

COVID-19 Alert

CARES ACT PAYCHECK PROTECTION PROGRAM LOANS JUNE 4, 2020 UPDATE

JUNE 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).

MAJOR CHANGES TO PPP

On June 3, 2020 the Senate by unanimous consent passed H.R. 7010, better known as the [“Paycheck Protection Program Flexibility Act of 2020”](#) (the New Act). The New Act was previously passed 471 to 1 by the House of Representatives on May 28, 2020. The President’s signature is expected shortly.

Assuming the New Act becomes law, it will be effective immediately and make significant changes, particularly to the forgiveness rules applicable to PPP loans. Those rules were established in broad outline in the CARES Act, and then in more detail by SBA rule-making and guidance.

CHANGES TO LOAN TERM

The CARES Act originally contemplated loan terms of up to 10 years. SBA by rule-making settled on two year terms. The New Act now establishes a minimum term of five years. This portion of the New Act is applicable only for loans originated after the New Act takes effect, although it permits lenders and borrowers to modify the terms of loans previously made. This provision will be of interest mainly to borrowers who cannot achieve full loan forgiveness. Those borrowers with pre-existing loans should reach out to lenders to discuss possible loan modifications.

We note the CARES Act originally contemplated that PPP loans could bear interest rates of up to 4.00%, while SBA later established a fixed 1.00% interest rate. The New Act does not make any changes regarding interest rates.

CHANGES TO COVERED PERIOD

The CARES Act originally provided for a Covered Period for expenses that would give rise to forgiveness of eight weeks commencing with loan origination. Subsequently SBA clarified “loan origination” to mean the date of loan funding, and then introduced the concept of an Alternate Payroll Covered Period (see our [May 18](#) and [June 1](#) updates). However, the CARES Act in all events limited the Covered Period to a period ending June 30, 2020, a problem for any borrower obtaining a PPP loan after May 5, 2020.

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In Sections 3(a) and (b) of the New Act, the back-end cut-off date is extended out to December 31, 2020. More significantly, the Covered Period itself is now extended from eight weeks to 24 weeks (subject to the ultimate December 31 end date). However, borrowers already in receipt of their loans can continue to go with the original eight week period.

This provides planning opportunities for borrowers: those already at, or close to achieving, expenses giving rise to full-forgiveness can proceed to seek forgiveness as originally planned; those not yet able to do so can hold off and obtain greater forgiveness than previously possible. In making this evaluation, borrowers should take into account other changes to the forgiveness rules discussed below.

The New Act does not address the Alternate Payroll Covered Period created by SBA, and whether that concept will survive is one of the new open questions from the New Act. In any event, SBA will need to modify its form Application for Loan Forgiveness to account for changes made by the New Act.

CHANGES TO MIX OF FORGIVABLE EXPENSES

The CARES Act originally identified the types of expenses that will give rise to PPP loan forgiveness, generally consisting of Payroll Costs (actual payroll, employer health and retirement plan fundings, etc.) and Non-Payroll Costs (mortgage interest, rent and utility expenses). Subsequently SBA established rules requiring that the amount to be forgiven must consist of at least 75% Payroll Costs, and not more than 25% Non-Payroll Costs. This effectively limited the amount borrowers whose Payroll Costs were down in the Covered Period could plan to have forgiven, an effect exacerbated by the reductions to forgiveness for certain compensation reductions and, more so, FTE reductions.

Section 3(b) of the New Act adds a new provision re-setting SBA's standard to at least 60% Payroll Costs, and not more than 40% Non-Payroll Costs. This, coupled with the extended Covered Period, should provide great benefit to many borrowers.

Unfortunately, the new provision is poorly drafted, and begins with the wording "To receive loan forgiveness under this section, an eligible recipient shall use at least 60 percent of the covered loan amount for [P]ayroll [C]osts . . ." The wording appears to now not just create a limitation on forgiveness, but a threshold amount of Payroll Cost that must be surpassed to obtain ANY forgiveness. Whether this will be clarified in subsequent legislation or SBA rule-making thus becomes another new question.

