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PPP Loan Forgiveness June 24, 2020

Paycheck Protection Program Summary

Any business, nonprofit organization, veterans' organization, or Tribal business, which meets certain requirements qualify for loans up to $10 million under the Paycheck Protection Loan Program ("PPP").

PPP Loan funds can be used for payroll costs; cost related to the continuation of group health care benefits during periods of paid sick, medical, or family leave, and insurance premiums; interest payments on any mortgage; rent and utility payments; and interest payments on any other debt obligations that were incurred before February 15, 2020.

The CARES Act and related guidance provided the ability to get the whole loan or a portion of the loan forgiven if certain rules were followed. The Paycheck Protection Program Flexibility Act of 2020 ("PPPFA") was signed into law on June 5th. The PPPFA modified and amended certain provisions of the Cares Act. We are uncertain how the passing of the PPPFA will affect the guidance that was published pre-PPPFA. We expect that further guidance from the SBA will be required to reconcile the difference between the CARES Act and the PPPFA.

Loan Forgiveness

Loan Forgiveness Application

Two PPP Loan Forgiveness Applications have been published. Both are shorter than the original 11 page document. There is a 5 page Loan Forgiveness Application document that will be required of many businesses.

There is also a 3 page EZ Loan Forgiveness Application document that is available for the following types of businesses:

1. Self-employed, independent contractors, or sole proprietors with no employees;

2. Borrowers who did not reduce salaries by more than 25% during the Covered Period and did not reduce the number of employees or the average paid hours of employees from January 1, 2020 to the end of the Covered Period (ignoring reductions from the safe harbor related to an inability to hire qualified employees, and reductions due to an employee refusing to accept a restoration of hours); and

3. Borrowers who did not reduce salaries by more than 25% during the Covered Period and was unable to operate during the Covered Period at the same level of business activity due to COVID-19 related safety requirements promulgated by the CDC, HHS, or OSHA.

Loan Forgiveness Application Timing

A borrower may submit a loan forgiveness application any time on or before the maturity date of the loan – including before the end of the covered period – if the borrower has used all of the loan proceeds for which the borrower is requesting forgiveness. If the borrower applies for forgiveness before the end of the covered period and has reduced any employee's salaries or wages in excess of 25 percent, the borrower must account for the excess salary reduction for the full 8-week or 24-week covered period. In effect, borrowers that apply early for loan forgiveness forfeit a safe-harbor provision allowing them to restore salaries or wages by Dec. 31 and avoid reductions in the loan forgiveness they receive (the guidance does not address the FTE safe harbor).

If the borrower does not apply for loan forgiveness within 10 months after the last day of the covered period, or if SBA determines that the loan is not eligible for forgiveness (in whole or in part), the PPP loan is no longer deferred and the borrower must begin paying principal and interest. If this occurs, the lender must notify the borrower of the date the first payment is due. The lender must report that the loan is no longer deferred to SBA on the next monthly SBA Form 1502 report filed by the lender.

Covered Period

The loan may be forgiven to the extent certain Payroll and Nonpayroll Costs are incurred and paid during the Covered Period. The Covered Period begins on the date the lender makes the first disbursement of the PPP loan to the borrower. The CARES Act originally set forth the Covered Period as an 8 week period. The PPPFA and related guidance sets forth the Covered Period as a period ending on the earlier of the 24 weeks after the loan disbursement date or December 31, 2020. Generally, the lender must make the first disbursement of the loan no later than ten calendar days from the date of loan approval. If a borrower has already received a loan before June 5th, 2020, that borrower can choose to maintain the original 8 week Covered Period under the CARES Act or select the 24 week Covered Period provided in the PPPFA.

An Alternative Payroll Covered Period was also established. For administrative convenience, Borrowers with a biweekly (or more frequent) payroll schedule may elect to calculate eligible payroll costs using an Alternative Covered Period that begins on the first day of their first pay period following their PPP Loan Disbursement Date (the "Alternative Payroll Covered Period").

