



MEMBER GUIDANCE: PAYMENT PROTECTION PROGRAM LOANS AT SBA

(Updated as of March 31, 2020 - 10:30 P.M.)

This week the Department of Treasury released guidance on implementation of the Paycheck Protection Program (PPP) at the Small Business Administration (SBA), which, most notably, forgives substantial portions of the loan when spent on allowed expenses. There are, as expected, several notable changes in the guidance that may impact your business. Unfortunately, the changes announced this week may significantly decrease the value of this loan program to your business. Please read this closely and reach out with any questions. **This guidance supersedes all former guidance which may no longer be accurate.**

NEW GUIDANCE...Key pieces of information from this week's guidance:

- Fixed loan terms of 2 years and a set 0.5% (50bps) interest rate. Banks must follow these terms.
- 75% of forgiven loan amount must go to payroll (this is a new requirement and not in the law).
- Small businesses and sole proprietorships can apply through a bank beginning April 3, while independent contractors and self-employed individuals can apply beginning April 10 (this was not in the law).
- Non-SBA lenders will be added as soon as they are approved by SBA and Treasury.
- The limitation on non-profits to only 501c3 organizations is not found in the guidance.

(CONTINUED)

- Average payroll costs for 2019 (x 2.5), not the previous 12 months, will be used for loan size calculation.
- Loan size is significantly less generous than legislation: benefits are included in \$100,000 cap per employee and cap is now firmly set at \$100,000 regardless of calculation.
- Payments to 1099s are now unclear as being allowed for loan size or forgiveness.
- As predicted, but now confirmed, companies have until April 26 as safe harbor for reduction of salary or headcount
- Interest will accrue (at 0.5%) during loan period, but is deferred for 6 months (unclear if interest is due if all of loan is forgiven).
- 2019 tax documents will be used determine loan size.



MEMBER GUIDANCE: PAYMENT PROTECTION PROGRAM LOANS AT SBA

(for business under 500 employees)

With the CARES Act (stimulus package) signed into law, many employers are seeking clarity on what was included and how it impacts them. One of the key provisions of the 880-page bill is the creation of the Paycheck Protection Program Loans at the Small Business Administration (SBA), which, most notably, forgives substantial portions of the loan when spent on allowed expenses.

SAY THAT AGAIN...THE LOAN IS FORGIVABLE?

This is the cornerstone of the small business relief and has \$350 billion set aside to pay for it. The loan details are below, but in short, businesses can borrow money and amounts spent on operational expenses for two months will be paid back. Interested? You should be! The questions below will give more clarity.

Note: *We expect demand for these loans to be exceedingly high. You should engage your banker immediately and begin preparing the necessary paperwork. All of that is covered below.*

AM I ELIGIBLE?

Businesses with fewer than 500 employees (including the self-employed) are automatically eligible, as are the following groups (under 500 employees): franchisees, recipients of SBIC investments, and 501(c)(3) organizations (and non-profit veterans and tribal organizations). Note: each person counts as an employee, regardless of part or full-time or hourly vs. salaried status. Also note, businesses with investors that control the company, may be found "affiliated" which could combine employee totals. More on affiliation here.

Your business must have been in existence before February 15, 2020.

I HAVE MORE THAN 500 EMPLOYEES. DOES THAT MEAN I CANNOT PARTICIPATE? IS THERE OTHER RELIEF?

Certain industries are allowed to have up to 1,250 employees and still qualify. You can check your industry "size standard" here. Many manufacturing (and other seemingly random industries) have larger size standards, so make sure! Businesses in the food and hospitality sectors are allowed to have more than 500 employees, but not more than 500 per location.

In addition to the small business lending programs (PPP is one of several, but certainly the most robust), there are additional programs across government to support businesses. Additional legislation is also expected (and can be shaped). Please reach out for questions about accessing this additional relief.

OKAY, SO I AM ELIGIBLE, AND THE LAW PASSED. DOES THAT MEAN THE LOANS ARE AVAILABLE NOW?

No. Beware of fraudulent sites offering these loans already! Lenders are working with the government to understand how this new program will function and will then roll out loans on a bank-by-bank basis. The timeline for implementation is unclear, though efforts are being made to expedite the process as much as possible.

USBC INSIGHT: Banks are racing to get this set up, but there was confusion as the legislation was put together on the back-end operation. Loans may start being available in early-April, but that may prove optimistic.

HOW LARGE OF A LOAN CAN I GET?

