



BEST PRACTICES

PPP Loan Eligibility & Forgiveness

A key provision of the Coronavirus Aid, Relief and Economic Security (CARES) Act, which was signed into law on March 27, 2020, is the SBA's Paycheck Protection Program (PPP). The purpose of the PPP is to help small businesses cover their operating costs and keep workers employed during the COVID-19 crisis. This emergency funding, provided in the form of loans, is helping to alleviate some of the financial stress small businesses have endured as a result of the pandemic. If used for approved purposes, PPP loans to small businesses may be forgiven.

ELIGIBILITY

In order to be eligible for a PPP loan, the SBA and Treasury Department have stipulated that a business must:

- Have 500 or fewer employees;
- Be a 501(c)(3) non-profit organization, 501(c)(19) veterans' organization, or tribal business concern (sec. 31(b)(2)(C) of the Small Business Act) with the greater of (a) 500 employees, or (b) meets the SBA industry size standard if more than 500;
- Have a NAICS Code that begins with 72 (Accommodations and Food Services) that has more than one physical location and employs fewer than 500 per location; *or*
- Be an eligible self-employed individual, independent contractor or sole proprietorship.

These eligibility requirements were enacted to help ensure that only small businesses that rely heavily on cash flow to help fund operating expenses can continue as a going concern.

FORGIVENESS

In order to be eligible for loan forgiveness, the business or covered person must comply with the approved uses of funds, put the funds to work within the required 8-week or 24-week period, and adhere to the 60/40 allocation thresholds (at least 60% must be used for payroll, while 40% can be applied to the other approved uses).

The approved uses of the PPP funds are as follows:

- Payroll – which may include salaries, wages, commissions, vacation, family, sick and medical leave
- Mortgage interest – as long as the mortgage was signed prior to February 15, 2020 (which shall not include any prepayment or payment of principal)
- Rent – for any lease agreement entered into prior to February 15, 2020
- Utilities – incurred after February 15, 2020
- Interest on any other debt obligations that were incurred prior to February 15, 2020.

If the above criteria are met, your business will be eligible to apply for forgiveness through your financial institution that approved the PPP assistance. If the funds are used for other purposes, or do not meet the approved criteria, they will be not be eligible for forgiveness. Instead, the assistance will be a loan with a five-year maturity bearing 1% interest. Therefore, developing a plan upfront as to how you intend to use the funds and sticking to it will help ensure a favorable forgiveness application outcome.

INTERNAL TRACKING & ACCOUNTING

The PPP loan application process involves presenting a bevy of documents and supporting materials to your financial institution to determine eligibility. Applying for forgiveness will involve the same level of scrutiny on how these funds are used.

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ISSUES WITH MEETING THE 60/40 TEST

Some small business are having trouble meeting the allocation rule requiring them to apply at least 60% of their PPP loan amount toward payroll, either because they have laid off a large number of employees post-loan approval or management has reduced employee pay to the degree that total payroll costs have fallen below the 60% threshold.

In the case of the first scenario, the SBA's FAQ #40 grants an exception in the case of layoffs, if the borrower has made a good-faith, written offer to rehire the employee and the employee has rejected that offer, also in writing. Both should also be aware that employees who reject good-faith offers of re-employment may forfeit their eligibility for continued unemployment compensation.

In evaluating the total funding applied toward payroll costs, as in the second scenario above, a business must calculate the amount on an individual employee basis during the covered period. If the business cannot meet the 60% test, either because of a reduction in its Full-time Equivalent (FTE) employee headcount or a reduction in employee pay, and the remaining PPP funds have been applied toward other approved purposes, the amount not spent on payroll-related costs will be limited to 40% of the total PPP amount received, for forgiveness purposes, and the remainder will be treated as a loan.

Therefore, businesses should ensure they not only have the proper documentation in place to support their eligibility, but also need to be able to present supporting schedules detailing how these funds were received, the amount and percentage of the total funds applied toward both approved payroll costs and other approved items, and when these PPP funds were used. The ability to provide this evidence, through a detailed tracking process, will be crucial to support the desired outcome of loan forgiveness for the business.

Applying the right accounting treatment for your books and records will be vital to ensure you have recorded the receipt and use of the PPP funds in accordance with U.S. GAAP. Creating separate GL accounts, journal entries, financial statement disclosures, and internal whitepapers outlining the accounting considerations identified and accounting treatment applied will go a long way to ensuring a smooth audit process with the SBA and/or your external financial statement auditors.

THE REVIEW PROCESS

As part of the PPP application, all borrowers are required to certify in good faith that current economic uncertainty makes the PPP loan request necessary to support the ongoing operations of the applicant. The Treasury Department and SBA are still evaluating the review and/or audit requirements for the PPP program, though they have outlined who will be subject to a review in their [Paycheck Protection Program Loan FAQs](#).

According to FAQ #39, the SBA and Treasury will be reviewing all loans in excess of \$2 million, in addition to other loans as appropriate, following the lender's submission of the borrower's

loan forgiveness application. However, as later clarified in FAQ #46, "Any borrower that, together with its affiliates, received PPP loans with an original principal amount of less than \$2 million will be deemed to have made the required certification concerning the necessity of the loan request in good faith."

AN EVOLVING ENVIRONMENT

Since the PPP program was first enacted into law, there have been numerous updates to the rules and regulations regarding the receipt, use, and subsequent tracking of the funds, made available via the Treasury Department's FAQs. The Treasury Department has made it clear that the laws, rules, and guidance applied to businesses will be based on the rules in effect at the time of their relevant application. Therefore, we encourage businesses that are currently undergoing their application process or who have submitted their application but have not yet been processed, to stay up to date on the FAQs and interpretations that are released, as those will impact their PPP loan.

REDW will continue to monitor any updates arising from the Treasury Department, as well as interpretations from the FASB, and will release updates to these materials as appropriate. For further details on this discussion, or to find out more on how REDW can assist your company through the PPP process, please contact one of our COVID-19 Response Team members.

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