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NEW GUIDANCE CONCERNING EMPLOYEE HEADCOUNT AND HIGHLY PAID PERSONNEL EXPENSES EXPANDS PPP ELIGIBILITY

Please note: *Information in the following advisory was accurate upon its date of publication. However, given the rapidly changing nature of guidance from the Department of the Treasury and others, we recommend you visit the Treasury website and our COVID-19 Resource Center for the latest updates.*

The U.S. Department of the Treasury (the Treasury) has issued new guidance addressing how employee headcount and "payroll costs" impact Paycheck Protection Program (PPP) loan eligibility and the opportunity for forgiveness of PPP loan expenditures for non-cash compensation to highly paid employees. In some respects, this guidance contradicts the limitations that some lenders had imposed on borrowers' calculation of the amount of PPP loans they are eligible to obtain and opens up the possibility that borrowers whose applications have not yet been processed can revise their loan applications to seek additional funds.

SOME NOT-SO-SMALL EMPLOYERS QUALIFY FOR PPP LOANS

Press regarding PPP loans has focused heavily on the 500-employee threshold as a cutoff for loan eligibility. However, the PPP eligibility criteria are far more nuanced. Many industry sectors have much higher headcount thresholds under Small Business Administration (SBA) size standards, which permit companies employing more than 500 workers in those sectors to seek PPP loans.

Furthermore, the question of which workers count toward a company's employee threshold should be considered carefully in lieu of relying on snap judgments about whether a company should or should not count a particular worker when determining PPP loan eligibility. After all, that determination could be worth up to $10 million in the form of a PPP loan. Recent guidance demonstrates that the "normal" rules for which workers count may not always apply in the context of PPP loans. For example, SBA regulations normally direct borrowers to include "the employees of its domestic ***and foreign*** affiliates," *see* 48 C.F.R. § 19.101; however, in its recent guidance, the Treasury explains

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that "a business is eligible for a PPP loan if the business has 500 or fewer employees ***whose principal place of residence is in the United States***, or the business meets the SBA employee-based size standards for the industry in which it operates (if applicable)." Similarly, while the normal SBA rules require a borrower to calculate its employee headcount based on the average number of employees per pay period for the 12 months preceding the loan, the Treasury has relaxed those rules for PPP borrowers, permitting companies to choose between the "normal" approach and the option of using headcount numbers from the 2019 calendar year. These examples demonstrate how paying careful attention to regulatory guidance concerning the PPP may give businesses hovering close to the 500-employee threshold (or another applicable threshold) the chance to claim a game-changing PPP loan. For further information, see our prior analysis of the application of the SBA affiliation rules to PPP loans.

THE PPP EMPLOYEE PAY CAP OF $100,000 APPLIES ONLY TO CASH COMPENSATION

As the SBA started accepting applications for PPP loans on Friday, April 3, some lenders interpreted the CARES Act conservatively to require borrowers to exclude all forms of employee remuneration, including employee benefits, that exceed an annualized rate of $100,000. This approach resulted in a lower PPP loan eligibility for many borrowers who had assumed they could include expense of insurance benefits in "payroll costs" and thus as part of their PPP loan calculations. The Treasury has now adopted a more narrow reading of the cap applying to employees who earn more than $100,000 per year. Under recently released guidance, the cap applies only to "cash compensation." Furthermore, the Treasury has explicitly advised that the following forms of non-cash compensation are excluded from the $100,000 pay cap:

- employer contributions to defined-benefit or defined-contribution retirement plans;
- payment for the provision of employee benefits consisting of group health care coverage, including insurance premiums; and
- payment of state and local taxes assessed on compensation of employees.

Thus, those borrowers who were required by lenders to carve out benefit costs attributable to employees earning annual pay in excess of $100,000, likely could have asked for more money than they did when applying for PPP loans. As we have previously explained, the value of a PPP loan can go up to the lesser of $10 million or 2.5 times the borrower's average monthly "payroll costs," which include the expense of providing group health plan coverage to employees.

AN EMPLOYEE’S SHARE OF FEDERAL PAYROLL TAXES COUNTS AS “PAYROLL COSTS”

The Treasury’s guidance served up yet another big win for employers desperate for PPP funds by announcing that the term “payroll costs” includes an employee’s share of federal payroll taxes. This guidance is based on a narrow reading of the CARES Act’s exclusion of certain federal taxes from the concept of “payroll costs.” The SBA has interpreted that statutory exclusion “to mean that payroll costs are calculated on a gross basis, without subtracting federal taxes that are imposed on the employee or withheld from employee wages.” In contrast, however, a borrower cannot include the employer’s share of federal payroll taxes in its calculation of “payroll costs” for purposes of a PPP loan.

A SECOND BITE AT THE PPP APPLE

Finally, the Treasury guidance authorizes borrowers to go back to their lenders and request a revision to their PPP loan application to seek a larger amount of money if their original application calculated available loan funds using methodology that has proved erroneous under the Treasury’s new guidance. Specifically, the guidance provides that “borrowers whose previously submitted loan applications have not yet been processed may revise their applications based on clarifications reflected in these FAQs.” Thus, for borrowers still waiting for PPP loan applications to be processed, time is of the essence in determining whether more money can be requested.

Armstrong Teasdale attorneys are actively monitoring and providing updates regarding the impact of COVID-19, including the PPP and other provisions of the CARES Act. Should the Treasury or the SBA provide additional guidance, we will be sure to update you.