COVID-19 ALERT
PAYCHECK PROTECTION PROGRAM GUIDE

The Paycheck Protection Program ("PPP"), a cornerstone of the Coronavirus Aid, Relief and Economic Security Act (the "CARES Act"), aims to provide relief to small businesses impacted by the COVID-19 pandemic. Since the initial enactment of the CARES Act on March 27, 2020, the Small Business Administration ("SBA"), in consultation with the Department of Treasury, has issued several Interim Final Rules and Frequently Asked Questions intended to provide guidance with respect to the implementation and administration of the PPP. In this alert, we have summarized the principal terms of the PPP, inclusive of recent rules and supplemental guidance.

We continue to monitor the additional rules, interpretations and guidance released by the SBA and Department of Treasury related to the PPP and will update this Paycheck Protection Program Guide as applicable. Our attorneys are available to guide you through this critical time and answer any questions regarding the PPP or other aspects of the CARES Act.

WHO IS ELIGIBLE TO APPLY FOR PPP FUNDING?	
Eligible Borrowers, Generally:	• Businesses (including some non-profits) with fewer than 500 employees with a principal place of residence in the United States, subject to the SBA's existing affiliation rules (detailed below). • Any U.S. business assigned a NAICS Code beginning with 72 (i.e., restaurant and hospitality industry), that employs no more than 500 employees per physical location. • Businesses with more than 500 employees with a principal place of residence in the United States that (i) meet statutory employee-based or revenue-based size standards for the applicants primary industry (based on NAICS Code), or (ii) meet the SBA's "alternative size standard" as of March 27, 2020 (based on maximum tangible net worth of not more than $15 million and average net income after taxes of not more than $5 million for the full two fiscal years prior to the application). • Sole proprietorships, self-employed individuals and independent contractors. Self-employed individuals are eligible to receive a PPP loan if such individual (i) has self-employment income (e.g., independent contractors and sole proprietors), (ii) has a principal place of residence in the United States, and (iii) has filed or will file a Form 1040 Schedule C for the 2019 tax year. In order to be eligible for a PPP loan, the applicant business must have been in operation as of February 15, 2020.

Updated as of June 3, 2020

Specific Exclusions:	The SBA has determined that the following businesses are ineligible to apply for a PPP loan, including:
	x Hedge funds and private equity firms
	x Debtors in bankruptcy proceedings (at the time it submits the application or any time prior to the loan being disbursed)
	x Individuals that employ household employees such as nannies or housekeepers.
	x Businesses owned or controlled by the applicant or any of its owners that are currently delinquent or has defaulted within the last seven years on a direct or guaranteed loan from the SBA or any other Federal agency that has caused a loss to such government agency.
	x Businesses engaged in any activity that is illegal under federal, state or local laws (as determined under SBA regulations).
	x Businesses that are owned 20% or more by someone who is presently (i) incarcerated, (ii) on probation, (iii) on parole, (iv) subject to an indictment, criminal information, arraignment, or by which criminal charges are brought, or (v) has been convicted of a felony or certain other criminal matters in the last five years.
	
	x Certain real estate businesses:
	    x Passive businesses owned by developers and landlords that do not actively use or occupy the assets acquired or improved with the loan proceeds.
	    x Businesses primarily engaged in subdividing real property lots and developing it for resale.
	    x Businesses that are primarily engaged in owning or purchasing real estate and leasing it for any purpose.
	    x Businesses that lease land for the installation of cell phone towers, solar panels, billboards or wind turbines.
	    x Businesses that have entered into a management agreement with a third party that grants the third-party manager sole discretion to manage operations of the business.
	    x Apartment buildings.
	    x Residential facilities that do not provide healthcare or medical services.

Determining Number of Employees for Eligibility Purposes:	• Applicants must include all individuals employed on a full-time, part-time or other basis. • Self-employed individuals and independent contracts are eligible to apply separately, and therefore should be excluded from the calculation for an entity application. • Partners of a partnership are required to apply on behalf of the partnership as a whole, rather than for their own benefit (by claiming "self-employment" income). Such limitation applies equally to members of a limited liability company that files as a partnership for tax purposes.

