

LEGAL UPDATES

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## Service

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# FAQ: Paycheck Protection Program Forgiveness for Borrowers

On May 22, 2020 the SBA and Department of the Treasury released the long awaited Interim Final Rule on Forgiveness of Paycheck Protection Program (PPP) Loans and the Interim Final Rule on SBA Loan Review Procedures, both of which have been revised, in part, by an Interim Final Rule posted by the SBA on June 22, 2020. On June 5, 2020, the Paycheck Protection Program Flexibility Act (PPP Flexibility Act) of 2020 was signed into law. On June 16, 2020, the SBA published revisions to its Form 3508 Loan Forgiveness Application and separate Instructions (“Form 3508”), reflecting changes as a result of the PPP Flexibility Act. The SBA also released a new, shortened Form 3508EZ Loan Forgiveness Application and separate Instructions (“Form 3508EZ,” together with Form 3508, the “Forgiveness Applications”) for certain eligible borrowers. Most recently, on August 4, 2020, the SBA released separate FAQs on loan forgiveness.

For more information on the Paycheck Protection Program, the Economic Injury Disaster Loans (EIDL) and the Emergency Economic Injury Grants (EIDL Grants), please see the FAQ: CARES Act SBA Loan Programs.

### **PPP Loan Forgiveness Information**

Procedure – PPP Loan  
Forgiveness

Eligibility – PPP Loan  
Forgiveness

Reductions to Forgiveness  
Amount

## ***Procedure – PPP Loan Forgiveness***

### **Q: How do Borrowers apply for PPP loan forgiveness?**

A: Borrowers must complete, and submit to the Lender that provided the PPP loan, either the Form 3508 Loan Forgiveness Application or, if eligible, the Form 3508EZ Loan Forgiveness Application. Both the Form 3508 Loan Forgiveness Application Instructions and the Form 3508EZ EZ Loan Forgiveness Application Instructions itemize the documents that each Borrower must submit with its application, including specific payroll records and non-payroll costs documentation. There are also documents that Borrowers are required to maintain, but are not required to submit unless requested. Borrowers should begin collecting this required documentation. The SBA has indicated that it will begin accepting forgiveness applications from lenders on August 10, 2020.

### **Q: Which Forgiveness Application should a Borrower complete?**

A: A Borrower may apply for forgiveness using Form 3508EZ **if at least one of the following are true:**

1. The Borrower is a self-employed individual, independent contractor, or sole proprietor who had no employees at the time of the PPP loan application and did not include any employee salaries in the computation of average monthly payroll in the Borrower Application Form (SBA Form 2483).
2. The Borrower did not reduce annual salary or hourly wages of any employee by more than 25% during the Covered Period (defined herein) or the Alternative Payroll Covered Period (defined herein) compared to the period between January 1, 2020 and March 31, 2020 (for purposes of this statement, “employees” means only those employees that did not receive, during any single period during 2019, wages or salary at an annualized rate of pay in an amount more than \$100,000); AND The Borrower did not reduce the number of employees or the average paid hours of employees between January 1, 2020 and the end of the Covered Period. (Ignore reductions that arose from an inability to rehire individuals who were employees on February 15, 2020 if the Borrower was unable to hire similarly qualified employees for unfilled positions on or before December 31, 2020. Also ignore reductions in an employee’s hours that the Borrower offered to restore and the employee refused.)
3. The Borrower did not reduce annual salary or hourly wages of any employee by more than 25% during the Covered Period or the Alternative Payroll Covered Period compared to the period

between January 1, 2020 and March 31, 2020 (for purposes of this statement, “employees” means only those employees that did not receive, during any single period during 2019, wages or salary at an annualized rate of pay in an amount more than \$100,000); AND The Borrower was unable to operate during the Covered Period at the same level of business activity as before February 15, 2020, due to compliance with requirements established or guidance issued between March 1, 2020 and December 31, 2020 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, related to the maintenance of standards of sanitation, social distancing, or any other worker or customer safety requirement related to COVID-19.

If a Borrower cannot satisfy at least one of the above, then it cannot use Form 3508EZ, and instead must apply for forgiveness using Form 3508.

### **Q: Is there a due date for the Forgiveness Applications?**

A: As of the date of this publication, nothing in the Forgiveness Applications, the Interim Final Rules or the SBA FAQs requires the Borrower to apply for forgiveness. However, Borrowers should review the promissory notes and other loan documents that they executed in connection with the PPP loan, because Lenders may have included terms that require the Borrower to apply for forgiveness and to do so within a certain period of time.

A Borrower may submit a loan forgiveness application before the maturity date of the loan – including before the end of the Applicable Covered Period (defined herein) – if the Borrower has used all of the loan proceeds for which the Borrower is requesting forgiveness. However, it should be noted that if a borrower applies for forgiveness before the end of the Applicable Covered Period, and it has reduced certain employee’s salaries or wages in excess of 25%, the borrower must account for the excess salary reduction for the full 8-week or 24-week covered period.

