Small Business Paycheck Protection Program

Please find below a summary of the Paycheck Protection Program, which was a key provision for small business included in H.R. 748, the Coronavirus Aid, Relief, and Economic Security (CARES) Act. This is a preliminary analysis of key provisions and should be reviewed with caution, given that the underlying legislative language may be subject to some unintended drafting errors and is subject to further interpretation by the Small Business Administration (SBA). Therefore, the forthcoming required guidance or regulations from the SBA should be relied upon and any examples should be reviewed with caution. Further, given the nature of this new program, information may change as the SBA and others address key outstanding issues.

Paycheck Protection Program
The CARES Act establishes a “Paycheck Protection Program” in Section 1102. The goal of this program is to enable employers to carry their payroll and other operating costs through this crisis. This program is administered by the Small Business Administration (SBA), with the support of the Department of Treasury. Logistical details are as follows.

Timeframe
“Covered period” begins on February 15, 2020 and ends on June 30, 2020. The loans are unavailable after June 30, 2020. And, the SBA has further clarified that the loans will be made on a first come, first serve basis.

Amount
The legislation establishes a cap of $10 million per loan or 250% of the average monthly payroll, whichever is less. For example, assuming no previous SBA loans for the same period or for the same purposes, if a business has a $300,000 monthly payroll, the loan amount would be $750,000.

Note: If you have an Economic Injury Disaster Loan from between January 31, 2020 and April 3, 2020, then special rules apply. If your EIDL loan was not used for payroll costs, it does not affect your eligibility for a PPP loan. If your EIDL loan was used for payroll costs, your PPP loan must be used to refinance your EIDL loan. Proceeds from any advance up to $10,000 on the EIDL loan will be deducted from the loan forgiveness amount on the PPP loan.

Eligibility
Employers with up to 500 employees within the United States (more below) will be eligible. Businesses in certain industries can have more than 500 employees within the United States if they meet applicable SBA employee-based size standards for those industries (click HERE for additional detail).

Subject to certain documentation requirements, individuals who are self-employed, independent contractors, or sole proprietors are eligible. Per the SBA interim final rule posted late on April 2, 501(c)(3) nonprofits are eligible.

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Definition of Employee

The new legislative text defines “employee” as “individuals employed on a full-time, part-time, or other basis.”

According to the SBA, the determination of the number of employees is the “average number of people employed for each pay period over the business’s latest 12 calendar months. Any person on the payroll must be included as one employee regardless of hours worked or temporary status. The number of employees of a concern in business less than 12 months is the average for each pay period that it has been in business.” The SBA calculates number of employees in accordance with 13 CFR 121.106. For more information on that definition, and others, visit 48 CFR 19. Note: The loan application tends to solely focus on payroll costs for 2019.

Independent contractors. With respect to independent contractors, the SBA interim final rule states the following:

Do independent contractors count as employees for purposes of PPP loan calculations?
No, independent contractors have the ability to apply for a PPP loan on their own so they do not count for purposes of a borrower’s PPP loan calculation.

On April 14, the SBA issued an interim final rule (IFR) related to independent contractors applying for the PPP loan. The rule clarifies how to make certain calculations under the PPP loan, among other items.

Affiliated entities. The SBA has recently issued an interim final rule related to affiliations, which primarily dealt with the affiliation rules as it relates to faith-based organizations. However, the rule does clarify that the appropriate affiliation rules are under 13 CFR 121.301, not 13 CFR 121.103. The SBA has also posted information regarding the affiliation rules for the PPP here.

In addition, the SBA’s affiliation standards are waived for small businesses (1) in the hotel and food services industries (click HERE for NAICS code 72 to confirm); or (2) that are franchises in the SBA’s Franchise Directory (click HERE to check); or (3) that receive financial assistance from small business investment companies licensed by the SBA.

Payroll Costs Defined

“Payroll costs” are broadly defined, as including:

- A salary, wage, commission, tips, or similar compensation for employees living in the United States (capped at $100,000 on an annualized basis for each employee),
- Employment costs for employees living in the United States such as costs for vacation; parental, family, medical or sick leave payment, dismissal or separation allowance, payments for an employer’s group health benefits (including premiums), and payment for retirement benefits, and
- Payment of State or local tax assessments on employee compensation.

