

## WHAT PPP BORROWERS NEED TO KNOW ABOUT NEWLY ENACTED CHANGES

Payroll Protection Program (“PPP”) borrowers should take heed of new changes to the PPP loan program made by the Paycheck Protection Program Flexibility Act (the “Flexibility Act”), which the President signed into law on June 5, 2020. The Flexibility Act significantly benefits PPP borrowers by providing additional time and flexibility as to loan terms and forgiveness. We have not yet received definitive regulatory guidance on the Flexibility Act; however, on June 8, 2020 the SBA and Treasury issued a joint press release (the “Joint Press Release”) stating that they will promptly issue additional guidance and modified loan and forgiveness applications to interpret and implement the changes to the PPP reflected in the Flexibility Act.

Specifically, the Flexibility Act contemplates the following changes to the PPP loan program:

1. **Loan Terms Extended from 2 Years to 5 Years (New Loans Only)**. All PPP loans made on or after the date of the Flexibility Act will have a minimum term of five years. All pre-existing PPP loans will continue to have two-year terms, unless modified by mutual agreement between the lender and borrower.
2. **Borrowers May Apply a Greater Percentage of PPP Loan Funds to Eligible Non-Payroll Costs**. Under the pre-Flexibility Act framework, PPP funds could only be spent on eligible payroll and non-payroll expenses<sup>1</sup> and no more than 25% of the amount for which forgiveness is sought could be attributable to eligible non-payroll expenses. Under the Flexibility Act, the 25% limitation on non-payroll expenses is relaxed to 40% (borrowers can spend proportionally more on non-payroll expenses). The Flexibility Act provides that “to receive loan forgiveness..., an eligible recipient shall use at least 60 percent of the covered loan amount for payroll costs, and may use up to 40 percent ... for [eligible non-payroll costs].” This change applies to all PPP loans, including those that pre-date the Flexibility Act.

*Note:* The phrase “shall use at least 60 percent of the covered loan” implies that a borrower *must* spend a minimum amount of its loan to receive forgiveness; *however*, the Joint Press Release stated that “[i]f a borrower uses less than 60 percent of the loan amount for payroll costs during the forgiveness covered period, the borrower will

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<sup>1</sup> Eligible non-payroll costs consist of (a) payments of interest (not prepayment) under real or personal property mortgages that were in place as of February 15, 2020; (b) rent or lease payments under lease agreements for real or personal property that were in place as of February 15, 2020; (c) payments for electricity, gas, water, transportation, telephone, or internet utilities for which service began prior to February 15, 2020.

continue to be eligible for partial loan forgiveness, subject to at least 60 percent of the loan forgiveness amount having been used for payroll costs.” The Joint Press Release indicates that instead of enforcing a threshold requirement that borrowers spend 60 percent of their *entire loan amounts* on eligible payroll costs to be eligible for forgiveness; the SBA will simply cap forgiveness at (i) the amount of eligible payroll costs spent during the covered period, *divided by* (ii) 60 percent.

3. **8-Week “Covered Period” Extended.** Under the pre-Flexibility Act framework, PPP funds properly expended during the 8-week “covered period” following loan disbursement were eligible for forgiveness. The Flexibility Act extends the window of time during which PPP funds can be used while maintaining eligibility for forgiveness. Specifically, the new “covered period” commences on the date loan proceeds are disbursed and continues until the earlier of (a) December 31, 2020, and (b) 24 weeks following loan disbursement (the “Flexibility Act’s Covered Period”). The Flexibility Act’s Covered Period applies to all PPP loans; however, borrowers that obtained PPP loans prior to enactment of the Flexibility Act have the option to utilize the previously allotted 8-week covered period, if desired.
4. **Safe Harbor Deadline to Restore Employment Levels Extended.** Under the pre-Flexibility Act regulations, borrowers could avoid certain reductions to their forgiveness amount by restoring the number of full time equivalent employees and/or restoring wages to pre-pandemic levels (i.e., as of February 15, 2020) by a deadline of June 30, 2020. The Flexibility Act extends the June 30, 2020 deadline to December 31, 2020. The extended deadline applies to all PPP loans, regardless of whether they pre-date the Flexibility Act.
5. **Forgiveness Available to Borrowers who are Unable to Return to Pre-Pandemic Employment Levels Due to Documented Inability and COVID-19 Compliance.** Under the pre-Flexibility Act framework, unless the applicable safe harbor applies, forgiveness is reduced in proportion to the decrease in the number of full time equivalent employees (“FTEs”) that a borrower employs during the “covered period,” as compared to the number of FTEs employed as of February 15, 2020 (the “FTE Reduction Penalty”). Under the Flexibility Act, an FTE Reduction Penalty does not apply in instances where a borrower documents, in good faith, that (a) it is unable to re-hire individuals who were employees on February 15, 2020, and is unable to hire similarly qualified employees for unfilled positions by December 31, 2020, or (b) is unable to return to its pre-February 15, 2020 level of business activity due to compliance with certain pandemic-related requirements and guidance issued by the Occupational Safety and Health Administration, the Centers for Disease Control and Prevention or Health and Human Services. This change applies to all borrowers, regardless of whether their loan pre-dates the Flexibility Act.

Note: While the language in the Flexibility Act suggests that satisfaction of one of the safe harbors described above would provide a complete exemption from an FTE Reduction Penalty, the Joint Press Release suggests that the SBA and Treasury interpret this section to only provide for a partial exemption from an FTE Reduction Penalty, which will be “based on” reductions in FTEs for the reasons described in the safe harbors.

6. **Loan Payment Deferment Period Extended.** The pre-Flexibility Act regulations provided a 6-month deferment period during which no PPP loan payments were due. Under the Flexibility Act, instead of a 6-month deferment period, payments are now deferred until the SBA remits the forgiven amount to the lender. Nevertheless, if a borrower fails to apply for forgiveness within 10 months following the end of the Flexibility Act's Covered Period, then the borrower must begin making loan payments at that time. The new deferment period applies to all loans, regardless of whether they pre-date the Flexibility Act.

*Note:* While the above-referenced change assures that loan payments will not be due prior to forgiveness, borrowers that obtain forgiveness within 6-months of obtaining a PPP loan and do not obtain 100% forgiveness could encounter a shorter deferment period than they may have originally anticipated.

7. **Deferrable Payroll Taxes.** Under the CARES Act, businesses may defer certain payroll taxes 50% to the end of 2021 and 50% to the end of 2022. PPP borrowers that obtain loan forgiveness were previously ineligible for the deferral. Under the Flexibility Act, all PPP borrowers are now eligible for the payroll tax deferral, regardless of whether they obtain forgiveness. This change applies to all PPP borrowers, regardless of whether their loan pre-dates the Flexibility Act.
8. **Waiver of SBA's Annual Fee.** Under the pre-Flexibility Act framework, the SBA's annual fee (charged to borrowers) was waived through June 30, 2020. Under the Flexibility Act, the fee waiver continues until the later of (a) the end of the Flexibility Act's Covered Period; and (b) the date on which the forgiven amount is paid to the lender by the SBA (except where the borrower fails to apply for forgiveness within 10 months of the end of the Flexibility Act's Covered Period). This change applies to all PPP loans, regardless of whether the loan pre-dates the Flexibility Act.

We continue to monitor developments and remain ready to assist you and your business in navigating these unprecedented times. Please feel free to consult with us for any questions or assistance. For SBA and government-backed lending specific questions, please reach out to a member of our SBA team:

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