

The Paycheck Protection Program: Where The Program Stands Now

The Paycheck Protection Program, created on March 27, 2020 under the Coronavirus Aid, Relief, and Economic Security Act (H.R. 748) (the “CARES Act”), empowers authorized Small Business Association (the “SBA”) lenders to provide up to \$659 billion of loans to businesses and not-for-profit organizations to help cover payroll costs and certain eligible non-payroll costs. As of July 17, 2020, approximately \$131.3 billion remained available. To give small business owners and not-for-profit organizations more time to take advantage of the program, Congress approved the extension of the deadline to apply for a loan under the Paycheck Protection Program from June 30, 2020 to August 8, 2020. Since its implementation, the Paycheck Protection Program has gone through various amendments and alterations leaving both borrowers and lenders looking for clarification from both the Treasury Department and the SBA. This memorandum is intended to assist borrowers and lenders by pulling together, in one place, the many salient rules and guidelines.

I. Basic Loan Terms

Loans under the Paycheck Protection Program have an interest rate of 1.00%. Loans granted on or after June 5, 2020 have a five-year maturity date. Loans granted prior to June 5, 2020 had a two-year maturity date, which may be extended if the lender agrees. By far the most attractive feature of the loans under the Paycheck Protection Program is the opportunity to have up to the full amount of the loan forgiven if certain conditions are satisfied. In order to give borrowers the opportunity to seek forgiveness, payments on the loans are deferred until the date on which the forgiveness amount is remitted to the lender. If a borrower does not seek forgiveness of the loan (likely because it has not satisfied the conditions), the deferral period is 10 months from the date of the loan.¹

II. Certification That Loan Is Necessary

In order to obtain a loan under the Paycheck Protection Program, the business must certify, in good faith, that “the uncertainty of current economic conditions makes *necessary* the loan request to support the ongoing operations of the eligible recipient.” While the Paycheck Protection Program waives the requirement under Section 3(h) of Small Business Act (15 U.S.C. 636) that small businesses must be unable to obtain credit elsewhere, the required certification that the loan is “necessary” has created some concerns on the part of borrowers, lenders, and lawmakers.

On April 23, 2020, the Treasury Department issued guidance instructing applicants to consider both their current business activity and their ability to access other sources of liquidity that are not significantly detrimental to their business. The guidance specifically states that public companies with substantial market value and access to capital markets unlikely could make this certification in good faith. An applicant should be prepared to demonstrate the basis for its certification to the SBA. A lender, however, can rely on an applicant’s certification. Borrowers may face civil liability under the False Claims Act for such false certifications.² Borrowers that applied for a loan under the Paycheck Protection Program before April 23, 2020 and repaid it in full by May 14, 2020³ will be deemed to have made the certification in good faith and will not be penalized.

¹ There has been no guidance issued that addresses what constitutes the deferral period if a borrower receives forgiveness on some, but not all, of the loan proceeds.

² Additionally, borrowers may face criminal and civil liability under 18 USC 1001 and 3571 by imprisonment of not more than five years and/or a fine of up to \$250,000, under 15 USC 645 by imprisonment of not more than two years and/or a fine of not more than \$5,000 and, if submitted to a Federally insured institution, under 18 USC 1014 by imprisonment of not more than thirty years and/or a fine of not more than \$1 million.

³ The Treasury Department extended this date from May 7, 2020 to May 14, 2020 in an FAQ dated May 5, 2020. A full set of

III. Who Can Borrow

Small businesses and not-for-profit organizations with fewer than 500 employees are eligible for loans under this program. The SBA has determined that businesses in certain industries with more than 500 employees may also qualify for a loan under the Paycheck Protection Program if they do not exceed the employee size standards listed in the table found [here](#). The CARES Act waives the Small Business Act's affiliation rules with respect to eligibility of businesses in the hospitality and food industry with more than one location. Therefore, if a business in that industry employs more than 500 workers, but less than 500 at each location, the business is eligible for a loan at each location. The affiliation rules continue to apply to all other borrowers and require careful analysis of all factors surrounding control of businesses with common ownership.

IV. Amount That Can Be Borrowed

Small business owners and not-for-profit organizations may borrow an amount equal to 2.5 times their average monthly payroll costs during a specified historical period, up to a maximum amount of \$10 million. Payroll costs include total compensation paid to employees whose principal place of residence is in the United States and who earn less than \$100,000 in total annual compensation. Total compensation includes wages and salary, payments for vacation, parental, family, medical or sick leave, allowance for separation or dismissal, payments for employee benefits and payment of state and local compensation taxes. Payroll costs exclude federal employment taxes imposed or withheld between February 15, 2020 and June 30, 2020, payments to independent contractors and 1099 workers, and qualified sick and family leave under Sections 7001 and 7003 of the Families First Coronavirus Response Act (H.R. 6201). In calculating estimated payroll costs, amounts paid to an employee in excess of \$100,000 per year are excluded.

