

SBA Issues Interim Final Rule on PPP Loan Forgiveness

By Peter E. Cooper

INTRODUCTION

On Friday, May 15, 2020, the Small Business Administration began outlining the process for obtaining forgiveness of loans issued pursuant to the Payroll Protection Program, when it issued SBA Form 3508, entitled "Paycheck Protection Program Loan Forgiveness Application" ("Forgiveness Application"). The 11-page document sets forth information and documentation required to obtain loan forgiveness, and begins to answer some (but not all) of the questions raised by the text of the CARES Act.¹

A week later, on Friday, May 22, 2020, the SBA expanded its guidance on loan forgiveness when it posted its Interim Final Rule on Paycheck Protection Program – Requirements – Loan Forgiveness ("Loan Forgiveness IFR"). The Loan Forgiveness IFR largely echoes the language of the Forgiveness Application and illuminates some of the Forgiveness Application's provisions. It also provides greater clarity as to the loan forgiveness process itself, the expenses that will be eligible for forgiveness and how forgiveness will be calculated, and the application for forgiveness reduction provisions.

THE LOAN FORGIVENESS PROCESS

The Loan Forgiveness IFR identifies the three participants in the loan forgiveness process and their respective roles: the borrower, the lender and the SBA.

Borrower's responsibilities: To receive loan forgiveness, a borrower must complete and submit the Forgiveness Application (SBA Form 3508 or lender equivalent) to its lender (or the lender servicing its loan). This includes:

- the PPP loan forgiveness calculation form ("Forgiveness Calculation");
- PPP Schedule A, including instructions;
- PPP schedule A Worksheet, including instructions; and
- the (optional) PPP borrower demographic information form.

A borrower also will need to submit substantial additional documentation concerning payroll costs, nonpayroll costs, and employment statistics as part of the forgiveness package.²

Lender's Responsibilities: As a general matter, a lender has 60 days from receipt of a completed Forgiveness Application and documentation to issue a decision on whether a loan qualifies for

¹ Please review our prior article, [SBA Releases Loan Forgiveness Application and Provides Guidance on PPP Loan Forgiveness](#), for a discussion of the Forgiveness Application.

² In addition, a borrower must retain other documentation, including documentation concerning borrowers' eligibility, for six years after repayment or forgiveness of the PPP loan.

forgiveness. If the lender determines that the borrower is entitled to forgiveness of some or all of the amount applied for under the statute and applicable regulations, the lender must request payment from SBA at the time the lender issues its decision to SBA. After the SBA's review, the lender is responsible for notifying the borrower of the forgiveness amount. If only a portion of the loan is forgiven, or if the forgiveness request is denied, any remaining balance due on the loan must be repaid by the borrower on or before the two-year maturity of the loan.

SBA's Responsibilities: The SBA will, subject to any SBA review of the loan or loan application, remit the appropriate forgiveness amount to the lender, plus any interest accrued through the date of payment, no later than 90 days after the lender issues its decision to SBA. If SBA determines in the course of its review that the borrower was ineligible for the PPP loan based on the provisions of the CARES Act, SBA rules or guidance available at the time of the borrower's loan application, or the terms of the borrower's PPP loan application (for example, because the borrower lacked an adequate basis for the certifications that it made in its PPP loan application), the loan will be deemed ineligible for loan forgiveness.

Every borrower should take particular notice of the timeline set forth above. The Loan Forgiveness IFR anticipates that the loan forgiveness process will take up to 150 days (approximately five months) from submission of the Forgiveness Application and documentation, which can be submitted, at earliest seven weeks after loan funding. Thus, a borrower likely will have to begin repaying its loan under the terms of the PPP loan promissory note before it ever receives loan forgiveness, even if such forgiveness is granted in full. While the borrower will be entitled to a rebate of any excess payments, it must expect to begin paying the loan after expiration of the six-month deferral period.

PAYROLL COSTS ELIGIBLE FOR LOAN FORGIVENESS

Covered Period: In general, payroll costs paid or incurred during the eight-week (56-day) "covered period" are eligible for forgiveness. Borrowers may seek forgiveness for payroll costs for the eight weeks beginning on either:

- i. the date of disbursement of the borrower's PPP loan proceeds from the lender (*i.e.*, the start of the covered period); or
- ii. the first day of the first payroll cycle in the covered period (the "alternative payroll covered period").

Payroll costs are deemed "incurred" on the day the employee's pay is earned (*i.e.*, on the day the employee worked) and "paid" on the day that paychecks are distributed or the borrower originates an ACH credit transaction. Generally, payroll costs incurred during the borrower's last pay period of the covered period or the alternative payroll covered period are eligible for forgiveness if paid on or before the next regular payroll date. Thus, if payroll costs are incurred during the eight-week alternative payroll covered period, but paid after the end of the alternative payroll covered period, such payroll costs will be eligible for forgiveness if they are paid no later than the first regular payroll date thereafter.

Bonuses and Hazard Pay and Payments to Furloughed Employees: Subject to the \$100,000 cap on annualized wage compensation, an employee's hazard pay and bonuses are eligible for loan forgiveness because such pay constitutes a supplement to salary or wages. Likewise, payments of salary, wages, or commissions to a furloughed employee during the covered period are eligible for

forgiveness, as long as they do not exceed an annual salary of \$100,000, as prorated for the covered period. An employee does not actually have to perform work to have the employee's wages counted as a forgivable payroll cost.

