



# SIMMS SHOWERS LLP

A PARTNERSHIP OF PROFESSIONAL CORPORATIONS

305 Harrison Street, S.E., 3<sup>rd</sup> Floor, Leesburg, Virginia 20175 ■ (703)771-4671 ■ Fax: (703)771-4681 ■ [www.simmsshowerslaw.com](http://www.simmsshowerslaw.com)

## Forgiveness and Audits of Paycheck Protection Program Loans

*By William R. Thetford, Esq. and H. Robert Showers, Esq.*

Last Updated: May 29, 2020.

*Note: This is the subject of a rapidly evolving landscape. Please stay tuned for updates as they become available.*

The Small Business Administration (SBA), in consultation with the United States Treasury, has released the [application](#) for forgiveness of loans under the Paycheck Protection Program (PPP) and followed the application with two much anticipated Interim Final Rules. One regarding the process for [PPP loan forgiveness](#) and the second for the SBA's [auditing and review procedures](#). **We discuss the application and the Interim Final Rules at length below.** For more information or to ask questions about these subjects, please take advantage of the **webinars** we will be hosting next week to strategize how businesses, churches, and nonprofit organizations can make sure they do not run afoul of the many regulations and remain eligible to maximize their loan forgiveness. See [www.simmsshowerslaw.com](http://www.simmsshowerslaw.com) for dates and times of webinars.

### Forgiveness of PPP Loans

Employers, both in the for-profit and nonprofit world, have suffered through a number of uncertainties involved with COVID-19 and the emergency pieces of legislation surrounding it, including the CARES Act and its flagship program the Paycheck Protection Program (PPP). Questions inevitably arise from major pieces of legislation and the CARES Act is no different, especially given the short timetable in which it had to be drafted and implemented. It was followed by now ***fourteen Interim Final Rules by the SBA and Treasury Department as well as frequently evolving guidance documents***. Fortunately, the long-awaited guidance from the SBA and Treasury has been released to assist employers who have received forgivable PPP loans to actually navigate the loan forgiveness process.

We consider the process in four steps:

Step 1: Plan spending to ensure it meets general threshold for forgiveness; at least 75% of amount allocated towards payroll costs (First Portion of the SBA Forgiveness Application).

Step 2: Calculate Potential Reductions and Exceptions from General Forgivable Amount in Step 1 (Second Portion of the Application and included Schedule and Worksheet).

Step 3: Gather Required Documentation

Step 4: Submit PPP Loan Forgiveness Application.

## **Step 1: Plan and manage spending for maximum loan forgiveness.**

The first step to determining loan forgiveness is to plan and account for how the proceeds are spent during the 8 week covered period. We advised many of our clients to put their loan proceeds in a separate bank account from their other funds to track how these are spent more easily.

- A. The first threshold a borrower must hit for full forgiveness is that at least 75% of the loan proceeds must be spent on payroll costs during that period.

Under the CARES Act and the associated guidance payroll, costs include:

- Salary, wage, commission, or similar compensation to employees (now including hazard duty pay and certain bonuses according to most recent IFR) up to a maximum of \$100,000 per year prorated to the covered period (\$15,385 for the eight-week period)
  - This also includes a minister's housing stipend or allowance.
- Payment of cash tip or equivalent;
- Payment for vacation, parental, family, medical, or sick leave;
- Allowance for dismissal or separation;
- Payment required for provision of group health care benefits, including insurance premiums;
- Payment of any retirement benefit;
- Payment of State or local tax assessed on the compensation of employees; or
- Wages paid to the employee typically withheld for *employee* portion of employment taxes ("payroll costs are not reduced by taxes imposed on an employee and required to be withheld by the employer, but payroll costs do not include the employer's share of payroll tax").<sup>1</sup>

**Payroll costs do not include:** compensation over \$100,000 on an annualized basis, compensation to employees whose principal place of residence is outside the United States, employer portion of FICA taxes (social security and Medicare), payments to independent contractors (contractors must apply in their own right for PPP loan), and qualified sick leave or family leave wages for which credit is allowed under the Families First Coronavirus Response Act.

