

Second Chance at Paycheck Protection Program Loan: An Overview of Program Application and Loan Forgiveness Requirements



**Prepared by Lindabury, McCormick, Estabrook & Cooper, P.C. as of April 23, 2020.*

The Coronavirus Aid, Relief, and Economic Security Act (“CARES Act”), signed into law on Friday March 27, 2020, introduced the Paycheck Protection Program (the “PPP”) with the intended goal of preventing job loss and small businesses failure due to losses caused by the COVID-19 pandemic. The PPP was designed to support small business and employees by providing forgivable loans to employers if they maintained their employees and payroll. It was initially funded with \$349 billion on a first come, first serve basis. Initial applications from small businesses and sole proprietorships opened on April 3, 2020 and all of this initial funding was exhausted within 13 days, or by April 15, 2020.

On Tuesday, April 21, 2020, the Senate passed an “interim” coronavirus relief Bill, titled the “Paycheck Protection Program and Health Care Enhancement Act” (the Senate Bill). The Senate Bill amends the CARES Act to (i) increase the amounts authorized for the PPP in accordance with Section 7(a) of the Small Business Act, increase the Economic Injury Disaster Loans (EIDL loans), and increase emergency grants under the CARES Act, and (ii) authorize additional funding for hospital and provider recovery and coronavirus testing.

Despite many complaints about the design, administration and fairness of the PPP, the new Senate Bill was passed by the House on Thursday, April 23, 2020. It is expected to be signed by the President soon thereafter. Notably, the Senate bill does not modify the PPP’s lending program in any material degree but simply appropriates additional emergency funds.

As currently designed the “Paycheck Protection Program and Health Care Enhancement Act” passed by the Senate:

- Provides an additional \$310 billion in PPP loans - forgivable loans to small business to cover the cost of payroll and operating expenses:
 - \$30 billion in guaranteed loans for lenders with less than \$10 billion in assets.
 - \$30 billion in guaranteed loans for lenders with \$10 billion to \$50 billion in assets.
 - \$60 billion dollars is set aside for loans made by smaller insured depository institutions and credit unions.
- Provides an additional \$10 billion for Emergency Economic Injury Disaster (EIDL) grants.
- Appropriates an additional \$50 billion for the Disaster Loans Program Account.
- Allows agricultural enterprises as defined by section 18(b) of the Small Business Act (15 U.S.C. 647(b)) with not more than 500 employees to receive EIDL grants and loans.
- Provides an additional \$75 billion for reimbursement to hospitals and healthcare providers to support the need for COVID-19 related expenses and lost revenue.
- Provides \$25 billion for necessary expenses to research, develop, validate, manufacture, purchase, administer, and expand capacity for COVID-19 tests.

Because the focus of this article is Paycheck Protection Program (PPP) forgivable loans, we will not discuss the other grant, loan and testing programs set forth in the Senate bill.

Where can I find PPP guidance which explains the PPP program requirements?

In addition to the initial CARES Act, the U.S. Small Business Administration ("SBA") issued two interim rules on [April 2, 2020](#) and [April 3, 2020](#), as well as an interim final rule issued on [April 15, 2020](#).

The SBA also issued [Affiliation Guidance](#).

And, Frequently Asked Questions were issued on April 6, 2020, and repeatedly updated, five times through April 17, 2020. The FAQ can be found [here](#) and should be consulted for updates.

Notably, FAQ #17 states that borrowers and lenders may rely on the laws, rules, and guidance available at the time their PPP application was submitted even though borrowers (who submitted loan applications that have not yet been processed) "may" revise their applications based on clarifications reflected in the FAQs. Also, please note FAQ #31, which addresses "economic need" certification requirements, as discussed more fully in heading "How do I apply?" below.

Who is Eligible for the PPP?

Eligibility for Covered Loans broadly includes any business concern, nonprofit organization, veterans organization, or Tribal business concern if:

1. it was in operation on February 15, 2020 paying employees or independent contractors, and
2. the entity employs no more than the greater of:
 - a. 500 employees whose principal place of residence is in the U.S.; or
 - b. if applicable, the business meets the SBA employee-based or revenue-based size standards for the industry in which the entity operates or the SBA's "alternative size standard" after application of the "affiliation" rules.

Also eligible for Covered Loans are individuals operating under sole proprietorships or as independent contractors or as eligible self-employed individuals if:

1. they were in business on February 15, 2020, and
2. they submit the necessary documentation to establish eligibility (*i.e.* payroll processor records, payroll tax filings, Form 1099-MISC, or income and expenses from a sole proprietorship).

If Eligible, How Much Can I Borrow and How Do I Determine that Amount?

Under the PPP, the maximum loan amount is the lesser of:

1. \$10 Million or
2. 2.5 times the average total monthly payments for “Payroll Costs” over the 12 months before applying for the loan, plus the outstanding amount of any Economic Injury Disaster Loan (EIDL) made between January 31, 2020 and April 3, 2020.

