

# Planning and Managing Loan Forgiveness for Family Businesses

April 21, 2020



PEOPLE | IDEAS | SOLUTIONS

Mario O. Vicari  
[mvicari@kmco.com](mailto:mvicari@kmco.com)  
[www.kmco.com](http://www.kmco.com)

# DISCLAIMER

THIS DOCUMENT IS A HIGH-LEVEL SUMMARY AND DISCUSSION OF SECTION 1106 (LOAN FORGIVENESS) OF H.R. 748, THE ‘CORONAVIRUS AID, RELIEF, AND ECONOMIC SECURITY ACT’ (“CARES ACT”), WHICH BECAME LAW ON MARCH 27, 2020. IT IS A SUMMARY OF THE TEXT OF THE LAW.

THE U.S. SMALL BUSINESS ADMINISTRATION ISSUED REGULATIONS ON APRIL 2, 2020 (INTERIM FINAL RULE) RELATED TO THE PAYCHECK PROTECTION PROGRAM. IN ITS REGULATIONS, THE SBA STATES “SBA WILL ISSUE ADDITIONAL GUIDANCE ON LOAN FORGIVENESS”. **NOTE: THESE REGULATIONS HAVE NOT BEEN ISSUED AS OF THE TIME OF THIS PRESENTATION.**

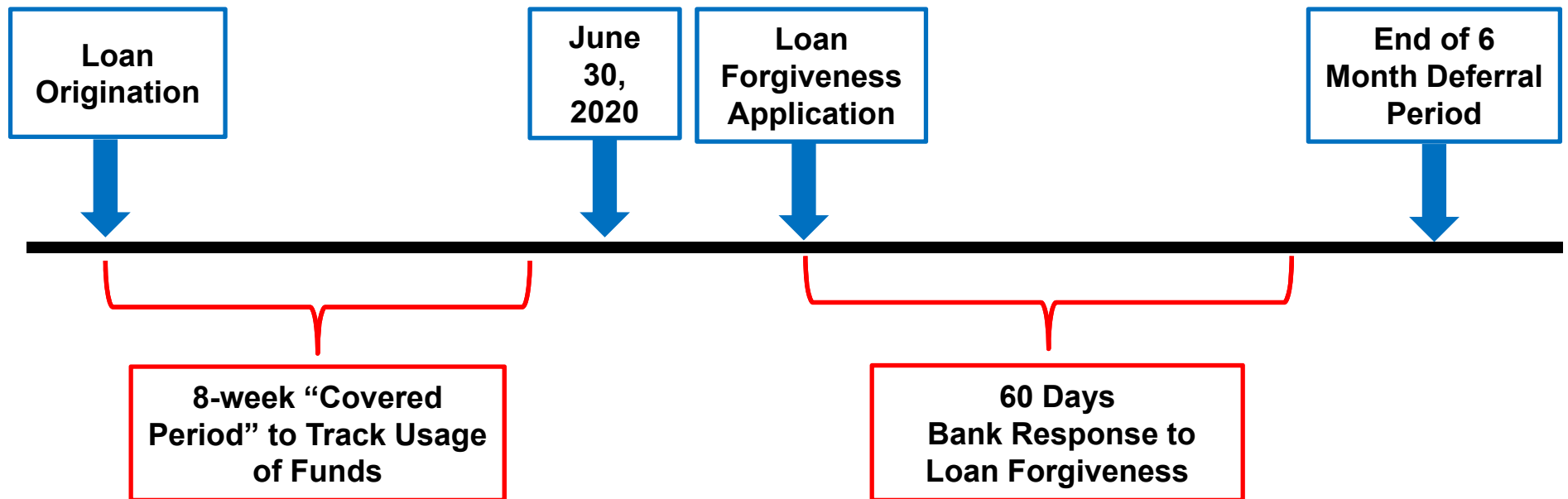
ADDITIONALLY, LOAN FORGIVENESS APPLICATIONS WILL BE MADE TO YOUR LENDER AND THEY HAVE AUTHORITY TO ADMINISTER THE PPP INCLUDING APPROVING LOAN FORGIVENESS. **IT WILL BE IMPORTANT TO COORDINATE LOAN FORGIVENESS CALCULATIONS WITH YOUR LENDER.**

THIS DOCUMENT SHOULD NOT BE USED AS A BASIS TO MAKE DECISIONS OR TAKE ACTIONS RELATED TO H.R. 748 AND THE LOAN FORGIVENESS PROVISIONS CONTAINED IN IT.