The remaining 25% of the PPP loan proceeds may be spent on certain other payments if the obligation was incurred before February 15, 2020 (1) business mortgage interest (prepayment of interest and any payment of principal is ineligible), (2) rent payments, and (3) business utility payments: electricity, gas, water, transportation, telephone, internet access, for which service began prior to February 15, 2020.

Any portion of the PPP loan proceeds that are (1) spent on anything other than the allowable purposes or (2) not in fact spent will not be forgiven but converted into an SBA loan at 1% interest to be paid in two years.

- B. Covered period begins on the date of disbursement or first payroll period start date thereafter.

When must the payroll costs be paid or incurred? Generally, to be eligible the payroll and other costs must be paid during the covered period. However, one of the questions that remained unanswered until recently was how to handle payroll costs that fell partially, but not fully within the covered period? Under a literal reading of the CARES Act, the covered period (currently eight weeks or 56 days) for reviewing how PPP expenses were spent invariably began on the date of the disbursement of the loan, and thus, it would be difficult to attribute payroll costs paid in the payroll period, but earned in a previous period and vice versa.

---

<sup>1</sup> SBA, Paycheck Protection Program FAQs, Question 16, [https://www.sba.gov/sites/default/files/2020-05/Paycheck-Protection-Program-Frequently-Asked-Questions\\_05%2027%2020.pdf](https://www.sba.gov/sites/default/files/2020-05/Paycheck-Protection-Program-Frequently-Asked-Questions_05%2027%2020.pdf) (last visited May 29, 2020).

Thankfully, the [application](#) and [Interim Final Rule on Forgiveness](#) announced that the borrower will have the choice between a review period (“covered period”) beginning on the date of disbursement OR the date the first payroll period begins after the disbursement (“alternative covered period”).

*Example:* If Employer A’s loan was disbursed on Wednesday April 8, 2020, towards the end of its regular two-week payroll period, the Employer may consider Monday April 13 to be the start date to coincide with the payroll period beginning that day.

The alternative covered period will probably be more convenient for most borrowers. The important thing to remember is to keep all calculations consistent for one or the other of the periods regardless of which method you elect to use.

Payroll costs paid during the covered period or alternative covered period are eligible. Certain other payments may qualify if they are incurred within the covered or alternative covered period, even if paid thereafter. For instance, though payroll costs are considered paid on the day borrowers pay their employees, payments made to employees outside the payroll period are also eligible for counting towards your forgivable payroll costs if the payment was made on the (1) next regular payroll date following the expiration of the covered period (or alternate covered period) for (2) work employees performed within the covered period.

*Example:* Employer A utilizes a bi-weekly pay period, with a new period beginning April 13. Because it chose the alternative payroll covered period beginning April 13 rather than the disbursement date of April 8, the end of the eight weeks would be June 7, 2020. However, paychecks for the week concluding June 7 are not issued until June 12, following the typical administrative and payroll schedule, and thus are paid outside of the alternative covered period. They are paid on the first regular payroll date thereafter. Are these payments still eligible to be reported as forgivable payroll costs? **Yes. According to the SBA’s Interim Final Rule, these payments will also be forgivable payroll costs to submit in the application.**

Non-payroll costs are eligible for forgiveness if it was either (i) paid during the covered period OR (ii) “incurred during the covered period and paid on or before the next regular billing date, even if the billing date is after the covered period.” The following example from the SBA Interim Final Rule is instructive.

