



PPP Update: Audits, Loan Forgiveness, and Changes In the Flexibility Act

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Forgiveness Topics

- PPP Program and Audits
- Loan Forgiveness Refresher
- Changes Proposed by Flexibility Act
- Determining Forgiveness Amounts
- The Forgiveness Application
- Necessary Documentation

PPP Program

- Designed to provide potentially forgivable loans to companies to meet payroll costs and pay other qualifying expenses
- Still approximately \$150 billion available to fund PPP loans
- Program rules are quickly changing
 - SBA FAQ and interim final rules
 - Payroll Protection Program Flexibility Act passed by House of Representatives on May 28; awaiting Senate action

PPP Audits

- The “necessity requirement”
 - “Current economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant”
- Safe Harbor - Loans under \$2 million presumed to comply with necessity requirement but SBA can still audit
- Loans over \$2 million will be subject to review

Loan Forgiveness Refresher

- PPP Loans are forgivable to the extent
 - Used for eligible purposes
 - During the “Covered Period”
 - In certain proportions of payroll to non-payroll costs
- The amount forgiven may be reduced if
 - Borrower has a reduced workforce during the covered period compared to an earlier designated period
 - Borrower has reduced, by more than 25%, the compensation of any employee who make less than \$100,000 annually

Covered Period

- The period during which the loan can be spent on permitted expenditures to qualify for forgiveness
- Currently: 8 weeks following loan funding date
- [Flexibility Act](#) would expand the Covered Period to 24 weeks after loan funding or Dec. 31, whichever comes first

Alternative Covered Period

- Available only to borrowers with a bi-weekly (or more frequent) payroll cycle
- Borrower may elect to begin Covered Period on first day of first payroll cycle after loan received
 - Continues for eight weeks thereafter

Permitted Expenditures

- Forgiveness available to the extent of the following **costs incurred** and **payments made** during the Covered Period:
 - Payroll costs
 - Interest on mortgages created before 2/15/20
 - Rent on leases in force before 2/15/20
 - Utility payments for service that began prior to 2/15/20

What Are Payroll Costs?

- Compensation (salary, wage, commission or cash tips)
 - Only up to \$100,000 annual rate
 - Regulations allow hazard pay, bonuses, pay to furloughed workers (subject to \$100,000 limitation)
- Payment for vacation, parental, medical, or sick leave
- Severance
- Health care benefits, including insurance premiums
- State or local tax assessed on employee comp

Paid vs. Incurred

- Payments **made** during the Covered Period may be included
 - Unclear whether prepayments are allowed, though this may become unimportant if Covered Period extended to 24 weeks
- Amounts **incurred** during the Covered Period may be included if paid by the next regularly scheduled date
 - Compensation earned during the Covered Period paid on next payroll date
 - Rent or utilities incurred during the Covered Period paid on next due date

When are Payroll costs Paid or Incurred?

- Payroll costs paid
 - On the day that paychecks are distributed or the borrower originates an ACH credit transaction
- Payroll costs incurred
 - On day employee earns pay (work day)
 - For employees not working but on payroll, incurred on borrower schedule (typically when work would have occurred)

75% Rule

- Payroll costs must be at least 75% of amount forgiven
- Non-payroll costs cannot be more than 25% of amount forgiven
- **Flexibility Act** would change these proportions to 60/40
 - But the language suggests no forgiveness at all is permitted unless at least 60% is spent on payroll costs

Limits on Forgiveness – Workforce Reduction

- Amount forgiven will be reduced if borrower reduces its workforce during the Covered Period
 - Pro rata reduction
 - Based on avg. monthly FTEs during the Covered Period compared to average monthly FTEs for one of two earlier periods chosen by borrower:
 - Feb. 15 to June 30, 2019
 - Jan. 1 to Feb. 29, 2020

FTE Definition

- “Full-time equivalent employee means an employee who works 40 hours or more, on average, each week.”
- Divide the average number of hours paid for each employee per week by 40, capping this quotient at 1.0.
- For employees who were paid for less than 40 hours per week, borrowers may choose to calculate the full-time equivalency in one of two ways.
 - Actual percentages vs. 40 hr. week
 - Use 0.5 for any less-than-full-time employee
 - Must use consistent method for all periods

Workforce Reduction - Exceptions

- SBA guidance provides exceptions for
 - Laid-off employees whom borrower offers to rehire for same salary and hours, or restore a reduction in hours
 - Employees who are fired for cause, resign or request reduction in hours

Workforce Reduction - Exceptions

- **Flexibility Act** provides exception if borrower can demonstrate:
 - inability to rehire employees who were employed February 15, 2020 and inability to hire similarly qualified employees for unfilled positions on or before December 31, 2020.
 - inability to return to same level of business activity as existed on February 15, 2020 due to compliance with health guidelines

