

PPP LOAN FORGIVENESS

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May 7, 2020

TODAY'S PRESENTERS



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AGENDA

- ▶ PPP Overview and Where we are Today
- ▶ Loan Forgiveness
 - Payroll Costs
 - Forgivable Costs
 - Employment Conditions for Forgiveness
 - FAQs and Examples
- ▶ Accounting and Tax Considerations
- ▶ How Kruggel Lawton Can Help

PAYCHECK PROTECTION PROGRAM RECAP

- ▶ As of 5/1/2020 – Almost 3.9M loans for a total of \$519B (avg ~\$133,000)
- ▶ Over 5,400 lenders participated
 - ~41% of loans were less than 50,000
 - ~80% of all loans were for less than \$150,000
 - only ~2% were greater than \$1M (About \$200b or 38% of total lent to date)
- ▶ All this was done in a matter of weeks – lack of advance planning and guidance
- ▶ So far, eight Interim Final Rules and over 40 FAQs issued to-date by the U.S. Treasury

PPP SCRUTINY INCREASING

- ▶ 4/29 – FAQ 31 and 37 stating “current economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant.” The return period was just extended to May 14, with more guidance on how this will be assessed expected.
- ▶ A number of large recipients, mostly public companies, have or will return PPP loans.
- ▶ Challenges and burden on borrowers (not lenders) for supporting original certification, use of proceeds, and loan forgiveness.
- ▶ This is a changing landscape and we expect it to continue to change.

HOW CAN PPP LOANS BE USED?

- ▶ Payroll costs (as defined in the Act and in 2.f.);
 - Gross wages
 - Employer paid health (health, dental, and vision) and retirement benefits
 - Employer paid state and local taxes
- ▶ Mortgage interest payments (but not mortgage prepayments or principal payments)*;
- ▶ Rent payments*;
- ▶ Utility payments (include electric, gas, water, internet, telephone, and transportation utilities (fuel costs)*; and/or
- ▶ Interest payments on any other debt obligations that were incurred before February 15, 2020

USE OF PPP LOANS FOR EIDL

- ▶ The PPP loan can be used to refinance an SBA EIDL loan made between January 31, 2020 and April 3, 2020.
 - If you received an SBA EIDL loan from January 31, 2020, through April 3, 2020, you can apply for a PPP loan.
 - If your EIDL loan was not used for payroll costs, it does not affect your eligibility for a PPP loan.
 - If your EIDL loan was used for payroll costs, your PPP loan must be used to refinance your EIDL loan.
 - Proceeds from any advance up to \$10,000 on the EIDL loan will be deducted from the loan forgiveness amount on the PPP loan.

FAQS & PAYROLL COSTS



GENERAL FAQs

▶ Can I get a partial forgiveness?

- Yes, based on the amount of funds used for “qualified costs” over the 8 week period and subject to the limiting factors (75% payroll, headcount and pay reductions).

▶ What happens to the rest of the amount?

- It can either be repaid (no prepayment penalty), or it becomes a term loan (still subject to use requirements) repayable within 2 years after a 6 month deferral period at 1%.

▶ Can I get multiple disbursements? When does the “clock” start?

- Limited to one disbursement for the full amount and the 8 week covered period begins on disbursement.

WHAT ARE “PAYROLL COSTS”?

- ▶ As of today, “payroll costs” eligible for forgiveness include:
 - Gross wages (limited to per period amount maximum of \$15,385 for 8 weeks - weekly \$1,923, bi-weekly \$3,846, etc., per employee)
 - Employer paid health (health, dental, and vision) and retirement benefits
 - Employer paid state and local taxes
 - This total must be a minimum of 75% of the used and “forgivable” amount of the loan
 - All expense must be “incurred and paid” (cash basis for now) within the 8 week window (beginning on loan funding) to be included in the calculation

*****Potential to change based on additional guidance*****

SAMPLE PAYROLL COST TEMPLATE

Expenses can be incurred and paid starting: 4/17/2020
 Last date that expense must be incurred and paid: 6/12/2020

