Payment Protection Program Under Title I of the CARES Act

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On March 27, the President of the United States signed the $2 trillion stimulus bill, the Coronavirus Aid, Relief, and Economic Security Act or the CARES Act (the Act), previously passed by the House and Senate. The Act includes many provisions and programs designed to provide individuals, businesses, healthcare providers, nonprofits, and state and local governments with economic and other relief from the ravages of COVID-19. Although the Act touches on many areas of law, the below is a summary of the specific provisions of Title I (Keeping American Workers Paid and Employed Act) relating to the Small Business Administration (SBA) 7(a) Loan Program.

SBA 7(a) Loan Program

- The Act has created a new SBA 7(a) loan program called the "Paycheck Protection Program" (PPP) and $349 billion has been allocated for PPP loans.

- The Act has increased the number of businesses that will be eligible to receive PPP loans by replacing the small business concern rules that apply to all other SBA loans with a broader definition. Under the PPP, any business concern, nonprofit organization, veterans organization, or Tribal business concern which employs not more than the greater of 500 employees total (or 500 employees per location for certain industries, including hotels and restaurants) or if applicable, the size standard in number of employees established by the SBA for the industry. The size standards have been established for types of economic activity, or industry generally under the North American Industry Classification System (NAICS) based on employee size or total annual receipts. The Act allows eligible borrowers to qualify for PPP loans even if they exceed the total annual receipts, but if an industry has an employee size criteria, the Act states that the business will be eligible if it employs not more than the greater of 500 employees (or 500 employees per location for certain industries, including hotels and restaurants) or if applicable, the size standard in number of employees established by the SBA for the industry. The full table of small business size standards can be found at 13 CFR § 121.201.

- During the "covered period", which the Act defines as the period beginning on February 15, 2020, and continuing through June 30, 2020, the loan amount available for a PPP loan is determined based on the lesser of (A) 2.5 times the average total monthly payments for payroll costs incurred during the one year period before the date the loan is made or (B) $10,000,000.00. There is an alternative formula if the Eligible Borrower was not in business during the period from February 15, 2019, through June 30, 2019. It is important to note that with respect to employees that earn in excess of $100,000.00 per year, an Eligible Borrower may only include $100,000.00 for purposes of determining its payroll costs.

- During the covered period, the proceeds of a PPP loan may be used only for the following purposes:

  1. Direct payroll costs;
  2. Payroll support, including paid sick, medical or family leave and costs related to the continuation of group health care benefits;
  3. Employee salaries, commissions or similar compensation;
  4. Payments of interest on any mortgage obligation (the payment or prepayment of principal is not permitted);
  5. Rent;
  6. Utilities; and
  7. Interest on other debt obligations that were incurred before the covered period.

- In order to be eligible for a PPP loan, an eligible borrower must have (i) been in operation on February 15, 2020 and (ii) (a) had employees for whom the eligible borrower paid salaries and payroll taxes or (b) paid independent contractors, as reported on a Form 1099-MISC.

- If an eligible borrower has received an Economic Injury Disaster Loan (EIDL) under the Disaster Assistance Program between January 31, 2020, and February 15, 2020, for a purpose other than an eligible PPP use, it will still be eligible for a PPP loan. However, it will not be able to receive assistance under both programs for the same purposes.

- Interest on PPP loans shall not exceed 4% and all guarantee, servicing, and prepayment fees are waived.

- The Act specifies that there shall be no personal guaranty or collateral requirements on PPP loans. PPP loans are to be nonrecourse loans for all purposes unless an owner of an eligible borrower uses the loan proceeds for a non-permitted purpose.

- The SBA guarantee amount on all PPP loans made prior to January 1, 2021 will be 100%. For PPP loan extended on and after January 1, 2021, assuming there are funds and eligible uses therefore remaining, the guarantee percentages shall revert to the amounts applicable for standard SBA 7(a) loans of similar size.

- Eligible borrowers will be entitled for loan deferment for a period of not less than six months and not more than one year if they are considered an impacted borrower. An impacted borrower is defined as an eligible borrower (i) in operation as of February 15, 2020 and (ii) who has made an application for a PPP loan that is approved or pending approval after the enactment of the Act. Any impacted borrower will be presumed to be impacted adversely by COVID-19. The SBA is to consider all eligible borrowers that apply for a PPP loan under the Act to be an impacted borrower.

- Within 30 days of the enactment of the Act, the SBA will provide guidance to lenders regarding the deferment process.