*Example:* A borrower’s covered period begins on June 1 and ends on July 26. The borrower pays its May and June electricity bill during the covered period and pays its July electricity bill on August 10, which is the next regular billing date. The borrower may seek loan forgiveness for its May and June electricity bills, because they were paid during the covered period. In addition, the borrower may seek loan forgiveness for the 13 portion of its July electricity bill through July 26 (the end of the covered period), because it was incurred during the covered period and paid on the next regular billing date.<sup>2</sup>

It is important to note that Congress is currently considering, but has not yet passed, legislation extending the eight week review period to a longer period which will make it easier for borrowers to get 100% of their loans forgiven.<sup>3</sup>

---

<sup>2</sup> Small Business Administration and Treasury Department, Interim Final Rule, Requirements for Loan Forgiveness, at 12, <https://home.treasury.gov/system/files/136/PPP-IFR-Loan-Forgiveness.pdf> (“Forgiveness Interim Final Rule”).

<sup>3</sup> Anne Sraders, *House passes bill to extend 8-week period to spend PPP loans and alter 75% rule*, FORTUNE, (May 28, 2020) <https://fortune.com/2020/05/28/house-bill-ppp-extension-8-weeks/>.

### C. Important Qualifiers in the First Stage Calculations

The wages of **owner employees** are capped at the lesser of (1) 8/52 times 2019 compensation (in other words, the average eight weeks of 2019) or (2) capped at \$15,385 across all businesses (the amount you would receive for an average eight week period if you earned the maximum \$100,000 for the year.)

Compensation paid by employers to employees (salary, wages, or commissions) even though employees are furloughed or unable to perform their day-to-day duties, whether due to lack of economic demand or public health considerations, is also forgivable.

The total you spent on applicable costs noted above, so long as the 75% requirement is met, is the maximum amount of payroll that may be forgiven. Once this number is calculated, enter this information on the application and proceed to the second stage of the analysis to see if this number is reduced by any of the following rules.

#### **Step 2: Calculate any reductions (or exceptions) to the general eligible forgivable amounts.**

At this stage in the calculation, you should utilize the [application](#) and included worksheets to determine any extent your overall PPP eligible forgivable proceeds may be reduced in accordance with the following qualifications and exceptions. In this step, there are two more ways that your forgiveness may be reduced: if you experience a decline in full-time equivalent employees (aggregate basis) or wages (per employee-basis).

##### A. Borrowers must first calculate the difference of full-time equivalent employees (FTE) before (“reference period”) and after the COVID-19 economic impacts and implementation of the PPP (covered period).

A full-time equivalent employee (FTE) is an employee who works 40 hours or more, on average, each week. The standard calculation is the average number of hours per week divided by 40. Thus, a full-time employee counts as 1.0 FTE (someone paid more than an average of 40 hours per week is still only 1.0 FTE).

The total amount of forgiveness will be multiplied by the quotient of the average number of FTEs in the reference period divided by the average number of FTEs in the covered period. Thus, a 10% reduction in FTEs will result in a 10% reduction in the loan forgiveness amount.

To ensure the highest forgiveness, follow the following steps in calculating your FTE differential.

- i. Calculate FTEs on the basis of each of the potential reference periods which best suits you for forgiveness of loans.*

Employers/borrowers have the option to choose from among three reference periods for the “before” snapshot of FTEs.

- February 15, 2019 through June 30, 2019 (roughly same time period as last year).
- January 1, 2020 through February 29, 2020 (this year before the COVID-19 emergency).
- Seasonal employers have an additional option to choose a 12-week reference period between May 1, 2019 and September 15, 2019

If your FTE numbers are the same or higher now than in the reference periods, this rule will not reduce your loan forgiveness. If your FTEs are lower now than under the reference periods, pick the reference period with the smallest number of FTEs to minimize loss and maximize loan forgiveness.

ii. Next, borrowers may also choose between two ways of calculating FTEs in any reference period.

The traditional way of calculating FTEs is taking the average number of hours worked per week and dividing by 40.<sup>4</sup> Thus, under this method, an employee who works 30 hours per week would be considered 0.75 of an FTE.

