



The Wait Is (Mostly) Over: SBA Releases Paycheck Protection Program Forgiveness Application

Insights

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The Small Business Administration finally released its much anticipated forgiveness application for borrowers who received a Paycheck Protection Program (PPP) loan. It has been nearly two months since the program was signed into law and, since that time, lenders and borrowers alike have been anxiously awaiting for the PPP merry-go-round to stop and for the Treasury Department or the SBA to provide clear direction to achieve loan forgiveness. And while some questions regarding forgiveness remain, the 11-page forgiveness application provides favorable guidance to borrowers to maximize their PPP loan forgiveness.

Flexibility For Payroll Periods, Costs Incurred, And Costs Paid

The forgiveness application's most significant development is what the SBA has dubbed the "Alternative Payroll Covered Period," which permits the borrower to align the eight-week/56-day covered period with the borrower's regular payroll schedule, rather than starting the clock on the day the loan was funded. Available to employers with a bi-weekly (or more frequent) payroll schedule, this is welcome news as many employers were grappling with how to account for wages earned and paid within the eight-week period. Now, borrowers may elect to start the eight-week clock – only for purposes of paying "payroll costs" – on the first day of the employer's regular pay period following the date on which the employer received the loan disbursement.

The SBA also clarified what the "costs incurred and payments made" language from § 1106 of the CARES Act really means with an interpretation that is generous to borrowers, both in terms of payroll costs and non-payroll costs. First, the application makes clear that, to be forgivable, at least 75% of the funds spent during the Covered Period (or Alternative Payroll Covered Period, if applicable) must be spent on payroll costs, and no more than 25% of the funds may be spent on non-payroll costs.

Payroll costs are paid on the day that paychecks are distributed, or the borrower initiates an ACH credit transaction. Payroll costs are incurred on the day the employee's pay is earned. Importantly, 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. Borrowers may only count the costs once, either when the cost is paid or incurred.

For eligible non-payroll costs, these must be paid during the Covered Period or 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. This means that borrowers can include more rental, utility, and interest payments (including those payments that have accumulated and remained unpaid due to the pandemic), so long as the expense was in place as of February 15, 2020, it is not a prepayment, and it does not exceed the 25% threshold.

Forgiveness Calculation

The application is consistent with the CARES Act in that, to maximize loan forgiveness, borrowers must maintain headcount and wages over the eight-week Covered Period. Headcount is determined by the employer's Full-Time Equivalent Employees (FTEs).

The CARES Act did not define FTE and it was assumed that because the CARES Act also referenced the Affordable Care Act, FTE had the same definition, and was based on a 30-hour workweek. But for the purposes of PPP forgiveness according to the application, FTEs are calculated during the Covered Period or the Alternative Payroll Covered Period.

Thus, for each employee, enter the average number of hours paid per week, divide by 40, and round the total to the nearest tenth. The maximum for each employee is capped at 1.0. A simplified method that assigns a 1.0 for employees who work 40 hours or more per week and 0.5 for employees who work fewer hours may be used at the election of the Borrower. For some borrowers, dividing the average number of hours paid per week by 40 may result in a higher FTE count which the borrower may want to maximize forgiveness. FTEs are calculated on a weekly basis.

The application requires borrowers to track, on a per-employee basis, the average wages each employee earned over the Covered Period. The CARES Act set limitations on the maximum amount that each employee may receive from PPP funds over the Covered Period to be forgivable, specifying that PPP funds may not be used to compensate an employee for any amount in excess of \$100,000, as prorated over the eight weeks.

Salary Reductions

The application also addresses salary reductions. A borrower's forgiveness will be reduced if, during the eight-week period, any employee's wages were reduced by more than 25% compared to the average wages that employee earned January 1, 2020 through March 31, 2020.

This differs somewhat from the plain language of the CARES Act which states that the average wages in the eight-week period are compared to the wages earned "during the most recent full quarter during which the employee was employed before the covered period." Under the specific language of the CARES Act, employers who laid off employees during Q1 would need to look to the fourth quarter of 2019. The application forecloses that obligation and all employees' wages will be compared to the first quarter of 2020.

If wages are reduced, they are deducted on a dollar-for-dollar basis from a borrower's forgiveness amount. Until now, there was an open question as to whether the wage reduction penalty applied to employees who earned *more* than \$100,000 in 2019. The application, however, makes clear that the

wage reduction requirement applies only to those who earned less than \$100,000 and requires employers to separate into two different tables – Table 1 and Table 2.

