

The Paycheck Protection Program: Plan & Prepare for Your Loan Forgiveness

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WIPFLI



Your Presenter



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Agenda

- ✓ Current State of the PPP
- ✓ New potential “gamechanger” rules passed by Congress awaiting President’s signature as we go to press
- ✓ Basic Review of the Forgiveness Guidance
- ✓ Loan Forgiveness Application – SBA Form 3508
- ✓ Loan Forgiveness Reductions
- ✓ Required Documentation
- ✓ Question and Answer

Current State of the PPP

- As of June 6, 2020, SBA has approved more than 4.5 million PPP loans totaling more than \$511 billion during both rounds of funding (down > \$10 Billion due to repayments)
- The average program loan size is approximately \$113,000
- About 29,600 loans over \$2 million (down > 3,000 from peak a few weeks ago prior to May 18 safe harbor repayment deadline)

Paycheck Protection Program Flexibility Act of 2020

- Passed the House 417-1 on May 28th, and the Senate unanimously on June 3rd. President signed on June 5th.
- **Extends the Covered Period from 8 weeks to the earlier of 24 weeks or December 31, 2020. However, we believe this also extends the FTE & wage reduction rules for the same period.**
 - ▶ Those with outstanding loans today can elect to retain the 8 week covered period and FTE & wage reduction testing period. This election may make sense for those who
 - Will have reached full or practical maximum forgiveness levels within the 8 weeks
 - Don't want to risk potential FTE/wage reduction forgiveness cutbacks through a 24 week covered period.
 - Want closure and certainty of outcome as soon as possible before year-end or other events.
- **Changes the SBA-imposed 75% payroll cost threshold for use of loan funds to 60%.**
 - ▶ Applies to all borrowers, regardless of elected covered period, BUT as drafted came with a new “cliff” requirement that if < 60% spent on payroll costs, then NONE of the loan is forgiven. This was a drafting error in the House version of the Bill.
 - ▶ **On June 8, Treasury Secretary Mnuchin clarified that partial forgiveness is still available even if < 60% of loan spent on payroll costs, subject to at least 60% of total forgiven amount being used on payroll costs.**
 - ▶ **Example: \$100K loan spent \$55K on payroll costs, \$45K on non-payroll costs. $\$55K / .60 = \$91,667$ maximum forgiveness, made up of \$55K payroll costs and \$36,667 of non-payroll costs, leaving a \$8,3333 loan balance.**

Paycheck Protection Program Flexibility Act of 2020 (continued)

- **Opens a new safe harbor exception from the FTE cutback rules for those who can't meet the current “re-hire by June 30” safe harbor, if the borrower can document that it is**
 - ▶ Unable to rehire those who were employees on Feb 15, 2020 and are unable to hire similarly qualified employees by December 31, 2020, OR
 - ▶ Unable to return to pre-February 15 2020 level of business activity (Sales? Profits?) due to compliance with requirements established or guidance issued by federal authorities, during the period March 1 through December 31, 2020 related to standards for distancing, or any other customer or worker safety requirement for COVID-19.
- **Revises the payment deferral period for any unforgiven loan balances**
 - ▶ Borrowers can defer payment on any loan balance until after SBA remits any forgiven portion to the lender
 - Eliminates cases where electing the 24-week covered period would have required starting loan amortization prior to any forgiveness BUT forgiveness must be applied for within 10 months of end of chosen covered period, or amortization will start on full loan balance.
 - ▶ Loans funded after date of enactment of THIS Act have a minimum 5-year amortization, while borrowers and lenders can mutually agree to modify the 2-year amortization for existing loans to as long as 5 years.

Paycheck Protection Program Flexibility Act of 2020 (continued)

- Amends the CARES Act to permit all borrowers to defer employer-share of FICA tax payments through December 31, 2020, without regard to whether a notice of loan forgiveness has been received or not
 - ▶ Obsoletes IRS Notice 2020-22 that required deferral to cease upon receipt of a notice of forgiveness
 - ▶ Deferred balance is still payable on the terms and conditions of the CARES Act
 - 50% of aggregate deferral is due December 31, 2021
 - Remaining 50% due December 31, 2022
 - Eliminates cases where electing the 24-week covered period would have required starting loan amortization prior to any forgiveness.
- **Questions!**
 - ▶ Will self-employed and employee-owners be able to use more than \$15,385 (8/52nds of \$100,000) as their covered payroll cost if electing the 24-week covered period? What about their health insurance and retirement benefits?
 - ▶ Will borrowers have to wait till the end of the 24-week covered period (if elected) to apply for forgiveness, or can the borrower toll the covered period at any time after 8 weeks by filing for forgiveness and computing FTE cutback safe harbors as of the date of filing?
 - ▶ What happens if a notice of forgiveness isn't received until after the end of the borrower's fiscal year, which could happen in a 24-week covered period scenario?

