



**Washington State
Department of Transportation**

Interpretive Guidance Document

*Paycheck Protection Program (PPP)
Loan Forgiveness and Indirect Cost Rates
for Architectural & Engineering Firms*

WSDOT Internal Audit Office

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Interpretive Guidance - PPP Loan Forgiveness and Indirect Cost Rates

Background

Paycheck Protection Program (PPP) loans are a US Small Business Administration – backed loan to help businesses keep their workforce employed during the COVID-19 pandemic. These loans are approved for certain expenses like payroll, payroll taxes, rent, mortgage interest, and utilities. Borrowers may be eligible for PPP loan forgiveness for all or a part of their loan.

This guidance document is intended to clarify how the federal regulations (FAR part 31) is applicable to the relief programs and how Architectural and Engineering (A&E) consultants should address the loans in their indirect cost rate (ICR) schedules. The accounting treatments described herein apply only to loan amounts which are forgiven, loan amounts repaid do not require such treatment. *Please note we may update this guidance as we receive new information, or further guidance from the Federal Government regarding PPP loans.*

Definitions

Credit: A credit is defined for this guidance document as: *a reduction to the firm's indirect cost rate, when required as a result of a forgiven PPP loan.*

Federal Requirements - Summary

The FAR and guidance from the Federal Highway Administration (FHWA), and the Defense Contract Audit Agency, address how to treat forgiven PPP loans in indirect cost rates for government contracts.

The FAR requires a credit to the Government, either as a cost reduction or by cash refund, when a firm receives an allowance, rebate or other credit relating to an allowable cost. The FAR, in 48 CFR 31.201-5 says in part...*The applicable portion of any income, rebate, allowance, or other credit relating to any allowable cost and received by or accruing to the contractor shall be credited to the Government either as a cost reduction or by cash refund...*

The Defense Contract Audit Agency's December 11, 2020 memorandum on PPP loans, loan forgiveness and subsequent credits to the government, confirmed that 48 CFR 31.201-5 is applicable to PPP loans.

FHWA's March 24, 2021 memorandum affirmed that when PPP loan proceeds are applied to a firm's costs (direct or indirect) within the scope of a federally funded contract and the PPP loan is forgiven, appropriate adjustments to consultant accounting records become necessary to comply with 48 CFR part 31.

Please see the *Federal Requirements – Detailed Analysis* section on page 5 for the complete references to the federal regulations and guidance.

Interpretive Guidance - PPP Loan Forgiveness and Indirect Cost Rates

When is a Credit Required?

When forgiven, the PPP loans have the effect of a prepayment of overhead expenses. PPP loans which are forgiven should be reflected in the ICR schedule as a credit to the applicable accounts to which the loan amounts were applied in accordance with the loan forgiveness application and 48 CFR 31.201-5. The credits resulting from the forgiven loans will affect Cost-Plus Fixed Fee and Negotiated Hourly Rate agreements.

WSDOT will not be including the credits in forward pricing agreements. Also, forgiven PPP loan funds used for otherwise unallowable indirect costs or direct costs for private clients may be exempt and therefore not part of an adjustment to the ICR. The Internal Audit Office would need to verify this information, but it is possible to reduce the required credit.

If reducing your ICR based on a forgiven PPP loan results in an undue burden or economic hardship for your firm, you may be asked to provide additional information to determine treatment of the credit. Please contact the WSDOT Audit and Consulting Services Manager for information needed in these circumstances.

What's included in the Credit?

Forgiven PPP loan funds spent on otherwise allowable indirect costs will be *included* in the credit to the indirect cost pool.

Forgiven PPP loan funds spent on direct costs for contracts subject to 48 CFR Part 31 will be *included* in the credit to the indirect cost pool.

Forgiven PPP loan funds spent on direct costs for commercial clients that were not reimbursed through contracts subject to 48 CFR Part 31 *may be excluded from the credit* to the indirect cost pool. Excluded direct costs must be supported by schedules listing the detailed transactions by excluded contract including contract client, contract basis of payment, employee name, hours and wages that can be reconciled to the forgiveness application. **Please note**, if excluded commercial direct costs were also billed to your clients it may invalidate the intent of the forgiven PPP loan, and WSDOT may need to notify the SBA.

