



 **City National Bank**
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Paycheck Protection Program Loan- A Matter of Forgiveness

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AGENDA

Part I

Paycheck Protection Program –
An Overview

Part II

Allowed Use of PPP Loan
Proceeds

Part III

Loan Forgiveness and Examples

Part IV

A Bank's Perspective

Part IV

Q&A

Part I – Paycheck Protection Program – An Overview

PPP Loan - Brief Introduction

The Keeping American Workers Paid and Employed Act is designed to keep workers from losing their jobs and maintaining small businesses due to the coronavirus pandemic. It enables cash-flow assistance through federally guaranteed loans to employers who maintain their payroll during the coronavirus crisis.

The Paycheck Protection Program provides hundreds of billions in loans for qualifying small businesses.

Paycheck Protection Program

PPP Loans

- Loans are to be available through existing Small Business Administration-certified and approved lenders, including banks, credit unions, and other financial institutions, and other lenders approved by the Small Business Administration (“SBA”);
- Loan proceeds are to be used for certain defined expenses during an 8 week period beginning upon the funding of the loan (called the “Covered Period”);
- The PPP Loans can be forgiven (in whole or in part) depending on various factors.

Payroll Costs

The CARES Act “Payroll Costs” include

- Wages
- Commissions
- Tips
- PTO (including paid sick leave)
- Severance or separation pay
- Payments for group health benefits including premiums
- Payment of retirement benefits;
- Payments of state or local tax assessed on compensation of employees.

*Note that for Payroll Costs, compensation payments (i.e. salary) per employee are capped at \$100,000 annualized per employee

Payroll Costs

The CARES Act uses “Payroll Costs”

- 1) To calculate the Loan Amount (using Payroll Costs from a prior period);
- 2) As an allowable use of the loan proceeds (for Payroll Costs during the Covered Period);
- 3) And to Calculate in part the amount of the loan that may be forgiven (for Payroll Costs during the Covered Period).

Guidance from the U. S. Small Business Administration has added a further qualification on how to use Payroll Costs: not more than 25% of the loan forgiveness amount may be attributable to non-payroll costs.

Pending Guidance

We Await Guidance

- The previous guidance issued on PPP loans explicitly states that the Government will issue Guidance on Loan Forgiveness. However, as of this date it has not been issued and no estimate has been given of when it will be issued.
- At this time, there remain many questions on how various provisions will be implemented.
- Recommend reviewing PPP Loan Forgiveness with CPA and Counsel after guidance is released and prior to submitting package to bank.

Part II – Allowed Use of PPP Loan Proceeds

Allowable Uses

A loan recipient can only use the loan proceeds for the following costs incurred and payments made during an 8-week period after the origination of the loan. The allowable uses are:

- Payroll costs as defined above,
- Any payment of interest on any covered mortgage obligation (not including any principal) – generally for debt incurred on property before February 15, 2020,
- Any payment on any covered rent obligation (under a lease in effect before February 15, 2020), and
- Any covered utility payment which generally are for utility payments for services which began before February 15, 2020.

Allowable Uses

Guidance as to 75% of Proceeds

- Interim Rule added a qualification of use of the proceeds: A FAQ stated that “At least 75 percent of the PPP loan proceeds shall be used for payroll costs.”
- We do not have any guidance about whether this is based on the total loan amount or the actual amount used.
- This qualification also limits the forgiveness amount.

Part III – Loan Forgiveness and Examples

Loan Forgiveness

Guidance on Loan Forgiveness

- Between the CARES Act and the Guidance, there are several limits and qualifications on what can be forgiven.
- There are still many questions that remain and the promised Guidance (which hopefully answer those questions) has not been issued.
- Despite the lack of Guidance, the CARES Act does lay out the general parameters and calculation of loan forgiveness.

