

# PPP Loan Forgiveness and Related Tax Issues (June 24, 2020 Update)

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# CPE

- There will be 4 Attendance Check Words
- PLEASE WRITE THESE DOWN!
- At the end of the program, you will receive a link where you will enter those words to verify your attendance and claim your certificate.

# Agenda

- How we got here
- The updated regulations
- Filing out the forms
- Tax issues
- Questions

# PPP Loan Forgiveness Application and Rules

- Since April 2, 2020 the SBA has been issuing a flurry of regulations FAQs and other guidance to implement the CARES Act
- On June 5, 2020 The Paycheck Protection Flexibility Act (the “PPFA”) was signed into law modifying the PPP in key ways, including:
  - Money can be spent over 24 weeks, instead of 8 weeks
  - Non-payroll expenses could be 40% of amount, instead of 25%
  - 5 year repayment, instead of 2 years
  - Loosening restriction on rehiring FTEs
  - Can defer employer paid withholding taxes
- On June 11, 12, 17, and 22, the SBA issued updated guidance and forms for loan forgiveness to implement the changes to the CARES Act by the PPFA
- The rules continue to change weekly, if not more often

# Process for Obtaining Loan Forgiveness

- Borrower to submit SBA Form 3508 or 3508-EZ – the loan forgiveness forms
  - Banks are likely to create on-line portals for borrowers to submit forgiveness information
- Lender has 60 days to review and submit to SBA with a reimbursement application
- SBA then has 90 days to review the lender's submission and issue reimbursement
- The SBA may retroactively determine that a borrower was not eligible for a PPP loan (“for example, because the borrower lacked an adequate basis for the certifications it made in its PPP application.”) 6/22/2020 Interim Final Rule at 8.
- The SBA issued a separate rule on May 22, 2020 concerning review of loan forgiveness applications. It is not clear if this will be updated.

# Deferral Period and Forgiveness

- Borrowers can apply for forgiveness anytime after they have used all of the loan proceeds (including before the end of the covered period)
- If you apply for forgiveness *before* the end of the covered period (be it 8 or 24 weeks) you must still account for additional FTE/wage reduction *for the entire covered period*
  - Thus, if you apply before the end of the covered period and later reduce FTEs/wages you will *not* be able to take advantage of FTE/wage restoration safe harbor
  - The open question is if you can *further* reduce FTEs/wages after the forgiveness application is filed and if that would effect forgiveness further
- You must apply for forgiveness within 10 months after the last day of the covered period, or the loan cannot be forgiven
- Borrowers decide whether to use the 8 or 24 week period when they submit the forgiveness application



# 8 vs. 24 Weeks: Which One?

## 8 Weeks

- Forgiven faster
- Less FTE turnover
- SBA rules are likely to change
- Easier to prepare financial report and tax documents due in Fall 2020
- Owner comp. limited to: \$15,385

## 24 Weeks

- More time to spend money
- Owner comp. capped at: \$20,833
- Employee comp. capped at: \$46,154
- Need time to bring back FTEs/wage (hospitality industry in particular)
- More time for SBA to write coherent rules

# Payroll Costs and The Covered Period

- Payroll costs “paid or incurred” during the covered period are eligible for forgiveness, as well as up to 40% of non-payroll costs
- The covered period starts the day the loan proceeds are deposited
- Payroll costs are considered paid on the day paychecks are distributed or an electronic payment is initiated
- Borrowers don’t have to change their payroll cycle to obtain forgiveness
  - Even if payroll costs are incurred after the end of the covered period, as long as paid during the regular payroll cycle they are forgivable



# Payroll Costs and The Covered Period: Owner Compensation

- Generally
  - If 8 weeks: 8/52nds of 2019 cash compensation
  - If 24 weeks: 2.5/12ths of 2019 cash compensation
- C-Corporations
  - Payroll costs include: salary, employer retirement and healthcare contributions
- S-Corporations
  - Payroll costs include employer retirement contributions
  - Payroll costs *do not* include healthcare insurance contributions
- Partnerships, LLCs
  - Payroll costs include: net earnings from self-employment x 0.9235 divided by either: 8/52 or 2.5/12
  - Payroll costs do not include retirement or health insurance contributions
  - Max. forgivable compensation to owners is \$20,833

# Non-Payroll Costs

- Non-payroll costs that are incurred during the covered period are forgivable (not to exceed 40% of the loan amount)
- If payments are made pursuant to a regular billing cycle, if the payment is made after the end of the covered period, it is still forgivable
- Example: Borrower receives its electric bill monthly on the 20<sup>th</sup>. The loan was advanced on May 1st and the borrower elects the 24 week period. The “covered period” ends October 16<sup>th</sup>. Even though the electric bill is received after the end of the covered period, it is for costs incurred during the covered period and will be a forgivable expense

