

Have Your Cake and Eat It Too!

How to Maximize Both PPP Loan Forgiveness and the Employee Retention Credit

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When the rules first came out, it was one or the other – Paycheck Protection Program (PPP) or Employee Retention Credit (ERC). Now, under the current provisions, you don't have to choose; you can participate in both, assuming you qualify. The goal of this article isn't to go into the nuances of how you qualify for either the PPP or the ERC. There have been countless articles already written about that, which can be accessed through our [Thought Leadership archives](#). Rather, the goal of this article is strategy. How do you allocate costs between the two programs to ensure both the forgiveness of a PPP loan, while also maximizing the ERC? The following are a few strategies to consider.

2020 versus 2021

Maximizing the ERC while ensuring full forgiveness of the PPP loan was much easier in 2020 as compared to 2021. This is because you effectively had nine months to accumulate the \$10,000 in wages per employee required to maximize the ERC. That nine-month window obviously depends on how you qualified for the ERC, but in many cases, governmental shutdown orders impacted hours of operations and presented capacity restrictions for a good part of 2020, thus allowing a company to qualify for multiple quarters.

In 2021, the ERC is determined quarter by quarter, so the challenge is to identify \$10,000 in wages per person, per quarter, to maximize the ERC. At the same time, you have to pay attention to the overlap with your PPP second draw covered period. Therefore, in 2020, where you had a relatively large window from which to identify \$10,000 in wages per person; in 2021, your window shrinks to three months or one quarter, because the 2021 ERC can be claimed each quarter.

Strategy for 2021

The overall goal is to ensure full forgiveness of your PPP loan, while also maximizing your ERC. The first step in this process is to determine for which periods you qualify for the ERC. If you qualify in the first quarter of 2021, there will be a stub period from the beginning of the year to the date you received your PPP second draw loan. The wages incurred during this period can all be allocated toward the ERC. In most cases, the entire second quarter of 2021 is going to be a direct overlap between the PPP and ERC. Then, the third quarter will have a similar split as the first quarter, with the beginning of the third quarter overlapping with your PPP covered period, and the end of your third quarter being available to apply toward the ERC without any PPP considerations.

Using a 24-week covered period for PPP forgiveness purposes will generally make sense, as it extends the window for incurring eligible wages to apply toward PPP forgiveness. Also, keep in mind is that you only need to incur a minimum of 60% of your eligible PPP costs on payroll related items; the remaining 40% can be comprised of rent, utilities, perishables, etc., preserving payroll related expenses for the ERC.

Other Considerations

Don't jeopardize PPP forgiveness for the ERC. Payroll costs applied to PPP forgiveness generate a dollar-for-dollar benefit, whereas payroll costs applied to the ERC generate only 70 cents of benefit on every payroll dollar. Also, forgiven PPP loans are not taxable, do not reduce expense deductions for income tax purposes, and generate tax basis for your company. The ERC, on the other hand, reduces the amount of expenses you can deduct on your tax return by the amount of your credit, so it effectively becomes taxable. Furthermore, the PPP funds are already in your hands. PPP funds are wired into your bank account on the first day of your covered period. The ERC can be somewhat elusive. It looks great on

paper, but the timing of actually receiving a refund check has been a bit of an enigma, as the IRS has been slow to process claims.

One way to accelerate the receipt of ERC funds is to claim the credit on a timely filed Form 941, as opposed to figuring out the credit after the fact and claiming it on an amended tax return. You'll only be able to do this if you know you qualify for the ERC before your Form 941 for the quarter is due. One way to know this is if you had a greater than 20% reduction in gross receipts in Q2 of 2021, as you will automatically qualify for the ERC in Q3. If you are in that scenario, you may want to contact your payroll company to see if they can claim the credit for you as subsequent payrolls are processed.

The key is to map out both PPP and ERC strategies simultaneously before committing any costs to either program. With proper planning, you can ensure that you will maximize the advantages of both programs. For example, you already know what your Q3 2021 gross receipts need to be to qualify for the ERC (no more than 80% of your Q3 2019 gross receipts). Managing your sales pipeline and the timing of revenue recognition could be the difference between qualifying for potentially millions of dollars in tax credits, versus looking in your rear view mirror regretting that you didn't plan properly.

Buyer Beware

Some payroll companies are offering to calculate the ERC for a very low fee. All payroll companies may not be doing it the same way, but the examples that we have seen are leaving a substantial amount of money on the table. Here's why: the payroll companies typically ask you for which periods you qualify for the ERC, as well as the date range of your PPP second draw covered period. Based on that information, they simply calculate the credit for the stub periods (the period before the PPP covered period starts and the period after the PPP covered period ends) and ignore excess wages during the PPP covered period which may be allocated toward the ERC. They also fail to consider using health benefits or any other strategies to minimize PPP payroll related costs (while still maximizing PPP forgiveness) as part of the ERC calculation.

It's not necessarily the payroll company's fault for not including these additional costs, but they simply don't have enough information to make that determination, and there is an obvious reason why they are offering to perform the calculation at such a reduced fee. They are simply using a black and white, simplistic formula that takes all of the strategy off the table and only claims the low hanging fruit. In the few cases that we have seen, the payroll company's ERC calculation equated to approximately 50% of the credit that the client was entitled to! At a maximum of \$7,000 of a credit per person, per quarter, that could result in leaving a substantial amount of money unclaimed.

Closing

This article may be a bit complex to those who don't live and breathe these strategies on a daily basis. We have processed countless PPP forgiveness applications, calculated numerous ERCs and have seen many very interesting situations presented before us. It really comes down to a relatively complicated mathematical equation. By customizing covered periods, allocating wages, identifying all possible eligible costs, and mastering the use of Microsoft Excel, your trusted PKFOD advisors will put you in the best position to optimize your financial outcome

Contact Us

If you have questions or require assistance, please reach out to your PKF O'Connor Davies client service team or email LoanForgiveness@pkfod.com.

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