

# Back to Business

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## Latest Guidance on Paycheck Protection Program Loan Forgiveness

The Small Business Administration (the SBA) recently provided additional guidance related to the forgiveness of loans under the Paycheck Protection Program (PPP). On May 15, 2020, the SBA released the PPP [Loan Forgiveness Application](#) (the Application) for borrowers to submit to their respective lenders in order to request forgiveness of all or part of their PPP loans, and on May 22, 2020, the SBA posted two Interim Final Rules, one of which relates to the loan forgiveness calculations (the Forgiveness IFR) and the other regarding SBA loan review procedures (the Review IFR).

The Application, the Forgiveness IFR and the Review IFR clarified which payments are eligible for forgiveness, how reduction to forgiveness works and certain aspects of the loan forgiveness process.

Additional information on PPP loan forgiveness can be found in our previous [alert](#) on the Coronavirus Aid, Relief and Economic Security Act (the CARES Act) and our [FAQ](#) on the PPP (the FAQ).

### Payments Eligible for Loan Forgiveness

#### Eligible Payroll Costs

Generally, a borrower is eligible to receive loan forgiveness for amounts spent on eligible expenses during the eight weeks following disbursement of its PPP loan (the Covered Period). Yet, for payroll costs (as defined in the [FAQ](#)) only, borrowers may elect to calculate eligible payroll costs using the:

1. Covered Period; or
2. Eight week period beginning on the first day of the borrower's first pay period following disbursement of the loan (the Alternative Payroll Covered Period).

### The Bottom Line

The SBA released long awaited guidance on calculating PPP loan forgiveness and the related steps involved in the forgiveness application process.

While the guidance does not answer every question, after reviewing the new guidance, borrowers will be in a much better position to make decisions related to their uses of loan proceeds.

The Davis & Gilbert team will continue to monitor SBA guidance regarding PPP loan forgiveness and provide updates as additional information becomes available.

Borrowers are eligible to receive loan forgiveness for payroll costs paid and payroll costs incurred during the Covered Period or the Alternative Payroll Covered Period. Payroll costs are considered paid when paychecks are distributed or when the borrower originates an Automated Clearing House (ACH) credit transaction. Payroll costs are considered incurred (i) when the employee earns the compensation or (ii) with respect to employees who remain on the borrower's payroll but who are not performing work, based on a schedule established by the borrower, which schedule is generally each day that the employee would have performed work.

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 such payments are paid on or before the borrower's next regular payroll date.

The Application and the Forgiveness IFR also provide helpful guidance as to what amounts should be included in payroll costs. For any owner-employee (or self-employed individual or general partner), the forgiveness amount for owner compensation may not include an amount in excess of eight weeks' worth of his or her 2019 compensation, capped at \$15,385 per individual, and no additional forgiveness will be provided for retirement or health insurance contributions for these individuals.

Additionally, for each individual employee, the total amount of cash compensation eligible for forgiveness cannot exceed \$15,385. While unclear from the original definition of "payroll costs" included in the CARES Act, the Forgiveness IFR indicated that payments of salary, wages and commissions for furloughed employees, hazard pay and bonuses are all considered payroll costs eligible for forgiveness.

## Eligible Non-Payroll Costs

The following are non-payroll costs eligible for forgiveness, to the extent they are paid during the Covered Period or incurred during the Covered Period (and paid on or before the borrower's next regular billing date, even if such date is after the Covered Period):

- >> Payments of interest (not including any prepayment of interest and not payment of principal) on any business mortgage obligation on real or personal property incurred before February 15, 2020;
- >> Business rent or lease payments pursuant to lease agreements for real or personal property in force before February 15, 2020; and
- >> Business payments for a service for the distribution of electricity, gas, water, transportation, telephone or internet access for which service began before February 15, 2020.

Eligible non-payroll costs cannot exceed 25% of the total forgiveness amount.



## Reductions to the Total Forgiveness Amount

Pursuant to the Application, the maximum amount of loan forgiveness a borrower is eligible to receive is the lowest of the:

1. Full loan amount,
2. Eligible payroll costs paid or incurred by the borrower during the Covered Period (or Alternative Payroll Covered Period) divided by 0.75, and
3. Sum of the borrower's eligible payroll costs and eligible non-payroll costs, minus any reductions based on reductions in salary or wages and the number of the borrower's full-time equivalent (FTE) employees, as explained below.

## Reductions Based on Reductions to Employee Salary or Wages

The Application clarifies that a borrower's total forgiveness amount will be reduced first, dollar for dollar to the extent that the total salary or wages of any employee is reduced during the Covered Period (or Alternative Payroll Covered Period) by more than 25% relative to the period beginning January 1, 2020 and ending March 31, 2020 (other than compensation reductions to an employee who received, during any pay period in 2019, wages or salary at an annualized rate in excess of \$100,000) (the Salary Reduction Rule). The Forgiveness IFR clarified that the Salary Reduction Rule applies only to the portion of the decline in an employee's salary or wages that is not attributable to the FTE reduction (i.e. a reduction in hours). This note ensures that borrowers are not doubly penalized for a reduction in an employee's hours.

