

# PPP Loan Forgiveness: Understanding the Loan Forgiveness Application (updated 5/25/2020)

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# PPP Loan Forgiveness Application

- On Friday, May 15<sup>th</sup>, the SBA issued its Loan Forgiveness Application (the “Application”) and instructions which is 11 pages long
- Borrowers will complete form and attach documentation to the bank that lent them PPP funds
- Lenders will review and certify accuracy of form and documentation. Lenders initials and signature required.
- The SBA will “review” loans in excess of \$2 million (FAQ 46)
- On May 22, 2020, the SBA released 2 additional interim final rules concerning:
  - PPP loan forgiveness (“Forgiveness IFR”)
  - The SBA loan forgiveness review procedures (“Procedure IFR”)

# Summary

- Form of Application
- Loan forgiveness process (Forgiveness IFR)
- Clarification of issues
  - Covered Period vs. Alternative Payroll Covered Period for computing payroll costs and forgiveness
  - “Payroll costs paid” and “payroll costs incurred” clarification
  - Loan forgiveness if 75% payroll cost test is not met
  - PPP Schedule A computation of FTE and payroll rate reductions
  - Definition of Full-Time Equivalent Employee
  - Definition of Cash and Non-Cash Compensation
  - Exceptions to FTE reduction and safe harbor
- Good faith certifications and potential legal implications for lender and borrowers
- Key unresolved issues

# Form of Application

## PPP loan forgiveness calculation form and instructions

- Includes Lines 1-11 to calculate forgiveness
- Requires that numbers be entered from PPP Schedule A
- Schedule A is where forgiveness amount is computed
- Check the box if loan *greater than* \$2 million (together with affiliates).
  - Per FAQ 46, this means the loan is subject to SBA review
  - Practically speaking, it is unclear how the SBA will have the resources to review the number of applications at issue
- Certain documents *must* be included with the application
- Other documents need not be submitted by the borrower, must be retained
- Borrower is required to maintain records for 6 years

# Form of Application

## PPP Schedule A

- Summarizes data that is calculated on supporting worksheets
- Worksheets calculate
  - Table 1: Under \$100,000 employee compensation
  - Table 2: Over \$100,000 employee compensation
- Worksheet for FTE reduction and safe harbor
- *For tipped employees:* Per Forgiveness IFR, the borrower (employer) needs to keep some record of tips, including for cash and “cash equivalents” (unclear what this means)

# Loan Forgiveness Process

## **Forgiveness IFR Q.2: The Forgiveness IFR sets forth a procedure for obtaining loan forgiveness:**

- Procedure applies to loan that are not already under review by the SBA.
- Borrower must complete and file the forgiveness Application
- Lender has 60 days (from completion) to review and make a forgiveness determination.
- At the time the lender makes its forgiveness determination, it notifies the SBA and requests reimbursement for the forgiven amount.
- The SBA may review the lender's forgiveness determination
- The SBA remits payment of the forgiven amount to the lender within 90 days *after* the lender notifies the SBA of its decision
  - Hence, a lender can expect payment ~150 days after the borrower submits its forgiveness Application
- If the SBA reviews the forgiveness Application and disagrees with the lender, the lender will not be reimbursed, and the loan not forgiven

# Loan Forgiveness Process

- If forgiveness is denied, the loan must be repaid over the 2-year period from the time the loan was approved.
- The SBA will establish a different procedure for loans that were reviewed prior to the submission of a forgiveness application



# What the Application Clarifies

## Length of the “Covered Period”

- Per the interim regs, the covered period was the 8 weeks from the day the bank deposited PPP loan proceeds in borrower’s account
- The Application’s definition of “Covered Period” provides flexibility in the 8 weeks:
- Option 1: Covered Period means: the 8 weeks (or 56 days) from deposit.
  - For example, if loan proceeds funded on April 20, 2020, the covered period is April 20 – June 14, 2020
- Option 2 (Alternative Payroll Covered Period) means: For borrowers with bi-weekly payrolls, the 8 weeks (or 56 days) commences on the first day of the pay period that begins *after* the PPP loan is deposited in their account.
  - For example, if the loan proceeds are deposited on Monday, April 20<sup>th</sup>, and the first pay period after that date commences Monday April 27<sup>th</sup>, the 8 week period runs from April 27<sup>th</sup> to June 28<sup>th</sup>.
  - Borrower must make this election on the forgiveness form
  - The election *only applies* to payroll items. Non-payroll items must abide by the 8 weeks from date of deposit rule.