# Discussion Agenda

- PPP Loan Forgiveness Timeline
- PPP Loan Forgiveness Definitions, Guidelines and Tests
- Case Study Examples
- Application for Loan Forgiveness / Tracking & Documenting Costs
- Estimating and Integrating Loan Forgiveness Into Business Planning
- What to Do if You Don't Qualify for Loan Forgiveness
- Taxation

# PPP Loan Forgiveness Timeline



# Important Definitions

# General Definitions

1. **COVERED PERIOD** - The 8 week period beginning on the date of the origination of the covered loan.
2. **COVERED RENT OBLIGATION** – Rent obligated under a leasing agreement in force before February 15, 2020.
3. **COVERED UTILITY PAYMENT** – Payment for a service for the distribution of electricity, gas, water, transportation, telephone or internet access for which the service began before February 15, 2020.

# Payroll Costs - Definition

**“Payroll Costs”** are defined as “the sum of payments for any compensation with respect to employees that is a -

- salary, wage, commission or similar compensation
- cash tip or equivalent
- vacation, parental, family, medical or sick leave
- allowance for dismissal or separation
- group health care benefits, including insurance premiums
- retirement benefits
- payment of state or local tax assessed on the compensation

# Payroll Costs – Excluded Amounts

## Excluded Amounts in Determining Payroll Costs:

- ✓ the compensation of an individual employee in excess of an annual salary of \$100,000.
- ✓ taxes imposed or withheld under chapters 21, 22 or 24 of the IRS Code.

(Note: FICA, FWT and Railroad Retirement Benefits are not deductions from “Payroll Costs”, they are just excluded since gross salaries and wages are already included)

- ✓ compensation of an employee with a principal residence outside of the U.S.
- ✓ qualified sick leave wages for which a credit is allowed under section 7001 of the Families First Coronavirus Response Act.
- ✓ qualified family leave wages for which a credit is allowed under section 7003 of the Families First Coronavirus Response Act.



# Step 1 – Determining Amount Eligible for Forgiveness

# Determining the Amount Eligible For Forgiveness

1. Loan principal and accrued interest are eligible for forgiveness
2. An eligible recipient shall be eligible for forgiveness of indebtedness on a covered loan in an amount equal to the following costs incurred and payments made during the covered period:
  - At least 75% of costs must be used for:
    - payroll costs (as defined)
  - Not more than 25% of the costs can be used for:
    - any payment of covered rent obligation
    - any covered utility payment
    - any payment of interest on any covered mortgage obligation
    - **NOTE: interest payments on any other debt obligation that were incurred before February 15, 2020 are NOT included in the debt forgiveness section 1106 but are identified as allowable costs in section 1102 under “allowable uses” of PPP loan proceeds**
3. Note: Refinancing an EIDL loan made between January 31, 2020 and April 3, 2020 is considered an allowable cost if your EIDL loan was used for payroll costs. The \$10,000 EIDL grant reduces loan forgiveness.


## Step 2 – Determining Limitations on Forgiveness


# Reduction Based on Reduction in Number of Employees

1. The average number of full time equivalent employees shall be determined by calculating the **average number of full-time equivalent employees for each pay period falling within a month.**
2. The amount of loan forgiveness shall be reduced, but not increased, by multiplying the amount of forgiveness by the ratio of the average number of full time equivalent employees per month employed during the covered period, divided by, at the election of the borrower, either:
  - The average number of full time equivalent employees per month employed by the eligible recipient during the period beginning on February 15, 2019 and ending on June 30, 2019, or
  - the average number of full time equivalent employees per month employed by the eligible recipient during the period beginning on January 1, 2020 and ending on February 29, 2020
  - for seasonal employers, the average number of full time equivalent employees per month employed by the eligible recipient during the period beginning on February 15, 2019 through June 30 2019.



# Reduction Relating to Salaries and Wages

- 
1. The amount of loan forgiveness shall be reduced by the amount of **any reduction in total salary or wages of any employee** during the covered period (8 week period after the loan is made) that is **in excess of 25%** of the total salary or wages of the **employee** **during the most recent full quarter** during which the employee was employed before the covered period.

