

Paycheck Protection Program Forgiveness Application and Additional Rules¹

On May 15, 2020, the Small Business Administration (“SBA”) released the loan forgiveness application (“Application”) for borrowers who participated in the Paycheck Protection Program (“PPP”). The Application, together with the accompanying instructions and worksheets, provide step by step assistance and guidance for forgiveness of up to 100% of the principal amount of the loans under the PPP and a summary is provided below. In addition, on May 22, 2020, the SBA published two Interim Final Rules (the “Rules”) providing further clarity on PPP loan forgiveness requirements, the loan review process and the responsibilities of borrowers and lenders. These Rules are summarized below as well.

Application

- **Costs Eligible for Forgiveness.** If at least 75% of the loan proceeds were used by borrowers for payroll costs², then borrowers may be eligible for loan forgiveness for expenditures made during an eight-week period following the loan’s origination for payroll costs and certain eligible non-payroll costs. In the Application instructions, the SBA clarified the costs eligible for forgiveness and the covered period.
 - **Alternative Payroll Periods.** To better correlate with borrower’s regular payroll cycles, the SBA clarified that the covered period may constitute (i) the 56 days from and including the date the PPP loan was received (the “Covered Period”) or, (ii) the 56 days commencing with the first day of the pay period immediately following receipt of the PPP loan (the “Alternative Covered Period”). Importantly, the Covered Period (and not the Alternative Covered Period) applies when determining forgiveness for non-payroll costs.
 - **Payroll Costs Incurred But Not Paid.** In calculating their payroll costs, borrowers may include both payroll costs actually paid as well as payroll costs incurred but not paid during either the Covered Period or Alternative Covered Period. Payroll costs paid are considered paid on the day that the paychecks are distributed, or the borrower originates an ACH credit transaction. Payroll costs are considered incurred on the day the pay is earned. If employees’ pay is earned but not paid during the applicable eight-week period, the payroll costs incurred are eligible for forgiveness if they are paid on or before the next regular payroll date. Payroll costs paid and incurred should only be counted once in calculating the forgiveness amount. Amounts paid to an employee in excess of \$100,000 annually (prorated to \$15,385 for the eight-week period) are excluded.
 - **Eligible Non-Payroll Costs.** Interest on mortgage obligations on real and personal property and business rent or lease payments for real and personal property pursuant to agreements entered into before February 15, 2020 will be eligible non-payroll costs that can be included in the Application. Payments of mortgage principal and any prepayments are expressly excluded. Eligible non-payroll costs also include payments for electricity, gas, water, transportation, telephone, or internet access for which service began before February 15, 2020. Eligible non-payroll costs include those paid during the Covered Period or incurred during the Covered Period and paid on or before the next regular payment date.
 - **Non-Payroll Cost Exclusion.** A borrower may exclude any non-payroll costs it is not seeking to include in the forgiveness amount. This could be helpful to borrowers who might otherwise not meet the requirement that at least 75% of the forgiveness amount must be spent on payroll costs.
- **Reduction In Loan Forgiveness.** Loan forgiveness will be reduced in proportion to the decrease, if any, in the number of full-time equivalent³ (“FTE”) employees during the Covered Period or the Alternative Covered Period, as applicable, compared to a reference period chosen by the borrower of either February 15, 2019 to June 30, 2019 or January 1, 2020 to February 29, 2020.
 - **FTE Reduction Safe Harbor.** Borrowers are exempt from this reduction under the FTE Reduction Safe Harbor if the number of full-time equivalent employees on June 30, 2020 is at least equal to the number of FTE employees on payroll for the pay period that includes February 15, 2020. Exceptions to the FTE reduction apply if the borrower made a “good faith, written offer to rehire” an employee during the Covered Period or

¹ This document is subject to the text of the Application, its instructions and the Rules in addition to any further guidance from the federal government, lenders and other agencies in connection with the PPP loan application, loan forgiveness or review process. As always, its highly recommended that you consult your attorney, accountant or other advisers for further advice on this matter.

