FAQ No. 44 Causes Panic for Some Borrowers with Foreign Affiliates

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On Wednesday evening, May 6, 2020, the Treasury Department released FAQ No. 44 which seems to reverse earlier guidance (FAQ No. 3) relating to the exclusion of non-U.S. based employees from the headcount number for purposes of determining eligibility for a Paycheck Protection Program (PPP) loan.

Specifically, FAQ No. 44 states:

> **Question:** How do SBA's affiliation rules at 13 C.F.R. 121.301(f) apply with regard to counting the employees of foreign and U.S. affiliates?
>
> **Answer:** For purposes of the PPP's 500 or fewer employee size standard, an applicant must count all of its employees and the employees of its U.S and foreign affiliates, absent a waiver of or an exception to the affiliation rules. 13 C.F.R. 121.301(f)(6). Business concerns seeking to qualify as a "small business concern" under section 3 of the Small Business Act (15 U.S.C. 632) on the basis of the employee-based size standard must do the same.

If your business, together with its domestic and foreign affiliates, had more than 500 employees on average during 2019, and you have received or applied for a PPP loan, we urge you to seek advice from qualified counsel immediately!

Among the options you might want to discuss with counsel are:

1. Return or refuse the funds. (See below for a discussion of the safe harbor rule as it relates to the return of funds.)
2. If you have already taken or deferred action based on receipt of the funds, such as rehiring furloughed workers or deferring lay-offs or salary reductions, you might return the unused funds.
3. Forego forgiveness and repay the entire amount in due course.
4. Apply for forgiveness for only the amount of funds used for incremental costs you incurred based on your receipt of the funds, such as the actions or inactions in 2., above.
5. Retain the funds and apply for forgiveness based on reliance on the guidance in FAQ No. 17 (discussed below).

The History of the Guidance

The Coronavirus Aid, Relief and Economic Security Act (CARES Act or Act) was signed into law on March 27, 2020. The Act seemed to exclude from eligibility any business which, together with its domestic and foreign affiliates, has more than 500 employees or the number of employees listed in the U.S. Small Business Administration's (SBA's) alternative size standards. (Note that the employee count is generally based on the average over the 12 months prior to submitting an application.) On April 2, 2020, the SBA posted Interim Final Rule (IFR) No. 1 which introduced the concept of eligibility for businesses with 500 or fewer employees *whose principal place of residence was in the U.S.* However, due to the use – or perhaps misuse – of "and" and "or," this new guidance was ambiguous.

On April 6, 2020, the SBA published FAQ No. 3, among others, which very *unambiguously* states:

> **Question:** Does my business have to qualify as a small business concern (as defined in section 3 of the Small Business Act, 15 U.S.C. 632) in order to participate in the PPP?
>
> **Answer:** No. In addition to small business concerns, 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).

Relying on this guidance, many businesses with more than 500 worldwide employees (inclusive of affiliates), 500 or fewer of which had a principal place of residence in the U.S., applied for and received PPP loans. As a word of caution, however, Note 1 to the FAQ document states, "This document does not carry the force and effect of law independent of the statute and regulations on which it is based." Despite this caveat, FAQ No. 17, also published on April 6, 2020, states:

> **Question:** I filed or approved a loan application based on the version of the PPP Interim Final Rule published on April 2, 2020. Do I need to take any action based on the updated guidance in these FAQs?
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> **Answer:** No. Borrowers and lenders may rely on the laws, rules, and guidance available at the time of the relevant application. However, borrowers whose previously submitted loan applications have not yet been processed may revise their applications based on clarifications reflected in these FAQs.

FAQ No. 17 seems to say that a borrower can rely on all the guidance available at the time the application was submitted, including the FAQs, and that no further action is necessary once the application is submitted, even if the guidance changes.

All was good, at least until last Wednesday evening (May 6) when FAQ No. 44 was issued. As a result of this FAQ, a borrower might feel compelled to return the PPP funds based on the safe harbor rule for returning PPP funds by May 7, 2020 (now extended to May 14, 2020) contained in IFR 4, posted on April 24, 2020. This is, perhaps, the safest course of action. But the safe harbor provision in IFR 4 only requires PPP borrowers to re-address their certification of the need for the funds. It is not a safe harbor provision that requires borrowers to reassess any other aspect of their applications. Additionally, for reasons mentioned above, returning all the funds may no longer be feasible.

In Conclusion

This conflicting guidance leaves borrowers, especially those that have already expended or taken action based on the receipt of the PPP funds, in a real quandary. Relying on FAQ No. 17 as a basis for keeping the funds is likely risky, particularly for borrowers with larger loans that will almost certainly be audited. On the other hand, returning all, or even some of the funds, may, at this point, be detrimental to your business. Therefore, we emphasize again that, if FAQ No. 44 applies to you, you should discuss your alternatives with counsel as soon as possible.

Contact Us

As always, for further guidance and assistance, please reach out to your PKFOD engagement team members, or Bruce L. Blasnik, CPA, CGMA, Partner at CLT-SBATechnical@pkfod.com. We are here to help.