Higher Education Accounting for COVID-19 Pandemic Relief Packages

To date, the United States government has passed three new laws designed to help the nation respond to the coronavirus (COVID-19) pandemic.

The first is the Coronavirus Preparedness and Response Supplemental Appropriations Act, 2020 (enacted March 6, 2020), which provides $7.8 billion in emergency funding for the development and manufacture of vaccines and other supplies; support to state, local, and tribal public health agencies; loans to affected small businesses; evacuations and emergency preparedness activities; and humanitarian assistance for affected countries. It also provides $490 million for expanded telehealth options through the Medicare program.

The second is the Families First Coronavirus Response Act (enacted March 18, 2020), which is intended to give relief to individuals affected by COVID-19 by, for example:

- Giving state governments the flexibility to interpret unemployment insurance eligibility as well as $1 billion in grants to pay for and process claims.
- Granting temporary emergency paid sick leave and paid family and medical leave for COVID-19-related reasons (primarily for employers with fewer than 500 employees and public agencies).
- Offering an employer payroll tax credit to offset the cost of paid leave.
- Increasing funding and expanding access to nutrition assistance for schools, low-income children, and seniors.
- Requiring private insurers, Medicare, and Medicaid to cover COVID-19 diagnostic testing at no cost and providing $1 billion for uninsured individuals to receive access to free testing.

The third and most recent law (enacted March 27, 2020) is the Coronavirus Aid, Relief, and Economic Security Act (CARES Act or the Act), which, from a monetary-relief perspective, dwarfs the prior two acts.

Most companies are receiving benefits, funding, loans and relief in some way from one or more of these laws. Below, we attempt to provide some guidance on how these various programs should be accounted for in a company's financial statements.

ECONOMIC INJURY DISASTER LOANS

Small business owners (generally employers with less than 500 employees but other stipulations apply and are industry specific) may be eligible to apply for an Economic Injury Disaster Loan (EIDL) of up to $2,000,000 because of the COVID-19 disaster. The loan is made by the Small Business Administration directly and up to a $10,000 advance on the loan can be requested. This loan advance will not have to be repaid.

For more information on this program, click here.

Accounting Considerations

These loans should be recorded as debt and interest should be recognized on the basis of the stated contractual terms. Borrowers should not impute interest on the basis of market rates.

The potential $10,000 advance that does not have to be repaid should be accounted for using a reasonable accounting model applicable to grants provided by governmental entities.

PAYCHECK PROTECTION PROGRAM

The $349 billion Paycheck Protection Program (PPP) is one of the largest relief packages of the CARES Act. Overseen by the U.S. Treasury Department, the PPP offers cash-flow assistance to nonprofit and small business employers, among others, through guaranteed loans for eligible expenses. The maximum loan amount per borrower is the lesser of:

(1) 2.5 times average monthly payroll costs during the previous one-year period (or alternative period if a seasonal business) plus the outstanding amount of any existing EIDL loan made between January 31, 2020 and April 3, 2020 (less any EIDL loan advance) that is being refinanced under the PPP, and

(2) $10 million.

These loans are potentially forgivable if the funds are spent appropriately. For more information on this program, click here.

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PAYCHECK PROTECTION PROGRAM

Accounting Considerations

There is no guidance in U.S. GAAP that specifically addresses the accounting by an entity that obtains a forgivable loan from a government entity. In the absence of specific guidance, U.S. GAAP instructs companies to use the most applicable authoritative guidance based on their specific circumstances. Entities may determine that Paycheck Protection Program Loans (PPPLs) represent government grants and account for them by using a reasonable accounting model applicable to grants provided by a government entity. Alternatively, entities may determine that it is appropriate to account for PPPLs as debt. We expect that if PPPLs are treated as debt instruments, borrowers would apply the interest method of recognizing interest expense in ASC 835-30, which should take into consideration the payment deferrals allowed for these loans. Entities should not impute additional interest on these loans by using a market rate even though the stated interest rate may be considered below market because ASC 835-30-15-3(e) excludes such loans from the scope of ASC 835-30. However, a borrower applying debt accounting should be mindful of the guidance in ASC 405-20-40-1, which indicates that "a debtor shall derecognize a liability if and only if it has been extinguished." In accordance with ASC 405-20-40-1(b), the portion of the principal payments to be forgiven on PPPLs would be extinguished for accounting purposes only when the "debtor is legally released from being the primary obligor under the liability."

We expect further discussions with standard setters, regulators, or both regarding (1) the appropriate application of U.S. GAAP to the borrower's accounting for PPPLs (i.e., whether PPPLs are accounted for as debt or as government grants) and (2) the disclosures that should be made for borrowers that obtain such loans. We will update this information as further guidance is released.

REFUNDABLE PAYROLL TAX CREDITS FOR EMPLOYERS

The Families First Coronavirus Response Act, or H.R. 6201, provides for refundable tax credits for employers required to provide paid sick or family leave, which can be taken against the employer's share of Social Security tax or Railroad Retirement tax.

