

PPP Loan Forgiveness



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Disclaimer

This presentation is based on relevant government guidance available as of October 7, 2020. There are many areas of the CARES Act, related guidance and the SBA's Loan Forgiveness Application that are unclear and additional clarification from the government is needed. In addition, there may be legislation in future weeks that modifies the program rules. This presentation includes our best interpretation of the guidance.

PPP Loan Forgiveness

- Applications: When and How?
- 3508EZ: Are you Eligible?
- Taxes and Tax Returns
- Equity Transactions
- Not for Profits and Government Contracts
- FTEs Revisited
- Open Q&A



Applications: When & How?

Applications: When?

- As of last Friday, the SBA had received over 100,000 applications in their portal
- According to a news article this morning, they began approving and remitting funds to lenders on October 2nd
- No known approvals locally based on our discussion with clients and lenders

Applications: When?

- Factors to consider (source: AICPA)

Factors impacting timing of forgiveness application

Has the borrower spent the full amount of PPP funds?

Is borrower trying to sell the business?

Is the loan under/over the dollar amount of potential threshold for simplified forgiveness? Current discussions set \$150k or a tiered system.

Has tax planning around timing of deductibility of expenses paid with PPP funds been considered? See Aug. 20 discussion with Ed Karl, AICPA VP, Tax

Does borrower need to make business operating decisions that may include FTE reductions?

Does borrower want to get PPP debt off the books? Are there loan covenants to consider?

Is the lender accepting applications?



#AICPATownHall



Applications: When?

- If your PPP loan is less than \$150,000 consider waiting to apply for forgiveness
- There is proposed legislation that would reduce the forgiveness paperwork required for loans this size
- With 10 months to apply for forgiveness, there is plenty of time to take a wait and see approach

Applications: When?

- Don't rush to apply
- Legislation continues to evolve
- Stay in touch with your lender



Applications: How?

- Some lenders are letting borrowers apply with less than 24 weeks of costs and before 24 weeks elapse.
- Some lenders are only allowing applications for 8 weeks or 24 weeks, and only after the covered period selected (8 or 24) has elapsed.
- Ask you lender what their interpretation is and what they will accept.

Applications: How?

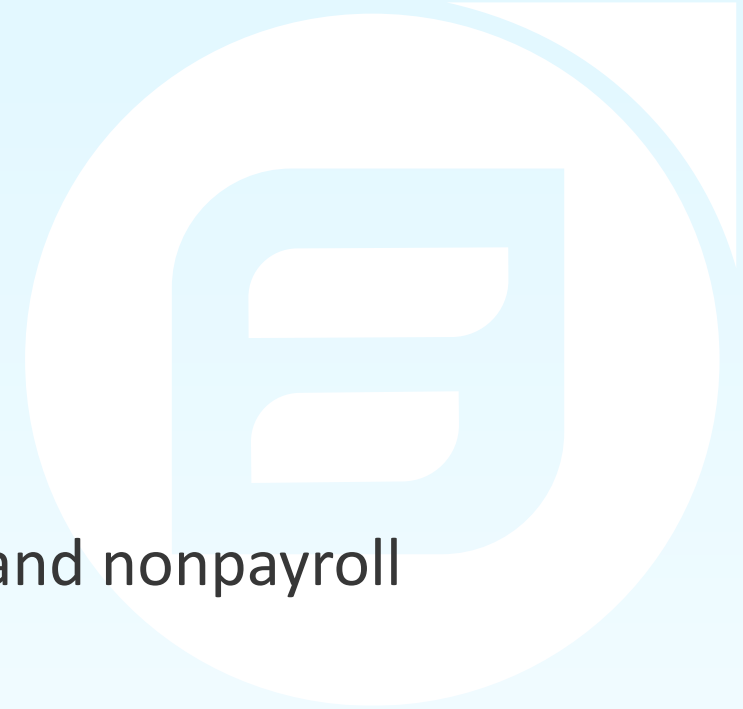
Reason some lenders are more strict?

- If you spend all of the PPP funds in less than 24 weeks, you are eligible to file for forgiveness at that time (per Secretary Mnuchin). HOWEVER, there is no guidance on how filing before 24 weeks affects the FTE computations and allowed wage limits.
- Some lenders take the conservative approach and enforce the full 24 week reporting of wages and FTEs.

Applications: How?

What covered costs should you use?

