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SBA Dispenses More Info for Maximizing PPP Forgiveness

Human Resources & Employment

Application Now Available With New Interim Final Rules for Paycheck Protection Program

By Emily Wessel Farr

The Small Business Association (SBA) has published the much-anticipated [Paycheck Protection Program \(PPP\) Loan Forgiveness Application](#), complete with an OMB Control Number (read: it's official). For borrowers who have crossed the Gulf of Good Faith Certification and are now looking to the Future of Forgiveness, the 11-page application that was published May 16 should have your attention.

Also worth noting are the two Interim Final Rules on [PPP loan forgiveness](#) and the [review process](#), both released on May 22 by the SBA. Questions remain, and we anticipate more guidance in the weeks ahead. For now, here are some of the notable issues covered by the Application and the Interim Final Rules:

Covered Period May Change for Administrative Convenience

Since the PPP first became a household name, the curious 8-week “covered period” has distressed accountants and confused everyone else. Way back in April, the SBA issued FAQ 20, which clarified that the covered period begins on the date the PPP funds are disbursed. Employers – required by the PPP to allocate at least 75% of loan payments to payroll – were left to wonder: can I count 8 weeks of payroll where I received funds in the middle of a payroll cycle?

Behold, the “Alternative Covered Period” has appeared. Introduced by the Forgiveness Application, employers with a biweekly (or more frequent) payroll schedule may elect to calculate eligible payroll costs using the eight-week (56-day) period that begins on the first day of their first pay period following their PPP loan’s date of disbursement.

The application notes that borrowers must apply the covered period (not the Alternative Payroll Covered Period) wherever there is a reference in the application to “the Covered Period” only. *Spoiler alert:* Eligible non-payroll costs (still limited to business mortgage interest payments, business rent or lease payments and business utility payments existing before Feb. 15, 2020), which can only make up 25% or less of the “total forgiveness amount” (more on this below), must be paid in the covered period. Essentially, the Alternative Covered Period is available to help employers match payroll to the PPP.

Furloughed Employees Don't Have to Report to Work When Work Is Shut Down

This would have been nice to know earlier, but the SBA has been busy. The Interim Final Rules clarified that payroll costs include the salary, wages or commissions of *furloughed* employees. The SBA states that it determined this interpretation is “consistent with the text of the statute and advances the paycheck protection purposes of the statute by enabling borrowers to continue paying their employees even if those employees are not able to perform their day-to-day duties, whether due to lack of economic demand or public health considerations.”

This makes a lot of sense – particularly for industries still out of operation due to shelter-in-place orders or the limitations imposed as states begin to allow non-essential businesses to reopen. Employers can rest assured that they do not have to plan a return to work when there is no work to return.

Forgiveness Extends to (Some) Payments Not Yet Made

Remember the CARES Act ... the federal legislation that invented the PPP in March 2020? The discerning employer may recall that the CARES Act sets forth that forgiveness is for debt in an amount equal to the sum of the eligible costs *incurred and paid* during the covered period. Since then, employers (and really anyone dealing with accounts payable) rightly pointed out that business doesn't always work that way. Nevertheless, the SBA FAQs did not address whether the SBA would hold borrowers to this condensed timeframe as a requirement for forgiveness.

Fortunately, the forgiveness application provides that payroll costs incurred but not paid during the borrower's last pay period of the Covered Period (or Alternative Payroll Covered Period) are eligible for forgiveness if they are paid on or before the next regular payroll date. The application clarifies that "payroll costs are considered paid on the day that paychecks are distributed or the borrower originates an ACH credit transaction," and are considered "incurred on the day that the employee's pay is earned." Of course, payroll costs incurred and later paid may only be counted once for use of PPP funds.

Clarification on What 75% of Wages Really Means

The CARES Act states that loan forgiveness will also be reduced by salary or wage deductions in excess of 25%. This became confusing as employers realized that lenders calculated the PPP loan amount by looking at quarterly wage earnings, and an 8-week period is only two-thirds of a 12-week period. The forgiveness application clears this up, stating the *average* monthly wage will be compared for purposes of determining any wage reduction.

More Nuance – and Exceptions – to FTE Reduction

The CARES Act requires PPP borrowers to not reduce their prior average FTE count during their Covered Period without reducing their forgiveness by the same ratio. On May 3, the SBA released FAQ 40 that states borrowers who make a "good faith, written offer of rehire" (at the same wages and hours) before June 30, 2020, and who document the employee's rejection of that offer, will not have to replace that employee to achieve their former FTE count and maximize forgiveness.

The forgiveness application adds to this exemption any employees who are fired for cause, voluntarily resign, or voluntarily request and receive a reduction of their hours. The Interim Final Rules state that "borrowers should not be penalized for changes in employee headcount that are the result of employee actions and requests" and that these actions do not impact FTE count. As employers deal with the realities of the pandemic, including, for example, former employees resigning due to out-of-state moves to be closer to family, these exemptions obviate the need to interview replacements hastily – saving companies a meaningful amount of money, time and resources.

It should be noted that rejected offers may impact unemployment benefits. Under Unemployment Integrity Rules, employers may be required to report such information to their state unemployment office. The SBA's Interim Final Rule notes that "further information regarding how borrowers will report information concerning rejected rehire offers to state unemployment insurance offices will be provided on SBA's website."

Finally, where employers reduce employee hours, resulting in a reduction of pay by more than 25%, the Interim Final Rules clarify that the employer is not doubly penalized for that reduction. The rules confirm that the salary/wage reduction applies only to the portion of the decline in employee salary and wages that is not attributable to the FTE reduction. Therefore, where an employer converts a full-time employee into a part-time employee, its forgiveness is reduced by the reduction of the FTE count by 0.5; however, there is no additional reduction based on the corresponding employee pay decrease.