On April 30, 2020, the SBA announced an interim final rule, 13 C.F.R. Part 120, which sets a maximum aggregate loan amount of \$20 million for businesses that are part of a single corporate group under the Paycheck Protection Program.⁴ Businesses are considered part of a single corporate group if they are at least majority owned, directly or indirectly, by a common parent. Applicants that applied for loans or borrowers that received loans after April 30, 2020 under the Paycheck Protection Program in excess of \$20 million must withdraw or request cancellation of any pending application or approved loan not in compliance with this rule. Applicants and borrowers that fail to withdraw or request cancellation will not be eligible for loan forgiveness under the Paycheck Protection Program. A lender, however, can rely on the applicant's representation that it is in compliance with this limitation.

V. Permitted Use Of Loan Proceeds

The loan proceeds may be used for payroll costs and to cover utilities, rent payments, and interest on existing debt and mortgages. Payroll costs include payroll costs paid and incurred. The non-payroll costs include interest on mortgage obligations on real and personal property, business rent or lease payments for real and personal property, and payments for electricity, gas, water, transportation, telephone, and internet access. Payment of principal on any mortgage is not permitted. Although these non-payroll costs are all permitted, the amount spent in total for all of these categories may impact loan forgiveness. If more than 40% of loan proceeds are spent to pay these non-payroll costs during the covered period (as defined below), loan forgiveness may be reduced. For more information, *see* Section VII, Loan Forgiveness Amount, below.

FAQs from the Treasury Department can be found [here](#).

⁴ For the full interim rule, *see* <https://home.treasury.gov/system/files/136/IFR--Corporate-Groups-and-Non-Bank-and-Non-Insured-Depository-Institution-Lenders.pdf>.

VI. SBA Review and Repayment of Loans

Any borrower that received or will receive a loan under the Paycheck Protection Program in a principal amount of less than \$2 million will be deemed to have made the required certification that the loan is necessary in good faith and will not be subject to automatic review by the SBA. The SBA has determined that borrowers with loans of less than \$2 million likely do not have access to adequate sources of liquidity when compared to borrowers that require larger loans. However, the SBA may review any loan application and any Loan Forgiveness Application (defined below) at its discretion.

Conversely, any borrower that received or will receive a loan in a principal amount in excess of \$2 million will be subject to review by the SBA. If the SBA determines that a borrower lacked the adequate basis for the certification regarding the necessity of the loan, the SBA will seek repayment of the loan balance and the borrower will not be eligible for loan forgiveness. If the borrower repays the loan after notification of its ineligibility, the SBA will not pursue administrative enforcement or referrals to other agencies based on its determination with respect to the certification concerning necessity of the loan.

VII. Loan Forgiveness Amount

The Paycheck Protection Program Flexibility Act of 2020 (H.R. 7010), signed into law on June 5, 2020, amended the Paycheck Protection Program's initial, comparatively rigid loan forgiveness requirements.⁵ Borrowers now may be eligible for loan forgiveness for any interest and expenditures made during the 24-week period following the loan's origination (or, at the election of the borrower, the 24-week period beginning with the first pay period following the date of the loan disbursement) or until December 31, 2020, whichever period is shorter (the "covered period"), for payroll costs and other permitted non-payroll costs, provided that at least 60% of the loan proceeds used during the covered period for which the borrowers seeks forgiveness were used for payroll costs. If a borrower received a loan prior to June 5, 2020, the borrower may elect an eight-week covered period beginning on the date of the loan's origination or the first pay period following the date the loan is made. The application for loan forgiveness under the Paycheck Protection Program (the "Loan Forgiveness Application") confirms payroll costs paid or incurred during the covered period are eligible for forgiveness.⁶ The two interim rules enacted on May 22, 2020 (13 C.F.R. Part 120) (the "May 22 Interim Rules") provide that payroll costs are considered to be "incurred" on the day the employee's pay is earned, meaning the day the employee worked. If the employee is not performing work, but is on the borrower's payroll, payroll costs are "incurred" according to a schedule established by the borrower, which is likely to be based on the days the employee would have worked. Furthermore, the May 22 Interim Rules confirm that salary, wages or commission payments to furloughed employees are considered payroll costs and are eligible for loan forgiveness. Additionally, hazard pay and bonuses are considered payroll costs and are eligible for forgiveness as long as the employee receiving the hazard pay or bonus does not receive total annual compensation over \$100,000.