- The PPP program guidelines allow you to use payroll and nonpayroll costs.
- If you can reach 100% forgiveness with payroll costs only, we recommend doing so.
- Documentation requirements for nonpayroll costs can be burdensome.



Applications: How?

Examples:

- For rent: Copy of the lease, verification of rent payment (statement, cancelled check, EFT, etc.)
- For utilities: Copy of the invoice for the period that includes 2/15/20 to prove service was in place on that date, copies of the invoices being included as covered costs, verification of payment (statement, cancelled check, EFT, etc.)



3508EZ: Are you Eligible?

3508EZ: Are you Eligible?



There are 3 ways to qualify to file Form 3508EZ:

#1 Sole proprietor with no employees

- Choose the 24 week period

- The formula for your forgiveness is:

 - 2019 Form 1040, Schedule C, line 31

 - Divided by 12 * 2.5

 - Maximum of \$20,833

3508EZ: Are you Eligible?

Documents required to submit for Option #1:

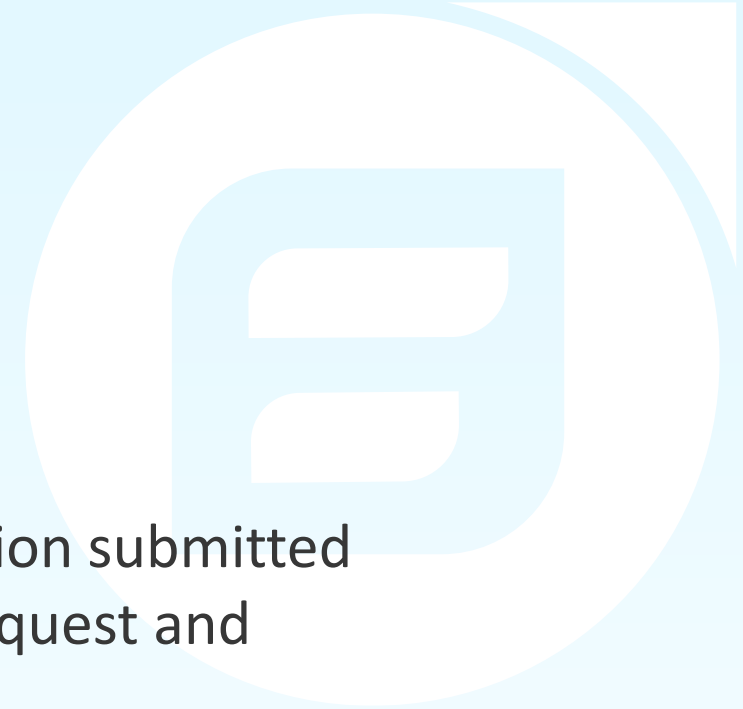
- Sign a certification statement.
- Provide a copy of your 2019 Form 1040, Schedule C



3508EZ: Are you Eligible?

Documents required to maintain, but not submit, Option #1:

- All records relating to the PPP loan, including documentation submitted with PPP loan application, support for necessity of loan request and eligibility for PPP loan.



3508EZ: Are you Eligible?



There are 3 ways to qualify to file Form 3508EZ:

#2 Meet two tests:

- Certify that you did not reduce the annual salary or hourly wages of any employee by more than 25% during the covered period, as compared to Q1 of 2020.
- Certify that you did not reduce FTEs between January 1, 2020 and the end of the covered period.

3508EZ: Are you Eligible?



Documents required to submit for Option #2:

- Sign a certification statement.
- Copies of payroll registers, Form 941, etc. for payroll costs
- Copies of invoices, proof of payment, etc. for all other costs
- The average # of FTEs on January 1, 2020 and the end of the covered period.

3508EZ: Are you Eligible?

Documents required to maintain, but not submit, Option #2:

- All records relating to the PPP loan, including documentation submitted with PPP loan application, support for necessity of loan request and eligibility for PPP loan.
- Documentation that salaries and wages were not reduced by more than 25%, computed by individual employee.

3508EZ: Are you Eligible?

Documents required to maintain, but not submit, Option #2:

- FTE computations for relevant base period(s) and the covered period to support certification that FTEs were not reduced, by individual employee.
- Payroll records for January 1, 2020 through the end of the covered period, by individual employee.
- Support for any FTE reduction exceptions claimed

3508EZ: Are you Eligible?



There are 3 ways to qualify to file Form 3508EZ:

#3 Meet two tests:

- Certify that you did not reduce the annual salary or hourly wages of any employee by more than 25% during the covered period, as compared to Q1 of 2020.
- Certify that you were unable to operate during the covered period at the same level of business activity as before 2/15/20, due to compliance with COVID restrictions.

