INTRODUCTION

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AGENDA

1. Lessons learned.
2. What is new.
3. Your loan has funded, now what.
4. Preparing for the forgiveness stage.
PAYCHECK PROTECTION PROGRAM

• The Paycheck Protection Program ("PPP") introduced as part of the CARES Act.

• $349 billion program, and is temporary. Initial appropriation exhausted as of April 16th, 2020.

• Administered through the existing Small Business Administration’s ("SBA") so called "7(a)" loan program.

• Fast moving program with daily updates and changes.

• Regulations released on April 2nd and April 14th, 2020. Updated FAQs released every few days.

• Two stages: the loan stage, and the forgiveness stage.
• In FAQs, the government has clarified that the following businesses are eligible for PPP loans.

1. Employers with 500 or fewer employees or the applicable industry size standard, taking into account the rules of affiliation and the special rules for franchises and hospitality industry.

2. Employers meeting the “small business concern” definition, even if exceed 500 employees. Small business concern definition generally based upon number of employees or revenue. Rules of affiliation apply.
3. Employers meeting the “alternative size standard”, even if exceed 500 employees. Rules of affiliation apply. Alternative size standard:

- Maximum tangible net worth of business not more than $15M, and
- Average net income (after taxes) of business for two full previous fiscal years is not more than $5M.
LESSONS LEARNED - PAYROLL TAX DEFERRAL

• In FAQ, IRS indicates an employer can claim the payroll tax deferral (provided for under the CARES act) up until the PPP loan is forgiven.

• Example:
  • Loan disbursement – Friday, May 1, 2020.
  • 8 week period up Friday, June 26th, 2020.
  • Assume you apply for forgiveness immediately (June 26\textsuperscript{th}).
  • Lender has up to 60 days (per statute) to approve the forgiveness application.
  • Per IRS FAQ, “Once employer receives decision from lender that its PPP loan is forgiven, the employer is no longer eligible to defer deposit and payment of employer’ share of social security tax due after that date.”
  • A lender can request forgiveness of a PPP loan from SBA after 7 weeks based on expected forgiveness amount. Does this trigger the end in deferral or does approval of a borrower’s forgiveness application?
LESSONS LEARNED - EIDL LOANS

• EIDL Loans.
  • Eligible borrowers can apply for both EIDL loans and PPP loans, but proceeds must be used for separate expenses. Also, the $10k EIDL advance reduces any PPP loan forgiveness.
  • Updates on EIDL applications from SBA:

Dear Applicant,

On March 29, 2020, following the passage of the CARES Act, the SBA provided small business owners and non-profits impacted by COVID-19 with the opportunity to obtain up to a $10,000 Advance on their Economic Injury Disaster Loan (EIDL). The Advance is available as part of the full EIDL application and will be transferred into the account you provide shortly after your application is submitted. To ensure that the greatest number of applicants can receive assistance during this challenging time, the amount of your Advance will be determined by the number of your pre-disaster (i.e., as of January 31, 2020) employees. The Advance will provide $1,000 per employee up to a maximum of $10,000.
LESSONS LEARNED - PAYROLL EXPENSES

• The $100k cap for payroll applies only to wages, not to benefits.
  • Example: Employee with $150k of wages, and $30k of retirement/health.
    • Qualified payroll = $100k of wages plus $30k of retirement/health.

• Gross wages are not reduced by federal withholding or FICA taxes.

• Payments to independent contractors are not payroll of the payor company, but are payroll of the recipient independent contractor.
LESSONS LEARNED - THE 75 PERCENT RULES

• Interim rules released on April 2, 2020 provide:

  • The “non-payroll” portion of the forgivable loan amount is limited to 25%. Said another way, it appears at least 75% of the loan proceeds must be used for payroll for forgiveness purposes.

    • “The Administrator has determined in consultation with the Secretary that 75 percent is an appropriate percentage in light of the Act’s overarching focus on keeping workers paid and employed.”

  • Also, “…at least 75% of the PPP loan proceeds shall be used for payroll costs.”

