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Balance sheet

Paycheck Protection Program Second Draw

By Timothy J. Gephart, CPA

At the end of 2020, Congress passed, and President Trump signed, a new law that provides for additional relief related to the coronavirus (COVID-19) pandemic. This law, the Consolidated Appropriations Act, 2021 (CAA, 2021), includes a second draw of Paycheck Protection Program (PPP) loans (PPP2). It also allows businesses to deduct ordinary and necessary expenses paid from the proceeds of PPP loans.

Background. In March 2020, the Coronavirus Aid, Relief and Economic Security (CARES) Act was enacted. The CARES Act authorizes the Small Business Administration (SBA) to make loans to qualified businesses under certain circumstances. The provision established the PPP, which provided up to 24 weeks of cash-flow assistance through 100% federally guaranteed loans (Original PPP Loans) to eligible recipients. Taxpayers could apply to have the loans forgiven to the extent their proceeds were used to maintain payroll during the COVID-19 pandemic and to cover certain other expenses.

Paycheck Protection Program Second Draw Loans (PPP2). The CAA, 2021 permits certain smaller businesses who received a PPP loan and experienced a 25% reduction in gross receipts to take a PPP Second Draw Loan of up to \$2 million.

Eligible entities. In order to qualify for a PPP2, a taxpayer must have taken out an Original PPP Loan. In addition, prior PPP borrowers must meet the following conditions to be eligible for the PPP2:

- Employ no more than 300 employees per physical location;
- Have used or will use the full amount of their first PPP loan; and
- Demonstrate at least a 25% reduction in gross receipts in the first, second, or third quarter of 2020 relative to the same 2019 quarter. Applications submitted on or after January 1, 2021 are eligible to utilize the gross receipts from the fourth quarter of 2020.



Eligible entities include for-profit businesses, certain non-profit organizations, housing cooperatives, veterans' organizations, tribal businesses, self-employed individuals, sole proprietors, independent contractors, and small agricultural co-operatives.

Loan terms. Borrowers may receive a PPP2 of up to 2.5 times the average monthly payroll costs in the one year prior to the loan or in calendar year 2019. However, borrowers in the hospitality or food services industries (NAICS code 72) may receive PPP2 of up to 3.5 times average monthly payroll costs. Only a single PPP2 is permitted to an eligible entity.

Gross receipts and simplified certification of revenue test. Taxpayers who borrow PPP2 of no more than \$150,000 may submit a certification, on or before the date the loan forgiveness application is submitted, attesting that the eligible entity meets the applicable revenue (gross receipts) loss requirement.

Loan forgiveness. Like Original PPP loans, PPP2 may be forgiven for payroll costs of up to 60% (with some exceptions) and nonpayroll costs such as such as rent, mortgage interest and utilities of 40%. Forgiveness of the loans is not included in income as cancellation of indebtedness income.

Deductibility of expenses paid by PPP loans. The CARES Act was silent on whether expenses paid with the proceeds of PPP loans could be deducted. IRS took the position that these expenses were nondeductible. The CAA, 2021 provides that expenses paid both from the proceeds of loans under Original PPP loans and PPP2 are deductible.

Please contact our office with any further questions you might have on PPP loan forgiveness.

Items presented are not intended to be technically complete. Additional information may be required to make an informed decision.

You cannot rely upon this information for avoiding tax penalties.