If a Borrower submits a loan forgiveness application before the end of the Applicable Covered Period, or within 10 months after the end of its Applicable Covered Period, it will not have to make any payments of principal or interest on its loan before the date on which the SBA remits the loan forgiveness amount to the Lender (or notifies the Lender that no loan forgiveness is allowed). The Lender will notify the Borrower of the date that its first payment is due.

If a Borrower does not submit its loan forgiveness application within 10 months after the end of its Applicable Covered Period, or if the 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.

**Q: My Applicable Covered Period is 24-weeks. If I spend all of my PPP loan proceeds before the end of the 24-weeks (e.g., at the end of 16-weeks), do I have to wait until the end of the 24-weeks to submit my Forgiveness Application?**

A: No. A Borrower may submit a loan forgiveness application anytime on or before the maturity date of the loan – including before the end of the Applicable Covered Period – if the Borrower has used all of the loan proceeds for which the Borrower is requesting forgiveness.

However, if the Borrower applies for forgiveness before the end of the Applicable Covered Period, and has reduced certain employee's salaries or wages in excess of 25%, then the Borrower must account for the excess salary reduction for the full 8-week or 24-week covered period.

For 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 24-week covered period, it must account for the salary reduction for the full 24-week covered period (totaling \$1,200).

**Q: When will I know if I was approved for forgiveness?**

A: For loans not reviewed by the SBA, the forgiveness process could take up to 5 months. This time period could be even longer for loans reviewed by the SBA.

After a Borrower submits a complete Forgiveness Application to its Lender, the Lender has 60 days to review the application and submit its decision to the SBA. The Lender's decision may take the form of an approval, in whole or in part; a denial; or if directed by the SBA, a "denial without prejudice" due to a pending SBA review of the loan.

If the Lender determines that the Borrower is entitled to forgiveness of some or all of the amount applied for, the Lender must request payment from the SBA at the time the Lender issues its decision to the SBA. The SBA, subject to any SBA review of the loan or loan application, has up to 90 days to remit the appropriate forgiveness amount to the Lender. If applicable, the SBA will deduct any EIDL Grant previously received by the Borrower from the forgiveness amount remitted to the Lender. The Lender is responsible for notifying the Borrower of remittance by the SBA of the loan forgiveness amount (or that the SBA determined that no amount of the loan is eligible for forgiveness) and the date on which the Borrower's first payment is due, if applicable.

A Borrower may request that the SBA review a Lender's decision denying forgiveness within 30 days of receiving the denial notice from the Lender. The SBA may decline or accept the Borrower's request for review.

As indicated on the Forgiveness Applications, the audit threshold is based on whether the Borrower, together with its affiliates, received PPP loans with an original principal amount in excess of \$2 million. The SBA may also review a PPP loan of any size – regardless of whether a forgiveness application has been submitted – at any time in its discretion. If the SBA reviews a PPP Loan, the SBA will notify the Lender in writing and the Lender is required within five (5) business days to notify the Borrower in writing of receipt and to provide certain information to the SBA including the loan application, the forgiveness application, and all supporting documentation. If the SBA determines that a Borrower was ineligible for the PPP loan, was ineligible for the PPP loan amount obtained or for the loan forgiveness amount claimed, the SBA will direct the Lender to deny the loan forgiveness application in whole or in part, as appropriate. The SBA may also seek repayment of the outstanding PPP loan balance or pursue other available remedies.

The Borrower may appeal the SBA's determinations, and the SBA has indicated that it intends to issue a separate interim final rule addressing this appeal process. The interim final rule does not impose a time frame on the SBA for its review of any PPP loan.

**Q: If my Lender denies my Forgiveness Application, can I appeal the Lender's decision?**

A: Yes. If a Lender denies a Borrower's Forgiveness Application, the Lender must notify the Borrower in writing that it has issued a decision to the SBA denying the loan forgiveness application. Within 30 days of such notice from the Lender, the Borrower may notify the Lender that it is requesting that the SBA review the Lender's decision. Within 5 days of receipt, the Lender must notify the SBA of the Borrower's request for review. The SBA will notify the Lender if the SBA declines a request for review. If the Borrower does not request SBA review, or if the SBA declines the request for review, the Lender is responsible for notifying the Borrower of the date on which the Borrower's first payment is due. If the SBA accepts a Borrower's request for review, the SBA will notify the Borrower and the Lender of the results of its review. If the SBA denies forgiveness in whole or in part, the Lender is responsible for notifying the Borrower of the date on which the Borrower's first payment is due.

