

Navigating Paycheck Protection Program Loan Forgiveness Webinar



Thank you for attending our August 5, 2020 webinar on Navigating Paycheck Protection Program Loan Forgiveness. We were pleased with the level of audience engagement and the number of questions we received. Since we did not have time to address all of your questions on the webinar, we have compiled your questions and answered them below. We are unable to address detailed, borrower-specific questions in this format. We encourage borrowers with such questions to seek advice from counsel or financial advisors. Please contact us with questions that arise during the forgiveness process.

Documentation

What form is used to show that an employee declined employment? Is a letter from an employee saying that she wanted to work part-time evidence of this, so there is no penalty for her working less hours?

Answer: There is no specific form used to show that a former employee declined re-employment or that an employee requested a reduction in hours. The Application Instructions for SBA Form 3508 say that the borrower must retain documentation related to employees' compensation and FTE safe harbors for six years after the loan is forgiven or paid in full. This documentation must include: "Documentation regarding any employee job offers and refusals, refusals to accept restoration of reductions in hours, firings for cause, voluntary resignations, written requests by any employee for reductions in work schedule, and any inability to hire similarly qualified employees for unfilled positions on or before December 31, 2020" (Instructions, page 6). A letter or email from an employee requesting a reduction in hours is documentation of her request. Such a letter should be retained for six years. Any FTE reductions based on employees voluntarily requesting reductions in hours do not reduce the borrower's loan forgiveness.

Cash Compensation – Payroll Costs

Are employer-paid health insurance premiums for family members considered payroll costs eligible for forgiveness?

Answer: Yes, health insurance premiums that cover family members are eligible for loan forgiveness.

Are employer contributions to health savings accounts considered forgivable payroll costs, similar to health insurance premiums?

Answer: Yes, employer contributions to health savings accounts are eligible for loan forgiveness.

Do payroll costs such as employer 401(k) contributions, which are incurred during the covered period but not paid until much later (such as at the end of the year), count as forgivable expenses?

Answer: If the costs were either incurred or paid during the covered period, they should be eligible for loan forgiveness. It's not clear whether 401(k) contributions that are paid at the end of the year would count as forgivable expenses or whether they would need to be paid no later than the next billing cycle (*i.e.*, the time that the employee receives their salary for the Covered Period). Forgiveness is not provided for employer contributions for retirement benefits accelerated from periods outside the Covered Period.

Is cash paid as a health insurance stipend considered cash compensation?

Answer: A cash stipend that is paid to employees in lieu of health insurance that employees have the option of using for purchasing their own health insurance is cash compensation. It is eligible for loan forgiveness but subject to the \$100,000 annual compensation limit.

Do bonuses or other supplemental pay types count towards the \$100,000 annual compensation limit per employee?

Answer: Yes.

Is the cap of \$46,154 for cash compensation for employees earning over \$100,000 in annual salary applicable to both base salary and benefits or base salary only?

Answer: The \$46,154 maximum (which is \$100,000 prorated for a 24-week covered period) applies only to cash compensation such as salary and bonuses. It does not include the cost of benefits.

A borrower received PPP loan funds on April 15, 2020. The next payday, April 17, covered the period from March 29 to April 11, 2020. Would our Alternate Payroll Covered Period start March 29, and then we can count all April payments?

Answer: If you begin your Covered Period on April 15, 2020, you would be able to include the payroll period that covers March 29 to April 11, 2020, because the payroll costs are paid during that Covered Period. Conversely, you would be able to include salary payments paid after the Covered Period to the extent that they were payment (at least in part) for some of the time worked during the Covered Period – because the payment obligation was incurred during the Covered Period. If you elect to use the Alternative Payroll Covered Period, you would start on the first day of the first pay period after PPP loan disbursement. Note that only borrowers with a biweekly (or more frequent) payroll schedule can elect to use an Alternative Payroll Covered Period.

Can I pay utilities or retirement plan contributions during the 24-week period in advance, such as paying SEP for the 4th quarter before the end of the 24-week period, and seek forgiveness on these amounts?

Answer: No. Utility costs incurred prior and paid during the Covered Period are eligible for loan forgiveness (as well as costs incurred during the Covered Period). The SBA has made clear that forgiveness is not provided for employer contributions for retirement benefits accelerated from periods outside the Covered Period. While we have not seen any guidance that addresses the issue of utility costs that are paid in advance, we do not believe that they would be.

Reductions in FTE and Salary/Wages

I own a construction company with a majority of employees being paid hourly. Each employee has missed at least one day in 8 weeks for sickness or personal reasons. Does that mean every hourly employee is reduced to a 0.5 FTE? That would be devastating.

Answer: No, the “simplified method” is optional. That method allows a borrower to assign 1.0 FTE for employees who work 40 hours or more per week and 0.5 FTE for employees who work fewer hours – rather than using employees’ actual FTEs. Electing the simplified method is beneficial for forgiveness only if an employee works the equivalent of 0.5 FTE or less. The same method must be used to calculate FTE in both the Covered Period and the borrower’s chosen reference period.

