

**NAVIGATING THE PAYCHECK PROTECTION
PROGRAM LOAN PROVISIONS OF THE CARES ACT (AND INTERIM
REGULATIONS)**

Executive Summary – A key portion of the Coronavirus Aid, Relief, and Economic Security Act (“CARES”) is an expansion of the SBA’s Section 7(a) loan program aimed primarily at businesses with fewer than 500 employees. Interim Regulations (“Regulations”), with respect to PPP loans, were issued on April 2, 2020. The loan program starts on February 15, 2020 and ends on June 30, 2020 (the “covered period”). The amount of available loan proceeds is equal to 2.5 times the business’s average monthly payroll costs for the one-year period before the loan is made. Loan proceeds received by the business must be used solely for payroll costs, mortgage interest, rent, utilities and interest on any other debt obligations incurred before the covered period. Loans can qualify for forgiveness and, importantly, such debt cancellation is not included in gross income for federal income tax purposes. If the business cannot show that it used the loan proceeds for the designated purposes, or lets employees go the loan must be repaid with interest. Businesses which take advantage of this loan program are excluded from certain tax stimulus provisions of the Cares Act, as I will discuss in a separate blog post titled Tax Stimulus Provisions of the CARES Act. Thus, some businesses may need to run the numbers on which program will provide the greatest benefits. On April 2, 2020 the SBA released Borrower Application Form 2483, which is to be used in applying for a PPP loan.

1. Eligible Loan Recipients.

- Small businesses with fewer than 500 employees;
- Small businesses which otherwise meet the SBA’s size standard;
- 501(c)(3) with fewer than 500 employees;
- Individuals who operate as sole proprietor;
- Individuals who operate as independent contractor;
- Self-employed individuals who regularly carry on any trade or business;
- Tribal business concerns that meet the SBA size standard;
- 501(c)(19) Veterans Organization that meets the size standard.

2. SBA Affiliation Rules. The SBA has also issued an Interim Final Rule confirming that in most cases a PPP borrower will be considered together with its affiliates for purposes of determining eligibility for a PPP loan. Specifically, the Interim Rule confirms that the affiliation rules of 13 CFR § 121.301 (but not 13 CFR § 121.103) will apply to PPP loans. Factors considered for affiliation include stock ownership, overlapping management, and identity of interest. The affiliation rules are waived for accommodation and food service businesses (i.e. assigned a NAICS code

beginning with 72) with 500 or fewer employees per location, businesses with SBA franchisor identifier codes; and any business that receives financial assistance from a company licensed under section 301 of the Small Business Investment Act.

3. Loan Maximum. The maximum loan amount (capped at \$10 million) is the lesser of: 2.5 times the borrower's average total monthly Payroll Costs incurred in the one-year period before the loan is made (special rules apply for seasonal employers and businesses which were not in existence during the period from January 1, 2020 to February 29, 2020); plus the outstanding amount of a loan made under the SBA's Disaster Loan Program between January 31, 2020 and the date on which such loan may be refinanced as part of this new program.
4. Loan Term. While the Act provided that the PPP Loan Term shall be up to ten years and the interest rate shall be up to 4%, the Regulations state that the term shall be only two years and the interest rate shall be 100 basis points, or 1.00%.
5. Principal Deferral. While the Act provided that PPP Loan payments may be deferred for up to one year, the Regulations provide that the deferral period will be only six months.
6. Borrower Requirements. There are a few borrower requirements to obtain a loan under this program. Those requirements, as modified by the Regulations, include a good-faith certification that:
 - The applicant was in operation on February 15, 2020 and had employees for whom it paid salaries and payroll taxes or paid independent contractors, as reported on a Form 1099-MISC;
 - Current economic uncertainty makes the loan request necessary to support the ongoing operations of the applicant;
 - The funds will be used to retain workers and maintain payroll or make mortgage, lease, and utility payments;
 - The applicant does not have any other application pending under this program for the same purpose;
 - From February 15, 2020 until December 31, 2020, the applicant has not received duplicative amounts under the PPP loan program.
7. Permissible Uses of Loan Funds. Businesses may use the loans for the following costs (the dollar amount of which must be provided to the lender):
 - Payroll Costs;
 - Payments of interest on mortgage obligations;
 - Rent/lease agreement payments;

- Utilities; and
- Interest on any other debt obligations incurred before the covered period.

[NOTE: While not a requirement of the Act, the Regulations provide that no more than 25% of the PPP loan proceeds may be used for listed costs other than payroll costs].