Week Number	Partial	1	2	3	4	5	6	7	Partial	
Week Beginning	4/17/2020	4/19/2020	4/26/2020	5/3/2020	5/10/2020	5/17/2020	5/24/2020	5/31/2020	6/7/2020	Total
Gross salary, wage, commission, bonus, etc.		-	-	-	-	-	-	-	-	-
Cash tips or equivalent										-
Partnerships - partner draws										-
Separation payments										-
Group health benefits										-
State or local tax assessed on compensation of employee										-
Employer portion of retirement plan contributions										-
Subtotal	-	-	-	-	-	-	-	-	-	-
Adjustment for Families First Coronavirus Response Act wages										-
Adjustment for wages in excess of \$100,000										-

— OTHER FORGIVABLE COSTS —



OTHER POTENTIALLY “FORGIVABLE COSTS”

- ▶ **Rent Expense** – Based off a signed lease agreement in effect prior to February 15, 2020.
- ▶ **Mortgage Interest** – Interest on mortgage obligations and loans secured by any business personal property are qualified expenses as long as these loans were incurred before February 15, 2020.
- ▶ **Utility Payments** – Include electric, gas, water, internet, telephone, and transportation utilities (fuel costs) in service as of February 15, 2020.

FAQS – FORGIVABLE COSTS

- ▶ **Can I prepay/prefund retirement, healthcare, etc?**
 - No prepayments are allowed, expenses must be incurred and paid within the 8 week period to qualify for forgiveness.
- ▶ **Can I pay bonuses, etc?**
 - The guidance states that they desire to “prevent windfalls that Congress did not intend.” So, as long as these have business purpose (retention, hazard, etc.) and are subject to the weekly maximum, they should be includable.
- ▶ **How does the \$100k work again?**
 - For forgiveness, the \$100k is pro-rata over the 8 weeks, capped at per pay period amount and max of \$15,385 for 8 weeks.
- ▶ **Do employees over \$100k count for forgiveness?**
 - Yes, up to the limit above over the 8 weeks
- ▶ **I am self-employed, can I include health insurance and retirement?**
 - According to the IFR these appear to be excluded from the forgiveness eligibility.

HOW DO WE THINK “FORGIVENESS” IS GOING TO WORK?

- ▶ Amount forgiven cannot exceed principal amount of the loan, need to create pool of eligible expense dollars or a cost bucket for the “covered period” (8 weeks beginning on loan funding)
- ▶ Maximum forgivable amount will be equal to costs incurred and payments made (using cash basis until further clarified, this may change) during covered period
- ▶ “Payroll costs” (as previously defined, must be a minimum of 75%)
- ▶ “Other Forgivable Costs” - Interest on mortgages (both real and personal property), Rent, Utilities in place prior to 2/15/2020

***** No prepayments of any type allowed as of today.
May require adjustment and planning*****

FORGIVENESS CONDITIONS & REMEDIATION

► **Conditions**

- Will be reduced for employee wage cuts or headcount reductions based on formulas in the guidance (more to come).

► **Remediation**

- Relief is available for employers who rehire employees or reinstate wages prior to June 30, 2020.

EMPLOYMENT CONDITIONS FOR FORGIVENESS



RETAIN WORKFORCE AND MAINTAIN PAY

- ▶ Full-time equivalent employee (“FTEE”)
 - Using definition under Affordable Care Act of 30 hours
- ▶ Sets a baseline – at the company’s option, either:
 - Average FTEES 2/15/2019 to 6/30/2019 -OR-
 - Average FTEES 1/1/2020 to 2/29/2020
- ▶ Compares the baseline to the average FTEEs during the 8 week period to create a percent of FTEEs retained.
- ▶ Can be “cured” by rehiring 100% of workforce by June 30, 2020 – Not sure exactly how this will work with current guidance.

