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Small Business Relief under the CARES Act

Overview of the SBA Paycheck Protection Program



Paycheck Protection Program

Below are answers to commonly asked questions about the Paycheck Protection Program established under the CARES Act for the period from February 15, 2020 until June 30, 2020. The program is designed to encourage employers to maintain payroll and to help small businesses cover their expenses (e.g., payroll, mortgage, rent, utilities, etc.) in the near-term.

The Small Business Administration (SBA) has issued a final loan application, multiple interim final rules, and FAQ guidance to implement this program. The program requirements in those rules supersede any conflicting SBA Loan Program Requirements contained in SBA Business Loan regulations (13 CFR 120.10, et seq.) until this program expires on June 30, 2020.

Because SBA is issuing new rules and guidance on a rolling basis, borrowers may rely on the rules and guidance in place at the time of application and do not need to take any further action based on subsequent SBA releases. Borrowers whose applications have not yet been processed may, however, amend those applications based on new rules/guidance.

When will these loans be available?

There are staggered loan availability dates:

- April 3, 2020 for small businesses and sole proprietorships; and
- April 10, 2020 for independent contractors and self-employed individuals.

What are some of the main benefits of a paycheck protection loan (PPL)?

- Loan amounts up to \$10 million per eligible entity;
- Loan payments are automatically deferred for six months, but interest will accrue during the deferral period;
- Full loan amount forgiveness for employers that maintain or restore pre-crisis payroll;
- 100% federally guaranteed;
- No recourse against individuals, shareholders, members, or partners of loan recipients for non-payment, unless s/he uses loan dollars for impermissible purposes;
- No collateral or personal guarantee requirements, or fees;
- Loans have a maturity of two years, but there is no penalty for prepayment; and

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- Fixed interest rate of 1%.

Who is eligible?

Any “small business concern”

- As defined in current SBA rules based on employee-based or revenue-based size standards for the entity’s primary industry (see www.sba.gov/size); or
- That meets both tests in the SBA’s alternative size standard as of March 27, 2020:
 - Maximum tangible net worth of the business is not more than \$15 million, and
 - Average net income after federal income taxes (excluding any carry-over losses) of the business for the two fiscal years before the date of PPL application is not more than \$5 million.

Additionally, entities (including sole proprietors, independent contractors, and self-employed individuals) that were operating and paying workers on February 15, 2020, and:

- Have 500 or fewer employees whose principal place of residence is in the US; or
- Satisfy the “small” SBA employee-based size standards for the entity’s primary industry, if applicable.

Eligible entities include for-profit businesses, 501(c)(3) nonprofits, 501(c)(19) veterans organizations, and Tribal business concerns described in section 31(b)(2)(C) of the Small Business Act.

Special Rules for Individual Applicants with Self-Employment Income

Regarding self-employed individuals, independent contractors, and sole proprietors, the rules clarify that you are eligible to apply for your own PPL if:

- You were in operation on February 15, 2020;
- You are an individual with self-employment income, including independent contractors and sole proprietors;
- Your principal place of residence is the US; and
- You filed or will file a Form 1040 Schedule C for 2019.

Notably, partners in partnerships may not submit separate PPL applications as self-employed individuals. Instead, self-employment income of general active partners may be reported as payroll costs (up to the \$100,000 limit discussed below) on the partnership’s application

Special Rules for Faith-Based Organizations

The rules also contain special eligibility provisions for faith-based organizations. Such entities are eligible if they:

- Have not more than 500 employees; and
- Pay federal payroll taxes using their own IRS employer identification number (EIN) or are eligible for the federal tax deduction for gross income derived from any unrelated trade or business regularly carried out by a parish, church, etc. (see 26 U.S.C. 512(b)(12)).