Thinking about Chuck in this example who was laid off, if our business elects the FTE Reduction Safe Harbor 1 due to not being able to return to business activity, is Chuck’s reduction now a “salary/hourly wage reduction?” Or do we essentially avoid any loan reduction due to laying him off?

Answer: If the FTE Reduction Safe Harbor for inability to return to previous level of business activity applies, then the borrower is exempt from the reduction in loan forgiveness based on a reduction in FTE. In our hypothetical example, Chuck’s salary was not reduced, he was laid off. The reduction in forgiveness amount based on salary/wage reduction applies only to the portion of a decline in an employee’s salary/wages that is not attributable to the FTE reduction. (See pages 33008-09 of this interim final rule: <https://home.treasury.gov/system/files/136/PPP-IFR-Loan-Forgiveness.pdf>.)

How is the FTE Reduction Quotient applied?

Answer: The FTE Reduction Quotient is multiplied by the total of eligible payroll costs, mortgage interest payments, rent or lease payments, and utility payments to determine the “Modified Total.” The forgiveness amount is then selected as the smallest of three amounts: the Modified Total, the loan amount, and an amount calculated to ensure the forgiveness amount conforms with the requirement that 60% of the forgiveness amount was spent on payroll costs.

What if there have been new hires in the covered period? Can their salaries still be part of the application for forgiveness?

Answer: Yes, so long as payroll costs are incurred or paid in the Covered Period, those costs are eligible for forgiveness.

On SBA Form 3508EZ, are “Employees at Time of Loan Application/Time of Forgiveness Application” FTEs or actual employees count? Is the “Time of Forgiveness Application” the date you submit the application or end of the covered period?

Answer: The Instructions for SBA Form 3508EZ indicate that borrowers should provide the “total number of employees” in the referenced blanks – that is, the actual employee count. The same approach is used on SBA Form 3508. The Time of Forgiveness Application is the date you are submitting the forgiveness application.

We have 2 hourly employees who are full-time but work only 37.5 and not 40 hours, how should these employees be treated for FTE?

Answer: These employees will be counted as 0.9 FTE, according to the method set out in the Instructions (see “Average FTE” on page 4). Importantly, the employees should be counted as 0.9 FTEs both in the Covered Period and in the chosen reference period. Therefore, if these employees worked the same hours weekly in both periods, no reduction in FTE will have occurred.

Is the safe harbor provision regarding the inability to resume normal business operations applicable if the borrower was unable to do so during the first months of the 24-week period but resumed near-normal operations toward the end of the period?

Answer: Unfortunately not. To be eligible for the FTE Reduction Safe Harbor related to federal health guidance, the borrower must “document that it was unable to operate between February 15, 2020, and the end of the Covered Period at the same level of business activity as before February 15, 2020” (see Instructions, page 5).

An IFR published well before these FAQs is consistent with the Instructions. It says: “This decision to permit seasonal employers to use, as a reference period, any consecutive 12-week period between May 1, 2019 and September 15, 2019 is an exercise of the Secretary’s rulemaking authority under section 1109 of the CARES Act. This reference period is consistent with the interim final rule on seasonal employers issued by Treasury. See 85 FR 23917 (April 30, 2020),” 85 Fed. Reg. 33004, 33007.

Nonpayroll Costs

Does storage rent count as rent in the forgiveness calculation?

Answer: Yes, storage rent is eligible for forgiveness if it was a business cost. The rental agreement must have been entered into before February 15, 2020.

If my payroll costs are significantly higher than my loan amount, can I ignore the nonpayroll costs?

Answer: A borrower is not required to include nonpayroll costs in the forgiveness amount calculation. It is prudent, however, to calculate and include all eligible nonpayroll costs in the event that the borrower’s payroll calculation is found to be incorrect (too high) by the lender or the SBA. Nonpayroll costs can be used to support the claimed forgiveness amount. Performing the calculation of nonpayroll costs will also assist the borrower in identifying the documentation to be retained. Documentation of eligible nonpayroll costs will then be available to provide support to the borrower’s requested forgiveness amount.

Owner-Employees, Self-Employed, Sole Proprietors

In the example forgiveness application, there were no payments for owner compensation. How is it handled when there is owner compensation and the owner is an employee who received a salary? What are the limits on owner and self-employed individual compensation? Is there a reference for self-employed individuals who received a PPP?

Answer: The amount of compensation of owners who work at their businesses that is eligible for forgiveness depends on the business type. We refer you to the SBA’s Frequently Asked Questions (FAQs) on PPP Loan Forgiveness for more details (see pages 4-6 of the FAQs, <https://home.treasury.gov/system/files/136/PPP--Loan-Forgiveness-FAQs.pdf>).

The amount of owner compensation eligible for forgiveness also depends on whether the borrower is using an 8-week or a 24-week Covered Period. The amount of forgiveness for payroll compensation for owner-employees and self-employed individuals is capped at \$20,833 per individual in total across all businesses in which he or she has an ownership stake. For borrowers that received a PPP loan before June 5, 2020 and elect to use an eight8-week Covered Period, this cap is \$15,385. This guidance can be found on page 4 of the FAQs and on page 3 of the Application Instructions.

