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The CFO Advisor

Guidance for Small Business Success™

Another year has quickly passed us by, and OH, WHAT A YEAR!... and as we get ready to close out 2020, it's important to set ourselves up to get 2021 started on the right foot.

This issue of **"The CFO Advisor"** focuses on peace, health, and prosperity as we get ready to ring in the new year. You'll read about how to keep a safe and peaceful work environment, as well as ways to keep motivated and inspired in tough times. You'll even learn tips on how to make it through the holiday shopping season!

From all of us at D.L. Hulse Consulting, we don't only wish you happy reading, but we also wish you **MERRY CHRISTMAS!**

Until next month...

Dwight L. Hulse, CPA/CITP,CGMA

Merry Christmas

How The PPP Loan Affects Taxes

Your 2020 taxes are likely going to look a little different than they normally do. There have been a lot of new programs created to help small businesses, which means you're probably going to deal with situations that you've never seen before including forgiven loans, grants, and unemployment benefits.

The Paycheck Protection Program (PPP) is a lifeline for businesses who are currently struggling due to COVID-19. The PPP is a loan intended to provide cash flow help for eight weeks (extended to 24 weeks), backed by the SBA.

What makes the PPP even more enticing for business owners is the potential that the loan amount can be forgiven, as long as the money was spent on payroll, mortgage interest, utilities, and rent (with the majority spent on payroll).

But with this new program came a question about how the IRS will view the money. If you meet the criteria for getting the loan forgiven, will the government tax you on the free money you're receiving?

Not directly, but it's a little more complicated than that.

Will I be taxed for my forgiven PPP loan?

The CARES Act spells out that the forgiven loan amount won't be included in taxable income. That means you don't pay taxes on the money that you receive. The aim of this loan is to provide businesses with the money to keep running and continue paying employees, not to create a tax burden for businesses receiving the funds.

But, there's a catch. The IRS later released a notice clarifying how the forgiven loan amount would be treated when it comes to 2020 taxes:

"This notice clarifies that no deduction is allowed under the Internal Revenue Code (Code) for an expense that is otherwise deductible if the payment of the expense results in forgiveness of a covered loan pursuant to section 1106(b) of the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), Public Law 116-136, 134 Stat. 281, 286-93 (March 27, 2020) and the income associated with the forgiveness is excluded from gross income for purposes of the Code pursuant to section 1106(i) of the CARES Act."

Put simply: if the forgiven loan isn't included in a business' taxable income, the expenses paid for with the forgiven loan aren't able to be included as a tax deduction. That may sound like a small detail, but it can potentially have a big impact on your final tax bill at the end of the year.

On November 18, the IRS released guidance clarifying that if you reasonably believe your PPP loan will be forgiven — regardless of whether it's 2020 or later — any expenses you used your PPP loan to cover are not deductible.

What does this look like on your tax return? Normally if a business has payroll, rent, mortgage interest, or utility expenses, these are deductible from taxable income. That deduction lowers your taxable income. Without that deduction, you'd owe the government more in taxes.

And that's what is going to happen in this situation: you lose out on some potential tax deductions, so you may have to pay more when it comes time to file your taxes.

Things still could change though. While this is a frustrating update to the loan program, it may not be the final decision. Rules are still being written and plenty of people are unhappy that the IRS has taken a position that would negatively impact businesses that are struggling.

Double Check The Check

Following these tips when you receive a payment from the Federal or State government can save you more head-aches than you can imagine.

Tip: Double-check the dollar amount of your refund check before you cash it. Make sure it matches the amount on your tax return.

Tip: If you have a direct deposit of your refund, only deposit it into one account. This makes matching the dollar amount easier to do.

Tip: Never cash a check received from the IRS or State tax departments that you cannot tie back to a specific reason or tax filing.

The reason for caution:

• **Wrong amounts usually mean errors.** The error could be yours, or the error could be from the IRS. For example, if the IRS misapplies a quarterly payment or modifies your tax return, they often will send back an amount that does not tie to your filed tax return.

• **No explanation.** Often checks received from the government have little to no description to help you figure out what the check is for and why is has changed from the amount you expected.*

• **Owed money can create penalties and interest.** Once cashed, the door is open for a future IRS bill with interest and penalties. For example, a small businessman sent in his quarterly payroll filing. The IRS misapplied the funds, determined the account they applied the money to had no tax, and then sent a check back to the taxpayer. The taxpayer cashed the check. Two years later the business received an underpayment notice along with substantial interest and penalties. The service even applied liens on the taxpayer's bank account.