**Q: If the SBA determines that I was ineligible for the PPP loan, or was ineligible for the PPP loan amount obtained or for the loan forgiveness amount claimed, can I appeal the SBA's determination?**

A: Yes. The SBA published an Interim Final Rule addressing this appeal process. According to the Rule, SBA loan review decisions may be appealed to the Office of Hearings and Appeals. Such loan review decisions eligible for appeal include a determination by the SBA finding a borrower (1) was ineligible for a PPP loan; (2) was ineligible for the PPP loan amount received or used the PPP loan proceeds for unauthorized uses; (3) is ineligible for PPP loan forgiveness in the amount determined by the lender in its full or partial approval decision issued to SBA (except for the deduction of any Economic Injury Disaster Loan advance in accordance with section 1110(e)(6) of the CARES Act); and/or (4) is ineligible for PPP loan forgiveness in any amount when the lender has issued a full denial decision to SBA.

**Q: Will my Forgiveness Application be audited by the SBA?**

A: As indicated on the Loan Forgiveness Applications, the audit threshold is based on whether the Borrower, together with its affiliates, received PPP loans with an original principal amount in excess of \$2 million. The SBA may also review a PPP loan of any size – regardless of whether a forgiveness application has been submitted – at any time in its discretion. If the SBA reviews a PPP loan, the SBA will notify the Lender in writing and the Lender is required within five (5) business days to notify the Borrower in writing of receipt and to provide certain information to the SBA including the loan application, the forgiveness application, and all supporting documentation. The SBA may request additional information from the Borrower in connection with its audit. The Borrower will have the opportunity to respond to the SBA's questions in a review. The Borrower's failure to provide the information requested by the SBA may result in a determination that the Borrower was ineligible for the PPP loan or ineligible to receive the loan amount or loan forgiveness amount claimed by the Borrower. If the SBA determines that a Borrower was ineligible for the PPP loan, was ineligible for the PPP loan amount obtained or for the loan forgiveness amount claimed, the SBA will direct the Lender to deny the loan forgiveness application in whole or in part, as appropriate. The SBA may also seek repayment of the outstanding PPP loan balance or pursue other available remedies.

The Borrower may appeal the SBA's determinations, and the SBA has indicated that it intends to issue a separate interim final rule addressing this appeal process. The interim final rule does not impose a time frame on the SBA for its review of any PPP Loan.

An audit may even occur after the PPP loan is forgiven or is repaid in full. Borrowers are reminded that they are required to keep all documentation related to their PPP loan for six (6) years after the date of forgiveness or repayment.

\*The SBA has started circulating certain proposed PPP loan necessity questionnaires following a recent notice in the Federal Register. The forms are focused on PPP borrowers that, together with their affiliates, received PPP loans of \$2 million or more. For informational purposes, a draft of Form

3509 (for-profit entities) can be found here while Form 3510 (non-profit entities) can be found here. As of November 6, 2020, these forms have not been officially published on the SBA's or Treasury's websites.

**Q: What happens if only a portion of my PPP loan is forgiven, or if my Forgiveness Application is denied?**

A: If a Borrower is denied forgiveness in whole or in part, the amount of the loan not forgiven must be repaid by the Borrower on or before the Borrower's applicable maturity date (two years for those PPP loans "made" prior to June 5, 2020 and five years for those loans "made" on or after June 5, 2020). The SBA has indicated that, for PPP loans "made" prior to June 5, 2020, the Borrower and its Lender may mutually agree to extend the existing 2-year maturity out to 5 years. Additionally, the SBA has indicated that a PPP loan is considered to be "made" on the date that the SBA assigns a loan number to the PPP loan.

This applies only to loan forgiveness applications that are not reviewed by the SBA prior to the Lender's decision on the forgiveness application, meaning that – under certain circumstances – the SBA may impose additional or different repayment terms.

A Borrower should also review its promissory note and the other loan documentation it executed in connection with its PPP loan for any additional implications of a denial of forgiveness and specific repayment requirements.

If a Borrower submits a Forgiveness Application before the end of the Applicable Covered Period, or within 10 months after the end of its Applicable Covered Period, it will not have to make any payments of principal or interest on its loan before the date on which the SBA remits the loan forgiveness amount to the Lender (or notifies the Lender that no loan forgiveness is allowed). The Lender will notify the Borrower of the date that its first payment is due.

If a Borrower does not submit its loan forgiveness application within 10 months after the end of its Applicable Covered Period, or if the 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.

If the SBA determines that the Borrower is ineligible for the PPP loan or is ineligible for the loan amount or the loan forgiveness amount claimed by the Borrower, the SBA may pursue other available remedies.

**Q: A Lender may deny a Borrower's Forgiveness Application "without prejudice" – what does this mean?**

A: If, at the time a Borrower submits its Forgiveness Application, the SBA is already reviewing the Borrower's loan and loan application, then the SBA may direct the Lender to "deny without prejudice" the Borrower's forgiveness application. In the case of a "denial without prejudice" the Borrower may subsequently request that the Lender reconsider its application for loan forgiveness, unless the SBA has determined that the Borrower is ineligible for a PPP loan.

