

PPP Update

Washington Building Congress
February 17, 2021

Welcome



Chris Vasquez

Partner, Construction & Real
Estate



Bill Foote

Partner, Financial Advisory
Services

Agenda

- Introduction
- PPP and the Economic Aid Act
- 2nd Draw PPP Loans
- Forgiveness Applications
- Tax Considerations
- Accounting and Reporting
- Closing

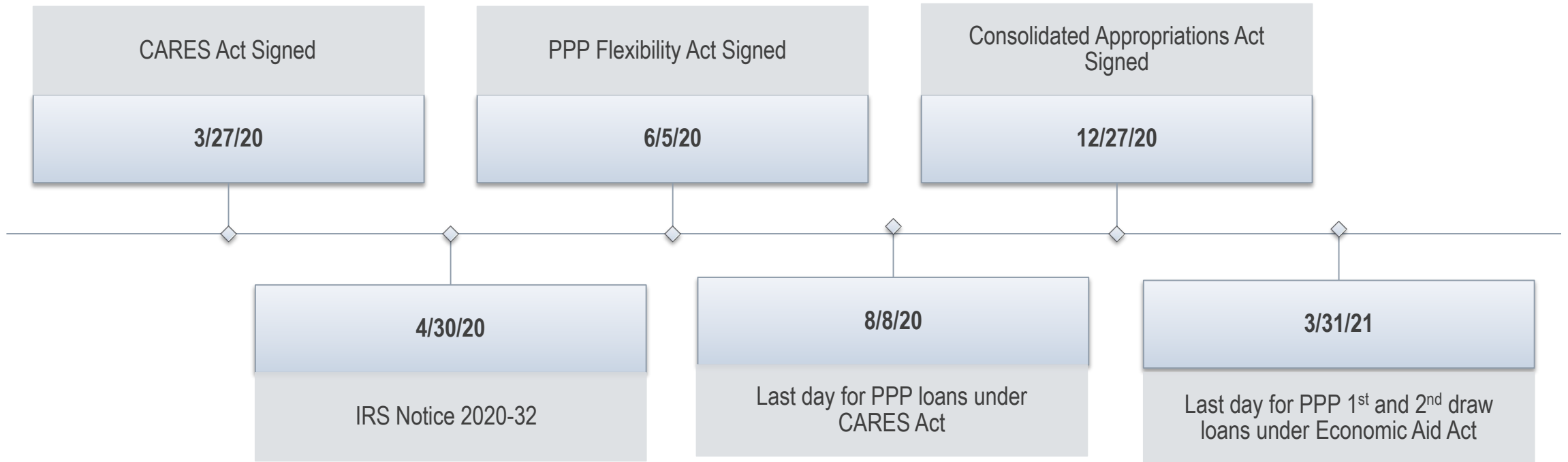


Introduction

PPP Overview

- Forgivable loan program established to assist small businesses nationwide adversely impacted by the COVID-19 emergency, by providing resources needed to:
 - maintain their payroll;
 - hire back employees who may have been laid off;
 - and cover applicable overhead.
- Five-year maturity
- 1.00% interest rate
- Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act (Economic Aid Act) added **\$284.5 billion** in PPP funding
- Continuation of 1st Draw PPP Loans
 - \$15 billion set aside for
 - borrowers with ≤ 10 employees; or
 - loans \leq \$250,000 to borrowers in low- or moderate-income neighborhoods
- Introduction of 2nd Draw PPP Loans
 - \$25 billion set aside for
 - borrowers with ≤ 10 employees; or
 - loans \leq \$250,000 to borrowers in low- or moderate-income neighborhoods

PPP Notable Dates





PPP and the Economic Aid Act

1st Draw and 2nd Draw PPP Loan Comparison

	1 st Draw PPP Loans	2 nd Draw PPP Loans
Maximum loan amount	<ul style="list-style-type: none"> • \$10,000,000 • \$20,000,000 for affiliated group 	<ul style="list-style-type: none"> • \$2,000,000 • \$4,000,000 for affiliated group
Borrower size	<ul style="list-style-type: none"> • ≤ 500 employees • ≤ 500 employees per location (NAICS 72) • SBA industry size standard 	<ul style="list-style-type: none"> • ≤ 300 employees • ≤ 300 employees per location (NAICS 72)
Maximum loan calculation	<ul style="list-style-type: none"> • Avg Monthly Payroll * 2.5 	<ul style="list-style-type: none"> • Avg Monthly Payroll * 2.5 • Avg Monthly Payroll * 3.5 (NAICS 72)
Avg Monthly Payroll calculation	<ul style="list-style-type: none"> • CY2019, CY2020, last 12 months 	<ul style="list-style-type: none"> • CY2019, CY2020, last 12 months
Gross receipts test	<ul style="list-style-type: none"> • Not applicable 	<ul style="list-style-type: none"> • ≥ 25% reduction in gross receipts