The May 22 Interim Rules provide further guidance for owner-employees, self-employed individuals, and general partners. Compensation to owner-employees and self-employed individuals is capped at the lesser of 8/25

⁵ In a letter dated July 20, 2020, Senators Chris Van Hollen and M. Michael Rounds urged U.S. Treasury Secretary Steven Mnuchin and SBA Administrator Jovita Carranza to issue guidance clarifying that small businesses and not-for-profit organizations can reapply for a loan under the Paycheck Protection Program if they previously returned their loans or accepted smaller amounts because they believed they could not meet the initial loan forgiveness requirements.

⁶ The loan forgiveness application was released on May 15, 2020 and can be found [here](#). The full loan forgiveness application instructions can be found [here](#).

of their total compensation for 2019 (or \$15,385) if the borrower elects an eight-week covered period or 2.5 months' worth of their total compensation for 2019 (or \$20,833) if the borrower elects a 24-week covered period. For owner-employees, this amount includes cash compensation, and employer retirement and health care contributions made on their behalf. General partners' compensation is capped at 92.35% of their 2019 net earnings from self-employment (reduced by expense deductions claimed under section 179 of the United States Internal Revenue Code and unreimbursed partnership expenses). Forgiveness is not available for retirement or health insurance contributions for self-employed individuals and general partners.

VIII. Reduction of Loan Forgiveness

Loan forgiveness will be reduced in proportion to a decrease in full-time equivalency during the eight-week or 24-week covered period, as applicable, compared to a reference period of either February 15, 2019 to June 30, 2019 or January 1, 2020 to February 29, 2020. However, there are several exceptions borrowers can take advantage of to avoid the reduction. Exceptions to the full-time equivalency reduction apply if (i) the borrower made a good faith, written offer to rehire an employee during the covered period and the employee declined or (ii) the employee was fired for cause, voluntarily resigned, or voluntarily requested and received a reduction of hours. Two additional exemptions apply if (i) the business cannot rehire the same employees and similarly qualified employees for unfilled positions by December 31, 2020 or (ii) the business is unable to return to the same level of business activity due to compliance with guidance issued by the Secretary of Health and Human Services, the Director of the Centers for Disease Control and Prevention, or the Occupational Safety and Health Administration during the period March 1, 2020 to December 31, 2020. The rules also specify a safe harbor for borrowers that exempts them from the loan forgiveness reduction if by December 31, 2020 the number of full-time equivalent employees is at least equal to the number of full-time equivalents on payroll for the pay period that includes February 15, 2020.

The amount of the loan that is forgiven may also be reduced if the borrower decreases the pay of any employee who receives an annual wage of less than \$100,000 by more than 25% as of the last calendar quarter. However, if salary and wages are reduced due to a decrease in hours that is reflected in the full-time equivalency calculations, the borrower will not be penalized a second time under the salary/wage reduction. Stated differently, the salary/wage reduction *only* applies to the portion of the reduction in employee salary and wages that is not attributable to a decrease in hours worked as reflected in the full-time equivalency calculation. For example, if an hourly employee works fewer hours and therefore earns less money, the business will not be penalized for both reducing the employee's hours and reducing that employee's total wages. However, if the business reduces both an hourly employee's hours and that employee's hourly wage by more than 25%, then forgiveness may be reduced under both the full-time equivalency reduction and the salary/wage reduction.

IX. Loan Forgiveness Process And Review

Borrowers may submit a loan forgiveness application to their lenders at any time on or before the maturity date of the loan. Once an application for forgiveness is submitted, a lender is expected to perform a good-faith review of the borrower's calculations and supporting documents for loan forgiveness. A lender has 60 days from receipt of the complete application to issue a decision to the SBA with the PPP Loan Forgiveness Calculation Form, PPP Schedule A, and PPP Borrower Demographic Information Form (if submitted to the lender). If the lender determines that the borrower is entitled to forgiveness in full or in part, the lender will also request payment from the SBA. If the lender determines that the borrower is not entitled to forgiveness, it must provide the SBA with the reason for denial. The lender is responsible for notifying the borrower of the amount to be forgiven or that the lender has issued a decision to the SBA denying the loan forgiveness application. A borrower may request that the SBA review the lender's decision within 30 days of notice from the lender. Within 90 days of a lender's request for payment, the SBA will remit to the lender the appropriate forgiven amount plus any accrued interest. If the

amount the SBA remits to the lender exceeds the remaining principal balance of the loan because the borrower made payments on the loan prior to the final determination regarding forgiveness, the lender must forward the excess amount to the borrower. Borrowers must retain copies of all submitted documentation for six years after the loan is forgiven or repaid in full.