    • “This limitation on use of the loan funds will help to ensure that the finite appropriations available for these loans are directed towards payroll protection, as each loan that is issued depletes the appropriation, regardless of whether portions of the loan are later forgiven.”
LESSONS LEARNED - THE 75 PERCENT RULES

• Interim rule also requires the following certification:

  • “I understand that if the funds are knowingly used for unauthorized purposes, the federal government may hold me legally liable such as for charges of fraud. As explained above, not more than 25 percent of loan proceeds may be used for non-payroll costs.”

• Important points.

  • Tracking and support for expenditures is borrower’s responsibility.
  • Consider a separate account.
  • Closely track expenses during the 8 week forgivable period to ensure payroll costs hit 75 percent threshold for forgiveness.
  • Statute states “costs incurred and payments made” in relation to forgivable expenses (more on this later).
LESSONS LEARNED - THE 75 PERCENT RULES

• Implications of not meeting 75 percent rules are unknown.

• At a minimum, appears to reduce forgiveness amount.

  • For instance, if the loan is $1 million, and a borrower only spends $700k on payroll during covered period, only $233,333 of the loan can go to eligible non-payroll expenses (75%=$700k, 25% equals $233,333).

  • Means roughly $66,666 of the loan is not forgivable. Is this money returned to lender? What if the money was spent on other non-payroll expenses?

• Other possibilities include: jeopardizing all forgiveness, or invalid loan?

• Importance of planning and modeling on the front end (more on this later).
WHAT IS NEW - MAIN STREET LENDING PROGRAM

• Announced April 9th.

• New lending program. Can be used alongside PPP loans, but not forgivable.

• Like PPP program, program begins with banks.

• Available to U.S. companies with up to 10,000 employees and less than $2.5 billion in 2019 revenue.

• Loans between $1 million and $25 million.

• 4 year term note with adjustable rate.
WHAT IS NEW - SELF EMPLOYED INCOME

• Interim rules released on April 14th, 2020.

• “Self-employment income of general active partners” can be reported as a partnership’s (including a LLC taxed as a partnership) payroll, up to $100k.
  • Appears to include guaranteed payments as well.
  • Unclear how a partnership demonstrates this amount as paid during the forgiveness period.
  • “General active partner” not defined.
  • Partnership, and not partners, must apply.
WHAT IS NEW - SELF EMPLOYED INCOME

• “Owner compensation replacement” can be used as payroll for purposes of 2.5 times loan calculation.
  • Use filed, or to be filed, 2019 IRS Form 1040 Schedule C line 31 net profit.
  • Divide by 12 and multiply by 2.5.

• Note: if had a loss in 2019, no loan allowed.

• For 8 week forgiveness period, use 8/52 multiplied by 2019 net profit. Appears to be automatic forgiveness for this portion.

• 75 percent rule also applies for self-employed individuals- is owner compensation included as part of “payroll”?
• Difference in forgiveness calculation vs loan calculation creating residual loan balance.

• 2019 Schedule C net Profit – $48,000.

• Loan amount – $48,000 / 12 x 2.5 = $10,000.

• Payroll (75%) $7,500; Other forgivable expenses (25%) $2,500.

• Forgiveness under 8/52 above - $48,000 x 8/52 = $7,385.
## LOAN FUNDING - DETAILS AS OF APRIL 13

<table>
<thead>
<tr>
<th>Loan Count</th>
<th>Net Approved Dollars</th>
<th>Lender Count</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,661,367</td>
<td>$342,277,999,103*</td>
<td>4,975</td>
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<table>
<thead>
<tr>
<th>Loan Size</th>
<th>Approved Loans</th>
<th>Approved Dollars</th>
<th>% of Count</th>
<th>% of Amount</th>
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<tbody>
<tr>
<td>$150K and Under</td>
<td>1,229,893</td>
<td>$58,321,791,761</td>
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<td>&gt;$150K - $350K</td>
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<td>&gt;$350K - $1M</td>
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<td>&gt;$1M - $2M</td>
<td>41,238</td>
<td>$57,187,983,464</td>
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<td>&gt;$2M - $5M</td>
<td>21,566</td>
<td>$64,315,474,825</td>
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<tr>
<td>&gt;$5M</td>
<td>4,412</td>
<td>$30,897,983,582</td>
<td>0.27%</td>
<td>9.03%</td>
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</tbody>
</table>

- Overall average loan size is $206K.
LOAN FUNDING

• Initial $349B appropriation exhausted as of April 16\textsuperscript{th}, 2020. Lending temporarily suspended.

