tri counties bank

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Tri Counties Bank FAQ – PPP Loan Disbursement & Forgiveness (Updated 05/18/20)

Disclaimer: Lenders are still awaiting additional guidance on Paycheck Protection Program (PPP) loan forgiveness from the US Treasury and SBA. The following FAQ is provided for your general informational purposes only, and not as legal, tax, or accounting advice, in the hope it will assist borrowers in understanding how PPP loan forgiveness will likely work based on guidance released to date. This FAQ and the ultimate forgiveness process may change as additional guidance is provided by the US Treasury and the SBA. Borrowers are urged to consult their own advisors to determine how the PPP loan forgiveness analysis will impact their individual situations.

You have already received loan proceeds or will be receiving them shortly. The disbursement date for your PPP loan is significant, as the amount of forgiveness for a PPP loan is based on the borrower's payroll cost over an eight-week period that begins on the date the lender makes the first disbursement to the borrower.

Determining how to properly spend the loan proceeds in order to maximize benefits under the program is a challenge. Please make sure you consult your counsel and other consultants to make sure you are maximizing your chances to receive full forgiveness on your PPP Loan. This is a crucial issue, as your business must adhere to rules governing the use of PPP loan proceeds, particularly in order to qualify for maximum loan forgiveness.

The PPP loan and forgiveness rules can be best understood by considering the objective of the program: to create a source of funds to allow businesses to keep their workforce employed and paid at a substantially similar level as before the COVID-19 crisis began. To incentivize employers to keep their historic level of employees and their salaries, the CARES Act allows loan forgiveness of up to 100% of the loan proceeds that are used for those purposes within a prescribed timeframe.

Based on the CARES Act, the interim final rules, and guidance from the SBA and U.S. Treasury to date (which, as noted above, remain subject to the issuance of additional guidance), below is an FAQ for you to consider as you seek to deploy your PPP funds most effectively.

Q #1: Do we have to accept the full loan amount?

A: The loan will fully disburse at closing, but you can repay any portion of the loan that you don't need/use any time after funding without penalty. Please refer to the "Loan Prepayment" section of your Promissory Note for information on when you need to notify the Bank of your intent to prepay the loan.

Q #2: I heard that we have to use all loan proceeds within 8 weeks of loan funding. Is that correct?

A: No. The loan fully disburses at closing and proceeds are available to cover eligible expenses (qualifying payroll, interest, utilities and rent) as needed up to the earlier of loan proceeds being exhausted or loan maturity. However, loan forgiveness will only be available for eligible costs paid during the 8-week period beginning on the date the loan disburses (the "8-Week Covered Period") and not more than 25% of the amount forgiven can be for non-payroll costs.

Q #3: What does it mean when you say that "not more than 25% of the amount forgiven can be for non-payroll costs?"

A: Consider the following example:

- Borrower obtains a $100,000 PPP loan and uses $90,000 of loan proceeds on eligible expenses over the 8-Week Covered Period ("8-Week Proceeds"). Borrower uses the remaining $10,000 of loan proceeds on eligible expenses after the 8-Week Covered Period.
- Since only $90,000 of the loan was spent during the 8-Week Covered Period, only the $90,000 can be considered for forgiveness.
- The $90,000 of 8-Week Proceeds were spent as follows:
  - Payroll: $60,000
  - Non-payroll (Rent, Interest & Utilities): $30,000
- In this example, payroll amounts to 66.7% of total eligible uses and non-payroll accounts for 33.3% of total eligible uses. Since "not more than 25% of the amount forgiven can be for non-payroll costs," forgiveness for this Borrower would be calculated as follows:
  - Payroll Forgiveness (75% of total forgiveness): $60,000
  - Non-payroll Forgiveness (25% of total forgiveness): $20,000
  - Gross Eligible Forgiveness:* $80,000
    - *This amount may be further reduced if the Borrower's employee headcount and/or wage rates aren't maintained during the 8-Week Covered Period. See Question #4 below for additional details.
- In this example, the Borrower's residual (unforgiven) loan balance would be $20,000 as follows:
  - Non-payroll exceeding 25% of 8-Week Proceeds: $10,000
  - Proceeds used to cover eligible expenses after 8-week period: $10,000
  - Total Residual (unforgiven) Loan Balance: $20,000**
    - **This amount must be repaid in accordance with the repayment schedule in the promissory note.

Q #4: I understand that loan forgiveness will depend, in part, on my ability to retain employees during the 8-Week Covered Period and to pay them wages that are comparable to historical rates. Can you explain how those benchmarks are calculated?

