Workforce Management to Maximize PPP Loan Forgiveness

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Overview

- How to Spend PPP Loan Funds on Payroll Costs
- How to Manage Wage Reductions to Avoid Losing Loan Forgiveness
- How to Manage Layoffs to Avoid Losing Loan Forgiveness

Spending PPP Loan Funds on Payroll Costs

- **Key Factors:**
  - At least 75% of the PPP loan funds must be spent on payroll costs
  - Only spending during the eight-week period from the loan origination date will be forgiven.
  - Documentation is key.
- **Consequences of Misusing PPP Loan Funds:**
  - If PPP funds are used for unauthorized purposes, SBA will direct you to repay those amounts.
  - If you knowingly use the funds for unauthorized purposes, you will be subject to additional liability such as charges for fraud.

Forgiveness-Eligible Expenditures

- **Eligible expenditures for forgiveness include payment of:**
  - **Payroll costs** (as defined by the CARES Act).
  - **Interest on any "covered mortgage obligation**."
    - Any indebtedness incurred before Feb. 15, 2020, that is

      (i) a liability of the borrower, and

      (ii) a mortgage on real or personal property.
    - No prepayment and no principal payments
  - **Covered rent obligations** under a leasing agreement in force before Feb. 15, 2020.
  - **Utility payments** for service that began before Feb 15, 2020, on any of the following services:
    - electricity, gas, water, transportation, telephone and internet access

Forgiveness-Eligible Expenditures

- **Definition of "payroll costs:"**
  - salary, wages, commissions or similar compensation;
  - cash tips or the equivalent (based on employer records or a reasonable, good-faith estimate of such tips);
  - payment for vacation, parental, family, medical,or sick leave;
  - allowance for separation or dismissal;
  - payment for providing employee benefits consisting of group health care coverage, including premiums, and retirement;
  - payment of state and local taxes assessed on compensation of employees; and
  - employee's share of federal payroll taxes.

Exclusions from Payroll Costs

- **Pay to employees residing outside of the United States**
- **Cash compensation in excess of an annual salary of $100,000, prorated as necessary, but not non-cash benefits:**
  - employer contributions to defined-benefit or defined-contribution retirement plans;
  - providing employee benefits consisting of group health care coverage, including insurance premiums; and
  - state and local taxes assessed on employee pay
- **Employer's share of federal payroll taxes**
- **Paid sick leave under the FFCRA**
- **Compensation paid to independent contractors**

Example: Loan Disbursed on April 21, 2020

President – Employee
$~~250k salary~~; $20k in benefit costs

~~**General Counsel – Contractor**~~
~~$90k in r[illegible]ual pay~~

VP Sales – Employee
$90k salary; $~~50k bonus in March~~; $10k in benefit costs

Avoiding Loss of Loan Forgiveness

- **Two personnel actions can erode loan forgiveness:**
  - Reducing salaries and wages, and
  - Reducing full-time equivalent headcount

Reductions to Loan-Forgiveness Eligibility

- **Wage Cuts**
  - Loan-forgiveness eligibility is also reduced to the extent that compensation for any individual making **less than $100,000** per year is reduced by more than 25% measured against the most recent full quarter prior to the loan.
  - Employees earning **more than $100,000** can have their compensation reduced by more than 25%.

Curing Wage Reductions

- **Wage reductions for employees earning less than $100,000 and occurring between Feb. 15 and April 26, 2020, can be cured**
- **Curing wage reductions requires the eligible employer to have "eliminated" the reductions no later than June 30, 2020**
  - What does "eliminated" mean?
- **Wage reductions occurring after April 26, 2020, cannot be cured**
- **Failure to cure reduces loan forgiveness by an amount equal to the total reduction in salary and wages**

How to Manage Layoffs to Avoid Losing Loan Forgiveness

Reductions to Loan-Forgiveness Eligibility

- Reducing full-time employee equivalents can erode eligibility for loan forgiveness.

Reductions to Loan-Forgiveness Eligibility

- **Terminations.** Loan-forgiveness eligibility will be reduced based on failure to maintain the average number of full-time equivalent employees benchmarked against one of two prior periods (which the borrower chooses):
  - Jan. 1, 2020, through Feb. 29, 2020; or
  - Feb. 15, 2019, through June 30, 2019

Reductions to Loan-Forgiveness Eligibility

- Curing Terminations
  - Terminations of full-time equivalent employees occurring between Feb. 15, 2020, and April 26, 2020, **can be cured** by June 30, 2020, to restore full loan-forgiveness eligibility.
  - Terminations of full-time equivalent employees occurring after April 26, 2020, **cannot be cured**.

Scenario

- Marleys Art Craze has two locations in the state of Kansas.
- Business teaches painting techniques at its two studio locations.
- Employs four full-time employees and two part-time employees.
- Leases both locations and pays monthly rent.
- Shut down since March 30 as a result of COVID-19.
- PPP loan applied for on April 3 with plans to move business to online teaching temporarily and continue operations.
- PPP loan granted on April 3 and received on April 10.
- Business downturn leads to consideration of layoffs.

What should Marleys do?

Marleys Loan

Marleys received a loan in the amount of $25,000 based on the following facts and calculation:

- No employees make more than $100,000
- Annual payroll: $120,000
- Average monthly payroll: $10,000
- There are no outstanding Economic Injury Disaster Loan (EIDL) amounts

Average Monthly Payroll X 2.5

$10,000 X 2.5=$25,000 Maximum Loan Amount

Forgiveness- Eligibility

- PPP loan funds must be used for approved expenses.
- At least 75% of PPP loan proceeds must be used for approved payroll costs
- Loan forgiveness amounts may be reduced if:
  - the number of full-time equivalent employees in the borrower's headcount is decreased; or
  - if employee salaries and wages are decreased by more than 25% for any employee who made less than $100,000 annualized in 2019.
- Borrowers who decreased their FTEs or wages below the threshold between Feb. 15, 2020, and April 26, 2020, have until June 30, 2020, to restore their numbers back to their Feb. 15, 2020 numbers.
- If requirements for forgiveness are met, the full principal and interest on a PPP loan may be forgiven
- The interim final rule further indicates that the SBA will issue additional guidance on loan forgiveness.

Pre-Layoff Considerations

- Implement a freeze on incurring unnecessary business expenses.
- Postpone any anticipated wage increases.
- Reduce any bonuses that were otherwise anticipated.
- Reduce compensation of employees by up to 25%.
- Consider implementing reduced work schedules for full-time hourly employees (be careful not to impact pay by more than 25%).
- Review the payment terms of current vendor contracts and look for opportunities to renegotiate the terms of those contracts as necessary to reduce costs or change the payment terms.
- Solicit new business. Market for new clients.
- Talent pool rehire availability.

Armstrong Teasdale

Recap and Next Steps

- <u>Step 1</u>: Calculate what 75% of your PPP loan value is.
- <u>Step 2</u>: Review employee-related expenses for the eight-week "covered period" to identify eligible "payroll costs."
- <u>Step 3</u>: Decide whether layoffs or wage reductions are needed in the next five days (i.e., no later than April 26).
- <u>Step 4</u>: Calculate your average FTE headcounts and select a lookback period (i.e., Feb. 15 – June 30, 2019, or Jan. – Feb. 2020).
- <u>Step 5</u>: If any layoffs or wage reductions have been made (or will be made by 4/26), develop a plan for "curing" those actions, if necessary, by June 30.
- <u>Step 6</u>: Document <u>all</u> expenditures of PPP loan proceeds.

Questions?

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