



HOW TO ACCOUNT FOR EIDL ADVANCE AND PPP LOANS

Accounting Strategies for EIDL Advance and PPP Loans

As of May 6, 2020

Congratulations! You just checked your bank account and noticed that both your EIDL advance (grant) for \$10,000 and PPP loan for \$100,000 were funded today. The hard part is over! Or is it? Today is also the end of the month, so you need to reconcile your bank account and post the entries for this activity. But what are the journal entries to record these transactions? Here are our recommended steps and journal entries to ensure the proper reporting treatment for these loans, based on the issuance of the loan, forgiveness of the loan, and recording of expenses related to the loan. Below are some discussion and suggested entries for GAAP basis financial statements. Income Tax basis financial statements may have different reporting.

Issuance of the Loan – Receipt of Cash

As the use of the PPP loan proceeds is important for the determination of forgiveness as well as deductibility for income tax purposes (discussed later), we recommend maintaining separate bank account specifically for the PPP loan and for added security the EIDL advance, separately if administratively feasible. Remember that you cannot use the funds from the EIDL advance for the same expenses that you wish to seek forgiveness for on the PPP Loan. Therefore, it is important, at a minimum, to track the activity of the PPP bank account separately from your operating funds in order to verify the forgiveness portion of the PPP loan. The bank transactions should match the use of the PPP loan and should be routinely documented.

The accounting entry for the receipt of the \$10,000 EIDL advance is:

Cash \$10,000	
	Other Income – EIDL Grant \$10,000

As the EIDL advance is considered a grant, and not subject to repayment, the forgiveness is automatic and thus is considered other income when received. As Other Income – EIDL Grant is not related to operations, it should be shown below operating income (loss), as part of other income and not netted against related expense accounts.

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Since this represents a contingency, the receipt of funds should be initially recorded as a liability. Once the contingency is resolved (i.e. the amount which will be forgiven is known), this amount can be adjusted accordingly. The entry, upon receipt of the PPP funds is:

Cash \$100,000

Current PPP Loan \$100,000

Forgiveness of the PPP Loan

The PPP loan forgiveness is treated as extinguishments of debt under ASC 405-20 once the SBA has approved the forgiveness as this is when the loan holder is legally released from being the prime obligor under the liability (ASC 405-20-40-1).

For example, if \$80,000 is approved for forgiveness by the SBA, the loan would be reclassified to income at that time:

Current PPP Loan \$80,000

Other income – Loan Forgiveness \$80,000

As the loan forgiveness income is not related to operations, it should be shown separate from income from operations, as part of other income and not shown netted against related expense accounts. This treatment is in accordance with GAAP as ASC 470-50-40-2 states debt extinguishment “shall be recognized currently in the income of the period of extinguishment as losses or gains and identified as a separate item.” The tax treatment for the PPP loan forgiveness is non-taxable and would be reflected on schedule M-1 or schedule M-3 as permanent non-taxable income.

Additionally, at this time the unforgiven portion of the loan would be converted into a 2-year loan. This would be reclassified from a current loan to a long-term loan.

Any payments towards the amount which is not forgiven and subject to repayment would simply be treated as any other debt repayment, based on the repayment terms, as follows:

Long term PPP Loan \$20,000

Cash \$20,000

Expense Tracking:

As mentioned above, it is important to track the expenses incurred under the PPP loan for determination of the amount to be forgiven. Furthermore, the expenses associated with the portion of the loan which is forgiven are non-deductible on your income tax return according to IRS Notice 2020-32. Therefore, we recommend recording these expenses as normal (i.e. payroll, rent, etc.), but again maintaining a tracking through the bank account or separate spreadsheet, as needed:

Incurrence of expense-

Expense accounts \$15,000



When the amount of the loan forgiven can be reclassified to a separate GL account, as they are non-deductible: However, consideration should be given to year over year comparisons and other issues before setting up these new accounts. If such reporting is used, the entry is:

Non-deductible PPP exp.	\$5,000
Expense accounts	\$5,000

Don't forget that the PPP loan accrues interest at 1%, which also may be forgiven. This will need to be accrued monthly for GAAP basis financial statements and included in the loan forgiveness piece upon closing of the loan. If your organization reports its financial statements on a cash basis, then you would record the interest when paid.

Since the tax treatment as of the date of this blog (5.6.2020) for the associated forgiven loan proceed expenses are non-deductible, the expenses would be reflected on schedule M-1 or schedule M-3 as permanent non-deductible expenses.

How to Handle Interim Time Periods:

One common question asked is how to treat these expenses if they are incurred in one time period but forgiven in another time period. For book purposes, these expenses will be recorded as usual. However, when calculating taxable income, consideration should be made of IRS Notice 2020-32, which states these expenses will be considered non-deductible. For Companies preparing tax provisions, this can be confusing. However, ASC 740-10-05-6 "provides guidance for recognizing and measuring tax positions taken or expected to be taken in a tax return that directly or indirectly affect amounts reported in financial statements." Based on this, management should assess the amount of the loan they think will be forgiven. If they expect all or a portion of the loan to be forgiven, the expenses associated with this amount of the loan would be treated as non-deductible on the tax provision in the period incurred regardless of when the actual forgiveness is approved. Following the recommendation above, these expenses would then be reclassified to a non-deductible account, which would be reported on the income tax return as an M-1 item and as a permanent item in the company's tax provision.

Our team is working around the clock to ensure we stay up to date on the latest guidance and information to assist you and your business during this unique time. For further assistance, please do not hesitate to reach out to your Windham Brannon advisor or email us at covid19advisory@windhambrannon.com.





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