• HOPEFULLY AN UPDATE BY MONDAY....
YOUR LOAN HAS FUNDED - PLANNING

• The “covered period” means “the 8-week period beginning on the date of the origination of a covered loan.”

• Don’t forget: 8 week forgiveness clock begins upon date of loan funding, even (we think, based upon a FAQ) if only take a partial draw.

• And lender must make the first disbursement of the loan no later than ten calendar days from the date of loan approval.
• Forgiveness amount equals the “the sum of the following costs incurred and payments made” during the covered period:

  • Payroll costs. Interest on a covered mortgage obligation (liability incurred in ordinary course of trade or business on real/personal property that was incurred before Feb. 15, 2020).
  
  • Payment on a covered rent obligation (rent obligated under leasing agreement in force before February 15, 2020).
  
  • Covered utility payment (electric, gas, water, transportation, telephone, internet, if service began before February 15, 2020).

• Don’t forget about the 75 percent rules.
YOUR LOAN HAS FUNDED - PLANNING

• Is the reference to amounts “incurred” and “paid” for the forgiveness period an accrual or cash reference?

• Is it just the actual cash outlay during the covered period, or is it an annualized accounting of expenses (8 weeks out of 52 weeks multiplied by the total costs, for example).

• Are prepayments and/or advanced payments allowed? What about paid overtime?
YOUR LOAN HAS FUNDED - PLANNING

• Examples with loan disbursement date of April 15, 2020 (covered period runs 8 weeks until June 10th):
  • Monthly rent paid April 1st – Incurred cost April 15 – 30th but no payment during 8 weeks.
  • Monthly rent paid June 1st – No cost incurred June 11th – 30th but payment made during 8 weeks.
• These issues could apply to payroll, utilities and interest as well.
YOUR LOAN HAS FUNDED - PLANNING

• Emphasis: planning and modeling on the front end.
• Waiting till the end may be too late.
  • Is possible even slight changes to payroll, FTE numbers, or non-payroll expenses could result in the loss of material forgiveness amounts.
YOUR LOAN HAS FUNDED - PLANNING

• Using a separate account. Not required but perhaps advisable:
  • Consider placing proceeds into your payroll account (if applicable).
  • Using a separate account may be beneficial for tracking purposes:
    • Pay expenses from operating account and replenish with PPP funds from separate account with detailed description of transaction (Flag with “PPP”).
  • Segregating PPP funds could help reduce possible unintended errors.
YOUR LOAN HAS FUNDED - PLANNING

• Beware reductions in FTE.

• Average number of FT employees employed per month during covered period, vs, at election of borrower:
  • Average number of FT employees employed during period running from Feb. 15, 2019 and ending June 30, 2019, or
  • Average number of FT employees employed during period running from January 1, 2020 and ending February 29, 2020.
  • Seasonal employers: use Feb. 15, 2019 and ending June 30, 2019.

• May require a business to restore its FTE count by beginning of covered loan period. Consider impact on employees claiming unemployment benefits.
What is a “FTE”? Traditional governmental guidance: 1 FTE = 30 hours per week. 2 part-time employees at 15 hours per week equal 1’s FTE.

Appears not to be employee specific.

Can bring FTE count back up by June 30th, but again, beware the 75 percent rule.
YOUR LOAN HAS FUNDED - PLANNING

• For example, if a business receiving a PPP loan has furloughed half its FTE count and plans to bring all furloughed employees back by end of 8-week covered period, the business may not be able to spend 75 percent of the loan on payroll.