Employers are entitled to a refundable payroll tax credit equal to 100% of "qualified sick leave wages" paid each calendar quarter. "Qualified sick leave wages" are those paid under the provisions of the Emergency Paid Sick Leave Act.

The amount of qualified sick leave wages an employer can take into account per employee is capped at the employee's regular rate of pay, up to $511 per day and $5,110 total, for employees who are unable to work (which includes telework) because they (1) are subject to a federal, state, or local quarantine or isolation order related to coronavirus; (2) have been advised by a healthcare provider to self-quarantine due to coronavirus concerns; or (3) are experiencing symptoms of coronavirus and seeking a diagnosis. For employees who are unable to work because they are caring for (1) another individual subject to a quarantine or isolation order or who has been advised by a healthcare provider to self-quarantine; or (2) a child whose school or place of care is closed due to coronavirus precautions, the amount of qualified sick leave wages the employer can take into account is capped at two-thirds the employee's regular rate of pay, up to $200 per day, and $2,000 total. The total number of days an employer can take into account per employee is limited to 10 days for all calendar quarters.

Employers also are entitled to a refundable payroll tax credit equal to 100% of "qualified family leave wages" paid each calendar quarter. "Qualified family leave wages" are wages paid under the Emergency Family and Medical Leave Expansion Act. The amount of qualified family leave wages an employer can take into account per employee is capped at two-thirds the employee's regular rate of pay, up to $200 per day and $10,000 total for all calendar quarters.

Both the paid sick and family leave tax credits are increased to include qualified health plan expenses allocable to the qualified sick and family leave wages.

Employers must include the full amount of the tax credits in gross income. Employers may deduct as a business expense amounts paid to an employee for qualified leave wages (and any allocable qualified health plan expenses) for which the employer expects to claim tax credits, if the employer is otherwise eligible to take the deduction.

For more information on the refundable payroll tax credits for paid sick and family leave, click here.

Accounting Considerations

While we wait for additional guidance from standard setters, we recommend accounting for these tax credits as a reduction to the applicable expenses.

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DEFERRAL OF EMPLOYER PAYROLL TAXES

The CARES Act provided an option for businesses to defer payment on certain payroll taxes. Employers and self-employed individuals can defer payment of the employer share of Social Security taxes payable for all reporting periods through the end of 2020. The deferred tax liability is due in two installments: (1) 50% of the deferred liability is due December 31, 2021; and (2) 50% of the deferred liability is due December 31, 2022 (the "applicable dates").

Generally, all employers are eligible for payroll tax deferral. However, the CARES Act provides that the deferral of employer payroll taxes does not apply to employers who have had debt forgiven with respect to a PPP loan. On April 10, the IRS issued guidance stating that employers who have received a PPP loan, but whose loan has not yet been forgiven, may take advantage of the deferral through the date the lender issues a decision to forgive the loan. In addition, the amount of the deposit and payment of the employer's share of Social Security tax that was deferred through the date the PPP loan is forgiven continues to be deferred and will be due on the applicable dates. This was good news for employers, as it provides a mechanism for businesses who have applied for PPP loans to free up current cash flow until the loan is forgiven.

The payroll tax deferral period began on March 27, 2020 (the date of enactment of the CARES Act) and ends on December 31, 2020.

For more information, read our recent articles, *The Deferral of Employer Payroll Taxes* and *The IRS Issues Guidance on Deferral of Employer Payroll Taxes – It Includes Some Good News*.

Accounting Considerations

These expenses should continue to be recognized in the period in which the expense was incurred (e.g. the respective payroll periods under which the taxes were due based on employee compensation). The unpaid portions should be recorded as a liability until paid.

EMPLOYEE RETENTION TAX CREDITS

The CARES Act provides businesses with an optional employee retention tax credit if certain criteria are met.

Eligible businesses are employers, including tax-exempt organizations, which were carrying on a trade or business during calendar year 2020 and meet one of the following criteria:

1. The operation of the business is fully or partially suspended during the calendar quarter due to orders from an appropriate governmental agency limiting commerce, travel, or group meetings because of COVID-19; or
2. The calendar quarter is within the period that: (1) begins with the first calendar quarter after December 31, 2019, for which gross receipts are less than 50% of gross receipts for the same calendar quarter in the prior year; and (2) ends with the calendar quarter following the first calendar quarter for which gross receipts are greater than 80% of gross receipts for the same calendar quarter in the prior year.

The operation of a business is "partially suspended" if the business can continue to operate, but not at its normal capacity.

Governmental employers, including the federal government, state and local governments, and governmental agencies and instrumentalities, are not eligible employers. Self-employed individuals also are not eligible for the employee retention tax credit.

