

OBSERVATIONS

CARES Act – Loan Forgiveness Interim Final Rules 2

May 29, 2020

On Friday, May 22, the Small Business Administration (SBA) released an Interim Final Rule (IFR) for the requirements of Loan Forgiveness under the CARES Act. Procedurally, the IFR is subject to public comment for 30 days before it can become final.

The SBA has already released the Paycheck Protection Program (PPP) Loan Forgiveness Application (“Forgiveness Application”). The Application can be found at <https://home.treasury.gov/system/files/136/3245-0407-SBA-Form-3508-PPP-Forgiveness-Application.pdf>.

The application itself has directions and guidance which is also referenced in this blog.

The SBA also released a 19 page interim final rule with respect to Review Procedures and Related Borrower and Lender Responsibilities (SBA Review Procedures).

We will provide several blogs to address the issues raised in the IFR. This blog will address:

- Non-Payroll Costs including:
 - Timing for determination of forgivable amounts
 - Definitions of non-payroll costs

Non-Payroll Costs are addressed on pages 12-13 of the IFR. The IFR generally provides information on the “timing” of costs that are eligible for forgiveness; specifically, it provides that costs are eligible if they are:

1. Paid during the covered period; or
2. Incurred during the covered period and paid on or before the next regular billing date, even if the billing date is after the covered period.

Based on this guidance, it appears that if a bill for a non-payroll cost was incurred prior to receiving PPP funds and paid during the covered period, it would be a forgivable cost. Costs incurred within the eight week period after receipt of the loan proceeds (“covered period”) and paid during the covered period or on the next regular billing cycle after the covered period, would also be eligible for forgiveness. If the invoice is paid after the close of the covered period, only the portion incurred up to the end of the covered period is eligible.

The guidance provides the following example:¹

1. PPP Loan proceeds are received June 1, so eight weeks ends July 26.
2. May bill was for costs incurred prior to receipt of loan but paid June 1; this amount is forgivable because it was paid within the covered period.
3. The June bill paid July 1 is forgivable as this was incurred and paid in the covered period.
4. The July bill paid on August 1, the next regular billing cycle for the bill, is partially forgivable. Even though this was paid after the covered period ended, the costs up to July 26 are still forgivable.

The guidance specifically notes that prepayments of interest on mortgage obligations are not eligible for loan forgiveness.² Payments of mortgage principal are not eligible. The IFR does NOT specifically reference prepayments of other non-payroll costs paid during the covered period. Also, the IFR notes that the SBA is looking to provide some simplification to the process and that the “25 percent cap on non-payroll costs will avoid excessive inclusion of non-payroll costs”.³ The general consensus, however, is that prepayment of costs would not be allowed for any payroll or non-payroll cost. Hopefully more guidance will be provided to absolutely clarify and confirm this point.

While the IFR does not provide any additional guidance on the definition of eligible non-payroll costs, the SBA Loan Application provides the following:

- Non-payroll costs eligible for forgiveness consist of:
 - (a) covered mortgage obligations: payments of interest (not including any prepayment or payment of principal) on any business mortgage obligation on real or personal property incurred before February 15, 2020 (“business mortgage interest payments”);
 - (b) covered rent obligations: business rent or lease payments pursuant to lease agreements for real or personal property in force before February 15, 2020 (“business rent or lease payments”); and
 - (c) covered utility payments: business payments for a service for the distribution of electricity, gas, water, transportation, telephone, or internet access for which service began before February 15, 2020 (“business utility payments”).

The application clearly indicates that internet access is included among covered utility payments along with other items so long as services began prior to February 15, 2020. Other costs, however, are still a little murky relative to what may be included, particularly transportation.

¹ SBA IFR Section 4, pg. 12

² SBA IFR Section 4, pg. 13

³ SBA IFR Section 4, pg. 13

On April 20, 2020 the SBA issued an interim final rule which provides additional information on non-payroll costs and which can be located at:

<https://www.federalregister.gov/documents/2020/04/20/2020-08257/business-loan-program-temporary-changes-paycheck-protection-program-additional-eligibility-criteria>

Within this guidance, there is reference to non-payroll costs related to self-employed individuals as follows:

“d. How can PPP loans be used by individuals with income from self-employment who file a 2019 Form 1040, Schedule C?

“The proceeds of a PPP loan are to be used for the following...

iii. Mortgage interest payments (but not mortgage prepayments or principal payments) on any business mortgage obligation on real or personal property (*e.g.*, the interest on your mortgage for the warehouse you purchased to store business equipment or the interest on an auto loan for a vehicle you use to perform your business),

business rent payments (*e.g.*, the warehouse where you store business equipment or the vehicle you use to perform your business), and

business utility payments (*e.g.*, the cost of electricity in the warehouse you rent or *gas you use driving your business vehicle*).

You must have claimed or be entitled to claim a deduction for such expenses on your 2019 Form 1040 Schedule C for them to be a permissible use during the eight-week period following the first disbursement of the loan (the “covered period”). For example, if you did not claim or are not entitled to claim utilities expenses on your 2019 Form 1040 Schedule C, you cannot use the proceeds for utilities during the covered period.”

The allowance to use PPP loan funds for “gas you use driving your business vehicles” is not referenced within the current IFR or Loan Forgiveness Application. It is unclear then if this is available to all borrowers or only self-employed individuals as explicitly referenced in the April 20 IFR. Hopefully the SBA will provide definitive guidance on this quickly prior to the filing of applications.

We will provide subsequent blogs shortly that deal with other aspects of the IFR and the SBA Review Procedures.

We encourage businesses to review the Application and work towards addressing the various documentation and calculation requirements so that they can submit their Forgiveness Application soon after the covered period has ended.

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