Ineligible Entities

The rules explicitly exclude “household employers” of nannies, housekeepers, etc. from eligibility. The rules also exclude from this program entities that are ineligible for SBA Business Loans under 13 CFR 120.110, except 501(c)(3)s and faith-based organizations. We encourage you to check the full list, but examples of excluded businesses include:

- Financial businesses primarily engaged in the business of lending;
- Passive businesses owned by developers and landlords that do not actively use or occupy the assets acquired or improved by the loan proceeds;
- Life insurance companies;
- Businesses located in a foreign country;
- Private membership clubs and businesses;
- Businesses deriving more than one-third of gross annual revenue from legal gambling activities (with an exception under SBA PPL rules for businesses with legal gaming revenue, net of payouts, of \$1 million or less in 2019 and whose legal gaming revenue, net of payouts, comprised less than 50% of total revenue in 2019); and
- Businesses primarily engaged in political or lobbying activities (a restriction being challenged in court).

How do I count my employees to figure out if I'm eligible?

General Rules

All entities count full-time, part-time, and “other basis” employees (e.g., employees from temp agencies or professional employer organizations) of the entity and of all of the entity’s affiliates, unless an affiliation rule exception applies. SBA guidance released on April 6, 2020, indicates that borrowers may use average employment numbers over the same time periods used for calculating monthly average payroll costs (discussed below) or they may use the average number of employees per pay period in the last 12 calendar months (or for the months the business has been operating, if fewer than 12 months).

The SBA issued special guidance on affiliation rules applicable to the PPL program. Generally, entities are affiliates when one controls or has the power to control the other, or a third party or parties has the power to control both. The guidance sets forth 4 tests/circumstances that will establish affiliations for PPL applicants:

- **Equity Ownership** – if an individual, concern, or entity owns or has the power to control more than 50% of the applicant’s voting equity; absent such over 50% ownership, SBA will consider the CEO, Board of Directors, or similar body in “control” of the applicant; it also will consider a minority shareholder that has the authority to block Board or other shareholder action to be in “control.”
- **Common Management** – when the CEO or President (or similar manager) of the applicant also controls the management of one or more other concern; or where an individual, concern or entity controls the Board/management of the applicant and the Board/management of one or more other concerns; or when a single individual, concern, or entity controls the applicant through a management agreement.

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- **Identity of Interest** – when close relatives (spouse, parent, child, or sibling – or the spouse of any such person) have identical or substantially identical business or economic interests (e.g., they operate concerns in the same or similar industry in the same geographic area) (but note, applicants may rebut a finding of affiliation under this test and show the businesses are separate).
- **Stock options, convertible securities, and agreements to merge** – generally will be considered to have present effect on the power to control a concern and are treated as though rights granted have been exercised. But no present effect will be given for:
 - Agreements to open or continue negotiations toward a possible merger or sale at a future date (don't count as agreements in principal);
 - Options, convertible securities, and agreements that are subject to conditions precedent which are incapable of fulfillment, speculative, conjectural, or unenforceable under state or Federal law, or where the probability of the transaction (or exercise of the rights) occurring is shown to be extremely remote, are not given present effect; or
 - Individuals', concerns', or other entities' ability to divest all or part of their ownership interest in order to avoid a finding of affiliation.

SBA has clarified that it is the borrower's responsibility to determine which, if any, entities are its affiliates. Lenders may rely on the borrowers' certifications regarding overall headcount of employees.

Special Counting Rules and Affiliation Waivers for Certain Businesses

Under the CARES Act, there are special employee counting rules for "business concerns" with NAICS industry codes starting with 72 (generally, "accommodations and food services"); namely:

- You are eligible for a PPL if you have 500 or fewer employees per location; and
- SBA affiliation rules are waived for these loan applicants (meaning only the employee count of the applicant entity, not the entity's affiliates, should count).

SBA affiliation rules also are waived for "business concerns" that:

- Operate as a franchise under an SBA franchise identifier code (list available on the SBA website);
- Receive financial assistance from Small Business Investment Act licensees.

Notably, to allow more businesses to take advantage of the franchise waiver, SBA has indicated that it will allow franchisors to apply for identifier codes for purposes of PPLs under a more relaxed process than would normally apply (but those codes will not extend beyond the PPL program).

