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Forgivable Paycheck Loan Or Tax Credit: You Can't Claim Both, Which Is Better?

The CARES Act provisions for small business include the Paycheck Protection Program, which calls for up to $10 million in forgivable loans to cover employee payroll, and immediate tax credits that are designed to do the same thing. You cannot get both a small business loan under the PPP **and also** claim a tax credit, so some comparison is needed. The Paycheck Protection Program allows loans of up to $10 million at 1% interest to employers with fewer than 500 workers to cover two months of payroll and overhead. If you keep your workers and do not cut their wages, the government will forgive most or all of the loan and even repay the bank that actually made you the loan. The loan amounts will be forgiven as long as: (1) The loan proceeds are used to cover payroll costs, and most mortgage interest, rent, and utility costs over the 8 week period after the loan is made; and (2) Employee and compensation levels are maintained. Payroll costs are capped at $100,000 for each employee. SBA lenders have details, though there has been controversy and hiccups in rolling out the program.

Who can apply? All businesses, even if the business is just you as a self-employed independent contractor, any business with 500 or fewer employees. That covers a lot of territory. You need to complete the Paycheck Protection Program loan application and submit the application with the required payroll and other documentation to an approved lender. A key feature is forgiveness of the loan. You will owe money when your loan is due if you use the loan amount for anything other than payroll costs, mortgage interest, rent, and utilities payments over the 8 weeks after getting the loan. The IRS says that not more than 25% of the forgiven amount may be for non-payroll costs. You will also owe money if you do not maintain your staff and payroll.

Your loan forgiveness will be reduced if you decrease your full-time employee headcount. 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. 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.

You also have to specifically request loan forgiveness. You can submit a request to the lender that is servicing the loan. The request will include documents that verify the number of full-time equivalent employees and pay rates, as well as the payments on eligible mortgage, lease, and utility obligations. 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.

Tax Credit Instead? One thing is clear. You can't get both a small business loan under the PPP **and also** claim a tax credit. See claiming CARES Act tax credits to keep employees. Which is better? It's one of those annoying "it depends." How does the tax credit work so you can compare? Designed to encourage businesses to keep employees on their payroll, this refundable tax credit is 50% of up to $10,000 in wages paid by an eligible employer whose business has been financially impacted by COVID-19. See IRS explains coronavirus tax credit details.

The credit is available to all employers regardless of size (a key difference from the loans), including tax-exempt organizations. There are only two exceptions: State and local governments and their instrumentalities and small businesses who take small business loans (once again, you can't have both). Qualifying employers must fall into one of two categories:

1. The employer's business is fully or partially suspended by government order due to COVID-19 during the calendar quarter.

2. The employer's gross receipts are below 50% of the comparable quarter in 2019. Once the employer's gross receipts go above 80% of a comparable quarter in 2019, they no longer qualify after the end of that quarter.

These measures are calculated each calendar quarter. The amount of the credit is 50% of qualifying wages paid up to $10,000 in total. Wages paid after March 12, 2020, and before Jan. 1, 2021, are eligible for the credit. Wages taken into account are not limited to cash payments, but also include a portion of the cost of employer provided health care. Qualifying wages are based on the average number of a business's employees in 2019. If the employer had 100 or fewer employees on average in 2019, the credit is based on wages paid to all employees, regardless if they worked or not. If the employees worked full time and were paid for full time work, the employer still receives the credit.

Employers can be immediately reimbursed for the credit by reducing their required deposits of payroll taxes that have been withheld from employees' wages by the amount of the credit. If the employer's employment tax deposits are not sufficient to cover the credit, the employer may receive an advance payment from the IRS by submitting Form 7200. Eligible employers can also request an advance of the Employee Retention Credit by submitting Form 7200. Updates on the implementation of this credit, Frequently Asked Questions on Tax Credits for Required Paid Leave and other information can be found on the Coronavirus page of IRS.gov. See also claiming CARES Act tax credits to keep employees.

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