

Government Clarifies PPP Loan Forgiveness for the Self-Employed

We now have both the new clarity and an easy road to Paycheck Protection Program (PPP) loan forgiveness for the self-employed with no employees.

New Easy Road to 100 Percent Forgiveness

Say thanks to the Paycheck Protection Program Flexibility Act of 2020. This new law creates a 24-week period for you to spend your PPP loan proceeds. If you obtained your loan proceeds before June 5, you can elect to use the eight-week period to spend your PPP loan proceeds.

Here's the big difference:

- If the 24-week covered period applies, your loan forgiveness for your *deemed payroll* is capped at 2.5 months of your 2019 Schedule C net profit, not to exceed \$20,833.
- If you elect the eight-week covered period, your loan forgiveness for your *deemed payroll* is capped at eight weeks, not to exceed \$15,385.

Why Is This Important?

When you file as a Schedule C taxpayer and have no employees, your PPP loan is based on 2.5 times your 2019 Schedule C, line 31, net profit, limited to \$20,833.

Here's how the loan amount works:

Sch. C Net Profit	Monthly	Loan Amount
\$125,000 limited to \$100,000	\$8,333	\$20,833
\$100,000	\$8,333	\$20,833
\$75,000	\$6,250	\$15,625
\$50,000	\$4,167	\$10,417
\$25,000	\$2,083	\$5,208

You may have your loan proceeds either in hand or in play at this point.

(If you have not yet applied for your PPP loan, do so now. Lawmakers recently reopened the program with an eye on using the remaining funds. Under this new law, the extension of the PPP loan program will last until the earlier of August 8, 2020, or the day the funds are exhausted.)

Let's keep our eyes on the "easy road" to forgiveness. Under the new 24-month rule, you achieve 100 percent forgiveness when you pay yourself the total loan amount within 10.8 weeks of the date you received your loan proceeds. Let's round the 10.8 to 11 weeks.

Yes, you are reading this correctly. By simply using the loan proceeds on yourself during the first 11 weeks, you achieve total forgiveness.

Note this. By using the 11 weeks, you achieve total PPP loan forgiveness without having to spend any money on rent, utilities, or interest.

When Can I Apply for Forgiveness?

According to SBA guidance issued on June 22, 2020, you may submit your loan forgiveness application anytime on or before the maturity date of the loan—including before the end of the covered period—if you used all the loan proceeds for which you requested forgiveness.

Example. You receive your \$20,833 PPP loan on May 15, 2020. You put the money in your business checking account. During the 11 weeks beginning with May 15, 2020, you write checks to yourself that total \$20,833. You can apply for \$20,833 of loan forgiveness anytime beginning week 11 or later.

Is It Really This Easy?

Yes.

What About Interest, Rent, and Utilities?

With the 11-week program described above, you don't have to consider interest, rent, or utilities to achieve 100 percent forgiveness. In fact, why bother? By simply using the 11 weeks, you have less paperwork and worry.

Of course, you might want to consider interest, rent, and utilities if this takes you to earlier forgiveness. To obtain full forgiveness, you could spend as little as 60 percent on payroll and the balance on interest, rent, and utilities.

Example. You file a Schedule C and have no employees, and on June 1, 2020, you obtain a PPP loan of \$20,000.

During the first eight weeks, you spend \$12,000 on yourself and \$8,000 on qualified Schedule C deductible business interest, rent, and utilities. You can elect the eight-week period and qualify for 100 percent forgiveness.

Here are the basic PPP forgiveness requirements that apply to your 2020 Schedule C business deduction payments for interest, rent, and utilities:

- Interest payments on any business mortgage obligation on real or personal property where such obligation was in place before February 15, 2020 (but not any prepayment or payment of principal)
- Payments on business rent obligations on real or personal property under lease agreements in force before February 15, 2020
- Business utility payments for the distribution of electricity, gas, water, transportation, telephone, or internet access for which service began before February 15, 2020

Meet the Paid Rule

On page 2 of the 3508EZ instructions, you find this:

Enter any amounts paid to a self-employed individual. 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.

We may suffer from unfounded paranoia because we find the word “paid” a word to be reckoned with. So, in our opinion, you should have your Schedule C business write you checks from its business account. If there's no separate business account, make sure the business writes checks that pay your personal expenses in the amount of the deemed compensation.

PPP Loan Forgiveness for Partnerships and S and C Corporations

If you operate your business as a partnership or an S or C corporation, you face entity-specific PPP loan forgiveness rules that apply to you as an owner-worker in the business.