² “Payroll costs” include salaries, wages, and other compensation, certain employment taxes, and qualified sick and family leave subject to certain credits, among other things.

³ Full-time equivalency is based on a 40-hour work week and calculated per individual based on their average hours worked during the relevant period.

Alternative Covered Period or the employee was (i) fired for cause, (ii) voluntarily resigned, or (iii) voluntarily requested and received a reduction of hours but only if the positions was not filled by a new employee.

- Salary/Hourly Wage Reduction Safe Harbor. Forgiveness also may be reduced for decreases of the wages of any employee who earns less than \$100,000 annually by more than 25% when compared to the period January 1, 2020 to March 31, 2020. Borrowers may be exempt from this reduction if they restore the wage level at June 30, 2020 to the level that existed for the pay period that includes February 15, 2020.

➤ Documents To Be Submitted To Request Loan Forgiveness. The following documents must be submitted:

1. The Loan Forgiveness Application, which consists of:

- a. PPP Loan Forgiveness Calculation Form (attached to the Application); and
- b. PPP Schedule A.

The SBA issued instructions for each of these forms and a worksheet with further instructions to help borrowers determine FTE for purposes of loan forgiveness.

2. Documentation verifying the eligible cash compensation and non-cash benefit payments from the Covered Period or the Alternative Covered Period, including:

- a. Bank account statements or third-party payroll service provider reports;
- b. Tax forms (or equivalent third-party payroll service provider reports); and
- c. Payment receipts, cancelled checks, or account statements documenting contributions to employee health insurance and retirement plans that the borrower included in the forgiveness amount.

3. Documentation showing the number of employees and payroll information used to calculate the FTEs.

4. Documentation verifying the existence of business mortgage obligations, rent and lease obligations and business utility services prior to February 15, 2020 and payments for such obligations and services made during the Covered Period.

➤ Document Retention. The Application also imposes strict document retention requirements on loan forgiveness applicants for purposes of inspection by the SBA. For a period of six (6) years from the date of forgiveness (or loan repayment in full), loan forgiveness applicants must preserve and be prepared to furnish upon request documentation that would support the facts and figures underlying the applicant's calculations and statements submitted as part of the Application, and underlying worksheets, including documents supporting applicants' salary/wage reduction calculation; documents evidencing job offers and rejections, firings for cause, voluntary resignations, and written requests for a reduced work schedule; and other documents supporting the maintenance or reduction of employment and salary levels, as reflected in the borrower's application.

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Additional Rules

On May 22, 2020, the SBA published the Rules providing further clarity on PPP loan forgiveness requirements and the loan review process.

➤ Loan Forgiveness Requirements.

- *Timeline*: Lenders will generally have 60 days from receipt of a completed Application to issue a decision regarding forgiveness to the SBA.
- *Furloughed Employees*: Wages to furloughed employees constitute "payroll costs" that are eligible for forgiveness, except to the extent such costs would cause an employee's total compensation to exceed \$100,000 on an annualized basis.
- *Compensation to Owner-Employees*: Loan forgiveness for owner-employees and self-employed individuals' payroll compensation is capped at the lesser of 8/52 of 2019 compensation (i.e., approximately 15.38% of 2019 compensation) or \$15,385 per individual in total across all businesses. Owner-employees are capped by the amount of their 2019 employee cash compensation, retirement and healthcare contributions.
- *Compensation to Self-Employed Individuals and General Partners*: Self-employed individuals filing a Schedule C are capped by the amount of their owner compensation replacement, calculated based on 2019 net profit. General

partners are capped by the amount of their 2019 net earnings from self-employment (reduced by claimed section 179 expense deduction, unreimbursed partnership expenses and depletion from oil and gas properties) multiplied by 0.9235. Self-employed individuals, including Schedule C filers and general partners, will not receive forgiveness for retirement or health insurance contributions.