For a sole proprietor or independent contractor: payment that is a wage, commission, income, net earnings from self-employment, or similar compensation, with a cap of $100,000 in one year (pro-rated for the covered period). For more information on these items, please review the SBA IFR on this topic.

Payroll costs specifically exclude: compensation of an individual above $100,000 annually (pro-rated for the covered period), taxes imposed or withheld under IRC Chapters 21, 22, or 24, any compensation of an employee
with a principal place of residence outside the U.S., and any sick or family leave for which a credit is allowed under the Families First Coronavirus Response Act.

**Allowable Uses**
During the covered period, the recipient may use the loan for:
- Payroll costs (see above)
- Costs related to the continuation of group health care benefits during periods of paid sick, medical, or family leave, and insurance premiums
- Interest on any mortgage obligation (but not any principal payment) **on obligations, incurred before February 15, 2020**
- Rent, **under lease agreements in force before February 15, 2020**
- Utilities, **for which service began before February 15, 2020**
- Refinancing an SBA EIDL loan made between January 31, 2020 and April 3, 2020, provided that the EIDL loan was for payroll expenses

Note: The items in **bold** are additional clarifications from the SBA/IRS guidance, while the information in **italics** was added as part of the initial SBA interim final rule.

**Process**
An eligible recipient shall make a good faith certification that the uncertainty of current economic conditions makes the loan necessary to support ongoing operations. The recipient must further certify that funds will be used to maintain payroll, make mortgage, lease, and utility payments. Finally, the recipient must certify that it does not have any duplicative applications. Fees are waived and the usual requirement that a small business cannot get credit elsewhere does not apply. The usual personal guarantee requirement is waived, and no collateral will be required. Recent SBA guidance indicates that the interest will be 1.0%, with a maturity in 2 years. Prepayment penalties are prohibited.

**Deferment**
Lenders are required to provide complete payment deferment relief for “impacted borrowers” for six months. This includes interest and fees. Impacted borrowers are presumed to have been impacted adversely by COVID-19, and all recipients are presumed to be “impacted borrowers.”

**Authorization**
For the period February 15, 2020 until June 30, 2020, the amount authorized for commitments for general business loans under Small Business Act Section 7(a) is $349 billion. Separately, the legislation provided the actual appropriations of $349 billion for the program. As of April 16, 2020, the initial $349 billion had been committed, but on April 24, a bill was enacted to provide an additional $310B for the program.

**Loan Forgiveness**
In section 1106, the bill creates “loan forgiveness” for loans described above (taken out pursuant to the new Payroll Protection Program). A recipient is eligible for forgiveness of indebtedness on a covered loan in amount equal to the sum of the costs incurred and payments made for one of the allowable uses, outlined above. Recent SBA guidance has noted that at least 75% of the forgiven amount must have been used for payroll. Here, for purposes of loan forgiveness, a “covered period” is the eight-week period starting on the date of loan origination.
Amounts forgiven shall be considered “canceled indebtedness” by a lender authorized by Section 7(a). Within 90 days after the date on which the amount of forgiveness is determined, the SBA shall remit to the lender the amount of forgiveness, with any interest accrued through the date of payment.

The amount of forgiveness is reduced based on a formula for business owners who have laid off employees or reduced wages, as follows:

- **Lay-offs**: The forgiveness amount is offset by the percentage reduction in total number of FTEs. It seems that the intent of the legislation is that, if an employer has 100 employees and lays off 25, their forgiveness should be offset by an equivalent percentage. However, the legislative language is unclear here.
  
  - Calculation of % reduction in FTEs:
    - Average number of Full-Time Equivalent Employees (FTEs) per month for the 8-weeks beginning on loan origination divided by the average number of FTEs per month, per one of three options below:
      - Option 1: Average number of FTEs per month from February 15, 2019 to June 30, 2019
      - Option 2: Average number of FTEs per month from January 1, 2020 to February 29, 2020
      - Seasonal workers: Average number of FTEs per month from February 15, 2019 to June 30, 2019
  
  - Example: A firm reduces the total amount of FTEs by 25%. As such, the total amount of the loan forgiveness is reduced by 25%.