PPP Borrowers

- In operation as of February 15, 2021
- Expansion of eligible borrowers
 - Housing Cooperatives
 - Nonprofit News Organizations
 - Destination Marketing Organizations
 - 501(c)(6) Organizations
- Ineligible
 - Receive grant under the Shuttered Venue Operator Grant program
 - Entities directly or indirectly controlled by Pres., Vice Pres., head of an Exec. Dept. or Member of Congress (incl. spouses)
 - Entities listed on a national securities exchange
 - Permanently closed / not reopening



Excess Loan Amount Errors

- Some borrowers received PPP loan amounts > correct maximum loan amount under the CARES Act/Economic Aid Act due to **errors made in good faith**
- No forgiveness for amounts > correct maximum loan amount permitted by statute
- Does not matter whether excess loan amount caused by borrower error or lender error
- Borrower make payments on the excess loan amount
- Errors made in good faith \neq **knowing misstatements**
- Knowing misstatements may result in additional action (e.g., charges for fraud)

Documentation

- Gross Receipts Test (2nd Draw PPP Loans)
 - Financial statements, bank statements, tax returns
 - Loans < \$150,000, documentation not required until forgiveness application
 - For CY2020 to CY2019 comparison, “draft” 2020 federal income tax return (signed/dated)
- Average Monthly Payroll
 - Form 941 and state quarterly wage unemployment insurance tax reporting forms (or equivalent reports)
 - Evidence of any employer retirement and group insurance contributions
 - Partnerships would include IRS Form 1065 K-1
 - For 2nd Draw PPP Loans, if CY2019 payroll costs are used, borrower shouldn't need to resubmit this information provided (i) same lender and (ii) 1st Draw PPP Loan application was also based on CY2019 payroll costs



2nd Draw PPP Loans

Maximum Loan Amount

- 2.5 times average monthly payroll costs, up to \$2,000,000
- 3.5 times average monthly payroll costs, up to \$2,000,000 (NAICS 72)
- Average Monthly Payroll can be based on CY2019, CY2020, or the 12-month period prior to when the loan is made
- Payroll costs include:
 - Gross wages and salaries
 - Employer-paid health insurance (group health, life, disability, dental and vision)
 - Employer-paid retirement benefits
 - Employer-paid state and local payroll taxes
- Payroll costs do not include:
 - Cash compensation > \$100,000 on an annualized basis
 - Compensation to non-US residents

Gross Receipts – Definition

- Gross receipts includes:
 - Sales (net of returns and allowances)
 - Rental income
 - Interest/dividend income
 - Commissions income
- Gross receipts does not include:
 - Sales to affiliates
 - Capital gains/losses
 - Sales taxes
 - Amounts collected for another
 - Forgiveness on 1st Draw PPP Loans

Gross Receipts – Measurement

- Measurement periods
 - Comparison of calendar quarters ($\geq 25\%$ reduction)
 - Q1 2020 to Q1 2019
 - Q2 2020 to Q2 2019
 - Q3 2020 to Q3 2019
 - Q4 2020 to Q4 2019
 - Comparison of calendar year 2020 to calendar year 2019 ($\geq 25\%$ reduction)
- Measurement technique
 - Accrual basis vs. cash basis
 - Period-to-period consistency
 - Consistency with income tax returns



Forgiveness Applications

Application Forms

Form 3508

- PPP Loan Forgiveness Calculation Form
- Representations and Certifications
- PPP Schedule A
- PPP Schedule A Worksheet
- PPP Borrower Demographic Information Form (Optional)

Form 3508EZ

- PPP Loan Forgiveness Calculation Form
- Representations and Certifications
- PPP Borrower Demographic Information Form (Optional)

Form 3508S

- Representations and Certifications
- PPP Borrower Demographic Information Form (Optional)

Forgivable Costs

Legacy Forgivable Cost Categories

- Payroll Costs
 - Cash compensation
 - \$100,000 annualized limit
 - Owner-employee limits
 - Non-cash compensation
 - Employer-paid group insurance
 - Employer-paid retirement benefits
 - Employer-paid state/local payroll taxes
- Non-Payroll Costs
 - Rent
 - Utilities
 - Mortgage interest

