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SBA Releases PPP Loan Forgiveness Application – Major Changes in Loan Forgiveness!

Updated May 26, 2020 to include SBA May 22, 2020 Loan Forgiveness and Loan Review Procedure Regulations

On Friday, May 15, 2020, the SBA released its Paycheck Protection Program ("PPP") Loan Forgiveness Application and detailed instructions (the "Application") that must be completed by borrowers and submitted to their lenders in order to obtain forgiveness. The Application provides greater clarity about what payments can be forgiven, provides more flexibility regarding costs, and reduces borrower compliance requirements, simplifying the process for borrowers. The SBA issued Interim Final Regulations on Loan Forgiveness and on Loan Review Procedures on May 22, 2020 (the "May 22 Interim Final Regulations") to further assist borrowers as they complete their Applications and to provide lenders with guidance on their forgiveness responsibilities. The regulations closely track the Application. This article includes the information from the May 22 Interim Final Regulations as well as the Application. This article provides changes to and further information on PBPA's Loan Forgiveness article.

Four Main Changes/Clarifications regarding Loan Forgiveness

The application lays out four main changes to or clarifications of the information regarding loan forgiveness in the CARES Act, the SBA/Treasury interim regulations and the FAQs.

1. ***Payroll Costs can be based on "Covered Period" or "Alternative Covered Period"***

The CARES Act, SBA/Treasury interim regulations and FAQs stated that the Covered Period begins the date the borrower first receives its loan money and lasts for eight weeks (56-days). One issue this raised is whether a borrower must change its payroll process to make sure it incurs and pays its payroll to match the eight-week period. The Application now allows borrowers with a biweekly (or more frequent) payroll cycle to elect to calculate payroll costs using the eight-week period that begins on the first day of their first pay period immediately after the borrower receives the loan money (the "Alternate Payroll Covered Period"). The Application has the following example:

> If a 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."

This Alternative Payroll Covered Period ONLY applies to payroll costs. Unless the Application specifically states that Borrower can use the Alternative Payroll Covered Period in calculating costs, Borrower should only use Covered Period costs.

2. ***Eligible Costs for Forgiveness Changes from Incurred <u>and</u> Paid to Incurred <u>or</u> Paid***

The CARES Act specifically stated that only "costs incurred and paid" during the Covered Period would be forgivable. The Application changes this complex requirement and makes it more manageable for borrowers. First, the Application clarifies that payroll costs paid during the Covered Period (or Alternative Payroll Covered Period) are eligible for forgiveness whether or not the costs were incurred during that period and that payroll costs are considered paid as "the day paychecks are distributed or the borrower originates an ACH credit transaction". Thus, if borrower chooses the Covered Period and if pay day is two days after the Covered Period begins, then it appears that the full amount of the gross pay for that pay day is included as eligible costs in the Covered Period.

In addition, the Application, which already offers the new Alternative Payroll Covered Period, states that any 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. Finally, the Application notes that all other payroll costs must be paid during either the Covered Period or Alternative Payroll Covered Period and that payroll costs that were both paid and incurred are only eligible once for forgiveness.

The Application also clarifies what is included for loan forgiveness regarding health insurance. Only the amount actually paid by the borrower during either the Covered Period or Alternative Payroll Covered Period (whichever borrower had chosen for payroll costs) for employer contributions for employee health insurance, including employer contributions to a self-insured, employer-sponsored group health plan but excluding any pre-tax or after tax contributions by employees, may be included in loan forgiveness.

Non-payroll costs, including mortgage interest, rent obligations, utilities, and interest on other debt obligations[1], must be **either** paid **or** incurred during the eight-week Covered Period (Alternative Payroll Covered Period does NOT apply) and, if incurred, then paid on or before the next regular billing date (even if the billing date is after the Covered Period).

3. Full-Time Equivalency (FTE) Calculation & New Safe Harbors

As explained in PBPA's Loan Forgiveness article, loan forgiveness will be reduced if the average weekly FTEs during the eight-week Covered Period (or now the Alternative Payroll Covered Period depending upon which period borrower picks for payroll cost consideration) is lower than the lower of the average weekly FTEs during the period of either February 15, 2019 through June 30, 2019 or January 1, 2020 through February 29, 2020 (respectively, the "Reference Period").

The Application defines FTE. Borrowers calculate FTEs by entering for each employee the average number of hours paid per week during the Covered Period/Alternative Payroll Covered Period, dividing by 40, and rounding the total to the nearest tenth. The maximum for each employee is capped at 1.0. For example, an employee who works on average 30 hours in a week would be treated as 0.8 FTE. This contradicts the Affordable Care Act methodology which was the expected methodology that would be applied prior to the release of this Application and is described in the PBPA Loan Forgiveness article. In the May 22 Interim Final Regulations, Treasury and the SBA also provided another option for calculating FTEs when considering part-time employees. Borrowers may use the approach stated above or, for any part-time employees, borrowers may simply list each part-time employee as .5 FTE. Whichever approach a borrower chooses, it must use the same approach for both the Covered Period (or Alternative Payroll Covered Period) and the Reference Period borrower chose.

