



Payment Protection Program

Loans Forgiveness



Provided by: Capstone Capital Group, LLC



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The novel coronavirus - COVID-19 has wreaked havoc on the U.S. and world economy, in addition to causing widespread human suffering and tragedy. In the 2nd Quarter, the U.S. economy registered the deepest decline since the government began keeping records with a contraction in GDP of 31.7%. The Conference Board's Base Case Forecast calls for a rebound in GDP of 32.9% in the 3rd Quarter, but high levels of unemployment are expected to dampen growth in the 4th Quarter with only 1.3% expansion forecasted. This will result in a net contraction in GDP of 3.8% in 2020. A modest recovery of 3.2% is expected in 2021. Recovery to pre-pandemic levels is expected to be a long and uncertain process.

The number of COVID-19 cases in the U.S. is now in excess of 6.6 million, and over 196,000 people have died from the virus. The human suffering resulting from the economic upheaval is reflected in continuing claims for unemployment through the week ending August 22nd, which were 13.3 million compared to continuing claims of only 1.8 million prior to the pandemic.

In an effort to cushion the economic shock, stimulate the economy, and reduce unemployment the Federal Reserve and Congress introduced a number of unprecedented monetary and fiscal measures. In March of 2020 Congress passed the Coronavirus Aid, Relief and Economic Security (CARES) Act a \$2.2 trillion package of direct payments, deferrals, lending and guarantee measures. An important part of the CARES package is the Paycheck Protection Program (PPP).

PPP Loans May Be Forgiven If the Proceeds Were Used in Accordance With the Loan Forgiveness Requirements



Provisions of PPP

The PPP provided \$659 billion for job retention and certain other expenses. Congress enacted the measure on the premise that it would be better to use fiscal stimulus to keep people on their employer's payroll than have them lose their jobs and receive fiscal stimulus through unemployment compensation, and to help keep small businesses afloat. Consequently, PPP loans may be forgiven if the proceeds were used in accordance with the loan forgiveness requirements.

Some of the key provisions of the PPP include:

Eligibility – small businesses, eligible nonprofit organizations, self-employed individuals, independent contractors, veterans organizations and tribal businesses

Size – less than 500 employees or qualifies as “small business concern” under SBA criteria

Loan Amount – lessor of 2.5 times average months payroll as defined or \$10 million

Use of Proceeds – payroll costs and certain other costs including mortgage interest, rent, personal property leases, utilities and interest on other debt (Interest on other debt does not qualify for loan forgiveness.)

Loan terms – 1% fixed rate

Loan forgiveness – eligible payroll and other costs



On June 5, 2020 the PPP Flexibility Act was passed to remedy a number of the shortcomings impacting the ability of businesses to utilize the PPP. Key provisions changed concerning the:

- Amount of proceeds that must be used for payroll costs decreased from 75% to 60%.
- Covered period for maximum loan forgiveness of permissible expenses increased from 8 weeks after funding to earlier of 24 weeks after loan origination or December 31, 2020. Borrowers who received loans prior to the Flexibility Act may use either covered period.
- Deadline for loan forgiveness application was not defined in the original PPP. The Flexibility Act established a deadline of within 10 months after the last day of the covered period.
- Forgiveness reduction safe-harbor deadline extended from June 30, 2020 to December 31, 2020.
- Time period to rehire individuals or replacements and adjust for salary and wage reductions extended to December 31, 2020.
- Loan maturity increased from 2 years to 5 years.
- Loan payment deferral period extended from 6 months to the date the lender receives the forgiveness approval from the SBA.
- Payroll tax deferral may now be used by loan forgiveness recipients.

PPP Utilization

There were four rounds to the PPP, which closed to new loan applications on August 8, 2020. As of that date over 5.2 million loans were approved for more than \$525 billion. The average loan size was approximately \$101,000 and 69% of the loans were \$50,000 or less. Industries with higher labor costs participated in the program to a greater degree as shown in the following sample:

Industry	% of Loans
Construction	12.4%
Manufacturing	10.3
Retail Trade	7.7
Wholesale Trade	5.3
Transportation & Warehousing	3.3

Additional rounds extending the PPP may be possible depending on the outcome of a second stimulus package being negotiated in Congress.

Loan Size	Loan Count	Net Dollars	% of Count	% of Amount
\$50K & Under	3,574,110	\$62,742,565,653	68.6%	12.0%
>\$50K - \$100K	683,785	\$48,676,961,052	13.1%	9.3%
>\$100K - \$150K	294,557	\$36,058,010,813	5.7%	6.9%
>\$150K - \$350K	377,797	\$84,782,932,509	7.2%	16.1%
>\$350K - \$1M	199,679	\$113,558,427,234	3.8%	21.6%
>\$1M - \$2M	53,218	\$73,887,171,387	1.0%	14.1%
>\$2M - 5M	24,248	\$72,184,996,045	0.5%	13.7%
>\$5M	4,734	\$33,121,136,431	0.1%	6.3%

While the PPP Flexibility Act helped to alleviate some of the problems businesses were having with the PPP a number of issues remain including:

Design flaws - Keeping businesses afloat and retaining employees can be incompatible. PPP's main objective is to keep people employed but requiring that 60% of loan proceeds be spent on payroll costs may be impractical if it will cause the business to fail.