# Reduction of Loan Forgiveness

- FTEs/wages now must be replaced by December 31, 2020
- Borrowers will not have forgiveness reduced if they cannot rehire FTEs because:
  - FTEs quit or refuse to return to work – you must document their refusal to return to work in writing to comply with record keeping requirements
    - Borrowers are required to inform state authorities of a refusal to return to work
  - A documented inability to rehire “similarly qualified” FTEs
  - A documented inability to return to the same business level as before 2/15/2020 *due to compliance with health and safety guidelines – for example: a restaurant that can only have 50% capacity*

# Loan Forgiveness Process for Lenders

- Must ensure forgiveness application is complete and all data is supported as required
- Must perform at least a “minimal review of calculations” and supporting documents, including third-party payroll processing information
- If the payroll is not well documented or not processed by a recognized third-party processor, more diligence will need to be undertaken (i.e. obtain cancelled checks, etc.)
- If the lender finds errors or missing information, it should inform the borrower of its errors and attempt to get a correct and complete application

# Loan Forgiveness Denial

- When a lender recommends **denial** of a forgiveness application, it must provide the SBA with: (a) the forgiveness application form, (b) confirm the accuracy of information in the forgiveness application, (c) proof that borrower has been notified, and (d) basis for the denial.
- The borrower has 30 days to protest the denial.
- The SBA has not released any guidance on the protest/appeal process and there is no statutory guidance.
- The SBA is not required to review the denial, and has 5 days to determine whether to deny review.
- If the SBA accepts review, it has 90 days to render a decision

# Completing the Form 3508-EZ

## When to Use

- If you are sole proprietor or an independent contractor; or
- If your business did not reduce FTEs or wages more than 25% during the covered period; or
- If your business did not reduce wages more than 25% but could not maintain FTEs due to compliance with governmental COVID-19 orders effecting normal operations

## Advantages

- 2 pages – much simpler





Paycheck Protection Program  
PPP Loan Forgiveness Application Form 3508EZ

OMB Control No. 3245-0407  
Expiration Date: 10/31/2020

**PPP LOAN FORGIVENESS APPLICATION FORM 3508EZ INSTRUCTIONS FOR BORROWERS**

**Checklist for Using SBA Form 3508EZ**

You (the Borrower) can apply for forgiveness of your Paycheck Protection Program (PPP) loan using this SBA Form 3508EZ if you can check at least one of the three boxes below. Do not submit this Checklist with your SBA Form 3508EZ.

- The Borrower is a self-employed individual, independent contractor, or sole proprietor who had no employees at the time of the PPP loan application and did not include any employee salaries in the computation of average monthly payroll in the Borrower Application Form (SBA Form 2483).  
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- The Borrower did not reduce annual salary or hourly wages of any employee by more than 25 percent during the Covered Period or the Alternative Payroll Covered Period (as defined below) compared to the period between January 1, 2020 and March 31, 2020 (for purposes of this statement, “employees” means only those employees that did not receive, during any single period during 2019, wages or salary at an annualized rate of pay in an amount more than \$100,000);  
**AND**  
The Borrower did not reduce the number of employees or the average paid hours of employees between January 1, 2020 and the end of the Covered Period. (Ignore reductions that arose from an inability to rehire individuals who were employees on February 15, 2020 if the Borrower was unable to hire similarly qualified employees for unfilled positions on or before December 31, 2020. Also ignore reductions in an employee’s hours that the Borrower offered to restore and the employee refused. See [85 FR 33004](#), 33007 (June 1, 2020) for more details.  
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- The Borrower did not reduce annual salary or hourly wages of any employee by more than 25 percent during the Covered Period or the Alternative Payroll Covered Period (as defined below) compared to the period between January 1, 2020 and March 31, 2020 (for purposes of this statement, “employees” means only those employees that did not receive, during any single period during 2019, wages or salary at an annualized rate of pay in an amount more than \$100,000);  
**AND**  
The Borrower was unable to operate during the Covered Period at the same level of business activity as before February 15, 2020, due to compliance with requirements established or guidance issued between March 1, 2020 and December 31, 2020 by the Secretary of Health and Human Services, the Director of the Centers for Disease Control and Prevention, or the Occupational Safety and Health Administration, related to the maintenance of standards of sanitation, social distancing, or any other work or customer safety requirement related to COVID-19.