Additionally, by SBA's rules, the affiliation rules do not apply to "the relationship of any church, convention or association of churches, or other faith-based organization or entity to any other person, group, organization, or entity that is based on a sincere religious teaching or belief or otherwise constitutes a part of the exercise of religion." SBA will permit faith-based applicants to make a good-faith determination about whether and to what extent this waiver applies to them and will not require lenders to assess the reasonableness of the applicant's determination.

Finally, there are general exceptions to the SBA's affiliation rules (*see* 13 CFR 121.103(b)(2)) that still apply for purposes of the PPL program.

A Few More Things to Consider Regarding These Counting Rules

Based on the information we have to date, it likely is worth evaluating PPL eligibility from the perspective of each separately organized business concern.

If your business operates under multiple NAICS industry codes (perhaps one of which begins with 72), the SBA will look at the code of your “primary industry” based on average receipts, employees, costs of doing business, etc.

“Business concerns” under the SBA are for-profit business entities with US locations that have primary operations in the US or make a significant economic contribution in the US (e.g., by paying taxes). “Business concerns” may be organized as sole proprietorships, partnerships, LLCs, corporations, associations, trusts, cooperatives, or joint ventures with under 50% foreign business participation.

How do I apply for a loan?

The rules clarify that entities may not apply for or receive more than one PPL in 2020.

Loans may be delivered immediately by banks that already issue SBA Business Loans and any other federally-insured depository institutions, federally-insured credit unions, and Farm Credit System institutions that choose to participate in the program. Treasury is authorizing additional lenders that satisfy certain criteria to participate in the program to expand the network of institutions available to deliver these loans. The Treasury Department has posted a link on its website to help you locate an eligible participating lender.

What is Required for the Loan Application?

There is a standard PPL loan application (SBA Form 2483), which is significantly streamlined compared to normal SBA Business Loan applications. By design, banks’ underwriting obligations for PPLs are very limited (essentially, verifying that documentation is submitted, payroll averages are substantiated, etc.) and banks may rely on borrowers’ documentation and certifications to determine eligibility and loan amounts.

The application generally requires:

- Basic business identification information;
- A list of all owners of the applicant with 20% or greater ownership stake;
- A list of any businesses under common ownership or management with the applicant;
- Details on any EIDL loan received by the business between January 1, 2020 and April 3, 2020;
- Information about individual applicants’ and 20%-plus owners’ criminal history; and
- The good-faith certifications described below.

The only blanket “borrower requirements” imposed by the CARES Act for PPLs are certain good-faith certifications. Under the application and rules, an authorized business representative must certify, among other things, that:

- The applicant was in operation on February 15, 2020 and paid workers at that time, and is otherwise eligible for a PPL.

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- The loan is needed to “support ongoing operations” during the COVID-19 emergency.
- Funds will be used to retain workers and maintain payroll or make mortgage, lease, and utility payments.
- You will provide to the lender documentation that verifies the number of full-time equivalent employees on payroll and the dollar amounts of forgiveness-eligible costs for the eight weeks after getting the loan.
- Loan forgiveness will be based on the sum of documented payroll costs, covered mortgage interest payments, covered rent payments, and covered utilities, but not more than 25% of the forgiven amount may be for non-payroll costs (as discussed below).
- The applicant has not and will not receive another PPL from now until December 31, 2020.
- 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.

The rules clarify that e-signatures and e-consents are permitted.

Note that you will not be approved for a loan if you are presently involved in a bankruptcy or if the business or any owner has defaulted on a federal government loan in the last 7 years, among other circumstances.

What Other Documentation Do I Need to Submit with My Application?

Ultimately, for applicants not applying as individuals with self-employment income, this will be up to your lender and we understand that there are some significant variations between banks at this time. At a minimum, however, all applicants will need to supply some payroll documentation along with Form 2483.

SBA FAQs provide some examples of what may suffice for such documentation, including: payroll reports from recognized third-party processors; an employer’s quarterly federal tax returns; or, for employers who contract with payroll providers or PEOs for payroll, relevant information from Schedule R (Form 941), Allocation Schedules for Aggregate Form 941 filers, and the like.