High payroll percentage - The requirement that 60% of loan proceeds be spent on payroll costs is still too high for many companies, especially those in industries with lower labor costs.

Ineligible expenses - Inventory, supplies and many operating expenses are not eligible uses of loan proceeds.

Application issues - There were problems applying for and obtaining loans. Some businesses have had better results working with smaller banks even when it is not the main bank they do business with.

Small loan amounts - Often times, loan amounts were too small to make a difference.

Denial - Some loans were frequently denied for even small amounts.

Transparency - There was a lack of program transparency and confusion with program requirements.

These are issues that you should keep in mind if the PPP is extended again and you choose to apply. In the meantime, you should consider alternative sources of financing to provide the working capital your business will need for the long road to full recovery. Transaction-based financing including factoring, purchase order financing and trade finance may be the solution you need to buy inventory and pay employees and operating expenses. Please see "Restarting Your Business After COVID-19 Mandatory Shutdown" available on our website at <https://capstonetrade.com> for additional suggestions.

3 Steps to Loan Forgiveness

Plan Ahead and Make Sure You Take the 3 Steps for Loan Forgiveness.

1

Staffing and pay levels must be maintained. Rehires must be made and salary/wage cuts restored by December 31, 2020.

2

Loan proceeds must be spent on eligible costs during the covered period – the earlier of 24 weeks after loan origination or December 31, 2020.

3

At least 60% of loan proceeds must be spent on eligible payroll costs and no more than 40% may be spent on other eligible costs during the covered period.



Use the below checklist as your guide to navigate the loan forgiveness process:

- 1. Forgiveness Application
- 2. Required Documentation
- 3. Calculating Staffing Levels for Forgiveness Application
- 4. FTE Calculation
- 5. Exemptions on Rehiring Employees
- 6. Pay Requirements
- 7. Grace Period
- 8. Eligible Costs for Loan Forgiveness
- 9. Applying for Loan Forgiveness

1. Forgiveness Application

The PPP loan forgiveness application must be made through the lender. There are two forgiveness applications – the long Form 3508 and the Form 3508 EZ. The Form 3508 EZ may be used if you are a self-employed individual, independent contractor or sole proprietor and does not include any employee salaries in calculating average monthly payroll costs when you applied for your PPP loan; or if you did not reduce salaries or hourly wages for any employee by more than 25% during the covered forgiveness period; or reduce your number of employees between January 1, 2020 and December 31, 2020.

The long Form 3508 includes worksheets for calculating payroll costs and full-time equivalent (FTE) employees. The amount of forgiveness is based on a ratio of FTEs in the covered period to FTEs in the specified period prior to the pandemic, times the eligible costs paid with the PPP loan proceeds in the covered period. If the ratio is greater than 1 you meet the requirements for full loan forgiveness. If it is less than 1 loan forgiveness is reduced proportionately.

If you received an Economic Injury Disaster Loan (EIDL), the proceeds from the advance will be deducted from your PPP loan forgiveness amount.

2. Required Documentation

Documentation is required for payroll costs, FTEs and non-payroll costs.

Payroll costs – bank statements, tax forms and receipts

FTEs – documentation of average FTEs monthly for appropriate periods for your application prior to the pandemic, and during appropriate subsequent periods

Non-payroll costs – verification of existence of payments prior to February 15, 2020, and documentation of eligible payments for the covered period including copies of loan documents, leases and utility bills

Having a system in place to gather and capture this information will help expedite your forgiveness application process.

**Each Employee that Works 40 or More Hours Per Week
During the Calculation Period Counts as One FTE.**

3. Calculating Staffing Levels for Forgiveness Application

Since the primary purpose of the PPP is retention of employees, staffing levels are calculated to determine if adequate staff levels have been maintained. The average number of FTE employees per month during the 24-week PPP period from the date of your loan is compared to one of two time periods.

February 15, 2019 – June 30, 2019
Or
January 1, 2020 through February 29, 2020

Self-employed individuals with no payroll do not need to calculate FTEs. Self-employed PPP is based on 2019 net profit, not payroll data.

4. FTE Calculation

Each employee that works 40 or more hours per week during the calculation period counts as one FTE. Over time does not apply, one employee cannot count for more than one FTE.

Any part-time employees that did not work more than 40 hours on average per week will have their average weekly hours added together. Divide the total by 40 and round to the nearest tenth to determine the FTE for part-time employees. For example, if you have 6 employees who consistently work 20 hours a week, in total they would count as 3 FTEs.

