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ALERT: AMENDMENT TO CARES ACT ADDS FLEXIBILITY TO PAYCHECK PROTECTION PROGRAM

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On Wednesday night, June 3, 2020, the Senate gave unanimous consent to the Paycheck Protection Program Flexibility Act of 2020 (the "PPPFA"), passed last week by the House, clearing it for the President's signature. It contains an important *election* described in paragraph 2 below that may benefit certain borrowers. The PPPFA provides the following changes to the Paycheck Protection Program ("PPP") loan rules and requirements originally established in March 2020 under the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act"):

– **Allocation of Use of Loan to Payroll Costs Reduced**. The PPPFA provides that the borrower shall use at least 60% of the loan proceeds on payroll costs and up to 40% of the proceeds may be used for other qualified costs. This overrides prior SBA guidance requiring that at least 75% of the loan proceeds be used for payroll costs, and restricted the forgiveness amount for other qualified costs to one–third of payroll costs. This may mean that no forgiveness can occur if less than 60% of the loan is used for payroll costs. Further clarification may be needed.

– **Covered Period for Spending is Extended for Loan Forgiveness**. The eight (8) week period in which to spend loan proceeds to obtain forgiveness is extended to the earlier of twenty-four (24) weeks or December 31, 2020; however, the borrower *may elect* to retain eight (8) weeks as its covered period. Using the extended period may not always be advisable as there can be unintended consequences. Factors to consider are whether there may be additional furloughs or wage reductions after the eight (8) week period that could reduce loan forgiveness, or whether the borrower intends to rely on safe harbors of restoring full-time equivalent employees ("FTEs") or certain wage reductions, discussed below. Careful consideration should be given to which period is likely to produce the best result.

– **Safe Harbor Period to Restore Full-Time Equivalent Employee Numbers is Extended**. The safe harbor time period to rehire or replace employees to February 15, 2020 FTE numbers to avoid reduction in loan forgiveness is extended to no later than December 31, 2020, instead of no later than June 30, 2020. Note that if the election is made to use an eight (8) week period, the safe harbor for rehires remains no later than June 30, 2020.

– **Safe Harbor Period to Restore Wage Cuts is Extended**. The CARES Act provides for loan forgiveness reductions due to wage cuts in excess of 25% (during the covered period compared to their first quarter 2020 annualized wages) to employees with annualized earnings of no more than $100,000. The time period to fully restore wage levels for these employees to avoid reduction in loan forgiveness, including by rehiring furloughed employees, is extended to no later than December 31, 2020, instead of no later than June 30, 2020. Note that if the election is made to use an eight (8) week period, the safe harbor for wage restoration remains no later than June 30, 2020. This is one of the most complex of the necessary calculations to retain loan forgiveness. Using the extended period of twenty-four (24) weeks may not always be advisable for this calculation as there can be unintended consequences.

– **Certain Reductions in FTEs Can be Disregarded**. The PPPFA codifies two (2) circumstances (which must be documented) where the amount of loan forgiveness can be determined without regard to a proportional reduction in the number of FTEs. The two (2) circumstances are (A) (i) an inability to rehire individuals who were employees on February 15, 2020; and (ii) an inability to hire similarly qualified employees for unfilled positions on or before December 31, 2020; or (B) an inability to return to the same level of business activity as such business was operating before February 15, 2020, due to compliance with requirements established or guidance issued by Health and Human Services, the CDC, or OSHA during the period beginning March 1, 2020 and ending December 31, 2020, related to maintenance of standards for sanitation, social distancing, or any other marker or customer safety requirement related to COVID-19.

– **Application Period**. It extends the application period for a PPP loan from June 30, 2020 to December 31, 2020.

– **Loan Term**. The PPPFA provides for a minimum loan term of five (5) years, instead of the two (2) year term set by the Small Business Administration ("SBA"), but only for loans made after the date of enactment; however, it provides that nothing shall prohibit borrowers and lenders from agreeing to extend the current two (2) year maturity to conform to this minimum requirement. Thus, the borrower of an existing loan must approach its lender to seek this extended maturity if desired.

– **Extension of Deferral Period for First Payment on Unforgiven Loan Portion**. Currently, the CARES Act provides that no loan payments will be due for a period of not less than six (6) months and not more than one (1) year. The PPPFA changes the deferral of payments to the date on which the amount of loan forgiveness determined is remitted by the SBA to the lender, which will likely be more than six (6) months. If a borrower fails to apply for forgiveness within ten (10) months of the end of its covered period, payments shall begin on the date that is not earlier than the date that is ten (10) months after the last day of such covered period. Borrowers of existing loans should consult with their lenders to confirm the revised deferral period, which will be different from the terms of the existing note.

Employers Can Continue to Defer the Employer Share of Social Security Tax (6.2%) Past the Date of Loan Forgiveness. The previous restriction on utilizing the CARES Act provision to defer the employer share of Social Security tax through the earlier of the date of loan forgiveness or December 31, 2020 has been deleted. Therefore, employers with PPP loans can continue to defer this tax through December 31, 2020, which deferral is then payable 50% on December 30, 2021 and 50% on December 31, 2022.

If you have any questions or require more information regarding this update or PPP loans in general, please contact one of our Tax Department Members John W. Schmehl, Esq., Matthew I. Whitehorn, Esq., or Stephanie S. Vogel, Esq., or our Team Ventilator Member William P. Hunter, Esq.