Davidson Pargman & Company, LLC
Certified Public Accountants and Advisors

January 11, 2021

Dear DPC Clients and Friends,

We want to share this information with you in case you are interested in the following:

1. First Draw PPP loan (did not already receive one)
2. Second Draw PPP loan (received initial PPP and would like to receive a second)
3. Employer Retention Credit

The SBA and Treasury issued guidance for the reconstituted Paycheck Protection Program (PPP). The SBA and Treasury announced Friday that the new PPP will re-open the week of Jan. 11 with community financial institutions exclusively allowed to make first-draw PPP loans on starting Jan. 11 and second-draw PPP loans starting Jan. 13. The PPP will open to all participating lenders at an unspecified date shortly thereafter and remain open through March 31.

We recommend contacting your bank to let them know you are interested in a PPP loan as soon as possible and find out what they may require.

First Draw PPP loan

If you did **not** get a First Draw PPP loan and are now interested, please contact us or your banker as soon as possible.

How much can I borrow?

Lesser of $10,000,000 or P/R-based formula (utilizing average P/R costs from 2019, 2020, or 1-year before date of loan).

Average P/R Costs (includes cash comp (salary, wages, commissions, similar comp, cash tips/equivalent, vacation, parental/family/medical/sick leave, allowance for separation/ dismissal), Employer (ER) share of EE benefits: Group health care/dental/vision /life/ disability including insurance, ER share of retirement, and SUTA) for EEs whose principal place of residence is the US, subtract comp paid >$100k annualized for period during which payments are made, divide by 12, multiply by 2.5.

(Ex. $240,000 P/R costs (cash plus ER benefits/SUTA as stated above in 2019, $264,000 P/R costs in 2020 - elect to use greater amount in 2020. 264,000 / 12 x 2.5 = $55,000 loan)

Specific Entities

1. S/E with no EEs, Sch C line 31 net profit, if >$100k, use $100k, divide by 12 x 2.5
2. Seasonal Employer - Does not operate for more than 7 months in any year, or preceding year had gross receipts for any 6 months of that year that were not >33.33% of gross receipts for other 6 mos. Avg monthly P/R for any 12-week period b/w 2/15/19-2/15/20.
3. Farmers/ranchers - No EEs - 2019/2020 Sch F gross income line 9 (limit to $100k) / 12 x 2.5
4. Partnerships - net earnings from s/e less 179, UPE, depletion x .9235 (limit to $100k), wages paid to EE (Box 5 Medicare wages plus pretax benefits reducing box 5 less amt >$100k) plus ER share of group health, life, disability, vision, and dental insurance, ER contribution to retirement, SUTA. Divide by 12 x 2.5.

Can I request an increase in my loan if I already applied?

1. Partnerships who did not include partner compensation on their original loan may reapply and include such amounts.
2. Seasonal employers who received a loan prior to 12/27/20 may revise the computation based on updated guidance.
3. Borrowers who returned all of their PPP funds after receiving an original loan may reapply.
4. Borrowers who returned part of their PPP loan may apply for the amount approved less the amount retained.
5. Borrowers who did not accept the full amount approved may request an increase up to the original amount approved.

Second Draw Details (IFR SBA-2021-0002) Summary

Last date to apply is March 31, 2021. Interest rate on loan is 1% and has a 5-year term. Loan repayments are required starting 10 months after the end of the 24-week period following the distribution of loan proceeds, if the entity has not applied for or is not eligible for loan forgiveness. No payments are required while your loan is being considered for forgiveness but will start after the SBA have remitted any forgiven amounts to the bank or have made their final determination regarding forgiveness. No personal guarantee is required.

Who qualifies?

1. Entity who has received a First Draw
2. Entity that has no more than 300 EEs
3. Must be able to show a decline in Gross Receipts from 2019 to 2020 of at least 25%
4. Have used entire first draw on or before the expected date of disbursement of Second Draw
5. Entire First Draw proceeds were spent on eligible expenses and 60% were used for payroll costs.
6. If NAICS code 72 and have more than 1 location, each location may qualify if no more than 300 EEs per location

How are Gross Receipts computed?

1. Use the accounting method used on tax returns.
2. Includes sales of products and services, interest, dividends, rents, royalties, fees or commissions less returns and allowances.
3. Generally, includes total income plus cost of goods sold less net capital gains or losses.
4. Does not include taxes collected to remit to taxing authority (sales tax and other taxes), amounts collected for another travel agent, real estate agent, advertising agent, conference management service provider, freight forwarder or customs broker.
5. Cannot exclude subcontractor costs, reimbursements for purchases a contractor makes at a customer's request, investment income, and employee-based costs such as P/R taxes from gross income.
6. Affiliate rules apply to add all affiliates gross receipts. However same waivers as first draw apply and add eligible news organizations and NAICS 72 with <=300 Ees and added religious exemption.

How do we compute a more than 25% decline in Gross Receipts?

