

## **Loans, Uses, and Forgiveness under the Paycheck Protection Program (“PPP”)**

### **Loan Uses**

1. During the covered period (February 15, 2020 through June 30, 2020), the loan can only be used for:
  - a. payroll costs;
  - b. costs related to the continuation of group health care benefits during period of paid sick, medical, or family leave, and insurance premiums;
  - c. employee salaries, commissions, or similar compensation;
  - d. payments of interest on any mortgage obligation (but not principal payments)
  - e. rent;
  - f. utilities; and/or
  - g. interest on any debt obligations that were incurred prior to February 15, 2020.

### **Forgiveness - Payroll**

1. Loans received under this Program can be **forgiven** to the extent that the proceeds are used during the eight-week period following the origination of the loan (probably the date you loan is funded) for:
  - a. payroll costs;
  - b. payment of interest on mortgage obligations incurred prior to February 15, 2020;
  - c. rent obligations for leases entered into prior to February 15, 2020; or
  - d. utility payments.
2. **The SBA website also states that "due to likely high subscription, at least 75% of the forgiven amount must have been used for payroll."**
3. NOTE: While the amount of the eligibility for a loan under the Paycheck Protection Program and the amount of any such loan are fairly straight forward, there is complexity and a lack of clarity associated with calculating the amount of any such loan actually forgiven. Specifically, the statute is unclear as to how to calculate the forgiveness of a loan made under the Paycheck Protection Program if salary or wages of one or more employees are reduced.
4. The amount of the loan which to be forgiven is subject to certain limitations.
  - a. If a business receiving a loan reduces the number of employees or the amount of compensation paid to such employees by 25%, then the amount eligible for forgiveness is also reduced.
  - b. The forgiveness is limited to the principal owed under the loan, and no forgiveness is available for interest owed under the loan. In any event, interest

owed under the loans will be at 1% per year for a two-year term and is deferred for a minimum of six months from the date of the loan.

5. Number of Employees Reduction:

- a. The amount of forgiveness is reduced by the dividing the average number of full-time equivalent employees employed during the covered period (which is defined as the eight-week period beginning on the date of the origination of the loan) by the average number of full-time equivalent employees for the period beginning February 15, 2019 through June 30, 2019, or, at the election of the borrower, the period beginning January 1, 2020 through February 29, 2020.
- b. For example, if an employer had 20 full-time employees for the period between February 15, 2019 through June 30, 2019, but only 15 employees during the eight-week covered period (February 15, 2020 through June 30, 2020), the amount of forgiveness that the employer is otherwise entitled to would be reduced by 25% (15 divided by 20 = 75%;  $1 - 75\% = 25\%$ ).

6. 25% Reduction in Compensation:

- a. The amount of the loan that could be forgiven is further reduced by the amount of any reduction in total salary or wages of any employee during the eight-week covered period in excess of 25% of the total salary or wages of the employee during the most recent full quarter that the employee was employed prior to the eight-week covered period.
- b. Solely for the purposes of this section, employees receiving annualized compensation in excess of \$100,000 are disregarded, which means that any reductions of total salary or wages of employees who received compensation during any pay period in 2019 which exceeded an annualized rate of pay equivalent to \$100,000 are not taken into account for the purposes of determining the amount of the forgiveness limitation.
- c. For example, if an employee making \$90,000 annually (or \$22,500 during the most recent quarter) had their salary reduced to \$60,000 (or \$15,000 per quarter),
  - i. the salary was reduced by more than 25% so a reduction should apply. The question is how is this reduction calculated? Is the reduction \$1,875 ( $\$22,500 \times 75\% = \$16,875$ ;  $\$16,875 - \$15,000 = \$1,875$ ), which compares quarter over quarter compensation before and after the reduction?
  - ii. Alternatively, is the reduction \$7,644 ( $\$9,231$  is the equivalent of \$60,000 annual salary payable over eight weeks;  $\$22,500 \times 75\% = \$16,875$ ;

\$16,875 - \$9,231 = \$7,644) which compares the actual salary paid during the eight-week covered period to a full quarter's compensation?

- d. It appears that the second alternative applies which would provide a harsh result for employers that reduce their salary by even \$1 since the statute seems to compare compensation paid during an eight-week period to compensation paid over a quarter which is 13 weeks. We will need guidance to know which calculation is correct.
7. It is not yet clear if the funds need be tracked specifically to the payments permitted for the forgiveness to occur. For example, if a business received a \$100,000 loan and has \$100,000 of income from their business during the covered period that was all deposited into the company's bank account. \$100,000 was spent on maintaining payroll and another \$50,000 was spent to buy a new vehicle for the owner. Is there a requirement that the business separately hold the loaned amount in a separate account that is solely used for the payment of the allowed expenses, or will there be no direct tracing of how the funds were spent?
  8. The amount of the forgiveness under the loan received under the Paycheck Protection Program is also limited by any EIDL Grant received by the business.
  9. In order to receive the forgiveness, the employer must apply to the lender which includes the following:
    - a. Documentation verifying the number of full-time equivalent employees on the payroll and their pay rates, which includes payroll tax filings reported to the IRS and state income, payroll, and unemployment insurance filings;
    - b. Documentation, including cancelled checks, payment receipts, transcripts of accounts of other documents verifying payments on mortgage interest, lease, and utility obligations;
    - c. A certification that the documentation is true and correct and that the amount for which forgiveness is requested was used to retain employees, make payments on mortgage interest obligations, rent, and utilities; and 4. Any other documentation that the Administrator deems necessary.

- I. Another outstanding question is how much activity does a business need to have in order to be considered a business? The Interim Final Rules issued by the SBA on April 2, 2020 provide that a small business is defined in Section 3 of the Small Business Act (15 USC 632), which provides that “a small-business concern, including but not limited to enterprises that are engaged in the business of production of food and fiber, ranching and raising of livestock, aquaculture, and all other farming and agricultural related industries, shall be deemed to be one which is independently owned and operated and which is not dominant in its field of operation.” The Interim Final Rules further provided that businesses listed in 13 CFR 120.110 **are not eligible** for PPP loans, which notably includes “**passive businesses owned by developers and landlords that do not actively use or occupy assets or improved with the loan proceeds** (except Eligible Passive Companies under 13 CFR 120.111).” **Therefore, landlords that solely collect rent from tenants that are not otherwise an operating business will not be eligible for PPP loans.** An example that illustrates this issue is a common arrangement whereby a group of doctors each own 100% of an S-corporation that in turns owns an equal percentage of a medical practice partnership. The statute only provides that the loans and \$10,000 grant are limited to one grant or loan per EIN, so can each separate S-Corporation apply for and receive the \$10,000 EIDL grant and considered as a separate business, or will only the medical practice partnership be eligible as a "business" to receive the loan? It is likely that only the medical practice partnership will be eligible as the “business”, but this is not entirely clear.

You must file timely as the loans will be granted - first come first serve.

One place to start and the one we used is at <https://www.fundera.com/>

We hope this helps you find the funding you need to weather this Corona virus storm.

*Freed & Shepherd, P.C.*