Eligible employers receive a refundable quarterly payroll tax credit equal to 50% of the "qualified wages" paid with respect to each employee. The definition of "qualified wages" varies depending on the average number of full-time employees employed by the employer during 2019. The credit applies to qualified wages paid after March 12, 2020, through and including December 31, 2020. The maximum amount of qualified wages that may be taken into account with respect to each employee for all calendar quarters is $10,000.

The credit is allowed against the employer portion of Social Security taxes and the portion of taxes imposed under the Railroad Retirement Act that corresponds to Social Security taxes.

Employers are not eligible for employee retention tax credits if they receive a PPP loan.

For more information on the employee retention tax credit, click here.

Accounting Considerations

While we wait for additional guidance from standard setters, we recommend that credits taken or refunded under the employee retention tax credit program should be accounted for using a reasonable accounting model applicable to grants provided by a government entity.

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TERM LOAN, MORTGAGE, OR LEASE MODIFICATIONS AS A RESULT OF COVID-19

Many businesses have seen significant impacts on their monthly cash flows as a result of COVID-19. Many banks and lending institutions are being flexible with payment terms and loan modifications. Borrowers that receive forbearances within relief offered in the CARES Act or outside of this relief would need to evaluate whether such forbearances represent Troubled Debt Restructuring (TDR) under ASC 470-60 in consultation with your accountant and lender.

If such forbearances do not represent TDRs, borrowers would need to consider whether such forbearances represent a modification or extinguishment of their loans under ASC 470-50. In addition, borrowers would need to consider the impact of such forbearances on their recognition of interest under the TDR guidance in ASC 470-60 or the interest method guidance in ASC 835-30.

NONFINANCIAL ASSET IMPAIRMENT

Disruptions to business operations and increased economic uncertainty due to COVID-19 may trigger the need to perform impairment testing in the first half of 2020. Estimating future cash flows to calculate the recoverable amount will be challenging given the high level of uncertainty.

SUBSEQUENT EVENT ACCOUNTING

(Information below obtained from the AICPA)

Entities may need to evaluate whether the consequences of COVID-19 represent subsequent events. FASB *Accounting Standards Codification* (FASB ASC) 855, *Subsequent Events*, defines subsequent events as events or transactions that occur after the balance sheet date but before financial statements are issued or are available to be issued. There are two types of subsequent events:

- The first type consists of events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements (that is, recognized subsequent events).
- The second type consists of events that provide evidence about conditions that did not exist at the date of the balance sheet but arose subsequent to that date (that is, nonrecognized subsequent events)

Practice Note: For calendar year end 2019 financial statements, any COVID-19 related subsequent events identified likely are to be nonrecognized subsequent events (Type II).

Some nonrecognized subsequent events may be of such a nature that financial statement disclosure is required to keep the statements from being misleading. In these situations, financial statements need to include disclosure of the following:

- The nature of the event or events
- An estimate of the financial statement effect of the event or events, or a statement that the estimate cannot be made

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EDUCATION STABILIZATION FUND: SEC. 18004

The CARES Act provided approximately $14 billion in direct support for higher education institutions allocated in the following way:

- Allocates 90 percent ($12.558 billion) directly to institutions through the Title IV distribution system.
  - » Institutional amounts are calculated using 75 percent of full-time equivalent enrollment of Pell students at an institution and 25 percent of the institutional award is calculated using full-time equivalent enrollment of non-Pell students.
  - » Students who were exclusively online are removed from the calculation.
  - » At least 50 percent of funds (or $6.279 billion) awarded to institutions must be used to provide direct emergency aid to students, including "grants to students for food, housing, course materials, technology, health care, and child care."
  - » Allowable uses for the institutional portion of the funds are broad, and can be used to "defray expenses for institutions of higher education, such as lost revenue, technology costs associated with a transition to distance education."
  - » Recipients of funds must retain current employees to the "maximum extent practicable."
- Reserves 7.5 percent ($1.047 billion) for minority-serving institutions (MSI).
- Reserves 2.5 percent ($349 million) for grants to institutions particularly impacted by coronavirus, to be administered through
  - » Priority for these grants goes to smaller institutions who received less than $500,000 under the formula and MSI grants and still have significant unmet need.

Are these funds considered student financial assistance?

According to the Recipient's Funding Certification and Agreement for the Emergency Financial Aid Grants to Students under the CARES Act, emergency grants to students are not considered Title IV aid under the Higher Education Act of 1965.

Should these funds be included on the Schedule of Expenditures of Federal Awards?

Yes! Grant funds from the $14 billion Higher Education Emergency Relief Fund (HEERF) in the Education Stabilization Fund should fall under CFDA 84.425E. For more information, visit the Department of Education website.

Do we know the specific compliance requirements related to these funds?

Depending on the amounts received and other factors considered, these grant funds could become a major program within your single audit. However, set audit procedures surrounding these funds do not exist. Additionally, the Department of Education has not specified how each institution should award these funds. Therefore, testing procedures will be based upon your policies and procedures.

Accounting considerations:

Institutions should account for these grant revenues in a similar manner to other non-operating federal grant dollars received.

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