If you can check at least one of the three boxes above, complete this SBA Form 3508EZ in accordance with the instructions below, and submit it to your Lender (or the Lender that is servicing your loan). Borrowers may also complete this application electronically through their Lender. If you are unable to check one of the boxes above, you cannot use SBA Form 3508EZ and instead you must apply for forgiveness of your PPP loan using SBA Form 3508.

**Line 1:** Enter total eligible payroll costs incurred or paid during the Covered Period or the Alternative Payroll Covered Period. To calculate these costs, sum the following:

**Cash Compensation:** The sum of gross salary, gross wages, gross tips, gross commissions, paid leave (vacation, family, medical or sick leave, not including leave covered by the Families First Coronavirus Response Act), and allowances for dismissal or separation paid or incurred during the Covered Period or the Alternative Payroll Covered Period. For each individual employee, the total amount of cash compensation eligible for forgiveness may not exceed an annual salary of \$100,000, as prorated for the Covered Period. For an 8-week Covered Period, that total is \$15,385. For a 24-week Covered Period, that total is \$46,154 for purposes of this 3508EZ. You can only include compensation of employees who were employed by the Borrower at any point during the Covered Period or Alternative Payroll Covered Period and whose principal place of residence is in the United States.

**Employee Benefits:** The total amount paid by the Borrower for:

1. Employer contributions for employee health insurance, including employer contributions to a self-insured, employer-sponsored group health plan, but excluding any pre-tax or after-tax contributions by employees. Do not add employer health insurance contributions made on behalf of a self-employed individual, general partners, or owner-employees of an S-corporation, because such payments are already included in their compensation.
2. Employer contributions to employee retirement plans, excluding any pre-tax or after-tax contributions by employees. Do not add employer retirement contributions made on behalf of a self-employed individual or general partners, because such payments are already included in their compensation, and contributions on behalf of owner-employees are capped at 2.5 months' worth of the 2019 contribution amount.
3. Employer state and local taxes paid by the borrower and assessed on employee compensation (e.g., state unemployment insurance tax), excluding any taxes withheld from employee earnings.

**Owner Compensation:** Enter any amounts paid to owners (owner-employees, a self-employed individual, or general partners). For a 24-week Covered Period, this amount is capped at \$20,833 (the 2.5-month equivalent of \$100,000 per year) for each individual or the 2.5-month equivalent of their applicable compensation in 2019, whichever is lower. For an 8-week Covered Period, this amount is capped at 8/52 of 2019 compensation (up to \$15,385).

# Completing the Form 3508 (Long Form)

## When to Use

- Business has reduced FTEs or wages more than 25%
- Business used more than 40% of loan for non-payroll costs

## Form and Instructions

- Have not changed much from the last iteration
- Contains a worksheet for calculating wage reduction
  - Safe harbors still apply: (1) employee refuses to return to work and refusal is documented, (2) COVID-19 prevented “regular” operations due to governmental action, or (3) restoration of FTEs/wages by 12/31/2020
- FTE reduction has been simplified.
  - FTEs are those working 40+ hours/week – assigned a value of 1.0
  - If an FTE is reduced (and not restored), they get a value of 0.0
  - If FTEs are >0.75, *pro rata* forgiveness reduction



Step 1. Determine if pay was reduced more than 25%.

a. Enter average annual salary or hourly wage during Covered Period or Alternative Payroll Covered Period:

\_\_\_\_\_.

b. Enter average annual salary or hourly wage between January 1, 2020 and March 31, 2020:\_\_\_\_\_.

c. Divide the value entered in 1.a. by 1.b.:\_\_\_\_\_.

If 1.c. is 0.75 or more, enter zero in the column above box 3 for that employee; otherwise proceed to Step 2.

Step 2. Determine if the Salary/Hourly Wage Reduction Safe Harbor is met.

a. Enter the annual salary or hourly wage as of February 15, 2020:\_\_\_\_\_.

b. Enter the average annual salary or hourly wage between February 15, 2020 and April 26, 2020:

\_\_\_\_\_.

If 2.b. is equal to or greater than 2.a., skip to Step 3. Otherwise, proceed to 2.c.

c. Enter the average annual salary or hourly wage as of the earlier of December 31, 2020 and the date this application is submitted:\_\_\_\_\_.

If 2.c. is equal to or greater than 2.a., the Salary/Hourly Wage Reduction Safe Harbor has been met – enter zero in the column above box 3 for that employee. Otherwise proceed to Step 3.

