HINSHAW

# Alerts

## A Summary of PPP Updates, Including Early Filing of Forgiveness Application

**July 13, 2020**
*Hinshaw Alert*

The U.S. Treasury and the SBA released two Paycheck Protection Program (PPP) Interim Final Rules on June 17, 2020 and June 22, 2020. A summary of the key points of these rules follows below.

### Early Filing of the Forgiveness Application

The June 22 Rule provides that a borrower may submit a loan forgiveness application at any time **on or before** the maturity date of the loan, **including before the end of the Covered Period**. The agencies cautioned that if the borrower applies for forgiveness before the end of the Covered Period and has reduced any employee's salaries or wages in excess of 25%, the borrower must account for that excess salary reduction for the entire eight or 24 week Covered Period.

To illustrate this issue, the agencies provided the following examples:

> **Example:** A borrower is using a 24-week Covered Period. This borrower reduced a full-time employee's weekly salary from $1,000 per week during the reference period to $700 per week during the Covered Period. The employee continued to work on a full-time basis during the Covered Period, with an FTE of 1.0. In this case, the first $250 (25% of $1,000) is exempted from the loan forgiveness reduction. The borrower seeking forgiveness would list $1,200 as the salary/hourly wage reduction for that employee (the extra $50 weekly reduction multiplied by 24 weeks).
>
> If the borrower applies for forgiveness before the end of the Covered Period, it must account for the salary reduction for the full 24-week Covered Period (totaling $1,200) even if it restores the salary at a later date.
>
> **Example:** A borrower that received a PPP loan before June 5, 2020 has elected to use an eight-week Covered Period. This borrower reduced a full-time employee's weekly salary from $1,000 per week during the reference period to $700 per week during the Covered Period. The employee continued to work on a full-time basis during the Covered Period, with an FTE of 1.0. In this case, the first $250 (25% of $1,000) is exempted from the loan forgiveness reduction.

### Attorneys

Timothy M. Sullivan

### Service Areas

Business & Commercial Transactions

The borrower seeking forgiveness would list $400 as the salary/hourly wage reduction for that employee (the extra $50 weekly reduction multiplied by eight weeks).

## 60/40 Split

The June 17 Rule confirms one of the legislative fixes adopted on June 5. It provides that at least 60% of the PPP loan proceeds must be used for payroll costs instead of 75%, as was noted under the previous Rule.

## Covered Period

Certain provisions regarding the forgiveness of PPP loans are limited to the "Covered Period." The term "Covered Period" was originally defined as the eight-week period beginning on the date of the disbursement of a PPP loan. However, a legislative fix extended the length of the Covered Period from eight weeks to 24 for all PPP loans made after June 5, 2020.

Borrowers who received PPP loans before June 5, 2020 have been given the option to either use the original eight-week Covered Period or elect to use the 24-week period.

With the creation of the 24-week Covered Period, the Covered Period of any borrower using the extended Covered Period will end no later than December 31, 2020.

These three changes were confirmed by the June 17 Rule.

## Extended Loan Term

PPP loans issued before June 5, 2020, have a two-year term. A legislative fix provides that all PPP loans issued after June 5, 2020 will have a five-year loan term. In addition, the legislation alters the term for loans prior to June 5, 2020, allowing them to be extended to five years if the lender and borrower agree.

The June 17 Rule confirmed these legislative changes.

## Permitted Payroll Expenses

Additionally, the June 17 Rule confirmed that the amount of loan forgiveness can be up to the full principal amount of the loan plus accrued interest. Under the 24 week (or eight week) Covered Period, the actual amount of loan forgiveness will depend on the total amount spent over the Covered Period on permitted payroll expenses, beginning on the date the PPP loan is disbursed as follows:

- Payroll costs including salary, wages, and tips, up to $100,000 of annualized pay per employee (for 24 weeks, a maximum of $46,154 per individual, or for eight weeks, a maximum of $15,385 per individual), as well as covered benefits for employees (but not owners), including health care expenses, retirement contributions, and state taxes imposed on employee payroll paid by the employer (such as unemployment insurance premiums).
- Owner compensation is calculated based on 2019 net profit as described in the PPP rules, with forgiveness of such amounts limited to eight weeks' worth (8/52) of 2019 net profit (up to $15,385) for an eight-week Covered Period or 2.5 months' worth (2.5/12) of 2019 net profit (up to $20,833) for a 24-week Covered Period, but excluding any qualified sick leave equivalent amount for which a credit is claimed under section 7002 of the Families First Coronavirus Response Act (FFCRA) or qualified family leave equivalent amount for which a credit is claimed under section 7004 of FFCRA.

