

September 9, 2020

## LEGAL ALERT

### Developments in Loan Forgiveness for the Paycheck Protection Program ("PPP")

As discussed in previous Legal Alerts, the CARES Act (the "Act") was passed on March 27, 2020, to expand the scope of the Small Business Act in order to provide forgivable Paycheck Protection Loans to allow qualifying employers to meet certain payroll and other related costs. While the Small Business Administration (the "SBA") began accepting forgiveness applications on August 10, 2020, the SBA has continued to issue additional rules to clarify use and forgiveness of PPP loans. This Legal Alert provides an update regarding an interim final rule recently issued on August 24, 2020, that addresses owner-employee compensation, permissible non-payroll costs related to tenants and home-based businesses, and related party rent.

#### Forgiveness for Owner Compensation

The SBA had previously capped the amount of loan forgiveness for payroll compensation attributable to an owner-employee regardless of the owner's equity interest in the borrowing business. Owner compensation was universally limited to the lesser of 15.385% of 2019 compensation or \$15,385 when electing an eight-week covered period, and 20.833% of 2019 compensation or \$20,833 when electing a twenty-four-week covered period. The SBA has now clarified that "an owner-employee in a C- or S-Corporation who has less than a 5 percent ownership stake will not be subject to the owner-employee compensation rule," noting that owners with these fractional shares of an entity "have no meaningful ability to influence decisions over how loan proceeds are allocated." Accordingly, such owner-employees may now receive up to \$46,154 for the 24-week covered period, if otherwise permitted by applicable regulations. As stated, this exception is limited to C- or S-Corporations, and does not apply to partnerships even where a partner has an equity stake of less than five percent.

#### Tenant and Home-Based Business Cost Forgiveness

The SBA clarified that "the amount of loan forgiveness requested for nonpayroll costs may not include any amount attributable to the business operation of a tenant or sub-tenant of the PPP borrower, or for home-based businesses [and] household expenses." As examples the SBA notes that a PPP borrower renting an office building for \$10,000 per month, but subletting a portion of that office for \$2,500 per month, is only eligible for \$7,500 per month in loan forgiveness. The PPP has further clarified that forgiveness is "limited to the share of the fair market value of the space that is not leased out to other businesses." Prorated rent and utilities costs are determined as eligible based on 2019 tax filings, or 2020 tax filings for new businesses.

#### Rent and Mortgage Payments to Related Parties

Rent payments to related parties are forgivable if the requested forgiveness is no more than the mortgage interest attributable to the rented property, and the underlying lease was entered into

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prior to February 15, 2020. Mortgage payments made to a related party are not eligible for forgiveness. Any common ownership between the business and the property owner triggers these requirements.

As detailed in this and previous Legal Updates, SBA guidance has been and continues to be subject to change. Additional governmental regulation could significantly alter the manner in which this program is applied. If you would like to better understand how these regulations might impact your business, we would be happy to schedule a call for further discussion. Please note this summary does not constitute legal or tax advice.