Loans are limited to the lesser of \$10 million or 2.5 multiplied by average total monthly payroll costs for 2019. For example, if a business with \$100,000 average payroll costs in 2019:

Average Total Monthly Payments for Payroll Costs in 2019 x 2.5

$$\$100,000 \times 2.5 = \$250,000$$

If you received a disaster loan after January 31, 2020, you may add that disaster loan balance into this loan to refinance. Note: for all aspects of this loan program, if you are a seasonal employer, there are modifications. Similarly, if you were not in business until this year, there are modifications.

USBC INSIGHT: This number and the forgiveness number want to be as large as possible. You will not have to make payments on this loan in 2020. Use the full definition of payroll cost (see next).

DEFINE "PAYROLL COSTS" PLEASE.

The Treasury Department is limiting the total payroll cost for an employee to \$100,000. That includes:

1. Compensation: Salary/Wages/Commissions and Cash Tips or Equivalent
2. Leave: vacation, parental, family, medical, or sick
3. Allowance for dismissal or separation (this is not defined)
4. Group health benefits including premiums
5. Retirement benefits
6. Employee state and local taxes

Payroll costs do not include and/or are limited by:

1. The maximum per employee is \$100,000. We believe, per guidance, this includes all benefits listed above. **This is a significant change.**
2. Federal Income Taxes (IRS Chapters 21, 22 and 24), which include FICA (Medicare, Social Security) taxes, Railroad Retirement Taxes and regular income withholding (federal) cannot be included.

3. Compensation of employees who live (principal place of residence) outside the United States, and
4. Sick or family leave already being paid for through the phase 2 (March 18) legislation.

PAYROLL COSTS DO NOT INCLUDE AND/OR ARE LIMITED BY:

1. For compensation and payments to 1099, you can only count up to \$100,000 for calculations after February 15, 2020. The principle here is government is only subsidizing up to \$100,000 in income. An example: Employee A makes \$240,000 annually (including all benefits, etc. for simple calculation) and payroll is being calculated on April 1, 2020 for purpose of loan size. March 2019 – January 2020 payroll is \$20,000. For half of February (days 1-14), the full payroll can be counted (\$10,000). The maximum for the second half of February and March however is a pro-rated \$100,000 salary see calculation below), so we can \$8,333 for March and \$4167 for an additional \$12,500. **Employee A's adjusted payroll cost is \$225,000 (from \$240,000).**

For bi-weekly and semi-monthly payroll that is:

Bi-weekly (26 paychecks):

\$100,000 / 26 = \$3,846 per pay period

Semi-monthly (24 paychecks):

\$100,000 / 24 = \$4,167 per pay period

2. Federal Income Taxes (IRS Chapters 21, 22, and 24), which include FICA (Medicare, Social Security) taxes, Railroad Retirement Taxes and regular income withholding (federal) cannot be included.
3. Compensation of employees who live (principal place of residence) outside the United States, and
4. Sick or family leave already being paid for through the phase 2 (March 18) legislation.

OKAY, SO NOW I KNOW HOW MUCH I CAN ASK FOR. CAN I USE IT FOR ANY EXPENSE?

No, but the allowable costs are pretty broad. The basic principle is you cannot use it to increase your assets (paying principal on a mortgage or buying new machinery). The loan is to keep employees, but also covers:

1. The “payroll costs” defined on page 2
2. Mortgage interest (but no payment of principal or prepayment)
3. Rent and utilities
4. Interest on any debt obligation incurred prior to February 15, 2020
5. Post-January 31, 2020 Economic Injury Disaster Loans (EIDL) can be refinanced into the loan

We are getting additional clarity, but currently we believe the loan amount must be used in its entirety by June 30, 2020.

WHAT ARE THE LOAN TERMS?

Ideally, much of the loan is forgiven as detailed below. There are no fees to the borrower and any unforgiven loan amounts have no payments due for six months. There is no personal guarantee or collateral requirement, and the normal SBA “cannot get credit elsewhere” test is entirely waived. Remaining balances (after forgiveness) will have a two (2) year term and 0.5% interest rate (note: these are new).

Business owners must certify to lenders that:

1. The loan is needed due to the uncertain economic conditions;
2. Funds will be used to retain workers, make payroll, or mortgage, rent and utility payments; and
3. They are not duplicating this loan application with other relief programs (including other SBA loans).

GET TO THE GOOD PART. HOW DOES THE FORGIVENESS WORK?