## Reductions Based on Reductions in FTE Employees

According to the Application, after the borrower's forgiveness amount is reduced due to the Salary Reduction Rule, it will be reduced further by the percentage reduction in FTE employees during the Covered Period (or Alternative Payroll Covered Period) as compared to the reference period (the FTE Reduction Rule). For the reference period, the borrower is entitled to select either the period between February 15, 2019 and June 30, 2019 or January 1, 2020 and February 29, 2020.

A 40-hour work week should be used to calculate the average number of FTE employees for purposes of determining whether there has been a reduction in FTE employees.

This calculation can be done by:

- >> Dividing the average number of hours worked by each employee per week by 40 and aggregating the quotients (provided that each individual employee's quotient is capped at 1.0); or



- >> Attributing a 1.0 to each employee working 40 hours or more and 0.5 to each employee working less than 40 hours (the Alternative FTE Calculation Method).

The Forgiveness IFR notes that whichever method a borrower opts to use must be used consistently for both the Covered Period (or Alternative Payroll Covered Period) and the selected reference period.

## Exceptions to the Salary Reduction Rule and FTE Reduction Rule

In the three circumstances below, a borrower's forgiveness amount will not be reduced despite a reduction in employee salary or wages and/or FTE employees (the Safe Harbors).

The forgiveness amount will not be reduced:

- >> If an employee was fired for cause, voluntarily resigned or voluntarily requested and received a reduction in his or her hours.
- >> If the borrower has terminated an employee or reduced an employee's hours, the borrower makes a good faith offer, in writing, to rehire the employee or restore the reduced hours and the employee rejects the offer. In order to take advantage of this Safe Harbor, the borrower must maintain written records of the employee's rejection of the offer and inform the applicable state unemployment insurance office of the employee's rejection of the offer within 30 days. Additionally, the offer must be for the same salary or wages and same number of hours earned or worked, as applicable, in the last pay period prior to the termination of the employment relationship or reduction in hours.
- >> If the borrower reduced its FTE employee levels, employee salary or wages in the period from February 15, 2020 through April 26, 2020 and the borrower subsequently restored its FTE employee levels or employee salary or wages, as applicable, by June 30, 2020 to the FTE employee levels or salary levels from the pay period that included February 15, 2020. Neither the Application nor the Forgiveness IFR states how long following June 30, 2020 the borrower must maintain the higher FTE employee levels or salaries.

## Process to Receive Loan Forgiveness

To receive loan forgiveness, a borrower needs to submit its Application to its lender. The borrower is also required to submit detailed documentation to verify payroll, headcount and non-payroll expenses including, but not limited to, bank account statements, tax forms, invoices, account statements and receipts (the Supporting Documents). The Application also requires the borrower to make additional certifications, including that the tax documents that the borrower submits to its lender are consistent with those that it has submitted (or plans to submit) to the IRS and/or the state tax or workforce agencies.



Once submitted, the lender has 60 days to review the Application and issue a decision to the SBA. The lender will review the Application and assess the borrower's eligibility for loan forgiveness in accordance with the PPP regulations and guidance issued by the SBA through the date of the borrower's application.

If, in its review, the lender determines that the borrower miscalculated its forgiveness amount or that the Supporting Documents do not provide adequate support for the calculation, the lender must work with the borrower to attempt to remedy any defects.

In issuing its decision, the lender will request that the SBA make a payment of the forgiveness amount and notify the borrower of the lender's decision. If a borrower disagrees with a lender's decision regarding the amount of forgiveness it is entitled to receive, within 30 days after receiving the decision, the borrower can request that the SBA review the lender's determination.

## SBA's Review of Loan Forgiveness Applications

Upon receipt of a decision from the lender, the SBA has an additional 90 days to review the applicable Application and Supporting Documents and remit payment of the forgiveness amount (plus any accrued interest) to the lender. The SBA may further reduce the forgiveness amount based on the results of its review of the Application and the Supporting Documentation. Any amounts not forgiven must be paid by the borrower before the two-year maturity date.

The SBA has indicated that it maintains the discretion to review Applications for loans of any size and that it will review for both calculation of loan forgiveness as well as a borrower's eligibility for a PPP loan. If the SBA challenges a borrower's forgiveness calculation, the borrower will have an opportunity to provide additional information for the SBA's consideration and/or answer the SBA's questions. If the SBA determines that the borrower was not eligible for a PPP loan, the borrower will be ineligible for forgiveness. In these circumstances, the SBA may also request repayment of the loan, in addition to pursuing other remedies.

The SBA previously provided limited guidance on its review of eligibility, but that guidance was limited to the required certification concerning the necessity of the loan request (See Question B.5 of the [FAQ](#)). In the Review IFR, the SBA has indicated that it may still review loan applications for eligibility beyond the "necessity certification." In the Review IFR, the SBA indicated that if a borrower who was ineligible for a PPP loan fails to repay its loan, the SBA will have recourse against individual shareholders, members or partners of the borrower.

Any borrower may challenge an adverse determination from the SBA regarding the amount of loan forgiveness the borrower is entitled to receive. The SBA indicated that additional information is forthcoming regarding this process.



## For More Information

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Please contact the attorneys listed below or the D&G attorney with whom you have regular contact.

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