Expanded Forgivable Cost Categories

- Covered operations expenditures
- Covered property damage costs
- Covered supplier costs
- Covered worker protection expenditures

- Employer-paid group insurance can include **life** and **disability** insurance (i.e., in addition to medical, dental, vision)

Forgiveness Amount Calculation

Form 3508

Forgiveness Amount Calculation:

Payroll and Nonpayroll Costs

Line 1. Payroll Costs (enter the amount from PPP Schedule A, line 10):

Line 2. Business Mortgage Interest Payments:

Line 3. Business Rent or Lease Payments:

Line 4. Business Utility Payments:

Line 5. Covered Operations Expenditures:

Line 6. Covered Property Damage Costs:

Line 7. Covered Supplier Costs:

Line 8. Covered Worker Protection Expenditures:

Adjustments for Full-Time Equivalency (FTE) and Salary/Hourly Wage Reductions

Line 9. Total Salary/Hourly Wage Reduction (enter the amount from PPP Schedule A, line 3):

Line 10. Sum the amounts on lines 1 through 8, then subtract the amount entered in line 9

Line 11. FTE Reduction Quotient (enter the number from PPP Schedule A, line 13):

Potential Forgiveness Amounts

Line 12. Modified Total (multiply line 10 by line 11):

Line 13. PPP Loan Amount:

Line 14. Payroll Cost 60% Requirement (divide line 1 by 0.60):

Forgiveness Amount

Line 15. Forgiveness Amount (enter the smallest of lines 12, 13, and 14):

Form 3508EZ

Forgiveness Amount Calculation:

Payroll and Nonpayroll Costs

Line 1. Payroll Costs:

Line 2. Business Mortgage Interest Payments:

Line 3. Business Rent or Lease Payments:

Line 4. Business Utility Payments:

Line 5. Covered Operations Expenditures:

Line 6. Covered Property Damage Costs:

Line 7. Covered Supplier Costs:

Line 8. Covered Worker Protection Expenditures:

Potential Forgiveness Amounts

Line 9. Sum the amounts on lines 1 through 8:

Line 10. PPP Loan Amount:

Line 11. Payroll Cost 60% Requirement (divide Line 1 by 0.60):

Forgiveness Amount

Line 12. Forgiveness Amount (enter the smallest of Lines 9, 10, and 11):

Form 3508EZ Eligibility

- The Borrower did not reduce annual salary or hourly wages of any employee by more than 25 percent during the Covered Period compared to the most recent full quarter before the Covered Period. (For purposes of this statement, “employees” means only those employees that did not receive, during any single period during 2019, wages or salary at an annualized rate of pay in an amount more than \$100,000.);

AND

The Borrower did not reduce the number of employees or the average paid hours of employees between January 1, 2020 and the end of the Covered Period.

- Ignore reductions that arose from an inability to rehire individuals who were employees on February 15, 2020 if the Borrower was unable to hire similarly qualified employees for unfilled positions on or before December 31, 2020 (or, for a PPP loan made after December 27, 2020, the last day of the Covered Period).
- Also ignore reductions in an employee’s hours that the Borrower offered to restore and the employee refused. See [85 FR 33004](#), 33007 (June 1, 2020) for more details.

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- The Borrower did not reduce annual salary or hourly wages of any employee by more than 25 percent during the Covered Period compared to the most recent full quarter before the Covered Period. (For purposes of this statement, “employees” means only those employees that did not receive, during any single period during 2019, wages or salary at an annualized rate of pay in an amount more than \$100,000.);