The rules that apply to you do not apply to the rank-and-file employee group. The government puts you, the owner-worker, in a separate “owner-employee” category to limit your business’s PPP benefits.

There are four types of owner-employees:

1. General partners in partnerships
2. S corporation shareholder-employees
3. C corporation shareholder-employees
4. Form 1040, Schedule C filers (e.g., the self-employed, sole proprietors, 1099 recipients, single-member LLCs, and husband and wife LLCs treated as single-member LLCs)

If you own all or part of your business and work in the business, you fall into one of the four categories.

The maximum loan attributable to and forgiveness available for the “compensation paid” to any owner-employee across all businesses is

- \$15,385 for borrowers who received a PPP loan before June 5, 2020, and elected to use an eight-week covered period, or
- \$20,833 for borrowers under the 24-week covered period.

Owners of Multiple Businesses Beware

If you have ownership interests in more than one business, you need to consider that the owner-employee loan maximums apply to all your businesses.

The new interim final rule puts the \$15,385 or \$20,833 deemed compensation cap on the loan forgiveness for the defined owner-employee, but contains no guidance on how to allocate or otherwise deal with the caps when you have ownership interests in multiple businesses.

Example. You operate an S corporation and a proprietorship. You receive your PPP loan on June 17. The cap on your combined S corporation and proprietorship loan forgiveness attributable to (a) your employment in the S corporation and (b) your profits from the proprietorship is \$20,833.

We know you can obtain loan forgiveness for up to \$20,833, but we have no guidance on how you would allocate the forgiveness between the S corporation and proprietorship. Perhaps by the time you apply for PPP loan forgiveness, we will have some directions.

Partnerships

The PPP loan forgiveness begins for general partners at the amount of their 2019 net earnings from self-employment (reduced by claimed Section 179 expense deductions, unreimbursed partnership expenses, and depletion from oil and gas properties) multiplied by 0.9235.

You then take the lesser of the amount determined above or \$100,000, divide by 12, and multiply by 2.5 to find the loan amount. With this calculation, the maximum loan is \$20,833.

The maximum forgiveness attributable due to the partner’s self-employment income is

- \$15,385 if the partnership obtained its loan before June 5, 2020, and elected the eight-week regime, or
- \$20,833 if the partnership is under the 24-week program.

Planning note. Under the 24-week program, the partnership with no employees does not need to spend any amounts on interest, rent, or utilities to obtain full forgiveness. It can obtain full forgiveness in 11 weeks using the calculated self-employment income of up to \$20,833 for each partner.

S Corporations

As with any owner-employee, the PPP loan and its forgiveness for “compensation” is capped at \$15,385 under the eight-week covered period and \$20,833 under the 24-week covered period.

Reminder. The \$20,833 cap is based on the maximum defined compensation of \$100,000 divided by 12 and then multiplied by 2.5.

Under the 24-week program, the S corporation whose only employee is an owner-employee obtains full loan forgiveness after 11 weeks when using the 24-week covered period without spending anything for interest, rent, or utilities.

If the S corporation with no employees other than the owner-employee elects the eight-week covered period, the corporation has to spend money on interest, rent, and utilities to rise above the compensation cap and create full forgiveness.

The Paycheck Protection Program Flexibility Act of 2020 created a new statutory 60 percent payroll rule that can make it easier to qualify for full forgiveness with payments for interest, rent, and utilities when electing the eight-week covered period.

S corporation owner-employees are capped by the amount of their 2019 employee cash compensation and employer retirement contributions made on their behalf, but employer health insurance contributions made on their behalf cannot be separately added because those

payments are already included in their employee cash compensation.

Example. You operate your solo business as an S corporation. Your 2019 W-2 compensation of \$68,000 included \$18,000 for medical insurance. Your payroll cost for the PPP loan and its forgiveness includes the full \$68,000 plus what the S corporation paid into your retirement plan and to the state for unemployment insurance. The total of these amounts is capped at \$100,000, which creates the \$20,833 maximum loan amount as explained above.

C Corporations

C corporation owner-employees are capped by the amount of their 2019 employee cash compensation and employer retirement and health insurance contributions made on their behalf.

Example. You operate your business as a C corporation where you are the only employee. In 2019, the corporation paid you a salary of \$60,000, contributed \$12,000 to your retirement plan, paid \$20,000 for your family’s medical insurance, and paid \$350 to the state for unemployment insurance.