SBA has clarified that most borrowers may calculate average monthly payroll costs based on either data from the previous 12 months or from calendar year 2019 (seasonal businesses may use data from February 15, 2019 or March 1, 2019 until June 30, 2019; and new businesses not operating between February 15, 2019 and June 30, 2019 may use data from January 1, 2020 through February 29, 2020).

SBA guidance further clarifies that it is the borrower’s obligation to accurately calculate payroll costs and lenders need only do a “good faith review in a reasonable time” – but ultimately, the lender may rely on the borrower’s certification that the “payroll cost” numbers submitted are correct.

For individual applicants earning self-employment income, the rules are more prescriptive about the documentation you must submit with your application. Specifically, you must provide:

- 2019 Form 1040 Schedule C to substantiate your loan amount (whether or not you have filed 2019 tax returns with the IRS); and

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- 2019 Form 1099-MISC detailing non-employee compensation received, invoice, bank, statement, or book of record that establishes you are self-employed; and
- 2020 invoice, bank statement, or book of record to establish that you were in operation on or around February 15, 2020; and
- If you have employees, Form 941 (or other tax forms or equivalent payroll records); and
- If you have employees, 2019 state quarterly wage unemployment insurance tax reporting forms (or equivalent payroll records); and
- If you have employees, evidence of any retirement or health insurance contributions.

What if I already got an SBA loan for economic injury due to the COVID-19 emergency?

Under the CARES Act, SBA economic injury disaster loans (EIDLs) made under the SBA's Disaster Loan Program between January 31, 2020 and April 3, 2020 may be refinanced as PPLs. The implementing rules further state that if your EIDL loan was used for payroll costs, your PPL loan must be used to refinance your EIDL loan. But, according to the rules, if your EIDL loan was not used for payroll costs, it does not impact your eligibility for a PPL.

Additionally, the CARES Act clarifies that you may have a post-January 31, 2020 EIDL and a PPL if the EIDL is for a purpose other than paying payroll costs and other obligations that may be paid with PPLs (see full list below).

What is my maximum loan amount and how can I spend it?

Calculating Maximum Loan Amounts

Under the rules, loan amounts are, up to \$10 million:

- 250% of average monthly "payroll costs" (defined below) paid by the applicant during the last 12 months (or one of the alternate look-back periods noted above), plus
- Any outstanding amount of an EIDL made between January 31, 2020 and April 3, 2020, less any advances taken under a COVID-19 EIDL loan.

There are special calculation rules for individual applicants with self-employment income. If you are such an individual and you have no other employees, your maximum loan amount is (again, up to \$10 million):

- 250% of your net profit amount from Form 1040 Schedule C line 31 (capped at \$100,000 annualized) divided by 12; plus
- Any outstanding amounts from an EIDL made between January 31, 2020 and April 3, 2020 that you seek to refinance as a PPL, less any amounts you took as an advance on such EIDL.

Note that if your net profit amount is zero or less, you do not qualify for a PPL.

If you are an individual applicant and you do have employees, your maximum loan amount is the outstanding amount on any refinanced EIDL (less any advances taken on the EIDL), plus 250% of the monthly average of:

- Net profit amount from Form 1040 Schedule C line 31 capped at \$100,000 annualized;
- 2019 gross wages and tips paid to employees whose principal place of residence is in the US (capped at \$100,000 annualized for any individual employee) computed using 2019 Form 941 Taxable Medicare

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wages & tips (line 5c-column 1) from each quarter, plus any pre-tax employee contributions for health insurance or other fringe benefits excluded from Taxable Medicare wages & tips; plus

- 2019 employer health insurance contributions (from Form 1040 Schedule C line 14), retirement contributions (Form 1040 Schedule C line 19), and state and local payroll taxes.

