June 15, 2020

[Important Updates]: The President Signs PPP Reform Bill: Loosening PPP Use and Forgiveness Standards and Expands Payroll Tax Deferral

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Original article released on June 5, 2020. This has been updated as of June 15, 2020.

Today, June 5, 2020, the President signed into law H.R.7010 that extends and modifies provisions of the Paycheck Protection Program (PPP). The following changes have been made to the PPP:

- **Extension of the Covered Period.** The bill extends the covered period for purposes of loan forgiveness from eight (8) weeks to twenty-four (24) weeks after the origination of the loan (or December 31, 2020, if earlier).
    - This will make it much easier for employers with longer recovery periods to use the PPP loan money to stay in business. However, some employers that may have spent all or a larger portion of their funding rehiring employees without work will now be spread thinner than if they had planned for the longer period.
    - The “covered period” concept is used for numerous purposes throughout the PPP. As a result, there will be other consequences associated with this change in terms of loan forgiveness.
    - This extension of the covered period of the loan does not impact the total amount of proceeds received.
- **New Forgiveness Limitations.** Under the bill, loan forgiveness is now contingent upon using at least 60 percent of the loan proceeds on payroll costs. The bill

also indicates that up to 40 percent of the loan proceeds may be used on payment of interest on any covered mortgage obligation (which does not include any prepayment of or payment of principal on a covered mortgage obligation), any payment on any covered rent obligation, or any covered utility payment.

- We expect that the SBA will recognize that this should replace both of the regulations that added similar, but more stringent requirements. The first was the SBA regulatory requirement to use 75 percent of the loan proceeds on payroll costs and the second was that no more than 25 percent of the forgiveness could be attributable to mortgage interest, covered rent, or covered utilities.
  - **UPDATE:** The SBA has issued regulations interpreting the PPP Flexibility Act to mean that 60 percent of the loan forgiveness must be attributable to payroll costs (with no more than 40 percent attributable to nonpayroll costs allowed under the CARES Act).
- It is critical to note that the PPP and the regulations have not previously made loan forgiveness explicitly contingent upon the use of the loan proceeds for payroll costs. It is unclear whether this bill would change existing SBA regulations in manner that would make forgiveness of **any portion of the loan** contingent upon meeting the 60 percent payroll cost requirement. Further guidance on this issue is required. Again, employers that have already used their proceeds in compliance with the prior rule will see little benefit from this feature modification.
  - **UPDATE Adjustment to Loan Forgiveness Regulation:** The SBA has issued regulations interpreting this portion of the PPP Flexibility Act as NOT providing for a "cliff" with respect to forgiveness. Instead, if a borrower uses less than 60 percent of its PPP loan for payroll costs, it will receive partial forgiveness. The borrower would receive partial forgiveness based on the requirement that 60 percent of the forgiveness amount must be attributable to payroll costs. The new regulations provide the following helpful example: "…if a borrower receives a $100,000 PPP loan, and during the covered period the borrower spends $54,000 (or 54 percent) of its loan on payroll costs, then because the borrower used less than 60 percent of its loan on payroll costs, the maximum amount of loan forgiveness the borrower may receive is $90,000 (with $54,000 in payroll costs constituting 60 percent of the forgiveness amount and 36 percent in nonpayroll costs constituting 40 percent of the forgiveness amount)."
  - **UPDATE Adjustment to Use of Loan Proceeds Regulation:** In the same regulations, the SBA retained the payroll costs "use" requirement, but changed it from 75 percent to 60 percent. Although still unclear, we expect that the proper reading of this provision (which is separate from the loan forgiveness provisions discussed in the previous bullet point) is that borrowers must use at least 60 percent of their loan proceeds on payroll costs before December 31, 2020 (even if they did not meet the 60 percent threshold during the covered period). The result of failing to do so is also unclear, but it would not appear to include any loss of loan forgiveness other than as discussed in the previous bullet point.

Instead, we expect that such borrowers could potentially be pursued by the SBA for "misuse" of PPP loan proceeds.

- **Payroll Tax Deferral Now Allowed for PPP Loan Recipients.** Under the CARES Act, employers may defer a portion of their social security taxes for payment in a later year. Originally, this rule ceased to apply to a PPP loan receipt once they received forgiveness. That limitation is removed by this bill.

- **Modifications to the Rehire Rule.** The bill modifies the rule regarding rehires so that the rehire date is now December 31, 2020. The rehire rule mitigates the impact on loan forgiveness of having laid-off employees during the covered period.

    - This might not be a favorable change for some employers who were planning on a June 30, 2020 rehire date. Simply as a matter of order of operations, rehires will need to occur before a borrower applies for forgiveness.

- **Additional Relief from Limitations on Forgiveness.** The bill provides additional relief from the forgiveness reduction rules that normally applies if headcount is reduced during the covered period. Under the new rule, forgiveness will be determined without regard to a proportional reduction in full-time equivalent employees if the borrower can provide good faith documentation of either:

    - An inability to rehire individuals who were employees on February 15, 2020 and an inability to hire similarly qualified employees for unfilled positions on or before December 31, 2020; or

    - An inability to return to the same level of business activity as such business was operating at before 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 customer safety requirement related to COVID-19.

        - The latter standard is new but notably does not apply to state and local regulations that may be have prevented a business from returning to the same level of business activity.

- **Optional Applicability of 24 Week Covered Period.** Under the bill, a borrower that received a covered loan before the date of this new bill may elect to instead apply the 8 week covered period.

    - Some employers that were planning layoffs or furloughs after the end of the 8-week covered period may now also be forced to reevaluate such plans if they do not elect to apply the 8-week covered period. For example, some employers may have to perform a cost-benefit analysis as to whether to accept the 24-week covered period and increase the potential forgiveness (but then be unable to make any layoffs or furloughs for another 4 months without adversely affecting the potential loan forgiveness) or elect to keep the

8-week covered period, use as much of the PPP money as possible within such 8-week period and then make layoffs or furloughs immediately thereafter to preserve cash.

- **Increase Loan Maturity for New Loans.** The bill adds a minimum maturity period for PPP loans of five years. The original statute did not have a minimum and the SBA set the initial maturity for loans at two years. It is important to note that this does not apply to existing PPP loans unless the lender and the borrower mutually agree to modify the loan.

- **Deadline for Commencement of Loan Payments.** If a borrower fails to apply for forgiveness within 10 months after the last day of the covered period (for forgiveness purposes) ends, the borrower must make payments of principal, interest, and fees on such covered loan beginning on the day that is not earlier than the date that is 10 months after the last day of such covered period.

Congress has authorized a total of $669 billion for the PPP. As of June 3, 2020, about 4.5 million loans have been approved totaling about $510.6 billion.

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