Are nonpayroll expenses (rent/utilities) available for forgiveness for self-employed individuals?

Answer: Yes.

Timing of Forgiveness Application

I'm waiting to apply for forgiveness, is there an end date set by which all applications must be received? When is the loan forgiveness due date?

Answer: A PPP borrower must apply for forgiveness within 10 months after the last day of the borrower's Covered Period.

A borrower received its PPP loan after June 5, 2020 and is therefore using the 24-week Covered Period. The borrower uses the loan fund to pay eligible payroll and nonpayroll costs. The funds are used by the end of week 12. Does the borrower have to wait until the full 24-week period has passed before filing for forgiveness?

Answer: No, the borrower does not have to wait until the end of the 24-week period to file its forgiveness application with its lender. There may be advantages to waiting, however, including avoidance of any corrections based on unanticipated changes before the Covered Period ends.

If a borrower spends its PPP loan funds before the end of the 24-week period and files for forgiveness at that point, is the borrower able to do lay-offs or reduce hours once its application is submitted?

Answer: If a borrower reduces FTEs or salary/wages at any time within the Covered Period, it will need to account for these reductions in its forgiveness application (including any FTE reduction safe harbors that apply). If a borrower has submitted its forgiveness application before the end of the Covered Period, and then makes further reductions in FTE or salary/wages, the borrower would be required to correct its forgiveness application to account for the additional reductions occurring before the end of the 24-week Covered Period.

Can a borrower use a Covered Period different from the 8-week or 24-week period, for instance if a borrower spends all PPP loan funds before the end of the 24-week period?

Answer: No. The Covered Periods for forgiveness are established by statute, and the applicable period cannot be changed for an individual borrower. Borrowers that received PPP loans before June 5, 2020 (the date of enactment of the Paycheck Protection Program Flexibility Act) can elect to use either the 8-week period or the 24-week period.

Accounting for PPP Loan

As a non-profit utilizing all funds for allowable expenses before fiscal year end, but not yet having been notified of loan forgiveness approval, would I record the grant revenue at year end?

Answer: A non-profit would follow ASC 958-605 Revenue Recognition – Contributions. The PPP grant is considered to be a conditional contribution so long as the organization has reasonable assurance that will comply with the conditions and forgiveness will be received. All of the conditions must be met in order to recognize the revenue. The conditions are: (1) the entity met the eligibility requirements upon applying, (2) incurred the allowable expenses, (3) FTE's and wage rates were maintained or safe harbors were available, and (4) SBA/lender forgave the loan. Upon these conditions being met, the organization can recognize the revenue.

There is uncertainty surrounding whether the forgiveness application process is a substantial condition or an administrative task. Under ASC 958-605, if the borrower considers it to be an administrative task, the organization could recognize the revenue when the other conditions are met. This is a more aggressive accounting position and should be discussed with your auditors or accountants. It could result in more testing by your auditors. Additional guidance may be forthcoming from the SBA regarding the forgiveness process.

For a non-profit, is it permissible to record the loan as deferred revenue and then move to grant revenue upon forgiveness? I'm very confident we will meet all criteria for full forgiveness.

Answer: If you are confident that you will meet the requirements for forgiveness, then record it as a refundable advance (a liability, similar to deferred revenue).

Government Audits of PPP Loans

If the original loan amount was more than \$2 million – however, you pay back enough to drop the forgivable amount below \$2 million – will we still be subject to mandatory audit?

Answer: PPP loans over \$2 million are subject to mandatory SBA “review” for compliance with program requirements including eligibility and certification of necessity. These reviews are based on loan amount, not the amount of forgiveness requested. Loans of \$2 million and below are subject to review as well, if SBA and Treasury determine that review is “appropriate.”

If SBA determines that the borrower did not have an adequate basis for the required certification of necessity, SBA will seek repayment of the outstanding PPP loan balance and will inform the lender that the borrower is not eligible for loan forgiveness. If the borrower repays the loan, SBA will not pursue enforcement actions.

We strongly advise borrowers with PPP loans subject to review to seek legal advice pertaining to their unique situations.

Further Legislation

Do you have any additional information about the potential additional round of PPP funding that Congress is currently considering? I understand that, although there is a lot of disagreement over many aspects of this additional legislation, both sides agree that PPP should be included.

Answer: Congressional negotiations over the future of the Paycheck Protection Program have stalled and further action is not expected until September. Many proposals have been considered, including automatic forgiveness of smaller loans and streamlined forgiveness for others. We will continue to monitor developments and provide client alerts to flag important changes in the PPP.

Thank you for participating in our ***Navigating*** series webinar on Paycheck Protection Program Loan Forgiveness and for all your questions. Remember that rules for the PPP have been in flux, and further legislation may change the rules yet again. Always check the latest rules and guidance from the Small Business Administration and Treasury: <https://home.treasury.gov/policy-issues/cares/assistance-for-small-businesses>. Please contact us with questions that arise during the forgiveness process.

Please visit our ***Coronavirus: Preparation & Response*** series for additional resources we hope will be helpful.