For ease of calculation or if exact hours are unknown, the SBA has also allowed a second way of borrowers calculating their FTEs. Under this second method all full-time employees are 1.0 FTE and all part-time employees are 0.5 regardless of hours worked.

Since the method you choose must be applied to both the reference period and the covered period, the choice of method will probably not make a drastic difference in the ultimate amount of forgiveness for most borrowers. However, there are cases that it may be to your advantage to choose one method over the other. For instance, a 30 hour a week employee will be the same as a 10 hour a week employee under the second approach. If you are a borrower/employer that had to reduce the hours of your full-time employees to approximately 30 hours a week, utilizing the second method will make your FTE reduction look larger than it actually is and result in a larger loss of forgiveness. By contrast, utilizing the second method is to your advantage if any reduced hours were concentrated in those who were already part time (since all part time employees are counted as 0.5 FTEs). Since SBA gives you the option, we recommend running the numbers both ways in case one presents a better opportunity for your organization.

iii. Calculate FTE Reduction Amount

Once you choose your reference period and method of calculating FTEs, run the final calculation and you will know the extent to which FTEs may reduce your forgiveness amount. If you experience a reduction or you anticipate that you will, see the exceptions in Section C below.

#### B. Calculate the Difference in Wages

Generally, a reduction in an employee's salary or wages that is greater than 25% will result in a reduction in the loan forgiveness amount, unless an exception applies. When the reduction applies, the borrower "must reduce the total forgiveness amount by the total dollar amount of the salary or wage reductions that are in excess of 25 percent of base salary or wages" during the reference period (January 1, 2020 to March 31, 2020).<sup>5</sup>

Unlike the FTE test, this is on a per-employee basis so you will need to pull the wages or salary data for the reference period and the covered period on all employees. Also, unlike the FTE calculation, this reference period is the first quarter of 2020 (January 1, 2020 to March 31, 2020).

*Example:* A borrower reduced a full-time employee's weekly salary from \$1,000 per week during the reference period to \$700 per week during the covered period. The employee continued to work on a full-time basis during the covered period with an FTE of 1.0. In this case, the first \$250 (25 percent of \$1,000) is exempted from the reduction. Borrowers seeking forgiveness would list \$400 as the salary/hourly wage reduction for that employee (the extra \$50 weekly reduction multiplied by eight weeks).<sup>6</sup>

Thus, in the above example, since there is a 30% reduction only the \$50 per week reduction in excess of the 25% is multiplied by the number of weeks ( $\$50 * 8 = 400$ ).

---

<sup>4</sup> Note that other laws requiring calculation of FTEs may utilize a different hour threshold for full time, such as 30 hours per week under the Patient Protection and Affordable Care Act.

<sup>5</sup> Forgiveness Interim Final Rule at 19.

<sup>6</sup> *Id.*

You will need to fill out the PPP Schedule A Worksheet Table 1, or obtain an equivalent report from your payroll system or processor, for these calculations. Keep these records as you will need to keep them in support of your application for forgiveness.

Importantly, reduction in pay is not doubly penalized if the reason for all, or a portion, of the reduction in pay is simply a reduction in hours (and therefore already accounted for in the FTE reduction above).

*Example:* An hourly wage employee had been working 40 hours per week during the borrower selected reference period (FTE employee of 1.0) and the borrower reduced the employee's hours to 20 hours per week during the covered period (FTE employee of 0.5). There was no change to the employee's hourly wage during the covered period. Because the hourly wage did not change, the reduction in the employee's total wages is entirely attributable to the FTE employee reduction and the borrower is not required to conduct a salary/wage reduction calculation for that employee.<sup>7</sup>

### C. Exceptions to the Reductions

There are three exemptions to the loan forgiveness reduction that would otherwise occur as a result of FTE or wage reduction. The first exception is expressly provided in the CARES Act itself. The next two are additional exceptions created by the SBA and Treasury Department in implementing the CARES Act.