## ***Eligibility – PPP Loan Forgiveness***

[Back to the top](#)

### **Q: What amount of my PPP loan is eligible for forgiveness?**

A: A Borrower is eligible for forgiveness of part or all of its PPP loan, subject to adjustments and limitations, if proceeds are used for eligible purposes and the Borrower can provide the required supporting documentation to demonstrate that it qualifies for forgiveness.

Additionally, in order to be eligible for full forgiveness, a Borrower must use at least 60% of the PPP loan for payroll costs, and not more than 40% of the loan forgiveness amount may be attributable to nonpayroll costs. If a Borrower uses less than 60% of its PPP loan for payroll costs, it will not receive the full amount of loan forgiveness it might otherwise be eligible to receive. Instead, the Borrower will receive partial loan forgiveness, based on the requirement that 60% of the forgiveness amount must be attributable to payroll costs. For example, if a Borrower receives a \$100,000 PPP loan, and during the Applicable Covered Period the Borrower spends \$54,000 (or 54%) of its loan on payroll costs, then because the Borrower used less than 60% of its loan on payroll costs, the maximum amount of loan forgiveness the Borrower may receive is \$90,000 (\$54,000 divided by 60%). This \$90,000 is further broken down to \$54,000 in payroll costs (constituting 60% of the \$90,000 maximum forgiveness amount) and to \$36,000 in nonpayroll costs (constituting 40% of the \$90,000 maximum forgiveness amount).

### **Q: Which expenses from my PPP loan proceeds are eligible for forgiveness?**

A: The sum of the following costs incurred and payments made during the Applicable Covered Period, subject to certain other terms and limits discussed elsewhere in this FAQ and as set forth on the Forgiveness Applications and the terms of SBA Interim Final Rules and guidance, are eligible for forgiveness:

Payroll costs (defined below);

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For Borrowers using the 8-Week Covered Period, the maximum amount of cash compensation is \$15,385 per individual.

For Borrowers using the 24-Week Covered Period, the maximum amount of cash compensation is \$46,154 per individual.

Interest payments on any business mortgage obligation on real or personal property (such as an auto loan) that was incurred before February 15, 2020\*;

Business rent payments on real or personal property under a lease agreement in force before February 15, 2020\*;

Business utility payments for the distribution of electricity, gas, water, transportation (meaning transportation utility fees assessed by state and local governments), telephone or internet access for which service began before February 15, 2020; and/or

Refinancing an SBA EIDL loan made between January 31, 2020 and April 3, 2020.

\* The SBA issued an Interim Final Rule indicating that rent payments to a related party are eligible for forgiveness as long as (1) the amount of the loan forgiveness requested for rent or lease payments to the related party is no more than the amount of mortgage interest owed on the property during the Covered Period that is attributable to the space being rented by the business and (2) the lease and the mortgage were entered into prior to February 15, 2020. Furthermore, the SBA indicated that mortgage interest payments to a related party are not eligible for forgiveness.

Although interest on unsecured credit incurred before February 15, 2020 is a permissible use of PPP loan proceeds, this expense is not eligible for forgiveness.

“Applicable Covered Period” means either the “Covered Period” or the “Alternative Covered Period.” “Covered Period” means either: (1) the 24-week (168-day) period beginning on the disbursement date of the PPP loan, or (2) if the Borrower received an SBA loan number before June 5, 2020, the Borrower may elect to use an 8-week (56-day) period beginning on the disbursement date of the PPP loan. For example, if the Borrower received its PPP Loan proceeds on April 20, 2020 and elects to continue using the 8-week (56-day) period, then the first day of the “Covered Period” is April 20, 2020 and the last day of the “Covered Period” is June 14, 2020. The SBA has also established an “Alternative Payroll Covered Period” for Borrowers with bi-weekly (or more frequent) payroll periods. Such Borrowers may elect to calculate eligible payroll costs using the 24-week (168-day) period (or if the Borrower received an SBA loan number before June 5, 2020 – at the Borrower’s election – the 8-week (56-day) period) that begins on the first day of the Borrower’s first pay period following its PPP loan disbursement date. For example, if the Borrower received its PPP loan proceeds on April 20,

2020, and the first day of its first pay period following its PPP loan disbursement is April 26, 2020, then the first day of the “Alternative Payroll Covered Period” – if elected by the Borrower – is April 26, 2020 and the last day of the “Alternative Payroll Covered Period” is June 20, 2020 (if the Borrower elects the 8-week (56-day) loan forgiveness period). It is important to note that the “Alternative Payroll Covered Period,” if applicable, is only to be used in relation to payroll costs and cannot be used to determine non-payroll expenses included in the forgiveness calculation. Additionally, in no event, may the Applicable Covered Period extend beyond December 31, 2020.