Consistent with previous regulations, safe harbors remain in place in which FTE reductions do NOT reduce loan forgiveness. Those safe harbors were described in PBPA's Loan Forgiveness article, but the Application adds several new safe harbors. Specifically, any employees who (a) were fired for cause, (b) voluntarily resigned, or (c) voluntarily requested and received a reduction of their hours during the Covered Period/Alternative Payroll Covered Period will not cause a loan forgiveness reduction.

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[1] Note, the Application does not define rent or utilities, but it does note that interest on personal property (such as a company car loan) is included in nonpayroll costs that can be forgiven.

Borrower should document all of these events in writing and keep this information for six years in case of audit.

4. Calculation of Wage Reduction Affecting Forgiveness & New Safe Harbor

As a reminder, loan forgiveness will be reduced if salaries/wages were reduced by more than 25% during the Covered Period/Alternative Payroll Covered Period. The Application provides a clear method for calculating salary/wage reductions in order to determine loan forgiveness reduction. Salary/wage is analyzed separately for each employee.

The first step is to determine if each employee's pay was reduced by more than 25%. The Application's Schedule A Worksheet provides a step-by-step process for calculating each employee's salary/wage reduction. The calculation compares the average annual salary/wage by employee during the Covered Period/Alternative Payroll Covered Period to the average annual salary/wage during the period from January 1, 2020 through March 31, 2020[2]. If the difference is greater than 25%, then the worksheet asks whether a safe harbor applies for each employee. The Schedule A Worksheet does not require that this calculation be done for employees normally paid over $100,000 annually as their salaries/wages must be reduced in order to obtain forgiveness.

PBPA's Loan Forgiveness article describes most of the safe harbors. The Application adds an additional safe harbor: If a salary/wage reduction in excess of 25% occurs for an employee, loan forgiveness will not be affected if the borrower eliminates the reduction by June 30, 2020. Thus, if an employee's average annual salary/wages as of June 30, 2020 is equal to or greater than the annual salary/wages as of February 15, 2020, then no reduction to forgiveness will apply.[3]

If no safe harbor applies for an employee, borrower's loan forgiveness will be reduced by the amount of each employee's salary/wage reduction beyond the 25% reduction.

Other Important Aspects of the Application

- There is a specific box that must be checked by borrowers that receive loans in excess of $2 million dollars.
- The Application makes it clear that the SBA will deduct EIDL Advance amounts from the forgiveness amount remitted to the Lender. In fact, the form asks specifically for the amount of any EIDL Advance.

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[2] This is a change from the SBA interim regulations which had the period from January 1, 2020 – February 29, 2020.
[3] However, note the requirement that 75% of loan funds must be spent on payroll costs may not be met if the employee is not paid his or her average salary/wages received in 2019.

- The Application includes specific certifications such as how the dollar amount of forgiveness was spent, that if the monies were used for unauthorized purposes various consequences could occur, and that the borrower has accurately verified the payments for the eligible payroll and nonpayroll costs for which the borrower is requesting forgiveness. See the Application for the full list of certifications.
- The SBA may direct a lender to disapprove a borrower's loan forgiveness application if the SBA determines that the Borrower was ineligible for the PPP loan.

Application Form & Instructions

The Application includes two required parts that must be submitted to the lender (1) the PPP Loan Forgiveness Calculation Form and (2) the PPP Schedule A. The Application also includes a Schedule A Worksheet that must be used in order to complete Schedule A. The Calculation Form, Schedule A and the Schedule A Worksheet along with the instructions for each provide step-by-step instructions for how to perform the calculations for PPP loan forgiveness. The Application includes an optional demographic information form.

Finally, the Application clearly identifies what documentation must be submitted with PPP Schedule A and what documents must be maintained by the borrower in its files for six years in case of audit.

Loan Forgiveness Process

Once a borrower submits its Application and all supporting documentation, the borrower's lender or the lender servicing the loan must make a decision regarding loan forgiveness and submit it to the SBA within 60 days. The SBA then has 90 days to review and may: (a) provide the money to the lender or(b) tell the lender how much will be forgiven (if not the full amount or even any amount) and either ask the lender to obtain additional information from the borrower or reach out directly to the borrower for additional information. Failure to respond to SBA's inquiry may result in a determination that the borrower was ineligible to receive the loan amount or loan forgiveness amount claimed by the borrower. The SBA will consider the additional information provided and make a final determination. There will be an appeals process established in future regulations should loan forgiveness be denied.

If you have additional questions about loan forgiveness, contact your attorney or accountant.