- 
2. An employee, for purposes of this section, is any employee who did not receive, during any **single pay period during 2019, wages or salary at an annualized rate of pay in an amount more than \$100,000.**

# Exemption for Re-Hires

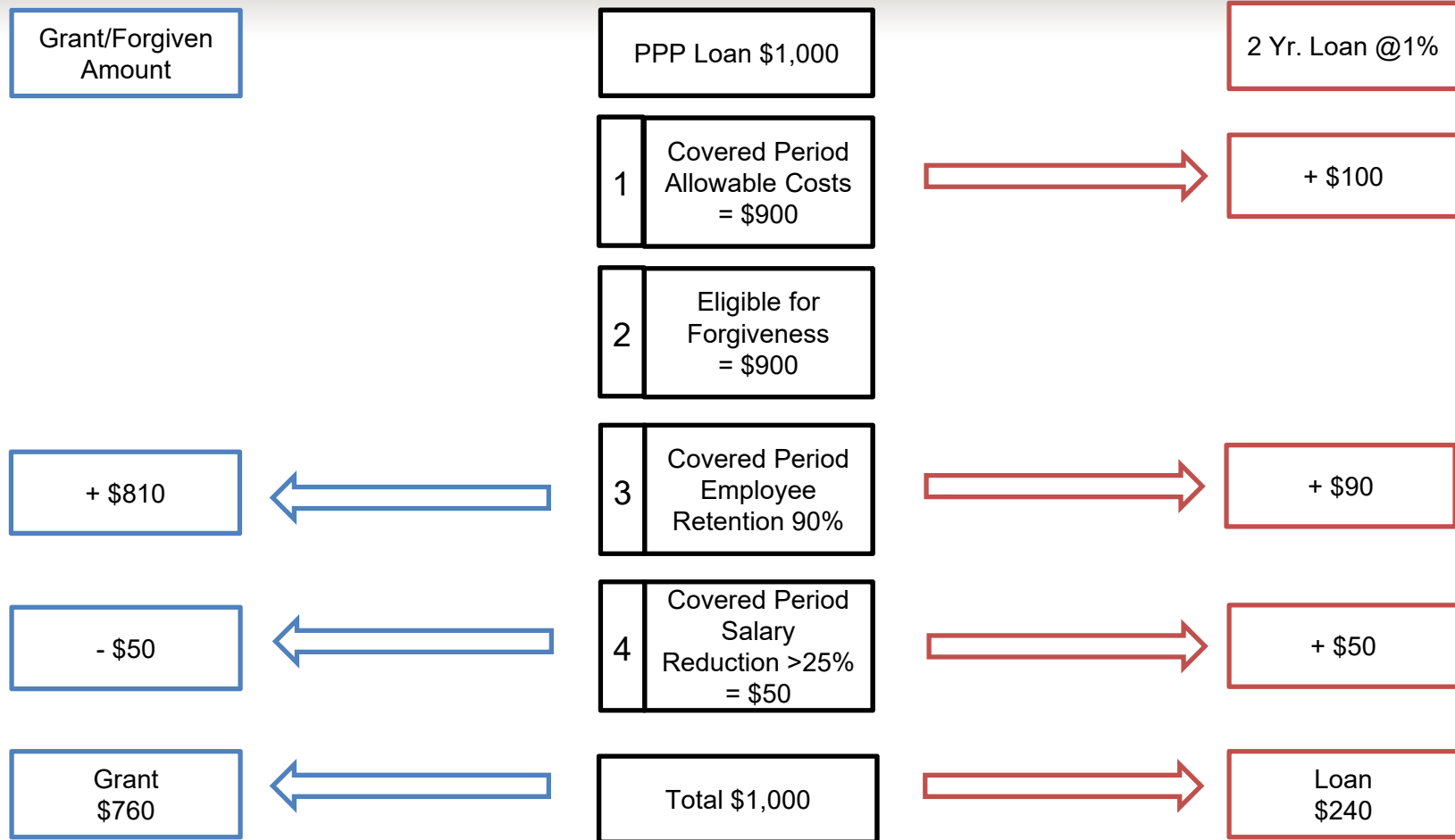
The amount of loan forgiveness under this section shall be determined without regard to a REDUCTION IN THE NUMBER OF FULL TIME EQUIVALENT EMPLOYEES or a REDUCTION IN THE SALARY OF 1 OR MORE EMPLOYEES during the period beginning on February 15, 2020 and ending on the date that is 30 days after the date of enactment of the Act (April 26, 2020),