Required Certification:	• The PPP Borrower Application Form requires applicants to certify as to a number of important matters, including that **"[c]urrent economic uncertainty makes [this] loan request necessary to support the ongoing operations of the Applicant."** Any borrower that submitted an application prior April 23, 2020, and repaid such loan in full by May 18, 2020, will be deemed to have made the required certification in good faith. This "safe harbor" is intended to ensure that borrowers promptly repay PPP loans that were obtained based on misunderstanding or misapplication of the required certification standard, taking into account updated guidance on such standard. • The applicant must: (1) assess their economic need for the loan; (2) certify in good faith that the loan is necessary; and (3) make this certification in good faith, taking into account their current business activity and its ability to access other sources of liquidity sufficient to support ongoing operations in a manner that is not significantly detrimental to the business. While the CARES Act does not require that borrowers be unable to obtain credit elsewhere, access to capital and current financial and business conditions should be carefully analyzed. Each applicant should be prepared to demonstrate to the SBA, upon request, the basis for the determination. • The SBA will review all loans in excess of $2 million, in addition to other loans, as appropriate, following the submission of the loan forgiveness application, to confirm need, eligibility and other compliance matters. The SBA has stated that any borrower that, together with its affiliates, received PPP loans with an original principal amount of less than $2 million will be deemed to have made the required certification in good faith, on the basis that borrowers below the $2 million threshold are generally less likely to have had access to adequate sources of liquidity under the current circumstances. • It is unlikely that public companies with substantial market value and access to capital markets will be able to make the required certification. • *Penalties for False Statements and/or Certifications:* x Imprisonment of up to five years and/or a fine in the amount of up to $250,000 (18 U.S. Code 1001 and 3571); x Imprisonment of up to two years and/or a fine in the amount of up to $5,000 (15 U.S. Code 645); and x If the loan application is submitted to a federally insured institution, imprisonment up to 30 years and/or a fine in the amount of up to $1 million (18 U.S. Code 1014).
HOW ARE AFFILIATED ENTITIES TREATED IN DETERMINING ELIGIBILITY?	
SBA Affiliation Rules:	• Most applicants will be considered collectively with its affiliates for the purpose of qualifying for a PPP loan. Businesses are deemed "affiliated" when they are under common control, which may be exercised through ownership, management or other relationship between the parties.

	○ *Ownership*: A person or entity is deemed an affiliate if such person or entity owns or controls more than 50% of the voting stock of a business concern. Where the voting stock of a business is widely held, or in the event that no person or entity is found to control, the Board of Directors or Chief Executive Officer or President (or other officers, managing members, or partners who control the management of the entity) are deemed to have control. ○ *Minority Shareholders*: A minority shareholder is deemed to be an affiliate of an applicant if such shareholder has control over the business by virtue of the right to prevent a quorum or otherwise block actions by the board of directors or other shareholders. A minority shareholder will not be considered an affiliate of an applicant if such rights are irrevocably waived or otherwise relinquished. ○ *Unvested Rights*: For purposes of determining size, the SBA treats all stock options, convertible securities and agreements to merge as fully vested and/or exercised. Options, convertible securities and agreements that are subject to conditions precedent that are either speculative, unenforceable under applicable law or incapable of fulfillment are not considered vested/effective. ○ *Management*: A person or entity is deemed an affiliate if the Chief Executive Officer or President of the applicant (or other officers, directors, managing members or general partners vested with management authority) also control the management of one or more additional businesses. • Private equity-owned portfolio companies are bound by SBA affiliation rules in the same manner as any other business concern subject to outside ownership or control. • For purposes of determining whether an applicant meets the "500 or fewer" employee size standard, such applicant must count all of its employees, and all employees of its U.S. and foreign affiliates, subject to any applicable exceptions.
Exceptions:	• Businesses operating under NAICS Code 72 (Accommodation and Food Services) with fewer than 500 employees per physical location. Additionally, if each hotel or restaurant location owned by a parent business is a separate legal entity, each such legal entity is eligible to apply for a separate loan so long as such entity uses its unique Employer Identification Number. • Franchises, so long as they are listed on the SBA Franchise Directory. Each franchisee that meets the SBA's applicable size standard is eligible to apply for its own PPP loan. • Government-funded hospitals receiving less than 50% of its funding from state or local governments (exclusive of Medicaid).