3508EZ: Are you Eligible?

Documents required to submit for Option #3:

- Sign a certification statement.
- Copies of payroll registers, Form 941, etc. for payroll costs
- Copies of invoices, proof of payment, etc. for all other costs



3508EZ: Are you Eligible?

Documents required to maintain, but not submit, Option #3:

- All records relating to the PPP loan, including documentation submitted with PPP loan application, support for necessity of loan request and eligibility for PPP loan.
- Documentation that salaries and wages were not reduced by more than 25%, computed by individual employee.

3508EZ: Are you Eligible?

Documents required to maintain, but not submit, Option #3:

- Support for inability to operate, including relevant financial records (to show revenue/cost impact)
- Copies of the federal, state and/or local COVID guidelines that your business was required to follow that restricted your ability to operate. Most of these can be found online on the municipalities website.

Taxes and Tax Returns

Taxes

- As of today, October 7, 2020, the forgiven portion of the loan is not taxable and the expenses for which the PPP money was used for are not deductible.
- Your expenses may hit in one tax year and the loan forgiveness income in another... how does that get reported?
- Legislation has been introduced to make the expenses deductible

Taxes

Under current law:

- What is the impact of nondeductible payroll on your R&D Credit or QBI computation?
- How should you compute projected taxable income and quarterly estimates?
- Fiscal year filers.... How do you compute your extension payment?



Taxes

What to do?

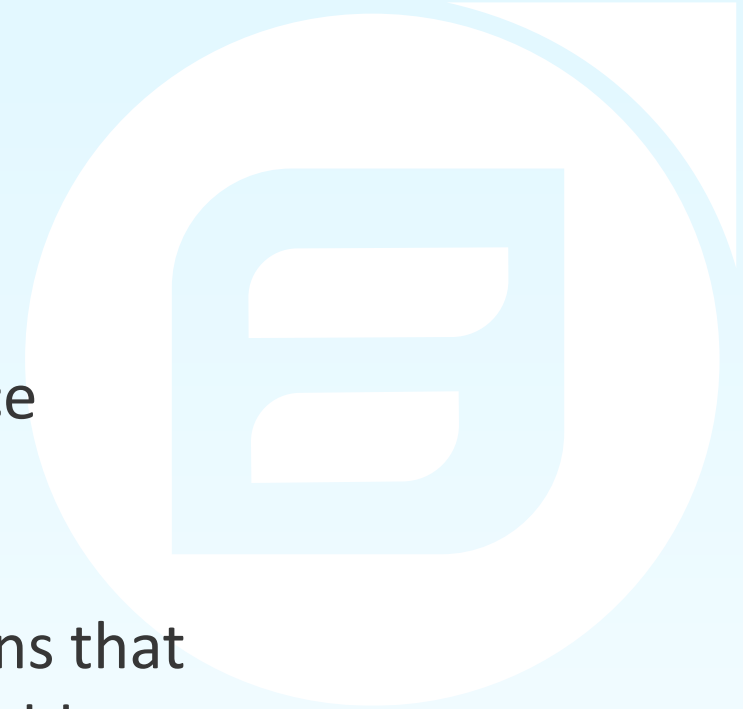
- Fiscal year filers... Consider an extension
- Decide how to compute estimates and extension payments, use current law or compute assuming expenses will be deductible.
- This is a business owner / business risk decision