- **Wage reductions**: The forgiveness amount is offset for each salary reduction of more than 25% (for employees making under $100,000 annually). The total salary reduction amount would be subtracted from the forgiveness amount.
  
  - Calculation of wage reduction: Subtract from the payroll costs the amount of any reduction in wages that is greater than 25% compared to their most recent full quarter for each employee who did not earn during any pay period in 2019 wages at an annualized rate more than $100,000.
  
  - Example: A firm reduces the salary of a salaried employee who makes $90,000 per year to $60,000 per year, which is more than 25% of the annualized salary (i.e., more than $67,500). Therefore, the loan forgiveness should be reduced by $7,500.

However, there is an exemption for rehires or increasing the salary of an employee. You have until June 30, 2020 to restore your full-time employment and salary levels for any changes made between February 15, 2020 and April 26, 2020.

Further, if you receive the emergency EIDL grant award of up to $10,000, then that amount would be subtracted from the PPP loan forgiveness total.

To obtain loan forgiveness, the recipient must submit an application to the lender. The bill specifically prohibits forgiveness without this documentation. The lender must make a decision with 60 days, and the application is to include:

- Documentation verifying the number of full-time equivalent employees on payroll and pay rates for the periods described in subsection (d), including payroll tax filings reported to the IRS and state income, payroll, and unemployment insurance filings.
- Documentation, including canceled checks, payment receipts, transcripts of accounts, or other documents verifying payments on covered mortgage obligations, payments on covered lease obligations, and covered utility payments.
• A certification that the documentation presented is true and correct and that the amount for which forgiveness is requested was used for allowable uses, and
• Any other documentation the Administrator determines necessary.

Timeline For Forgiveness
Within 60 days after a lender receives an application for loan forgiveness, the lender must issue a decision. Within 90 days after the date on which the amount of forgiveness is determined, the SBA shall remit that forgiveness amount, with interest, to the lender.

When to Apply
According to recent SBA guidance, starting April 3, 2020, small businesses and sole proprietorships can apply. Starting April 10, 2020, independent contractors and self-employed individuals can apply. The SBA encourages eligible entities to apply as quickly as possible due to the funding cap and has further clarified in its interim final rule that the funds will be made available on a first come, first served basis.

How to Apply
You can apply through any existing SBA 7(a) lender or through any federally insured depository institution, federally insured credit union, and Farm Credit System institution that is participating. Other regulated lenders will be available to make these loans once they are approved and enrolled in the program. You should consult with your local lender as to whether it is participating. All loans will have the same terms regardless of lender or borrower. A list of participating lenders as well as additional information and full terms can be found at www.sba.gov. To assist you with finding a lender, the SBA has added a lender finder here.

What do I need to apply? You will need to complete the Paycheck Protection Program loan application and submit the application with the required documentation to an approved lender that is available to process your application by June 30, 2020.

What other documents will I need to include in my application? You will need to provide your lender with payroll documentation. See below for additional information which may be requested by your lender:

  Company Information
  • Proof of existence of the company, including articles of incorporation, operating agreements, and proof of existence from the applicable state’s Secretary of State
  • Existing notes and debts of the company

  Payroll
  • Payroll reports from 2/15/20 to 6/30/20, as well as the amount paid from 4/1/19 to the date of the loan
  • Form 941's for 6/30/19, 9/30/19, 12/31/19, and 3/31/20

  Benefits
  • Health care benefits paid by the company from 2/15/20 to 6/30/20, as well as the amount paid from 4/1/19 to the date of the loan
  • Unemployment Tax Returns for 6/30/19, 9/30/19, 12/31/19, and 3/31/20, showing each individual’s compensation
  • Retirement plan summary including plan audits and Form 5500 from the most recent tax year

  Rent & Utilities
  • Current lease agreements
  • Recent utility bills from 2/15/20 through 6/30/20
How many loans can I take out under the PPP? Only one. You may opt to take out other loans through the SBA, including the EIDL and 7(a) programs. However, the loans must be for mutually exclusive purposes. As part of the SBA interim final rule, the SBA clarified that, if you have an EIDL loan with the purpose of offsetting payroll costs, then you must refinance that loan as part of the PPP, minus the amount of the EIDL grant award of up to $10,000. Further, if you receive the emergency EIDL grant award of up to $10,000, then that amount would be subtracted from the PPP loan forgiveness total.

