

May 13, 2020

One Month Into PPP: How to Maximize Forgiveness and Ensure Compliance

Human Resources & Employment

UPDATE – May 13, 2020: This morning, the Small Business Association (SBA) finally released the promised guidance regarding what a “good faith certification” looks like for the purpose of complying with the Paycheck Protection Program (PPP) – and avoiding criminal prosecution. This guidance is limited in scope to the good faith certification over the necessity of the loan. Notably, the SBA is providing a safe harbor based on the original principal amount of a loan. FAQ 46 states that recipients (and their affiliates) with loans of less than \$2MM will be deemed to meet the requirement of good faith. (For full text of FAQ 46, click [here](#).)

FAQ 46 also provides a second safe harbor of sorts for recipients of \$2MM+ loans. If the SBA investigates and determines the borrower lacked a good faith certification over the necessity of the loan, and the borrower repays the loan, the SBA will not pursue administrative enforcement or referral to other agencies. The deadline to return PPP funds without any possible penalty is tomorrow, May 14, 2020.

This seems like another way of saying: we get it – it’s confusing. Here’s one easy definition of good faith and another easy out for the rest of you. To see all of the FAQs, click [here](#).

UPDATED May 7, 2020, to reflect new deadline for loan repayment amnesty and additional information regarding FTEE calculation for forgiveness (in bold).

Since the CARES Act became law on March 27, 2020, many businesses focused on securing a Paycheck Protection Program (PPP) loan, and it’s no wonder why: unprecedented loan forgiveness. However, while it turns out there may be such a thing as free money, there are still no guarantees in life. PPP funds are targeted for specific expenses during an 8-week period following disbursement, and borrowers must understand the rules to gain the maximum benefit.

Employers who were able to secure a loan during the initial round are a couple weeks into the program; others are waiting to hear if they benefit from last week’s injection of an additional \$310 billion into the program. Here are some tips on how to navigate the PPP:

Know the CARES Act List of Eligible Expenses

Unlike the 880-page CARES Act, the PPP list of eligible expenses is short, divided into “payroll costs” and other allowable uses.

Eligible expenses – Payroll Costs – for 75% or greater of your loan

Per the Small Business Administration’s (SBA) Interim Final Rule, payroll costs

“...consist of compensation to employees (whose principal place of residence is the United States) in the form of salary, wages, commissions, or similar compensation; cash tips or the equivalent (based on employer records of past tips or, in the absence of such records, a reasonable, good-faith employer estimate of such tips); payment for vacation, parental, family, medical, or sick leave; allowance for separation or dismissal; payment for the provision of employee benefits consisting of group health care coverage, including insurance premiums, and retirement; payment of state and local taxes assessed on compensation of employees; and for an independent contractor or sole proprietor, wages, commissions, income, or net earnings from self-employment, or similar compensation.”

Per SBA guidance out April 24, housing stipends and allowances also count as payroll costs.

Excluded from payroll costs are:

- Federal employment taxes imposed or withheld between Feb. 15, 2020, and June 30, 2020
- Sick and family leave provided by the Families First Coronavirus Response Act (FFCRA)
- Any compensation to an employee whose principal place of business is outside the United States
- Any compensation exceeding \$100,000 annually (per recent SBA guidance, compensation is exclusive of non-cash benefits such as employer contributions to retirement, healthcare, etc.)

Eligible Expenses – Non-Payroll – for no more than 25% of your loan

The PPP may also be used for costs related to:

- Continuation of group health care benefits during periods of paid sick, medical or family leave, and insurance premiums
- Mortgage interest payments (but not mortgage prepayments or principal payments)
- Rent payments
- Utility payments (electricity, gas, water, transportation, telephone, or internet access for which service began before Feb. 15, 2020)
- Interest payments on any other debt obligations that were incurred before Feb. 15, 2020, and/or refinancing an SBA Economic Injury Disaster Loan (EIDL) loan made between Jan. 31, 2020 and April 3, 2020. (However, in the interim final rule, the SBA states that “such amounts are not eligible for PPP loan forgiveness”).