PPP Loan Forgiveness General Rules

- The amount of loan forgiveness can be up to the full principal amount of the loan. That is, the borrower may not be responsible for any loan repayment if the borrower uses all the loan proceeds for covered costs in the prescribed proportion, maintains or restores employee headcount, and maintains or restores individual employee compensation at defined amounts.
- While there is the potential for full loan forgiveness, borrowers need to properly model various calculations when considering whether to reduce or maintain employee and compensation levels.
- To the extent the loan is not fully forgiven, the balance is payable over a two to five year period (with payments deferred until SBA remits any forgiven portion to lender) with an interest rate of 1%.

How to Request Loan Forgiveness

- A borrower will submit an application to the lender that is servicing the loan
- The forgiveness request can generally be submitted after the end of the 8-week/24 week covered period or the June 30/December 31, 2020 deadline for restoring employee headcount and compensation (but note new 10-month post-covered period requirement)
 - Will lenders be ready when 8-week period ends for some borrowers?
- Consider waiting until further guidance is issued or a revised SBA loan forgiveness form is released
- The application must be submitted with required documentation
- The lender must make a decision on forgiveness within 60 days upon receipt of completed application, unless SBA has initiated a review of the loan prior to the lender's decision
- SBA then has 90 days to issue funds (forgiven amount plus accrued interest) to the lender
 - When will the borrower be informed? When the lender submits its decision to SBA or only after SBA review?

Loan Forgiveness Application

- The SBA Form 3508 application for loan forgiveness has the following components:
 - PPP Loan Forgiveness Calculation Form
 - PPP Schedule A
 - PPP Schedule A Worksheet
 - Optional PPP Borrower Demographic Information Form

Calculation of Loan Forgiveness - Payroll Costs

- Payroll costs includes gross wages, paid leave, health insurance and retirement costs, severance or dismissal costs, and state payroll and unemployment taxes
- Includes amounts paid or incurred during the covered period
 - “Paid” - the day of check disbursement or ACH origination
 - “Incurred” - the day earned by the employee
 - Use normal working schedule for paid non-working employees
- Alternative Payroll Covered Period (“APCP”) - may be selected by borrowers with a biweekly or more frequent payroll
 - Begins on first day of first pay period following loan disbursement date
 - If elected, must use throughout application when referenced
- Example - Funded on April 15th and biweekly payroll paid on April 17th. 8-week covered period ends on June 9th. Last biweekly payroll period June 12th.
 - Whether CP or APCP is elected, may get more than 8 weeks of payroll, depending on payroll cycle

Payroll Costs - PPP Schedule A

- Gross wages
 - ▶ Cash compensation only or include taxable fringes
 - ▶ Bonuses, commissions, hazard pay (now explicitly provided for in SBA guidance)
 - ▶ Furloughed employees
 - ▶ \$100,000 cap - \$15,385 for the 8-week covered period (will it be the same for 24-weeks?)
- Health insurance
 - ▶ Self insured medical
 - ▶ Vision and dental
- Retirement payments
 - ▶ How far back can incurred period go?

Payroll Costs - PPP Schedule A Worksheet

- Worksheet Table 1 – Record 2019 employees who earned \$100,000 or less for all pay periods, and new employees since 2019
- Worksheet Table 2 – 2019 employees who earned more than \$100,000 annualized rate for any pay period
- Independent contractors are excluded
- Owner-employees, general partners and self-employed individuals are reported separately
 - ▶ Amount is capped at lesser of \$15,385 or 2019 8-week equivalent pay (8/52nds)
 - ▶ Appears that for this group, payments for health and retirement benefits are being included in the \$15,385 limit. This appears to contradict the Interim Final Rule issued April 2, 2020, which states that payments for health and retirement benefits would be added on top of the \$100,000 cap.

Calculation of Loan Forgiveness - Nonpayroll Costs

- Amounts paid during covered period or incurred during covered period and paid on or before the next regular billing date (even if after covered period)
 - ▶ Likely will be able to include more than 8-weeks of covered costs.
- Mortgage interest payments - real or personal property
 - ▶ Mortgage obligation incurred before February 15, 2020
 - ▶ No prepayments
- Business rent payments for real or personal property
 - ▶ Lease agreement in place before February 15, 2020
- Business utility payments for which service was in place on February 15, 2020
 - ▶ What is included in transportation?
- Loan forgiveness portion still limited to 40% of non-payroll costs