Your corporation has \$92,350 in qualifying payroll costs. Your loan and forgiveness are capped at \$19,240 ($\$92,350 \div 12 \times 2.5$).

Form 1040 Schedule C Businesses

Your PPP loan and its forgiveness for “compensation” are capped at \$15,385 under the eight-week covered period or at \$20,833 under the 24-week covered period. The cap amounts are computed using your net profit from line 31 of your 2019 Schedule C.

Your easy-peasy road to 100 percent loan forgiveness is the 11-week program. With 11 weeks of taking the loan amount out of the business, you obtain full forgiveness without paying any rent, utilities, or interest.

When Can the Owner-Employee's Business Apply for Forgiveness?

According to SBA guidance issued on June 22, 2020, you may submit your loan forgiveness application anytime on or before the maturity date of the loan—including before the end of the covered period—if you used all the loan proceeds for which you requested forgiveness.

Example. You receive a \$20,833 PPP loan on May 19, 2020. During the 11 weeks beginning with May 19, 2020, your corporation pays qualified payroll costs that total \$20,833. You can apply for \$20,833 of loan forgiveness anytime beginning with week 11.

COVID-19 Strategy: Hire Family Members to Create Tax Benefits

The COVID-19 pandemic may create tax benefit opportunities for you and your family members.

For example, you could hire your under-age-18 children, pay them, say, \$10,000 each, and they could pay zero federal income taxes. And you or your corporation, the employer, would deduct the \$10,000 you paid to each of the children. The child wins. You win. There's more.

Schedule C Business

Let's say you operate your business as a sole proprietorship, a single-member LLC that's treated as a sole proprietorship for tax purposes, a husband-wife partnership, or an LLC that's treated as a husband-wife partnership for tax purposes.

That means you can hire your under-age-18 child, and the child's wages will be completely exempt from Social Security and Medicare taxes (FICA tax) and FUTA taxes. To be clear, the FICA tax exemption applies to the employee's share of FICA tax that's withheld from the

employee's paychecks *and* to the employer's share of FICA tax that your business must pay over to the Feds.

For 2020, your under-age-18 employee-child's standard deduction will shelter from federal income tax the first \$12,400 of wages received if the child has no taxable income from other sources. In other words, no federal income taxes for the child with \$12,400 or less in wages.

You can hire the under-age-18 child part-time, full-time, or whatever works for you and the child. Right now, children in this age category are probably not attending school, and the school district's lengthy summer vacation may have already begun.

In the fall, will your under-age-18 child be attending school in person or online? You probably don't know anything for sure at this point. But in the COVID-19 era, your under-age-18 child's availability to work in your business may be at an all-time high.

The wages received by your child can be used to help keep the family afloat financially. If the family is not so financially stressed, your child can use some or all of the wages to fund a college savings account or make a Roth IRA contribution.

What if My Business Is Incorporated?

If you operate your business as an S or a C corporation, your child's wages received from the business are subject to FICA and FUTA taxes, just like any other employee, regardless of the child's age.

What if I Hire a Family Member over Age 21?

Do it—if this adds after-tax cash to the family unit! The wages received from your business are subject to FICA and FUTA taxes, just like any other employee. This is the case whether you operate your business as an unincorporated sole proprietorship, a partnership, an LLC, or as an S or a C corporation.

Tax Advantages for Your Business

When you hire a child or other family member, your business deducts the wages paid.

- If you operate the business as a sole proprietorship, a single-member LLC that's treated as a sole proprietorship for tax purposes, a husband-wife partnership, an LLC that's treated as a husband-wife partnership for tax purposes, or an S corporation, the wage expense deduction reduces (a) your individual federal taxable income, (b) your individual net self-employment income, and (c) your individual state taxable income (if applicable).
- If you operate the business as a C corporation, the corporation deducts the wages paid to a child or other family member. The deductions reduce the corporation's federal taxable income and probably the corporation's state taxable income (if applicable).
- If your business will be unprofitable this year due to the COVID-19 fallout, deductions for wages paid to a child or other family member can create or increase a net operating loss (NOL) for 2020. If so, you can carry back the 2020 NOL for up to five tax years—back to 2015. The NOL carryback can trigger a refund of income taxes paid for the carryback year. That can really help. An NOL carried back to a pre-2018 tax year can be especially helpful because tax rates were generally higher in those days.

Keep payroll records just like you would for any other employee to document hours worked and duties performed (e.g., timesheets and job descriptions). Issue W-2s just like you would for any other employee.