Forgiven PPP loan funds spent on indirect costs considered unallowable by FAR will be included in the credit to the indirect cost pool once and *require special consideration to avoid crediting these costs twice*. For example, if a firm were to incur expenses for advertising labor that are eligible to be covered by PPP loan fund yet are disallowed by FAR (48 CFR 31.205-1) during the period covered by a forgiven loan, the credit for the advertising labor would be included in the credit amount for the forgiven loan, so not to count this credit twice. We recommend firms document any disallowed labor incurred during the covered period for a forgiven loan to avoid two credits.

PPP loan funds may not be used for an employee's compensation over \$100,000 per year. As such, compensation over this limit cannot be included in the accounting for use of a forgiven PPP loan. Further, credits from *excess compensation* as calculated under FAR and the AASHTO Audit Guide will be made in full on the ICR schedule.

Interpretive Guidance - PPP Loan Forgiveness and Indirect Cost Rates

When to Apply the Credit

Which fiscal year to apply the credit for loan forgiveness will depend on what is known at the fiscal year end. Please note, that if a firm recorded the PPP Loan as a grant, different accounting procedures may apply; see the enclosed AICPA Technical Question and Answer Section 3200 for further details.



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- If a firm receives notice of forgiveness prior to the fiscal year end, then it will be reflected in that year's financial statements.
 - Example: Firm A has a calendar year end. Firm A receives a PPP loan in June 2020 and receives confirmation the full amount has been forgiven in September 2020. Firm A would include a credit in the ICR schedule for the full amount forgiven.
- If a firm receives forgiveness after the fiscal year end, but before the financial statements are issued, the forgiven amount should be included in that year's financial statements.
 - Example: Firm B has a calendar year end. Firm B received a PPP loan in June 2020 and received confirmation the loan was forgiven in February 2021 and the financial statements have not been issued. Those financial statements should be amended to reflect the forgiven loan and the credit should appear in the ICR schedule.
- If a firm hasn't yet decided to apply for forgiveness, or the amount forgiven is not known, the firm would apply any credit for forgiven loans in the fiscal year in which the amount becomes known.
 - Example: Firm C has a calendar year end. Firm C received a PPP loan in June 2020 and when the financial statements were issued, Firm C hadn't determined if any of the loan would be forgiven. Firm C would issue the financials for 2020 without recognizing the loan forgiveness. If the loan is then forgiven later, the firm would recognize the forgiven amount on that subsequent year's financial statements. The credit associated with the FY2020 PPP loan forgiven funds would then apply to the FY2021 ICR schedule.

How to Apply the Credit

Firms should be prepared to submit a copy of the application for loan forgiveness along with documentation to support how the firm executed the PPP loan received. The Internal Audit Office will work with each consultant to evaluate the applicable credit to the indirect cost pool. WSDOT will only seek recovery of the forgiven PPP loan through a credit to the ICR and not a direct payment from the firm based on the potential for improper payments mentioned in the FHWA guidance below. The resulting indirect cost rate schedule will include a reference for each cost pool subject to the credit per 48 CFR 31.201-5.

Interpretive Guidance - PPP Loan Forgiveness and Indirect Cost Rates

Independent audits of consultant indirect cost rates should disclose information regarding PPP loans including loan amounts, approval dates, forgiveness status, forgiven amounts, covered period for forgiveness, application of forgiven funds and repayment of principal.

Federal Requirements – Detailed Analysis

The Federal Acquisition Regulations (FARs) address the expectations on how consultants should treat credits received for expenses.

Title 48: Federal Acquisition Regulations System

PART 31—CONTRACT COST PRINCIPLES AND PROCEDURES

Subpart 31.2—Contracts with Commercial Organizations

31.201-5 Credits.