- *Mortgage Interest*: Advance payments of mortgage interest are not eligible for loan forgiveness.
- *FTE Reduction Safe Harbor - Rejected Offers*: The Rules provide additional clarification around the exemption from loan forgiveness reduction for borrowers who have offered to rehire laid-off employees or restore employee hours and the employee rejected such offer. In the event of such rejection, the Rules state that a borrower may nonetheless exclude any reduction in employee headcount that is attributable to such an employee if all of the following apply:
 - The borrower made a good-faith, written offer to rehire such employee (or restore the reduced hours of such employee) during the Covered Period or the Alternative Covered Period.
 - The offer was for the same salary or wages and same number of hours as earned by such employee in the last pay period prior to the separation or reduction in hours.
 - Such employee rejected the offer.
 - The borrower has maintained records documenting the offer and its rejection.
 - The borrower informed the applicable state unemployment insurance office of such employee's rejected offer or reemployment within 30 days of the employee's rejection of the offer.⁴
- *FTEs*: The Rules confirm that a "full-time equivalent employee" means an employee who works 40 hours or more, on average, each week.
- *Salary/Hourly Wage Reductions*: To ensure that borrowers are not doubly penalized for a headcount reduction and a salary/wage reduction, the salary/wage reduction applies only to the portion of the decline in employee salary and wages that is not attributable to the headcount reduction. For example:
 - An hourly wage employee had been working 40 hours per week during the reference period (FTE employee of 1.0), and the borrower reduced the employee's hours to 20 per week during the Covered Period (FTE employee of 0.5). There was no change to the employee's hourly wage during the Covered Period. Because the hourly wage did not change, the reduction in the employee's total wages is entirely attributable to the FTE employee reduction, and the borrower is not required to conduct a salary/wage reduction calculation for that employee.

➤ Loan Review Procedures.

- *SBA Review*: The Rules clarify that the SBA may review any PPP loan of any size the SBA deems appropriate (not just loans over \$2 million). If the SBA determines that a borrower may be ineligible for a PPP loan or ineligible to receive the requested forgiveness amount, the SBA will require the lender to obtain additional information from the borrower. Failure to respond to the SBA's inquiry may result in an ineligibility determination.
- *Notification of SBA Review*: If the SBA chooses to review a loan, the SBA will notify the lender, and the lender must notify the borrower within five (5) business days of receipt.
- *Appeal of Ineligibility Determination*: The SBA intends to issue a separate interim final rule establishing a process for borrowers to appeal an ineligibility determination.
- *Timing of SBA Loan Review*: The SBA may undertake a review at any time at the SBA's discretion. As noted on the Application, 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 the SBA to access such files on request.
- *Accounting for the Loan During Review*: The Rules do not specify how borrowers should account for the loans during the forgiveness review period. Please consult with your accountants or other financial advisers on this matter.

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⁴ A footnote to the Rules states that the SBA will post on its website further information regarding how borrowers should report information to state unemployment offices about rejected rehire offers.

**Paycheck Protection Program and Health Care Enhancement Act (the Act) that amends the
Coronavirus Aid, Relief, and Economic Security Act (CARES Act)**

Small Business Provisions Summary

Below is a summary of certain provisions applicable to small businesses under the CARES Act, as amended.

- **Small Business Assistance.** The Act will revive the Small Business Administration (SBA)'s initial \$349 billion Paycheck Protection Program (PPP) under the CARES Act and will make an additional \$310 billion available for PPP funding. The PPP allows small businesses that have been hurt by the epidemic to apply for government-guaranteed loans with participating banks. Those loans will be forgiven if they are used to cover payroll costs, subject to some conditions. Please refer to the Background section below for further details. The Act also increases the total amount of funding available for SBA loans under the Economic Injury Disaster Loan Program (further explained below).
- **Availability.** The initial amount that was available under the PPP was depleted within a few days and expected demand for this additional amount is also expected to be high. We suggest that you contact your lender and complete an application promptly.