#### *i. Safe Harbor Provision*

If the employees who saw their salaries reduced between February 15, 2020 and April 26, 2020 (safe harbor period) have their wages restored by June 30, 2020 or earlier, the borrower will be exempt from the loan forgiveness reduction that would otherwise occur due to the temporary reduction in wages.

Likewise, if FTEs fell between February 15, 2020 and April 26, 2020 but are fully restored by June 30, 2020, the temporary reduction in average FTEs will not reduce your loan forgiveness amount.

#### *ii. Good-faith, written offer to rehire declined*

If employees who were laid-off or had their hours reduced and **have now declined** the borrower's good faith, written offer to rehire, or restore reduced hours during the covered period, Employers/Borrowers will also be exempt from loan forgiveness reductions that would otherwise occur from a reduction in FTEs. This appears to reflect the government's policy that it would rather fund employers to keep their employees (even if unable to work) during the COVID economic slowdown than pay that same employee because he lost his job and is now paid through unemployment benefits. Unfortunately, some part time employees are making more from the COVID-19 enhanced unemployment than they would from their regular pay. As a result of this policy, if they decline the offer to rehire, their unemployment may be in jeopardy.

According to the new IFR on forgiveness, to qualify for this exemption a borrower must satisfy five conditions:

1. The borrower made a good faith, written offer to rehire the employee or restore the reduced hours of the employee during the covered period or the alternative payroll covered period;
2. The offer was for the same salary or wages and the same number of hours as earned by such employee in the last pay period prior to the separation or reduction in hours;
3. The offer was rejected by such employee;
4. The borrower has maintained records documenting the offer and its rejection; and

---

<sup>7</sup> Forgiveness Interim Final Rule at 20.

5. The borrower informed the applicable state unemployment insurance office of such employee's rejected offer of reemployment within 30 days of the employee's rejection of the offer.

We note that employees will need to be aware that refusal of a such a rehire offer will likely impact their eligibility for unemployment benefits.

*iii. Termination for cause, voluntary termination, or voluntary request for reduced schedule.*

Similarly, the SBA instituted a protection for borrowers who experience a reduction in FTEs because an employee is fired for cause, voluntarily resigns, or voluntarily requests a reduced schedule. The policy reason for this exemption is the reluctance to penalize employers for change in "employee headcount that are the result of employee actions and request."<sup>8</sup>

For these examples, borrowers may "count such employee at the same full-time equivalency level before the FTE reduction" when calculating the FTE employee reduction penalty on the application. Documentation supporting this decision must be retained by the borrower and provide that documentation upon request.

### **Step 3: Gather Required Documentation**

To streamline the many thousands of loan forgiveness applications the SBA is not requiring that all documents be submitted to the lenders and then the SBA. Instead, in addition to the specific categories of documents that are required, there is a separate list of documents that each borrower must maintain but is not required to submit.

For the full list of documents to be submitted or maintained, please see the page 10 of the [Application](#). All documentation must be retained for at least six years after the loan is forgiven or repaid in full. The highlights of required documentation are listed below.

#### Documentation Borrowers Must Submit with PPP Loan Forgiveness Application:

- **PPP Forgiveness Calculation Form** and **PPP Schedule A** (parts of the application).
- **Payroll documentation** verifying compensation during the covered period<sup>9</sup> including:
  - Bank account statements or third-party payroll service reports documenting compensation paid.
  - Tax forms for all periods overlapping with covered period including payroll tax filings (Form 941) and state quarterly business and individual employee wage reporting and unemployment insurance tax filings.
  - Payment receipts, cancelled checks, or account statements documenting the amount of any employer contributions to employee health insurance and retirement plans that the Borrower included in the forgiveness amount.
  - If you are a church seeking forgiveness for payroll amounts spent on housing allowance, you will have to provide separate documentation for the housing allowance if it does not appear on Form 941 or similar.
- **FTE Documentation** showing the average number of FTE employees on payroll per month during the borrower's chosen reference period. These documents may include payroll tax filings (Form 941), state

---

<sup>8</sup> Forgiveness Interim Final Rule at 22.