Equity Transactions

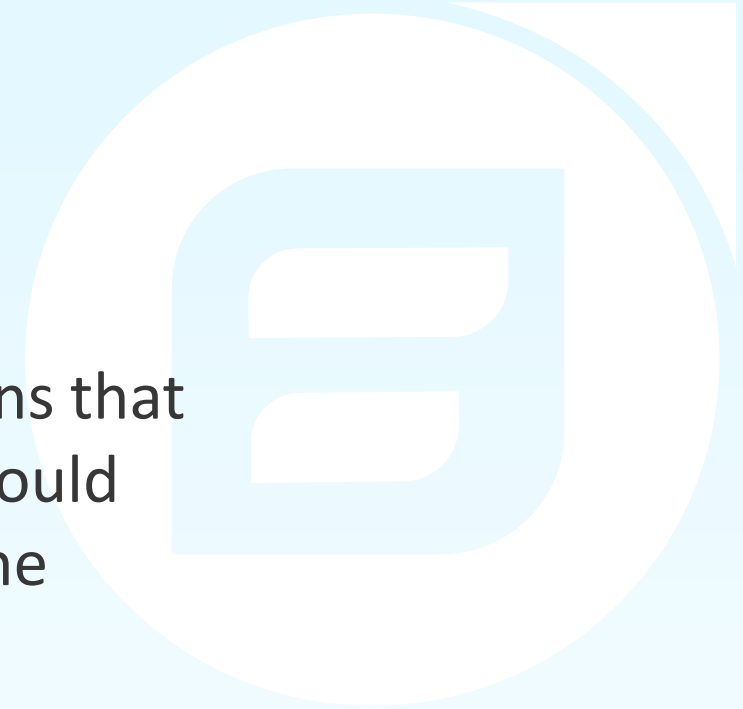
Equity Transactions

- On October 1, 2020 the SBA issued a procedural notice regarding changes in ownership.
- If you have a single transaction or series of transactions that is less than a 20% change in ownership, then you should notify the lender of the pending transaction(s), however there is no need to involve the SBA.



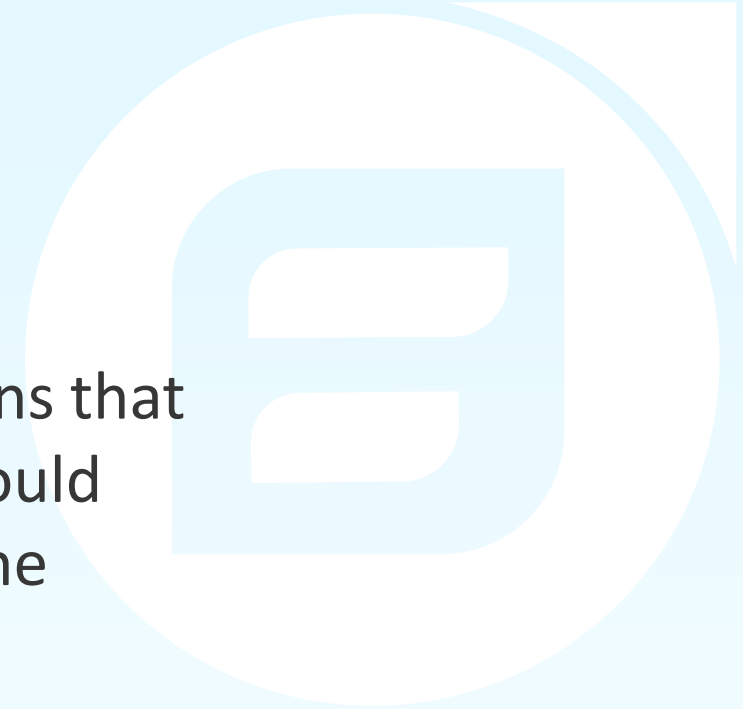
Equity Transactions

- If you have a single transaction or series of transactions that is more than a 20% change in ownership, then you should notify the lender of the pending transaction(s), and the lender must notify the SBA Loan Servicing Center.
- If the change in ownership is between 20-50%, the lender may unilaterally approve the transaction.



Equity Transactions

- If you have a single transaction or series of transactions that is more than a 50% change in ownership then you should notify the lender of the pending transaction(s), and the lender must notify the SBA Loan Servicing Center. In addition, if the borrower completes its forgiveness application and establishes an escrow account equal to the PPP loan until the forgiveness process is complete, no further action is required.