• **It may mean identity theft or missing forms.** A check with an unusual dollar amount could mean the IRS does not have the corresponding tax form on record. It could also mean your taxpayer account has been compromised.

Should you receive a payment that does not make sense to you, please review your tax return and call the IRS for assistance. An un-cashed check received in error can often be returned to avoid confusion and hassle when the IRS finally corrects the problem.

*__Note:__ Sometimes the memo line will include interest paid to you from the IRS. This interest will need to be reported on next year's tax return.

"So how do the 2021 numbers look?"

Look Beyond The Interest Rate Before You Refinance

When you're thinking of refinancing your home mortgage, simply comparing interest rates is not enough. Here are some other factors to consider before you refinance.

Compare apples to apples. Always request a good-faith estimate from any lender. This report should disclose all the fees and closing costs, such as points, credit report fees, inspection fees, private mortgage insurance, and appraisal fees. Use this information to evaluate competing loan proposals.

• **Calculate your break even period.** This is the length of time it takes you to recover the costs a lender typically charges to refinance your mortgage. To do this, divide your closing costs by your monthly savings (i.e. your current loan payment minus your new loan payment). If you plan on selling your home in the near future, refinancing may not save you money because it usually takes several years to recover your closing costs through a lower monthly payment.

• **Read the loan agreement.** Before you pay off your existing mortgage, check your loan for an early payment penalty clause. In addition, make sure you read and understand the terms of your new loan. For example, watch for restrictions against renting out your property without your lender's consent.

• **Evaluate the risks of debt consolidation.** When you refinance, it may be tempting to consolidate high-interest personal debts into a single lower-interest home loan. Securing a consolidation loan with your home may turn your interest into a tax deduction, but be aware of the risks as well. If you can't make the payments, you could lose your home.

Whether refinancing makes sense in your particular situation depends upon a number of factors. Call us if you would like a review of your situation. This extra step can help you select the loan that best fits your needs.

Are You In Need of a Trusted Business Advisor?

If you are not my client and would like to explore whether we might be a good fit, please contact me. As an experienced business advisor, I have worked not only in private and public industries but also across many functional areas and can help you implement best practice solutions to improve profits.

Do You Have A Tough Accounting / Finance Question You Want Answered?

I love hearing from my small business clients and friends who enjoy reading my monthly newsletter. I'm always looking to answer pressing questions you might have relating to small business.

If you have a question, tip or idea, please call me at 352-450-2880 or email me at dwight@dlhulseconsulting.com. Perhaps I'll feature you in a future issue!

Financial Basics: Calculate Your Net Worth

Whatever your financial goals in life—whether they include buying a new house, taking a trip to Europe, funding your children's college educations, having enough money for a comfortable retirement, or all of the above — you are more likely to reach your goals if you do some planning. The fact that you are reading this indicates your desire to plan and to take control of your financial life.

After you've set your financial goals, the next step is to determine your current net worth. Only when you know where you are today can you calculate how far you have to go to reach your financial goals in the future.

On a sheet of paper, list everything you own (i.e. your "assets") and everything you owe (i.e. your "liabilities"). Subtract the total liabilities from the total assets; the result is your current "net worth."

In doing this exercise, it's important to review the actual documents for the specific assets and liabilities and accurately record account numbers, identification, and dollar amounts. It's easy to forget details about assets and liabilities and to list misleading information.

After you've arrived at your current net worth, ask the following questions:

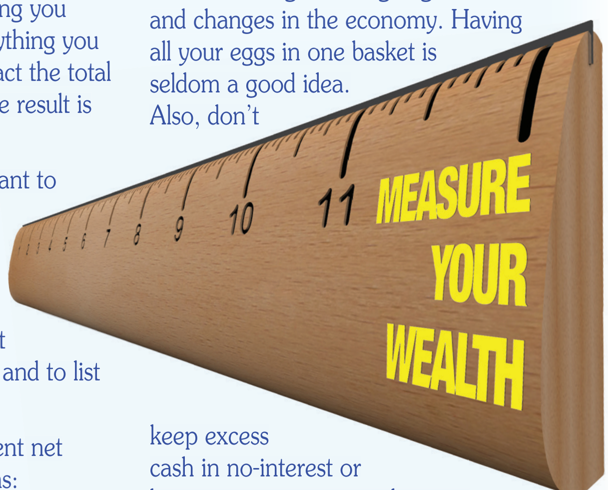
1. Has your net worth increased since you last did this listing? If it hasn't, you need to determine the reason and perhaps make some changes in your spending, saving, or other financial habits.