Allowable Uses for Loan Proceeds

Loan dollars may be used for:

- **Payroll Costs, as defined in the rules:**

Include (on a gross basis):

- individual employee compensation (salary, wages, commissions, cash tips, or similar) up to annualized compensation of \$100,000 (the cap applies only to cash compensation, not the additional items below);
- paid leave;
- severance payments;
- payment for group health benefits, including insurance premiums;
- retirement benefits (e.g., employer contributions to retirement or pension plans);
- state and local payroll taxes; and
- “owner compensation replacement” for self-employed, independent contractor and sole proprietor applicants only: wage, commissions, income, or net earnings from self-employment or similar compensation up to annualized compensation of \$100,000 (i.e., other employers may not include payments to these individuals under their “payroll cost” calculation);

Exclude:

- excess individual compensation above the \$100,000 threshold;
- federal employer-side taxes (e.g., employer’s share of federal payroll taxes);
- compensation to employees whose principal place of residence is not the US; and
- sick and family leave wages for which credit is allowed under the Families First Coronavirus Relief Act (for both employees and owners);
- Group health care benefits during periods of paid sick, medical, or family leave;
- Insurance premiums;
- Payments of interest on mortgage obligations;
- Rent (including rent under a lease agreement);
- Utilities;
- Interest on any other debt obligations incurred before February 15, 2020;

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- Any uses already permitted for SBA Business Loans (e.g., inventory, supplies, building or land purchases, construction, site improvements, etc.); and/or
- Refinancing an SBA EIDL loan made between January 1, 2020 and April 3, 2020.

The rules clarify that independent contractors and sole proprietors do not count as “employees” for purposes of calculating “payroll costs” because they may apply for their own loans under the program.

The rules also provide that at least 75% of the PPL proceeds “shall” be used for payroll costs.

Notably, these expenditures are all permitted under the PPL program, but not all of them are eligible for loan forgiveness. So, for example, you could use the loan dollars to pay inventory expenses, but that portion of the loan will not be forgiven.

Additional Clarifications & Limitations for Individual Borrowers with Self-Employment Income

The “allowable uses” rules described above generally apply to individual borrowers with self-employment income, but SBA rules make some additional and notable clarifications for these borrowers:

- You may use loan dollars for owner compensation replacement (as calculated above based on net profits and capped at \$100,000 annualized);
- “Payroll costs” follow the definition above for any employees you have (but you do not count owner benefits in “payroll costs”);
- Mortgage interest, rent, and utility payments must be business obligations/expenses, and you must have claimed or be entitled to claim a deduction for these expenses on your 2019 Form 1040 Schedule C for them to be permissible uses during the eight-week period following disbursement of your loan (this is to ensure loans are used for maintaining existing operations and not for business expansion); and
- The general “allowable use” categories for group health benefits and insurance premiums do not apply for these borrowers (but note employer payments for employees’ health benefits, including health premiums, are includable/allowable under “payroll costs”).

How much of my loan will be forgiven?

The rules and guidance issued to date generally do not address the forgiveness provisions in detail, but we do anticipate more rules from SBA on this particular portion of the program.

First, Determine Your Maximum Available Forgiveness Amount

Under the rules, the maximum available forgiveness amount (capped at principal amount of the loan) is the sum of the following **incurred and paid within eight weeks of receiving your first loan disbursement** (the “forgiveness period”):

- Payroll costs for employees (as defined above, including owner compensation replacement for individual borrowers with self-employment income);
- Interest on mortgage obligations that were in place before February 15, 2020;
- Rent obligations under leases that were in place before February 15, 2020; and
- Utility payments for services that began before February 15, 2020.

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The forgiveness rules incentivize quick deployment of loan dollars to these priority buckets of expenses, particularly payroll. The rules clarify that **not more than 25% of the loan forgiveness amount may be attributable to non-payroll costs**. Moreover, any dollars spent more than eight weeks after your loan is originated, even for these forgiveness-eligible expenses, will not be included in your forgiveness amount.

For purposes of forgiveness, the owner compensation replacement portion of “payroll costs” is limited to eight weeks’ worth (8/52) of 2019 net profit and you must exclude any sick leave amounts for which credit is claimed under the Families First Coronavirus Relieve Act. Also, as noted above, for these borrowers, you must have claimed or be entitled to claim a deduction for the business’s mortgage interest, rent, and utility expenses on your 2019 Form 1040 Schedule C for those to be allowable expenses during the forgiveness period (and thus forgivable).