IF:

- there is a reduction in the number of full-time equivalent employees during the period of February 15, 2020 and ending 30 days after the bill becomes law (April 26, 2020) as compared to February 15, 2020, AND, if by not later than June 30 2020, the eligible employer has eliminated the reduction in the amount of full time equivalent employees.
  
- there is a reduction in the salary or wages of 1 or more employees during the period of February 15, 2020 and ending 30 days after the bill becomes law (April 26, 2020) as compared to February 15, 2020, and, if by not later than June 30 2020, the eligible employer has eliminated the reduction in the salary or wages.

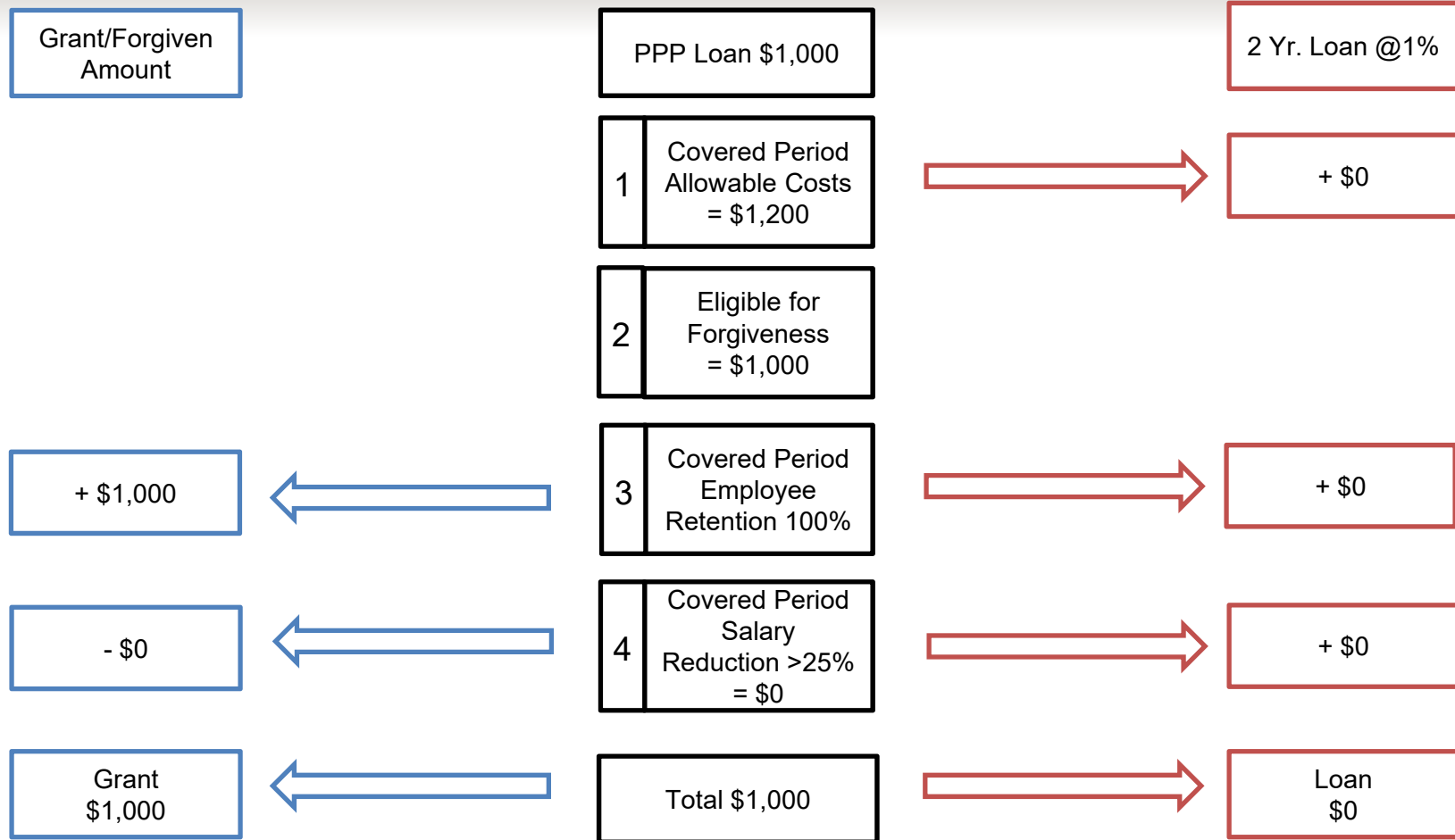
# Case Study Examples

# Case Study 1 - \$1M PPP Loan

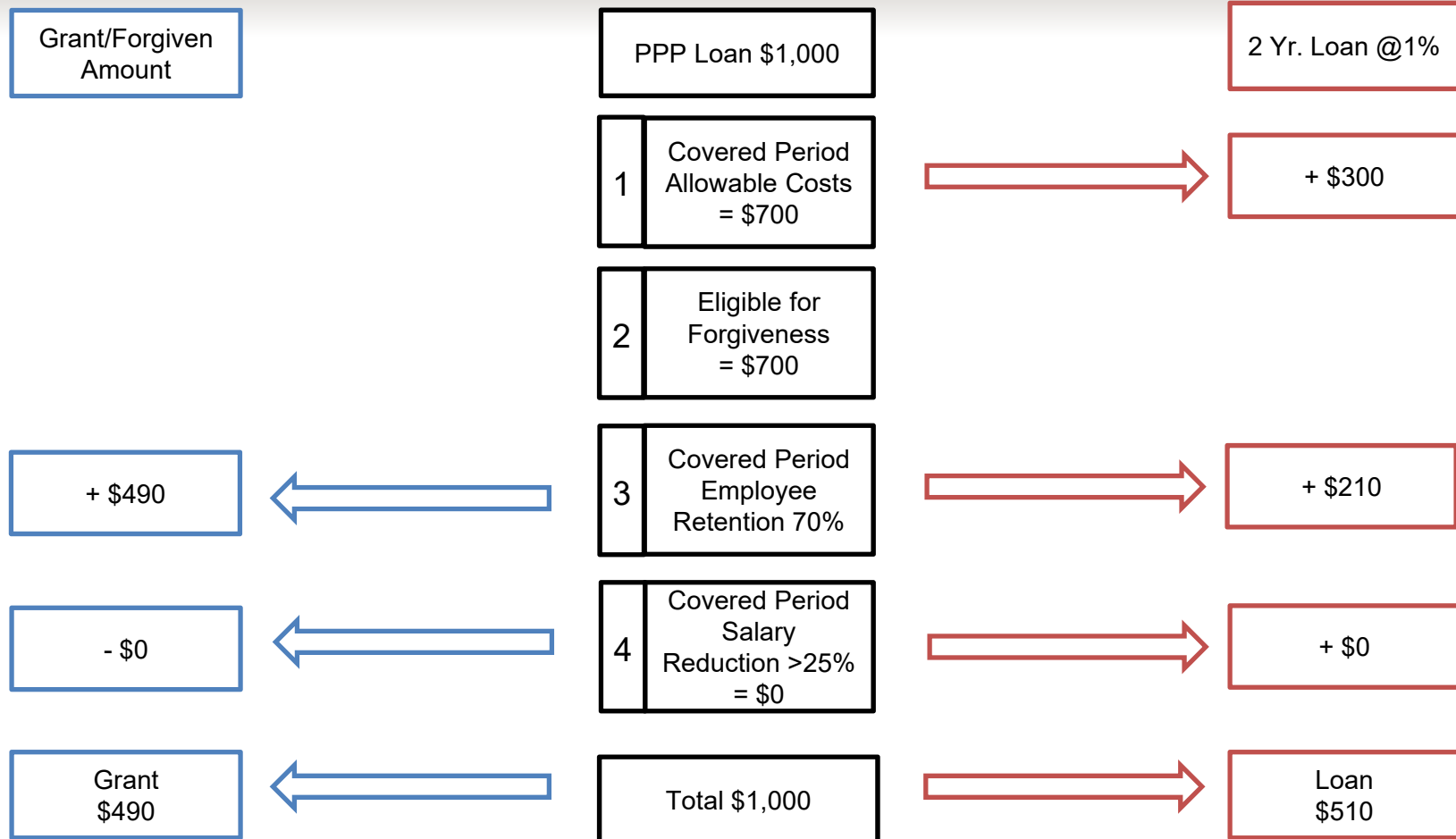




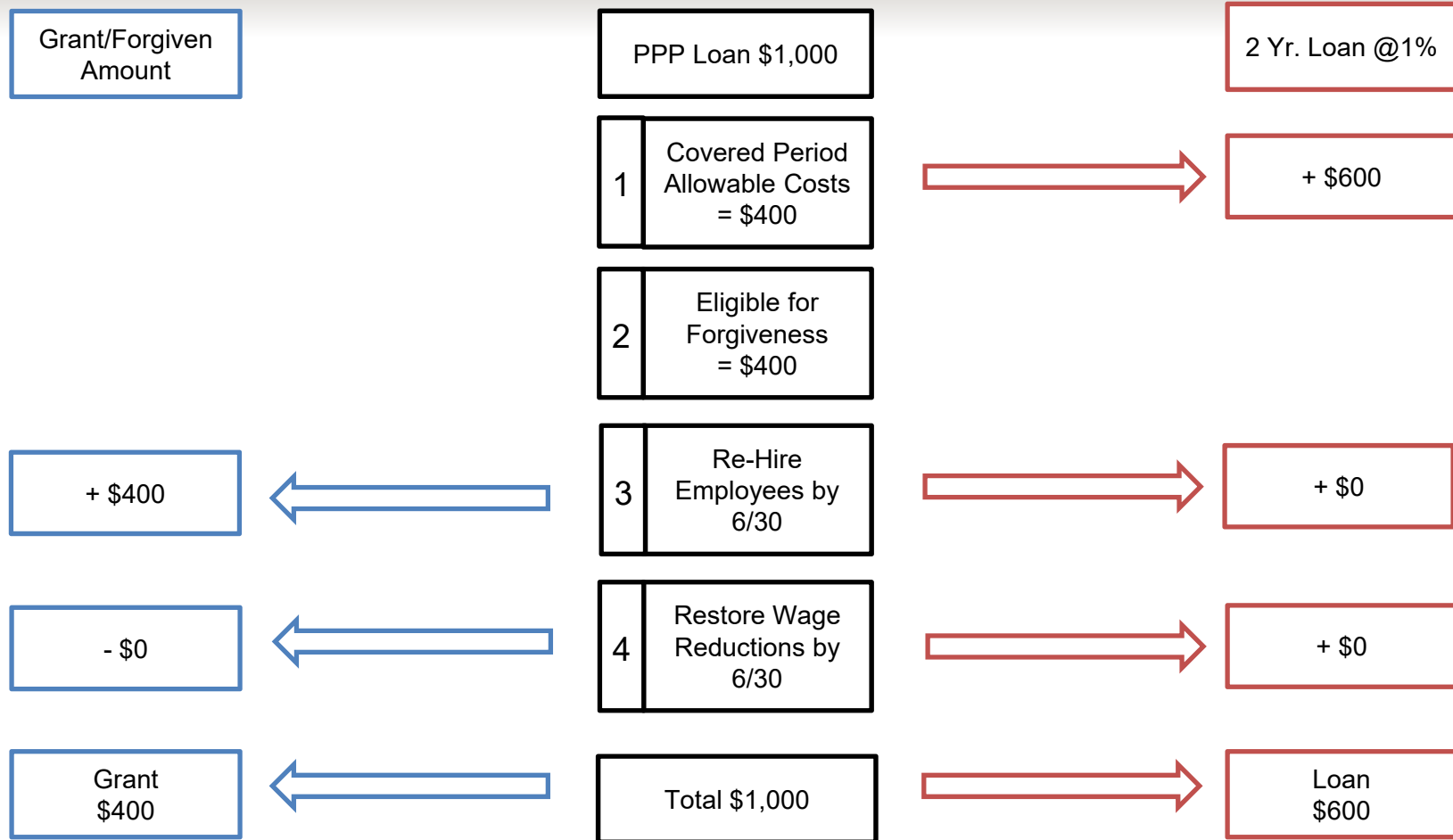
# Case Study 2 - \$1M PPP Loan



# Case Study 3 - \$1M PPP Loan



# Case Study 4 - \$1M PPP Loan(RE-HIRE)



# Application For Loan Forgiveness / Tracking & Documenting Costs

# Application for Loan Forgiveness

1. **No eligible recipient shall receive forgiveness without submitting to the lender that is servicing the covered loan the documentation required.**
  - Lender has 60 days to respond
2. An eligible recipient seeking loan forgiveness **shall submit to the lender servicing the covered loan an application**, which shall include