Maximum Potential Forgiveness Amount

Total Forgivable Amount

- The CARES Act outlines that a loan recipient is eligible for forgiveness “in an amount equal to the sum” of the same categories of “Allowable Uses” described above.
- Therefore, if you only use the loan for the “Allowable Uses,” then that entire amount will be your maximum forgivable amount .
- After determining your maximum forgivable amount, at this time there are three possible reductions.

75% Limit from Guidance

First Reduction

- The Interim Final Rule titled “Business Loan Program Temporary Changes; Paycheck Protection Program” created an additional limit on the maximum loan forgiveness amount.
- The Rule states that “not more than 25 percent of the loan forgiveness amount may be attributable to non-payroll costs.”
- This would therefore limit the maximum loan forgiveness amount even if all of the costs were Allowable Uses.

CARES Act Limitations on Forgiveness

Second and Third Reductions

- The CARES Act outlines two limitations on the Forgiveness Amount:
 - First, a proportional reduction in the forgiveness amount based on the number of “Full Time Equivalent Employees” on your payroll during the covered period compared to a previous choice period;
 - AND a dollar for dollar reduction for any reduction exceeding 25% of the salary or wages of any employee (excluding those who make less than \$100,000 annualized during any period last year).

CARES Act Limitations on Forgiveness

Forgiveness in the CARES Act

- The CARES Act also states that in the same section as above that “the amount of loan forgiveness under this section shall be determined without regard to” two circumstances:
 - First, if the employer has “eliminated the reduction in the number of full time employees” by June 30th (meaning rehired employees laid off between Feb 15 and 30 days after the CARES Act Passed); and
 - Second, if the employer “has eliminated the reduction in the salary or wages of [] employees” (meaning the employer restored the pay of those employees whose pay was reduced between Feb 15 and 30 days after the CARES Act Passed).

CARES Act Limitations on Forgiveness

Forgiveness in the CARES Act

- Therefore, pending regulations on the issue, it appears that employees rehired or whose pay is restored will not count against an employer for loan forgiveness.
- No Guidance has interpreted as to how this would be calculated.

Guidance on Forgiveness

Forgiveness in the CARES Act

- One FAQ does address the issue of employees who are not willing to return to work: it states that “SBA and Treasury intend to issue an interim final rule excluding laid-off employees whom the borrower offered to rehire (for the same salary/wages and same number of hours) from the CARES Act’s loan forgiveness reduction calculation.”

Forgiveness Formula

Proposed Formula based on CARES Act and Guidance: Step One

- First Calculate Payroll Costs expended during the Covered Period which consist of gross compensation paid to employees (capped at \$100,000 annual rate per employee) and employer contributions for health care coverage, retirement plan contributions and payment of state and local taxes assessed on employee compensation.
- Next Calculate Non-Payroll Costs expended during the Covered Period which consist of payments of interest on mortgage obligations, rent payments and utility payments.

Forgiveness Formula

Proposed Formula based on CARES Act and Guidance: Step Two

- To calculate the Maximum Allowable Amount eligible for forgiveness under the PPP divide your calculated Payroll Costs by 75 percent. If the total amount of your Payroll Costs and Non Payroll costs added together exceeds this amount, you must reduce your non-payroll costs so that when added to your Payroll costs it does not exceed the Maximum Allowable Expense (amount calculated by dividing your Payroll Costs by 75 percent).

Forgiveness Formula

Proposed Formula based on CARES Act and Guidance: Step Three

- Account for employee reduction. Take the average number of “Full-Time Equivalent Employees” (“FTEE”) per month during covered period and divide by: either a) the average number of full-time employees per month from February 15, 2019 through June 30, 2019 or b) the average number of full-time employees per month from January 1, 2020 through February 29, 2020. Now multiply this percentage with your Maximum Allowable Amount calculated in Step #2.

Forgiveness Formula

A Note on “Full-Time Equivalent Employees” (“FTEE”)

- Although the Guidance uses this term, it has not been defined.
- It is possible that they use the definition used for interpreting the Affordable Care Act, which uses the following formula:
 - Each employee who works 30+ hours a week counts as one FTEE.
 - For all employees who work less than 30 hours a week, total all the hours worked per month by part-time employees and divide the total hours worked by 120 hours to find how many full-time employees your part-time employees make up.
 - Total the two.