FAQ #14 clarifies that borrowers can calculate their aggregate payroll costs and number of employees using data from *either* the previous 12 months or from calendar year 2019.

What is included in Payroll Costs?

“Payroll cost” for borrowers (other than independent contractors/sole proprietorships) equals the sum of:

- a. payments of compensation to employees in the form of salary, wages, commission, or similar compensation; (other than excess portions of annualized compensation of an employee exceeding \$100,000);
- b. cash tips or the equivalent;
- c. payments for vacation, parental, family, medical, or sick leave; (but not including qualified sick or family leave benefits paid under FFCRA per FAQ #8);
- d. allowances for dismissal or separation;
- e. payments for the provision of group healthcare benefits, including insurance premiums;
- f. payments of any retirement benefits; and
- g. payment of State and local tax assessed on employee compensation. (FAQ #16 clarifies that payroll costs are calculated on a gross basis, without subtracting federal taxes that are imposed on the employee or withheld from employee wages)

FAQ #15 clarified that payments to independent contractors or sole proprietorships are not counted for purposes of Covered Loan calculations or forgiveness of other small business Borrowers.

For independent contractors, "payroll cost" is the sum of payments of any compensation or income of a sole proprietor or independent contractor that is a wage, commission, income, net earnings from self-employment or similar compensation (not in excess of more than \$100,000 in 1 year, prorated).

Are Employee Benefit Contributions included with payroll cost?

FAQ #7 clarifies that the CARES Act exclusion of annual employee compensation in excess of \$100,000 applies only to cash compensation, not to non-cash benefits, including: 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. Therefore, these non-cash benefits *may* be included as a payroll cost, even for employees who have cash compensation in excess of \$100,000 annually.

Which Payroll Costs are Excluded?

Payroll Costs expressly exclude: (1) compensation of an employee whose principal residence is outside the United States; (2) the excess portions of annualized compensation of an individual employee exceeding \$100,000; (3) Federal employment taxes imposed or withheld between February 15, 2020 and June 30, 2020, including the employee's and employer's share of FICA and Railroad Retirement Act taxes, and income taxes required to be withheld from employees; and (4) qualified sick and family leave benefits for which an employer tax credit is allowed under the Families First Coronavirus Response Act.

How many loans can I get?

Note that no eligible borrower may receive more than one PPP loan. This means that if you apply for a PPP loan, you should consider applying for the maximum amount.

If a borrower received an SBA EIDL loan between January 31, 2020 and April 3, 2020, the borrower can also apply for a PPP loan. If the EIDL loan was used for payroll costs, the PPP loan must be used to refinance the EIDL loan. Proceeds from any EIDL loan advance up to \$10K will be deducted from the loan forgiveness amount on the PPP loan.

What Can the Loan Be Used For?

The proceeds of a PPP loan are to be used for:

1. payroll costs (as defined above), **payroll costs must be at least 75% of loan proceeds;
2. costs of continuing group health care benefits;
3. interest payments on any mortgage obligation (but not any prepayment or principal on a mortgage);
4. rent and utilities;
5. interest on any other debt obligations incurred before February 15, 2020; and

6. the refinancing of any EIDL loan made between January 1, 2020 and April 3, 2020.

** Importantly, **at least seventy-five (75%)** of the loan proceeds must be used for payroll costs, and if not, only a portion of the loan that was used for qualified purposes will be forgiven.

If a borrower uses Covered Loan proceeds for unauthorized purposes, the SBA will direct the borrower to repay those amounts.

Furthermore, under the Guidance, if you knowingly use the funds for unauthorized purposes, you will be subject to additional liability such as charges for fraud, and the SBA will have recourse against shareholders, members, or partners who use Covered Loan proceeds for unauthorized purposes.

How do I apply?

You will need to complete the PPP loan application and submit the application with the required documentation to an approved lender that is available to process your application. Applications can be found [here](#).

When applying, you will need to provide your lender with payroll documentation. As part of your application, you will need to certify the following:

- Current economic uncertainty makes the loan necessary to support your ongoing operations.
- The funds will be used to retain workers and maintain payroll or to make mortgage interest, lease, and utility payments.
- You have not and will not receive another loan under this program.
- You will provide to the lender documentation that verifies the number of full-time equivalent employees on payroll and the dollar amount of payroll costs, covered mortgage interest payments, covered rent payments, and covered utilities for the eight weeks after getting this loan.
- Loan forgiveness will be provided for the sum of documented payroll costs, covered mortgage interest payments, covered rent payments, and covered utilities. Not more than 25% of the forgiven amount may be for non-payroll costs.
- All the information you provided in your application and in all supporting documents and forms is true and accurate. Knowingly making a false statement to get a loan under this program is punishable by law.
- You acknowledge that the lender will calculate the eligible loan amount using the tax documents you submitted. You affirm that the tax documents are identical to those you submitted to the IRS. And you also understand, acknowledge, and agree that the lender can share the tax information with the SBA's authorized representatives, including authorized representatives of the SBA Office of

Inspector General, for the purpose of compliance with SBA Loan Program Requirements and all SBA reviews.