All squares are rectangles, but not all rectangles are squares. All loan forgiveness expenses are allowed under the loan, but not all expenses allowed under the loan will be forgiven.

Certain expenses paid for by the loan will be entirely forgiven if incurred within eight (8) weeks of loan origination. Loan forgiveness does not count as income for tax purposes. The definitions and rules for this section are not necessarily the same as definitions for what is covered by the loan. The following expenses within 8 weeks of loan origination will be forgiven:

1. Payroll costs (defined on p. 2) pro-rated to \$100,000 per employee
2. Interest on mortgages or rent (with a lease) *in place before February 15, 2020*
3. Utilities for: electricity, gas, water, transportation, telephone, or Internet access where service was *in place before February 15, 2020*

The amount to be forgiven is reduced should employer either: a) terminate employees or b) reduce wages as discussed below. While not defined in the bill, we believe Full Time Employees (FTEs) are as defined in [4980H of the Internal Revenue Code of 1986](#) but also include equivalent employees (e.g. 2 half-time employees are 1 FTE)

- Reduction based on number of employees (denominator is borrower's choice):
Initial Forgiveness Amount
x Average FTEs during 8 weeks (calculated each pay period)
Average FTEs from FEB-JUN 2019 or JAN-FEB 2020
- Reduction based on salary/wages: If employer decreases salaries by more than 25% (compared to Q1 2020), their loan forgiveness is similarly decreased. However, employees earning more than \$100,000 pro-rated for any pay cycle (\$4,167 or \$3,846) in 2019 do not count for the purposes of this section.

- Neither reduction is enforced if reductions of employee count or salary were done between February 15 and April 26, 2020 and those reductions are reinstated by June 30, 2020.

USBC INSIGHT: Many companies have already taken action with regards to staffing and wages. Generally speaking, companies are safe to make these decisions as long as they are in proper parameters by June 30, 2020. This is also the section of legislation that has most potential implications by employer choices. Finally, this section is also open to flexibility from Treasury and SBA.

WHAT KIND OF DOCUMENTS ARE GOING TO BE NEEDED?

Everything described thus far will need documentation, including the establishment of a loan maximum (2.5 x payroll) as well as demonstrating proper actions for loan forgiveness. Below is what is listed in legislation, but we expect lenders to require additional information. Employers should be gathering all of this as soon as possible to expedite loan process.

1. Payroll tax filings reported to the IRS (both in aggregate and individual employees)
2. State income, payroll, and unemployment insurance filings
3. Canceled checks, payment receipts, transcripts of accounts,
4. Mortgage, lease, rent contracts and payments

Lenders must make a determination on forgiveness within sixty (60) days.

WILL EVERY BANK BE A PART OF THE PROGRAM? MORE IMPORTANTLY, IS MY BANK?

Banks can decide to participate, and we expect many of the major institutions to do so. Smaller banks, including community and regional banks, may elect not to because of paperwork concerns as well as possible additional requirements if they do significantly more lending (which this program may cause).

Many non-bank lenders are considering joining the program (depending on approval of SBA and Treasury). This may significantly expand options and expedite the lending process. Stay tuned on this front.

USBC INSIGHT: Be talking to your banker now. If they are participating, use this memo to show you understand the program (likely in more granular detail than the bankers!) and discuss what documents and preparation you can be doing now. Banks have signaled they will serve existing customers first, so if your bank is not participating, you should immediately explore other options (like moving banks).

HOW DOES THIS COMPARE TO OTHER LOAN PROGRAMS? WHAT ABOUT ANY EXISTING SBA LOANS?

This is the centerpiece of the stimulus package for small businesses. The loan forgiveness generally makes it the most generous of the programs. There are, however, other lending options. For example, if your most immediate need is small dollar (\$10,000 or less) cash, the new EIDL grants will advance \$10,000 within 3 days of loan application. Even if the loan is denied, the advance does not need to be repaid.

For pre-existing SBA loans, SBA will make the next six months payments of both principal and interest.

SO, I CAN GET \$10,000 FAST THROUGH AND EIDL LOAN AND FORGIVENESS THROUGH PPP?

Yes. But the programs are designed to prevent double-dipping. If you take an EIDL grant, it will be deducted from your forgiveness and having multiple loans may cause complications with your PPP loan.

