

# **Attention Small Business, Non-Profit, Sole-Proprietors, Independent Contractors and Other Self-Employed Individuals**

## **Client Update Article**

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On Friday March 27, 2020, Donald Trump signed into law the largest lifeline (the CARES Act) in United States history to combat the most trying economic times for the United States. As markets react, supply chains strain, and lockdowns ensue havoc, it's no secret that small business, the self-employed, independent contractors, and sole-proprietors are the most vulnerable during these uncertain times. To help the most vulnerable, the Cares Act provides a small business-focused Paycheck Protection Program (PPP) allowing the federal government to guarantee SBA 7(a) loans up to 100% through December 31, 2020. The SBA 7(a) loans are available to companies with 500 or less employees who are below a gross annual receipts threshold in certain industries. This article will lay out the latest developments regarding the PPP, more specifically, requirements to obtain the loan, the requirements as to how the loan can be used, and the underlying premise of the loan's "forgiveness."

SBA 7(a) loans are known to bypass the normal inefficiencies of SBA lending by allowing lenders to make determinations on borrower eligibility and creditworthiness without going through all of the normal SBA channels. While the SBA 7(a) loan has been in existence and is structured for this type efficiency, only 30% of banks in 2018 authorized such loans. This is important to understand as SBA 7(a) loans can only be obtained by lending institutions approved to provide such loans. When the prospective borrower locates an authorized lender, the focus of the lender's determination to provide the loan is based on whether the company was operational as of February 15, 2020 and had employees to whom it paid salaries and payroll taxes to at the time. Prospective eligible borrowers are required to make "a good faith certification that the loan is necessary due to the uncertainty of current economic conditions caused by Covid-19." Good faith borrowers will be required to use the funds to retain workers and maintain payroll, lease, and utility payments. Below sets forth a list of important lending aspects within the Paycheck Protection Program:

- Applicants may obtain PPP loans up to the lesser of 2.5 times their average monthly payroll costs in the 12 months prior to the date of the loan or \$10,000
- The maximum interest rate is 4%
- Eliminates personal guarantees, collateral and common SBA loan conditions (including certain SBA fees)
- Eliminates recourse to principals except for misuse of proceeds
- Lenders must provide COMPLETE payment deferment for a period of at least 6 months and not more than one year
- Borrowers can make loan payments without pre-payment penalties

It's also important to understand the limits of forgiveness as forgiveness only applies to the amounts spent during an 8-week period after the origination date of the loan (as shown in the calculation below). More specifically, forgiveness only covers payroll costs, interest payments on mortgages, rent and utility payments. Additionally, amounts in excess of the principal will not be forgiven and forgiveness will be reduced proportionally by any reduction in employees retained compared to either (i) the prior year, or (ii) the

period of January 1, 2020 thru February 29, 2020. Forgiveness will also be reduced proportionately by any reduction in pay to any employee beyond 25% of the prior year's compensation, measured from the most recent quarter to the origination of the loan. Additionally, payroll costs eligible for forgiveness do not include compensation paid to employees in excess of \$100,000. The forgiveness determination must be determined by the SBA within 60 days after the lender receives the loan application and the lender must attest the borrower accurately provided and verified the required documentation. Below is an example calculation of the loan application and forgiveness determination based on the information available as of March 28, 2020:

1 Payroll Protection Program ("PPP") Loan Calculations		
2	Trailing 12 Months	Running Total
3 Total compensation for prior 12 months	\$ 300,000	\$ 300,000
4 Compensation above \$100,000/recipient	\$ 50,000	\$ 250,000
5 Compensation paid to employees living outside of the U.S.	\$ 30,000	\$ 220,000
6 Employee portion of FICA	\$ 75,000	\$ 145,000
7 Employee portion of FICA on compensation above \$100,000/employee	\$ 1,500	\$ 146,500
8 Federal income tax withholding	\$ 17,500	\$ 129,000
9 Federal Income tax withholding on compensation above \$100,000/employee	\$ 3,000	\$ 132,000
11 Payroll Cost	\$ 132,000	
12 Monthly Payroll Cost	\$ 11,000	
13 2.5 x monthly payroll cost	\$ 275,000	
14 Cap on PPP loan	\$ 10,000,000	
15 <b>PPP Loan</b>	<b>\$ 275,000</b>	
16		
17		
# Calculation of Forgivable Portion of PPP Loan		
19 Total compensation for 8 weeks following receipt of PPP loan	\$ 50,000	
20 Portion for employees receiving annual compensation of \$100,000	\$ 8,333	
21 Mortgage interest paid in 8 weeks following receipt of PPP loan	\$ 2,500	
22 Rent paid in 8 weeks following receipt of PPP loan	\$ 5,000.00	
23 Utilities paid in 8 weeks following receipt of PPP loan	\$ 1,000.00	
24 Total eligible for forgiveness	\$ 50,167.00	
25 Reduction based on decrease in employer (1102(d)(2))	\$ -	
26 Reduction based on decrease in salary (1102(d)(3))	\$ -	
27 Total amount forgiven	\$ 50,167.00	
28 PPP Loan	\$ 275,000.00	
29 Amount forgiven	\$ 50,167.00	
30 Remaining PPP loan payable @ 4% over 10 years	\$ 224,833.00	

To receive the lender's attestation, it's important to understand what the prospective borrower will be required to provide the lender. Also, it's critical to keep in mind lender requirements will be further known in the next 12-15 days as the SBA is required to provide more detailed regulations. However, up to this point, a prospective borrower seeking loan forgiveness will be required to provide the following:

- 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
  - State income, payroll and unemployment insurance filings.
- Documentation verifying payments on covered mortgage obligations, payments on covered lease obligations, and covered utility payments, including canceled checks, payment receipts, transcripts of accounts, or other substantiating documents

- A certification from a representative of the borrower authorized to make such determinations that:
  - The documentation is true and correct; and
  - 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.

At The Center for Financial, Legal and Tax Planning, Inc., (“The Center”) we’re breaking down all aspects of the Cares Act to provide opportunities to our clients. If your business has been affected by Covid-19, please reach out the Center to ensure you’re maximizing every opportunity available to your business.