Equity Transactions

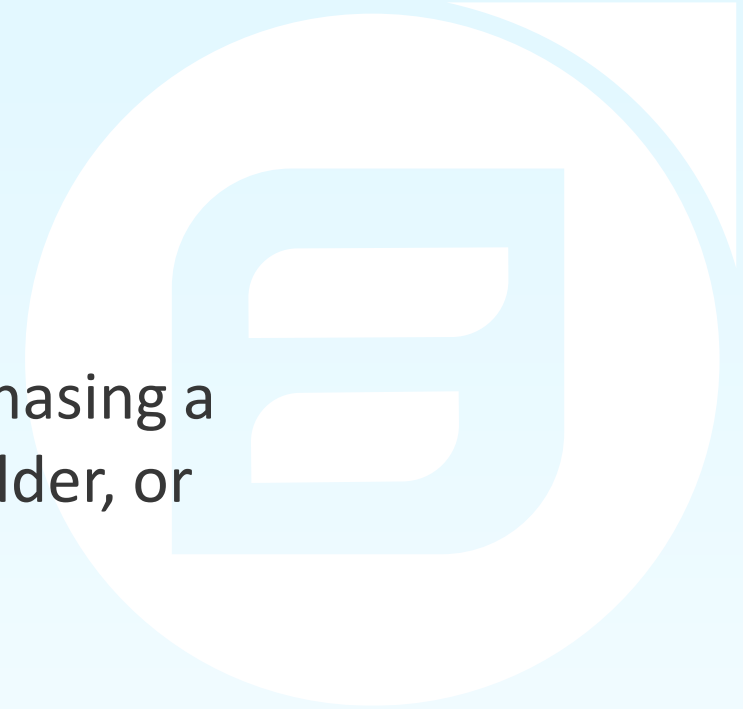
- If you have a single transaction or series of transactions that is a sale of at least 50% of the assets of the company then you should notify the lender of the pending transaction(s), and the lender must notify the SBA Loan Servicing Center. In addition, if the borrower completes its forgiveness application and establishes an escrow account equal to the PPP loan until the forgiveness process is complete, no further action is required.

Equity Transactions

- If you have a single transaction or series of transactions that is a sale of at least 50% of ownership interest OR a sale of at least 50% of the assets of the company and the borrower does NOT set up an escrow account at closing, the transaction is subject to prior SBA approval, the lender may NOT unilaterally approve the transaction.
- Specific documentation must be provided to SBA

Equity Transactions

- If you are considering a sale of your business, or purchasing a business that has a PPP loan, or buying out a shareholder, or one of your partners is retiring...
- Consult with the lender
- Consult with your CPA
- Consider consulting with an attorney



Not for Profits

Not for Profits

- Relevant if you are a NFP, or you sit on the Board of a NFP.
- Costs reimbursed under Cost Reimbursement Government Grants cannot also be included as PPP costs on your forgiveness application.
- Segregate costs and strategize how to maximize PPP forgiveness and cost reimbursement.



Government Contracts

Government Contracts

- Relevant to FOR PROFIT entities.
- Government contractors that must follow the FARs may have to treat a forgiven PPP loan as a direct reduction of the indirect cost pool.
(FAR part 31.201.5)
- DOD Guidance: https://www.acq.osd.mil/dpap/pacc/cc/docs/covid-19/FAQ_Implementation_Guidance_CARES_Act_Sec_3610_2020.08.17.pdf



Government Contracts

- If you have contracts with state agencies (like ADOT), contact them for guidance.
- If a significant portion of your annual revenues is from government contracts subject to the FARs, you may want to consider whether filing for forgiveness makes sense, or if repaying the PPP loan would make sense.
- Consult with your CPA



FTEs Revisited

FTEs Revisited



- FTE Formula: Hours worked per week / 40

Examples...

Joe works 30 hours a week, he is a 0.75 FTE

Mary works 20 hours a week, she is a 0.5 FTE

Bob works 55 hours a week, he is a 1.0 FTE

(can't be more than 1.0)

- For a payroll that includes the 3 employees above, the FTE count is: $0.75 + 0.5 + 1.0 = 2.25$

FTEs Revisited



- The Application allows a simplified method of computing FTEs. Employees working 40 or more hours are 1.0, employees <40 are 0.5.

Example using the simplified method...

Joe works 30 hours a week, he is a 0.5 FTE

Mary works 20 hours a week, she is a 0.5 FTE

Bob works 55 hours a week, he is a 1.0 FTE

- For a payroll that includes the 3 employees above, the FTE count is: $0.5 + 0.5 + 1.0 = 2.0$

FTEs Revisited

- For all periods that you have to compute FTEs, you need to pick one method (actual or simplified) and use it for all periods.
- Owners are EXCLUDED from all FTE computations.
- “Owner” has been defined as an individual that has a > 5% ownership interest



FTEs Revisited



- The FTE average during the covered period is then compared to the FTE average during the “base period”
- There are two options for the base period:
 - Option 1: 2/15/19 – 6/30/19
 - Option 2: 1/1/20 – 2/29/20
- Compute your FTE averages for both periods to determine which one is lower.

FTEs Revisited

- Compare FTEs during the covered period to the selected base period to determine whether the business has had an FTE reduction.
- Any reduction will affect the forgiveness computation.
- Example: If FTEs decline by 5%, eligible costs will be multiplied by 95% on Form 3508, page 1, line 7.



Q&A