Best Practices for Businesses During Crisis

We are in continuous conversation with policymakers, trade associations, business owners and financial experts. These are a few recommendations we have aggregated. These may be reproduced for organizational use and distributed widely. These should not be construed as financial or banking advice and every business will face unique challenges.

- 1. Engage your trusted advisors immediately.** Approach your banker, lawyer, accountant and key suppliers to understand options ahead of you. Prepare metrics like biweekly payroll, employee head count, accounts payable and receivable, etc. Understand where your first crisis is going to come from. Knowing these numbers will be critical for business owners facing tough decisions including securing additional capital.
- 2. Free up cash.** If needed, approach all your fixed payment recipients for forgiveness/forbearance. This includes any outstanding debt (to bank and non-bank lenders), landlord, utilities, etc. A number of entities are rolling out assistance programs for which you may qualify.
- 3. Engage corporate customers.** Some major companies are instituting support mechanisms for small businesses within their own supply chain. Facebook announced a \$100 million fund along these lines.
- 4. Engage your own supply chain.** Communicate with all your vendors and understand which, if any, have flexible payment terms. Identify which vendors are critical (e.g. raw materials for production vs. non-essentials).
- 5. Find new support structures.** Following this crisis is proving almost impossible given the unique impact on American way of life. Engage other business owners to understand their challenges and solutions. Consider SBA resource partners of local community small business experts (e.g. CDFIs).

ADDITIONAL LOANS TO MID-SIZE BUSINESSES

(for business with 500 employees or more)

While not eligible for paycheck protection loans, mid-size businesses – those with 500 to 10,000 employees – are also eligible for direct loans under the Emergency Relief and Taxpayer protections portion of the CARES Act. For a business to receive this type of loan under the Act, it must make a “good-faith certification” that it will comply with certain requirements listed in the CARES Act. This certification will likely occur on a form provided as part of the application for the loan and the failure to comply with the certifications could result in the rescission of the loan.

There are several certifications that any business applying for a loan should be aware of and discuss with counsel before accepting such a loan. Among other things, the business must certify that:

1. It intends to re-store at least 90% of its workforce that existed as of February 1, 2020, to include re-storing all compensation and benefits for those employees as of the same date. This restoration must be accomplished no later than 4 months after Health and Human Services declares an end to the public health emergency related to COVID-19;
2. It will not outsource jobs for the term of the loan (which cannot exceed five years) and for two years after repaying the loan;
3. It will not “abrogate” an existing collective bargaining agreement for the term of the loan and for two years after completing repayment of the loan. This language may impede efforts to engage in concessionary bargaining in the midst of such agreements;
4. It will remain “neutral in any union organizing effort for the term of the loan.” The term “neutral” in the context of union organizing has traditionally been used to impose significant restrictions on employer conduct beyond those imposed by other federal labor laws and regulations imposed by agencies such as the National Labor Relations Board (NLRB). A business subjecting itself to these terms may therefore limit the extent to which it could otherwise resort to its lawful “free speech” rights under these circumstances.

EMPLOYEE RETENTION TAX CREDIT

The CARES Act also provides a new “employee retention tax credit.” It is important to note, however, that this tax credit is not available to employers that receive the small business “paycheck protection” loans.

The employee retention tax credit provides eligible employers with a refundable payroll tax credit for 50% of the wages paid by employers during the COVID-19 crisis and applies to wages paid between March 13, 2020 and the end of the year. This tax credit is available to employers whose:

- Operations were fully or partially suspended due to a COVID-19 related “shut-down order,” or
- Gross receipts declined by more than 50% when compared to the same quarter in the previous year.

The tax credit is provided for the first \$10,000 of qualified wages paid to an eligible employee, which may include the employer’s contribution to the employees’ health insurance costs but will exclude any amounts that the employer already received a tax credit for under EFMLA or EPSL. For employers with more than 100 full-time employees, “qualified wages” will be further limited to wages paid to employees when they are not providing services due to the reasons specified above. For employers with 100 or fewer employees, employee wages may qualify for the credit, whether the employer is open for business or subject to a shut-down order.

PAYROLL TAX “HOLIDAY”

In order to assist employers with immediate cash-flow issues, the CARES Act also provides that employers may defer payment of their portion of Social Security taxes they would otherwise be obligated to pay. Any deferred payroll taxes would be required to be paid over the next two years – with half of the owed amount being required to be paid by December 31, 2021, and the remaining half by December 31, 2022. This payroll tax “holiday” may provide additional assistance to employers during this period of crisis.

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