➤ **BACKGROUND**

As previously discussed:

- Under the PPP program, small businesses include (i) businesses that have fewer than 500 employees; (ii) self-employed individuals; (iii) sole proprietors; (iv) independent contractors; and (v) businesses in the accommodation and food services sector with fewer than 500 employees per location. The measure defines "employee" for purposes of determining whether a business employs less than 500 employees to include full-time, part-time, and other basis employees.
- Loans are available to eligible borrowers under the program through June 30, 2020, fees are waived, payments are deferred by at least six months (but not more than one year), and the SBA's "credit elsewhere" test (the ability to obtain funding from other sources without undue hardship) is waived.
- The maximum loan amount under the Section 7(a) Paycheck Protection Program is the **lesser** of 2.5x your average monthly payroll costs over the last twelve months or \$10 million.
 - Applicable uses of loan funds include (i) payroll costs, (ii) costs related to the continuation of group health care benefits, like paid sick, family, or medical leave, (iii) insurance premiums, (iv) employee salaries or wages, (v) interest on any mortgage obligation, (vi) rent, (vii) utilities, and (viii) the interest on other debt obligations.
 - "Payroll costs" include salaries, wages, and other compensation, certain employment taxes, and qualified sick and family leave subject to certain credits, among other things.
- Loans under the program are 100% guaranteed by the federal government, which is an increase to the existing guarantee percentages under the current SBA loan program.
- Collateral and personal guarantees are not required.
- To be eligible, a borrower must have been in operation on February 15, 2020, and have paid employee salaries and payroll taxes.
- Loans under the program are eligible for forgiveness up to the aggregate amount of payroll cost, interest payments on mortgage obligations, rent payments and utility payments made during the eight-week period following loan origination as long as the amount does not exceed the original principal.
 - The amount forgiven is lowered by reductions in full-time employment and in situations where total salaries and wages for workers making less than \$100,000 fall by more than 25% from the applicable prior period, but this can be mitigated by rehiring employees and restoring compensation.
 - Amounts not forgiven continue to be guaranteed and will have a maximum maturity date of 10 years from the date the borrower applied for loan forgiveness.
- Borrowers are required to certify that (i) the uncertainty of current economic conditions makes the loan request necessary to support the borrower's ongoing operations, (ii) funds will be used to retain workers and maintain payroll

or make mortgage payments, lease payments, and utility payments, and (iii) the recipient does not have an application pending or received funding under this section for the same purpose and duplicative amounts.

- The loans will be at an interest rate no higher than 4%.

➤ Other Small Business Programs.

- The legislation also includes or expands a number of other programs targeted at small businesses:
 - Raising the maximum loan available under the existing *Express Loan program* from \$350,000 to \$1 million.
 - Supporting a grant program for small business development centers to facilitate coronavirus-related entrepreneurial development, with priority for women and minority business centers.
 - Requiring the SBA to pay for six months the principal, interest and associated fees for SBA-guaranteed loans made under existing SBA loan programs that are in regular servicing status, with borrowers relieved of the obligation to pay these amounts and financial institution lenders encouraged not to increase their reserves in connection with such payments.
- Economic Injury Disaster Loan (EIDL) Program.
 - The EIDL does not contain forgiveness provisions and is for small businesses that can prove economic damage.
 - EIDL loans may require a personal guarantee and/or the posting of collateral, as these loans have previously required.
 - The application process for the EIDL loan is available on the SBAs disaster relief site. The process could take a few weeks.
 - Subject to final regulations, borrowers can borrow under the Paycheck Protection Program and the EIDL program, but will be precluded from obtaining all or part of a PPP loan if they have already obtained an EIDL loan for the same purpose.
 - An EIDL loan made after January 31, 2020 and before the date on which PPP loans are made available may be refinanced into a PPP loan.
 - Eligible entities may also, in connection with the EIDL application, make an initial draw of \$10K that must be paid by the SBA within three days of submission of the application.

➤ CARES Act Process.

- Approach your lender and inquire about applying for a 7(a) small business loan.
- Loan information will be available from a variety of lenders and at www.SBA.gov.

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All of the foregoing is subject to the promulgation of implementing regulations for the CARES Act as well as further guidance from the federal government, lenders and other institutions and agencies. We recommend that you consult your attorneys and advisers for further advice and counsel.