On April 23, 2020, the SBA issued additional Guidance, stating that before submitting a PPP application, all borrowers must “assess their economic need for a PPP loan.” Specifically, all borrowers should review carefully the required certification that “current economic uncertainty makes this loan request necessary to support the ongoing operations of the applicant.” Borrowers must make this certification in good faith, taking into account their current business activity and their ability to access other sources of liquidity sufficient to support their ongoing operations in a manner that is not significantly detrimental to the business. While it is unclear as to how the SBA will interpret “access to other sources of liquidity,” and “not significantly detrimental to the business,” we expect that the forgiveness portion of the loan may include an audit of the loan amount to ensure the application was made in good faith.

Importantly, the newly issued Guidance allows a borrower that has obtained a PPP loan prior to April 23, 2020 to repay the loan in full by May 7, 2020. For example, according to the Guidance, it is highly unlikely that a public company with substantial market value and access to capital markets will be able to make the required certification in good faith, and such company should be prepared to demonstrate to the SBA, upon request, the basis for its certification. Therefore, any borrower that applied for a PPP loan prior to the issuance of the Guidance and repays the loan in full by May 7, 2020, will be deemed by the SBA to have made the required certification in good faith.

Is a Guaranty or Collateral Required for the Loan?

Neither a guaranty nor collateral is required for the loan. The CARES Act specifically provides that the loans are non-recourse against any individual, shareholder, member or partner of a recipient of a loan as long as such individuals use the loan proceeds for permitted uses (as discussed above)

What is the Interest and Maturity on the Loan?

Guidance has capped the interest rate at 1% with a 2-year maturity (decreased from a maximum maturity of 10 years under the Act). Prepayment penalties are not permitted.

When will I have to begin paying principal and interest on my PPP loan?

Even if the loan amount is not forgiven in whole or in part, you will not have to begin any payments for 6 months following the date of disbursement of the loan. However, interest at 1% will accrue on PPP loans during this 6-month deferment.

Can my loan be forgiven in whole or in part?

A PPP loan is eligible for loan forgiveness up to the full amount of the loan plus any accrued interest.

What time period is relevant for loan forgiveness?

PPP loan forgiveness is fact-sensitive and based upon the borrowers use of the PPP loan proceeds during the 8-week period that begins on the date the lender makes the first disbursement of PPP loan to the borrower. FAQ # 20 states that the lender must make the first disbursement of the loan no later than 10 calendar days from the date of loan approval.

Which expenses are potentially forgivable?

Under existing guidance, loan forgiveness is available for the sum of documented:

1. payroll costs (as defined above)
2. covered mortgage interest payments (which were in place prior to February 15, 2020)
3. covered rent and lease payments; (which were in place prior to February 15, 2020) and
4. covered utility payments (electricity, gas, water, telephone, and internet which were in place before February 15, 2020)

However, very importantly, at least 75% of the PPP loan must be used for payroll costs.

AND

The amount of PPP forgiveness may be reduced if the borrower either:

- a. reduces the number its employees during that 8-week period (as applied against the employer's "comparable period" which for most businesses is, at the Borrower's choice, the average number of "full-time equivalent" employees per month employed by the borrower between either February 15, 2019 through June 30, 2019, or January 1, 2020 through February 29, 2020); or
- b. reduces salaries by 25% or more of employees with annual salaries of \$100,000 or less (as compared to the employee's average compensation during the last full quarter).

Are there any exceptions if the employer was forced to reduce the number of its employees or reduces salaries during that 8-week period?

An employer may qualify for an exception if, prior to June 30, 2020, the employer rehires the number of employees or reinstates the compensation of an employee that was impacted between Feb. 15, 2020, through April 26, 2020.

What is the consequence if I cannot restore my number of employees or salary levels prior to June 30, 2020?

If an employer still does not meet the requirements for this exception by June 30, 2020, then the amount of the loan eligible for forgiveness will be reduced ratably, and the remaining unforgivable portion of the loan will become a 2 year loan at a 1% interest rate and 6 month initial deferral period on repayment.

How are "Full Time Equivalent" employees under the CARES Act defined in order to calculate the number of employees?

Presently, there is no definition of "full-time equivalent employees" in the statute or in the other SBA guidance issued to date. Until additional guidance is issued, it is therefore uncertain how the below categories of employees will be calculated.

- existing employees: on paid leave, on reduced leave, are furloughed, or on workshare programs
- former employees: receiving severance, who voluntarily terminated, or who were terminated for cause

When will additional loan forgiveness guidance be available?

Under the CARES Act, additional guidance on PPP loan forgiveness must be issued by the SBA by April 26, 2020 and because of the number of lingering questions, it is highly anticipated.

Conclusion:

Should you have any additional questions, the attorneys at Lindabury McCormick, Estabrook & Cooper are available to assist the MCAA members and affiliated chapters.