

# How to Prepare for Paycheck Protection Loan Forgiveness

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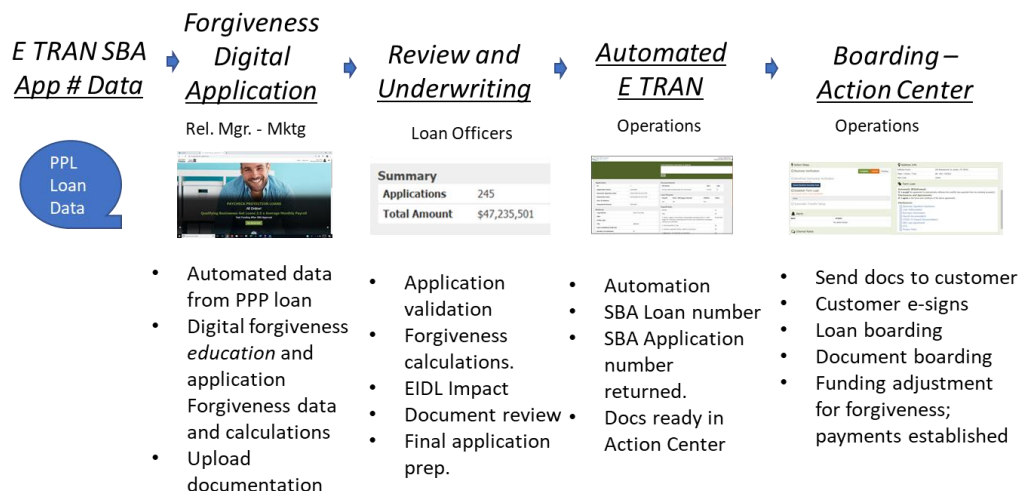
Many who have received Paycheck Protection Loans are eager to know how to apply for the forgiveness component of these of these loans. Ambiguity still exists as specific guidance from the SBA has still not been released. Here is what bankers and borrowers might expect based on current information.

## For Bankers Concerning PPP Forgiveness

Bankers are in the business of helping their customers. However, the lack of SBA guidance on how forgiveness of PPP loans will work leaves a frustrating lack of clarity that bankers cannot remedy. Bankers are advised to acknowledge we are all waiting for guidance, and:

- Avoid making statements that suggest that the rules for forgiveness assessment are settled.
- Recommend that customers consult their other trusted advisors (accountants and lawyers) for guidance in formulating strategies to achieve optimal loan forgiveness.
- Ensure that any guidance provided clearly indicates that the standards are unsettled and that the bank is in no position to opine on how the law will ultimately be interpreted.
- Suggest best practices that will be useful regardless of how the law is ultimately interpreted (record keeping, account segregation, types of records likely needed to demonstrate compliance with forgiveness standards); and
- Reference to relevant government issued rules and guidance.

While we wait for SBA information, we can plan logically the following process for Forgiveness:



A priority for bankers is to address quickly the week 7 forgiveness option. The Cares Act allows a lender or borrower to request that the SBA purchase the expected forgiveness amount of a PPP loan or pool of PPP loans at the end of **week seven** of the covered period.

The expected forgiveness amount is the amount of loan principal the lender and borrower reasonably expect the borrower to expend on payroll costs, covered mortgage interest, covered rent, and covered utility payments during the eight-week period after loan disbursement.

- At least 75 percent of the expected forgiveness amount shall be for payroll costs, as provided in 2.o. To submit a PPP loan or pool of PPP loans for advance purchase, a lender shall submit a report requesting advance purchase with the expected forgiveness amount to the SBA.
  
- The report shall include:
  - the Paycheck Protection Program Application Form (SBA Form 2483) and any supporting documentation submitted with such application,
  - the Paycheck Protection Program Lender’s Application for 7(a) Loan Guaranty (SBA Form 2484) and,
  - any supporting documentation, a detailed narrative explaining the assumptions used in determining the expected forgiveness amount,
  - the basis for those assumptions, alternative assumptions considered, and why alternative assumptions were not used,
  - any information obtained from the borrower since the loan was disbursed that the lender used to determine the expected forgiveness amount, which should include the same documentation required to apply for loan forgiveness such as payroll tax filings, cancelled checks, and other payment documentation; and any additional information the Administrator may require to determine whether the expected forgiveness amount is reasonable.

***The CARES Act does not require that banks offer week seven forgiveness, and our recommendation is that banks for the protection of their customers and themselves forego week seven forgiveness options until more information is available.***

Finally, bankers should provide as soon as possible communication on forgiveness at a forgiveness application website. This website will not have the application yet since much is undefined by the SBA but can provide initial definitions of process and options. Further, it can provide recommendations for “other expenses” which may be unclear, such as the percent of utility bills applicable to a home business when the bill is bundled in a package.

A preliminary application website would provide a source to refer customers to for a consistent set of comments and information about forgiveness, or a script for team members or a call center.

## For Borrowers Concerning PPP Forgiveness

This section for borrowers is presented in two parts: A. Review of Paycheck Protection Rules and Ambiguities which is meant to assist in understanding the confusion about forgiveness, and B. Preparing for Forgiveness, the steps borrowers can use to prepare for forgiveness.

### I. Review of Paycheck Protection Rules and Ambiguities

For businesses, sole proprietors and self-employed individuals, the Paycheck Protection Program allows loans equal to 2.5 times monthly allowable payroll and related expenses. Components of these loans may be forgivable if the proceeds are used for allowable payroll, rent, interest and utilities over the eight-week period following the receipt of the loan. Certain limitations exist such as 75% of the funds to be forgiven must be used for payroll.