1. If entity was in operation for all of 2019, Applicant can either compare all of 2020 to 2019, OR use any 1 quarter in 2020 compared to 2019.
2. If entity was not in business Q1 or Q2 2019, but was in business Q3 and Q4, then need to show that the entity had gross receipts in Q1, Q2, Q3, or Q4 of 2020 that were <25% of either Q3 or Q4 of 2019.
3. If entity was not in business Q1, Q2, or Q3 2019, but was in business Q4, then need to show that the entity had gross receipts in Q1, Q2, Q3, or Q4 of 2020 that were <25% of Q4 2019.
4. If the entity was not in business in 2019, but was in business 2/15/20, then need to show that the entity had gross receipts in Q2, Q3, or Q4 of 2020 that were <25% of Q1 2020.

How do we compute the loan amount?

Similar rules as the First Draw with the following exceptions:

1. Maximum loan is $2,000,000 ($4,000,000 for all entities as part of a single corporate group).
2. For NAICS code 72, substitute 3.5 for 2.5 x Avg P/R costs.
3. Farmers subtract out P/R from gross receipts to prevent double counting.
4. For P/R costs, can use 2019, 2020, or 12-month period prior to loan to compute avg.

What documentation is required?

1. Similar documentation to First Draw. If same lender used and no changes to P/R costs, lender should already have documentation.
2. If loan no more than $150k, then only certification required to prove 25% reduction in Gross Receipts.
3. If loan >$150k, will also have to provide documentation for 25% reduction in Gross Receipts.

Can I gain forgiveness of the Second Draw?

Procedures for forgiveness of Second Draw loans are the same as First Draw loans.

Employee Retention Credit (ERC)

This is a significant credit that should be reviewed by all businesses. The original rules stated if you claimed PPP you were NOT eligible for the credit – this has changed that even if you received PPP loan, you may qualify for the Employee Retention Credit.

Several key ERC features included:

Eligible Employer.
An employer was entitled to the ERC if they met one of two requirements: (1) they experienced more than a 50% reduction in gross receipts in 2020 in a calendar quarter compared with 2019; or (2) their business operations were fully or partially suspended by a government order imposing restrictions by curbing travel, commerce, or group meetings because of the pandemic. Provisions concerning the full or partial suspension of operations were not clearly spelled out in CARES, but the IRS offered several FAQs on situations when the ERC is or is not available.

Employee Wages. The employer received a 50% credit on wages up to $10,000 per employee paid in 2020. Thus, a maximum credit of $5,000 per employee in 2020.

Qualified Wages for ERC. A critical aspect of the ERC: the credit was only available for employees that the employer continued to pay for not working. Although, there was a special rule for small employers with less than 100 full-time employees that allowed the credit to be provided whether employees were working or not. The IRS also offered FAQs on how these qualified wages were determined for ERC purposes.

ERC vs. PPP. As noted, the ERC and PPP loan were structured much differently but with a common goal of paying employees. However, the CARES legislation stipulated that an employer could not obtain a PPP loan and also receive an ERC. It was one or the other.

ERC Mechanics. An employer did not need to wait until the end of the year to realize the ERC; rather they could receive this credit during the year on their payroll tax filings. This would offset the payroll tax deposits, and if the ERC exceeded other payroll tax deposits, this amount could be refunded. IRS Form 941, Form 941X, and Form 7200 were used to claim the ERC.

ERC REVISIONS AND EXPANSIONS IN THE CAA

The CAA made several favorable changes in the ERC that may apply beginning in 2021 or retroactively back to the enactment of CARES in March 2020. In some cases, employers may be able to realize some ERC savings in 2020 as well as benefit during 2021. It is therefore essential for employers to determine if the CAA change impacting them applies only for 2021 or back into 2020.

Here are several of the CAA provisions that apply beginning in 2021:

- The ERC is available for employers from January 1, 2021 through June 30, 2021.
- The rate of the ERC wage credit increases to 70% in 2021 (up from 50% in 2020).
- The wage limitation per employee changes to $10,000 per quarter in 2021, not $10,000 per year (as in 2020). Thus, the maximum per employee credit in 2021 rises to $14,000 – nearly triple the $5,000 per employee cap in 2020.
- The ERC eligibility is enhanced by reducing the year-over-year quarterly drop in gross receipts requirement to 20% (from 50%).
- It significantly increases the small employer exception to employers with less than 500 employees (up from 100 employees). These employers will be entitled to higher ERC credits in 2021 for paying wages to all employees regardless of whether they are working or not.

Consideration for employers. These new CAA changes present sizable opportunities for employers to take advantage of the ERC. The higher 70% and increase in qualifying wages jumps the maximum credit per employee up to $14,000 and offers more benefits to employers. Further, the drop in gross receipts factor of 20%, down from 50% in CARES, permits more employers to be in a position to claim the ERC.

CAA changes that apply retroactively in 2020:

- CAA specifies that employers obtaining PPP loans from the CARES Act would also be eligible for the ERC. This was not permitted before the CAA. Please note, an employer cannot claim the ERC on the same wages they used in their payroll forgiveness application. As a result, an employer might seek to specify non-payroll costs (up to the 40% threshold) as part of their PPP loan forgiveness application. This may permit more qualifying wages for the ERC.
- The new law indicates that health insurance coverage provided to an employee would be treated as employee wages for ERC purposes, even if no other wages were paid to the employee.

Consideration for Employers. Employers receiving a PPP loan can go back and review their loan forgiveness, while also seeking to revisit 2020 wages and possibly obtain an ERC by filing amended payroll forms for 2020.

Sources: ROI Business Services and Sikich