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SBA issues interim final rule on PPP loan forgiveness and unveils loan forgiveness application

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When Congress passed the CARES Act, many businesses were excited about the Paycheck Protection Program ("PPP") and its promise of loan forgiveness. But, as companies received PPP loans and began using the proceeds, questions abound about how to use such funds and qualify for forgiveness. The Small Business Administration ("SBA")—the agency tasked with administering the program—was required to issue guidance and regulations implementing the loan forgiveness portion of the PPP program. On May 15th and May 22nd, the SBA provided some clarity on outstanding questions as it released the PPP forgiveness application (the "Forgiveness Application") and its Interim Final Rule on PPP loan forgiveness (the "Forgiveness IFR").[1] Several of the key highlights included in the Forgiveness IFR and Forgiveness Application are outlined below.[2] Note, however, that additional developments are still possible when Congress reconvenes June 1 as competing Senate and House proposals to amend PPP forgiveness criteria have been drafted and likely will be considered.

Hazard pay and bonuses are eligible for forgiveness

One of the more welcome pieces of news in the Forgiveness IFR is that the SBA has clarified that bonuses and hazard pay are within the definition of covered "payroll costs" eligible for loan forgiveness. This means that employers that might otherwise struggle to meet the 75% payroll cost threshold have the option of temporarily increasing employee pay and have such increase still "count" toward their forgiveness amount. Employers that wish to offer hazard pay or to make bonus payments need to be mindful, however, of the $100,000 cap on salary/wages eligible for

[1] SBA has issued many Interim Final Rules for PPP and this one is distinguished by Docket Number SBA-2020-0032, issued on SBA's website on May 20, 2020. As of May 28, 2020, the official *Federal Register* notice has not yet been posted. Please note, that on May 20 the SBA also issued another Interim Final Rule, SBA-2020-0033, which speaks to related points about processing and reviews and makes clear that, regardless of a safe harbor, applications will be reviewed as part of the forgiveness process and SBA reserves all discretion to conduct any other review it believes necessary.

[2] For a summary of the PPP loan program, see our prior alert, "SBA issues interim final rule clarifying changes to PPP loans for eligible businesses."

forgiveness. In other words, to the extent a bonus or hazard pay would result in annualized salary/wages in excess of $100,000, that portion of the payment that brings the employee's salary/wages above $100,000 on an annualized basis will not be eligible for forgiveness as a covered payroll cost.

The Forgiveness IFR also confirms that salary, wages, or commissions made to furloughed employees can also be included in "payroll costs" even though those employees were not performing any services for the employer.

From "paid *and* incurred" to "paid *or* incurred" — maybe

The Forgiveness IFR provides, in part, that otherwise covered costs are eligible for forgiveness if they were "paid *or* incurred" during the applicable period. This could be significant, even though at another point the IFR refers to paid and incurred. At the least, SBA is using this variation to provide some additional flexibility in covered time periods.

For purposes of covered nonpayroll costs, the Forgiveness IFR explains that under this rule a covered nonpayroll cost is eligible for forgiveness if it was either (i) "paid" during the eight-week period starting on the date the loan was funded or (ii) "incurred" during the eight-week period starting on the date the loan was funded *and paid on or before the next regular billing date* (even if that date is after the eight-week covered loan period). This allows practical flexibility on the time limits for the eight-week period, making that eight-week period more flexible but only as long as the cost is paid shortly thereafter during the billing cycle that is typical for that cost. This means that, for example, a borrower whose eight-week loan period begins on June 1 and ends on July 26 and who pays its May and June electricity bill during the covered period and pays it July electricity bill in August (on or prior to the next billing date) can include the May and June electricity payments in its forgiveness application as well as that portion of the July electricity payment attributable to the period July 1 through July 26.

With respect to covered payroll costs, the Forgiveness IFR provides that payroll costs are eligible for forgiveness if they were paid or incurred during either the "covered period" or the "alternative covered period." Like with nonpayroll costs, the "covered period" is the eight-week period beginning on the first day of the first payroll cycle in the covered period. The "alternative covered period" is a new concept added by the Forgiveness IFR to ease administrative burdens by allowing certain borrowers to use, at their option, the eight-week period beginning on the first day of the first payroll cycle in the covered period for purposes of calculating payroll costs without splitting pay periods. To use the "alternative covered period" to calculate payroll costs, however, a borrower must operate on a bi-weekly (i.e., every other week) or more frequent payroll cycle in order to be eligible to use this new method (semi-monthly or monthly payroll periods are not eligible). Borrowers should calculate their covered payroll costs using both the "covered period" method and the "alternative covered period" method because in some instances one method may result in higher payroll costs being eligible for forgiveness than under the other method.

