

# 5 Steps Your Clients Can Take to Weather Mandatory PPP Audits

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by Jonny Frank and Ryan LaRue

The U.S. Department of Treasury and Small Business Administration (SBA) have promised the government will audit all recipients of Paycheck Protection Program (PPP) loans over \$2 million who seek loan forgiveness. So, the question is not if, but when, an audit is coming. Companies that fail audits jeopardize all or part of their loan forgiveness, and, worse, might face False Claims Act prosecutions by the U.S. Department of Justice (DOJ).

Besides SBA audits, borrowers must prepare for investigations by the Special Inspector General for Pandemic Recovery and reviews by the Pandemic Response Accountability Committee and the Congressional Oversight Commission. In addition, the DOJ and State Attorneys General have announced enforcement initiatives.

Below are five practical steps borrowers can take to withstand the scrutiny of PPP audits and investigations:

## **1** Start Now

Do not wait for Uncle Sam to come calling. Auditors regard contemporaneous documentation—or an accurate written record of how the funds were applied—as more persuasive than information created once an audit begins. Contemporaneous documentation also saves time. It is more efficient to organize records, receipts and documents now than it would be to re-create them later.



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## Assess Risks

PPP loan recipients must certify that “current economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant.” And, companies seeking loan forgiveness must certify they “used the forgiveness amount to keep employees and make eligible mortgage interest, rent, and utility payments.” Certifications found to be inaccurate or untrue are punishable under criminal and civil law. But, how does a company certify to an uncertainty and what makes the funds necessary? Ultimately, the courts will decide, but multimillion-dollar borrowers and public companies will face the greatest scrutiny. Given the stakes, borrowers in this category can expect a deep-dive forensic audit, not a bare-minimum file review.



## Document Analysis to Support Certifications

Document both evidence and analysis that demonstrate the necessity of loan funds to support ongoing operations. Analyze expected sources and uses of cash over a reasonable period and support why that period is an appropriate timeframe to consider “ongoing operations.” Base the analysis on historical financial information, budgets/projections, and experience operating in the current economic environment.

Start with all sources of funds (e.g., cash reserves, access to credit, expected revenues). Then, project uses of cash over the same period, including payroll, rent and lease payments, inventory purchases, administrative expenses, professional fees, and other likely uses of cash. These amounts should be consistent with the amounts in the loan forgiveness application for the eight-week period after loan proceeds are received. Link and maintain supporting

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documentation for each item on the analysis (e.g., bank statements to support existing cash reserves, loan documents to support debt obligations).

Judgment is required to project revenue and expenses during this uncertain time, including the ramp-up period after businesses reopen, but before the economy returns to pre-pandemic levels. Assumptions used for projecting revenues and expenses should be consistent.

After projecting sources and uses of cash, compare the net amount to the PPP funds received. Significant cash surpluses remaining should be supported with documentation on the use of those funds beyond the period analyzed. The results and underlying supporting documents should provide enough support for the certification.

Borrowers should not forget about other PPP application certifications. Create a file to save back-up to support these assertions. For example, include copies of payroll records to support the certification the company was in operation on February 15, 2020, and had employees for whom it paid salaries and payroll taxes. Similarly, include payroll records and invoices to support the borrower certification that the company will use funds to retain workers and maintain payroll or make mortgage interest payments, lease payments, and utility payments.



## Prepare for Loan Forgiveness Application

The government has not yet provided prescriptive guidance on the loan forgiveness calculations or application process. In the absence of guidelines, borrowers should prepare now and maintain meticulous records of how the company used

the loan funds. We suggest creating a separate general ledger account for these funds, as well as a separate bank account, where possible. Examples of supporting documentation companies should maintain include:



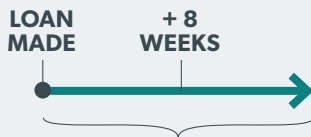
### Loan Forgiveness Criteria

**Funds are used to cover payroll costs, mortgage interest, rent, and utility costs**

#### Potential Supporting Documentation

- Payment support to demonstrate funds used for payroll, mortgage interest, or lease and utility payments
- Invoices for mortgage interest, lease payments, and utility services
- Lease agreements stating monthly amounts due
- General ledger account details showing use of PPP funds

#### Documentation Timeframe



8-week period after the loan is made



### Loan Forgiveness Criteria

**Employee and compensation levels maintained to pre-loan levels**

#### Potential Supporting Documentation

- Payroll records such as payroll tax reports, employee benefit records, and compensation records
- Calculation of full-time equivalents and pay rates
- Documentation to support headcount changes

#### Documentation Timeframe



From periods beginning Feb. 15, 2020 through the end of the 8-week period after the loan is made



## Consider a “Mock” Audit

Audits are not an all-or-nothing proposition. It does the borrower little good if the government allows the application, but slashes the amount forgiven. Multimillion-dollar borrowers and public companies might consider “mock audits” as a trial run. A mock audit replicates procedures inspectors general apply to investigations of fraud, waste and abuse. The review identifies holes the borrower must fill to maximize forgiveness allowance. Aggressive borrowers can gauge the likelihood of passing the government “smell test” and a referral to DOJ.

### Conclusion

The PPP was intended to ensure small businesses are provided sufficient resources to keep workers employed while they weather the storm brought on by the pandemic. Eligible borrowers should not be frightened by the government’s warning that audits are coming; instead, use this time to prepare. Do everything you can today to ensure your business reaps full benefits as intended by the spirit of the PPP, while remaining compliant with its uncertain requirements. Remember: Begin early, maintain accurate documentation, assess risks, consider the assessment criteria, and prepare for a likely audit by conducting a mock audit internally to successfully withstand regulatory scrutiny.

### About the Authors

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