The applicable portion of any income, rebate, allowance, or other credit relating to any allowable cost and received by or accruing to the contractor shall be credited to the Government either as a cost reduction or by cash refund. See 31.205-6(j)(3) for rules governing refund or credit to the Government associated with pension adjustments and asset reversions.

On December 11, 2020 the Defense Contract Audit Agency issued a memorandum on PPP loans, loan forgiveness and subsequent credits to the government in which it confirmed 48 CFR 31.201-5 is applicable.

- **Question 2:** *Do the requirements of FAR 31.201-1, Composition of Total Cost, and FAR 31.201-5, Credits, apply to the provisions in the FFCRA and CARES Act?*

Answer: Yes. *FAR 31.201-5, Credits, states “the applicable portion of any income, rebate, allowance, or other credit relating to any allowable cost and received by or accruing to the contractor shall be credited to the Government either as a cost reduction or by cash refund.” FAR 31.201-1, Composition of Total Cost, states that total cost is the sum of the direct and indirect costs allocable to the contract less any allocable credits.*

To the extent that PPP credits are allocable to costs allowed under a contract, the Government should receive a credit or a reduction in billing for any PPP loans or loan payments that are forgiven. Furthermore, any reimbursements, tax credits, etc. from whatever source that contractors receive for any COVID-19 Paid Leave costs should be treated in a similar manner and disclosed to the government.

The U.S. Department of Transportation Federal Highway Administration (FHWA) released a memorandum on March 24, 2021 titled: *Treatment of Paycheck Protection Program Funds for Architectural and Engineering Consultants Guidance*. The memo reaffirms that FAR applies to PPP loan forgiveness, stating part: *“should the PPP loan proceeds be applied to costs (direct or indirect) within the scope of a federally funded contract and the PPP loan is forgiven, appropriate adjustments to consultant accounting records become necessary to comply with 48 CFR part 31.”*

Interpretive Guidance - PPP Loan Forgiveness and Indirect Cost Rates

The FHWA guidance memo goes on to state:

- *While the PPP was enacted to permit an impacted employer to retain its employees on the payroll, it was not enacted to provide an economic windfall to the employer (e.g., where costs are reimbursed by the Federal government under a federally funded contract and the PPP loan is also forgiven by the SBA).*

The following applies when an A&E consultant's PPP loan is partially or completely forgiven:

- *A&E consultants cannot use PPP loan proceeds to pay for the direct costs on a Federal-aid or Federal lands highway program funded contract.*
 - *A&E consultants cannot bill direct costs and use PPP loan proceeds to fund the compensation costs of direct labor and other direct costs dedicated to federally funded contracts. This practice results in an improper payment for billing the Federal government twice. A consultant may use the PPP loan as a working capital loan to pay the direct costs of a contract but must submit a timely claim for reimbursement to the contracting agency and complete the proper and necessary adjustments to their accounting records once the reimbursement is received.*
 - *PPP loan proceeds cannot be used to pay the direct project costs even if those costs are not billed to the federally funded contract. This action has the effect of a donation to the project, which was not authorized and conflicts with the terms and conditions of the contract. A&E consultants should continue to allocate and invoice both direct and indirect costs in accordance with contract terms.*
- *A&E consultants may use PPP loan proceeds to pay for indirect costs, but an adjustment to the indirect cost rate is required in accordance with 48 CFR § 31.201-5.*
 - *A&E consultants must adjust their indirect cost rates for PPP funds forgiven to provide the corresponding credit to the Federal government. All credits to indirect costs should be reflected in the subsequent adjusted indirect cost rate. If an A&E consultant can apply the appropriate indirect cost credit on existing contracts, the contracting agency may allow the consultant to do so.*
 - *All applicable credits (or loan recoveries) are to be applied based on an equitable allocation to all benefiting costs objectives in accordance with 48 CFR § 31.201-4. The indirect cost rate credit should only be applied until the credit is recovered fully. If adjustments to an A&E consultant's indirect cost rate has no bearing on the award or contract type (e.g., firm fixed price or lump sum contract), adjustment to that contract would not be required.*