Clarity on the headcount reduction penalty and how certain employment decisions affect loan forgiveness

The Forgiveness IFR also explains how borrowers are to calculate their full-time equivalent ("FTE") employee count for purposes of determining whether they are subject to a reduction in the amount eligible for forgiveness under the FTE reduction penalty.

As a rule, employees who worked 40 hours or more in a week are assigned an FTE score of 1.0. For employees who worked less than 40 hours in a week, a borrower may use one of two methods for counting employees: (i) divide the actual number of hours worked by 40; or (ii) assign each employee with less than 40 hours worked in a week an FTE score of 0.5. Whichever method the borrower chooses to use, it must use that method to calculate its FTE employee-count during the covered period (or the alternative covered period, as the case may be) and for calculating its FTE employee-count during the prior "reference period" (which, at the borrower's option, may be the period February 15, 2019, through June 30, 2019, or January 1, 2020, through February 29, 2020[3]).

To calculate whether the FTE reduction penalty applies, the Forgiveness IFR explains that a borrower must first calculate the average FTE count during the "covered period" or the "alternative covered period."

For the purposes of this calculation, the Forgiveness IFR states that where an employee is fired for cause, voluntarily resigns, or voluntarily requests a reduced schedule during the relevant period, the borrower may count that employee at the same FTE score before the FTE reduction event. Moreover, loan forgiveness will not be reduced if the borrower laid-off or reduced the hours of an employee, then offered to rehire or restore the employee's hours, but the employee declined the offer. Note that the offer to re-hire or restore must be made in writing, and that the employer is required to document the employee's rejection of the offer in writing as well. Further, the borrower is required to "inform[] the applicable state unemployment insurance office" of the employee's rejected offer within 30 days.

Next, the borrower must calculate its average FTE count during the borrower's selected "reference period." Because the borrower can select from multiple available reference periods and use the period that produces the lower FTE score, borrowers should calculate their FTE score for all available periods. Finally, the borrower must divide the average FTE count during the covered period/alternative covered period by the average FTE count in the selected reference period. If the result is one or greater, the FTE reduction penalty does not apply. If the result is less than one, the borrower must multiple the result by the amount it would otherwise be entitled to have forgiven to arrive at its discounted forgiveness amount.

Borrowers will not be double penalized where reduction in FTE count results in lower employee pay

Another piece of welcome news from the Forgiveness IFR relates to the interplay between the FTE reduction and the salary/wage reduction penalties. Under the salary/wage reduction penalty, the borrower must reduce the total forgiveness amount by the total dollar amount of a salary or wage reduction in excess of 25 percent of the base salary or wages between January 1, 2020, and March 31, 2020, of each new employee in 2020 and each existing employee who earned less than the annualized equivalent of $100,000 in any pay period in 2019. However, the Forgiveness IFR clarifies that this reduction only applies to the portion of the decline in an employee's salary/wages that is not attributable to a reduction in the employee's FTE count. In other words, a borrower will not be double penalized where an employee works less and therefore makes less money than they

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[3] Seasonal employers may use either of these reference periods or a consecutive 12-week period between May 1, 2019, and September 15, 2019.

otherwise would have during the covered/alternative covered period if not for the reduction in hours.

Documenting forgivable expenses

The Forgiveness IFR provides that there are certain documents that a borrower must retain in connection with its application for loan forgiveness, but that the borrower is not required, initially, to submit to its lender. Those documents are set forth in the Forgiveness Application and include:

- Documentation supporting the listing of each individual employee in the Forgiveness Application, including the "Salary/Hourly Wage Reduction" calculation, if necessary;
- Documentation supporting the listing of each individual employee in the Forgiveness Application that received during any single pay period in 2019 compensation at an annualized rate of more than $100,000;
- Documentation regarding any employee job offers and refusals, firings for cause, voluntary resignations, and written requests by an employee for reductions in work schedule; and
- Documentation supporting the borrower's entitlement, if any, to the "FTE Reduction Safe Harbor."

The Forgiveness Application also provides that all of the documents listed above, as well as any others submitted with the original loan application and those that support the borrower's eligibility for a PPP loan, must be retained for six years after the date the loan is forgiven or repaid in full.

Still not the final word?

Finally, even at this late date, both Senate and House lawmakers are circulating competing bills proposing a variety of additional changes to the PPP's forgiveness provisions including possible extension of the eight-week period for the use of loan funds, elimination of the 75% payroll cost threshold, and expanding or clarifying permitted uses of PPP loan funds. Votes on those proposals are possible as early as June 1, so even this latest Forgiveness IFR and Forgiveness Application may not be the final word. We are monitoring these bills and will update this alert to report any material developments.

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