BURR ALERT

So You Qualify for a Paycheck Protection Loan… Now What?

By Callie Whatley, George Morrison and Jennifer Leaphart April 2020

Since the end of last week when the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act" or the "Act") was signed into law, there has been a lot of discussion about the new Small Business Administration ("SBA") loan program created by the Act: the paycheck protection program ("PPP"). Under the CARES Act, these PPP loans offer a variety of benefits, including partial forgiveness and a deferral period in which no payments are due for at least 6 months and up to 1 year.

This week the U.S. Department of Treasury ("Treasury") and the SBA have presented additional guidance on these PPP loans and have also circulated an application form. The purpose of this alert is to highlight the ways in which these agency materials modify the general rules set forth in the Act, as described in our prior alerts, which generally describe the business relief offered in the Act and outline various options for SBA relief thereunder. This alert is based on guidance released from Treasury and the SBA as of Friday, April 3, 2020. This guidance is subject to update, and therefore this alert is necessarily also subject to further revision as Treasury and SBA guidance develops.

It is important to remember that these PPP loans are extended by private lenders who are authorized to do so by the SBA. Many of these lenders are setting up portals through which you may submit an application. You should ask your existing bank if it is an SBA-approved lender that will be offering these PPP loans and, if so, what that bank's particular application process will look like.

What does Treasury and SBA guidance change so far?

In Treasury's borrower guidelines and the SBA's interim final rules, which are effective immediately, the agencies have provided the following information that materially affects these PPP loans, including with respect to the amount you may be eligible to borrow and the amount that may be forgiven.

Forthcoming Rules on Eligibility: Typically, under existing SBA rules, in determining whether a business is "small," you must consider its affiliates. The Act only excepts certain industries from this typical rule, namely, those in hospitality industries having an NAICS code beginning with 72, certain franchises and those receiving financial assistance from a licensed small business investment company. The SBA interim final rules explicitly contemplate that the SBA will issue additional guidance with respect to applying its existing affiliation rules for PPP loans.

Clarifying Status of Independent Contractors: The Act is not clear as to whether a business that hires independent contractors could include those contract workers in its payroll costs for purposes of a PPP loan. The SBA interim final rules clarify that independent contractors do not count for purposes of determining a business's PPP loan calculations because these independent contractors are capable of applying directly for their own PPP loans.

Maximum Amount of PPP Loan: Under the Act, an eligible borrower may generally obtain a PPP loan equal to the lesser of (i) $10 million or (ii) (a) 2.5 x that borrower's average monthly payroll costs from the 1-year period prior to the date on which the loan is made plus (b) the amount of disaster loan issued to the borrower between January 31, 2020 until the date that PPP loans are made available. In the SBA interim final rules, the agency has interpreted (ii)(b) to mean that you may only add amounts for a disaster loan made between January 31, 2020 until April 3, 2020, less any advance you received on that disaster loan that is not subject to repayment. Therefore, if you do not have an outstanding disaster loan as of the date hereof that was issued on or after January 31, 2020, you only consider your payroll costs in determining your maximum eligible amount of PPP loan.

In addition, it is unclear based on the application for these PPP loans that has been circulated (and is linked below) and the SBA interim final rules what time period a borrower should use to determine its average monthly payroll costs for purposes of determining its maximum loan amount. The application suggests that the agencies have interpreted the relevant 1-year period for determining a borrower's average monthly payroll costs to be the preceding complete calendar year, but the SBA interim final rules provide that a borrower would make the determination based upon the "last twelve months."[1] Examples in the SBA interim final rules, though, appear to use an annual approach, and the SBA interim final rules applicable to lenders provide for those lenders to review documentation for the "preceding calendar year." It is likely 2019 will be used by lenders as the relevant time period in that case, and you should work with your bank to determine your maximum PPP loan amount.