Forgiveness Formula

A Note on “Full-Time Equivalent Employees” (“FTEE”)

- It is possible that the Guidance uses a different formula.
- Further, Guidance could put further restrictions on this calculation; for example to avoid rewarding businesses that terminate high wage earners and then replace them with minimum wage employees.

Forgiveness Formula

Proposed Formula based on CARES Act and Guidance: Step Three

- Note on Step Three: Pending further clarification in the expected guidance, you may be able to include FTEEs hired back before June 30th (but possibly after Covered Period) in your calculation of FTEEs.
- Additionally, the existing Guidance also implies that you may also include some FTEEs that have turned down offers to return to work.
- Both of these inclusions can lead to a larger forgivable amounts.

Forgiveness Formula

Proposed Formula based on CARES Act and Guidance: Step Four

- >25% Reduction. For full-time employees (paid less than annual compensation of \$100,000), identify their average prior compensation earned in the prior full quarter and subtract 25% (the “reference amount”). Compare each employee’s compensation earned during the eight-week covered period to the reference amount. For every dollar that the reference amount exceeds the average compensation received for the eight-week period, you must reduce the amount calculated in Step #3 by a dollar to obtain the final Loan Forgiveness Amount.

Forgiveness Formula

Proposed Formula based on CARES Act and Guidance: Step Four

- Note on Step Four: Pending further clarification in the expected guidance, you may be able to disregard reductions in pay for employees whose pay is restored before June 30th (but possibly after Covered Period).
- This exclusion can lead to a larger forgivable amount.

Forgiveness Formula Recap

Recap: Loan Forgiveness Formula

- The maximum amount of eligible loan forgiveness (at least 75% of which is Payroll Costs); multiplied by
- [Average Number of FTEE per month calculated during the Covered Period divided by the Average Number of FTEE per month calculated during the Choice Period]; minus
- Any reduction in average salary or wages of any employee during the covered period that is in excess of 25 percent of the average salary or wages of the employee during the most recent full quarter during which the employee was employed before the covered period; equals
- **Total Forgivable Amount**

Examples

Example #1: Full Forgiveness

- Amount of Loan: \$200,000
- Payroll Costs (8 week): \$160,000
- Mortgage Int., Rent, Utilities: \$40,000
(may not exceed 25% of Forgiveness Amount)
- Estimated Max Forgiveness Amount \$200,000
- FTEEs during Covered Period: 10
- FTEEs during Comparison Period: 10
- Employee Pay Reduction Amount: 0
- Wage Decrease Amount (> 25 percent): \$0

- **Forgiveness Amount: \$200,000**

Examples

Example #2: Payroll Costs Expended Are Less Than 75 percent of Loan

- Amount of Loan: \$200,000
- Payroll Costs (8 week): \$140,000
(less than 75% of Amount of Loan)
- Mortgage Int., Rent, Utilities: \$60,000
(exceeds 25% of Forgiveness Amount by \$13,333)
- Estimated Max Forgiveness Amount \$186,666.66
- FTEEs during Covered Period: 10
- FTEEs during Comparison Period: 10
- Employee Pay Reduction Amount: 0
- Wage Decrease Amount (> 25 percent): \$0
- **Forgiveness Amount: \$186,666.66**

Examples

Example #3: Employee Reduction

Amount of Loan:	\$200,000
Payroll Costs (8 week):	\$160,000
Mortgage Int., Rent, Utilities: <i>(may not exceed 25% of Forgiveness Amount)</i>	\$40,000
Estimated Max Forgiveness Amount	\$200,000
FTEEs during Covered Period:	8
FTEEs during Comparison Period:	10
Employee Pay Reduction Amount:	20%
Wage Decrease Amount (>25%):	\$0