# What the Application Clarifies

## Payroll Costs: Meaning of “Paid and Incurred”

- Payroll costs *incurred* but not *paid* during the last pay period of the Covered Pay Period or Alternative Payroll Covered Period are eligible for forgiveness ***if paid on or before the next regular payroll date.***
- Eliminates need to schedule a special payroll to be paid on day 56 of the applicable covered period.
- Count payroll costs that were both paid and incurred once.

# What the Application Clarifies

## Payment of Bonuses in Excess of Regular Payroll

- Nothing in the Application specifically addresses increasing compensation during the Covered Period
- Compensation paid to any employee (or owner) during the Covered Period cannot exceed \$15,385.
- Increases in owner compensation are likely to be scrutinized

# What the Application Clarifies

## The Forgiveness IFR further clarifies certain items not explicitly addressed in the Application:

- Forgiveness IFR Q.3(b) clarifies:
  - Bonuses and other income supplements to non-owners *are* permissible so long as the total does not exceed the \$15,385 cap.
  - Payments to furloughed employees are forgivable
- Forgiveness IFR Q.3(c) clarifies:
  - That member/partner/Sched. C compensation is capped at the lesser of \$15,385 or 8/52<sup>nd</sup> of 2019 net earning from self-employment.
  - That member/partner/Sched. C filers cannot use PPP loan proceeds to pay healthcare or retirement.

# What the Application Clarifies

## Non-Payroll Costs: Meaning of “Paid and Incurred”

- Costs must have commenced prior to 2/15/2020
- Payments *incurred* during the 8 weeks must be paid prior to the next regularly scheduled due date for the bill (even if paid outside the 8 week period)
- Costs can only be paid/incurred once
  - A prepayment of a bill is not eligible
  - A bill incurred before the covered period and paid during the covered period would be eligible
- Transportation costs are considered a *utility* payment and thus forgivable. Not clear what “transportation” means; is it filling a gas tank?
- Forgiveness IFR Q.4(b): Prepayments of mortgage interest is not permitted

# What the Application Clarifies

## The 75% Rule is Not a Bar to Loan Forgiveness

- The 75% rule is not a total bar to forgiveness if it is not met.
- If <75% of loan proceeds are used for eligible payroll costs, i.e. if 70% of loan proceeds were used for eligible payroll costs, seek forgiveness of that 70%. However, eligible nonpayroll costs cannot exceed 25% of the total forgiveness amount.
- Could SBA issue further guidance on these % caps eligible for forgiveness?

# What the Application Clarifies

## Payments to Owners/Self-Employed

- Amount capped at \$15,385 (\$100,000/52 Weeks x 8 week covered period) or 8 week equivalent of 2019 compensation if lower. 85 FR 21747, 21749.
- Amounts paid to owner-employees are excluded from calculation of FTE or salary reduction calculations.
- “Owner” is still not a defined term.
- Under the Forgiveness IFR, 92.35% of Section 179 depreciation is excluded for purposes of calculating net business income.
- Rules for defining who is an “owner” may depend on state laws
  - For example, in community property states, are both spouses treated as owners if the business is treated as community property?
- *Practice Point:*
  - If the owner is treated as an employee for tax purposes (C and S corps): It may be possible to use PPP loan proceeds to fund healthcare and retirement payments
  - If the owner is *not* treated as an employee for tax purposes (LLCs, partnerships, contractors, Sched-C): PPP loan proceeds cannot *not* be used to fund healthcare or retirement payments

# What the Application Clarifies

## Defining FTEs

- 2 options in calculating FTE:
  - Option 1: Average full-time equivalency (FTE) is the average number of hours paid per week divided by 40 (rounded to nearest tenth), with the maximum for each employee capped at 1
  - Option 2: Borrower may elect to assign a 1.0 for employees who work 40 hours/week or more and 0.5 for employees who work less than 40 hours/week
- Forgiveness IFR Q.5(d) provides further explanation.



