable Credit [online](#).
- Payroll costs do not include payroll processing or worker's compensation costs.

How much of my loan will be forgiven?

You must repay any portion of the loan if you use the loan amount for anything other than payroll costs, mortgage interest, rent, and utilities payments. However, if a borrower, over the 8 weeks after getting the loan, pay qualifying costs the loan total, including accrued and unpaid interest, will be forgiven. Not more than 25% of the forgiven amount may be for non-payroll costs. You will see your forgiveness portion reduced if you do not maintain your staff and payroll.



- **Number of Staff:** Your loan forgiveness will be reduced if you decrease your full-time equivalent employee headcount over a base period. However, see below for exceptions.
- **Level of Payroll:** Your loan forgiveness will also be reduced if you decrease salaries and wages by more than 25% for any employee, making less than \$100,000 annualized in 2019, over a base period
- **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. Laid off employees who were issued a good faith offer of rehire, at the same salary/wages and number of hours, but reject that offer will not be included in the full-time equivalent headcount reduction calculation. The offer must be in writing and the rejection must be documented by the employer

Practical tips to maximize loan forgiveness:

- Based on the foregoing analysis, a business seeking to maximize its loan forgiveness should, to the extent possible, consider the following tips:
 - o Avoid reducing employee equivalent headcount or compensation during the 8 week period.
 - o During the 8 week period, try to ensure that at least 75% of the loan proceeds used to pay permitted expenses are for Payroll Costs, and that no more than 25% are used for non-Payroll Costs.

How can I request loan forgiveness?

You will submit a request to the lender that is servicing the loan after the 8 week period. Your lender should provide you with instructions on how to apply for loan forgiveness. The request will include documents as outlined below. You must certify that the documents are true and that you used the forgiveness amount to keep employees and make eligible mortgage interest, rent, and utility payments. The lender must make a decision on the forgiveness within 60 days.

These are the required documents you will need to collect to provide with your PPP forgiveness application. Your lender may have additional requirements.

- Documents verifying the number of full-time equivalent employees on payroll and their pay rates, for the periods used to verify you met the staffing and pay requirements:
 - o Payroll reports from your payroll provider.
 - o Payroll tax filings (Form 941).
 - o Income, payroll, and unemployment insurance filings from your state.
 - o Documents verifying any retirement and health insurance contributions.
- Documents verifying your eligible interest, rent, and utility payments (canceled checks, payment receipts, and account statements).

Sole-proprietorships will, in addition to the above if they have employees, will need to use their 2019 federal Schedule C Form 1040 to calculate the amount of the loan and also the forgiveness calculation. 8/52 of the net income from a sole proprietorship will be used. Owner's health and retirement expenses are not included.

Good recordkeeping and bookkeeping will be critical for getting your loan forgiven—you'll need to keep track of eligible expenses and their accompanying documentation over the eight weeks. Your lender will likely require these documents in digital format, so take the time to scan any paper documents and keep backups of your digital records.



If you don't have a reliable bookkeeping solution in place, Avitus Group can do your bookkeeping for you, all online. Learn more for a free consultation by contacting us at referral@avitusgroup.com.

What happens if I'm not approved for forgiveness?

Your lender may allow you to provide additional documentation so they can reevaluate your request. Otherwise, your outstanding balance will continue to accrue interest at 1%, for the remainder of the 2-year period. There is no prepayment penalty. You can pay off the outstanding balance at any time with no additional fees.

Virtual Hotline Available

To help with your concerns related to COVID-19, Avitus Group has a Virtual Hotline Form where you can submit questions or requests to our leading experts in all categories of business support. To give it a try, please click here: [Virtual Hotline Form](#).

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