Restriction on Forgivable Amounts: Under the Act, amounts incurred or paid by the eligible borrower during the 8-week period after the origination date of the loan for (i) payroll costs, (ii) mortgage interest on any mortgage incurred prior to February 15, 2020, (iii) rent on a lease in force prior to February 15, 2020, and (iv) payments for utilities for which service began prior to February 15, 2020, would be forgiven, subject only to certification requirements on payments and certain reductions in forgivable amounts on the basis of workforce reduction or cuts in compensation.[2] However, guidance has provided that not more than 25% of the forgiven amount for these PPP loans may be for non-payroll costs reflected in (ii)-(iv) above. For purposes of determining if 75% of proceeds have been used for payroll costs, the amount of any refinanced disaster loan is included. You should remember to keep careful records to document the use of PPP loan proceeds, as amounts are not forgivable without proper documentation that they were used for the foregoing permissible purposes.

Lower Interest Rate: Under the Act, the interest rate on PPP loans could go up to 4%. The SBA interim final rules have provided that the interest rate will be 1%.

Shorter Term: Under the Act, the term for PPP loans could go up to 10 years. Agency guidance has stated that these loans will become due in 2 years. Accordingly, you should keep in mind that any PPP loan amount which is not forgiven must be re-paid within 2 years.

Short Deferral Period: Under the Act, payments on PPP loans could be deferred for at least 6 months and up to 1 year. Agency guidance has clarified that payments on these loans will only be deferred for the minimum 6 months.

This guidance is a stark reminder that these PPP loans, while potentially forgivable, are indeed loans, which are subject to repayment. Further, guidance thus far suggests that Treasury and the SBA fear

[1] Special rules apply to seasonal employers.
[2] Special rules apply to employers that eliminate any workforce reductions or compensation cuts by June 30, 2020.

over-subscription for PPP loans, and future guidance may further tailor the benefits these PPP loans offer.

How do you apply for a PPP loan?

The agencies have released a revised application here and anticipate that lenders will be capable of taking applications on Friday, April 3, 2020 for small businesses and sole proprietorships.[3] However, it is unclear if these private lenders will have their internal processes prepared by this date.

In the revised application, an authorized representative of the eligible business must certify to various statements under criminal penalty. These statements include that (i) the PPP loan request is necessary to support the business's ongoing operations and (ii) the PPP loan funds will be used to retain workers, maintain payroll, or make mortgage, rent or utility payments. The application explicitly contemplates that the Federal government may pursue criminal charges against any business that uses these PPP loan funds for unauthorized purposes. Neither the application nor the SBA interim final rules designate a particular individual as an authorized representative for this purpose. The SBA interim final rules merely contemplate that a representative can make these certifications so long as it is legally authorized to do so. In general, officers of a business will have general agency authority to make these certifications.

In addition to the application, you will need to provide your lender with payroll documentation. The SBA interim final rules contemplate that borrowers must provide documentation that is necessary to establish its payroll processor records, any payroll tax filings, and, as relevant, Form 1099-MISC, and other income and expenses of a sole proprietorship. We recommend that you discuss documentation required with your lender and gather, at minimum, the following in order to be best prepared for your application:

- 2019 Internal Revenue Service ("IRS") annual 940, annual 944 and quarterly 941 payroll tax reports;
- 2020 quarterly 940 payroll tax reports for the first quarter;
- Payroll reports for the preceding 12-month period (to include the first quarter of 2020), which include:
    - Gross wages for each employee, including any officers if paid W-2 wages, which includes paid time off, vacation and paid sick leave and
    - State and local taxes on each employee's compensation;
- Documentation detailing payments required for group health care benefits, including insurance premiums; and
- Documentation of payments for any retirement plan benefits paid for by the business.

In addition, self-employed individuals are recommended to include the following items, in addition to the above items for all employees:

- 2019 Income Statement (inclusive of income and expenses);
- All IRS Form 1099-MISC that you received and are included as income; and

[3] Treasury anticipates that applications for independent contractors and self-employed individuals will be capable of being processed by April 10, 2020.

- Documentation detailing payments for any direct self-employed retirement plan contributions.

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To discuss this further, please contact:

George Morrison at (615) 724-3248 or gmorrison@burr.com

Callie Whatley at (205) 458 5441 or cwhatley@burr.com

Jennifer Leaphart at (803) 753-3252 or jleaphart@burr.com

or the Burr & Forman attorney with whom you normally consult.