# What the Application Clarifies

## Borrower Not Penalized for FTE Refusing to Return to Work

FAQ 40 – Borrower does not have to reduce FTE if borrower shows:

- Good faith written offer to rehire that was rejected by employee;
- Employee was fired for cause;
- Employee voluntarily resigned; or
- Employee voluntarily requested (in writing) and received a reduction in their hours

# What the Application Clarifies

## FTE Re-Hire Safe Harbor

- No loan forgiveness reduction as long as FTEs are rehired by June 30<sup>th</sup>. Forgiveness IFR Q.5(h) reinforces this.
  - *Note*, funds must still be expended during Covered Period
  - 25% cap on non-payroll expenses still applies
- Borrower must restore FTEs to February 15<sup>th</sup> level.
- No relief if employer reduced employees before February 15<sup>th</sup>.

# What the Application Clarifies

## Forgiveness IFR Q.5(f) explains what happens when FTEs are not restored and salary is reduced by more than 25%

- Nothing in the CARES Act specifically addresses this
- Wage reduction applies *only* to the part of reduced wage that is *not* also attributable to FTE reduction
- Example: If an employee's hours are cut to ½ time, but their hour rate remained the same, there is no wage reduction. *But*, if the employee's wages were also reduced by ½ the wage reduction forgiveness limitations would be applicable.

# Documentation to be Provided for Forgiveness

## To Verify Payroll

- Bank account statements or payroll service provider reports to verify cash compensation
- Tax forms (i.e. Forms 941, state wage reporting and unemployment insurance tax filings) for the Covered Period
- Receipts, cancelled checks, account statements verifying employer benefit contributions for health insurance and retirement plans

## To Verify FTEs

- Information showing the average number of FTEs between 2/15/2019 and 6/30/2019
- Information showing the average number of FTEs between 2/15/2020 and 6/30/2020
- *Seasonal employers may use alternative test: (1) average FTEs between 2/15/2019 and 6/30/2019, (2) average FTEs between 1/1/2020 and 2/15/2020, or (3) average number of FTEs for any 12 week period between 5/1/2019 and 9/15/2019*

# Documentation to be Provided for Forgiveness

## To Verify Non-Payroll Costs

- Verify existence of all nonpayroll eligible payments and that they were paid.
  - Cancelled checks, ACH/wire confirmation, credit card statements, etc.
  - Invoices, bills, etc.
  - What you would need to justify the expense for an IRS audit!
- For Mortgages: Loan agreement and amortization schedules.
- For Leases: Lease agreement.

# PPP Loans: Good Faith Certification

## Borrower Must Certify That:

- Request for forgiveness is as to funds were knowingly used for authorized purposes
- Confirms that borrower acknowledges civil and criminal liability for seeking forgiveness of unauthorized amounts
- The Application is accurate
- Submission to lender of required verification docs.
- The Application is correct in all “material” respects (The Application cites USC codes and defines fines and imprisonment time frames if there is a false statement held to be knowingly made (i.e. fraud)).
- Tax documents given to lender are the same as those provided to the IRS
  - Lender can share tax documents with the IRS
- That SBA may request additional information and Borrower’s failure to provide it may result in denial of loan forgiveness.
- SBA has authority to direct lender to disapprove loan forgiveness

# Procedures IFR

## Q.1 – Review of PPP Loans

- (a) SBA may review any loan (so much for FAQ 46?)
- (c) SBA may review a loan at any time – records must be kept for 6 years
- (d) failure to respond to an SBA inquiry can result in forgiveness denial/revocation
- (e) if the SBA decides (retroactively apparently) that a borrower was not eligible for a PPP loan, the loan is not forgivable.
- (f) An appeals process is in the works

# Procedures IFR

## Q.2 – Procedures for Lenders

- Lender must confirm receipt of required documents and double-check calculations (“perform a good faith-review”) to ensure loan is forgivable.
- No forgiveness unless lender gets all required documents.
- Lender may rely on the borrower’s reasonable representations and need not independently verify all supporting documentation.