Step 3. Determine the Salary/Hourly Wage Reduction.

a. Multiply the amount entered in 1.b. by 0.75:\_\_\_\_\_.

b. Subtract the amount entered in 1.a. from 3.a.:\_\_\_\_\_.

If the employee is an hourly worker, compute the total dollar amount of the reduction that exceeds 25% as follows:

c. Enter the average number of hours worked per week between January 1, 2020 and March 31, 2020:

\_\_\_\_\_.

d. Multiply the amount entered in 3.b. by the amount entered in 3.c.\_\_\_\_\_. Multiply this amount by 24 (if Borrower is using a 24-week Covered Period) or 8 (if Borrower is using an 8-week Covered Period):\_\_\_\_\_. Enter this value in the column above box 3 for that employee.

If the employee is a salaried worker, compute the total dollar amount of the reduction that exceeds 25% as follows:

e. Multiply the amount entered in 3.b. by 24 (if Borrower is using a 24-week Covered Period) or 8 (if Borrower is using an 8-week Covered Period):\_\_\_\_\_. Divide this amount by 52:\_\_\_\_\_.

Enter this value in the column above box 3 for that employee.

# Calculating Forgiveness Reduction Due to Wage Reduction of More than 25%

## Example

- Prior to the February 15<sup>th</sup> Eric's Café had average monthly wages of \$250,000 (\$3,000,000 annually)
- Due to COVID Eric's Café reduced its monthly payroll to \$100,000/month as it was only able to do take-out and delivery (\$1,200,000 annually)
- On May 5<sup>th</sup>, Eric's Café applied for and received a \$625,000 PPP loan
- To date, Eric's Café has not restored wages

# Salaried Employee

## Step 1. Determine if pay was reduced more than 25%.

- a. Enter average annual salary or hourly wage during Covered Period or Alternative Payroll Covered Period: **\$50,000**
- b. Enter average annual salary or hourly wage between January 1, 2020 and March 31, 2020: **\$75,000**
- c. Divide the value entered in 1.a. by 1.b.: **0.67**

If 1.c. is 0.75 or more, enter zero in the column above box 3 for that employee; otherwise proceed to Step 2.



# Salaried Employee

## Step 2. Determine if the Salary/Hourly Wage Reduction Safe Harbor is met.

- a. Enter the annual salary or hourly wage as of February 15, 2020: **\$75,000**
- b. Enter the average annual salary or hourly wage between February 15, 2020 and April 26, 2020: **\$60,000**

**If 2.b. is equal to or greater than 2.a., skip to Step 3. Otherwise, proceed to 2.c.**

- c. Enter the average annual salary or hourly wage as of the earlier of December 31, 2020 and the date this application is submitted: **\$75,000.**

**If 2.c. is equal to or greater than 2.a., the Salary/Hourly Wage Reduction Safe Harbor has been met – enter zero in the column above box 3 for that employee. Otherwise proceed to Step 3.**

# Salaried Employee

## Step 3. Determine the Salary Reduction (salaried employee)

a. Multiply the amount entered in 1.b (**\$75,000**) by 0.75: **\$56,250**

b. Subtract the amount entered in 1.a. from 3.a.: **\$56,250 - \$50,000 = \$6,250**

# Salaried Employee

**If the employee is an hourly worker, compute the total dollar amount of the reduction that exceeds 25% as follows:**

- c. Enter the average number of hours worked per week between January 1, 2020 and March 31, 2020:
- d. Multiply the amount entered in 3.b. by the amount entered in 3.c. Multiply this amount by 24 (if Borrower is using a 24-week Covered Period) or 8 (if Borrower is using an 8-week Covered Period):\_\_\_\_\_ . Enter this value in the column above box 3 for that employee.

**If the employee is a salaried worker, compute the total dollar amount of the reduction that exceeds 25% as follows:**

- e. Multiply the amount entered in 3.b. by 24 (if Borrower is using a 24-week Covered Period) or 8 (if Borrower is using an 8-week Covered Period):  **$\$6,250 \times 24 = \$150,000$** , divide this amount by 52 =  **$\$2,884.62$**

Enter this value in the column above box 3 for that employee.

# Hourly Employee

## Assumptions

- \$25/hourly wage
- 40 hours per week work

## **Step 1. Determine if pay was reduced more than 25%.**

- a. Enter average annual salary or hourly wage during Covered Period or Alternative Payroll Covered Period: **\$16.75/hour**
- b. Enter average annual salary or hourly wage between January 1, 2020 and March 31, 2020: **\$25.00/hour**
- c. Divide the value entered in 1.a. by 1.b: **0.67**

If 1.c. is 0.75 or more, enter zero in the column above box 3 for that employee; otherwise proceed to Step 2.