<sup>9</sup> For the purposes of the listing of these required documents "covered period" can mean alternative covered period if applicable.

quarterly business and individual wage reporting and unemployment insurance tax filings. These often quarterly filings may cover periods longer than just the covered period.

- **Documentation of Nonpayroll Obligations** Prior to February 15, 2020 and eligible payments from covered period.
  - For business mortgage interest payments: copy of lender amortization schedule and receipts or cancelled checks verifying payments during covered period or lender account statements verifying interest amounts and eligible payments.
  - For business rent or lease: Copy of lease and receipts; or lessor account statements.
  - For business utility payments: Copy of invoices from February 2020 and those paid during Covered period and receipts verifying payments.
  - See application for more options in these areas.

#### **Documentation Borrowers Must Maintain (Not Required to Be Submitted)**

- PPP Schedule A Worksheet (part of application) or its equivalent.
- Documentation supporting the listing of each employee in Schedule A Worksheet concerning the salary and wage reduction calculation or whether the employee received more than \$100,000.
- Documentation regarding any employee job offers and refusals, firings for cause, voluntary resignations, and written requests by any employee for reductions in work schedule.
- Documentation supporting the PPP FTE Reduction Safe Harbor worksheet.
- All other records relating to the borrowers PPP loan or forgiveness application: including documentation submitted with the application and supporting the borrower's certification as to the necessity of the loan request and its eligibility for PPP loan.

We note that it is important to document the reasons you believed it was necessary to apply for the PPP loan in the first place such as anticipated and actual revenue declines and cash on hand. Hopefully you had all of those records from the date you applied, if not, you should make sure that information is available. It will assist you if you are ever audited and let you enjoy peace of mind in the meantime.

#### **Step 4: Submit Your Application**

Once you assemble all of the above information and documents and have filled out the application, it is ready for submission to your lender. Due to the anticipated volume of forgiveness applications you probably will not receive an answer immediately. The lender "has 60 days from receipt of a complete application to issue a decision to SBA." At that point the SBA may also review the loan and forgiveness application. The SBA will make a decision within 90 days of receiving the information from the lender.

*When should I submit my application?* Most borrowers will want to apply soon after they become eligible to do so (after the covered period ends and all after period payments are made) to get loans forgiven before payments start. You will need to start making payments after a six-month deferral from the disbursement of loan. However, borrowers are under no obligation to apply as soon as they are eligible; and it may be in your best interest to wait in some cases. For instance, if your forgiveness will be limited due to a decrease in FTEs or employee wages but you may be eligible for the safe harbor exception described above, you should consider waiting to apply until you eliminate the FTE or wage reduction if that can be done by June 30, 2020.

Likewise, if you are not going to receive 100% forgiveness at this point because of some other restriction, you should wait for proposed federal legislation currently making its way through the House and Senate that aims to make more PPP borrowers eligible for forgiveness by extending the eight week review period to sixteen or twenty-



four weeks, reducing the 75% payroll costs threshold, and increasing the number of items PPP funding can be used for and forgiven.<sup>10</sup>

## More FAQs

### 1. What Happens if My Loan is Not Fully Forgiven?

To the extent that your loan is not fully forgiven, your organization will remain on the hook for repaying the unforgiven portion of the loan, with 1% interest, due two years from disbursement. However, if the SBA determines that the reason the loan cannot be forgiven is that your organization acted fraudulently or in bad faith, other penalties can apply.

### 2. What should I do if my projections show I will not spend 75% of the PPP proceeds on payroll costs?

You have a number of options available to you. First, be aware that Congress may extend the eight week window or reduce the 75% requirement, making it easier to qualify for loan forgiveness. If the reason is a lack of opportunities for your employees to work, consider paying your employees something anyway (including sick leave and vacation) so that you qualify for loan forgiveness.