The SBA may undertake a review of any loan or forgiveness application at its discretion, regardless of the size of the loan. The SBA will review applications relating to loans that are in excess of \$2 million. If the SBA undertakes such a review, within five business days, the lender must submit the Borrower Application Form, the Loan Forgiveness Application, a signed and certified transcript of account, a copy of the executed note evidencing the loan, and any other documents relating to the loan requested by the SBA. If such documentation indicates that the borrower may not be eligible for forgiveness, the lender must request additional information from the borrower in writing and provide any such additional information to the SBA. While review is pending, the lender may not approve any Loan Forgiveness Application for such loan. If, within one year after the loan was disbursed, the SBA determines that the borrower was ineligible for a loan under the Paycheck Protection Program, the SBA will seek repayment of the lender processing fee from the lender.

The Consumer Bankers Association and the Bank Policy Institute are lobbying Congress to provide for automatic forgiveness of all loans under \$150,000, without the additional burden of the loan forgiveness application process. They believe this would save billions of dollars and tens of millions of hours of paperwork and encourage small business owners to utilize the program. Congress has not indicated whether any loans will be automatically forgiven at this point, but on July 17, 2020, Secretary Mnuchin stated he was open to automatically forgiving loans of smaller amounts with some level of reporting. Further guidance from the Treasury Department is expected.

X. Short Form Loan Forgiveness Application

In recognition of the significant cost and effort required to prepare the loan forgiveness application, the Treasury Department and the SBA released a short form forgiveness application called the PPP Loan Forgiveness Application Form 3508EZ⁷ for borrowers who can meet one of the following requirements:

- a. the borrower is self-employed, an independent contractor, or sole proprietor who had no employees at the time of submitting the PPP loan application and did not include any employee salaries in the computation of average monthly payroll in the Borrower Application Form; or
- b. the borrower did not reduce the annual salary or hourly wages of employees who received an annualized rate of pay in 2019 of \$100,000 or less during the 24-week (or 168-day) period or 8-week (or 56-day) covered period, as applicable, by more than 25% compared to the period between January 1, 2020 and March 31, 2020; and one of the following:
 1. the borrower did not reduce the number of employees or the average paid hours of employees between January 1, 2020 and the end of the applicable covered period, taking into consideration the exceptions described and safe harbor summarized in Section VIII above; or
 2. the full-time equivalency has not been restored because the business is unable to return to the same level of business activity due to compliance with guidance issued by the Secretary of Health and Human Services, the Director of the Centers for Disease

⁷ The PPP Loan Forgiveness Application Form 3508EZ can be found [here](#). The full instructions can be found [here](#).

Control and Prevention, or the Occupational Safety and Health Administration during the period March 1, 2020 to December 31, 2020.

The short form application requires the borrower to make representations and certifications that the loan proceeds were used for the permitted uses, payroll costs account for 60% of the forgiveness amount, compensation paid using the loan proceeds does not exceed an annual rate of \$100,000, salaries and wages were not reduced more than 25%, the borrower has accurately verified payments for which the borrower is requesting forgiveness, and the borrower has submitted required documentation to the lender.

XI. Additional Considerations For Public Companies

On June 23, 2020, the staff of the Division of Corporation Finance of the Securities and Exchange Commission (the “Staff”) issued guidance regarding disclosures companies should consider regarding operations, liquidity, and capital resources due to business and market disruptions related to the COVID-19 pandemic. The Staff advises that businesses receiving federal assistance should consider the short- and long-term impacts of that assistance. Specifically, the business should consider whether the assistance involves new material accounting estimates or judgments that should be disclosed and what accounting estimates and uncertainties are involved. The Staff noted that it would not object to a business accounting for a loan under the Paycheck Protection Program as either debt or a government grant, if conditions are met to demonstrate that it is probable that the business will qualify for loan forgiveness.⁸

XII. Conclusion

The Paycheck Protection Program has evolved since its implementation in attempt to meet the needs of small businesses and not-for-profit organizations. especially due to the lengthening of the anticipated road to recovery from the pandemic and its economic consequences. Despite the many changes and clarifications, there remains a push for legislation and guidance to provide for additional borrowing, as well as for some level of automatic loan forgiveness. Further changes and guidance are likely as the impact of COVID-19 continues, in order to provide small businesses and not-for-profit organizations and their employees a clearer way forward in these uncertain times.

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If you have any questions about the issues addressed in this memorandum or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email authors Helene R. Banks at 212.701.3439 or hbanks@cahill.com or Robyn Sablove at 212.701.3753 or rsablove@cahill.com; or email publications@cahill.com.

⁸ For more information, see “Coronavirus (COVID) – Disclosure Considerations Regarding Operations, Liquidity, and Capital Resources,” found [here](#).