Limits on Compensation for Owner-Employees and Self-Employed Individuals: An owner-employee or self-employed individual may request loan forgiveness in an amount that is the lesser of (i) 8/52 of 2019 compensation or (ii) \$15,385 per individual in total across all businesses. An owner-employee's eligible compensation is capped by the amount of the employee's 2019 cash compensation and employer retirement and health care contributions made on the employee's behalf. Schedule C filers are capped by the amount of their owner compensation replacement, which is 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.

NONPAYROLL COSTS ELIGIBLE FOR LOAN FORGIVENESS

Eligible Costs Paid *or* Incurred: The striking distinction between the treatment of payroll costs and nonpayroll costs for eligibility purposes is the use of the conjunction "or." While payroll costs must be incurred and paid during the covered period, in general, nonpayroll costs must be incurred or paid during the relevant period.

The Loan Forgiveness IFR states, a nonpayroll cost is eligible for forgiveness if it was:

- i. paid during the covered period; or
- ii. 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.

The Loan Forgiveness IFR offers the example of a borrower with a covered period between June 1 and July 26, 2020. The borrower may seek forgiveness for the amount of electricity bills paid during that eight-week period, even though those bills included electricity usage before the covered period. The borrower may also seek forgiveness for the portion of an electricity bill paid after the covered period for the usage portion during the covered period. Thus, in the example, a borrower could seek forgiveness of the portion of the bill for usage through July 26th, even though the bill was not paid until August—a date outside of the covered period.

REDUCTIONS TO LOAN FORGIVENESS AMOUNT

Section 1106(d) provides for reduction of loan forgiveness based upon a reduction of staff and reduction of salary paid to an employee. The Loan Forgiveness IFR clarifies some of the directions given in Forgiveness Application.

Treatment of Employees Who Decline Offers of Rehire: Under §1106(d)(2), loan forgiveness of a PPP loan is to be reduced in proportion to the amount by which a borrower reduced employment during the covered period as compared to the chosen "reference period" (generally either February 15, 2019 to June 30, 2019, or January 1, 2020 to February 29, 2020). The actual loan forgiveness that the borrower will receive may be reduced if the borrower's average number of FTE employees during the covered period is less than the number of FTE employees during the borrower's chosen reference period.

The Forgiveness Application provides that loan forgiveness will not be reduced by FTE reductions with respect to any positions for which the Borrower made a good-faith, written offer to rehire an employee

during the covered period that was rejected by the employee. The Loan Forgiveness IFR now adds three additional steps to this “credit”:

- i. the rehire 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;
- ii. the borrower must maintain records documenting the offer and its rejection; and
- iii. the borrower must inform the applicable state unemployment insurance office of such employee’s rejected offer of reemployment within 30 days of the employee’s rejection of the offer.

In this regard, the Loan Forgiveness IFR echoes the warning contained in FAQ No. 40, published by the SBA on May 3, 2020, which states: ***“Employees and employers should be aware that employees who reject offers of re-employment may forfeit eligibility for continued unemployment compensation.”***

Harmonization of Reductions in the Number of FTE and Reductions Relating to Salary and Wages: As noted above, CARES Act §1106(d)(2) reduces loan forgiveness of a PPP loan in proportion to the amount a borrower reduces FTE during the relevant period. Likewise, CARES Act §1106(d)(4) provides for reduction in loan forgiveness based upon the reduction in employee wage compensation in excess of 25 percent of the total salary or wages for an individual employee during the comparison period.

A problem arises, however, where a borrower reduces an employee’s hours, thereby resulting in a decrease in an employee’s wages as well. For example, if an hourly employee working 40 hours per week saw her hours reduced by half, the change in status would see her FTE reduced from 1.0 to 0.5, and her wages also reduced by half. To ensure that borrowers are not doubly penalized, the Loan Forgiveness IFR holds that the salary/wage reduction applies only to the portion of the decline in employee salary and wages that is *not* attributable to the FTE reduction. While a borrower would be required to include the reduction in FTE in its calculation of FTE Reduction Quotient in the Forgiveness Application, it would not have to consider the wage reduction for that same employee as part of its calculation of the Salary/Hourly Wage Reduction in that same document.

CONCLUSION

The SBA continues to refine its interpretation and guidance with respect to the PPP program. Rarely, if ever, have we seen such dynamic and radical evolution in regulation and rule-making over such a short period of time. Borrowers must continue to monitor the SBA and Department of Treasury websites to follow changes and developments in clarification and administration of the PPP. What is clear is that PPP loan forgiveness may not turn out to be as quick or straightforward as the CARES Act seemed to promise.

Forgiveness Application: <https://home.treasury.gov/system/files/136/3245-0407-SBA-Form-3508-PPP-Forgiveness-Application.pdf>

PPP Loan Frequently-Asked Questions:

<https://home.treasury.gov/system/files/136/Paycheck-Protection-Program-Frequently-Asked-Questions.pdf>

If you have questions about SBA PPP Loan Forgiveness, please contact your Lawrence Kamin attorney.

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