Forgiveness Amount: **\$160,000**
(80% of \$200,000)

Examples

Example #4: Wage Decrease

Amount of Loan:	\$200,000
Payroll Costs (8 week):	\$160,000
Mortgage Int., Rent, Utilities: <i>(may not exceed 25% of Forgiveness Amount)</i>	\$40,000
Estimated Max Forgiveness Amount	\$200,000
FTEEs during Covered Period:	10
FTEEs during Comparison Period:	10
Employee Pay Reduction Amount:	0
Wage Decrease Amount (>25%):	\$10,000

Forgiveness Amount: \$190,000

Examples

Example #5: Employee Reduction and Wage Decrease

Amount of Loan:	\$200,000
Payroll Costs (8 week):	\$160,000
Mortgage Int., Rent, Utilities: <i>(may not exceed 25% of Forgiveness Amount)</i>	\$40,000
Estimated Max Forgiveness Amount	\$200,000
FTEEs during Covered Period:	8
FTEEs during Comparison Period:	10
Employee Pay Reduction Amount:	20%
Wage Decrease Amount (>25%):	\$10,000
Forgiveness Amount:	\$150,000

Part IV – A Bank's Perspective

A Bank's Perspective

Things to Consider

- Documentation for Forgiveness
- Payroll Records
- Receipts
- Banks' Perspective on Guidance
- Bank Determines Forgiveness

Part IV – Q&A



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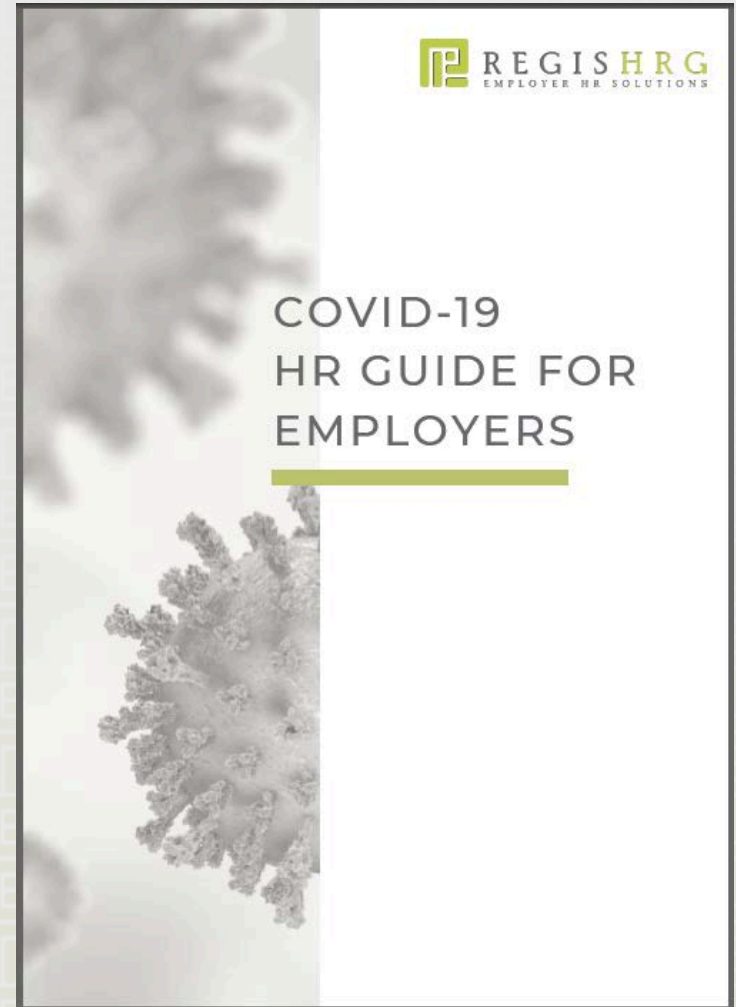
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**Thank you
&
Stay Safe!**



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