WILENTZ
—ATTORNEYS AT LAW—
WILENTZ, GOLDMAN & SPITZER, P.A.

CARES Act Establishes the SBA's Paycheck Protection Loan Program—A Lifeline for COVID-19 Impacted Businesses

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The CARES Act, signed into law by the President on March 27, 2020, includes a program to provide immediate cash flow relief to small businesses which are suffering due to the coronavirus pandemic. The relief is provided through loans intended to bridge an employer's future, short-term cash flow demands through June 30, 2020. In return for an employer's general continued employment of workers and sustained wage levels through the covered period (ending June 30, 2020) and compliance with expenditure rules, the loan is eligible for forgiveness.

Specifically, the Paycheck Protection Program (PPP) is an approximate $350 billion federal appropriation designed to provide that cash-flow bridge. Essentially, small businesses (generally, those with no more than 500 employees) may apply for a federal loan to fund eight weeks of certain operating costs. The loans are federally guaranteed and, under certain circumstances, are eligible to be forgiven. The loans are being administered by the Small Business Administration (SBA) and the loans will be available from banks currently authorized to issue SBA 7(a) loans, and may also be expanded to include other banks that are not currently authorized to issue SBA 7(a) loans.

The following FAQ provides answers to the fundamental questions faced by businesses owners who are interested in accessing financial assistance under the Paycheck Protection Program.

FAQ: Paycheck Protection Program (PPP)

1. Who qualifies to apply for a loan?

Entities that qualify to apply for the loan include small businesses, sole proprietorships, independent contractors, and self-employed individuals if the entity employs no more than 500 employees. In most cases, affiliates are aggregated in the head count. Certain employers in industries (such as Accommodation and Food Services) may be eligible if they have no more than 500 employees at a location. In addition, the Federal Administration is permitted to establish a size standard for certain other industries as an exception to the rule.

The CARES Act provides that an applicant would be required to certify that the loan is needed to continue operations during the pandemic, that funds will be used to retain workers, make payroll and pay certain other limited expenses, that it has no other applications pending under the PPP and that it has not received any other benefits under the PPP.

2. What is the maximum amount of the loan?

The maximum loan amount is calculated by multiplying 2.5 times the applicable business' average monthly payroll costs over the prior 12-month period. The term "payroll costs" is broadly defined under the CARES Act to include, among other things, payment of (i) salary wages, commissions and similar compensation, (ii) cash tips, (iii) vacation, parental, family, medical and sick leave, (iv) health care benefits and health insurance premiums, (v) retirement benefits, and (vi) state or local tax assessed on the compensation of employees. The loan amount is capped at $10 million.

Payroll costs include compensation to employees such as salary, wages, commission and paid leave, group health benefits, retirement benefits and state and local payroll taxes all up to $100,000. Compensation to an employee over $100,000, compensation to an employee whose principal place of residence is not the US, and certain sick and family leave under the Families First Coronavirus Response Act are excluded from the calculation of the maximum loan amount.

The monthly average payroll cost of seasonal employers is calculated differently taking into consideration the seasonal nature of the business. The maximum loan amount also takes into consideration any loan balances an applicant may have outstanding under the SBA's EID Program. For businesses not in existence from February 15, 2019 to June 31, 2020, there is an alternative calculation for the maximum loan amount.

3. What can the loan funds be used for?

The loan may be used for payroll costs, payment of interest on mortgages and certain other debt incurred prior to February 15, 2020, lease payments and utility payments. As a precondition for forgiveness, the employer must agree to use, and in fact use, the loan funds for such purposes. To the extent that the employer uses the loan proceeds for other purposes, eligibility for forgiveness and the non-recourse nature of the loan is at risk.

4. Under what circumstances is the loan eligible for forgiveness?

The loan is eligible for forgiveness in an amount equal to the costs set forth above (payroll costs, interest of mortgages and certain other debt, lease payments and utility payments) which are incurred and paid during the period from February 15, 2020 to June 30, 2020, provided further that the amount forgiven may not exceed the principal amount of the loan. Interest on the loan is not forgiven.

Importantly, eligibility for forgiveness is further reduced based upon reductions in either employee head count or wages. A reduction in the number of employees is calculated by dividing the average full time equivalent employees (FTEE) per month during the covered period (8 week period beginning on the date of origination of the loan) by either (a) average FTEEs per month from February 15, 2019 to June 30, 2019 or (b) average FTEEs per month from January 1, 2020 until February 29, 2020. If that calculation produces a number less than 1, forgiveness is accordingly reduced by such factor. If the number is greater than 1, forgiveness is not increased.

In addition, if, during the covered period (8 week period beginning on the date of origination of the loan), total salary or wages are reduced in excess of 25% of an employee's salary/wages during the most recent quarter prior to the beginning of the covered period, loan forgiveness is reduced by a corresponding amount. Any reduction in an employee's salary who, on an annualized basis, earned over $100,000 in 2019 will not reduce the loan forgiveness amount.

In addition, an employer may receive relief from forgiveness reduction if it rehires employees or makes up for such wage reductions by June 30, 2020.

5. How is the loan paid back if all or a portion of the loan is not forgiven?

Any loan amounts not forgiven are carried forward as an ongoing loan with max terms of 10 years, at a maximum interest rate of 4%. Principal and interest payments with respect to any amounts not forgiven may be deferred for a period not exceeding one (1) year.

6. How do I apply for a loan?

The SBA is required, under the CARES Act, to issue implementing regulations within 15 days of March 27, 2020. It is assumed that such implementing regulations will include a form an application. The SBA website can be found here.

7. 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*** (set forth above).

8. What are the main differences between a PPP Loan and an EID Loan? Can I apply for both?

The EID loan program and PPP loan program have some important differences that should be noted here. Although the focus of this article is to discuss the provisions of the CARES Act which establishes the PPP loans, the following are the main ways in which a EID loan differs from a PPP loan:

- EID loan applications are currently being accepted by the SBA, while the PPP loan applications are not yet available. A company may apply for both an EID loan and a PPP loan; however, "double-dipping" is not permitted so the amount advanced under an EID loan will reduce the amount a business may receive under a PPP loan.
- Although companies with 500 and fewer employees can now apply for an EID loan, the maximum amount of an EID loan is capped at $2,000,000.00.
- An EID loan can cover many operating expenses that a PPP loan cannot be utilized for, including most operating expenses.
- While a PPP loan is forgivable if certain conditions are complied with, an EID loan is not forgivable.
    - It should be noted however, that an EID loan may be refinanced with the proceeds of a PPP loan, thereby potentially making a portion of it forgivable depending on how the loan proceeds are utilized.
- The EID loan program includes a special feature called an "Emergency EIDL Grant" which provides for a company applying for an EIDL loan to receive an emergency grant in an amount up to $10,000.00 which must be used for the purposes that an EID loan may be used for. In order to receive the grant the company must self-certify that they are an eligible entity (i.e. 500 employees or less) when submitting their application for an EID loan and request the grant. Within three (3) days of the submission of the EID loan program application, the company will receive the grant. The grant does not need to be repaid if the EID loan application is ultimately denied—however, if the EID loan is approved, the grant amount will reduce the amount approved for the EID loan and may need to be repaid. There is no such grant associated with the PPP loan application.

Companies can apply for an EID loan and grant at this link.

If you have a question about the CARES Act Paycheck Protection Program, please contact Anthony Osbourne.

Attorney

- Anthony M. Osbourne

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