# Procedures IFR

## Q.2(b) – Forgiveness decisions made within 60 days:

- Approval (forgiveness – yeah!)
- Denial in whole
- Denial in part
- If directed by the SBA, *denial without prejudice*: the borrower's application is incomplete and the lender will reconsider it following submission of additional information. *Unless* the SBA has already ordered denial.
- If SBA agrees with forgiveness decision, it will pay lender within 90 days of lenders decision

# Procedures IFR

## Q.2(b) Lender's decision on forgiveness must include:

- The PPP loan forgiveness calculation form and schedule A
- Borrower's demographic information (if submitted)
- Confirmation that the information provided is accurate
- The lender has complied with Q.2(a)
- If the lender has approved forgiveness, the lender must apply for reimbursement in that amount (plus interest)
- SBA will deduct EIDL loan balances from the forgiveness amount
- The lender must notify the borrower of its decision.
- If denied forgiveness, the borrower may request the SBA review the decision of the lender. Time to seek review is 30 days from denial.

# Procedures IFR

## Q.2(c) - SBA review procedures:

- SBA may review any loan at any time (what about FAQ 46?)
- Once SBA has commenced a review, the lender shall not approve any forgiveness until the review is complete

# Procedures IFR

## Q.3 Lender's Fees:

- (a) If the SBA decides the borrower was ineligible – lender does not get paid its processing fees
- (b) Fees paid to lenders that originated ineligible loans can be clawed back
  - However, the SBA will not seek to claw back guarantee payments
- (c) If a lender fails to meet documentation requirements, its fees can be clawed back

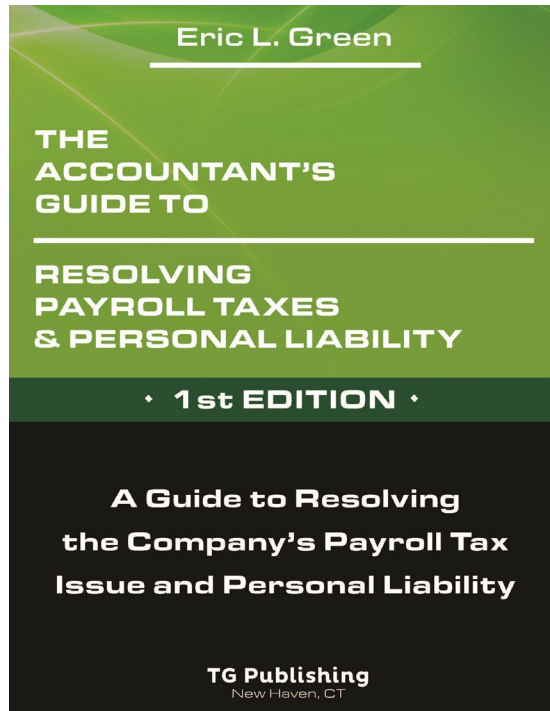
# Key Unsettled Issues

- The new Interim Final Rules inject more uncertainty
  - Is FAQ 46 now moot – since the SBA says it can review any loan or forgiveness application of any size
  - What will the SBA actually review
  - When will borrower's and lender's have certainty (if ever) that the loan is forgiven
  - What is the diligence requirement for lenders
- Treatment of owners as employees for closely held C and S corps.
  - Why should they get to use PPP money to fund healthcare and retirement expenses?
- Retirement Plans
  - Discretionary contributions to qualified plans
  - Contributions to non-qualified plan

# Key Unsettled Issues

- Do owners count as part of FTE calculation
- Do owner pay-cuts reduce loan forgiveness
- Rent costs
  - Do they include real estate taxes?
- Meaning of “unauthorized”
  - Does it mean can't use at all? Or, just not forgiven?
- What happens to funds that cannot be spent during Covered Period?

# Release of the New Accountant's Guide



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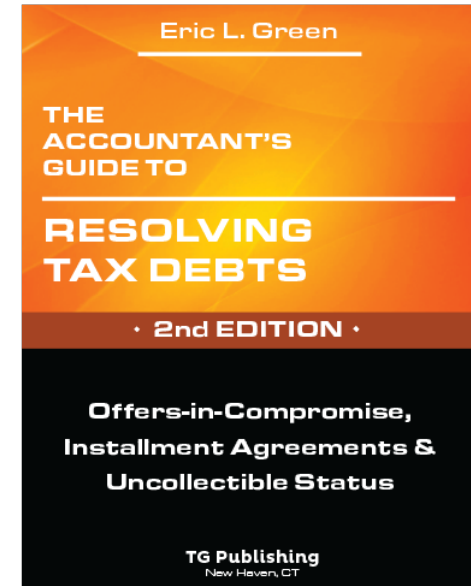
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# Questions?