RETAIN WORKFORCE AND MAINTAIN PAY (CONT'D)

- ▶ Not the same employees, simply an FTEE count – recent FAQ attempts to clarify
 - Must document if same employee declines job
 - Further reduction for any “individual” whose pay has been reduced by more than 25%
 - Does not include employees who make more than \$100,000 on an annualized basis
 - Can be mitigated by putting salaries back to pre-reduction levels by June 30, 2020
- ▶ Maintain Rate for Certain Employees
 - For employees that did not receive, during any single pay period during 2019, wage or salary at an annualized rate of pay > \$100k
 - i.e. Annualized Rate 100k, maximum reduction to 75k rate, to avoid additional excludable amounts

*****We expect clarification on this guidance as it is critical to managing the PPP forgiveness*****

EXAMPLE #1

Scenario #1 (Simple) - Ideal Scenario

Loan Amount:	\$ 400,000		Maximum Forgiveness	\$ 400,000
Disbursement Date:	4/20/2020			
Incurred and Paid in 8 weeks after disbursement				
Payroll Costs	\$ 350,000	88% > 75%	% Spent on Payroll	\$ 350,000 =350000*1
Rent	\$ 37,500	9%	Other Costs	\$50,000 =400000-350000
Utilities	\$ 12,500	3%	Amount Eligible for Forgiveness	<u>\$ 400,000</u>
Total	<u>\$ 400,000</u>			
			Payroll Reductions	0
Avg FTEE - 2/15/2019 - 6/30/2019	80		Workforce Retention	101%
Avg FTEE - 1/1/2020 - 2/29/2020	90			
Avg FTEE - 8 weeks after the loan	81		Debt Forgiveness	\$ 400,000
No salary reductions			Loan Amount	\$ -
			PPP Expense Cash Flow	\$ -

EXAMPLE #2

Scenario #2				
Loan Amount:	\$	1,000,000	Maximum Forgiveness	\$ 1,000,000
Disbursement Date:		4/20/2020		
Incurred and Paid in 8 weeks after disbursement				
Payroll Costs	\$	175,000	48% <75%	% Spent on Payroll
Rent	\$	50,000	14%	Other Costs
Utilities	\$	37,500	10%	Amount Eligible for Forgiveness
Interest on debts	\$	100,000	28%	
Total	\$	<u>362,500</u>		
Avg FTEE - 2/15/2019 - 6/30/2019			Payroll Reductions	0
Avg FTEE - 1/1/2020 - 2/29/2020			Workforce Retention	33%
Avg FTEE - 8 weeks after the loan			Debt Forgiveness	\$ 76,667
No salary reductions			Loan Amount	\$ 923,333
			PPP Expense Cash Flow	\$ (285,833)

EXAMPLE #2 ADDITIONAL HEADCOUNT

Scenario #2 Headcount partially restored

Loan Amount: \$ 1,000,000
 Disbursement Date: 4/20/2020

Maximum Forgiveness \$ 1,000,000

Incurred and Paid in 8 weeks after disbursement

Payroll Costs	\$ 175,000	48% <75%	% Spent on Payroll	\$ 145,250 =175000*0.83
Rent	\$ 50,000	14%	Other Costs	\$ 48,417 =(145250/.75)*.25
Utilities	\$ 37,500	10%	Amount Eligible for Forgiveness	<u>\$ 193,667</u>
Interest on debts	\$ 100,000	28%		
Total	<u>\$ 362,500</u>			

Payroll Reductions 0

Workforce Retention 83%

Avg FTEE - 2/15/2019 - 6/30/2019 150

Avg FTEE - 1/1/2020 - 2/29/2020 175

Avg FTEE - 8 weeks after the loan 50

No salary reductions

Headcount Restored by 6/30/2020 125

Debt Forgiveness \$ 193,667

Loan Amount \$ 806,333

PPP Expense Cash Flow \$ (168,833)