Limits on Forgiveness – Compensation Reductions


- Amount forgiven will be reduced to the extent borrower reduces salary or wages paid to an employee by more than 25% during the Covered Period compared to previous quarter
 - Only applies to reductions for employees not paid at rate of more than \$100,000 annually for any 2019 pay period
 - Dollar for dollar reduction, calculated for each individual employee (not in the aggregate)
 - SBA guidance looks at rates of pay for the two periods

Exception to Reductions

- Forgiveness will not be reduced:
 - In the case of staff reductions, if the employer eliminates the reduction in the number of FTE's that occurred between Feb. 15 and April 26 by June 30
 - [Flexibility Act](#) would extend to Dec. 31
 - In the case of compensation reductions made between Feb. 15 and April 26, if the employer eliminates the reduction in salary or wages by June 30
 - [Flexibility Act](#) would extend to Dec. 31
- SBA: compensation reduction applies only to portion of decline not attributable to the FTE reduction.
 - Prevents double penalty

Forgiveness Application

- Made available on May 22
- Will have to be revised if Flexibility Act becomes law
- Consists of
 - Instructions
 - Loan Forgiveness Calculation Form
 - Schedule A
 - Schedule A Worksheet

 Paycheck Protection Program
Loan Forgiveness Application
OMB Control Number 3245-0407
Expiration Date: 10/31/2020

PPP Loan Forgiveness Calculation Form

Business Legal Name ("Borrower")		DBA or Trademarks, if applicable	
Business Address	Business YIN (EIN, SSN)	() -	Business Phone
	Primary Contact		E-mail Address

SBA PPP Loan Number: _____ Lender PPP Loan Number: _____
PPP Loan Amount: _____ PPP Loan Disbursement Date: _____
Employees at Time of Loan Application: _____
Employees at Time of Forgiveness Application: _____
EIDL Advance Amount: _____ EIDL Application Number: _____
Payroll Schedule: The frequency with which payroll is paid to employees is:
 Weekly Biweekly (every other week) Twice a month Monthly Other _____
Covered Period: _____ to _____
Alternative Payroll Covered Period, if applicable: _____ to _____
If Borrower (together with affiliates, if applicable) received PPP loans in excess of \$2 million, check here:

Forgiveness Amount Calculation:

Payroll and Nonpayroll Costs
Line 1. Payroll Costs (enter the amount from PPP Schedule A, line 10): _____
Line 2. Business Mortgage Interest Payments: _____
Line 3. Business Rent or Lease Payments: _____
Line 4. Business Utility Payments: _____

Adjustments for Full-Time Equivalency (FTE) and Salary/Hourly Wage Reductions
Line 5. Total Salary/Hourly Wage Reduction (enter the amount from PPP Schedule A, line 3): _____
Line 6. Add the amounts on lines 1, 2, 3, and 4, then subtract the amount entered in line 5: _____
Line 7. FTE Reduction Quotient (enter the number from PPP Schedule A, line 13): _____

Potential Forgiveness Amount
Line 8. Modified Total (multiply line 6 by line 7): _____
Line 9. PPP Loan Amount: _____
Line 10. Payroll Cost 75% Requirement (divide line 1 by 0.75): _____

Forgiveness Amount
Line 11. Forgiveness Amount (enter the smallest of lines 8, 9, and 10): _____

Basic Structure of Application

- List payroll and nonpayroll costs
- List adjustments for salary/wage reduction and workforce reduction
- Schedule A and related worksheet
 - Used for determining payroll costs and calculating relevant deductions for workforce reductions and salary reductions
 - Requires separate tables listing employee names and compensation
 - Actual 8-week comp for employees under \$100k annual rate.
 - \$15,385 for employees over

Certifications Required

- Funds were used for permitted purposes
- Forgiveness amount properly calculated
- Borrower has verified the payments
- Borrower has submitted required documents to lender
- Information provided is true and correct
- Tax documents submitted to lender match IRS filings

Necessary Documentation

- Three categories of documents
 - Documents that must be submitted with forgiveness application
 - Documentation that borrowers must maintain and provide on request
 - Documentation borrowers may voluntarily submit with forgiveness application
- Must retain documents for six years after forgiveness or repayment, and permit access to SBA and Inspector General

Tax Consequence of Forgiveness

- Forgiven amounts do NOT constitute cancellation of debt income
 - However, the IRS has stated that, in accordance with existing principles, expenses paid with forgiven amounts will NOT be deductible
- Payroll tax deferral eligibility ends when forgiveness granted
 - **Flexibility Act** would eliminate this restriction, so borrowers remain eligible

What if the Loan is NOT Forgiven?

- Portion not forgiven continues as a loan at 1% interest
- CARES Act said term would be up to ten years.
 - SBA determined that the term will be 2 years
- [Flexibility Act](#) provides that minimum term for *new* loans is 5 years
 - Borrowers and lenders may modify existing loan terms to conform
- Principal and interest will be deferred for a total of 6 months after disbursement of the loan.
 - [Flexibility Act](#) changes this; deferral lasts until forgiveness amount is remitted by SBA to lender

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