8. Included Employer Payroll Costs. The following are included in determining employer Payroll Costs:

- Salary, wage, commission or similar compensation;
- Payment of cash tip or equivalent;
- Payment for vacation, parental, family, medical, or sick leave;
- Payment for vacation, parental, family, medical, or sick leave;
- Allowance for dismissal or separation;
- Payment required for the provision of group health care benefits, including insurance premiums;
- Payment of any retirement benefit; and payment of state or local tax assessment on the compensation of the employee.

9. Excluded Employer Payroll Costs. The following may not be included in determining employer Payroll Costs:

- Compensation of an individual employee in excess of an annual salary of \$100,000, as prorated for the Covered Period;
- Payroll taxes, railroad retirement taxes, and income taxes;
- Any compensation of an employee whose principal place of residence is outside of the United States; and
- Qualified sick leave wages for which a credit is allowed under section 7001 of the Families First Coronavirus Response Act.

10. Sole Proprietors and Independent Contractors. For sole proprietors and independent contractors, payroll costs include the sum of payments of compensation to or income of the sole proprietor or independent contractor that is in an amount that is not more than \$100,000 in one year, as prorated for the covered period. [NOTE: The Regulations state that because independent contractors have the ability to apply for a PPP loan on their own, they do not count as employees for

a borrower's PPP loan calculation (presumably meaning a payor's loan calculation)].

11. Loan Forgiveness and Payment Deferral Relief. The Program loans qualify for the CARES Act's broader loan forgiveness provisions in Section 1106. Specifically, indebtedness is forgiven (and excluded from gross income for federal income tax purposes). The Regulations clarify that the amount forgiven cannot exceed the sum of accrued interest and principal. The actual amount forgiven will depend on the amount of the following costs incurred prior to February 15, 2020 and paid during the covered period:

- Payroll Costs;
- Interest payments on mortgages;
- Rent; and
- Utility payments.

[**NOTE:** According to the Regulations, not more than 25% of the loan forgiveness amount may be attributable to non-payroll costs. The Regulations further state that the SBA is to provide additional guidance with respect to loan forgiveness.]

12. Forgiveness Reduction for Employee Cuts. Forgiveness amounts will be reduced for any employee cuts or reductions in wages. The reduction formula for fewer employees (as stated in the statute) is:

- The maximum available forgiveness under the rules described above **multiplied by the quotient obtained by dividing:**
- The average number of full-time equivalent employees (FTEEs) per month – calculated by the average number of FTEEs for each pay period falling within a month – during the covered period **by:**
- Either (at election of the borrower) – the average number of FTEEs per month employed from February 15, 2019 to June 30, 2019; or
- The average number of FTEEs per month employed from January 1, 2020 until February 29, 2020; or
- For seasonal employers – Average number of FTEEs per month employed from February 15, 2019 until June 30, 2019. Note that this formula will be used to reduce forgiveness amounts, but cannot be used to increase them.

13. Forgiveness Reduction for Wage Cuts. For reductions in wages, the forgiveness reduction is a straight reduction by the amount of any reduction in total salary or wages of any employee during the covered period that is in excess of 25% of the employee's salary or wages during the employee's most recent full quarter of

employment before the covered period. “Employee” is limited, for these purposes only, to any employee who did not receive during any single pay period during 2019 a salary or wages at an annualized rate of pay over \$100,000.

14. Relief for Rehires. There is relief from these forgiveness reduction penalties for employers who rehire employees or make up for wage reductions by June 30, 2020. Specifically, in the following circumstances, the forgiveness reduction rules above will not apply to an employer between February 15, 2020 and 30 days following enactment of the CARES Act if:
 - The employer reduces the number of FTEEs in this period and, not later than June 30, 2020, the employer has eliminated the reduction in FTEEs; or
 - There is a salary reduction, as compared to February 15, 2020, during this period for one or more employees and that reduction is eliminated by June 30, 2020 [**NOTE:** it is unclear whether this is also intended to be limited to employees who made under \$100,000 in 2019].
15. Tipped Employees. The CARES Act clarifies that employers with tipped employees (as described in the Fair Labor Standards Act) may receive forgiveness for additional wages paid to those employees.
16. Documentation for Loan Forgiveness. Borrowers seeking forgiveness of amounts must submit a request for forgiveness to their lender and provide the following:
 - Documentation verifying FTEEs on payroll and their pay rates, including payroll tax filings with the IRS and State income, payroll, and unemployment insurance
 - Documentation on covered costs/payments (e.g., documents verifying mortgage, rent, and utility payments);
 - Certification from a business representative that the documentation is true and correct and that forgiveness amounts requested were used to retain employees and make other forgiveness-eligible payments;
 - Any other documentation the Administrator may require.
17. [**NOTE:** Qualification for forgiveness is expressly conditioned on providing the foregoing documentation.]

For any questions regarding the paycheck protection loan provisions of the CARES Act please contact Tom Hineman at thineman@meadowscollier.com.