EXAMPLE #3 SELF-EMPLOYED

- ▶ Based on current guidance (IFR 4.14.20), we believe that the maximum amount of “forgiveness” for a Schedule C filer will be limited to the following:
 - 2019 Schedule C income * 8/52 (maximum of \$15,385 = (\$100,000 * 8/52))
 - An additional 25% of the amount above may be used for separate premises rent, utilities or mortgage interest (up to total of 25% of the above, maximum of \$5,128) – must be deductible on Schedule C and in place as of February 15, 2020
 - Maximum forgivable amount of \$20,513 for self-employed individual
 - Self-employed retirement and health care is excluded from forgiveness
- ▶ If you have employees, they would be included in addition as previously discussed.
- ▶ Guidance states this will be based upon 2019 Schedule C amounts for forgiveness, pending additional clarification on what additional documentation is required.

FAQS - HEADCOUNT

▶ **What if my 8 week covered period ends before 6/30/2020?**

- The CARES Act guidance states that you have until 6/30/2020 to cure the reduction in headcount for purposes of the %, we expect further guidance.

▶ **How do you calculate FTEE for headcount?**

- The best guidance for this is based on the Affordable Care Act. Anyone who works on average more than 30 hours a weeks counts as one FTEE. For part time employees, you add up all part time hours and divide by 30 to get FTEE. Most payroll software has this report previously built.

FAQS – HEADCOUNT/REHIRES

► What about rehires?

- Recently issued Treasury FAQ: “Will a borrower’s PPP loan forgiveness amount (pursuant to section 1106 of the CARES Act and SBA’s implementing rules and guidance) be reduced if the borrower laid off an employee, offered to rehire the same employee, but the employee declined the offer?”
- Answer: No. As an exercise of the Administrator’s and the Secretary’s authority under Section 1106(d)(6) of the CARES Act to prescribe regulations granting de minimis exemptions from the Act’s limits on loan forgiveness, SBA and Treasury intend to issue an interim final rule excluding laid-off employees whom the borrower offered to rehire (for the same salary/wages and same number of hours) from the CARES Act’s loan forgiveness reduction calculation. The interim final rule will specify that, to qualify for this exception, the borrower must have made a good faith, written offer of rehire, and the employee’s rejection of that offer must be documented by the borrower. Employees and employers should be aware that employees who reject offers of re-employment may forfeit eligibility for continued unemployment compensation.

— OTHER CONSIDERATIONS —



ACCOUNTING

► Balance Sheet

- Upon receipt of funds, record amount received as debt on the balance sheet. As it stands now, this is a 24-month note with no stated (or vague) repayment terms, so classifying as long term debt should suffice.

► Recording Interest

- Per GAAP standards, while the loans provide for a six-month deferral of interest and principal payments, interest should be accrued for on a monthly basis. It is possible that the interest will be forgiven, but until confirmed, it should be recorded.

► Derecognition

- As it relates to the PPP, borrowers must formally apply for loan forgiveness, including providing documentation to verify the existence and accuracy of the qualified expenses. Therefore, the PPP obligation should be derecognized only when the debt is formally forgiven.

ACCOUNTING

► Earnings and Income

- While the PPP loan provides for forgiveness, the related qualified expenses should continue to be accounted for in earnings. Payroll, rent, utilities and mortgage interest are costs that should be shown in the income statement as usual, not as reductions of the PPP, during the forgivable measurement period.

► Gains and Losses

- The gain that results from forgiveness will be measured based on the net carrying value of the PPP loan, which should include accrued interest (if forgiven). Within the income statement, this gain is presented as a separate line item. Given that current standards do not specify where in the income statement debt extinguishment gains and losses should be presented, there are varying opinions in practice. Clarifying guidance is expected to be forthcoming.