Payroll Costs

Payroll Costs consist of compensation to employees (whose principal place of residence is the United States) in the form of salary, wages, commissions, or similar compensation; cash tips or the equivalent (based on employer records of past tips or, in the absence of such records, a reasonable, good-faith employer estimate of such tips); payment for vacation, parental, family, medical, or sick leave; allowance for separation or dismissal; payment for the provision of employee benefits consisting of group health care coverage, including insurance premiums, and retirement; payment of state and local taxes assessed on compensation of employees; and for an independent contractor or sole proprietor, wages, commissions, income, or net earnings from self-employment, or similar compensation.

If a borrower pays furloughed employees their salary, wages, or commissions during the covered period, those payments are eligible for forgiveness as Payroll Costs as long as they do not exceed an annual salary of $100,000, as prorated for the covered period. Amounts paid to employees for hazard pay and bonuses are eligible for loan forgiveness as Payroll Costs, if an employee's total compensation does not exceed $100,000 on an annualized basis.

The PPPFA guidance states that you should not include more than $46,154 in cash compensation for any individual employee. You can add to cash compensation for employees covered benefits for employees (but not owners), including health care expenses, retirement contributions, and state taxes imposed on employee payroll paid by the employer (such as unemployment insurance premiums).

The PPPFA and related guidance sets forth limitations on owner compensation. For borrowers who elect to use an 8 week covered period, the amount of loan forgiveness requested for owner-employees and self-employed individuals' payroll compensation is capped at eight weeks' worth (8/52) of 2019 compensation (i.e., approximately 15.38 percent of 2019 compensation) or $15,385 per individual, whichever is less, in total across all businesses. For borrowers who elect to use a 24 week covered period, the amount of loan forgiveness requested for owner-employees and self-employed individuals' payroll compensation is capped at 2.5 months' worth (2.5/12) of 2019 compensation (i.e., approximately 20.83 percent of 2019 compensation) or $20,833 per individual, whichever is less, in total across all businesses.

C-corporation owner-employees are capped by the amount of their 2019 employee cash compensation and employer retirement and health insurance contributions made on their behalf. S-corporation owner-employees are capped by the amount of their 2019 employee cash compensation and employer retirement contributions made on their behalf, but employer health insurance contributions made on their behalf can't be separately added.

Schedule C and F filers are capped by the amount of their owner compensation replacement, calculated based on 2019 net profit. The amount of loan forgiveness requested for schedule C and F filers can be no more than the lesser of eight weeks' worth (8/52) of 2019 net profit (up to $15,385) for an eight-week covered period or 2.5 months' worth (2.5/12) of 2019 net profit (up to $20,833) for a 24-week covered period.

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.

For self-employed individuals, including Schedule C or F filers and general partners, retirement and health insurance contributions are included in their net self-employment income and therefore cannot be separately added to their payroll calculation.

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). Count Payroll Costs that were both paid and incurred only once.

Nonpayroll Costs

Nonpayroll Costs eligible for forgiveness consist of: (a) covered mortgage obligations: payments of interest (not including any prepayment or payment of principal) on any business mortgage obligation on real or personal property incurred before February 15, 2020 ("business mortgage interest payments");

(b) covered rent obligations: business rent or lease payments pursuant to lease agreements for real or personal property in force before February 15, 2020 ("business rent or lease payments"); and (c) covered utility payments: 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 ("business utility payments").

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 PPPFA guidance provides that business mortgage payments, rent and utilities as listed on Form 1040 Schedule C are now included for forgiveness for owners in such a position.

Prepayments of interest on covered mortgage debt is not eligible for loan forgiveness.

<u>Reduction to Loan Forgiveness Amount Based on Payroll Costs</u>

At least 60 percent of the amount forgiven must be attributable to payroll costs. If a borrower uses less than 60% of the loan amount for payroll costs during the forgiveness covered period, the borrower will continue to be eligible for partial loan forgiveness, subject to at least 60% of the loan forgiveness amount having been used for payroll costs.

