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PPP Loans: Debits, Credits, and Financial Reporting FAQS

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The past twelve months have presented many new challenges, both personal and professional. Among the most prevalent professional challenges that many practitioners have faced over that time period began in March 2020 when Congress passed the Coronavirus Aid, Relief and Economic Security Act (CARES Act), which included the Paycheck Protection Program (PPP) and authorizing the Small Business Administration (SBA) to guarantee PPP loans that are forgivable if certain criteria have been met. Since that time, Congress added additional funds to the program in April 2020 and passed new legislation in December 2020 which opened a new window for PPP loans, allowing entities to take a first time loan or make a second draw loan if eligibility conditions were met.

As we approached the calendar year-end, we noticed a significant increase in inquiries from practitioners confirming clients had made the correct journal entries for PPP loans and had made the appropriate disclosures in financial statements. In this special report, we'll explore the debits and credits for PPP loans under the three primary models[1] covering when the loans are received and forgiveness is recognized, as well as the appropriate classification on the balance sheet, income statement, cash flow statement, and within the notes to the financial statements.

Want to know more about timing of derecognition?

While not covered in this report, we have written extensively on the timing of derecognition under each model, as well as other PPP/COVID related topics. A listing of those reports and resources can be found on our website.

[1] While an allowable option for accounting for PPP loans for commercial entities, this report will not discuss accounting for loans under FASB ASC 450-30 also known as the gain contingency model. From what we have seen in practice, this model is not used as frequently as the other three options which are presented in this report. In addition, please note the gain contingency model is not an option for not-for-profit entities.

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The positions expressed in this report should not be viewed as official positions of the AICPA. Official AICPA positions are determined through certain specific committee procedures, due process, and extensive deliberation. Application of U.S. generally accepted accounting principles (U.S. GAAP) is the responsibility of an entity's management.

Clear, authoritative guidance on the accounting for some aspects of PPP loans is lacking as of the writing of this report. Diversity of thought and multiple approaches exist, which we have noted throughout this report. Absent more authoritative guidance, practitioners will need to exercise professional judgment when determining the accounting for PPP loans.

In this report, the CPEA presents the current thinking on the accounting for PPP loans and we express our opinions, which may change in light of any subsequently issued guidance in this area. Our viewpoints do not represent positions of the AICPA or consensus views of stakeholders in the profession. We recommend rigorously documenting the decisions reached and reasons underpinning those decisions on significant judgments related to the accounting for PPP loans.

Financial Reporting for PPP loans

Meet our Business:

Within this report for all models discussed we are going to assume the same set of basic facts for simplicity that can be referred to throughout the remainder of this report:

Entity Type:	Commercial
Loan amount:	$100,000
Interest Rate:	1% (Monthly interest of $83, (rounded))
Loan Received:	June 1, 2020
Year-End:	December 31, 2020
Forgiven Date:	February 1, 2021 (SBA notification date)

Model #1: Account for PPP Loans as Debt Under FASB ASC 470, *Debt*

Q: Who can use this model?

Any nongovernmental entity can apply the debt model to account for PPP loans, including not-for-profit entities (NFPs). AICPA Technical Question and Answer (TQA) 3200.18, *Borrower Accounting for a Forgivable Loan Received Under the Small Business Administration Paycheck Protection Program (AICPA TQA),* indicates that the debt model can be used “regardless” of the situation, effectively sanctioning the model as a safe harbor.

Q: What is the journal entry when a loan is received?

Account	Debit	Credit
Cash	$ 100,000	
PPP Loan		$ 100,000

When the loan is received, the entity records a liability for the PPP loan amount. The title of the account used and related naming on the balance sheet can be a generic term such as ‘note payable’ and included with other debts, or it can be more specific wording that clearly identifies the loan as a PPP or SBA guaranteed loan.

Under this model, the entity is considering the loan to be debt. As a result, interest needs to be accrued each month:

Account	Debit	Credit
Interest Expense	$ 83	
Accrued Interest		$ 83

All PPP loans carry an interest rate of 1% as mandated in available guidance. Since the rate was set by a government agency, imputed interest is not required to be considered. For our client, based on the date and amount of their loan, at year-end, they will have accrued $583 of total interest ($83/month X 7 months). **Note:** Interest payments are not due until 10 months after the end of the covered period.

