PPP Loan Accounting for Manufacturers | Ask the Experts Video Transcript

Chad Martin, Director & Manufacturing Practice Leader
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Kat Jenkins (00:08):

Hi, and welcome to Barnes Dennig Ask the Experts. I'm Kat Jenkins, marketing director. And today we have manufacturing practice leader and Barnes Dennig director Chad Martin, talking PPP loan accounting for manufacturers with Nick Pennekamp from our COVID-19 advisory team. Chad, Nick, thanks for joining us today.

Nick Pennekamp (00:29):

Thanks Kat. We'll jump right into it. Chad, I've got a couple of questions for you. First one being there's a lot of discussion and information about PPP loans. This year, an entity can receive a loan that is forgivable by the SBA. How does the company get forgiveness for this loan?

Chad Martin (00:46):

That's a great question, Nick, let's go back on that PPP loan program and look at the loan application process. And if you recall back in March and April, as we were carrying those, it took a time period of 10 weeks worth of payroll cost is what was included on that application to receive those funds on the PPP loans. From the funds that were received, the company then initially had eight weeks to spend those funds and to spend those on items such as our payroll costs, rent and utilities and certain health insurance and retirement payments, some interest on certain loans, some of the employment taxes on those types of things that the company could spend those funds on. As they went through that time and spent those funds, then they could fill out yet another form of forgiveness application to submit and ultimately to the SBA to receive their forgiveness amount on that loan. And with that time period there of that, that initial eight-week period, it required some companies to get rather creative on the cost that they were incurring.

Nick Pennekamp (02:01):

So the first few months of the pandemic were a little scary. Businesses that were not essential were shutting down. Future customer orders were in question. We didn't know if any of the businesses were ever going to get back to normal. What are some of the creative ways that companies combated this and kept their employees on payroll?

Chad Martin (02:19):

Well, and Nick, if you look at that concept of the PPP loan and they were spending that money during that time, they had to increase primarily their payroll costs is what they use because that was the big driver on the PPP loan program. So some companies would increase the hourly wage rate for their hourly workers. Called it something like a hazardous duty pay to increase those wages. Their salary to employees, they would provide a discretionary bonus to those salaried employees. During that time again, to increase their labor costs. A lot of companies have a Christmas bonus. Some companies pull that Christmas bonus up until that time period in April and May during their forgiveness period, even possibly taking the Christmas party that they figured they probably would not be able to have in December and use that money to pay out as labor costs during that forgiveness time. One company even revamped their PTO policy during that forgiveness time. And they paid out a contribution to employees' retirement accounts in lieu of lost PTO during that policy change. Then just get other companies were paying health insurance stipends, such as a one-time payment to an HSA account for their employees.

Nick Pennekamp (03:45):

So the pandemic has changed the way we've been interacting with people, entering buildings, dining and restaurants. Becoming second nature is wearing masks nowadays. Likewise companies have made changes to their physical operations and protecting their employees sanitizing other than the PPP loan costs. What are some types of expenses companies are incurring this year?

Chad Martin (04:07):

Companies are incurring different costs related to the pandemic. And as individuals we're familiar with the face masks and with hand sanitizer. And if you recall, during that time, there were shortages of those. And we found that personal protective equipment companies as well were purchasing face mask and hand sanitizer. We saw them purchasing face shields for employees. We saw plexiglass shields going up. Most retail outlets that you go into today at the checkout counter, that will be some type of a plexiglass shield in place there. The cleansers that are used for common touch areas inside of a company are being purchased. Some companies are hiring additional cleaning contractors to come in and cleanse or sanitize their facilities. We saw other companies who hired onsite health professional to provide those screenings for employees and visitors coming into their facility. And a few companies went so far as purchasing a system that would automatically read a person's body temperature. And if that temperature was too high, that system would lock certain doors and prevent access to certain areas of the building. We saw this particularly in cases where there was a delivery driver who before might have more freedom and movement inside of a building, but now they're limited to a very strict and small area, if at all inside the building.

Nick Pennekamp (05:41):

All right. So manufacturing companies, they use a standard costing system for tracking inventory and cost of goods sold within a system. What should a company do to account for these additional pandemic costs?

Chad Martin (05:55):

Nick is as you know, working with a lot of our manufacturers, they use a standard cost system. And the premise of that standard cost system is using an average cost of producing goods on a repetitive basis. So the company will take the budgeted amount of costs, labor materials, and overhead, divide that by a budget of units of production and labor hours to come up with these standard costs at the beginning of the year. And then it's actual costs or incurred during, throughout the year. And actual cost was compared to the standard cost and it would any underage or overage would cause a variance.

Chad Martin (06:36):

If the budget was pretty close and the company could fairly manage its production cycle, these variances would be rather small. The best reflection of these additional PPP loan program costs would be to post them to the sales general and administrative area of the income statement because they are a discretionary cost incurred by the company. It's not a direct cost in producing that their goods.

Chad Martin (07:05):

Some companies applied for and received grants to help offset these costs. The grants come in are received and they should be recorded on a gross basis to other income, as opposed to offsetting the expense.

Chad Martin (07:27):

Outside of the PPP loan costs, there are those costs for the face masks and the contractors to come in and clean up, those costs as well should be posted to the selling general and administrative area of the income statement.

Nick Pennekamp (07:43):

So does the manufacturing company have an option to record these additional PPP related costs to cost of goods sold? And if they choose that, what are some of the ramifications for doing that?

Chad Martin (07:54):

This is a great question. And we've had that question from quite a few manufacturing companies around the area. Yes, the manufacturer does have a choice on whether they post their PPP loan program payroll expenses through their standard costing system. If they choose to do that, then that actual cost of additional labor in that April, may, June timeframe is going to cause their labor variances to spike, because they're paying more for the labor costs. With those variances in labor, then that's going to require them then to capitalize those variances onto the balance sheet as additional inventory, because it's an indicator of increased production costs for the inventory of the items. The company needs to consider that this possible overstatement of inventory might drive them to re cord a reserve for this overvalued inventory if they choose that method.

Nick Pennekamp (09:00):

All right, the question we're all wondering: earlier, you mentioned PPP loan forgiveness. There are companies with these loans on their books and the finance managers are wondering how do they post this loan forgiveness to income? And what would you tell a finance manager asking these questions?

Chad Martin (09:18):

We've had this question from quite a few finance managers as well. The PPP loan program has created quite a unique type of transaction for a lot of companies.

Chad Martin (09:33):

That being said U.S. GAP does not have a specific county rule on point with how and when to record that debt forgiveness from the PPP loan, there are four different accounting rules that are alternatives for a company that they could use and how they record that debt forgiveness and when they do that, and also keeping in mind this PPP loan program has been in a state of continuous change since it came out. So we're watching as more changes are being made even through this month. Now that finance manager is also going to have some income tax considerations that they need to take into account when recording the debt forgiveness from the PPP loan forgiveness, each company is going to be in a different situation with different factors and different drivers for their decision making, and they should reach out to their advisor. I would have them reach out to Barnes Dennig to talk more about their debt forgiveness.

Nick Pennekamp (10:42):

Chad, thanks so much for answering all these questions. That's all I've got for you today.

Chad Martin (10:45):

Thank you, Nick.