WINSTON & STRAWN LLP

CLIENT ALERT

SBA Paycheck Protection Program Update - SBA and Treasury Department Publish Loan Program Details and Application

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This briefing was originally written on March 26 and was updated on April 1.

On Tuesday, March 31, 2020, the U.S. Small Business Administration ("SBA") and U.S. Department of the Treasury published new details regarding the Paycheck Protection Program ("PPP") established by the Coronavirus Aid, Relief, and Economic Security Act ("CARES" or "CARES Act"). SBA and the Treasury Department released a sample form of PPP loan application and announced that applications will be accepted by participating lenders beginning on Friday, April 3, 2020. SBA and the Treasury Department also announced that all PPP loans have a 0.5% interest rate and a two-year maturity, both of which are well below the maximum level permitted by the CARES Act. While questions remain, these announcements mark an important step in implementing the PPP, which will make forgivable loans of up to $10 million available to qualifying small businesses. To view the PPP loan application and other information provided by SBA and the Treasury Department, visit SBA's PPP page or the Treasury Department's CARES Act page. Please see below for a brief summary of the main provisions of the CARES Act applicable to PPP loans.

Who is eligible for PPP loans?

A business, including a qualifying nonprofit organization, is eligible for PPP loans if it has an employee headcount that is lower than the greater of (i) 500 employees or (ii) the employee size standard, if any, under the applicable North American Industry Classification System (NAICS) Code. Businesses that fall within NAICS Code 72, which applies to accommodations and food services, are also eligible if they employ no more than 500 people per physical location. Businesses that meet the applicable NAICS Code-based size standard or other applicable 7(a) loan size standard should also be eligible, but this is not addressed in the PPP loan application. Sole proprietorships, independent contractors, and self-employed individuals are also eligible. It is unclear as of what date the size test will be applied, but historically, SBA size tests have been applied on the date of application for financing. More information on the NAICS-Code-based size standards can be found here: https://www.sba.gov/document/support--table-size-standards

How do affiliates, such as private equity sponsors, affect eligibility for PPP loans?

Applicants for SBA loan programs, including PPP loans, are typically combined with their affiliates when applying size tests to determine eligibility. Affiliation can be based on factors such as ownership of a majority of voting equity, ability to block a quorum of directors for board action, economic dependence, management rights, and being under common control. In some circumstances, a minority owner may be deemed an affiliate of a business by virtue of contract rights, such as veto rights. A business that is controlled by a private equity sponsor would likely be deemed an affiliate of each of the other businesses controlled by that sponsor, and combining the employees of those businesses when applying the size test could render that business ineligible for PPP loans. However, the CARES Act waives the affiliation requirement for the following applicants:

1. Businesses within NAICS Code 72 with no more than 500 employees
2. Franchises with codes assigned by the SBA, as reflected on the SBA franchise registry
3. Businesses that receive financial assistance from one or more small business investment companies (SBIC)

How are PPP loans made?

PPP loans will be made by lenders who are currently approved as 7(a) lenders or who are approved by the SBA and the Treasury Department to become PPP lenders. PPP lenders are delegated authority to make and approve PPP loans, with no additional SBA approval required. PPP lenders are only required to consider whether an applicant was in operation on February 15, 2020, and either had employees for whom it paid salaries and payroll taxes or paid independent contractors. Unlike other 7(a) loans, applicants are not required to show that credit is unavailable elsewhere or demonstrate repayment ability. PPP loans are backed by a 100% guaranty from SBA. Participating lenders will begin accepting PPP loan applications on April 3, 2020.

How much can be borrowed in PPP loans?

The CARES Act increases the maximum availability of 7(a) loans, including PPP loans, to $349 billion. The maximum PPP loan available to any business is $10 million or, if less, 2.5 times the average monthly payroll costs of the business over the year prior to the making of the loan (practically, this may become the year prior to the loan application), excluding the prorated portion of any annual compensation above $100,000 for any person. Note that under the CARES Act, “payroll costs” include vacation, parental, family, medical, and sick leave; allowances for dismissal or separation; payments for group health care benefits, including insurance premiums; and retirement benefits. Calculations vary slightly for seasonal businesses and businesses that were not in operation between February 15 and June 30, 2019.

How can PPP loan proceeds be used?

PPP loan proceeds are generally to be used for:

- Payroll costs, excluding the prorated portion of any compensation above $100,000 per year for any person
- Group healthcare benefit costs and insurance premiums
- Mortgage interest (but not prepayments or principal payments) and rent payments
- Utilities

What are the primary terms of PPP loans?

PPP loans bear 0.5% interest and mature in two years. Payments under PPP loans and all other 7(a) loans will be deferred for six months, and the SBA is directed to issue guidance on the terms of this deferral. Unlike other 7(a) loans, PPP loans have no collateral or personal-guarantee requirements. There will be no recourse to owners of borrowers for non-payment, except to the extent proceeds are used for an unauthorized purpose. For PPP loans, the SBA has waived prepayment penalties and has waived the guaranty fee and annual fee applicable to other 7(a) loans.

Can PPP loans be forgiven?

PPP loans can be forgiven to the extent that the loan proceeds have been used for the following costs incurred and payments made during the eight-week period after the loan is made:

- Payroll costs, excluding the prorated portion of any compensation above $100,000 per year for any person
- Group healthcare benefit costs and insurance premiums
- Mortgage interest (but not prepayments or principal payments) and rent payments on mortgages and leases in existence before February 15, 2020
- Certain utilities, including electricity, gas, water, transportation, and phone and Internet access for service that began before February 15, 2020

However, the amount forgiven is reduced based on failure to maintain the average number of full-time equivalent employees versus the period from either February 15, 2019, through June 30, 2019, or January 1, 2020, through February 29, 2020, as selected by the borrower. The amount forgiven is also reduced to the extent that compensation for any individual making less than $100,000 per year is reduced by more than 25% measured against the most recent full quarter. Reductions in the number of employees or compensation occurring between February 15, 2020, and April 26, 2020 will generally be ignored to the extent reversed by June 30, 2020. Forgiven amounts will not constitute cancellation of indebtedness income for federal tax purposes.

Does having a PPP loan subject a business to terms regarding stock buybacks, dividends, employee retention, or other employment terms?

No. The CARES Act imposes restrictions on relief provided by the Treasury Department, but these types of restrictions do not apply to PPP loans.

Can I get a PPP loan if I got an Economic Injury Disaster Loan?

Yes, to the extent that the disaster loan was used for a purpose other than those permitted for PPP Loans. Disaster loans may be refinanced with proceeds of PPP loans, in which case the maximum available PPP loan amount is increased by the amount of disaster loans being refinanced.

If I'm interested in a PPP loan, whom should I call?

We recommend contacting existing 7(a) lenders as soon as possible to learn what you will need to provide for underwriting and approving a PPP loan.

View all of our COVID-19 perspectives here. Contact a member of our COVID-19 Legal Task Force here.

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