



CURRENT GUIDANCE ON THE USE AND FORGIVENESS OF PAYCHECK PROTECTION PROGRAM FUNDS

May 6, 2020

Now that lenders have started to advance funds under the Paycheck Protection Program (“PPP”), recipients of those funds need to turn their focus to the proper use of PPP funds and the measures that can be taken to maximize the debt forgiveness feature of PPP loans.

The information in this alert is derived from the CARES Act and all available guidelines released by the Small Business Administration (“SBA”) and U. S. Department of Treasury as of the date of this alert. Please be aware that even with these resources, a multitude of unanswered questions remain regarding many aspects of the PPP - particularly the forgiveness process. In the Interim Final Rule implementing the PPP published in the Federal Register on April 15, 2020, the SBA indicated that it would be issuing additional guidance on loan forgiveness and when that guidance is released, we will update the information contained in this alert accordingly.

HOW CAN I USE MY PPP LOAN FUNDS?

Funds received under the PPP can only be used to pay the following “allowable expenses”:

- payroll costs
- costs related to the continuation of group health care benefits during periods of paid sick, medical, or family leave, and insurance premiums
- mortgage interest payments relating to a mortgage on real or personal property in existence before February 15, 2020 (but not prepayments or principal payments)
- rent payments under a lease in force before February 15, 2020
- payments for utilities (electricity, gas, water, transportation, telephone, or internet access) for which service began before February 15, 2020
- interest payments on any other debt obligations that were incurred before February 15, 2020
- refinancing an SBA EIDL loan received between January 31, 2020 and April 3, 2020

If you use PPP funds for unauthorized purposes, the SBA will direct you to repay those amounts. If you knowingly use the funds for unauthorized purposes, you will be subject to additional liability, including fraud. If one of your shareholders, members or partners uses PPP funds for unauthorized purposes, the SBA will have recourse against such shareholder, member or partner for the unauthorized use.

HOW CAN MY PPP LOAN QUALIFY FOR FORGIVENESS?

As mentioned, we expect further guidance on PPP loan forgiveness, but at this point borrowers are without clear direction on many aspects. What follows is the best guidance we can provide at this time regarding the use of PPP funds to most effectively maximize forgiveness.

You will be eligible for forgiveness of the full principal amount of your PPP loan and any accrued interest provided you utilize all of the loan proceeds for the “forgivable expenses” over the eight-week period beginning on the date your lender advances your PPP loan. Under the PPP, you will not be responsible for repayment of your loan to the extent you utilize your PPP proceeds for these expenses and your employee headcount and compensation levels are maintained. You should be acutely aware of the dates between which your use of PPP funds will be eligible for forgiveness.

While there is significant overlap between “allowable” and “forgivable” expenses, the categories of expenses eligible for forgiveness are more limited and include:

- payroll costs
- interest (but not prepayments) on a mortgage in effect before February 15, 2020
- rent payments under a lease in force before February 15, 2020
- utility payments for services in effect before February 15, 2020

Forgivable expenses do not include (i) costs related to the continuation of group health care benefits during periods of paid sick, medical, or family leave, and insurance premiums, and (ii) interest (but not prepayments) on any other debt obligations, both of which are allowable loan uses.

To qualify for maximum forgiveness, 75% of your PPP funds must be used for payroll costs during the eight-week period. While the current guidance is unclear, if a borrower utilizes less than 75% of their PPP funds for qualified payroll expenses, they may face a proportional reduction in loan forgiveness.

The SBA has announced that no more than 25% of your loan forgiveness amount may be attributable to non-payroll costs. However, borrowers looking to maximize those costs are - for the moment - forced to plan and make those expenditures notwithstanding a lack of specific SBA instruction. Among other things, guidance is anticipated as to whether forgivable lease expenses will include equipment rental payments and rent paid to related parties. Additionally, we expect there will be further clarification of the types of “utilities” that can be categorized as forgivable expenses.

After your “forgivable amount” is determined by calculating your eligible expenditures during the eight-week period, the amount eligible for forgiveness can be reduced under any of the following circumstances:

- you employ fewer full-time equivalent (FTE) employees during your eight-week period than you did during your “Base Period,” which, at your option, can be either February 15, 2019 through June 30, 2019, or January 1, 2020 through February 29, 2020
- the salary or wage of an employee is less than 75% compared to the most recent full quarter before your eight-week period (this only applies to employees who made less than \$100,000 in 2019)

Any headcount reduction or wage reduction will cause a proportionate reduction in your PPP loan forgiveness. However, any such reduction that occurred between February 15, 2020, and April 26, 2020 will be ignored if the number of FTEs or wage of a given employee is restored by June 30, 2020. For the moment, it is unclear whether the reduction will be ignored completely (or subject to a pro rata reduction) if the restoration occurs at or near the end of the eight-week period or after the eight-week period, but before June 30, 2020.

In addition, many other questions remain surrounding headcount reduction and loan forgiveness, including whether reductions unrelated to the COVID-19 crisis (such as retirements, voluntary employee departures or terminations due to poor performance) will be ignored for the purposes of the headcount calculation. At the moment, it does not appear that there is relief for a borrower that reduced headcount for a non-COVID-19 related reason. There is also uncertainty as to whether a 30 hour or 40 hour per week standard will be used to determine a borrower’s number of FTEs.

Ultimately, under current SBA guidelines, your PPP lender will make the final determination on what amounts will be forgiven.

HOW SHOULD I TRACK MY USE OF PPP LOAN FUNDS?

You should immediately start tracking and gathering data and documenting all your expenditures to maximize forgiveness through the appropriate use of your PPP funds. You must also keep track of the ratio between payroll and non-payroll expenses (mindful of the 25% limitation with respect to non-payroll expenses).

While neither the loan forgiveness application nor further details about the forgiveness process are available, it is a certainty that you will be required to present complete and thorough proof of the proper usage for your PPP funds.

When applying for loan forgiveness, you must be prepared to verify the number of your FTE employees and to provide support for employee pay rates, which could include documentation such as Form 941 quarterly tax filings and payroll reports and registers. You must also be

prepared to provide proof of expenditures on eligible mortgage, lease and utility payments, which could include cancelled checks, payment receipts and copies of vendor invoices.

WHAT IF PART OF MY PPP LOAN IS NOT FORGIVEN?

Any portion of your PPP loan that is not forgiven must be paid back within two years of the date of funding and will bear interest at the rate of 1% per annum. Payments are deferred for six months, although interest will continue to accrue. Any outstanding loan amount can be prepaid at any time, without penalty.

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If you have any questions concerning PPP loans and the forgiveness process, please contact any of the undersigned or your regular Warshaw Burstein attorney.

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| Frederick R. Cummings, Jr. | fcummings@wbny.com | (212) 984-7807 |
| Pankaj Malik | pmalik@wbny.com | (212) 984-7742 |
| Steve Semian | ssemian@wbny.com | (212) 984-7764 |
| Kyle A. Taylor | ktaylor@wbny.com | (212) 984-7797 |

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