We note that the New Act does not address SBA's allowance of expenses "incurred" but not "paid" during the Covered Period (or Alternate Payroll Covered Period, if that concept remains). We presume, but do not know, that the "incurred" concept remains, but note that it may be inconsistent with the substantially increased Covered Period, particularly given the original CARES Act references to amounts of "payments." It is possible that SBA maintains the "incurred" concept for borrowers sticking with an eight week Covered Period, but not for those making use of the new 24 week Covered Period.

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NEW EXEMPTIONS FOR SOME FTE REDUCTIONS

The CARES Act contemplated that the loan amount otherwise to be forgiven is to be reduced proportionately by a factor equal to the proportionate reduction in the borrower's full-time equivalent employees (FTEs) during the Covered Period relative to an applicable reference period, with an ability to reverse the reduction by restoring FTEs subsequent to the Covered Period up to June 30, 2020. SBA by rule-making has created some exceptions, in the cases of employees who refuse offers to return at their prior hour and pay rates, who are discharged for cause, who voluntarily resign, or whose hours and pay are reduced at their voluntary request (see our [May 18](#) and [June 1](#) updates).

Section 3(b) of the New Act creates new exemptions for borrowers. First, a borrower that is unable to rehire individuals who were previously employed on February 15, 2020, or similarly qualified employees, by December 31, 2020, will not lose forgiveness by reason of the resulting FTE reduction. Second, and potentially of much greater significance, a borrower will not lose forgiveness if unable to return to "the same level of business activity as existed at before [sic] 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 safety requirement related to COVID-19." We note the standard ties to standards or guidance of specified Federal agencies; how exactly this applies to orders of Governors or other state or local officials or bodies is a bit unclear, although one would think that it would take into account those types of orders issued reciting the applicable Federal guidance. Similarly, how it applies to decisions made by borrowers on their own in reliance on applicable Federal guidance is a bit unclear. Borrowers must, in any event, act in good faith in making use of either exemption, and must document the factors giving rise to reliance on either exemption.

Apart from the new exemptions, the date to reverse Covered Period FTE reductions (or compensation reductions) is now pushed back to December 31, 2020.

We again note that it is unclear if the Alternate Payroll Covered Period survives the New Act. If it does, under the current SBA rules borrowers electing to use it to calculate forgivable Payroll Costs must also use it for purposes of making FTE reduction calculations.

EXTENSION OF DEFERRAL PERIOD

The CARES Act contemplated a deferral period of six months to one year for payments of principal, interest, and fees with respect to PPP loans. SBA locked this period at six months from loan funding. As noted in our [June 1](#) update, this created the potential for PPP loans to move into payment status before a borrower is informed of a decision on its forgiveness application.

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Section 3(c) of the New Act resolves the dilemma by pushing back deferral “until the date on which the amount of forgiveness determined under section 1106 of the CARES Act is remitted to the lender.” Accordingly, borrowers will not be obligated to begin payment until SBA has confirmed the amount of the loan to be forgiven.

However, it was unclear under the CARES Act when precisely a borrower was required to apply for loan forgiveness. Section 3(c) of the New Act adds a new provision requiring that the application be placed within 10 months of the last day of the Covered Period. Failure to so apply triggers the start of loan payments on the last day of that 10-month period.

PAYROLL TAX DEFERRAL

Section 4 of the New Act amends the CARES Act to permit PPP borrowers, including those receiving loan forgiveness, to make use of the CARES Act payroll tax deferral provisions.

IS THIS THE FINAL WORD?

No. At a minimum, SBA will need to revise its Loan Forgiveness Application and undertake new rule-making to account for the New Act. Whether additional Congressional action will be forthcoming is unknown.

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](#), and [June 1, 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.

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