COVID-19 Alert

REID & RIEGE ATTORNEYS

CARES ACT PAYCHECK PROTECTION PROGRAM LOANS AUGUST 11, 2020 UPDATE

AUGUST 2020

This continues our efforts to provide updates on the Paycheck Protection Program (PPP) loan offerings created by the CARES Act and overseen by the Small Business Administration (SBA).

WHAT IS NEW?

The extended deadline for obtaining PPP loans passed on August 8, 2020.

As that deadline loomed, SBA published a new set of FAQs titled "Frequently Asked Questions (FAQs) on PPP Loan Forgiveness" (the New FAQs). The New FAQs compress a good deal of previously available guidance into a more user friendly format and adds guidance, not all welcome, on a few issues. One hopes that, with the New FAQs in hand, lenders will now open the forgiveness application process for those borrowers ready to proceed.

WHAT DO THE NEW FAQS SAY?

We encourage all readers to review the New FAQs themselves. They are broken into four broad categories containing three to eight FAQs, and are more user friendly than the Interim Final Rules that underlie them. Here are quick summaries arranged by category:

General Loan Forgiveness FAQs

- A lender may accept scanned copies of loan forgiveness applications and supporting documents, as well as E-consents and E-signatures (subject to the lender's obligations under other applicable law). See FAQ 2.
- Borrowers are not required to make any payments on their PPP loans until the SBA has remitted the forgiveness amount to the lender (or, presumably, forgiveness is disallowed). This is premised on the borrower submitting the forgiveness application within 10 months following its Covered Period. Any amount not forgiven must be repaid prior to the loan maturity date, with this including interest on the amount not forgiven from the original date of loan funding until payment. The lender is obligated to notify the borrower of SBA remittance of the loan forgiveness amount (or SBA's determination of no forgiveness) and the date the borrower's first payment is due. See FAQ 3.

Loan Forgiveness Payroll Costs FAQs

- FAQs 1, 2 and 3 address topics of paid and incurred Payroll Costs, as well

OUR COVID-19 TEAM

Business & Contracts
Kathleen M. Coss
(860) 240-1035 • kcoss@rrlawpc.com
Thomas R. Kasper
(860) 240-1084 • tkasper@rrlawpc.com
Cathryn A. Reynolds
(860) 240-1019 • creynolds@rrlawpc.com

Commercial Real Estate
Louis J. Donofrio
(860) 240-1042 • ldonofrio@rrlawpc.com
Thomas R. Kasper
(860) 240-1084 • tkasper@rrlawpc.com

Employee Benefits & Compensation
Douglas K. Knight
(860) 240-1028 • dknight@rrlawpc.com

Estate Planning & Trust Matters
John R. Ivimey
(860) 240-1062 • jivimey@rrlawpc.com
Barbara A. Taylor
(860) 240-1033 • btaylor@rrlawpc.com

Finance & Business Insolvency
Jon P. Newton
(860) 240-1090 • jnewton@rrlawpc.com

Government & Regulatory Investigations
Thomas V. Daily
(860) 240-1067 • tdaily@rrlawpc.com

Health Care Providers & Privacy
Adam Carter Rose
(860) 240-1065 • arose@rrlawpc.com

HR & Employee Issues
Adam T. Boston
(860) 240-1023 • aboston@rrlawpc.com
Brian O'Donnell
(860) 240-1012 • bodonnell@rrlawpc.com

Trust & Wealth Management
*David L. Sullivan, CTFA**
(860) 240-1022 • dsullivan@rrlawpc.com

**Mr. Sullivan is a Certified Trust Financial Advisor; he is not an attorney.*

as the Alternate Payroll Covered Period. FAQ 2 provides definitive clarity that Payroll Costs incurred prior to the Covered Period (or Alternative Payroll Covered Period) but paid during it are fully eligible for forgiveness (although FAQs 6 and 7 seem to differ on this in the cases of Payroll Costs in the form of health care and retirement benefit costs).

- FAQ 4 makes clear that in calculating cash compensation, the relevant starting point is gross amount before deductions for taxes and employee benefit and similar payments.
- FAQ 5 provides confirmation that "Payroll [C]osts include all forms of cash compensation paid to employees, including tips, commissions, bonuses, and hazard pay." However, this is subject to the rule that "forgivable cash compensation per employee is limited to $100,000 on an annualized basis."
- FAQs 6 and 7 provide details on group health care benefits and retirement benefits that are eligible for forgiveness (subject to FAQ 8 in the case of owners of the borrower). New here is a restriction to costs for benefits attendant to the Covered Period (or Alternate Payroll Covered Period), not costs "accelerated from periods outside" the applicable period. Despite the use of "accelerated," the point seems to be to disallow both prepayment of costs not yet incurred for future period benefits and payment of costs previously incurred for prior period benefits.
- FAQ 8 will likely be the most controversial of the New FAQs. It addresses owner compensation, with a general rule and then specific rules depending on the tax status of the borrower.
  - <u>General Rule</u>: No owner's eligible cash compensation can give rise to forgiveness to the extent in excess of $20,833 if the Covered Period (or Alternate Payroll Covered Period) is 24 weeks, or $15,385 if the Covered Period (or Alternate Payroll Covered Period) is eight weeks. This rule is to be applied across all businesses, so if the owner is compensated via multiple entities each with its own PPP loan, the amount must be allocated between those borrowers. It also serves as a superseding cap for cash compensation discussed below.
  - <u>C Corporation Owners</u>: Cash compensation (defined as for all other employees) is limited to 2.5/12 of 2019 cash compensation. Costs for employer state and local taxes paid on owner compensation, and for employer provided contribution for employee health insurance appear to be fully eligible, but costs for employer-provided retirement plan contributions are capped at 2.5/12 of the 2019 contribution amount; all costs contemplated by this sentence do not count toward the cap amount in the general rule.
  - <u>S Corporation Owners</u>: Cash compensation (defined as for all other employees) is limited to 2.5/12 of 2019 cash compensation. Costs for employer state and local taxes paid on owner compensation are eligible, and costs for employer-provided retirement plan contributions are eligible but capped at 2.5/12 of the 2019 contribution amount; all costs contemplated by this sentence do not count toward the cap amount in

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the general rule. For employees who own at least 2% of the S corporation, and for their family members under tax family attribution rules, employer contributions for health insurance are not eligible for forgiveness because they are included in cash compensation.