Employees who earned less than or equal to \$100,000 for all pay periods in 2019 and employees who did not work for the employer in 2019 are listed in Table 1. Employees who earned more than \$100,000 for all pay periods in 2019 are included in Table 2. Importantly, the deduction of wages reduced from the total forgiveness amount is done *before* the FTE reduction is determined. This is a much more favorable forgiveness calculation for the borrower, as it results in a smaller reduction in the amount of forgiveness than determining the reduction based on FTEs first.

If a borrower's loan forgiveness eligibility is reduced based on the reduction of employees' wages, there is a safe harbor which would avoid the reduction altogether. This "safe harbor" varies from the plain language of the CARES Act, but to the benefit of employers.

To determine if the safe harbor applies, the employer must first look at what the employee was earning as of February 15, 2020, and then determine what the employee earned on average from February 15 through April 26, 2020. If the amount the employee earned on average between February 15 and April 26, 2020 is less than what the employee earned as of February 15, 2020, the employer then looks to the employee's average wage as of June 30, 2020. If, the employee earned on average, the same, or more on June 30, 2020, compared to what the employee earned as of February 15, 2020, the safe harbor applies. This means that for forgiveness purposes, a salary reduction during the 8-week period will not count against PPP loan forgiveness, so long as that salary is restored by June 30, 2020.

Full-Time Equivalent Employee (FTE) Reduction

Consistent with the Act, the application states that borrowers generally must maintain their average FTE count over the eight weeks following the loan disbursement, compared to one of two time periods, at a borrower's election:

- February 15, 2019 – June 30, 2019

OR

- January 1, 2020 – February 29, 2020
- (Or, for seasonal employers, any consecutive 12-week period between May 1 and September 15, 2019)

The FTE reduction is performed after the salary reduction referenced above. The average FTEs during the eight-week period is divided by the average FTEs in one of the two (or three, for seasonal employers) time periods referenced above, resulting in a quotient. The quotient is then multiplied times the total PPP loan amount eligible for forgiveness. The product results in the total amount of forgiveness.

However, this reduced amount is also eligible for safe harbor application. Like the safe harbor for wage reductions, the safe harbor for FTEs looks at two points in time – FTEs for the pay period including February 15, 2020 and the average FTEs from February 15, 2020 through April 26, 2020. If an employer had more FTEs on February 15, 2020 than the average FTEs between February 15, 2020 and April 26, 2020, so long as the employer restores the FTE count to what it was as of February 15, 2020, the safe harbor is met and the employer avoids a reduction in forgiveness based on FTEs within the eight-week period.

No Penalty For Employees Who Quit Or Refuse To Work

But what if an employer cannot maintain its FTE count due to circumstances beyond its control, such as a voluntary separation or a termination for cause? In any of the following circumstances, the employer will not be penalized for a reduction in FTEs:

- Employer makes a good-faith written offer to return to work, but employee refuses;
- Employee voluntarily quits;
- Employee is terminated for cause; or
- Employee voluntarily takes a reduction in hours.

This new guidance alleviates the need for an employer to backfill positions that were vacated due to no fault of the employer. It is recommended that all separations of employment should be well documented and all offers to return to work be in writing to the employee.

Borrower Certification

The SBA recently announced a safe harbor for those borrowers who received less than \$2 million in PPP funds, and after much back-and-forth on the certification for need for PPP loans, the application requires borrowers that, along with any affiliates, borrowed more than \$2 million to check a box on the application. Thus, the \$2 million-dollar threshold is likely to be viewed collectively with affiliates.

Thus, borrowers who have already returned a portion of their PPP loan to fall below the \$2 million threshold should not expect to escape forgiveness scrutiny and should prepare themselves for an audit. The same goes for borrowers that together with its affiliates received loans totaling \$2 million or more.

Additional Guidance Needed

Although the application undoubtedly answers more questions than any other single piece of guidance that has been released by either the Treasury or the SBA, questions remain unanswered. For example, the definition of the “transportation” utility is undefined. Is it permissible to pay employees not working if the business is shut down by a government order? Can businesses offer employee incentives to entice employees to return to work and will those incentives be forgiven? Can 2019 payments to pension funds count toward forgiveness? These questions and more will hopefully be addressed by additional guidance from the SBA and Treasury.

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Conclusion

Fisher Phillips' SBA Loan Team will continue to monitor the ever-changing COVID-19 situation and provide updates. Make sure you are subscribed to [Fisher Phillips' Alert System](#) to get the most up-to-date information.

For further information, contact your Fisher Phillips attorney, [or any member of our SBA Loan Task Force](#). You can also review our [FP BEYOND THE CURVE: Post-Pandemic Back-To-Business FAQs For Employers](#) and our [FP Resource Center For Employers](#).

This Legal Alert provides an overview of a specific developing situation. It is not intended to be, and should not be construed as, legal advice for any particular fact situation.

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