A: Loan forgiveness is determined by three factors, including:

1. Eligible Use of Proceeds – Amount of loan proceeds used to cover eligible expenses during the 8-Week Covered Period following loan disbursement and not more than 25% of loan forgiveness will be for non-payroll expenses (see Question #3 above). This is the first step in the calculation and is used to determine Gross Eligible Forgiveness.
2. Employee Retention – Degree to which the Borrower maintained full-time equivalent employee levels (FTE's) during the 8-Week Covered Period when compared to a historical baseline period. The amount of loan forgiveness is reduced by the same percentage that employee headcount is reduced. This is the second step in the calculation. Using the same example from Question #3 above, here's how the employee retention calculation works:
   - Average FTE Headcount During 8-Week Period: 11
   - Average FTE Headcount from Baseline Period. For seasonal employers, the baseline period should be 02/15/19 to 06/30/19. For non-seasonal employers like the company in this example, the baseline can be the lesser of the following two periods at the borrower's choice:
     - Average FTE Headcount from 02/15/19 to 06/30/19: 14
     - Average FTE Headcount from 01/01/20 to 02/29/20: 12
       - Final Baseline FTE Headcount (lesser of 14 and 12): 12

- Employee Reduction %: (12-11)/12, or 1/12, or: 8.33%
- X Gross Forgiveness Amount (from Question 3 above): $80,000
- = Amount Ineligible based on Employee Reduction: ($6,667)
- = Resulting Forgiveness Amount $73,333

In this example, the average FTE Headcount for this non-seasonal employer during the 8-Week Covered Period was 8.33% less than the average FTE Headcount during the Baseline Period. Per the PPP Act, gross loan forgiveness is reduced by this same percentage of 8.33%.

NOTE: In the context of PPP, FTE means "full-time equivalent" employees. See Question #6 for information on calculating FTE's.

3. Salary/Wage Reduction – Degree to which the Borrower maintained wage levels during the 8-week period following loan disbursement when compared to a historical baseline period. This calculation is more involved and works as follows:

   - Identify all employees who did not receive during any single pay period in 2019, wages or salary at an annualized rate of pay of more than $100,000 (each referred to herein as a "covered employee" for the purpose of this calculation).
   - Compare each covered employee's wages or salary during the 8-week period to his/her wages or salary during the first quarter of 2020.
   - For any covered employee whose wages or salary during the covered period decreased by more than 25%, the amount of decrease over 25% is deducted from the loan forgiveness amount. Here's how to calculate this:

   Assumption as to Wages:

   - Using the same example as above, assume that all 11 of the company's 11 existing employees are covered employees (i.e. employees who did not receive during a single pay period in 2019 wages or salary at an annualized rate of pay of more than $100,000).
   - Additionally, assume covered employees were collectively paid an 8-week equivalent rate of $74,000 during Q1, 2020 (Q1, 2020 wages / 13 weeks x 8 weeks) and are paid a rate of $54,000 for the 8-Week Covered Period due to pay reductions implemented by management.
   - Calculated as follows:
     - Q1, 2012 Wages / 13 weeks x 8 weeks): $74,000
     - x 0.75 = Wage Reduction Allowance: $55,500
     - (-) 8-Week Covered Period Wages: ($54,000)
     - = Amount Ineligible based on Pay Reduction: $1,500
     - Final Forgiveness Amount ($73,333* - $1,500): $71,833
       - *Maximum forgiveness amount from A.2 above

Q#5: We reduced staff and/or wages during the 8-week period, which may affect the amount of loan forgiveness we qualify for. Can we re-hire employees and/or restore previous wage rates in order to qualify for more forgiveness after the loan is obtained?

A: Yes. In the event you had a reduction of employees during the period from February 15, 2020, through April 26, 2020, as long as you rehire those employees no later than June 30, 2020, the FTE calculation for the number in the fraction will treat those rehired employees as if they were included in the FTE for the entire 8-week period. Please note that while a delayed rehire date won't cause issues with the employee retention fraction, it may cause you to spend less than the required 75% threshold on payroll costs during the 8-week covered period, and therefore could result in a reduction in the amount of loan forgiveness.

Both the average reduction in FTE and reduction in pay must be restored to eliminate the reduction in loan forgiveness.

Q #6: The above examples require me to determine average full-time equivalent employees (aka FTE) for certain periods. How should I calculate average FTE for loan forgiveness purposes?

A: Guidance is still forthcoming on this. For now, it would be reasonable to calculate FTE's in accordance with the Internal Revenue Code's method as follows:

- Employees working 30 hours per week or more are considered full-time employees.
- Employees working less than 30 hours per week are considered part-time employees. Here, add the hours of part-time employees on a monthly basis and divide by 120 to determine average FTE equivalents.
- Combined full-time employees and FTE equivalents to determine total FTE's.

Q #7: If I have an employee making over $100,000 per year, do I have to limit my paycheck to them to $8,333.33/month ($100,000 annualized) or can I pay them their regular paycheck amount?

A: You can pay them their regular paycheck amount. The $100,000 threshold is the maximum amount per employee that will be forgiven, not the maximum amount of payroll that you can pay your employees. For example, if you pay an employee $10,000 per month ($120,000 annualized), PPP loan forgiveness will only be available for an amount equal to $8,333.33 per month during the 8-week covered period.