AND

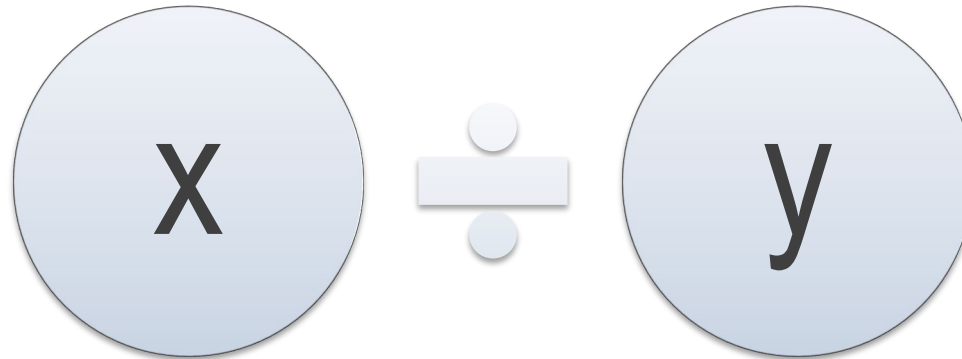
The Borrower was unable to operate during the Covered Period at the same level of business activity as before February 15, 2020, due to compliance with requirements established or guidance issued between March 1, 2020 and December 31, 2020 (or, for a PPP loan made after December 27, 2020, requirements established or guidance issued between March 1, 2020 and the last day of the Covered Period) by the Secretary of Health and Human Services, the Director of the Centers for Disease Control and Prevention, or the Occupational Safety and Health Administration, related to the maintenance of standards of sanitation, social distancing, or any other work or customer safety requirement related to COVID-19.

Document Retention Period

- Borrower must keep all records for **6 years** after the date the loan is forgiven or repaid in full
- Borrower must permit authorized representatives of SBA to access these records upon request

FTE Reduction Quotient

- Loan forgiveness otherwise available may be reduced based upon the quotient of $x \div y$
- x = the average number of non-owner FTEs per week during the covered period
- y = the average number of non-owner FTEs per week during either:
 - the period beginning 2/15/19 and ending 6/30/19; **or**
 - the period beginning 1/1/20 and ending 2/29/20



Safe Harbors

- Safe Harbor 0 – no reduction to the **number of employees** or the average paid hours of your employees between 1/1/20 and the end of the covered period
- Safe Harbor 1 – unable to operate between 2/15/20 and the end of the covered period at the same level of business activity as before 2/15/20 due to compliance with ...
- Safe Harbor 2 –
 - Borrower reduced FTE levels in the period beginning 2/15/20 and ending 4/26/20; **and**
 - Borrower then restored FTE levels to its FTE employee levels in the Borrower's pay period that included 2/15/20

Exceptions

- Positions for which the Borrower made a good-faith, written offer to rehire an individual who was an employee on February 15, 2020 and the Borrower was unable to hire similarly qualified employees for unfilled positions
- Positions for which the Borrower made a good-faith, written offer to restore any reduction in hours, at the same salary or wages, during the covered period and the employee rejected the offer
- Any employees who during the covered period
 - were fired for cause;
 - voluntarily resigned; or
 - voluntarily requested and received a reduction of their hours

PPP Loans and SBA Review

- Loans \geq \$2,000,000
 - Expect full reviews prior to forgiveness after the lender submits the application to SBA
 - Necessity questionnaire required to be completed
- Loans $<$ \$2,000,000
 - “SBA may review at any time” using its discretion
 - Not considered an “automatic” review by SBA
 - No requirement to complete necessity questionnaire
- Loans $<$ \$150,000
 - Short application; reduced risk of review



Tax Considerations

Treatment of Forgiveness and Forgivable Costs

- Cancellation of Debt (“COD”) income is the general rule for debt forgiveness
- PPP loan forgiveness is an exception to the general rule
- PPP loan forgiveness does not constitute taxable income
- IRS Notice 2020-32 (April 30, 2020)
 - Expenses paid using PPP proceeds are **not** deductible for federal tax purposes to the extent that the loan is forgiven
- Revenue Ruling 2021-02 (January 6, 2021)
 - Recognizes Economic Aid Act
 - Expenses paid using PPP proceeds **are deductible** for federal tax purposes

Other Tax Considerations

- Section 199A (QBI) inter-play for pass-through entities
- Non-taxable forgiveness will increase partner/shareholder basis
- State tax matters
- Employee Retention Credit (ERC) in tandem with PPP



Accounting and Reporting

GAAP Accounting for PPP Loan Forgiveness

There are multiple options to account for PPP loans. All can be used.

- Accounted for as debt under ASC 470.
- Accounted for as government assistance by analogy to other guidance:
 - *International Accounting Standards (IAS) 20, Accounting for Government Assistance.* (for-profits only)
 - *ASC 958-605, Accounting for Contributions Received.*
- ASC 450-30, *Gain Contingencies.*

Note: No matter the method chosen, management should disclose the accounting method and policy used for material amounts.

ASC 470, Debt

Any entity can use this accounting method for **initial receipt of loan**.

- Recorded as normal debt: **Debit: Cash, Credit: PPP loan liability**.
- Classify entire amount of loan as a long-term liability by default. **However**, entity may make accounting policy election to classify as short term if intend is to apply for forgiveness.
- If material, present as a separate line item, not combined with other loans.
- Record interest expense as incurred, and likely not material. No need to impute interest.