# Hourly Employee

## Step 2. Determine if the Salary/Hourly Wage Reduction Safe Harbor is met.

- a. Enter the annual salary or hourly wage as of February 15, 2020: **\$25.00/hour**
- b. Enter the average annual salary or hourly wage between February 15, 2020 and April 26, 2020: **\$16.75/hour**

**If 2.b. is equal to or greater than 2.a., skip to Step 3. Otherwise, proceed to 2.c.**

- c. Enter the average annual salary or hourly wage as of the earlier of December 31, 2020 and the date this application is submitted: **\$16.75.**

**If 2.c. is equal to or greater than 2.a., the Salary/Hourly Wage Reduction Safe Harbor has been met – enter zero in the column above box 3 for that employee. Otherwise proceed to Step 3.**

# Hourly Employee

## Step 3. Determine the Salary/Hourly Wage Reduction.

a. Multiply the amount entered in 1.b **\$25/hour** by 0.75: **\$18.75**

b. Subtract the amount entered in 1.a. from 3.a.: **\$18.75 - \$16.75 = \$2.00**



# Hourly Wage Example

**If the employee is an hourly worker, compute the total dollar amount of the reduction that exceeds 25% as follows:**

c. Enter the average number of hours worked per week between January 1, 2020 and March 31, 2020: **40**

d. Multiply the amount entered in 3.b. by the amount entered in 3.c. Multiply this amount by 24 (if Borrower is using a 24-week Covered Period): **\$48.00** or 8 (if Borrower is using an 8-week Covered Period): **\$16.00**. Enter this value in the column above box 3 for that employee.

**If the employee is a salaried worker, compute the total dollar amount of the reduction that exceeds 25% as follows:**

e. Multiply the amount entered in 3.b. by 24 (if Borrower is using a 24-week Covered Period) or 8 (if Borrower is using an 8-week Covered Period): \_\_\_\_\_, divide this amount by 52.

Enter this value in the column above box 3 for that employee.

# Tax Issues

- PPFA allows employers to *both* obtain a PPP loan and defer the employer portion of withholding taxes through the remainder of 2020
- Borrower's loan and forgiveness applications must be consistent with tax documents
- No fix (yet) for non-deductibility of expenses paid with PPP funds
  - S.3612, Small Business Expense Protection Act, introduced on May 5<sup>th</sup> has not received any action
  - Several arguments have been raised as to why the expenses are not taxable despite IRS Notice 2020-32
  - If Congress does not act, the issue is sure to be litigated
- On June 19<sup>th</sup> the IRS issued Notice 2020-50 related to taxpayers who took retirement distributions due to COVID-19

# June 22, 2020 IRS FAQ

- IRS released updated FAQs on tax issues related to employment tax deferrals
- Employers can now *both* obtain a PPP loan and defer the employer portion of withholding taxes, with payments due:
  - 50% by 12/31/2020
  - 50% by 12/31/2021
- The IRS is taking the position that once a PPP loan is forgiven, the employer mat no longer defer (FAQ 1, 4)
- The IRS has clarified that the deferral period is March 27 – December 31, 2020 (unless the loan is forgiven earlier)
- The IRS will be revising Form 941 and providing guidance on how to properly prepare Q2 2020 941s
- If an employer believes they are entities to refundable tax credits for paid COVID-19 leave, they can still defer

# June 22, 2020 IRS FAQ (cont.)

- Independent contractors/sole proprietors may defer
- If you defer, there will be no estimate tax penalty on the deferred amount

# Notice 2020-50 (Jun. 22, 2020)

- Allows “qualified individuals” to avoid 10% penalty on early withdrawals (or certain loans) from qualified plans taken during 2020
- Permits employers to implement rules to facilitate early distributions/loans
  - Not required
- Definition of “qualified individual”:
  - Diagnosed with COVID-19
  - Spouse or dependent is diagnosed with COVID-19
  - Experienced adverse financial consequences due to (a) being quarantined, (b) unable to work due to lack of childcare, (c) lost job or hours, (d) job rescinded, (e) adverse financial consequences of spouse or family member who share’s individual’s personal residence

# Sales Tax Audits vs IRS Audits: A Review of State & Federal Audit Techniques and How to Protect Your Clients

June 30, 2020 | 1pm – 4pm Eastern | via Live Webinar

**THIS IS A PROGRAM  
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We will walk you through how sales tax audits are done, the techniques used by the various states, and how practitioners can help protect their client from the overzealous state auditor.

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# Questions