The June 22 Rule restated the payroll compensation rules for owner, employers, and self-employed individuals providing the following with respect to owner-employee compensation:

- C-corporation owner-employees are capped by the amount of their 2019 employee cash compensation and employer retirement and health insurance contributions made on their behalf.

- S-corporation owner-employees are capped by the amount of their 2019 employee cash compensation and employer retirement contributions made on their behalf, but employer health insurance contributions made on their behalf cannot be separately added because those payments are already included in their employee cash compensation.
- Schedule C or F filers 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.
- Retirement and health insurance contributions are included in the net self-employment income of self-employed individuals, including Schedule C or F filers and general partners, and therefore cannot be separately added to their payroll calculation.

## Permitted Non-Payroll Expenses

Under the 24 week (or eight week) Covered Period, the actual amount of loan forgiveness will depend on the total amount spent over this period, beginning on the date the PPP loan is disbursed on permitted payroll expenses discussed above and the following permitted non-payroll expenses:

- payments of interest on mortgage obligations on real or personal property incurred before February 15, 2020, to the extent they are deductible on Form 1040 Schedule C;
- rent payments on lease agreements in force before February 15, 2020, to the extent they are deductible on Form 1040 Schedule C; and
- utility payments under service agreements dated before February 15, 2020 to the extent they are deductible on Form 1040 Schedule C.

As stated previously, a nonpayroll cost is eligible for forgiveness if it was:

- paid during the Covered Period; or
- incurred during the Covered Period and paid on or before the next regular billing date, even if the billing date is after the Covered Period.

Permitted non-payroll expenses may not exceed 40% of the amount to be forgiven.

## FTE Reductions from Forgiveness Amount

In calculating the loan forgiveness amount, a borrower must review the possible decreases in the amount to be forgiven based on its FTE headcount. The June 22 Rule reviewed three provisions that would eliminate decreases in the amount to be forgiveness due to reductions in FTE headcount.

1. A borrower may exclude any reduction in FTE headcount that is attributable to an individual employee if:

- The borrower made a good faith, written offer to restore the reduced hours of such employee;
- 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 reduction in hours;
- the offer was rejected by such employee; and
- the borrower has maintained records documenting the offer and its rejection.

2. Borrowers are exempted from loan forgiveness reduction arising from a proportional reduction in FTE headcount during the Covered Period if the borrower, in good faith, is able to document:

- An inability to rehire individuals who were employees of the borrower on February 15, 2020; and

- an inability to hire similarly qualified individuals for unfilled positions on or before December 31, 2020.

Borrowers are required to inform the applicable state unemployment insurance office of any offer rejected by an employee within 30 days of the employee's rejection of the offer.

Borrowers should maintain documents to illustrate their compliance with this exemption. Documentation could include the written offer to rehire an individual, a written record of the offer's rejection, or a written record of efforts to hire a similarly qualified individual.

3. A borrower is also exempted from the loan forgiveness reduction arising from a reduction in the FTE headcount during the Covered Period if the borrower, in good faith, is able to document an inability to (1) return to the same level of business activity as the borrower was operating at before February 15, 2020 and (2) that this inability was due to compliance with requirements established or guidance related to the maintenance of standards for sanitation, social distancing—or any other worker or customer safety requirement concerning COVID-19 (COVID Requirements or Guidance)—issued between March 1, 2020 and December 31, 2020 by the:

- Secretary of Health and Human Services;
- Director of the Centers for Disease Control and Prevention (CDC); or
- the Occupational Safety and Health Administration (OSHA).

If a borrower can certify that it has documented in good faith that its reduction in business activity during the Covered Period stems directly or indirectly from compliance with such COVID Requirements or Guidance, it will be exempt from any reduction in its forgiveness amount stemming from a reduction in FTE headcount during the Covered Period. Such documentation must include copies of applicable COVID Requirements or Guidance for each business location and relevant borrower financial records.

The agencies offered the following example:

> **Example:** A PPP borrower is in the business of selling beauty products both online and at its physical store. During the Covered Period, the local government where the borrower's store is located orders all non-essential businesses, including the borrower's business, to shut down their stores, based in part on COVID-19 guidance issued by the CDC in March 2020. Because the borrower's business activity during the Covered Period was reduced compared to its activity before February 15, 2020 due to compliance with COVID Requirements or Guidance, the borrower satisfies the exemption and will not have its forgiveness amount reduced because of a reduction in FTEs during the Covered Period.