

January 19, 2021

## MEMORANDUM

**TO:** SBDC Network

**FROM:** MD Austin

**SUBJECT:** **FAQ - How to Calculate Maximum Loan Amounts for First Draw Loans**

The second round of PPP funding portal opened for all lenders today, and already the SBA has issued a list of FAQs for borrowers and lenders related to first draw loans. These scenarios include:

1) Self-employed with no employees:

- a. Use 2019 form 1040 schedule C, line 31 (net profit amount). If over \$100,000, reduce to \$100,000, but if -0- or negative, *borrower is not eligible*
- b. Calculate the average monthly net profit amount (divide amount in step “a” by 12)
- c. Multiply the average monthly net profit amount X 2.5

*Required Documentation includes:*

- 2019 1040 Schedule C to support amount of PPP
- 2019 form 1099-MISC reflecting non-employee compensation
- 2019 1099-K
- 2019 invoices
- Bank statement
- Book of record establishing self-employment status
- 2020 invoices
- Bank statements
- Book of record reflecting operating on 2/15/2020

2) Self-employed with employees:

- a. Compute 2019 payroll costs by adding the following:
  - i. 2019 Form 1040 Schedule C line 31 net profit amount
    1. If over \$100,000, reduce to \$100,000
    2. If the amount is -0- or less, set at -0-
  - ii. 2019 gross wages and tips paid to employees residing in the US, up to \$100,000 per employee based on:
    1. 2019 form 941 (line 5c – column #1) for each quarter
    2. Add pre-tax employee contributions for health insurance or other fringe benefits excludible from Taxable Medicare wages and tips,

- a. Minus amounts paid over \$100,000 and employees residing outside the US
  - iii. 2019 employer contributions for employee group health, life, disability, vision, and dental insurance (1040 schedule C, line 14)
  - iv. 2019 employer contributions to employee retirement plans (1040 schedule C, line 19)
  - v. 2019 employer state and local taxes assessed on employee compensation, primarily state unemployment tax insurance (from quarterly state wage reporting forms)
- b. Calculate average monthly payroll cost amount (divide step 1 by 12)
- c. Multiply step 2 X 2.5

*Required Documentation Includes:*

- 2019 1040 Schedule C
- 941 and state quarterly wage unemployment insurance tax reporting
- Documentation of any retirement, group health, life, disability, vision, and dental contributions
- Payroll statement or similar document dated 2/15/2020 to confirm in operation

3) Self-employed farmers and ranchers:

- a. Use 1040 schedule F
- b. Use same calculations as above
- c. Use same additions and subtractions as above

*Required Documentation Includes:*

- Same as for 1040 Schedule C filers

4) Partnerships:

- a. Compute 2019 payroll costs using the following:
  - i. 2019 schedule K-1 (form 1065) Net Earnings from Self-employment subject to self-employment tax, X .9235, up to \$100,000 per partner
    - 1. Compute the net earnings from self-employment of individual US-based general partners (box 14a, schedule K-1) less:
      - a. Any section 179 expenses in box 12
      - b. Any unreimbursed partnership expenses claimed
      - c. Any depletion on oil or gas properties
        - i. If over \$100,000, reduce to \$100,000
        - ii. If less than -0-, set amount to -0-
  - ii. 2019 gross wages and tips paid to US based employees, up to \$100,000 per employee, based on the following:

1. 2019 quarterly form 941 (line 5c, column 1)
  2. Add pre-tax employee contributions for health insurance or other fringe benefits excluded from Taxable Medicare wages and tips, and
  3. Subtract any amounts paid to employees over \$100,000 and any non-US employees
  4. Add 2019 employer contributions for employee (but not partner) group insurances (form 1065 line 19)
  5. Add 2019 employer contributions to employee (not partner) retirement plans (1065 line 18), and
  6. Add 2019 employer state and local taxes, primarily unemployment insurance, from state quarterly wage reporting forms
- b. Calculate average monthly payroll costs (step i divided by 12)
  - c. Multiply average monthly payroll costs X 2.5

*Required Documentation Includes:*

- 2019 1065, including K-1s
- 2019 941s
- State & local quarterly unemployment insurance forms
- Records of any retirement or group health, life, etc., insurance contributions
- Proof of that partnership had employees on 2/15/2020 (if claimed)
- If no employees, an invoice, bank statement, or book of record indicating business operational on 2/15/2020

5) S and C corporations:

- a. Compute 2019 payroll costs
  - i. 2019 gross wages and tips paid employees, up to \$100,000 per employee, based on:
    1. 2019 941, line 5c- column 1, from each quarter
    2. Add any pre-tax employee contributions for health insurance or other fringe benefits excluded from Taxable Medicare wages & tips
    3. Subtract amounts paid employees more than \$100,000, and any employee residing outside the US
    4. 2019 employer group insurance (from form 1120, line 24 or 1120-S line 18)
    5. 2019 employer retirement contributions (form 1120 line 23 or 1120-S line 17)
    6. 2019 state and local taxes assessed (from quarterly wage reporting forms)
- b. Calculate average monthly payroll costs (divide i by 12)

- c. Multiply average monthly payroll cost X 2.5

*Required Documentation Includes:*

- 2019 form 941 for each quarter (or payroll records from 3<sup>rd</sup> party provider)
- 2019 1120 or 1120-S or other documentation that supports amount included
- Payroll or other statement reflecting operation on 2/15/2020