  - **documentation verifying the number of full-time equivalent employees on payroll and pay rates for the relevant periods including:**
    - payroll tax filings reported to the IRS, and
    - state income, payroll and unemployment insurance filings;
    - documentation including cancelled checks, payment receipts, transcripts of accounts, or other documents verifying payments on covered mortgage obligations, payments on covered lease obligations and covered utility payments;
  - **a certification from a representative of the eligible recipient authorized to make such certifications that:**
    - the documentation is true and correct
    - the amount for which forgiveness is requested was used to retain employees, make interest payments on a covered mortgage obligation, make payments on a covered rent obligation or make covered utility payments; and
    - any other documentation deemed necessary by the SBA

# Documentation and Cost Tracking

1. **Best to track usage of funds for allowable costs and collect documentation for your forgiveness calculation as you spend the money over the 8 week period** so you can complete your loan forgiveness application soon after the covered period.
2. Some suggestions:
  - Use of a separate bank account to track funds
  - Set up separate GL accounts to classify costs separately
  - Establish HR systems/protocols to produce reports on FTEs for each payroll
  - Produce documentation as costs are spent to be used later as part of your debt forgiveness application
  - Produce separate payroll reports for documentation purposes

# Estimating and Integrating Loan Forgiveness Into Business Planning

# Integration in Business Planning

Planning for the survival of the business from a cash flow standpoint has to come first, however, we suggest **integrating your PPP loan forgiveness calculations with your planning**:

## 1. **Estimate Allowable Costs**

- Project your allowable payroll costs and non-payroll costs during the covered period to estimate your “Amount Eligible for Forgiveness”

## 2. **FTEs**

- Determine the most favorable period of comparison for the forgiveness test related to maintaining FTE levels
- Project your FTE levels during the covered period

## 3. **Wage and Salary Levels**

- Determine wage and salary levels for all employees during the most recent full quarter
- Project wage and salary levels for employees during the covered period



# Planning Considerations/Issues

NOTE: Language in the Act: “costs incurred and payments made during the covered period”

IMPORTANT – REGULATIONS HAVE NOT YET BEEN ISSUED BY THE SBA, HOWEVER, BE PREPARED IN YOUR PLANNING WHILE WE AWAIT SPECIFIC GUIDANCE.