	• Faith-based organizations, for which a relationship among affiliated entities constitutes part of religious practice or is otherwise based on sincere religious teachings or beliefs. • A business's participation in an Employee Stock Ownership Plan (ESOP) does not create an affiliation between such business and the ESOP.
HOW IS THE MAXIMUM LOAN AMOUNT CALCULATED?	
Business Applicants:	• **2.5 times** an applicant's average monthly payroll costs for either (i) the trailing 12-month period or (ii) calendar year 2019 *plus* the outstanding amount of any Economic Injury Disaster Loan ("EIDL") made between January 31, 2020 and April 3, 2020 *less* the amount of any advance made under an EIDL COVID-19 loan. If the proceeds of an EIDL were used for payroll costs, the PPP loan must be used to refinance the EIDL. In all cases, the maximum loan amount is capped at $10 million. • Applicants that were not in business from February 15, 2019 through June 30, 2019 may instead use average monthly payroll costs for the period January 1, 2020 through February 29, 2020. • For seasonal businesses, the measurement period with respect to the average monthly payroll calculation may start on February 15, 2019 or March 1, 2019 and end on June 30, 2019, at the applicant's option. • Businesses that are part of a single corporate group shall in no event receive more than $20 million in the aggregate. For purposes of this limitation, businesses are part of a single corporate group if they are majority owned, directly or indirectly, by a common parent.
Self-Employed and Independent Contractors:	*Applicants Without Employees*: **2.5 times** an applicant's average monthly net profit amount, as identified on IRS Form 1040 Schedule C, Line 31 *plus* the outstanding amount of any EIDL made between January 31, 2020 and April 3, 2020 *less* the amount of any advance made under an EIDL COVID-19 loan. All amounts in excess of $100,000 are excluded from net profits and, in all cases, the maximum loan amount is capped at $10 million. *Applicants With Employees*: **2.5 times** an applicant's average monthly payroll costs for fiscal year 2019, plus the outstanding amount of any EIDL made between January 31, 2020 and April 3, 2020 less the amount of any advance made under an EIDL COVID-19 loan. In all cases, the maximum loan amount is capped at $10 million. For purposes of the calculation, payroll costs include: • Net profit amount as reflected on the applicant's 2019 Form 1040 Schedule C, line 31, up to $100,000 annualized. If the net profit amount is negative, this component should be set to zero.

	• 2019 gross wages and tips paid to employees (with a principal place of residence in the United States) on a quarterly basis, calculated using 2019 Form IRS Form 941 (Taxable Medicare Wages & Tips), plus any pre-tax employee contributions for health insurance or other fringe benefits excluded from taxable wages. Amounts in excess of $100,000 per employee must be subtracted, as well as amounts paid to non-U.S. resident employees. • 2019 employer health insurance contributions, retirement contributions and state and local taxes assessed on employee compensation.
Payroll Costs:	*Qualifying Payroll Costs:* • Compensation to U.S. employees in the form of salary, wages, commissions or similar compensation, and cash tips or the equivalent (based on employer records of past tips or a reasonable good-faith employer estimate) • Payment for vacation, parental, family, medical, or sick leave • Allowance for separation or dismissal • Payment for group health care benefits (including insurance premiums) and retirement • Payment of state and local taxes assessed on compensation of employees • For independent contractors and sole proprietors only: wages, commissions, income or net earnings from self-employment or similar compensation *Specific Exclusions:* x Compensation to non-U.S. employees. x Cash compensation (not authorized benefits) in excess of $100,000 per employee on an annualized basis. x Federal employment taxes imposed or withheld between February 15, 2020 and June 30, 2020. x Qualified sick and family leave wages for which a credit is allowed under Sections 7001 and 7003 of the Families First Coronavirus Response Act. x Partnership income, which is instead required to be reported as payroll costs (up to $100,000 annualized) on a PPP loan application filed by the partnership itself. This prohibition applies not only to active partners of a partnership, but also to members of a limited liability company that files as a partnership for tax purposes.