TAX

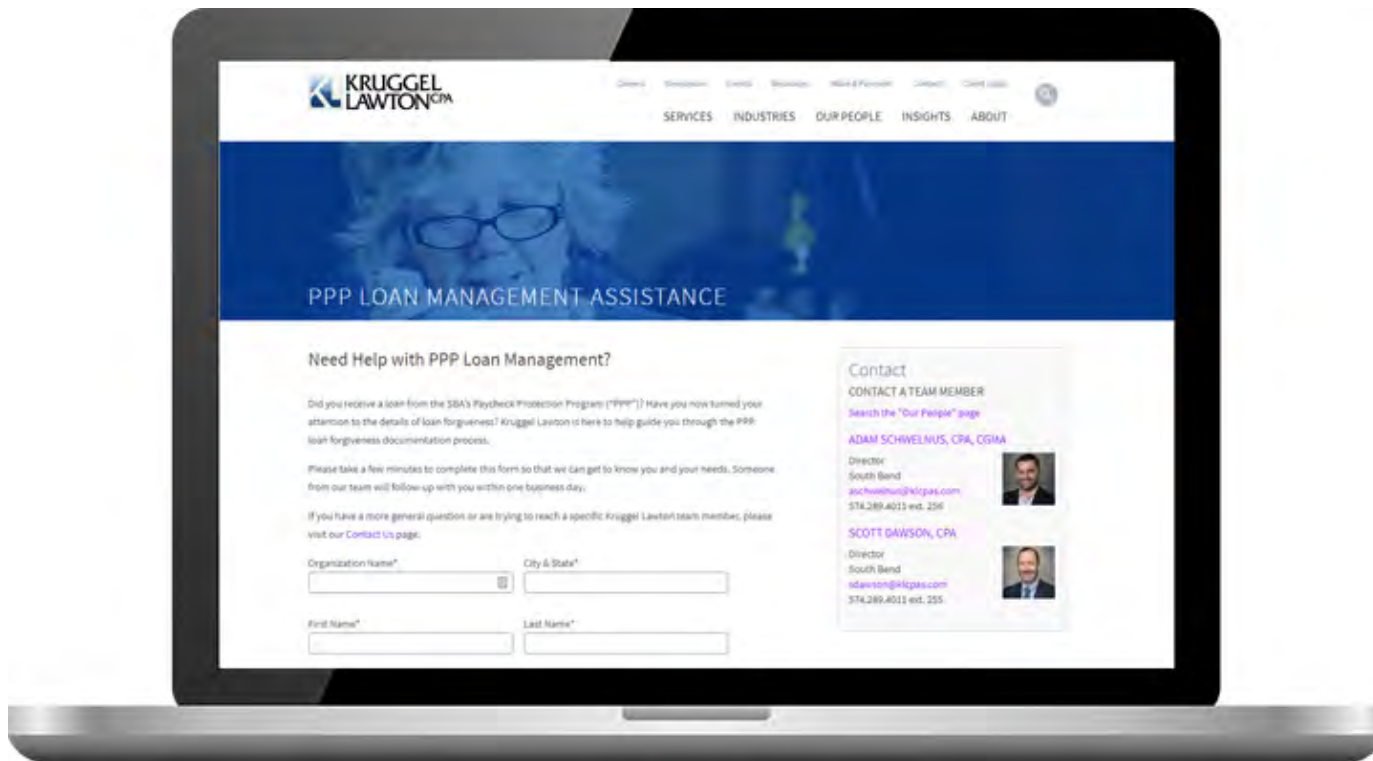
- ▶ Originally advertised as ‘non-taxable’ income. Led many to believe there could be potential for double tax benefit – deduction of qualified expenses, AND PPP from SBA to cover those qualified expenses that would ultimately be forgiven and not included in taxable income.
 - On April 30, the IRS issued notice 2020-32 that sought to clarify this interpretation and in summary “does not allow for business expense deductions for those qualified expenses that were considered qualified expenses and forgiven as a part of the PPP forgiveness process.”

*****Consult your tax advisor for further guidance on this topic and interpretation.*****

NEXT STEPS – PPP LOAN MANAGEMENT



www.klcpas.com/ppp-loan-management-assistance/





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Thank You!