

Client Alert

June 2020

The Paycheck Protection Program Flexibility Act of 2020 (H.R. 7010)

Legislative Background

On June 5, 2020 (the “*Enactment Date*”), the President signed the Paycheck Protection Program Flexibility Act of 2020 (the “*Flex Act*”), after the Senate approved the House bill without change. While the Flex Act makes welcome improvements to the Paycheck Protection Program (“*PPP*”), implementing administrative guidance remains necessary. On June 8, the SBA issued a press release clarifying a key Flex Act provision on loan forgiveness and outlining its initial regulatory priorities (the “*Press Release*”).

Summary of Flex Act Changes

No Extension of Application Date – In the Press Release, the SBA confirmed that the application window closes on June 30, 2020. A borrower must apply for *and* receive approval of a PPP loan prior to the June 30 deadline.

Effective Date for Flex Act Amendments – Except for the term extension (as discussed below), the Flex Act amendments apply retroactively to loans originated prior to the Enactment Date. The term extension applies only to loans “made” on or after the Enactment Date.

Term Extension – Only for loans made after the Enactment Date, the term is extended from two to five years. The term of a loan originated prior to the Enactment Date (an “*Existing Loan*”) remains at two years, unless the borrower and the lender mutually agree to amend the term (as the Flex Act permits).

Extension of Spending Period – For forgiveness purposes, the spending period for loan proceeds increases from the original 8 weeks to 24 weeks (capped at December 31, 2020) from the first disbursement date. A borrower under an Existing Loan can elect to use the original 8-week spending period (instead of the extended 24-week period), which may be advantageous for a borrower that took action based on original 8-week period.

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Reduction in Required Spending for Payroll Costs – The Flex Act reduces the percentage of loan proceeds that, as a pre-condition to loan forgiveness, a borrower must spend on payroll costs to 60% (down from 75%). In the Press Release, the SBA clarified that a borrower can still qualify for partial loan forgiveness if the borrower uses less than 60% of the loan proceeds for payroll costs, allaying concerns that a payroll spending miss would result in a complete “cliff” loss of loan forgiveness.

Minimum Deferral Period – If a borrower applies for loan forgiveness within 10 months from the end of the borrower’s selected spending period, loan repayment remains deferred until the SBA’s final determination on loan forgiveness. Some have cautioned that an application for loan forgiveness must be made within the 10-month period or not at all. In our view, if a borrower applies for loan forgiveness after the 10-month period, the borrower’s PPP loan will go into repayment mode, and the borrower will have to seek reimbursement for any excess loan repayments as part of the loan forgiveness process. We recommend a borrower file within the 10-month period to avoid running any risk on loan forgiveness.

Deadline Extension for Re-Hiring and Wage Restoration – Under the original provisions of the CARES Act, loan forgiveness is scaled back to reflect lay-offs and wage cuts, unless restored by June 30, 2020. The Flex Act extends the deadline for re-hiring employees and/or restoring wage cuts from June 30 to December 31, 2020.

Relief for Inability to Re-Hire Employees – Under the CARES Act, loan forgiveness is reduced proportionately to reflect any reduction in the borrower’s full-time equivalent (FTE) count during the borrower’s selected spending period (8 or 24 weeks) as compared to borrower’s historic FTE count (as measured over one of two alternative time periods). Under the Flex Act, a lost FTE will not reduce loan forgiveness under the FTE reduction rule, if the borrower in good faith can document either of the following with respect to one or more FTEs:

1. The borrower is unable to (a) rehire a laid-off employee who was on payroll on February 15, 2020, and (b) fill the resulting vacancy with a similarly qualified employee on or before December 31, 2020; or
2. The borrower is unable return to “the same level of business activity the business was operating at before February 15, 2020,” as a result of compliance with health guidelines issued during the February 15 to December 31, 2020 period by a specified federal (not state) agency (i.e., the U.S. Department of Health and Human Services, Centers for Disease Control and Prevention or Occupational Safety and Health Administration).

No Loss of Payroll Tax Deferral – Forgiveness of a PPP loan no longer results in the loss of payroll tax deferral under the CARES Act.

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Open Issues

The Flex Act makes many improvements to the PPP. But additional guidance will be required on various aspects.

1. First and foremost, the interaction of the CARES Act and the Flex Act implies that the expansion of the spending period from 8 to 24 weeks raises the per-employee cap on payroll costs from \$15,385 (8/52 * \$100,000) to \$46,155 (24/52 * \$100,000). Given the importance of this cap in determining loan forgiveness, SBA guidance on this point is crucial.
2. Agreements and other documentation for Existing Loans do not sync with the Flex Act. Unless documentation for an Existing Loan is amended to take into account the Flex Act, a borrower cannot benefit from the Flex Act's improvements and following the Flex Act will put a borrower into default.
3. For tax purposes, a modification of an Existing Loan to reflect the Flex Act will likely result in a constructive cancellation and reissue of the Existing Loan, possibly causing the borrower to recognize debt discharge income. Guidance on this point from the Internal Revenue Service is needed.
4. The relief from rehiring and wage restoration does not apply to state or local restrictions that prevent a borrower from returning to pre-February 15 business activity.

For More Information

Olshan lawyers from multiple practice groups are working together with clients to address COVID-19-related matters, including the CARES Act stimulus programs (i.e., the PPP and EIDL) and other corporate matters, including contractual analysis and financing, tax, restructuring, employee benefits and employment practices, insurance coverage, and litigation. Click [here](#) to access additional materials addressing issues raised by COVID-19.

Please contact the Olshan attorney with whom you regularly work or one of the attorneys listed below if you would like to discuss this client alert or have questions about its content.

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