Q: How should costs incurred to obtain the PPP loan be accounted for?

Costs paid to third parties should be deferred and amortized over the course of the agreement as they would for any other debt instrument. Costs which would be deferred include accounting, advisory, and legal services as well as document preparation costs. For simplicity, in our example, we assume that such costs are zero.

Q: What is the journal entry when the loan is forgiven?

Account	Debit	Credit
PPP Loan	$ 100,000	
Accrued Interest	$ 666	
Forgiveness of PPP Loan		$ 100,666

For PPP loans accounted for under FASB ASC 470, the loan is not derecognized until legal release of the liability has occurred. As we detail in our February 2021 report, that likely would not occur until the bank/SBA has indicated that the loan has been repaid by the SBA. In our case, the loan was not formally forgiven until February 1, 2021, so the entity would need to record an additional month of accrued interest for January 2021 of $83. Combined with the previously recorded $583, that results in $666 of total interest forgiven.

Q: How should the PPP loan appear on the balance sheet at year-end?

Since our entity has not received forgiveness of the PPP loan prior to year-end, the loan will appear on the balance sheet. Since they intend to request forgiveness of their PPP loan, the CPEA believes that the entity may make a policy election on how to account for the loan on the balance sheet, choosing to either:

- Classify the entire balance based on contractual terms as they would any other long-term debt under FASB ASC 470 (including any potential current portion of long-term debt based on contractual repayment) or
- Classify the entire balance expected to be forgiven as current debt, analogizing to TQA 3200.12, if application for forgiveness is expected to be filed in current operating cycle

Further detail related to our thinking associated with the reporting options can be found in our October 2020 report. If the entity was intending to repay the debt opposed to receiving forgiveness, the loan would be classified in accordance with the contractual payment terms of the loan like any other debt.

In situations where entities expect partial forgiveness of loans, the CPEA believes entities may make the policy election described above for the portion they expect to be forgiven, and classify the amounts expected to be repaid in accordance with the contractual repayment provisions of the agreement and FASB ASC 470 guidance on debt classification.

As an important point of emphasis, **there is no explicit guidance that would apply to PPP loan classification** so, the above is our belief as to how the loans should be classified. As a result, reasonable arguments could be made for other classifications. To that end, we have seen filings from public companies that have taken varying approaches but included sufficient disclosure of the loans to allow users to understand the terms.

Q: How should the PPP loan appear on the income statement at year-end?

As legal release for the PPP loans had not yet been received for our example entity, there would be no forgiveness of debt recognized for the year-ended December 2020. This would be the case even if legal release was received prior to the issuance of the financial statements, as we discuss further in our February 2021 report. This would result in expenses that the loan was used for (the expenses which make the loan eligible for forgiveness) being incurred in a different period then when forgiveness is recognized.

When legal release has occurred and the liability is derecognized, the CPEA believes the most appropriate treatment is to record the forgiven amount as a separate line item in other income with an appropriately descriptive title, such as “Forgiveness of PPP Loan.” This treatment would be most consistent with how the extinguishment of debt is otherwise treated under U.S. GAAP.

While the CPEA believes the above approach to be the most appropriate, similar to classification on the balance sheet, an argument could be made for including forgiveness in the income statement items for which the expenses were incurred (as a reduction to payroll, utilities, rent, etc.) with disclosure of how those amounts were allocated in the notes. We do not advocate for this approach since it makes it harder for users to identify the amount forgiven and makes comparisons between periods of income statement amounts less meaningful.

Q: How should the PPP loan appear on the cash flow statement at year-end?

The initial proceeds of the loan should appear as a cash flow from financing activities. For our entity, since there was no forgiveness and no amounts paid for interest, there would be no additional impact on the year-end cash flow statement.

When the loan is forgiven, the forgiveness of the loan and any accrued interest would be a noncash financing activity. In order for the cash flow statement to balance, when forgiveness is recognized, the noncash gain is deducted from net income, similar to how depreciation is adjusted for in the cash flow statement.

