You’ve received your Paycheck Protection Program loan. Now what?

BILL DANIELSON / BRYAN WELSH / SHAWN DUBINSKY

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As the government issues billions of dollars in forgivable loans through the CARES Act Paycheck Protection Program, borrowers are seeking clarity on the rules for forgiveness. Answers to these frequently asked questions will help you prepare for a trouble-free application.

One of the key lifelines of the CARES Act — the $659 billion Paycheck Protection Program (PPP) — is providing financial assistance loans to thousands of businesses nationwide. The good news is up to 100% of the loans are forgivable — if the funds are used in a government-mandated way and borrowers are able to satisfactorily document how they were spent. But current guidance is sparse, and many businesses are wondering how to make sure the borrowed funds will be forgiven.

We’ve brought together frequently asked questions from our clients about requirements and best practices to support and track forgiveness calculations. While we await full guidance from the Department of Treasury and Small Business Administration (SBA), we hope the following discussion will help you prepare for a trouble-free loan forgiveness process.

What’s the best way to track payments for loan forgiveness?

We suggest launching a PPP treasury management process to track and properly record all disbursements. It should include detailed spreadsheets that itemize covered expenses, a gross-to-net pay breakdown of employee compensation, wage reductions, and full-time equivalent (FTE) headcount on a weekly basis. Develop an eight-week cash flow forecast and compare the forecast on a weekly basis to your actual check-run. The SBA has been clear that no supporting documentation equals no loan forgiveness.

What documentation will I have to provide to support my forgiveness calculation?

Consider using a cloud-based storage system with detailed naming conventions for schedules and supporting documents to easily identify covered expenses. Detailed records and proof of payment should include:

- Calculations for FTEs, itemized payroll costs, and a weekly expense tracker
- Payroll tax filings (Form 941 and payroll registers)
- Payroll processor reports (several leading payroll processing providers have formed a coalition to work with the SBA on developing custom PPP reports)
- Payment verification (canceled checks, bank statements)
- Rent invoices, utility bills, loan statements, and copies of lease and loan agreements

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Should we put the proceeds of the PPP loan in a separate bank account?

Yes. It's best practice to create a separate bank account to manage your PPP loan funds to assist with compliance and oversight as part of the loan forgiveness process. All covered expenses should be paid from this dedicated account or, at a minimum, amounts should be transferred from this account to your normal disbursement account to enable an audit trail. The goal is to avoid the need for extensive research to document qualifying expenditures.

I used a different lender than my current one. Do I need to notify my existing lender?

In most cases, yes. The secured lender will need to consent to the debt unless your credit agreement includes a category of permitted indebtedness (often referred to as a "basket") that applies to this type of loan. Even if the credit agreement includes a basket, permitting the PPP loan, the lender and borrower may not want to use the capacity if it's limited to specific purposes set out in the original loan. In this case, the parties should amend the provision to allow for further loan relief.

Can I use the proceeds of the PPP loan to pay down my revolving line of credit?

The CARES Act states that proceeds cannot be used to pay down principal of existing debt. Always consider the overall impact to forgiveness if PPP funds aren't fully used on covered expenses and what could happen if your bank activity shows the loan was used to pay nonmandated expenses.

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When does the eight-week covered period for qualifying expenditures start?

The eight-week covered period begins on the date the PPP loan is funded. The SBA stated that funding must occur within 10 days of closing of the loan.

What expenses are included in determining the amount of loan forgiveness?

While we anticipate forgiveness will include the following items, we’ve seen conflicting interpretations from trade organizations, the media, and other professional firms. Until full official guidance is released, we recommend creating a detailed, itemized schedule of all possible expenditures that may fall within the following definition of “covered expenses.” It should include:

- Payroll costs — that are defined in the same manner as the determination of the PPP loan amount ($100K annualized limit per person; exclude foreign employees, etc.). Note the definition of retirement benefits — “the payment of any retirement benefit” — is very broad and may be subject to further clarification.
- Payment of interest (not principal) on any covered mortgage obligation. (The debt must have been incurred prior to Feb. 15, 2020.)
- Payment of any covered rent obligations. (The lease must have been in effect prior to Feb. 15, 2020). Note the definition of rent obligations is very broad: “rent (including rent under a lease agreement).”
- Payment of covered utility expenses includes payment for a service for the distribution of electricity, gas, water, transportation, telephone, or internet access for service that began before Feb. 15, 2020.

Note that the interim final rule requires payroll costs to be at least 75% of the covered expenses paid for with loan proceeds. The maximum loan forgiveness will be based on the same 75% threshold. Also note that while the Act defines interest on debt incurred prior to Feb. 15, 2020 as an “Allowable Use of Covered Loans,” it’s not included in the definition of “expected forgiveness amount” (while the other listed expenses are included). The best practice is to track interest payments as a repayable item while the rules are being finalized.

How are employee reimbursements or nonqualifying expenses treated?

Many companies include expense reimbursements to employees as part of their normal payroll payments. These amounts should be excluded from compensation and should be paid separately from the covered payroll to the extent possible.

How are partner guaranteed payments handled in all of this?

There’s been a great deal of discussion as to whether partner guaranteed payments are included in initially determining the PPP loan amount and whether these payments would represent qualifying payroll expenditures during the eight-week covered period. In the absence of further guidance, the most conservative approach is not to include these payments either as part of the loan calculation or as a qualified payroll expenditure.

What method of accounting is used to calculate these expenses?

This is a key question that needs to be resolved and clarified by the SBA. The CARES Act states that expenses need to be incurred and paid during the eight-week period. The meaning of the phrase “incurred and paid” may be interpreted in a number of ways, and guidance from Treasury has been requested. Fortunately, many payroll service providers are working with the SBA and lenders to create specific PPP reports that help track and submit support for loan forgiveness.

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What if an employee leaves and a new employee starts? Do both wages count?

Yes. Both employees’ wages should be tracked to the extent the wages are incurred and paid during the eight-week period. There may also be an effect on the FTE calculation depending on the timing. We await further guidance on the definitions and process of loan forgiveness.

What if we’ve already made layoffs and wage reductions?

The amount of loan forgiveness a company is entitled to will be reduced if the number of FTE employees falls during the eight-week period or the amount of compensation to employees who made less than $100,000 is reduced by more than 25% during the eight-week period. However, the CARES Act provides an exemption from the reduction if a company cures any FTE or salary reduction by June 30, 2020. As with most of the forgiveness rules of the CARES Act, additional guidance from Treasury is needed.

I’ve applied for and received a PPP loan but it’s not yet forgiven. Can I defer the employer's share of social security tax without penalties?

Yes. Employers who have received a PPP loan but whose loan has not yet been forgiven may defer the deposit and payment of the employer’s share of Social Security tax that otherwise would be required to be made. This rule is in effect as of March 27, 2020, and continues until the earlier of the loan forgiveness date or Dec. 31, 2020. Once the employer receives a decision from its lender that its PPP loan is forgiven, the employer is no longer eligible to defer the deposit of the applicable payroll taxes and payment is due after that date.

The deferred portion of an employer's Social Security payments will be due as follows:

- On Dec. 31, 2021, 50% of the deferred amount
- On Dec. 31, 2022, the remaining 50% of the deferred amount

If you have additional questions around the paycheck protection loans, we're here to help. **Contact us** to get in touch with one of our experts.

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