### **Q: What “payroll costs” are eligible for loan forgiveness?**

A: “Payroll costs” eligible for loan forgiveness include compensation up to \$100,000 (applies only to cash compensation, and not to non-cash benefits) on an annualized basis to employees with a principal place of residence in the U.S. in the form of:

gross salary, gross wages, gross commissions, or similar compensation (including bonuses and hazard pay);

gross 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 (does not include benefits accelerated from periods outside of the Applicable Covered Period); and

payment of state and local taxes assessed on compensation of employees.

The following caps on the amount of loan forgiveness apply to owner-employees and self-employed individuals’ own payroll compensation (please note that per the SBA’s August 24, 2020 Interim Final Rule, any employee with less than a 5% ownership interest in a C- or S-Corporation PPP borrower is not subject to the owner-employee compensation rule):

for Borrowers that received an SBA loan number before June 5, 2020 and 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 8-weeks’ worth (8/52) of 2019 compensation (i.e., approximately 15.38% of 2019 compensation) or \$15,385 per individual, whichever is less, in total

across all businesses in which he or she has an ownership stake. For *self-employed individuals*, retirement and health insurance contributions are included in their net self-employment income and therefore cannot be separately added to their payroll calculation.

for Borrowers using 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% of 2019 compensation) or \$20,833 per individual, whichever is less, in total across all businesses in which he or she has an ownership stake. For *self-employed individuals*, retirement and health insurance contributions are included in their net self-employment income and therefore cannot be separately added to their payroll calculation.

*C-corporation owner-employees* are capped at 2.5/12 of their 2019 employee cash compensation, state and local taxes paid and assessed on their compensation and employer retirement and health insurance contributions made on their behalf.

*S-corporation owner-employees* are capped at 2.5/12 of their 2019 employee cash compensation, state and local taxes paid and assessed on their compensation and employer retirement contributions made on their behalf, but employer health insurance contributions made on their behalf cannot be separately added because those payments are already included in their employee cash compensation.

*Schedule C or Schedule F filers* are capped at 2.5/12 of their 2019 net profit as reported on IRS Form 1040 Schedule C line 31. Retirement and health insurance contributions are included in their net self-employment income and therefore cannot be separately added to their payroll calculation. State and local taxes are not eligible for forgiveness.

*General partners* are capped at 2.5/12 of their 2019 net earnings from self-employment that is subject to self-employment tax, which is computed from 2019 IRS Form 1065 Schedule K-1 box 14a (reduced by box 12 section 179 expense deduction, unreimbursed partnership expenses, and depletion from oil and gas properties) multiplied by 0.9235. Retirement and health insurance contributions are included in their net self-employment income and therefore cannot be separately added to their payroll calculation. Compensation is only eligible for forgiveness if the payments to partners are made during the Applicable Covered Period.

LLC owners must follow the instructions that apply to how their business was organized for tax filing purposes for tax year 2019, or if a new business, the expected tax filing situation for 2020.

“Payroll costs” may not include:

Cash compensation of an individual employee *in excess* of an annual salary of \$100,000 in one year, pro-rated during the Applicable Covered Period (i.e., for a 24-week covered period, a maximum of \$46,154 per individual, or for an 8-week covered period, a maximum of \$15,385 per individual);

any compensation of an employee whose principal place of residence is outside of the United States;

qualified sick leave wages or family leave wages for which a credit is allowed under sections 7001 or 7003 of the Families First Coronavirus Response Act; or

amounts paid to independent contractors.

Borrowers are generally eligible for forgiveness for the payroll costs “paid” and the payroll costs “incurred” during the Applicable Covered Period. 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 Applicable Covered Period are eligible for forgiveness if paid on or before the next regular payroll date. If the Borrower has an insured group health plan, insurance premiums “paid” or “incurred” during the Applicable Covered Period are eligible for forgiveness as long as premiums are paid during the Applicable Covered Period or by the next premium due date after the Applicable Covered Period. For a more in-depth discussion of payroll cost forgiveness, see the SBA’s PPP Loan Forgiveness FAQs.

**Q: Are bonuses or hazard pay eligible for forgiveness?**

A: Yes. If an employee’s total compensation does not exceed \$100,000 on an annualized basis, the employee’s hazard pay and bonuses are eligible for loan forgiveness.

**Q: Are amounts attributable to the business operation of a tenant or sub-tenant of the PPP borrower or, in the context of home-based businesses, household expenses, eligible for forgiveness?**

A: No, the amount of loan forgiveness requested for nonpayroll costs may not include any amount attributable to the business operation of a tenant or sub-tenant of the PPP borrower or - for home-based businesses - household expenses.

**Q: What non-payroll costs are eligible for forgiveness?**

A: Non-payroll costs eligible for forgiveness include:

covered mortgage obligations: payments of interest (not including any prepayment or payment of principal) on any business mortgage obligation on real or personal property (such as an auto loan) incurred before February 15, 2020\*;

covered rent obligations: business rent or lease payments pursuant to lease agreements for real or personal property in force before February 15, 2020\*; and

covered utility payments: business payments for a service for the distribution of electricity, gas, water, transportation (meaning transportation utility fees assessed by state and local governments), telephone, or internet access for which service began before February 15, 2020.

