

SBA RELEASES PPP LOAN FORGIVENESS APPLICATION AND INSTRUCTIONS



On May 15, 2020, the SBA and U.S. Department of the Treasury finally released the much anticipated **PPP Loan Forgiveness Application and Instructions**. As expected, it provides, "to apply for forgiveness of your PPP loan, you (the Borrower) must complete this application as directed in the instructions, and submit it to your Lender (or the Lender that is servicing your loan)." Clearly, all PPP borrowers who wish to have some or all of their PPP loan forgiven should review this carefully now to ensure their use of PPP loan funds is in accordance with the rules to the greatest extent possible.



The Loan Forgiveness Application and Instructions provide additional clarification and guidance (some positive and some negative) on several (but not all of the many) issues regarding PPP loan forgiveness. Initially, we note the following key provisions:

- **Covered Period:** The 8 week (56 day) forgiveness period, or "Covered Period", begins with the PPP Loan Disbursement Date. "For example, if the Borrower received its PPP loan proceeds on Monday, April 20, the first day of the Covered Period is April 20 and the last day of the Covered Period is Sunday, June 14." Unfortunately, the SBA did not extend the Covered Period to 12 weeks or allow it to begin when the borrower was permitted to re-open for business under the applicable state Governor's "Stay Home" or lockdown order(s), as had been requested and rumored.
- **Alternative Payroll Covered Period:** Here, the SBA provided some helpful flexibility to coordinate the Covered Period with the borrower's payroll period. "For administrative convenience, Borrowers with a biweekly (or more frequent [i.e., not bi-monthly or monthly]) payroll schedule may elect to calculate eligible payroll costs [*but not "eligible nonpayroll costs"*] using the eight-week (56-day) period that begins on the first day of their first pay period following their PPP Loan Disbursement Date (the "Alternative Payroll Covered Period"). For example, if the Borrower received its PPP loan proceeds on Monday, April 20, and the first day of its first pay period following its PPP loan disbursement is Sunday, April 26, the first day of the Alternative Payroll Covered Period is April 26 and the last day of the Alternative Payroll Covered Period is Saturday, June 20. Borrowers who elect to use the Alternative Payroll Covered Period must apply the Alternative Payroll Covered Period wherever there is a reference in this application to "the Covered Period or the Alternative Payroll Covered Period." However, Borrowers must apply the Covered Period (not the Alternative Payroll Covered Period) wherever there is a reference in this application to "the Covered Period" only."
- **Use of Cash Method or Accrual Method Permitted:** By providing the following definitions of "eligible payroll costs" and "eligible nonpayroll costs" as the two categories of expenditures for which PPP loan funds can be forgiven, the SBA effectively confirmed that the borrower may use either the cash method or accrual method of accounting for forgiveness, but (obviously) **not both to the effect that costs are counted twice.**
- **Eligible payroll costs.** "Borrowers are generally eligible for forgiveness for the payroll costs paid and payroll costs incurred during the eight-week (56-day) Covered Period (or Alternative Payroll Covered Period) ("payroll costs"). Payroll costs are considered paid on the day that paychecks are distributed or the Borrower originates an ACH credit transaction. Payroll costs are considered incurred on the day that the employee's pay is earned. **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 paid on or before the next regular payroll date.** Otherwise, payroll costs must be paid during the Covered Period

(or Alternative Payroll Covered Period). For each individual employee, the total amount of cash compensation eligible for forgiveness may not exceed an annual salary of \$100,000, as prorated for the covered period. Count payroll costs that were both paid and incurred only once."