In the event the loan was repaid opposed to forgiven, the repayments would be cash outflows from financing activities and cash paid for interest would appear as an additional disclosure item on the cash flow statement.

Q: What disclosures are required under FASB ASC 470?

There are no specific disclosure requirements for PPP loans that would differ from any other debt instrument. As a result, entities would need to disclose general information about the debt agreement including the amount borrowed, interest rate, repayment provisions, maturity date, and the amount outstanding at year-end.

PPP loans accounted for under FASB ASC 470 also would be included in the disclosure which outlines maturities of debts for the five years after the balance sheet date in accordance with the contractual provisions of the agreement when the entity intends to repay the loan. We believe that, when the entity intends for the loan to be forgiven, amounts which they have classified under the policy election to treat as they would any other long-term debt (including a potential current portion of long-term debt) also should be included within that schedule.

While the level of disclosure may vary by entity, a disclosure such as the following may be sufficient:

Illustrative Disclosure

On June 1, 2020 the Company received a loan in the amount of $100,000 under the Payroll Protection Program (PPP Loan). The loan accrues interest at a rate of 1% and has an original maturity date of two years which can be extended to five years by mutual agreement of the Company and the lender. Payments are deferred during the Deferral Period. The Deferral Period is the period beginning on the date of this Note, June 1, 2020, and ending 10 months after the last day of the covered period (Deferral Expiration Date). Any amounts not forgiven under the Program will be payable in equal installments of principal plus any interest owed on the payment date from the Deferral Expiration Date through the Maturity Date. Additionally, any accrued interest that is not forgiven under the Program will be due on the First Payment Date, which is the 15th of the month following the month in which the Deferral Expiration Date occurs.

Under the requirements of the CARES Act, as amended by the PPP Flexibility Act and Consolidated Appropriations Act, 2021, proceeds may only be used for the Company's eligible payroll costs (with salary capped at $100,000 on an annualized basis for each employee), or other eligible costs related to rent, mortgage interest utilities, covered operations expenditures, covered property damage, covered supplier costs, and covered worker protection expenditures, in each case paid during the 24-week period following disbursement. The PPP Loan may be fully forgiven if (i) proceeds are used to pay eligible payroll costs or other eligible costs and (ii) full-time employee headcount and salaries are either maintained during the 24-week period following disbursement or restored by December 31, 2020. If not maintained or restored, any forgiveness of the PPP Loan would be reduced in accordance with the regulations that were issued by the SBA. All the proceeds of the PPP Loan were used by the Company to pay eligible payroll costs and the Company maintained its headcount and otherwise complied with the terms of the PPP Loan.

Illustrative Disclosure (cont.)

While the Company believes that it has acted in compliance with the program and will seek forgiveness of the PPP Loan, no assurance can be provided that the Company will obtain forgiveness of the PPP Loan in whole or in part. The balance on this PPP loan was $100,000 as of December 31, 2020 and has been classified as current and non-current based on the contractual repayment terms.

Model #2: Account for PPP Loans as a Government Grant Under IAS 20, *Accounting for Government Grants and Disclosure of Government Assistance*

Q: Who can use this model?

For-profit nongovernmental entities may apply this model. Since there already is existing guidance under U.S. GAAP for NFPs for government grants, these entities may not apply IAS 20 but, instead, would follow the guidance in FASB ASC 958, *Not-for-Profit Entities,* more specifically FASB ASC 958-605, if they choose to account for PPP loans as a government grant opposed to debt.

While most for-profit entities likely do not have an existing policy for accounting for government grants, entities in the healthcare, bioresearch, and other industries may already have policies in place to account for government grants. If an entity already has a policy for accounting for government grants, they should consider if PPP loans are sufficiently similar to grants received in the past (as prescribed by FASB ASC 250, *Accounting Changes and Error Corrections*) and would fall under that policy or, if they differ enough to necessitate the creation of a new accounting policy. That determination will require judgment.