<u>Other Reductions to Loan Forgiveness Amount</u>

Prior to the PPPFA, a borrower had until June 30, 2020, to eliminate a reduction in employment, salary and wages that would otherwise reduce the forgivable amount of its PPP loan. The PPPFA changed that date to December 31, 2020. This is another example in which there is doubt as to whether this was intentional or unintentional. There is some thought that another bill will be passed that will change the date to August 31, 2020, but for now this is the rule.

There will be no further reduction to loan forgiveness if you meet the following standard:

1. If the reduction in the number of [full time equivalent] employees between February 15, 2020 and April 26, 2020 is completely eliminated by December 31, 2020. This is a simple quantitative test—the SBA will look at the number of employees on February 15 on a full time equivalent (FTE) basis and compare that number to the number of FT employees at December 31, 2020; or

2. If the salary or wages of one or more employees was reduced between February 15, 2020 and April 26, 2020, and the employer has subsequently restored pay by December 31, 2020.

Borrowers that apply early for loan forgiveness forfeit the safe-harbor provision above allowing them to restore salaries or wages by Dec. 31 and avoid reductions in the loan forgiveness they receive (Current guidance does not address calculating FTEs when a borrower files before the end of the covered period). For instance, if a borrower has a 24-week period that ends in November but wants to apply in September, any wage reduction in excess of 25% as of September would be calculated for the entire 24-week period even if the borrower restores salaries by Dec. 31.

> *Example*: A borrower is using a 24-week covered period. This borrower reduced a full-time employee's weekly salary from $1,000 per week during the reference period to $700 per week during the covered period. The employee continued to work on a full-time basis during the covered period, with an FTE of 1.0. In this case, the first $250 (25% of $1,000) is exempted from the loan forgiveness reduction. The borrower seeking forgiveness would list $1,200 as the salary/hourly wage reduction for that employee (the extra $50 weekly reduction multiplied by 24 weeks). If the borrower applies for forgiveness before the end of the covered period, it must account for the salary reduction for the full 24-week covered period (totaling $1,200).

The PPPFA provides that borrowers will not experience a reduction in their forgiveness amount due to a decline in the FTE employee count if the borrower, in good faith, is able to document:

> (A) (i) an inability to rehire individuals who were employees of the PPP borrower on February 15, 2020; and (ii) an inability to hire similarly qualified employees for unfilled positions on or before December 31, 2020; or
>
> (B) an inability to return to the same level of business activity as such business was operating at before February 15, 2020, due to compliance with requirements established or guidance issued by the Secretary of Health and Human Services, the Director of the Centers for Disease Control and Prevention, or the Occupational Safety and Health Administration during the period beginning on March 1, 2020, and ending December 31, 2020, related to the maintenance of standards for sanitation, social distancing, or any other worker or customer safety requirement related to COVID–19.

If the borrower does not meet the above safe harbor then the amount forgiven will be reduced proportionally by any reduction in the number of employees retained during the applicable period after receipt of the loan compared to one of two prior pay period time periods (described below) determined by the borrower and reduced by the reduction in pay of any employee beyond 25% of their prior year compensation.

Note: It is uncertain how the PPPFA will affect the following italicized previously released guidance, but the new guidance on this topic may mirror the guidance for those submitting loan forgiveness applications early.

The borrower must first select a reference period: (i) February 15, 2019 through June 30, 2019; (ii) January 1, 2020 through February 29, 2020; or (iii) in the case of a seasonal employer, either of the two preceding methods or a consecutive 12-week period between May 1, 2019 and September 15, 2019.

If the average number of FTE employees during the covered period or the alternative payroll covered period is less than during the reference period, the total eligible expenses available for forgiveness is reduced proportionally by the percentage reduction in FTE employees.

> *Example: if a borrower had 10.0 FTE employees during the reference period and this declined to 8.0 FTE employees during the covered period, the percentage of FTE employees declined by 20 percent and thus only 80 percent of otherwise eligible expenses are available for forgiveness.*

In calculating the loan forgiveness amount, if: i. the borrower made a good faith, written offer to rehire such employee (or, if applicable, restore the reduced hours of such employee) during the covered period or the alternative payroll covered period; ii. the 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; iii. the offer was rejected by such employee; iv. the borrower has maintained records documenting the offer and its rejection; and v. the borrower informed 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.