\* The SBA issued an Interim Final Rule indicating that rent payments to a related party are eligible for forgiveness as long as (1) the amount of the loan forgiveness requested for rent or lease payments to the related party is no more than the amount of mortgage interest owed on the property during the Covered Period that is attributable to the space being rented by the business and (2) the lease and the mortgage were entered into prior to February 15, 2020. Furthermore, the SBA indicated that mortgage interest payments to a related party are not eligible for forgiveness.

Eligible non-payroll costs 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. It is important to note that the “Alternative Payroll Covered Period,” if applicable, is only to be used in relation to payroll costs and cannot be used to determine non-payroll expenses included in the forgiveness calculation. As a reminder, as a result of the PPP Flexibility Act, eligible non-payroll costs cannot exceed 40% of the total forgiveness amount.

**Q: I incurred certain eligible payroll or non-payroll costs before I actually received my PPP loan proceeds, but I paid those costs during the Applicable Covered Period. Are those amounts incurred prior to – but paid during – the Applicable Covered Period eligible for forgiveness?**

A: Yes.

Borrowers are generally eligible for forgiveness for the payroll costs “paid” and the payroll costs “incurred” during the Applicable Covered Period. 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 Applicable Covered Period are eligible for forgiveness if paid on or before the next regular payroll date. If the Borrower has an insured group health plan, insurance premiums "paid" or "incurred" during the Applicable Covered Period are eligible for forgiveness as long as premiums are paid during the Applicable Covered Period or by the next premium due date after the Applicable Covered Period.

For example, a Borrower's Applicable Covered Period runs from April 14 through June 8, 2020. The Borrower has a bi-monthly payroll schedule that pays on the 15th and the last day of each month. The Borrower may use PPP loan funds to pay the payroll costs that would be paid on April 15, 2020 ("paid" during the Applicable Covered Period even though for payroll prior to the Applicable Covered Period). The Borrower may also use PPP loan funds to pay the payroll costs that would be paid on April 30, 2020; May 15, 2020; and May 31, 2020 ("incurred" and "paid" during the Applicable Covered Period). Additionally, on June 15, 2020 (next regular payroll date), the Borrower may use PPP loan funds to pay the payroll costs attributable to June 1 through June 8, 2020 ("incurred" during the Applicable Covered Period even though paid after the Applicable Covered Period). All such payments may be included in the requested forgiveness amount.

Eligible non-payroll costs 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. The Interim Final Rule on forgiveness provides the example of an electric bill. Electric bills are typically paid in arrears. The Borrower received a loan before June 5, 2020 and uses a 24-week covered period that begins on June 1, 2020 and ends on November 15, 2020. The Borrower pays its electricity bills for June through October during the Covered Period and pays its November electricity bill on December 10, 2020, which is the next regular billing date. The Borrower may seek forgiveness for its June through October electricity bills, because they were paid during the Covered Period. In addition, the Borrower may seek loan forgiveness *for the portion of its November electricity bill through November 15, 2020* (the end of the Covered Period), because it was incurred during the covered period and paid on the next regular billing date. It is important to note that the "Alternative Payroll Covered Period," if applicable, is only to be used in relation to payroll costs and cannot be used to determine non-payroll expenses included in the forgiveness calculation.

**Q: Is interest that accrued on the PPP loan eligible for forgiveness?**

A: Yes, the June 17, 2020 Interim Final Rule on Revisions to the Third and Sixth Interim Final Rule states that "the amount of loan forgiveness can be up to the full principal amount of the loan plus accrued interest."

**Q: What if I applied for my PPP loan based on a good faith belief that I was eligible, but a later Interim Final Rule or SBA guidance made clear my interpretation was not in**

## **line with what the SBA intended?**

A: In discussing the SBA's determination of forgiveness, the Interim Final Rule on forgiveness states "The Administrator may review whether a borrower is eligible for the PPP loan based on the provisions of the CARES Act, the rules and guidance *available at the time of the borrower's PPP loan application*, and the terms of the borrower's loan application. See FAQ 17 (posted April 6, 2020)." FAQ 17 states that Borrowers and Lenders may rely on the laws, rules and guidance available at the time of the application, but if the loan proceeds had not been disbursed at the time of the clarifying guidance, then the Borrower should have modified its application. The eligibility review will be "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..." The SBA's review will also examine whether the Borrower provided adequate documentation for the certifications on the loan application.

## **Q: What if I have not been able to open my business at all, but I am still paying employees?**

A: For employees who are not performing work but are still on the Borrower's payroll, payroll costs are "incurred" based on the schedule established by the Borrower (typically, each day that the employee would have performed work). Therefore, such payroll costs are eligible for forgiveness.