Second, Be Aware of Penalties That Will Reduce Your Forgiveness Amount

Because the policy goal of the PPL program is to encourage employers to keep employees on payroll at something at least close to their normal base pay, the maximum forgiveness amount will be reduced:

- Proportionately for reductions in average full-time equivalent employees (FTEEs) between pre-crisis levels and the eight-week forgiveness period;
- Via a straight reduction for payroll reductions over 25% (compared to the prior completed quarter of employment) for workers making less than \$100,000 annually; and
- For any advances taken on SBA EIDLs.

Note that the law does not say whether “full time” will be based on a 40-hour work week or some other measure, but we hope this point will be clarified in future SBA guidance.

Third, there are Opportunities to Negate Forgiveness Amount Penalties

There is relief from these forgiveness penalties for businesses that restore payroll to pre-crisis levels in the next few months. Specifically, the reduction rules described above will not apply (i.e., eligibility for your maximum forgiveness amount is restored), if the employer eliminates by June 30, 2020:

- Reductions (compared to February 15, 2020) in the number of FTEEs made between February 15, 2020 and April 26, 2020; and/or, as applicable,
- Salary reductions (compared to February 15, 2020) made between February 15, 2020 and April 26, 2020 for one or more employees (*Note: the legislation does not specify whether this also is limited to employees making under \$100,000 per year).

How do I get my loan forgiven and what if I have unforgiven amounts left over?

To receive loan forgiveness, you must apply to the lender servicing your loan with documentation:

- Verifying FTEEs on payroll and their pay rates (IRS payroll tax filings and state income, payroll, and unemployment filings);
- On covered costs/payments (e.g., canceled checks, receipts, or other documents verifying mortgage, rent, and utility payments); and

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- Certifying (by an authorized 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.

For individual borrowers with self-employment income, you will have to submit Form 941 and state payroll tax records for any employees, evidence of eligible business rent, utility, and/or mortgage interest payments, and 2019 Form 1040 Schedule C to determine net profits for purposes of calculating the maximum owner compensation replacement amount.

Regarding loan amounts remaining after the forgiveness determination, it appears that the intent of the CARES Act is for the same loan terms to continue applying (e.g., 1% interest rate, federally-guaranteed, two-year maturity, etc.), but future SBA guidance on the forgiveness provisions may elaborate more on this topic.

Are there other considerations I should evaluate before I apply for a PPL?

There are some trade-offs for businesses that receive PPL loans and/or loan forgiveness with respect to some other tax benefits in the CARES Act.

For instance, an employer that receives a PPL is not eligible for the employee retention credit in section 2301 of the law, which provides eligible employers a refundable credit against payroll tax (Social Security and Railroad Retirement) liability equal to 50% of the first \$10,000 in wages per employee (including value of health plan benefits). Eligible employers must have carried on a trade or business during 2020 and be experiencing either: at least a partial suspension of operations due to government orders (e.g., limiting commerce, travel, group meetings, etc.); or a year-over-year gross receipts reduction of at least 50%.

In addition, an employer that receives loan forgiveness on a PPL is not eligible for the employment tax deferral in section 2302 of the CARES Act, which postpones the due date for depositing employer payroll taxes and certain self-employment taxes (with half due at the end of 2021 and the other half due at the end of 2022).

Businesses will have to compare the benefits of PPLs and these tax credits/deferrals to determine which path provides the greater financial benefit (e.g., compare immediate liquidity needs with longer-term time value of money calculations).

When can we expect further guidance from the SBA on this new program?

The SBA already has released rules and FAQ guidance on the PPL program, which will be updated on a rolling basis. The SBA also has until April 26, 2020 to issue specific guidance on loan payment deferment relief and the loan forgiveness provisions.

For additional guidance, please refer to [Step toe's COVID-19 Resource Center](#).

Last modified: April 14, 2020