## Planning Considerations:

- FTE Calculations – timing/handling part-time/job sharing/short shift workers
- Payroll Tax Deferral Program – timing of forgiveness
- Timing of reductions/layoffs/furloughs
- Degree/timing of pay decreases
- Degree/timing of benefit reductions
- Delay of production into covered period
- Rent Payments – Leases/related party issues
- Q1 incentives, commissions – timing of payments
- 2019 profit sharing payments to retirement plans – timing of payments

# If You Don't Qualify for Forgiveness

1. Set aside and track funds carefully in the covered period and repay that portion of the loan
  - No prepayment penalty
2. Use proceeds of the “non-forgivable” portion of the loan to fund the business
  - Loan Terms - 2 year maturity at 1% interest rate
    - Nonrecourse
    - No fees
    - No personal guarantees
    - No collateral required
    - Principal and interest are deferred for 6 months (but interest accrues)

# Taxation of Debt Forgiveness

1. Debt forgiveness on a PPP loan “shall be excluded from gross income” for federal tax purposes.
  - Potential conflict with other sections of the IRS code related to deductibility of expenses related to tax-exempt income.
  - Taxability at the state level is unclear.
  - Look for guidance from the KM Tax Group.

# Thanks for your Time and Attention!

Webinar Rebroadcast

Go to our website at:

[www.kmco.com](http://www.kmco.com)