### ***Reductions to Forgiveness Amount***

[Back to the top](#)

## **Q: What actions will reduce my forgiveness amount?**

A: Generally, the amount of loan forgiveness will be reduced if the number of full-time equivalent employees is reduced (FTE Reduction), if employees' salaries or hourly wages are reduced by more than 25% (Salary/Hourly Wage Reduction), or if the Borrower's eligible non-payroll expenses exceed 40% of the total eligible expenses. However, the CARES Act, as amended by the Flexibility Act, includes a handful of safe harbors and exemptions (discussed in more detail below) which, if applicable, will not result in a reduction of the loan forgiveness amount. For example, Borrowers have until December 31, 2020 to eliminate any FTE Reduction or the Salary/Hourly Wage Reduction. There are also exemptions based on employee availability and business activity. Additionally, there is an exemption for Borrowers that have offered to restore employee hours at the same salary or wages, even if the employees have not accepted.

## **Q: How should a Borrower calculate a full-time equivalent employee (FTE)?**

A: There are two (2) methods for a Borrower to calculate FTEs:

Option #1 – for each employee, take 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.

Option #2 – assign a 1.0 for employees who work 40 hours or more per week and 0.5 for employees who work fewer hours.

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

## **Q: What is the FTE Reduction?**

A: Generally, the Borrower's loan forgiveness will be reduced if the Borrower's average number of FTEs during the Applicable Covered Period is less than the average number of FTEs during the Borrower's chosen reference period. Borrowers can choose between the following reference periods:

February 15, 2019 to June 30, 2019;

January 1, 2020 to February 29, 2020; or

for seasonal employers, either of the preceding periods or a consecutive 12-week period between May 1, 2019 and September 15, 2019; however, a seasonal employer that elects to use a 12-week period between May 1, 2019 and September 15, 2019 to calculate its maximum PPP loan amount must use the same 12-week period as the reference period for calculation of any reduction in the amount of loan forgiveness.

The same method must be used for each employee.

## **Q: By what amount is my loan forgiveness reduced if I have fewer FTEs during the Applicable Covered Period?**

A: If none of the FTE Reduction exceptions or safe harbors (discussed below) apply, the average number of FTEs during the Applicable Covered Period reduces the amount of forgiveness proportionally by the percentage of reduction in FTEs. For example, if the Borrower has 20% fewer FTEs during the Applicable Covered Period, then the amount of forgiveness is reduced by 20%. The Forgiveness Application and schedules account for these reductions.

**Q: What is the Salary/Hourly Wage Reduction?**

A: Generally, for employees who earned \$100,000 or less for all pay periods in 2019 (or were not employed by the Borrower in 2019), the Borrower's loan forgiveness will be reduced for each employee whose average pay (salary or hourly wage) during the Applicable Covered Period is less than 75% of their average pay compared to the period from January 1, 2020 to March 31, 2020. Borrower should only take into account decreases in salaries or wages, and not other forms of compensation.

The total amount of forgiveness is reduced by the total dollar amount of salary or wage reduction in excess of 25% of the salary or wages between January 1, 2020 and March 31, 2020. This reduction calculation is done on a per employee basis, not in the aggregate.

It should be noted that if a Borrower applies for forgiveness before the end of the Applicable Covered Period, and it has reduced those certain employee's salaries or wages in excess of 25%, the Borrower must account for the excess salary reduction for the full 8-week or 24-week covered period.

**Q: Will a Borrower's PPP loan forgiveness amount be reduced if the Borrower reduced the hours of an employee, then offered to restore the reduction in hours, but the employee declined the offer?**

A: No. In calculating the loan forgiveness amount, a Borrower may exclude any reduction in full-time equivalent employee headcount that is attributable to an individual employee if:

1. the Borrower made a good faith, written offer to restore the reduced hours of such employee;
2. 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 reduction in hours;
3. the offer was rejected by such employee; and
4. the Borrower has maintained records documenting the offer and its rejection.

**Q: Will a Borrower's PPP loan forgiveness amount be reduced if the borrower is unable to rehire individuals who were employees of the Borrower on February 15, 2020?**

A: In calculating its loan forgiveness amount, a borrower may exclude any reduction in full-time equivalent employees during the Applicable Covered Period, as long as the Borrower is able to document, in good faith, the following:

1. an inability to rehire individuals who were employees of the borrower on February 15, 2020; and

2. an inability to hire similarly qualified individuals for unfilled positions on or before December 31, 2020.

Further, Borrowers are required to inform the applicable state unemployment insurance office of any employee's rejected rehire offer within 30 days of the employee's rejection of the offer. The documents that borrowers should maintain to show compliance with this exemption include the written offer to rehire an individual, a written record of the offer's rejection, and a written record of efforts to hire a similarly qualified individual.