### 3. How does the EIDL and Advance fit in with loan forgiveness?

This has been a source of some uncertainty throughout the process. Another CARES Act program allowed up to \$10,000 advances with an Economic Injury Disaster Loan (EIDL) application. Thankfully, once you are in the forgiveness stage, the matter is out of your hands and in the SBAs. The loan application simply requires you to document the amount you received as an advance with an EIDL and the associated EIDL application number. “If applicable, SBA will deduct EIDL Advance Amounts from the forgiveness amount remitted to the Lender” as required by the CARES Act.<sup>11</sup>

Most commentators now believe that the consequence of receiving both a PPP and an EIDL grant is that you will have to repay the grant (and any amount of EIDL that you refinanced into the PPP) at 1% interest, with a two-year term as if it was an Economic Injury Disaster Loan refinanced as an unforgivable PPP loan.

We continue to find the guidance less than clear on this subject. Such a result seems contrary to the intent of the CARES Act unless this mechanism was intended to be a guard against perceived double dipping. It may also be that the grant amount is “deducted” from the forgiveness amount because it the grant already forgiven to the borrower and was not issued the grant through the PPP lender.

Ultimately, it is up to the Congress and the agencies administering the program to make these decisions, you do not have to factor the amount into your calculations on the application. Please note, however, that you may be on the hook for repaying the grant which could be considered to be an obligation refinanced under the terms of PPP loans or potentially simply as an EIDL (higher rate of interest but a longer period of time to repay.)

The example below shows how the scenario could play out for a typical borrower who receives both a EIDL grant and a PPP loan.

*Example:* A borrower receives a \$100,000 PPP loan and a \$10,000 EIDL Advance (grant). Under the guidance of most commentators, even if the borrower qualifies for 100% forgiveness in all of the PPP tests stated above, the SBA may forgive the \$100,000 PPP loan, but construe the \$10,000 EIDL grant as

---

<sup>10</sup>Anne Sraders, *House passes bill to extend 8-week period to spend PPP loans and alter 75% rule*, FORTUNE, (May 28, 2020) <https://fortune.com/2020/05/28/house-bill-ppp-extension-8-weeks/>.

<sup>11</sup> Forgiveness Interim Final Rule at 8.

a loan that must be repaid under the terms of the PPP (1% interest; 2-year repayment term; payments starting six months after disbursement).

However, it is also possible that the SBA will decide to consider both the EIDL Advance and the PPP loan forgiven. Time will tell, but this is as much as we know given the current guidance.

#### 4. **What Happens if I do not get a determination of forgiveness before my first repayments are due?**

You should likely be making these payments. Once a final determination of forgiveness is made, any amounts that you paid prior to receiving a forgiveness determination will be returned to you to the extent your loan is forgiven.

For example, a Borrower receives a \$100,000 PPP loan and makes payments in a total amount of \$10,000 before forgiveness is determined. The lender and SBA determine that \$95,000 of the loan is forgivable (perhaps due to a slight reduction in average FTEs in the covered period or one of the other reductions discussed above). The Borrower will have the remaining amount of the loan forgiven and \$5000 returned (minus any amount retained for accrued interest for the unforfeitable portion of the loan).

### **Audits and Reviews**

Due to public outcry over relatively large businesses (public companies and those with large reserves) taking advantage of large PPP loans to the exclusion of smaller businesses for whom the PPP was intended, the SBA has announced that it will be reviewing all PPP loans over \$2,000,000 as well as some below that threshold.<sup>12</sup>

The biggest concern for many borrowers was after the fact audits of its good-faith certification on the applications that “[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant.” Given the economic uncertainty that existed for almost all small businesses, churches, and nonprofits during this time, and to allay concerns about the nebulous nature of the determination, the SBA announced it will not be contesting the good-faith certifications of “necessity” for borrowers receiving less than \$2,000,000 under the PPP.<sup>13</sup> However, the SBA may review other aspects of borrower eligibility, loan amounts and use of proceeds, and loan forgiveness amounts for PPP loans “of any size” and may do so “at any time in SBA’s discretion.”