Some practitioners and clients also have questioned if applying guidance from an international standard such as IAS 20 would result in the financial statements no longer being considered issued under U.S. GAAP or otherwise require a departure from U.S. GAAP. Since there is no authoritative guidance in U.S. GAAP for a business entity, FASB ASC 105, *Generally Accepted Accounting Principles*, allows business entities to apply other guidance by analogizing to other guidance, such as international standards. As a result, in this situation, using IAS 20 would not be a departure from U.S. GAAP for a business entity.

Q: What is the journal entry when PPP funds are received?

Account	Debit	Credit
Cash	$ 100,000	
Paycheck Protection Program Liability		$ 100,000

When initially received, the PPP funds should be recorded as an income related grant, recording the amount as deferred income to be recognized as the criteria are met. The title of the liability on the balance sheet itself can vary, but we suggest a descriptive title such as included above.

Unlike considering the PPP loan as debt under FASB ASC 470, when entities determine that the PPP loan is considered an income related grant, interest is not accrued.

We have heard from some practitioners that lenders are asking clients to make interest payments on PPP loans despite the 10 month deferral period noted, which has caused some confusion on how to record those payments when accounting for a PPP loan under either the IAS 20 or FASB ASC 958-605 model since interest is likely not accrued since the PPP loan is not being accounted for as debt.

Assuming an entity anticipates receiving forgiveness of the PPP loan, any interest that the lender requires them to pay that will ultimately be returned to them should be recorded as an 'other asset' on the balance sheet (debit to other asset and credit to cash), which would then be reversed upon forgiveness. If this amount is material to the financial statements, disclosure would be appropriate.

Q: How should costs incurred to obtain the PPP loan be accounted for?

Costs paid to third parties should be expensed as incurred since the loan is accounted for as a government grant opposed to a debt instrument.

Q: What is the journal entry when the PPP loan is forgiven?

IAS 20 requires reasonable assurance that the criteria for forgiveness will be met in order for grant income to be recognized. While reasonable assurance is not defined, AICPA interpretations indicate that it may be analogized to "probable" as it is applied in U.S. GAAP. Once reasonable assurance has been attained, per IAS 20.12, government grants should be recognized in profit or loss on a systematic basis over the periods in which the entity recognizes as expenses the related costs for which the grants are intended to compensate. All things equal, this will result in recognition much sooner than other available methods of accounting for PPP loans as we outline fully in our July 2020 report on derecognition. This results in a greater likelihood of avoiding a mismatch in periods between when the expenses are incurred and when income is recognized.

Account	Debit	Credit
Paycheck Protection Program Liability	$XX,XXX	
Income- Government Grants		$XX,XXX

The titles of accounts for both recording the liability and recognizing the income from the grants will vary from entity to entity.

Q: How should the PPP loan appear on the balance sheet at year-end?

If the entity has not met the criteria for recognition for all or a portion of the grant, the remaining amount generally should be presented as a current liability. That classification is based on PPP funds needing to be spent within a specified period after receipt (a maximum of 24 weeks) in order to qualify for forgiveness, which is less than one year.

In the event the entity does not anticipate qualifying for forgiveness for the amounts which have not been recognized at year-end, the entity would classify the remaining amounts in accordance with the contractual repayment terms. This determination also would be considered a change in accounting estimate and should be accounted for accordingly.

Q: How should the PPP loan appear on the income statement at year-end?

IAS 20 allows entities the option of either recognizing income from government grants as a separate line item in other income or as a reduction to the associated expenses.

Entities are permitted to make a policy election as to which approach they believe is most appropriate in their circumstances.

Q: How should the PPP loan appear on the cash flow statement at year-end?

IAS 20 allows entities the option to account for PPP funds on the cash flow statement either as a cash flow from operations or as a cash inflow from financing activities. In practice, most entities choose to classify PPP loans as a cash flow from operating activities as the nature of the expenses that are being paid for via the grant are operational in nature. However, the CPEA believes classification of the cash inflows as a financing activity also would be acceptable.

Q: What disclosures are required under IAS 20?