Q #8: Our PPP loan disbursement date is 04/24/20 and runs 8 weeks to 06/23/20. I understand that payroll within that period is eligible for forgiveness. Are we looking at any/all pay dates that fall within that range (aka "cash-basis wages") or only the actual daily payroll incurred within that range (aka "accrual-basis wages")?

A: Guidance doesn't elaborate on this question. However, the intent of the program is to cover eligible expenses (including payroll) within the 8 week period following loan disbursement. Since forgiveness covers actual expenses paid during the 8-week period, Borrowers should use the loan to cover payroll costs as they are normally incurred/processed over the 8-week period. Start these payments from the very date you receive the money, or as close to that as possible, and make sure your pay periods fall within the 8 week window. Using your particular situation as an example, if your loan funded on 04/24/20 and you normally process payroll on 04/28/20, you could use proceeds to cover the 04/28/20 payroll expense even though it largely related to payroll costs accrued prior to the loan disbursing on 04/24/20. This is a cash payroll expense that was paid during the 8-week period following loan disbursement and therefore meets the intent of the PPP loan.

Q #9 Many of our furloughed employees have already filed and are receiving unemployment benefits and have indicated that they may stay there making $26.25/hr until the Fed supplement runs out 7/31. Since I cannot force them to return, if we hire somebody other than our original furloughed employee to fill needed positions does this new employee get counted as it relates to payroll and FTE requirements for forgiveness or are only our past employees eligible?

A: We are awaiting guidance from the Treasury and SBA on this.

Q #10 Do you have any suggestions on what I should do to ensure compliance and maximize loan forgiveness?

A: Guidance is constantly evolving and we encourage you to consider the following to increase your ability to maximize forgiveness:

- **Check for Changes.** Periodically check SBA and US Treasury websites for additional guidance:
  - SBA: https://www.sba.gov/funding-programs/loans/coronavirus-relief-options/paycheck-protection-program
  - US Treasury: https://home.treasury.gov/policy-issues/cares/assistance-for-small-businesses
- **Open a Separate Bank Account or Segregate the PPP Funds.** Borrowers may only spend the PPP loan proceeds on specified business expenses, and they will be required to substantiate the proper use of their PPP loan proceeds to their lenders in order to qualify for loan forgiveness. Segregating your PPP funds will make it easier for you to trace the proceeds and avoid comingling. We will be required to substantiate your request for forgiveness.

- **Maintain Records to Substantiate Expenses.** For example, if you have an employee with a salary over $100,000 – do you pay only up the cap from the fund or do you pay all and then reimburse the fund for the excess? There is no guidance on this – but it will be important that your records support your decision.
- **Use the Loan Proceeds Only for Permissible Purposes.** If you use PPP loan proceeds for any purpose other than those permitted under the PPP, the SBA will direct you to repay those misused amounts. If you knowingly use the PPP loan proceeds for an unauthorized purpose, you may be subject to additional criminal liability, such as charges for fraud. If one of your shareholders, members, or partners uses PPP loan proceeds for unauthorized purposes, the SBA will have recourse against such shareholder, member, or partner for the unauthorized use.
- **Re-review the Certifications You Made Regarding Qualifying for a PPP Loan.** The SBA has indicated that there may be misunderstandings by borrowers of a certification they made in their PPP loan application, notably the economic need for the loan. Loans under the PPP are intended to keep struggling businesses afloat during the COVID-19 crisis. The PPP application thus requires a certification that the "[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant." On April 23, SBA updated its FAQ - urging borrowers to "review carefully the required certification" regarding necessity of the loan to support ongoing operations. See Question 31 in the SBA FAQ: https://www.sba.gov/document/support--faq-lenders-borrowers. Companies with alternative access to capital need to justify their determination that the loan was in fact necessary. The SBA, in an interim final rule, gave borrowers that applied for a loan prior to the issuance of the rule a "limited safe harbor" window of opportunity to return funds that in retrospect they should not have received. Most recently, on May 13, 2020, the SBA further clarified by providing a safe harbor for loans under $2 million and extended the deadline to return the funds under the limited safe harbor to May 18, 2020. See FAQs 46 and 47 in the SBA Frequently Asked Questions in the SBA FAQ link above. You should consider documenting your thought process behind your determination of economic uncertainty. Since this is a legal question, we urge you to consult counsel if you have any questions on this rule and its potential impact.

Q #11 What if my loan is not able to be completely forgiven?

A: In the case that you don't meet all requirements for complete loan forgiveness, you'll have specific terms to pay back the required portion of the loan, and these terms are the same for every business:

- 1% interest rate
- Maturity of 2 years (meaning the full amount of non-forgiven principal and any interest is due in 2 years)
- 6-month deferment (you don't have to start paying back the loan for 6 months—however, interest still accrues during this period)
- No collateral is required
- No borrower or lender fees need to be paid to the SBA
- No personal guarantees