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What to Watch Out for in the Paycheck Protection Program Flexibility Act

The Paycheck Protection Program (PPP) Flexibility Act amends the Small Business Act and the CARES Act, modifying certain provisions in an attempt to make it easier for businesses to have their PPP loans forgiven. For many companies these are welcome changes. However, there are few things to bring to your attention which could lead to unintended consequences in limited cases.

The one constant in the PPP is that the program will change. We do not expect this recent update to be the final PPP outlook, and we anticipate changes to the forgiveness form, as well as more regulatory interpretations that will impact the Program.

Updated Provisions as of 6/5/2020	What to Know
Unforgiven portion of loan is extended from a 2-year term to a 5-year term with a longer period to not have to make principal payments	• We have heard rumors banks will **NOT** be required to redo existing loan applications. So, new loans after this enactment will be 5 years, but loans issued prior may not be and may need to be a one-off renegotiation with your bank if you believe you will have substantial amounts of your loan not forgiven.
Extension of covered period to earlier of 24 weeks or 12/31/20 (or elect to retain current 8-week covered period)	• We assume the SBA's alternative covered period to align the cover period to your payroll dates will remain for the 8-week covered period for those on certain frequencies of payroll, but that is an assumption. • Certain companies may still want to elect the 8-week period if the PPP is creating operational restrictions and/or contractual complexities. • It is also unknown if the SBA will allow mid-covered-period forgiveness applications if you meet full forgiveness between 8 and 24 weeks.
More exemptions and exceptions on the proportional reduction of forgiveness quotient	• Timelines are generally extended to Dec. 31 to return to pre-pandemic employment level, a change from the previous deadline of June 30, for full forgiveness. • We have not seen official guidance on how to handle post-covered-period reductions in force, and there may end up being tactical considerations on when to apply. • Previous guidance already allowed borrowers to exclude from those calculations employees who turned down good faith offers to be rehired at the same hours and wages as before the pandemic. • The new bill allows borrowers to adjust because they could not find qualified employees or were unable to restore business operations to Feb. 15, 2020, levels due to COVID-19 related operating restrictions.

Updated Provisions as of 6/5/2020	What to Know
60% payroll cost use of proceeds requirement to get any forgiveness *6/8/2020 Update: SBA has indicated that partial forgiveness will be permitted. Read the full press release for more details.*	• For many companies this is a welcome change from the limit on forgiveness to 25% to non-payroll costs. • However, this new 60% threshold is based on the total loan amount and not the loan forgiveness. Therefore, if you are not able to spend 60% of the loan proceeds on payroll costs, then you are ineligible for forgiveness as currently written. • This may be potentially problematic for companies negatively impacted by the oil and gas price collapse in addition to the pandemic.
Change of payment (principal, interest, fees) deferral period from 6 months to until the forgiveness form is remitted to the lender	• There may be operational strategies in the timing of applying for forgiveness. • We are unsure of the methodology of how interest will accrue for amounts ultimately forgiven in the window of the end of the covered period and the forgiveness application date.
10 months to apply for forgiveness	• Payments start if you don't apply for forgiveness by 10 months after the last day of your covered period.
Payroll tax deferral will be now open to those with PPPs.	• This change can free-up cash flows. • This is not a forgiveness amount and is only a deferral. • Your controls should have been designed to NEVER allow payroll taxes to go unpaid. This means that to enact this option, companies need to override their operational controls and put in new controls for monitoring and be ready with the cash flows. Companies should be careful in the way they implement this benefit and be precise in their calculations and planning to pay back what they will owe.
The deadline for PPP loan applications remains June 30, 2020.	• Don't forget the SBA said if you had a mistake related to how your partners' "compensation" was treated in your original PPP application, you can go back and apply for more PPP funds.

Unintended Consequences

Although there is optionality and relief through these programs, companies should be careful on their balance sheets and controls. These programs are creating liabilities on the balance sheet.

- If you have required key metrics for licensing agencies, vendors, customers, and/or bank debt covenants, you can accidentally run in to technical violations.
- Additionally, if you have various levels of debt seniority (such as certain mezzanine debt), there may also be problems with respect to debt subordination clauses that could create a technical default in the terms of your note.
- Further, many of these programs (as well as the work-from-home model accounting departments are operating in) are creating the need to override companies' control environment in order to mechanically execute some of these programs.
- Of course, if companies have financial statement audits, these issues can create future audit complexity.

How Can We Help?

These changes now allow business owners the time to make strategic business decisions versus being reactive to time constraints. Reach out to the PKF Texas Entrepreneurial Advisory Services team with questions early in the process and if you need assistance in adapting controls, pro-forma-ing financial statements for key stakeholders and/or scenario modeling.

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