IAS 20 includes specific disclosure requirements for government grants as follows:

a) the accounting policy adopted for government grants, including the methods of presentation adopted in the financial statements

b) the nature and extent of government grants recognized in the financial statements and an indication of other forms of government assistance from which the entity has directly benefited and
c) unfulfilled conditions and other contingencies attaching to government assistance that has been recognized

The criteria outlined above in (b) would include disclosure of the total amount received as a PPP loan as well as the amount recognized in income and remaining as deferred income as of the balance sheet date.

While the level of disclosure may vary by entity, a disclosure such as the following may be sufficient:

Illustrative Disclosure

In June 2020, the Company received a loan in the amount of $100,000 under the Payroll Protection Program (PPP Loan). The PPP Loan has a 2-year term and bears interest at an annual interest rate of 1%. Monthly principal and interest payments are deferred for 10 months, and the maturity date is June 1, 2022.

Under the terms of the CARES Act, PPP Loan recipients can apply for, and be granted forgiveness for, all or a portion of the PPP Loan and accrued interest. Such forgiveness will be determined, subject to limitations, based on the use of PPP Loan proceeds for payment of payroll costs and any payments of mortgage interest, rent, utilities, covered operations expenditures, covered property damage, covered supplier costs, and covered worker protection expenditures, and retention of employees and maintaining salary levels. However, no assurance is provided that forgiveness for any portion of the PPP Loan will be obtained.

In June 2020, the AICPA issued TQA 3200.18, *Borrower Accounting for a Forgivable Loan Received Under the Small Business Administration Paycheck Protection Program*. The TQA addresses accounting for nongovernmental entities that are not NFPs, i.e. business entities, that believe the PPP Loan represents, in substance, a grant that is expected to be forgiven, it may account for the PPP Loan as a deferred income liability. The TQA further indicates that, if such an entity expects to meet the PPP's eligibility criteria and concludes that the PPP Loan represents in substance, a grant that is expected to be forgiven, it may analogize to IAS 20 to account for the PPP Loan.

Illustrative Disclosure (cont.)

IAS 20 provides a model for the accounting of different forms of government assistance, which includes forgivable loans. Under this model, government assistance is not recognized until there is reasonable assurance (similar to the probable threshold in U.S. GAAP) that any conditions attached to the assistance will be met and the assistance will be received.

As of December 2020, we have used the full amount received to fund eligible payroll, rent, and utility expenses under the terms of the PPP Loan. As a result, we believe and expect that we will meet the PPP eligibility criteria for forgiveness and have concluded that the PPP Loan represents, in substance, funds provided under a government grant. As such, in accordance with IAS 20, we have recognized the use of $100,000 of the PPP Loan proceeds as of December 31, 2020 as Other Income.

Model #3: Account for PPP Loans as a Government Grant Under FASB ASC 958-605

Q: Who can use this model?

This model is available to both NFP and for-profit nongovernmental entities if the loan meets certain criteria. If a nongovernmental entity that is not an NFP (that is, it is a business entity) expects to meet the PPP eligibility criteria and concludes that the PPP loan represents, in substance, a grant that is expected to be forgiven, the AICPA staff observed in TQA 3200.18 that it also can analogize to the guidance in FASB ASC 958-605.

Q: What is the journal entry when PPP funds are received?

Account	Debit	Credit
Cash	$ 100,000	
Refundable Advance		$ 100,000

Using the conditional contribution model under FASB ASC 958-605, the entity would initially record the loan as a refundable advance.

Q: How should costs incurred to obtain the PPP loan be accounted for?

Costs paid to third parties should be expensed as incurred since the loan is accounted for as a conditional contribution opposed to a debt instrument.

Q: What is the journal entry when a PPP loan is forgiven?

Account	Debit	Credit
Refundable Advance	$XX,XXX	
Contribution Revenue		$ XX,XXX

FASB ASC 958-605 indicates that a transfer of assets that is a conditional contribution is accounted for as a refundable advance until the conditions have been substantially met or explicitly waived by the donor. Therefore, in lieu of loan treatment, the PPP loan would be treated more similarly to deferred revenue. The key to determining when to recognize the contribution revenue is when the conditions have been "substantially met." Under FASB ASC 958-605, conditions can be met in stages- or over a period of time.