- **Eligible nonpayroll costs.** "An eligible nonpayroll cost [i.e., business rent or lease payments*, business mortgage interest, and utilities as discussed in our previous memos], must be 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. Eligible nonpayroll costs cannot exceed 25% of the total forgiveness amount. Count nonpayroll costs that were both paid and incurred only once." *Note, the SBA has now clarified that covered **business lease payments include real or personal property** (e.g. leased equipment).
- **FTE Headcount Reduction Test:** Here, the SBA added some helpful, though not always positive, clarification. The borrower's forgiveness amount may be **reduced proportionally if ". . . the Borrower's average weekly number of FTE employees [defined below*] during the Covered Period or the Alternative Payroll Covered Period was less than during the Borrower's chosen reference period [February 15, 2019 to June 30, 2019, or January 1, 2020 to February 29, 2020]"**. However, the SBA has now fortunately provided both **an exception** for some headcount reductions, as promised in FAQ #40, **and a safe harbor exemption**, as referenced in the CARES Act itself, for the Test:
 - **FTE Reduction Exceptions.** The following FTE headcount reductions are not counted in the Test and, thus, **do not reduce the Borrower's loan forgiveness: "(1) any positions for which the Borrower made a good-faith, written offer to rehire an employee during the Covered Period or the Alternative Payroll Covered Period which was rejected by the employee; and (2) any employees who during the Covered Period or the Alternative Payroll Covered Period (a) were fired for cause, (b) voluntarily resigned, or (c) voluntarily requested and received a reduction of their hours.**
 - **FTE Reduction Safe Harbor.** "The Borrower is **exempt from the reduction** in loan forgiveness based on FTE employees described above **if both** of the following conditions are met: **(1) the Borrower reduced its FTE employee levels in the period beginning February 15, 2020, and ending April 26, 2020; and (2) the Borrower then restored its FTE employee levels by not later than June 30, 2020 to its FTE employee levels in the Borrower's pay period that included February 15, 2020.**" Note, the specific dates that apply to the borrower's reductions and the requirement for borrower to "restore" by June 30 its full FTE headcount as of February 15.
- ***An FTE (full time equivalency) employee** is an individual who is paid for (not necessarily works) 40 or more hours per week. Those who are paid for less must be combined to total 1 FTE employee in the count (e.g., 1 employee paid for 35 hours and 1 paid for 15 hours, equals a FTE). The SBA has also now helpfully indicated, "a simplified method that assigns a 1.0 for employees who work 40 hours or more per week and 0.5 for employees who work fewer hours may be used at the election of the Borrower."
- **Additional Cap on Owner Compensation:** As discussed in our previous memos, the borrower may not use PPP loan funds to pay any person more than \$100,000 annualized, or \$15,385 during the applicable Covered Period. The Forgiveness Application and Instructions confirm that the use of PPP loan funds to pay ". . . **owner-employees, a self-employed individual, or general partners**" is capped at \$15,385 ". . . **or the eight-week equivalent of their applicable compensation in 2019, whichever is lower.**"
- **At least 75% Payroll Costs Test:** Fortunately, despite the SBA's unclear earlier guidance, the Application and Instructions effectively indicate that the requirement to spend at least 75% on

"payroll costs" (for forgiveness purposes) applies to determine "whether **at least 75% of the potential forgiveness amount was used for payroll costs**" during the applicable Covered Period; **not 75% of the total PPP loan proceeds**. That is **good news** for any borrower than spends less than its total PPP loan proceeds on the applicable Covered Period and has PPP money left over. However, unlike it did with the FTE Headcount Reduction Test, the SBA **didn't make an exception** to the 75% Test for "payroll costs" not paid to employees who rejected re-hire, were terminated for cause, quit or requested a cut in hours.

Finally, it is important to remember that PPP loan funds which are not forgiven, including all PPP loan funds which are not spent during/for the applicable Covered Period, will simply remain part of the borrower's outstanding PPP loan on a 2 year term, at 1% interest, deferred for 6 months, with no personal guarantee or pre-payment penalty. Failure to satisfy any forgiveness rule or test, **does not** constitute, in and of itself, an improper use of PPP loan funds or subject the borrower to any penalties.

This memo is intended only as a summary and general overview. If you have any questions or would like legal advice regarding the above or any other employment issue, please contact [David Lawrence](#) or [Sarah Gidley](#).