How does the PPP interact with the payroll tax relief provisions created in the CARES Act and in the Families First Coronavirus Response Act (FFCRA)?
The CARES Act and FFCRA include several tax relief provisions in addition to the small business loan relief described above. Each of these provisions interacts with the PPP and you should consult with your tax advisor before pursuing any of these options.

The main three tax provisions related to employers are:

- Payroll tax deferral, created by section 2302 of CARES Act
- Employee Retention Credit, created by section 2301 of CARES
- Family and Medical Leave Act (FMLA) credit, created in 2017, expanded by FFCRA to cover 100% of eligible COVID-related paid leave

At this time, it is our understanding that the interactions work as follows:

- Payroll tax deferral: per the statute, the deferral of payroll tax payments is disallowed if a loan is forgiven under the PPP, but not necessarily disallowed if a loan is obtained under the PPP. However, it is possible that we will see future guidance disallowing this deferral for any employer who used the PPP loan, whether forgiven or not.
- Employee Retention Credit: the credit is disallowed if a loan is received under the PPP, whether forgiven or not.
- FMLA credit: the latest IRS guidance states that an entity can receive a PPP loan and may have the loan forgiven without jeopardizing the FMLA credit. However, the amounts taken as a credit will reduce the amount eligible to be forgiven under the PPP. Future guidance may be developed to address the interactions between the FMLA credit and loans received under the PPP.

How can I request loan forgiveness? You can submit a request to the lender that is servicing the loan. The request will include documents that verify the number of full-time equivalent employees and pay rates, as well as the payments on eligible mortgage, lease, and utility obligations. You must certify that the documents are true and that you used the forgiveness amount to keep employees and make eligible mortgage interest, rent, and utility payments. The lender must make a decision on the forgiveness within 60 days.

What is my interest rate? 1% fixed rate.

When do I need to start paying interest on my loan? All payments are deferred for 6 months; however, interest will continue to accrue over this period.

When is my loan due? In 2 years.

Can I pay my loan earlier than 2 years? Yes. There are no prepayment penalties or fees.
Do I need to pledge any collateral for these loans?  No. No collateral is required.

Do I need to personally guarantee this loan?  No. There is no personal guarantee requirement.

***However, if the proceeds are used for fraudulent purposes, the U.S. government will pursue criminal charges against you.***

What happens if PPP loan funds are misused?  If you use PPP funds for unauthorized purposes, SBA will direct you to repay those amounts. If you knowingly use the funds for unauthorized purposes, you will be subject to additional liability such as charges for fraud. If one of your shareholders, members, or partners uses PPP funds for unauthorized purposes, SBA will have recourse against the shareholder, member, or partner for the unauthorized use.

Additional Resources

Small Business Administration PPP information
PPP Sample Loan Form  (updated April 2)
SBA Interim Final Rule (posted April 2)
SBA Interim Final Rule (related to affiliations)
SBA Interim Final Rule (related to self-employed entities)
SBA Interim Final Rule (related to certain hospitals and private equity)
Joint Statement by Treasury Secretary Steven T. Mnuchin and SBA Administrator Jovita Carranza on the Resumption of the Paycheck Protection Program (4/24)
How to Calculate Loan Amounts
IRS PPP Overview
IRS PPP Borrower Information
IRS PPP Lender Information
IRS FAQ (updated regularly)
Find an eligible lender
U.S. Senate Committee on Small Business & Entrepreneurship FAQ on PPP (majority)
U.S. Senate Committee on Small Business & Entrepreneurship FAQ on PPP (minority)
U.S. Chamber of Commerce information on the PPP
NFIB: comparison of EIDL and PPP