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PPP Flexibility Act - Welcome Changes

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After significant speculation and discussion (which began almost the moment the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) was signed into law back in March), Congress passed the Paycheck Protection Program Flexibility Act of 2020 (Flexibility Act) and President Trump signed the Flexibility Act into law on June 5, 2020. The Flexibility Act addresses significant issues with the Paycheck Protection Program (PPP) created by the CARES Act by making many changes to the PPP, some of which apply only to those loans issued going forward and some that apply retroactively to all borrowers. Most of the revisions are borrower friendly and will be helpful to a borrower trying to maximize the forgiveness aspect of its PPP loan. Below is a highlight of some of the key changes and additions under the Flexibility Act.

A. Maturity for Loans

The Flexibility Act extends the term for all new PPP loans going forward. Instead of a twoyear loan, the Act revises the term to a minimum of five years. This only applies to PPP loans issued after the date of enactment. However, the Flexibility Act adds that lenders and borrowers of previously issued PPP loans could mutually agree to modify the terms of their existing loans to incorporate the longer 5-year maturity term.

B. Amendments to Forgiveness

The Flexibility Act changes the “covered period” for both use of the loan and for the forgiveness application. Unlike the extended maturity, these changes are applied retroactively to all PPP loans regardless of when the loan was applied for or issued.

1. Period to Use Borrowed Funds. In its original form, the CARES Act limited the use of the funds distributed under PPP loans, and required that all borrowed funds be used by June 30, 2020. The Flexibility Act revises that period so that borrowed funds can be used on the allowed expenses through December 31, 2020. This gives borrowers an additional six months to use the funds borrowed under the PPP program.

2. Covered Period for Calculating Forgiveness of PPP Funds. One of the most significant changes in the Flexibility Act is the extension of the period of time to use the borrowed funds and still be able to seek forgiveness. The CARES Act required that, in order to qualify for forgiveness, borrowed funds had to be used in the first 8 weeks after the loan was issued. That period is extended to the earlier of December 31, 2020 and the 24 week period after the origination of the loan. A borrower can still elect to have the 8 week period govern its PPP loan, which might be a consideration if a borrower anticipates changes to its workforce or a reduction in employee pay or salary workforce in the time covered by the 24 week period. If a borrower elects the 24 week "covered period" that period also impacts the potential reductions to forgiveness because of reductions to employee headcount or material reductions in employee pay. 2

3. New Ways to Avoid Reduction in Forgiveness. The Flexibility Act also creates two new ways for borrowers to avoid a reduction in the amount forgiven due to reduction in full time equivalent employees. Under the CARES Act and subsequent rules promulgated by the SBA, the amount of a PPP loan eligible for forgiveness is reduced if a borrower suffers a reduction in the average number of FTEEs during the covered period. The Flexibility Act creates new exemptions to that reduction in forgiveness if the loss of FTEEs is documented and attributable to either (a) the inability to hire prior employees or similarly qualified employees by December 31, 2020; or (b) an inability to return to the same level of business activity due to compliance with HHS, CDC or OSHA guidance or requirements related to sanitation, social distancing or other safety requirements related to COVID-19. The Flexibility Act does not give much guidance on how these exemptions will apply and it will be interesting to see how the SBA interprets these provisions in its future guidance. Also, the Flexibility Act extends from June 30, 2020, until December 31, 2020, the end period during which borrowers can rehire employees and thereby limit reductions in forgiveness.

C. Change to the Limitation of Forgiveness for Non-Payroll Costs

When the CARES Act was passed, there was no requirement on what portion of forgivable funds had to be applied to payroll costs. However, the SBA quickly by guidance and then interim rules required that borrowers use at least 75% of the amount forgiven on payroll costs. The Flexibility Act essentially overrules the SBA's rulemaking on this point and provides that only 60% of the amount forgiven is required to be used on payroll costs. This change may relieve many borrowers in high-rent districts of a burden that limited the total amount forgivable and may be particularly beneficial to restaurants, bars, and retail stores. Of course, borrowers can use more than 60% of the forgiven amount on payroll costs, without any issue.

D. Change to the Deferral Period

An issue that many early borrowers had under the CARES Act was the possibility that their first payment on the PPP loan could become due prior to the borrowers learning how much of the loan would be forgiven. To prevent this situation, the Flexibility Act defers payment on the loan until the date that the borrower learns the amount of forgiveness.

Borrowers are not required to seek forgiveness of PPP loans, although the expectation is that most will seek to have at least some portion forgiven. For those borrowers who do not apply for forgiveness under the program, the loan deferment period lasts until 10 months after the applicable covered period expires. For borrowers using the 24 week covered period, this means that payment could be deferred up to nearly 16 months if they do not seek forgiveness. However, borrowers who have already received their PPP funds should be aware that if they are unable to negotiate an extension to the maturity date, 3 they will have only 8 months to pay off the entire balance of the loan if they do not seek forgiveness, which could leave borrowers with some hefty monthly payments.

E. Payroll Tax Deferral Permitted Regardless of Forgiveness

As discussed in a prior advisory (available here), the CARES Act allows employers to defer payment of the employer's share of the Social Security tax on wages paid beginning on March 27, 2020 and ending on December 31, 2020 ("Qualified SSI Taxes"). The deferred Qualified SSI Taxes are payable to the IRS in two installments, with 50% of such taxes being due on December 31, 2021, and the remainder due on December 31, 2022.

Under the CARES Act, an employer that received a PPP Loan was allowed to defer Qualified SSI Taxes, but only for taxes that were due to the IRS prior to the forgiveness of the PPP Loan. Any Qualified SSI Taxes that were due to the IRS after forgiveness were not eligible for deferral. The Flexibility Act eliminates the CARES Act rule that prevented continued deferral following PPP Loan forgiveness. Accordingly, an employer that receives a PPP Loan is eligible to defer Qualified SSI Taxes both before and after forgiveness of its PPP Loan. This new rule applies to all PPP Loans.

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