

Contact

Houston

1200 Smith Street, Suite 1400
Houston, Texas 77002-4310
Tel: 713.658.1818
Fax: 713.658.2553

Atlanta

191 Peachtree Street, N.E.,
Forty-Sixth Floor
Atlanta, Georgia 30303
Tel: 404.659.1410
Fax: 404.659.1852

Philadelphia

50 South 16th Street, Suite
1700
Philadelphia, PA 19102
Tel: 610.772.2300
Fax: 610.772.2305

San Antonio

112 East Pecan Street, Suite
1450
San Antonio, Texas 78205
Tel: 210.253.8383
Fax: 210.253.8384

Paycheck Protection Program Loans Under the CARES Act

Chamberlain Corporate Update - Paycheck Protection Program Loans Under the CARES Act

April 6, 2020

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act" or the "Act") was signed into law. The CARES Act, among other things, provides certain employers (generally, those with 500 or fewer employees, discussed below) an opportunity to apply for an SBA loan of up to \$10 million to cover payroll costs and other operation expenses. Our previously published summary of the Paycheck Protection Program loans ("PPP Loans") under the CARES Act is accessible here.

Last week, the Small Business Administration issued guidance, Interim Final Regulations, and an Application form, each of which provide further clarity as to how the PPP Loans may be applied for and how the funds may be used and forgiven. Certain key points in the currently available clarifying documents are addressed below.

When to Apply

As of April 3, 2020, businesses are able to apply for a PPP Loan. Independent contractors and sole proprietorships are able to apply for a PPP Loan as early as April 10, 2020.

Exclusion of Independent Contractors

Independent contractors are not counted as "employees" when determining if the borrower has 500 or fewer employees. Also, payments to independent contractors are not included in payroll costs or the calculation of the maximum loan amount. The Interim Final Regulations clarify that payments to independent contractors are excluded because the independent contractor itself is eligible to apply for a PPP Loan.

Restrictions Related to U.S. Residency

The form of PPP Loan application issued last week included a statement that an entity owned 20% or greater by a person who is not a U.S. Citizen or Lawful Permanent Resident would not qualify for a PPP Loan. That statement was removed from the current application, issued Friday, April 3, 2020. However, the final determination of whether foreign-owned entities are eligible for a PPP Loan will ultimately reside with the lender. Borrowers with foreign ownership or non-U.S. holding companies should discuss eligibility with their lenders and advisors.

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Regardless, the restriction remains that payroll costs will not be counted for those employees whose principal place of residence is outside the U.S., nor will such payroll costs be forgiven.

Additional Exception to Affiliation Rules for Certain Faith-Based Organizations

When determining if an entity has 500 or fewer employees, the CARES Act waives the application of affiliation rules for (1) any business concern with 500 or fewer employees that, as of the date of the loan disbursement, is assigned a North American Industry Classification System (NAICS) code beginning with 72 (accommodation and food service establishments), (2) any business concern operating as a franchise with a franchise identifier code assigned by the SBA, and (3) those businesses that receive financial assistance from Small Business Investment Companies (SBICs). The Interim Final Regulations regarding affiliation provide an additional exemption for faith-based organizations. Specifically, an entity will not be considered an affiliate of a faith-based organization if its relationship with the faith-based organization is based on a religious teaching or belief or otherwise constitutes part of the exercise of religion.

Clarification on Interest Rate and Maturity Date

In the event any portion of the PPP Loan is not forgiven, the remaining loan will bear an annual interest rate of 1.0% and will mature in two (2) years.

Household Employers are Excluded

Household employers are those individuals who employ household employees, such as nannies or housekeepers. The Interim Final Regulations provide that household employers will not qualify for a PPP Loan.

One Loan Per Applicant

The SBA has limited each applicant to one loan. For example, your business cannot apply for a \$5 million PPP Loan in April and another \$5 million PPP Loan in June. Rather, if your business applies for a PPP Loan in April 2020, it is prohibited from applying for another loan later in the covered period (February 15, 2020 through June 30, 2020). The Interim Final Regulations encourage businesses to apply for the maximum loan amount available to them.

Permitted Loan Uses

The Interim Final Regulations provide further clarity on the permissible use of PPP Loan funds. Specifically, the PPP Loan may be used for any of the following:

- 1 Payroll costs;
- 2 Costs related to the continuation of group health care benefits during periods of paid sick, medical or family leave, and insurance premiums;
- 3 Mortgage interest payments (but not mortgage prepayments or principal payments);
- 4 Rent payments;

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- 5 Utility payments;
- 6 Interest payments on any other debt obligations that were incurred before February 15, 2020; and/or
- 7 Refinancing an SBA Section 7(b)(2) disaster loan made between January 31, 2020 and April 3, 2020. Notably, if your disaster loan was used for payroll costs, your PPP Loan must be used to refinance your disaster loan.

Changes to Forgiveness

Generally, so long as the borrower does not reduce its workforce or reduce its workforce's pay by more than 25% during the covered period, the PPP Loan will be forgiven in an amount equal to the permissible costs actually incurred in the eight (8) week period immediately following the disbursement of the loan (the "Forgiveness Period").

The Interim Final Regulations and Application further limit the forgiveness provisions. Currently, payroll costs must comprise at least seventy-five percent (75%) of the total forgiveness amount. That is to say, if the borrower had payroll costs of \$75,000 during the Forgiveness Period, the maximum amount of non-payroll costs that will be forgiven is \$25,000.

The forgiveness amount will also be reduced by any advance the borrower receives under a SBA Section 7(b)(2) disaster loan under the CARES Act.

Forgiveness Documentation Provided to Lender

Regulations regarding PPP Loan forgiveness are forthcoming. However, available guidance materials indicate that the following documentation should be provided when applying for loan forgiveness:

- 1 Documentation verifying the number of full-time equivalent employees on payroll;
- 2 Dollar amounts of payroll costs;
- 3 Dollar amounts of covered mortgage interest payments;
- 4 Dollar amounts of covered rent payments; and
- 5 Dollar amount of covered utilities.

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