Payroll Costs of the Self-Employed and Owner-Employees

The Interim Final Rules state that, for the self-employed and the owner employees, payroll compensation can be no more than the *lesser* of 8/52nds of 2019 compensation (i.e., approximately 15.38 percent of 2019 compensation) or \$15,385 per individual in total across all businesses. Unlike regular employees, no additional forgiveness is provided for retirement or health insurance contributions for self-employed individuals, including Schedule C filers and general partners, as such expenses are paid out of their

net self-employment income

Fear of the All-or-Nothing PPP Loan Is No Longer Necessary

Perhaps the most problematic aspect of the PPP for many businesses is the requirement that loan proceeds be used for no more than 25% of non-payroll eligible costs. The language was ambiguous as to whether an employer in, say, New York City, which spent 75% of loan proceeds on rent while keeping its business closed and few people employed, would receive any forgiveness, or would be found non-compliant and therefore ineligible for any forgiveness.

Before the release of the forgiveness application, the SBA did not give any such assurance – in the form of FAQs or otherwise. However, the PPP Loan Forgiveness Calculation Form (page 3 of the application) instructs borrowers to calculate their “potential forgiveness amounts” by looking at 1) a modified PPP loan amount when factoring in wage and workforce reductions, 2) the entirety of the PPP loan, and 3) “The Payroll Cost 75% Requirement,” which is the borrower’s payroll costs divided by 0.75. Notably, the “Forgiveness Amount” is defined as the smallest of the three options for the forgiveness amount. *In other words, this is not an all-or-nothing scenario.*

As a simple example: suppose a borrower had a payroll cost of \$40,000 per month, and it received and spent 2.5 times that amount, or \$100,000, in a PPP loan. The borrower has yet to reopen for business and decided to rehire all employees at 50% of their pay. The borrower spent the remainder of the PPP loan on rent and utilities.

Modified Loan[\$100,000]- [\$40,000] = \$60,000

[spent][reduction in wages over 8 weeks]

PPP Loan Amount\$100,000

Payroll Cost 75% \$75,000

The borrower would receive \$60,000 in forgiveness, not 0.

It is also worth noting that the forgiveness application’s representations and warranties section (page 4) requires the borrower to certify that the “dollar amount **for which forgiveness is requested**” does not include “nonpayroll costs in excess of 25% of the amount requested.” Therefore, if the fictional New York City employer mentioned above spent 75% of its loan proceeds on rent, the maximum amount of loan forgiveness would be equal to 50% of the loan, or 25% (leftover for payroll costs) plus 25% (that percentage of the loan that can be forgiven for non-payroll costs).

Payroll Costs Are Broader Than They Appear

Many employers empathize with the fictional New York City employer, struggling to make the 75/25 ratio of payroll to non-payroll costs. As such, whether or not bonuses can be paid out with PPP money has been a popular question. Good news: the Interim Final Rules clarify that bonuses and hazard pay are payroll costs “because they constitute a supplement to salary or wages, and are thus a similar form of compensation.” These payouts are still subject to a cap so that the employee’s total compensation does not exceed \$100,000 on an annualized basis.

One note of caution: Employer should not use bonus and hazard pay interchangeably – the latter suggests danger (and awareness of such). The U.S. Department of Labor defines hazard pay as work that “causes extreme physical discomfort and distress which is not adequately alleviated by protective devices ... and is deemed to impose a physical hardship.” Employers should consult employment counsel before determining whether work is eligible for hazard pay.

The Shake Shack Effect

For those employers keeping up with the SBA’s FAQs, on May 13, the agency created a safe harbor for all borrowers of PPP loans of less than \$2 million – a surprisingly simple criterion, but a designation borrowers of smaller loans welcomed. Employers should note the forgiveness application asks those who received loans (together with their affiliates) equaling \$2 million or more to check a

box. Employers should take care to not mistakenly check the box when it does not apply – and might lead to more paperwork.

Your Mysterious EIDL Advance Deposit

For employers who received an EIDL emergency advance, the Interim Final Rules confirm that the SBA will deduct it from the total amount forgiven. The forgiveness application asks for both the amount of any EIDL advance and the EIDL application number. Employers should take care to not confuse the EIDL loan (which is interest bearing) with the EIDL *advance*. Employers who received an EIDL but did not receive an advance will not have their forgiveness reduced.

Your Lender – or the SBA – may audit you

The Final Interim Rules state that, as a general matter, the lender will review and determine its borrower's loan forgiveness. Once the lender receives a complete application, it has 60 days to issue a decision to the SBA and request payment from the agency. However, that may not be the end of the story. The SBA can review the loan and the loan application and can disagree with the lender's conclusion on eligibility. More specifically, the SBA can review whether the borrower calculated the loan correctly, whether it used the loan for allowable purposes, and if it was entitled to partial or full forgiveness.

The forgiveness application includes a long list of documents that will be required of borrowers, and other documents that must be maintained but not submitted. Employers are encouraged to start organizing their documents now.

Additionally, the application states that the borrower must retain all documentation for a period of six years. As the SBA reminds us in the Interim Final Rules: "As noted on the Loan Forgiveness Application Form, the borrower must retain PPP documentation in its files for six years after the date the loan is forgiven or repaid in full, and permit authorized representatives of SBA, including representatives of its Office of Inspector General, to access such files upon request." (*Note: It is always wise to call your lawyer first when you receive such a request*). In sum, your PPP loan documentation should stick around for some time.