6) Non-profits:

- a. Compute 2019 payroll costs by adding the following:
  - i. 2019 gross wages and tips paid US employees, up to \$100,000 per employee computed using:
    - 1. 2019 form 941, line 5c- column 1 for each quarter
    - 2. Add pre-tax employee contributions for insurance and other fringe benefits from Taxable Wages & Tips
    - 3. Subtract amount paid for employees more than \$100,000 and non-US employees
  - ii. 2019 employer group insurance (form 990, part IX, line 9)
  - iii. 2019 employer retirement contributions (form 990, part IX, line 8)
  - iv. 2019 employer state and local taxes assessed (from quarterly wage reporting forms)
- b. Calculate average monthly payroll costs (divide i by 12)
- c. Multiply average monthly payroll X 2.5

*Required Documentation Includes:*

- 2019 form 941s for each quarter
- State quarterly wage unemployment tax reporting form (or equivalent provided by a 3<sup>rd</sup> party provider)
- 2019 form 990, part IX or other document supporting benefits paid
- Payroll record or other document supporting that entity was operational on 2/15/2020
- Some smaller entities may use the 990 EZ instead of the 990

7) Eligible non-profit religious institutions, veterans' organizations, and tribal businesses:

- a. Compute 2019 payroll costs by adding the following:
  - i. 2019 gross wages and tips, up to \$100,000 for US resident employees, based on the following:
    - 1. 2019 IRS 941 (line 5c- column 1) from each quarter
    - 2. Add pre-tax employee contributions for insurance and other fringe benefits excluded from Taxable Wages
    - 3. Subtract employee wages more than \$100,000, and any non-US resident employees

- ii. 2019 employer group insurance contributions
  - iii. 2019 employer retirement contributions
  - iv. 2019 employer state and local taxes and unemployment insurance (from state quarterly wage reporting forms)
- b. Calculate average monthly payroll costs by dividing i by 12
  - c. Multiply average monthly payroll costs X 2.5

*Required Documentation Includes:*

- 2019 form 941
- State quarterly wage unemployment tax reporting form (or equivalent documentation from a 3<sup>rd</sup> party)
- Documentation for any retirement or group insurance contributions
- A payroll record indicating entity was operational on 2/15/2020

*Miscellaneous Questions:*

LLCs – use the instructions above that apply to their tax filing status.

Documentation acceptable to support payroll costs include:

- W-2s or W-3s or payroll processor reports, including quarterly and annual tax reports
- 941, or 943 or 944

Entities operational 2/15/2020 but not 2/15/2019. Options for filing include:

- Use 2020 payroll documentation
- Use average monthly payroll costs in January and February 2020, using the following guidelines:
  - Gross pay to employees for those 2 months, for US residents, up to \$16,667 per employee
  - Employer group insurance for the 2 months
  - Employer retirement contributions for the 2 months
  - Employer state and local taxes on employee compensation for the 2 months (primarily unemployment insurance)
- Calculate average monthly payroll costs (divide the 2 months by 2)
- Multiply the cost calculated above by 2.5
- Add any EIDL obtained before 4/3/2020 that will be refinanced, excluding first advance

*Required Documentation Includes:*

- If borrower chooses option #2, they must provide payroll records for January and February 2020
- 941 for Q 1 2020
- Documentation of any employer benefits from that period

Self-employed or partnership operational 2/15/2020 but not in operation between 2/15/2019 and 6/30, 2019. Entity has or will file 1040 schedule C or F, or form 1065 for 2020.

- There are 2 options:
  - Use payroll for all of 2020 instead of 2019
  - Use average monthly payroll costs in January and February 2020
- Using option #2, there are several steps required, including:
  - Complete a 1040 schedule C for January and February 2020. These must include all income and expenses, with the exception that on Schedule C line 13:
    - Include only 1/6<sup>th</sup> of the amount of any annual depreciation and section 179 expenses made in those 2 months
    - Include 1/6<sup>th</sup> of the amount of the 2020 depreciation attributable to investment made in prior years
  - Take net profit from January and February on Schedule C line 31.
    - If this amount is more than \$16,667 for the combined period, then set it to \$16,667
    - If this amount is -0- or less, then set at -0-
  - If you had employees, add employee payroll costs for January and February 2020 to net profit above. Include only US resident employees and \$16,667 per employee
  - Divide the total by 2 then multiply by 2.5
  - Add any EIDL obtained prior to 4/3/2020 to be refinanced, excluding EIDL first advance

*Required Documentation Includes:*

- A completed 1040 Schedule C
- Supply bank statements from business account for January and February 2020 to support net profit in Schedule C
- Employees require payroll records for those 2 months
- Form 941 for Q 1 2020
- Documentation of any retirement or group insurance contributions from employer

Schedule F filers must complete a Schedule F and insert gross income from Schedule F line 9 (no employees) or Schedule F lines 15, 22, and 23.

Partnerships complete a 1065 and replace net profit with net earnings from self-employment for each individual.

There are several other categories of expenses that can be included in payroll costs. In addition to group insurance costs, employee contributions from flexible spending arrangements, or other nontaxable benefits under cafeteria plans, parking, etc.