

## Lender Considerations During PPP Loan Forgiveness Review and After

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security (CARES) Act was enacted to provide emergency assistance and healthcare response for individuals, families and businesses. Under Sections 1102 and 1106, the Small Business Administration (SBA) was given funding to establish a new loan program to assist small businesses nationwide that were negatively impacted by COVID-19. The program provides a 100 percent SBA guaranty and forgiveness up to the full principal amount of the qualifying loan. This program is known as the Paycheck Protection Program (PPP).

All existing SBA-certified lenders, federally insured depository institutions, credit unions and farm credit system (FCS) institutions, non-bank and non-insured depository institution lenders<sup>1</sup> were asked to participate in the PPP loan program and were offered some attractive incentives for participation. While the SBA has provided both lenders and borrowers with a plethora of information and assurances, lenders familiar with SBA lending understand the underlying risks associated with obtaining repayment against a full (or partial) SBA guaranty. Under existing SBA programs (such as the SBA 7(a)), the guaranty can be at risk due to improper loan closing and servicing by the lender.

When considering the financial institution's PPP loan portfolio, the lender should ensure its loan origination and lender review processes were completed based on the appropriate PPP loan guidance. If your institution has a PPP loan portfolio, the focus should be on the loan forgiveness process. Currently, lenders are expected to perform a good-faith review and issue a decision regarding loan forgiveness to the SBA. This review and decision should occur no later than 60 days after receipt of a completed forgiveness application from the borrower. Once the lender determines the borrower is entitled to forgiveness of all (or a portion) of the PPP loan amount, the lender must request payment from the borrower at the time the decision is issued by the SBA.

The lender review required for the loan forgiveness application (SBA Form 3508 or 3508EZ) is as follows<sup>2</sup>:

1. Confirm receipt of borrower certifications;
2. Confirm receipt of required documentation to aid in verification of payroll/non-payroll costs as specified in SBA Form 3508 and 3508EZ Instructions;

<sup>1</sup> [PPP Information Sheet- Lenders, Who is eligible to lend?](#)

<sup>2</sup> [SBA Procedural Notice 7/23/2020](#), Page 2 of 8 Forgiveness and Loan Review Procedures IFRs.

3. Confirm borrower's calculations on the following:
  - a. SBA Form 3508, including the dollar amount of:
    - i. Cash compensation, non-cash compensation and compensation to owners claimed on Lines 1, 4, 6, 7, 8 and 9 on PPP Schedule A; and,
    - ii. Business Mortgage Interest Payments, Business Rent or Lease Payments, and Business Utility Payments claimed on Lines 2, 3 and 4 on PPP Loan Forgiveness Calculation Form.
  - b. SBA Form 3508EZ, including the dollar amount of:
    - i. Payroll costs, business mortgage interest payments, business rent or lease payments and business utility payments claimed on Lines 1, 2, 3 and 4.
4. Confirm the borrower made the calculation on Line 10 of SBA Form 3508 (Line 7 of SBA Form 3508EZ) correctly, by dividing the borrower's eligible payroll costs claimed on Line 1 by 0.60.
5. If during the review, the lender identifies errors in the borrower's calculations or material lack of substantiation (a term used but not clearly defined by the SBA) in the borrower's supporting documents, the lender should work with the borrower to remedy the issue.

Once the lender completes the review and issues its decision to the SBA, the SBA, subject to their review of the loan/ loan application, will remit the forgiveness amount, plus any accrued interest through the date of payment, no later than 90 days after the lender issues its decision to the SBA. If applicable, the SBA will deduct any Economic Injury Disaster Loans (EIDL) advance amount from the forgiveness amount remitted to the lender.<sup>3</sup> If the SBA remits a forgiveness amount less than the amount in the forgiveness decision issued by the lender, the lender must notify the borrower. If a portion or the full amount of the loan is not forgiven, the remaining balance must be repaid by the borrower on or before the maturity of the loan.<sup>4</sup>

If full (or partial) forgiveness from the SBA is denied for one or more PPP loans, it is important to consider whether the borrower is a new or existing bank customer, and if the loan was denied (in whole or in part) due to:

1. Loan origination issues;
2. Improper use of funds; and/ or,
3. Improper certifications.

Next, the bank should establish a process for servicing and risk grading the PPP loan portfolio. The following are the minimum recommended considerations:

***Consideration 1: Complete an internal/external loan review, to include, but not limited to, the following:***

1. *Identifying the borrower as a new or existing customer;*
2. *Statement regarding why the loan was denied (in whole or in part);*
3. *Determine if the loan was properly originated by the institution;*
4. *Determine if the funds were properly utilized;*
5. *Review certifications;*
6. *Review of the lender's PPP loan forgiveness review process; and,*
7. *Review for required loan documentation.*

**Consideration 2: Complete a credit memorandum, to include, but not limited to, the following:**

1. Loan terms:
  - a. Confirm loan terms are in compliance with SBA PPP lending guidelines.
2. Background/banking relationship;
3. Servicing recommendations:
  - a. If new client, request the most recent financials (while not required for origination, at this time the SBA does not specifically state you can NOT obtain if the loan is not fully forgiven);
  - b. Establish annual (semi-annual) covenants, at modification (in compliance with any ongoing SBA guidance); and/or,
  - c. Sell the loan.
4. Recommended risk rating.

**Consideration 3: Obtain approval of the credit memorandum and attach the loan review as supporting documentation:**

1. Use the institution's existing approval process; or,
2. Establish an approval process specific to the PPP loan portfolio.

The considerations outlined above are the minimum lenders should bear in mind when working with partially or fully unforgiven PPP loans. However, the financial institution should also be mindful that the PPP forgiveness process started with the origination of the PPP loan.<sup>5</sup>

### About DHG Financial Services

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DHG Financial Services professionals provide you with in-depth industry knowledge and a wide range of advisory, assurance and tax services to address issues facing your industry in today's challenging environment.

### About DHG Credit Risk Management

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DHG Credit Risk Management is here to assist as you continue to navigate the evolving landscape of PPP lending. We have a dedicated team that works with subject matter leaders focused on the SBA PPP loan forgiveness initiative. We work diligently to provide industry intelligence and technical experience to help our clients.

<sup>3</sup> [SBA Procedural Notice 7/23/20](#), Page 3 of 8

<sup>4</sup> [PPP Frequently Asked Questions](#), #49

<sup>5</sup> This information is up to date, and within the guidelines established by the SBA (under the Department of Treasury), please [click here](#) for supporting information, and updated information.

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