**Q: Will a Borrower's PPP loan forgiveness amount be reduced if the Borrower is unable to return to the same level of business activity as the Borrower was operating at before February 15, 2020?**

A: No. A Borrower is exempted from the loan forgiveness reduction arising from a proportional reduction in full-time equivalent employees during the Applicable Covered Period, as long as the Borrower is able to document, in good faith, an inability to return to the same level of business activity such as the Borrower was operating at before February 15, 2020 due to compliance with requirements established or guidance issued between March 1, 2020 and December 31, 2020 by HHS, the CDC or OSHA, related to the maintenance of standards for sanitation, social distancing or any other worker or customer safety requirements related to COVID-19.

Such documentation must include copies of applicable COVID-19 requirements or guidance for each business location and relevant Borrower financial records.

This exemption includes both direct and indirect compliance with such COVID-19 requirements or guidance.

**Q: Will a Borrower's PPP loan forgiveness amount be reduced if the Borrower fired an employee for cause during the Applicable Covered Period?**

A: No.

**Q: Will a Borrower's PPP loan forgiveness amount be reduced if an employee voluntarily resigned during the Applicable Covered Period?**

A: No.

**Q: Will a Borrower's PPP loan forgiveness amount be reduced if an employee requests and receives a reduction in its hours during the Applicable Covered Period?**

A: No.

**Q: If a Borrower restores reductions made to employee salaries and wages or FTE employees by no later than December 31, 2020, can the Borrower avoid a reduction in its loan forgiveness amount?**

A: Yes. If certain employee salaries and wages were reduced by more than 25% between February 15, 2020 and April 26, 2020 (the safe harbor period), but the Borrower eliminates those reductions by December 31, 2020 or earlier, then the Borrower is exempt from any reduction in loan forgiveness amount that would otherwise be required.

Similarly, if a Borrower eliminates any reductions in FTE employees occurring during the safe harbor period by December 31, 2020 or earlier, then the Borrower is exempt from any reduction in loan forgiveness amount that would otherwise be required.

**Q: If a Borrower terminated an employee or reduced their hours from full-time to part-time, does it count those reductions in both the calculations for the FTE Reduction and the Salary/Hourly Wage Reduction?**

A: The Salary/Hourly Wage Reduction applies only to the portion of the Salary/Hourly Wage Reduction that is not attributable to the FTE Reduction. The SBA and Treasury make clear that Borrowers should not be doubly penalized by having such reductions count in both the Salary/Hourly Wage Reduction and the FTE Reduction. For example, an hourly wage employee had been working 40 hours per week during the Borrower selected reference period (FTE employee of 1.0) and the Borrower reduced the employee's hours to 20 hours per week during the Applicable Covered Period (FTE employee of 0.5). There was no change to the employee's hourly wage during the Applicable Covered Period. Because the hourly wage did not change, the reduction in the employee's total wages is entirely attributable to the FTE Reduction and the Borrower is not required to conduct a Salary/Hourly Wage Reduction calculation for that employee. However, in this same example, if that employee's hourly wage was also reduced, the FTE Reduction calculation is impacted and the Salary/Hourly Wage Reduction calculation is impacted, but only by the reduction attributable to the wage rate reduction, not the number of reduced hours.

**Q: The new requirement is that at least 60% of the PPP loan proceeds shall be used for payroll costs, and not more than 40% of the loan forgiveness amount may be attributable to nonpayroll costs. What if a Borrower spends less than 60% on payroll costs? Will it receive any forgiveness?**

A: In order to be eligible for full forgiveness, a Borrower must use at least 60% of the PPP loan for payroll costs, and not more than 40% of the loan forgiveness amount may be attributable to

nonpayroll costs. If a Borrower uses less than 60% of its PPP loan for payroll costs, it will not receive the full amount of loan forgiveness it might otherwise be eligible to receive. Instead, the Borrower will receive partial loan forgiveness, based on the requirement that 60% of the forgiveness amount must be attributable to payroll costs. For example, if a Borrower receives a \$100,000 PPP loan, and during the Applicable Covered Period the Borrower spends \$54,000 (or 54%) of its loan on payroll costs, then because the Borrower used less than 60% of its loan on payroll costs, the maximum amount of loan forgiveness the Borrower may receive is \$90,000 (\$54,000 divided by 60%). This \$90,000 is further broken down to \$54,000 in payroll costs (constituting 60% of the \$90,000 maximum forgiveness amount) and to \$36,000 in nonpayroll costs (constituting 40% of the \$90,000 maximum forgiveness amount).

### Contact us

Husch Blackwell's CARES Act resource team has reviewed the Act carefully and is developing content to help clients determine how best to access the available assistance. The team will add new content frequently as the Act is implemented through a number of agency rulemakings over the coming weeks. If you have further questions or require more information regarding this update, please contact Jessica Zeratsky, Christopher W. Peterson, Chrissie Simpson or your Husch Blackwell attorney.

*Disclaimer: The issues discussed above are under further review, and guidance is not complete. Please continue to check back as we continue to update regularly.*