When an employee of the borrower is fired for cause, voluntarily resigns, or voluntarily requests a reduced schedule during the covered period or the alternative payroll covered period (FTE reduction event), a borrower may exclude any reduction in full-time equivalent employee headcount that is attributable to an individual employee.

Full-time equivalent employee means an employee who works 40 hours or more, on average, each week. The hours of employees who work less than 40 hours are calculated as proportions of a single full-time equivalent employee and aggregated.

Borrowers must divide the average number of hours paid for each employee per week by 40, capping this quotient at 1.0. For example, an employee who was paid 48 hours per week during the covered period would be considered to be an FTE employee of 1.0.

For employees who were paid for less than 40 hours per week, borrowers may choose to calculate the full-time equivalency in one of two ways:

1. The borrower may calculate the average number of hours a part-time employee was paid per week during the covered period.

   Example: if an employee was paid for 30 hours per week on average during the covered period, the employee could be considered to be an FTE employee of 0.75. Similarly, if an employee was paid for ten hours per week on average during the covered period, the employee could be considered to be an FTE employee of 0.25.

   Or,

2. For administrative convenience, borrowers may elect to use a full-time equivalency of 0.5 each part-time employee.

Borrowers may select only one of these two methods, and must apply that method consistently to all of their part-time employees for the covered period or the alternative payroll covered period and the selected reference period.

A reduction in an employee's salary or wages in excess of 25 percent will generally result in a reduction in the loan forgiveness amount. For each new employee in 2020 and each existing employee who was not paid more than the annualized equivalent of $100,000 in any pay period in 2019, the borrower must reduce the total forgiveness amount by the total dollar amount of the salary or wage reductions that are *in excess of 25 percent of base salary or wages between January 1, 2020 and March 31, 2020 (the reference period).This reduction calculation is performed on a per employee basis, not in the aggregate.*

> *<u>Example</u>: A borrower reduced a full-time employee's weekly salary from $1,000 per week during the reference period to $700 per week during the covered period. The employee continued to work on a full-time basis during the covered period with an FTE of 1.0. In this case, the first $250 (25 percent of $1,000) is exempted from the reduction. Borrowers seeking forgiveness would list $400 as the salary/hourly wage reduction for that employee (the extra $50 weekly reduction multiplied by eight weeks).*

Loan Forgiveness Process

The maximum loan forgiveness amount is capped at the loan principal plus accrued interest.

A borrower must complete and submit the Loan Forgiveness Application with documents required to be submitted as detailed in the Loan Forgiveness Application to its lender (or the lender servicing its loan). As a general matter, the lender will review the application and make a decision regarding loan forgiveness. The lender has 60 days from receipt of a complete application to issue a decision to SBA. The SBA will render its decision 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 not be eligible for loan forgiveness.

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.

The general loan forgiveness process described above applies only to Loan Forgiveness Applications that are not reviewed by SBA prior to the lender's decision on the forgiveness application. In a separate interim final rule on SBA Loan Review Procedures and Related Borrower and Lender Responsibilities, SBA will describe its procedures for reviewing PPP loan applications and Loan Forgiveness Applications.

Change to Loan Terms

The PPPFA extends the maturity date to at least a minimum of 5 years for PPP loans disbursed on or after June 5th, 2020. For PPP loans disbursed prior to June 5th, 2020, the PPPFA permits borrowers and lenders to mutually agree and modify the existing maturity terms to conform with the new minimum of 5 years maturity for any remaining outstanding balance of a PPP loan after determination of forgiveness.

The PPPFA extends the deferral period from 6 months to the "date on which the amount of forgiveness determined under Section 1106 of the CARES Act is remitted by the lender". The PPPFA further provides that a borrower that fails to apply for forgiveness within 10 months after the last day of the 24-week forgiveness period must begin making principal and interest payments on that date.

Disclaimer: CBIZ MHM, LLC is not a law firm and is not providing legal advice. If you have any questions regarding how the new COVID-19 legislation or any other legislation applies to you or your business, please contact your legal counsel.