IRS Enables Millions to Qualify for the \$100,000 IRA Grab and Repay

New IRS guidance expands the possibilities for what is an adverse COVID-19 impact on you for purposes of taking up to \$100,000 out of your retirement accounts and repaying it without penalties.

First, let's look at the rules as they existed before this new IRS guidance. The CARES Act created the first set of favorable rules, and those rules are still in play.

What the CARES Act Says

A coronavirus-related distribution from your qualified retirement plan, Section 403(b) plan, or IRA gets two tax benefits:

1. If you withdraw and keep the money, you pay no 10 percent early withdrawal penalty and you can spread the income equally over tax years 2020, 2021, and 2022. You also can elect to include it all in tax year 2020, if you want.
2. You can repay the money within three years of the distribution date and pay no tax or penalty on the amount.

Under the CARES Act relief, you qualify for a coronavirus-related distribution if

- you, your spouse, or your dependent is diagnosed with COVID-19 with a CDC-approved test;

- you experience adverse financial consequences as a result of being quarantined, being furloughed or laid off, or having work hours reduced due to COVID-19;
- you experience adverse financial consequences as a result of being unable to work due to lack of childcare due to COVID-19; or
- you experience adverse financial consequences as a result of closing or reducing your business hours due to COVID-19.

- your spouse or a member of your household is unable to work due to lack of childcare due to COVID-19; or
- your spouse or a member of your household owns or operates a business that closed or reduced hours due to COVID-19.

Household

For purposes of applying the additional factors, a member of the individual's household is someone who shares the individual's principal residence.

Merriam-Webster defines a household as

- those who dwell under the same roof and compose a family, and
- a social unit composed of those living together in the same dwelling.

You have to think roommates living together create a household, and if one of them is affected by COVID-19—say, lost his or her job and stopped contributing to the rent—the remaining roommates were adversely affected and should be entitled to the IRA grab-and-repay strategy.

Your Repayment Options

You have many repayment options, as we explain below. To make this easy, let's say you grab \$30,000 from your IRA today and you want to know how you can repay the \$30,000 with no taxes or penalties. Here are five scenarios:

Scenario 1. You repay the \$30,000 before you timely file your 2020 tax return:

And then there are two additional CARES Act rules for coronavirus-related distributions:

1. You can't treat more than \$100,000 per person as a coronavirus-related distribution, and
2. You must take the distribution on or after January 1, 2020, and before December 31, 2020.

IRS Expands Relief

With the new IRS relief, you now also qualify for coronavirus-related distributions if you experience adverse financial consequences because

- you, your spouse, or a member of your household has a reduction in pay or self-employment income due to COVID-19;
- you, your spouse, or a member of your household has a job offer rescinded or a start date for a job delayed due to COVID-19;
- your spouse or a member of your household is quarantined, is furloughed or laid off, or has work hours reduced due to COVID-19;

- You don't include any of the \$30,000 in income on your 2020 tax return. You pay no taxes or penalties.

Scenario 2. You elect to include all \$30,000 as income on your timely filed 2020 tax return, but then repay the full \$30,000 sometime between filing the 2020 return and July 15, 2023:

- You amend your 2020 tax return to remove the \$30,000 from income and claim a refund of tax paid on that amount.

Scenario 3. You include \$10,000 as income on your timely filed 2020 tax return, but then repay the full \$30,000 sometime between filing the 2020 return and July 15, 2023:

- You claim \$10,000 of income on your original 2020 tax return, and
- You later amend your 2020 tax return to remove the \$10,000 from income and claim a refund of tax paid on that amount.

Scenario 4. You include \$10,000 as income on your timely filed 2020 tax return, but then decide to repay \$10,000 of the total \$30,000 distribution, which you do on March 1, 2022:

- You claim \$10,000 of income on your 2020 tax return,
- You claim no income on your 2021 tax return (because you made the \$10,000 repayment prior to filing the return), and
- You claim \$10,000 of income on your 2022 tax return.

Scenario 5. You include \$10,000 as income on your timely filed 2020 tax return, but then decide to repay \$20,000 of the total \$30,000 distribution, which you do on November 1, 2021. This one is tricky because you have two ways to do it:

- You claim no income from the distribution on either your 2021 or 2022 tax return, or
- You claim \$10,000 of income on your 2022 tax return and amend your 2020 tax return to remove the \$10,000 from income and claim a refund of tax paid on that amount.

As you can see, you have many options to repay or not when it comes to taking up to \$100,000 from your retirement plan.