For-profit companies can also use ASC 470 for **forgiveness of loan**.

- When notification of loan forgiveness is obtained, record as **debt extinguishment**.
 - Debit to PPP loan liability
 - Credit to Extinguishment gain
- Nonprofits must recognize a **contribution upon loan forgiveness**, not as a gain.

Remember: This is the easiest option!

PPP Loan Forgiveness under IAS 20

By drawing analogy to IAS 20, for-profit businesses can account for a PPP loan as follows:

- Upon loan receipt, deferred income is recognized.
- As qualifying payroll and other costs are incurred. Grant income is recognized to reflect amounts expected to be forgiven.
 - **Grant income** can take the form as a separate credit line on the income statement or be combined under a general heading, such as **other income**.
 - Alternatively, income can be recorded as a reduction to related expenses.
- Standard to recognize revenue is **reasonable assurance**—analogous to **probable** in U.S. GAAP under FASB ASC 450-20-20—that the entity will meet the terms for forgiveness.



PPP Loan Forgiveness under ASC 958

NFP guidance under ASC 958-605 may be **applied by all entities**.

- Loan receipt may be **initially** recorded as a conditional contribution with a journal entry to **Debit: Cash** and **Credit: Refundable advance**.
- Contribution revenue is recognized as conditions are **substantially met**, that is, forgiveness is obtained as qualifying expenses under program are incurred.

Substantially met: higher standard (ASC 958) vs. probable: lower standard (IAS 20).

Remember to consider all conditions like **FTE** and **hour reductions**, because they might **reduce amount forgiven**.



Closing



Additional Resources

- Aronson LLC
 - <https://aronsonllc.com/industry/construction-and-real-estate/>
 - <https://aronsonllc.com/service/covid-19-resources/>
- Treasury/SBA PPP sites:
 - <https://home.treasury.gov/policy-issues/cares/assistance-for-small-businesses>
 - <https://www.sba.gov/page/coronavirus-covid-19-small-business-guidance-loan-resources>
 - <https://www.sba.gov/document/procedural-notice-5000-20078-paycheck-protection-program-excess-loan-amount-errors>
 - <https://home.treasury.gov/system/files/136/PPP--Loan-Forgiveness-Application-and-Instructions--Form-3508-1192021.pdf>
 - <https://home.treasury.gov/system/files/136/PPP--Loan-Forgiveness-Application-Instructions--Form3508EZ-1192021.pdf>
 - <https://home.treasury.gov/system/files/136/PPP--Loan-Forgiveness-Application-Instructions--Form-3508S-1192021.pdf>

Contact Us

Bill Foote



301.231.6299



wfoote@aronsonllc.com

Chris Vasquez



301.231.6244



cvasquez@aronsonllc.com

Let Us Know How We Can Help!

- Debt restructuring
- PPP loan forgiveness and accounting considerations
- NOL carryback analysis
- Forecasts and scenario analysis
- Business interruption claims
- Distressed M&A due diligence
- Impairment analyses

COVID-19 Advisory Services



Aronson LLC is deeply committed to helping you navigate the uncharted waters of COVID-19 and the financial emergencies that lie beneath the surface. Our dedicated team is available to help you understand recent government stimulus packages and address the economic impacts of the evolving coronavirus outbreak to your business or organization.



Evaluating Financing Options

- Paycheck Protection Program (PPP)
- Economic Injury Disaster Loan (EIDL) Program
- State and local relief programs
- Restructuring existing debt



Quantifying Stimulus Tax Benefits

- PPP loan forgiveness and accounting considerations
- Employee retention tax credit
- Payroll tax deferral
- NOL carryback analysis



Formulating Financial Strategies

- Financial ratios and covenants calculations
- Near-term cash flow budgets and working capital analysis
- Longer-term forecasts and scenario analysis
- Cost-containment initiatives
- Business interruption and other claims



Supporting Transactions

- Distressed M&A due diligence
- Quality of earnings and adjusted EBITDA analysis
- Post-acquisition disputes



Reconsidering Business and Asset Valuations

- Impairment analyses
- Estate, gift and trust valuations
- 409A valuations

For questions about these services, contact our COVID-19 Advisory team at 301.231.6200 or info@aronsonllc.com. To learn more visit our resource hub at aronsonllc.com/service/covid-19-resources.

Industry Focuses



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