Loan Forgiveness Reductions

- Loan forgiveness is reduced if borrower did not maintain headcount or wages during covered period.
- Safe harbor calculations can eliminate the reductions
- Application reduces total payroll and nonpayroll covered costs by the wage reduction amount. That net amount is then multiplied by a FTE reduction quotient to get a “modified total”.
- The maximum forgiveness amount is the lesser of the “modified total”, PPP principal amount, or total payroll costs divided by 60%.
- May 22, 2020 Interim Final Rule provides that there is no double penalty for wage and FTE reductions. For example, if an employee making \$1,500 a week is reduced to 60% time with a new weekly wage of \$900 ($\$1,500 \times 60\%$), there will be a FTE reduction, but no wage reduction.
 - ▶ Current application does not appear to adopt this approach

Wage Reduction

- Reduction is dollar for dollar to the extent covered period or APCP annualized wages are less than 75% of annualized Q1 2020 wages
 - Calculated on a per employee basis
 - Exception for employees who earned more than \$100,000 in annualized wages for any pay period in 2019
- Example - Borrower reduced full-time employee weekly wage from \$1,000 to \$700. Absent any safe harbor, borrower's loan forgiveness is reduced by \$400. Excess reduction is \$50 ($\$1,000 \times 75\%$ minus \$700) for 8 weeks
- Safe harbor provides that wage reductions between February 15, 2020 and April 26, 2020 that are restored on or before June 30, 2020 will be ignored for purposes of the wage reduction calculation
 - Compare salary or hourly wage on June 30, 2020 to salary or hourly wage on February 15, 2020
 - Full restoration required, not just to 75%
 - Any requirement to maintain wages after June 30, 2020/Dec 31, 2020 or after forgiveness has been granted?

FTE Quotient Reduction

- Reduction based on percentage of average FTEs during covered period or APCP as compared to average FTEs for a reference period selected by borrower.
 - ▶ Calculated on a per employee basis and then aggregated
 - ▶ Selected period - February 15 – June 30, 2019 or January 1 – February 29, 2020. Seasonal employers may also select a consecutive 12-month period between May 1, 2019 and September 15, 2019
- FTE is based on 40 hour work week.
 - ▶ Average number of hours paid per week/40 and round to nearest tenth, not to exceed 1.0
 - ▶ Alternatively, borrowers may elect to use 1.0 for employees working 40 hours or more and .5 for all others
 - ▶ Furloughed employees continuing to be paid should be counted as FTEs based on hours paid

FTE Quotient Reduction - Continued

- Safe harbor provides that FTE reductions between February 15, 2020 and April 26, 2020 that are restored on or before June 30, 2020 will be ignored for purposes of the FTE reduction calculation (for 8-week covered period elections)
- No FTE reduction for employees terminated for cause, employees who voluntarily resign or voluntarily request a reduced schedule, employees who reject a rehire offer at same hours and wages
 - ▶ SBA has determined borrowers should not be penalized for these events
 - ▶ Must maintain records and provide documentation upon request
 - ▶ Borrower must report rejected employment offer to state UI agency within 30 days
- Application appears to add a second FTE safe harbor based on there being no reduction of FTEs or wages between January 1, 2020 and borrower's covered period - more explanation is needed on this provision

Application Documentation

- The application must include the following supporting documents:
 - Verification of cash compensation paid to employees and employer contributions to health and retirement plans
 - Verification of the number of FTE employees for reference period
 - Payroll tax filings reported to the IRS and State tax authorities
 - Agreements, leases, contracts, invoices, statements, receipts, canceled checks for eligible mortgage interest, lease, and utility obligations during the covered period and from February 2020
- In addition, borrowers are required to maintain listings of employees identified in the forgiveness application, records regarding job offers and refusals, firings and resignations, and all other records relating to its PPP loan, loan application, certifications and eligibility for 6 years
- SBA has the right to access such records upon request

SBA Review – May 22, 2020 Interim Final Rules

- SBA to review all PPP loans over \$2 million and others as deemed appropriate
- Can review eligibility, loan amounts and uses, and loan forgiveness
 - ▶ SBA can initiate a review at any time; lender must notify borrower within 5 business days
- Lenders must inform SBA of forgiveness decision within 60 days of application receipt
- SBA must remit the forgiveness amount to lender within 90 days after lender issues its forgiveness decision, subject to any SBA review of the loan or loan application
- Borrowers will have an opportunity to address any unfavorable determinations made by SBA or lender

Income Tax Treatment

- CARES Act Section 1106(i) provides an exclusion from gross income for amounts otherwise taxable
- IRS issued Notice 2020-32 applying IRC 265 to disallow expenses to the extent they were funded with PPP loan amounts that were forgiven
- Proposed legislation (SB 3612 and identical HR 6821) would overrule IRS Notice 2020-32
 - ▶ No action yet on this in the Senate or House, and the PPP Flexibility Act failed to include it—is this dead in the water, or will it be taken up after June 30 in the House?

Questions and Answers

Resources



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