The American Institute of CPAs, AICPA, has reviewed the ambiguities of PPP forgiveness, and is making [the following broad recommendations](#) for the PPP application and forgiveness process. ***We have no knowledge if these will be accepted.***

- The eight-week covered period under PPP should align with the beginning of a pay period, not the date loan proceeds are received.
- The eight-week period should be flexible, with businesses able to choose to commence it once stay-at-home restrictions are lifted instead of when loan proceeds are received.
- Full-time equivalents (FTEs) should be calculated using a simple wage-based proxy when hours worked are not tracked by the employer (e.g., for salaried workers or those paid by piece).
- Payroll reduction calculations should be based on an employee's average payroll per week in the eight-week period compared to the prior quarter, rather than comparing total compensation in the periods. Loan forgiveness is reduced if an employee's compensation decreases by more than 25% but an eight-week period will naturally have 33% less payroll than a 12-week quarter.

These recommendations reflect the confusion about exactly how forgiveness may happen. The lack of clarity is particularly well defined by [Evergreen Small Business](#) and summarized below.

- A. The 8-week period for forgiveness immediately after funding occurs while many states are still in quarantine, making use of funds more challenging.
- B. Headcount reduction or pay rate reduction during the 8-week period after the receiving the loan could limit forgiveness.
- C. The re-hire window is limited and leaves open what to do with re-hires after 8 weeks.
- D. The 25% non-payroll costs limitation and failing to spend at least 75% on payroll may present challenges.
- E. Self-employed individuals and sole proprietors are likely limited to 75% loan forgiveness by SBA rules.
- F. Documentation is critical and not fully clarified.

Our next section provides likely documentation required for forgiveness by entity type for your preparation with thanks to AICPA, no specific guidance exists.

## II. Preparing for Forgiveness

### A. Loan forgiveness documentation for corporations, LLCs and partnerships.

1. **Payroll tax reports:** 2020 IRS Forms 941, state income and unemployment tax returns that include the 8-week covered period. (See recommendation below regarding 8-week covered period.) If your organization contracts with a payroll provider or Professional Employer Organization (PEO) you can supply other documents, such as reports reflecting employment tax returns filed.
2. **Compensation and FTEs:** In general, payroll reports which will include the following:
  - a. Gross wages for each employee for the following:
    - i. During the 8-week covered period
    - ii. During the most recent full quarter before the 8-week covered period
  - b. Identifying employees who during any period in 2019, received an annualized pay of more than \$100k and also employees whose principal place of residence is outside the U.S.
  - c. State and local employer taxes assessed on an employee's compensation (i.e. SUTA) during the 8-week covered period

- d. The average number of full-time equivalents (FTEs) per month for the following:
  - i. During the 8-week covered period
  - ii. Feb. 15 through June 30, 2019
  - iii. Jan. 1 through Feb. 29, 2020

Note: borrower elects which period, ii or iii, to compare to i

3. **Group health care benefits:** Documentation showing total costs paid for all health care benefits, including insurance premiums paid by the organization under a group health plan. a. Include all employees and company owners. b. Do not include employee withholdings for their portion of contributions to the plan.
4. **Retirement plan benefits:** Documentation showing the sum of all retirement plan funding costs paid by the organization.
  - a. *Include funding for all employees* and the company owners.
  - b. Do not include employee withholdings for their portion of contributions to the plan.
5. **Other documentation:** Canceled checks, receipts, account statements or other documentation of payment for other eligible costs incurred and paid during the covered period such as mortgage interest, lease payments, utility payments.

**B. For Sole Proprietors Having More Than One Employee**

1. The 2019 Form 1040 Schedule C to verify net income (line 31) for owner income replacement calculation.
2. Provide payroll documentation including 2020 IRS Forms 941, state income and unemployment tax returns that include the 8-week covered period, including documentation of healthcare and retirement benefits costs. Exclude owner from healthcare and retirement costs.
3. Canceled checks, receipts, account statements or other documentation of payment for other eligible costs incurred and paid during the covered period such as mortgage interest, lease payments, utility payments. Note: these types of expenses must have been deducted on the 2019 Form 1040 Schedule C to be eligible for forgiveness.

**C. For Sole Proprietors Having One Employee, 1099 Provider or Self-Employed**

1. For individuals with self-employment income who file a Schedule C (for farmers Schedule F, line 34) or a 1099, the Administrator, in consultation with the Secretary, has determined that it is appropriate to limit loan forgiveness to a proportionate eight-week share of 2019 net profit or 1099, as reflected in the individual's 2019 Schedule C (for farmers Schedule F, line 34) or a 1099. You will only be eligible for about 74% of your loan to be forgiven, although final guidance may allow you to round this to 75%.
2. To illustrate this, if your 2019 Schedule C or 1099 shows exactly \$52,000 of profit or income in 2019, so you earned \$4,000 a month and \$923 a week in 2019.
3. Your loan likely equaled 2.5 times \$4,000, or \$10,000. But forgiveness equals 8 weeks times \$923 per week, or \$7,384. You will want to provide your 2019 Schedule C or 1099 as documentation for profit last year, and your payroll records and/or cancelled checks showing you paid yourself the \$7,384 during the eight-week forgiveness period. Sole proprietors and self-employed might be able to pay themselves at a higher rate during the 8-week forgiveness period to achieve full forgiveness of the loan.