Pay Attention to Percentages

In its interim final rule on the PPP, the SBA determined that borrowers must use a “substantial portion of the loan proceeds for payroll costs, consistent with Congress’ overarching goal of keeping workers paid and employed.” Specifically, the SBA requires that 75% of the loan be used for payroll costs, as defined above.

This leaves 25% of the loan to be used for those other expenses. However, how borrowers allocate loan proceeds is just one factor in forgiveness, and may negatively impact another: employee compensation.

Want Forgiveness? Know Your Benchmarks

The PPP ties loan forgiveness to two data points that are company-specific: Employee compensation and full-time equivalent employee (FTEE) count. Loan forgiveness will be reduced dollar for dollar by a reduction in employee compensation during the loan period that is greater than 25% of the total salary or wages of the employee during the most recent full quarter during which the employee was employed prior to the loan period.

Therefore, if you plan to use 25% of your PPP loan to pay rent, you should ensure that doing so does not reduce wages by greater than 25%. *Remember: you can always use more than 75% of the PPP loan on payroll costs.* There is no obligation to use the PPP for non-payroll expenses.

In addition to employee compensation, PPP forgiveness is also tied to the borrower’s FTEE count. Loan forgiveness will be reduced by the same ratio as the FTEE count declined. Here, according to the CARES Act, the borrower has a choice: It can choose to compare its FTEE count on June 30, 2020, to either its average FTEEs per month between Feb. 15, 2019, and June 30, 2019, or the average FTEEs per month between Jan. 1, 2020, and Feb. 29, 2020.

A FTEE is not defined by the CARES Act, but in the absence of further guidance, the IRS definition likely applies (the CARES Act uses the IRS definition in computing FTEEs for the Employee Retention Credit). FTEEs are calculated by adding the hours of part-time employees on a monthly basis and dividing by 120, and employees who work 30 hours or more are counted as full time. **There**

is an exception to the FTEE calculation. On April 29, the SBA issued FAQ 40, which provides that employers need not replace those employees who are offered their job back but turn it down. Specifically, the SBA states that where an employer offers to rehire an employee for the same salary/wages and for the same number of hours, and at that employee declines, the resulting decrease in FTEs will not impact the employer's forgiveness. Employers must keep a record of a "good faith, written offer of rehire," as well as the employee's rejection.

Borrowers have until June 30, 2020, (PPP's current expiration, which could change) to restore full-time employment and salary levels for any changes made between Feb. 15, 2020, and April 26, 2020.

Understand the Interaction Between PPP and EIDL

Many companies will receive both a PPP and EIDL loan. While the CARES Act permits borrowers to do so, spending the money on the same costs is prohibited. For example, companies may not use both the PPP and EIDL for payroll for the month of May 2020. In fact, if a borrower uses EIDL funds for payroll costs, its PPP loan must be used to refinance the EIDL loan. Additionally, proceeds from any advance up to \$10,000 on the EIDL loan will be deducted from the loan forgiveness amount on the PPP loan.

Study the Certification Requirement

In the past few days, the media reported on a number of well-financed companies receiving PPP loans. On April 23, the SBA updated its guidance to address the questions surrounding just who can certify in good faith that "the uncertainty of current economic conditions makes necessary the loan request to support the ongoing operations of the eligible recipient."

In its FAQ 31, the SBA clarifies that borrowers should "take into account their current business activity and their ability to access other sources of liquidity sufficient to support their ongoing operations in a manner that is not significantly detrimental to the business." The SBA also provides an example, stating "it is unlikely that a public company with substantial market value and access to capital markets will be able to make the required certification in good faith, and such a company should be prepared to demonstrate to SBA, upon request, the basis for its certification."

If You Are Questioning Your Eligibility, Follow SBA Guidance

If you received PPP funding and feel the rules have since changed, don't despair. The SBA has updated its guidance since the publication of its interim final rule. In fact, the SBA's guidance addresses the issues resulting from its updated guidance: "Borrowers and lenders may rely on the laws, rules, and guidance available at the time of the relevant application. However, borrowers whose previously submitted loan applications have not yet been processed may revise their applications based on clarifications reflected in these FAQs."

One additional note: In the same guidance, the SBA also states that any company who repays the loan in full by May 14, 2020, will be deemed by the SBA to have made the required certification in good faith.