

# PPP LOAN FORGIVENESS EXPLAINED

Here are some important things you need to know when requesting Paycheck Protection Program loan forgiveness under the CARES Act. The recently enacted Paycheck Protection Program Flexibility Act has modified some of the original requirements, with a goal of making it easier for small businesses to qualify for forgiveness in the wake of coronavirus-related restrictions and guidelines that have delayed reopening for many businesses.

PPP loans are eligible for full or partial forgiveness if the loan proceeds are used in accordance with forgiveness rules and guidelines, which have already been modified several times.



In addition to changes introduced in the Flexibility Act, the Treasury Department on June 17 revised the PPP loan forgiveness application to make it more borrower friendly. Besides revising the full application, the Small Business Administration has added an EZ Forgiveness Application for certain borrowers.

## **What are the main changes in the new Paycheck Protection Program Flexibility Act?**

Small businesses that qualify for a PPP loan now have up to 24 weeks, or no later than Dec. 31, 2020, to use the money to qualify for loan forgiveness, which is an increase from the previous eight-week period. If your loan was funded prior to the passage of the PPP Flexibility Act, your covered period is automatically extended to 24 weeks, but if you choose to follow the original eight-week period you have that option.

Another change modifies the requirements that at least 75% of the funds had to be used for payroll costs and 25% for certain other costs. Those numbers have now been shifted to 60% for payroll-related costs and 40% for expenditures on mortgage interest, rent, and utility costs.

Additionally, new borrowers will have five years to repay the loan, instead of two.

## **Who is responsible for documenting my eligible costs?**

As the loan recipient, you are responsible for documenting your eligible expenses.

## **When does 24-week the clock start?**

The 24-week covered period begins on the date your loan is funded.

## **Is there a deadline to apply for a PPP loan?**

Yes, the new deadline to apply for a loan has been extended until August 8, 2020.

## Where do I submit my potentially forgivable expenses?

At the end of the 24-week covered period, you will need to provide the necessary documentation to your lender when applying for loan forgiveness. The Flexibility Act allows borrowers up to 10 months from the date their covered period ends to apply for loan forgiveness. Principal and interest payments would begin at that time.

## How has the PPP Loan Forgiveness Application changed?

The full original PPP forgiveness application was 11 pages long, but the new one has been reduced to 5. In addition, the EZ Forgiveness Application is only 3 pages. The SBA says the EZ application “requires fewer calculations and less documentation for eligible borrowers.”

- The EZ application applies to borrowers that:
- Are self-employed and have no employees; OR
- Did not reduce the salaries or wages of their employees by more than 25%, and did not reduce the number or hours of their employees; OR
- Experienced reductions in business activity as a result of health directives related to COVID-19, and did not reduce the salaries or wages of their employees by more than 25%.

The two applications allow borrowers the option of using either the extended 24-week covered period introduced in the Flexibility Act, or the original 8-week covered period if their loan was made prior to June 5, 2020.

Before starting an application, you should discuss with your lender what which one would be right for your business.

## What documents will be required for forgiveness?

While some lenders could have additional requirements, here are the documents you'll need:

- Verification of full-time equivalent employees and their pay rates, including:
  - Payroll reports.
  - Payroll tax filings (Form 941).
  - Payroll, income and unemployment insurance filings from your state.
- Verification of any health insurance and retirement contributions.
- Verification (payment receipts, account statements, canceled checks) of eligible utility, rent and mortgage interest payments.
- You'll need to certify that the documents are true and that you used the forgiveness amount to keep employees and make eligible utility, mortgage interest and rent payments.

## How do the loan numbers break down?

Small businesses were eligible to borrow 2.5 times their average monthly payrolls costs, but the amount could not exceed \$10 million. To maximize forgiveness, at least 60% of the loan must be used for payroll costs, plus health and retirement benefit costs.

The SBA and the Treasury Department have clarified some confusion about partial loan forgiveness under the Flexibility Act by stating that if a borrower uses less than 60 percent of the loan amount for payroll costs during the forgiveness covered period, the borrower will continue to be eligible for partial forgiveness, subject to at least 60 percent of the loan forgiveness amount having been used for payroll costs.

Up to 40% can be spent on approved expenses such as utilities, mortgage interest or rent. Any amount above this percentage will not count toward forgiveness.

Money used for other purposes will not qualify for forgiveness.