For simplicity, the SBA will allow the use of 1.0 FTE for employees that work 40 or more hours per week, and 0.5 FTE for all other employees. Either method may be used but you must be consistent in how you do the FTE calculation.

5. Exemptions on Rehiring Employees

There may be employees that you had to lay off but are having problems rehiring, which could affect your FTE calculation. Employees who were on your payroll as of February 15, 2020 who were laid off or put on furlough may not wish to be rehired. If an employee rejects your re-employment offer, you may be allowed to exclude this employee when calculating loan forgiveness.

Qualifying for this exemption requires the following:

- You have made a written offer to rehire in good faith
- You have offered to rehire for the same salary/wage and number of hours as before they were laid off
- You have documentation of the employee's rejection of the offer

If any of these criteria apply to an employee, you can also qualify for an exemption if the employee:

- Was fired for cause
- Voluntarily resigned
- Requested and received a reduction of hours

You may also be required to show that you were unable to hire similarly qualified employees for unfilled positions, or document that due to health and safety requirements you were not able to return to normal levels of operation.

6. Pay Requirements

You must maintain at least 75% of total salary and wages. If an employee's pay over the 24 weeks is less than 75% of the pay received during the most recent quarter in which they were employed, the eligible amount for loan forgiveness will be reduced by the difference between current pay and 75% of the original pay.

7. Grace Period

You can rehire any staff laid off or furloughed and reinstate any pay decreased by more than 25% to meet the requirements for loan forgiveness, if these actions were taken to comply with health and safety regulations due to COVID-19 between February 15 and April 26, 2020. The grace period ends December 31, 2020.

8. Eligible Costs for Loan Forgiveness

Payroll costs which are eligible for loan forgiveness include:

- Salaries and wages
- Vacation pay
- Parental, family, medical and sick leave
- Health benefits

The PPP allows loan forgiveness for eligible payroll costs up to \$100,000 annualized per employee, or \$15,385 per person over the eight-week period, or \$46,154 for the 24-week period.

Other or non-payroll costs eligible for loan forgiveness include:

- Mortgage interest on loans existing prior to February 15, 2020
- Rent for real property leases in effect prior to February 15, 2020
- Rent on personal property leases in effect prior to February 15, 2020
- Utility expenses – electric, gas, water, telephone, transportation and internet access in service prior to February 15, 2020

9. Applying for Loan Forgiveness

Many lenders have created online portals to simplify the application submission process for loan forgiveness. The SBA Forms 3580 and 3508EZ will need to be completed and submitted.



Financing Alternatives

PPP loans were a great alternative to closing down your business during the pandemic when times were less certain than the present where the economy is reopening and things are slowly getting back to normal. If a second stimulus plan is offered and PPP is included in the next round it may not be the right answer for many small businesses. You will need to consider whether it is worth your while to apply for a loan if:

- The application process is still difficult.
- You have problems finding a bank to work with that has a good track record originating PPP loans.
- The amount of the loan you can get is too small to make much difference to your business.
- You will have difficulty meeting the 60% payroll spend requirement.
- You will have difficulty meeting the requirements for loan forgiveness.
- Your working capital needs are primarily for inventory, accounts receivable and non-payroll operating expenses.



Alternative funding companies, such as Capstone may be able to provide the working capital you need to reboot your business

If PPP loans don't make sense for your business, then alternative funding companies, such as Capstone, may be able to provide the working capital you need to reboot your business and negotiate the long road to full economic recovery. Capstone can provide flexible and reliable transaction-based financing to buy inventory, and turn accounts receivable into cash to pay employees and operating expenses without the hassle of applying for and complying with government-backed loan programs.

Capstone can provide transaction-based credit facilities including:

- Factoring programs to quickly convert your accounts receivable to cash to buy inventory and pay employees and operating expenses
- Purchase order programs to finance the purchase of finished goods inventory
- Trade finance programs to support your international trade requirements

The road to full recovery will be long and fraught with uncertainty. Government loan programs may not be the solution to your financing needs, and your bank may not be willing or able to help you. You need a business partner that has the experience and expertise to help you with alternative financing to provide the working capital to reboot your business and negotiate the ups and downs on the long road to full recovery.

Capstone Capital Group, LLC is a leading commercial finance company that is focused on providing capital to growing companies in need of working capital solutions. As a private finance company, Capstone is committed to assisting clients with cash flow issues. We understand businesses have unique financial needs and we provide specific financing solutions to fit those needs. Some of our products include Purchase Order (PO) Financing, Factoring Services, and International Trade Financing. We work with businesses offering services and products who bill their customer through “process billing” type contracts, typical for those in the construction trade, publishing, service businesses, suppliers to government agencies, staffing companies, as well as wholesalers. Each of our divisions handle a different aspect of business with one goal in mind: to help our clients grow and remain competitive by ensuring they have access to the capital they need.