The effect of this new guidance and the perceived uncertainty surrounding SBA enforcement has appeared to sharply reduce new applications and chill the demand for the second round of PPP funding. **This means that if you are eligible for the PPP there is still time and funds for you to apply.** In fact, you will have the added advantage of having the forgiveness application and guidance available to you as you strategize at the outset whether you are eligible for forgiveness of the loan. Highlights of the [auditing and review Interim Final Rule](#) are provided below.

All PPP loan recipients of more than \$2 million will need to ensure their documentation supports their certification that **economic uncertainty** made the loan request necessary. For instance, documenting whether cash on hand was low, projected income declined, workforce and/or projects were in jeopardy, etc. will be helpful. Due to the sheer number of loans and expected applications for forgiveness, the SBA will not be able to subject each one to an exhaustive and grueling audit, in the way businesses fear IRS audits. We expect the majority or all of the audits may be **merely paper audits** (i.e. no investigators coming to your business or mandatory interviews). However, the SBA may impose random, more thorough audits to try to keep the system honest and pursue more investigation on matters that warrant suspicion. The six year document retention period gives the SBA time to

---

<sup>12</sup> SBA, Paycheck Protection Program Frequently Asked Questions, <https://home.treasury.gov/system/files/136/Paycheck-Protection-Program-Frequently-Asked-Questions.pdf> (last visited May 29, 2020)

<sup>13</sup> *Id.* at question 46.

come back to revisit a loan if evidence of wrongdoing arises later, and implies the SBA realizes that it will not be able to discover all wrong doing in its initial reviews. SBA appears to be looking for egregious violations, like Borrowers with have millions of dollars of useable endowments and reserves or being a publicly traded company with adequate sources of investment income, not small businesses or nonprofits with the usual six month business reserves.

If the SBA determines that the borrower was ineligible for a PPP loan in the first place, the loan will not be forgiven, and the borrower will have to repay the outstanding PPP loan balance with interest, and other remedies may be available to the SBA as well.

*What rights do I have if I am audited or otherwise questioned?* These procedures are going to be the subject of future guidance. At a minimum, borrowers will have the opportunity to provide additional information to the lender (such as regarding economic uncertainty at the time of application for the loan) if a review determines that the borrower was not eligible for the loan itself or for forgiveness. The SBA will consider all information provided by the borrower in response. Additionally, the SBA intends to issue a separate interim final rule regarding an appeal process if the SBA determines that the borrower is ineligible for the PPP for the loan forgiveness amount claimed.

If the SBA initiates a review of a PPP loan, the SBA will notify the lender, and the lender is required to notify the borrower of the review within 5 days. The lender will then submit its documentation about the particular PPP loan to the SBA for its review. **Lenders are incentivized to weed out fraud at the outset and get their borrowers to the forgiveness finish line once the loan is made, as the banks will not get paid (and in fact may have to return fees to the government) for PPP loans that are determined to have been ineligible when made.**

\*\*\*\*\*

*Disclaimer: This memorandum is provided for general information purposes only and is not a substitute for legal advice particular to your situation. No recipients of this memo should act or refrain from acting solely on the basis of this memorandum without seeking professional legal counsel. Simms Showers LLP expressly disclaims all liability relating to actions taken or not taken based solely on the content of this memorandum. Please contact Robert Showers at [hrr@simmsshowerslaw.com](mailto:hrr@simmsshowerslaw.com) or Will Thetford at [wrt@simmsshowerslaw.com](mailto:wrt@simmsshowerslaw.com) or call at 703.771.4671 for legal advice that will meet your specific needs.*