### **What eligible costs should I be tracking?**

**Payroll costs:** These costs include:

- Salary and wages (not to exceed \$100,000 for any individual employee as prorated during the covered period), commissions and other compensation.
- Cash tips
- Retirement contributions
- Parental, family, medical or sick leave
- Payments for vacation
- Group health care coverage, including insurance premiums
- Separation or dismissal allowance
- State and local payroll taxes

**Utilities:** You can include the costs of the following services if established before Feb. 15, 2020 – Electricity, water, gas, internet, telephone, and fuel costs for business vehicles.

**Mortgage interest:** If mortgage was signed prior to Feb. 15, 2020.

**Rent:** If leasing agreement was in effect prior to Feb. 15, 2020.

### **How should I record my expenses?**

You should keep careful records for all qualifying forgiveness expenses. While some experts advise converting all records to digital files, you should ask your lender how it prefers to receive documentation and plan accordingly.

### **What are the top considerations for PPP loan forgiveness?**

Employee retention and salaries or wages paid to employees are the primary considerations. It is important that you maintain your staff headcount and compensation levels to maximize loan forgiveness.

### **How will I know if I've met my staffing requirements?**

A reduction in the number employees will affect the amount of your loan forgiveness. You can take the number of full-time equivalent employees you had between either Feb. 15 and June 30, 2019, or Jan. 1 and Feb. 29, 2020, and compare that number to the number of FTEs you had during the covered 8-week period after your loan was funded. If during your coverage period you have equal to or more employees than your comparison period, that would meet the requirement for forgiveness. If you have fewer, your forgivable expenses will be reduced.

For seasonal businesses, you can use average monthly payroll for the period between Feb. 15, 2019, or March 1, 2019, and June 30, 2019. An applicant that was not in business from February 15, 2019 to June 30, 2019 may use the average monthly payroll costs for the period Jan. 1, 2020 through Feb. 29, 2020.

### **What if I need to rehire employees to qualify for loan forgiveness?**

You have until Dec. 31, 2020, to restore your full-time employment and meet compensation

requirements, but the new legislation offers an exception for borrowers who lose FTEs. It allows that if between Feb. 15 and Dec.31, 2020, the amount of loan forgiveness won't be reduced if the borrower, in good faith, is able to document any of the following circumstances:

- An inability to rehire someone who was an employee of the business on Feb. 15 or being unable to hire a similarly qualified person.
- The business was unable to return to the same level of activity as it was operating at before Feb. 15th due to compliance with requirements or guidance from Health and Human Services Department, the Centers for Disease Control and Prevention, or the Occupational Safety and Health Administration during the period between March 21 and Dec. 31, 2020, related to the maintenance of standards for sanitation, physical distancing, or any other worker or customer safety requirement related to COVID- 19.

### **What if I decreased employee wages?**

If an employee is earning \$100,000 annually or less and their pay is reduced by more than 25%, the amount of forgiveness will be reduced by the difference between their coverage period pay and 75% of their comparison period pay.

For example, if an employee was earning \$24,000 during the 24-week comparison period, but earns only \$15,000 during the PPP covered period you'd calculate it like this:

$$\$24,000 \times .75 = \$18,000$$

$$\$18,000 - \$15,000 = \$3,000 \text{ (not qualified)}$$

$$\$15,000 - \$3,000 = \$12,000 \text{ (forgivable amount)}$$

### **What happens if I'm not OK'd for PPP loan forgiveness?**

If you do not qualify for any forgiveness based on the documentation you provide, the amount of your outstanding PPP loan balance will need to be repaid over the term of the loan at a 1% interest rate from the time the loan was funded. Under the Flexibility Act, principal and interest are allowed to be deferred until the date the lender receives the forgiveness amount from the SBA.

### **My existing PPP loan is for two years, can that be changed?**

Yes, but it will be up to you and your lender. While new borrowers will have five years to repay their loans, previous borrowers only had two. The Flexibility Act allows that to be changed to five years if the lender and borrower agree.

### **What about forgiveness for sole proprietors and independent contractors?**

For your loan to be forgiven, you must have spent at least 60% of the funds on payroll costs, which include an amount for owner compensation based upon 2019 net earnings. The remaining amount, which cannot exceed 40% of the loan, must be spent on interest on a mortgage, a loan secured by personal property used in the business, rent, and utilities. To the extent that these expenses are incurred in connection with a home office, only the tax-deductible portion will apply. These expenses much have occurred within the 24 weeks after the loan is funded.

NOTICE: The information in this article is not definitive and requirements can change as new guidance is issued. As necessary, you should consult with your accountant, attorney or lender on questions regarding forgiveness of your PPP loan.