- Self-employed Schedule C (or Schedule F) Filers: Eligible cash compensation is limited to 2.5/12 of 2019 net profit (or net farm profit) as reported on IRS Form 1040 Schedule C (or Schedule F). Borrower payments for health insurance, retirement, or state or local taxes are not eligible for forgiveness. The owner's 2019 IRS Form 1040 Schedule C (or Schedule F) must be provided as part of the loan forgiveness application if it was not submitted with the original loan application.
- General Partners: Eligible cash compensation is limited to 2.5/12 of 2019 net earnings from self employment that is subject to self-employment tax, computed from 2019 IRS Form 1065 Schedule K-1 box 14a (reduced by box 12 section 179 expense deduction, unreimbursed partnership expenses deducted on IRS Form Schedule SE, and depletion claimed on oil and gas properties) multiplied by 0.9235. Further, compensation is only eligible if payments are made during the Covered Period (or Alternate Payroll Covered Period). Borrower payments for health insurance, retirement, or state or local taxes are not eligible for forgiveness. The borrower's 2019 IRS Form 1065 K-1s must be provided as part of the loan forgiveness application if they were not submitted with the original loan application.
- LLC Owners: Apply the above rules depending on the borrower's status for tax filing purposes for 2019 (or as anticipated for 2020 if a new business).

Loan Forgiveness Non-Payroll Costs FAQs

- FAQs 1 and 2 address topics of paid and incurred Non-Payroll Costs (i.e., mortgage interest, rent and lease costs, and utility payments).
- FAQ 3 reiterates clear that the Alternate Payroll Covered Period concept does not apply to Non-Payroll Costs.
- FAQ 4 makes clear that interest on unsecured credit is not eligible for loan forgiveness. However, payment of that type of interest is a permissible use of PPP proceeds.
- FAQ 5 addresses the topic of renewed leases and refinanced mortgage debt. Recall that to give rise to forgiveness, the lease or mortgage obligation had to be in place prior to February 15, 2020. In new guidance, SBA is permitting forgiveness eligibility where the pre-February 15, 2020 lease or mortgage debt has been renewed or refinanced subsequent to February 15, 2020.
- FAQ 7 makes clear that eligible utility expenses for electricity include both supply charges and distribution charges.

Loan Forgiveness Reductions FAQs

- FAQ 1 addresses the topic of FTE loss due to a laid-off employee that has declined the borrower's rehire offer. Such an employee can be excluded for

For information regarding Reid and Riege, P.C., please visit our website at www.rrlawpc.com or contact us at:

Reid and Riege, P.C.
One Financial Plaza
Hartford, CT 06103

or

Reid and Riege, P.C.
234 Church Street
New Haven, CT 06510

purposes of calculating any reduction in FTEs so long as the borrower can document the refusal and the inability to rehire someone similarly qualified by December 31, 2020, and so long as the borrower notifies the applicable state unemployment office of the former employee's rejection of the rehire offer.

- FAQ 3 makes clear that employees making more than $100,000 per year must be included in calculating FTE reductions, although they are not included for determining reductions in salary or wages.
- FAQ 4 address forgiveness reductions due to salary and wage reductions. While the examples are helpful, they do not appear to provide new guidance.
- FAQ 5 also touches on forgiveness reductions due to salary and wage reductions. It makes clear that, for purposes of the calculation, only decreases in salary or wages are taken into account, not all cash compensation. Thus, reductions in tips, commissions, bonuses, etc. would appear to be irrelevant to the analysis.

PRIOR UPDATES

For our previous PPP articles, please see April 1, 2020, April 3, 2020, April 9, 2020, April 16, 2020, April 24, 2020, May 1, 2020, May 6, 2020, May 13, 2020, May 18, 2020, June 1, 2020, June 4, 2020, June 12, 2020, June 22, 2020, June 26, 2020, and July 7, 2020.

We are interested to hear your experiences with the PPP.

Please contact the Reid and Riege attorney with whom you regularly work, or a member of our Business Services practice listed to the right, for more up to date information, or questions about your unique circumstances.

BUSINESS SERVICES

Karen L. Brand
(860) 240-1089 • kbrand@rrlawpc.com

Kathleen M. Coss
(860) 240-1035 • kcoss@rrlawpc.com

Louis J. Donofrio
(860) 240-1042 • ldonofrio@rrlawpc.com

Coleen Hurlie-Dunn
(860) 240-1085 • churlie-dunn@rrlawpc.com

Thomas R. Kasper
(860) 240-1084 • tkasper@rrlawpc.com

Earl F. McMahon
(860) 240-1016 • emcmahon@rrlawpc.com

Robert M. Mulé
(860) 240-1010 • rmule@rrlawpc.com

Cathryn A. Reynolds
(860) 240-1019 • creynolds@rrlawpc.com

Adam Carter Rose
(860) 240-1065 • arose@rrlawpc.com

Mark X. Ryan
(860) 240-1056 • mryan@rrlawpc.com