- During the covered period, the lending limit for the SBA Express loan program is being increased from $350,000 to $1,000,000.

- The Act provides that the SBA will make the next six regularly scheduled principal and interest payments on all existing SBA 7(a) loans made before the enactment of the Act that are not then on deferment.

<u>Loan Forgiveness</u>

- Pursuant to the Act, an eligible borrower who obtains a PPP loan during the covered period may qualify for forgiveness of a portion of the principal of the indebtedness to the extent expended during the eight week period beginning on the date of the origination of the PPP loan (the forgiveness covered period). Qualified uses for loan forgiveness include amounts spent during the forgiveness covered period for (i) payroll costs, (ii) payment of interest on mortgage obligations incurred before February 15, 2020 (specifically excludes the payment or prepayment of principal), (iii) payment of rent under an agreement entered into before February 15, 2020 and (iv) any utility payment for services on an account established prior to February 15, 2020 (collectively “eligible forgiveness costs”).

- Payroll costs mean:

1. Any compensation paid to employees that is:
    a. Salary, wage, commission or similar compensation;
    b. Payment of cash tip or equivalent;
    c. Payment for vacation, parental, family, medical or sick leave;

d. Allowance for dismissal or separation;
e. Payment required for the provisions of group health care benefits, including insurance premiums;
f. Payment of any retirement benefit; or
g. Payment of state or local tax assessed on the compensation of employees

2. Any compensation to or income of a sole proprietor or independent contractor that is a wage, commission, income, net earnings from self-employment, or similar compensation that is an amount that is not more than $100,000 in one year, as prorated for the covered period

- Payroll costs shall NOT include (i) the compensation of an individual employee in excess of $100,000 in one year, as prorated for the covered period, (ii) taxes imposed or withheld under chapters 21 (Federal Insurance Contributions Act), 22 (Railroad Retirement Tax Act) or 24 (Collection of Income Tax at Source of Wages) of the IRS Code of 1986, (iii) any compensation of an employee whose principal place of residence is outside of the United States (iv) qualified sick-leave wages for which a credit is allowed under section 7001 of the Families First Coronavirus Response Act, or (v) qualified family-leave wages for which a credit is allowed under section 7003 of the Families First Coronavirus Response Act.

- The amount forgiven shall not exceed the principal amount of the PPP loan.

- The loan forgiveness will be reduced by multiplying the eligible forgiveness costs by the number obtained by dividing (x) the average number of full-time equivalent employees per month employed by eligible borrower during the forgiveness covered period by, at the election of the eligible borrower (y)(i) the average number of full-time equivalent employees per month employed by eligible borrower during the period from February 15 – June 30, 2019, or (ii) the average number of full-time equivalent employees per month employed by eligible borrower during the period from January 1 – February 29, 2020 (except for seasonal employers which shall be required to use option (i)).

- The loan forgiveness will also be reduced proportionately by the amount of any reduction in excess of 25% of compensation in the most recent full quarter in which the employee was paid during the forgiveness covered period.

- An eligible borrower with tipped employees may receive forgiveness for additional wages paid to those employees.

- Loan forgiveness shall not take into consideration a reduction in full-time equivalent employees or a reduction of salary of employees from February 15, 2020, and ending on the date that is 30 days after the date of enactment of the Act if the eligible borrower has eliminated the reduction (i.e. rehired employees or adjusted salaries) by no later than June 30, 2020.

- In order to be eligible for loan forgiveness the eligible borrower will need to submit the following to its lender:

  1. Documentation verifying the number of full-time equivalent employees on payroll and pay rates;
  2. Payroll tax filings reported to the IRS;
  3. State income, payroll and unemployment insurance filings;
  4. Documentation including cancelled checks, payment receipts, transcripts of accounts or other documentation verifying payments made on mortgage obligations, rent or utility payments all entered into before February 15, 2020;
  5. Certification from eligible borrower certifying the documentation is true and correct and the amount of forgiveness requested was used for eligible loan forgiveness purposes; and
  6. Any other documentation the SBA deems necessary.

- The forgiven debt under the Act shall be excluded from gross income.

- After any portion of the loan is forgiven under the Act, the remaining balance will continue to be guaranteed by the SBA and shall have a maximum maturity of 10 years from the date which the eligible borrower applies for loan forgiveness.

- Within 30 days after enactment of the Act, the SBA will issue guidance and regulations to implement the loan forgiveness provisions.

Please contact a member of the COVID-19 Task Force or your MMM attorney with any questions about how the Payment Protection Program may help your business.