2. Does your net worth statement reflect a preference for personal assets such as an expensive home, cars, furs, and jewelry? Your balance sheet should show a concern for acquiring investment assets, not just personal assets that are far less likely to increase in value or produce income that will help you meet other financial goals.

3. Is your debt out of proportion? If your sheet shows excessive debt, especially for personal consumption, that's a signal to review your spending. Keeping debt under control is essential in good financial management.

4. Have you given enough thought to money needed for retirement? If your sheet shows total neglect for accumulating funds for retirement, you'll want to make some changes as soon as possible.

5. Are your assets diversified? Diversification is a good hedge against inflation and changes in the economy. Having all your eggs in one basket is seldom a good idea. Also, don't keep excess cash in no-interest or low-interest accounts unless you have an immediate need for the cash.



6. Where do you want to be three years, five years, and ten years from now, in terms of your net worth? You might determine this by doing projected net worth calculations for three years, five years, and ten years from now.

Conduct a net worth calculation like this every year in order to chart the progress you're making in increasing your net worth.

How The EIDL Advance Affects Taxes

The **Economic Injury Disaster Loan (EIDL)** is a loan option available through the SBA to help businesses struggling with financial hardship due to COVID-19. While it is a loan and doesn't have any special treatment when it comes to taxes, there is one thing that may affect your taxes: **the EIDL advance.**

The EIDL advance is technically a grant for small businesses of up to $10,000. Because it's a grant, it's not part of the loan that needs to be repaid. That means it's going to be treated differently than a loan on your financial statements and your tax return at the end of the year.

Unlike the PPP loan forgiveness, this grant will probably need to be included in taxable income. This isn't definitive because the IRS hasn't specifically said that this advance should be included in taxable income, but previously they've been pretty clear that *any forgiven SBA loan amounts need to be included in income.*

If you received an EIDL advance for the maximum amount of $10,000, that money will need to be added to your taxable income at the end of the year. But if it's added to your taxable income, you'll be able to deduct any expenses that you use to pay for this grant.

Quotes:

"Youth is when you're allowed to stay up late on New Year's Eve. Middle age is when you're forced to." — Bill Vaughn

"New Year's Day is every man's birthday." — Charles Lamb

"Cheers to a new year and another chance for us to get it right." — Oprah Winfrey

"I love those who can smile in trouble..." — Leonardo da Vinci

"These are the times that try men's souls." — Thomas Paine, The American Crisis

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See What's Inside...

Healthy Ways To Cope With Stress

Feeling emotional and nervous or having trouble sleeping and eating can all be normal reactions to stress. Here are some healthy ways you can deal with stress:

- **Take care of yourself.**
  - Eat healthy, well-balanced meals.
  - Exercise on a regular basis.
  - Get plenty of sleep.
  - Give yourself a break if you feel stressed out.
- **Talk to others.** Share your problems and how you are feeling and coping with a parent, friend, counselor, doctor, or pastor.
- **Avoid drugs and alcohol.** These may seem to help, but they can create additional problems and increase the stress you are already feeling.
- **Take a break.** If news events are causing your stress, take a break from listening or watching the news.
- **Recognize when you need more help.** If problems continue or you are thinking about suicide, talk to a psychologist, social worker, or professional counselor.

Should You Invest in Rental Real Estate?

If you want to make a profit by investing in rental real estate, you must be willing to commit more resources to this property than you would to an investment made at your bank, through a broker, or in a mutual fund.

Someone has to collect rents, find good tenants, and maintain the property. If you hire help to do these tasks, your profit shrinks.

Also, if you borrow money to buy the property, you have to pay the mortgage whether or not the property is rented. You should have emergency funds so that you will not lose the property to foreclosure if you lose your tenant.

If you decide to invest in rental property, you may need professional help to match your resources to property that will meet your goals. Some of the questions you should consider before you invest:

- **What can you afford?** Determine the highest price range you can sustain, given your present resources and the projected cash flow from the property.
- **Is the property fairly priced?** Get a list of comparable listings and recent sales from a real estate company. Make any purchase offer contingent on the results of structural and pest inspections. Check local records to verify that additions and major improvements were made in compliance with building codes.
- **Are there any restrictions on the property?** Rent control will lower the price that you can afford to pay for a property.
- **Who will be your tenants?** Evaluate the likelihood of nonpayers, transients, and untidy housekeepers — and adjust your price accordingly. If you are buying a condominium in a building populated with young people, you may find it difficult to interest a retired couple (if that's your market) in living in the unit.

Investing in rental property can be very profitable, but you should be fully informed before you invest, or you could end up with more work and less return than you anticipated.

Please ask for help if you are considering this investment strategy.