<table>
<thead>
<tr>
<th></th>
<th>Average Payroll</th>
<th>Multiplier</th>
<th>Loan Amount</th>
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</thead>
<tbody>
<tr>
<td>Average Payroll</td>
<td>10,000.00</td>
<td>2.5</td>
<td>25,000.00</td>
</tr>
<tr>
<td>Furlough of 50%</td>
<td>(5,000.00)</td>
<td></td>
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</tr>
<tr>
<td>Payroll after Furlough</td>
<td>5,000.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>8 Weeks Payroll Costs</td>
<td>10,000.00</td>
<td>68.97%</td>
<td>Below 75%</td>
</tr>
<tr>
<td>Other Eligible Costs</td>
<td>4,500.00</td>
<td>31.03%</td>
<td></td>
</tr>
<tr>
<td>Total 8 Week Costs</td>
<td>14,500.00</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
YOUR LOAN HAS FUNDED - PLANNING

• Beware reductions in salary.
  • Forgiveness reduced by amount of any reduction in total salary or wages of any employee (making $100k or under for 2019) during covered period in excess of 25% of total salary or wages of the employee during the most recent full quarter during which the employee was employed before the covered period.
  • Note focus is on “any employee”.
  • Note also employees making more than $100k completely excluded.
  • Can avoid this reduction by restoring any salary cuts.
Example:

- Employee 1’s salary reduced from $50k to $40k (20%).
- Employee 2’s salary reduced from $50 to $30k (40%).
- Employee 3’s salary reduced from $150k to $50k (66%).

Only Employee 2’s salary reduction impacts loan forgiveness (apparently).

But as always, beware the 75 percent rule.
Open question on salary reductions.

- Note comparison is between 8 week covered period and the most “recent full quarter during which the employee was employed before the covered period”.
- Literally an apples to oranges comparison: a full quarter (3 months) to 8 weeks.
- How can an employer spend an amount of payroll in 8 weeks for an employee equal to that employee’s payroll for the previous quarter?
YOUR LOAN HAS FUNDED - PLANNING

• Summary points for avoiding forgiveness reductions.

• During 8 week period, avoid FTE reductions (if possible).

• Strive to use at least 75% of the loan proceeds on payroll costs.

• If FTE headcounts are reduced, be strategic in choosing the comparison period and attempt to restore FTE headcount by June 30th.

• During the 8 week period, do not reduce any individual employee’s compensation by more than 25% (ignoring any employee making $100k or more). If pay is reduced by more than 25%, attempt to restore pay by June 30th.
THE FORGIVENESS STAGE

• Many open questions.
  • We know the forgiven debt is not taxable income, but are the expenses giving rise to the forgiven debt tax deductible?
  • State tax considerations.
  • Consequences of not meeting the 75 percent tests.
  • Uncertain interpretations (for example, using a “quarter” time period to compare to an 8 week time period would appear to be an apples to oranges comparison).
  • Unused portions of the PPP loan- are they rolled into the 2 year term note, or are they returned to the lender?
  • What are the consequences of an unintentional miscalculation of loan amounts during application and funding stage.
THE FORGIVENESS STAGE

• The application process may be lengthy, with substantial required documentation, including: payroll records, invoices, bank statements, tax forms, and others.

• Importance of planning on the front end and tracking progress during 8 week covered period.

• Given the uncertainty during the application and approval stage, some borrowers may discover they borrowed more (or less) than should have. Banks may ask more questions as well during the forgiveness stage.
WHAT EIDE BAILLY IS DOING FOR OUR CLIENTS

- We assisted many clients with gaining an understanding of the PPP program and preparing for and making application for the loan.

- We are now focused on the next phase of the process and have developed a modeling tool to assist our clients in maximizing their loan forgiveness. This model allows us to:
  1. Project what forgiveness will look like if you stay the course.
  2. Project what forgiveness will look like if you change your actions.

- Time is of the essence and we recommend you contact your Eide Bailly representative as soon as possible. If you are not a client you can go to our website and submit your information.
WHAT EIDE BAILLY IS DOING FOR OUR CLIENTS

EIDE LIKE ... TO MAXIMIZE MY LOAN FORGIVENESS
THANK YOU