A major change from the legacy standard to FASB ASC 958-605 Conditional Contribution model (in the amendments in ASU 2018-08) is related to probability. A probability assessment about whether the recipient is likely to meet the stipulation is NOT a factor when determining whether an agreement contains a barrier. Therefore, even if an NFP is certain it will hit the required targets, that does not mean that the PPP funds would be recorded as revenue upon receipt. The conditions would have to be met before recognizing revenue.

There is an argument to be made in some cases that, once an entity has met the requirements (which clearly meet the definition of a condition under FASB ASC 958-605 such as full time equivalent employees, limitation in reduction in compensation, and qualified expenses), the conditions have been substantially met and; therefore, having to submit loan forgiveness documents is merely an administrative matter especially if the PPP loan is under the required bank/SBA review threshold of $2,000,000. However, uncertainties may exist with particular PPP loan recipients which may mean that the bank/SBA review should be treated as an additional condition under FASB ASC 958-605.

Similar to the IAS 20 model, since recognition of a contribution occurs as conditions are substantially met, the entire amount is not typically recognized at the same time. However, as discussed above, if the bank/SBA review is deemed to be a condition, recognition of a contribution would not take place until the bank/SBA review is completed and satisfied. Since recognition of the contribution under FASB ASC 958-605 is delayed until the most restrictive condition has been substantially met, the presence of a condition under FASB ASC 958-605 for the bank/SBA review likely will delay contribution recognition for the full amount until well after the covered period for expenses.

Q: How should the PPP loan appear on the balance sheet at year-end?

Under this model, the only balance sheet item related to the PPP loan would be the refundable advance that is recorded on the date the loan is received. That refundable advance gets reduced as the contribution income is recognized and the conditions for recognition are substantially met. The refundable advance would be classified as a current liability, assuming the entity expects to meet the remaining criteria.

If at any point the entity expects that all or a portion of the PPP loan will need to be repaid and will not be forgiven, it should continue to show that amount as a refundable advance and consider a need for an interest accrual.

Q: How should the PPP loan appear on the income statement at year-end?

The loan would appear as contribution revenue for the portion where the conditions for recognition have been substantially met. Similar to other approaches, the CPEA encourages entities to break-out these amounts separately from other revenue to both ensure that users of the financial statements are aware of the amount recognized and enhance comparability between other line items. In addition, under FASB ASC 958-605, entities should not net PPP loan forgiveness with related expenses on the income statement.

Q: How should the PPP loan appear on the cash flow statement at year-end?

The initial proceeds of the loan should appear as cash flow from operating activities as increase in refundable advance and, then, net income for any amounts that were recognized into income during the year.

Q: What disclosures are required?

Entities should ensure that disclosures clearly explain the interpretation of what conditions are included and when they are deemed to be substantially met.

While the level of disclosure may vary by entity, a disclosure such as the following may be sufficient based on the disclosure requirement for a conditional promise to give in FASB ASC 958-310-50-4:

Illustrative Disclosure

In June 2020, the Company received a loan in the amount of $100,000 under the Payroll Protection Program (PPP Loan). The PPP Loan and accrued interest are forgivable after the covered period, up to 24-weeks, if the borrower uses the PPP Loan proceeds for eligible purposes, including payroll, benefits, rent, utilities, covered operations expenditures, covered property damage, covered supplier costs, covered worker protection expenditures and maintains its payroll levels. The amount of the PPP Loan forgiveness will be reduced if the borrower terminates employees or reduces salaries during the covered period, up to 24-weeks. The unforgiven portion of the PPP Loan is payable over 2 years at an interest rate of 1%, with a deferral of payments for the first 10 months.

The Company expects to meet the PPP's eligibility criteria and, therefore, has concluded that the PPP Loan represents, in substance, a grant that is expected to be forgiven. As a result, the Company has accounted for the PPP Loan in accordance with FASB ASC 958-605 as a conditional contribution. The Company initially recorded the amount received as a refundable advance followed by a reduction in the advance and recognition of revenue as the aforementioned conditions are substantially met. During the year ended December 31, 2020, the Company has used the entire proceeds for purposes consistent with the PPP, resulting in recognition of the entire PPP Loan amount as contribution revenue in the accompanying financial statements.