HOW CAN PPP LOAN PROCEEDS BE DEPLOYED? WHAT ARE THE BASIC TERMS?

Non-Payroll Costs:	PPP loan proceeds can be used to cover the following payroll and non-payroll expenses: • Payroll costs (see above) paid or incurred during the covered period. • Costs related to continuation of group health care benefits during periods of paid sick, medical, or family leave, and insurance premiums.

	• Interest on mortgage obligations, where such mortgage obligations were incurred before February 15, 2020. Such mortgage obligations may relate to real or personal property ("Covered Mortgage Obligations"). • Rent obligations under lease agreements in force before February 15, 2020. Such lease obligations may relate to real or personal property ("Covered Rent Obligations"). • Utilities (i.e., utility services for the distribution of electricity, gas, water, transportation, telephone or internet access) for which service commenced prior to February 15, 2020 ("Covered Utility Payments"). • Interest payments on any other debt obligations incurred prior to February 15, 2020. • Refinancing an EIDL loan made from January 31, 2020 through April 3, 2020. An applicant who received an EIDL from January 31, 2020 through April 3, 2020, can apply for a PPP loan. If the proceeds of an EIDL were used for payroll costs, the PPP loan must be used to refinance the EIDL. Proceeds from any advance (up to $10,000) on the EIDL will be deducted from the forgiveness amount on the PPP loan.
Terms:	• *Interest Rate*: 1.0% • *Term*: 2 years • No prepayment penalties or premiums • Loan is unsecured, uncollateralized and is not required to be personally guaranteed. • Payment is deferred for 6 months following the date of disbursement of the PPP loan (however, interest will accrue from the date of disbursement). • PPP loan documentation is not uniform, with each lender using its own form, subject to the PPP requirements and otherwise not inconsistent with the PPP. Applicants should carefully review all terms and conditions prior to executing PPP loan documents to confirm accuracy and to confirm that such terms and conditions are not unnecessarily restrictive.
Disbursements:	PPP lenders must make a one-time, full disbursement of the PPP loan within ten calendar days of loan approval (i.e., upon assignment of a loan number by the SBA). For PPP loans approved prior to April 29, 2020, such ten-day period beings on April 28, 2020, and the eight-week covered period begins on the date of first disbursement.

HOW IS THE FORGIVENESS AMOUNT DETERMINED?	
Generally:	• PPP loans are eligible for forgiveness up to the full principal amount of the loan and any accrued interest. On May 15, 2020, the SBA released the Paycheck Protection Program Loan Forgiveness Application (the "Forgiveness Application") and instructions (the "Forgiveness Instructions"), which details the forgiveness calculation and parameters for eligible PPP borrowers. The SBA issued supplemental guidance by way of Interim Final Rule released on May 22, 2020 (the "Interim Rule"). • Per the Forgiveness Application, the aggregate forgiveness amount is calculated based on the total loan proceeds deployed to cover payroll costs paid or incurred and the non-payroll costs (specified below) over the eight-week period following disbursement of the loan ("Covered Period"), subject to adjustment as detailed below. The Forgiveness Application and Forgiveness Instructions also provide for an alternative eight-week covered period, which would commence on the first day of the first pay period following disbursement of PPP loan proceeds (the "Alternative Payroll Covered Period"). The Interim Rule clarifies that the Alternative Payroll Covered Period is intended only for borrowers operating on a biweekly (or more frequent) payroll cycle. • At least 75% of the loan forgiveness amount must be attributable to payroll costs and not more than 25% of loan forgiveness may be attributable to eligible non-payroll costs (specifically, Covered Mortgage Obligations, Covered Rent Obligations and Covered Utility Payments). All non-payroll costs must be paid during the Covered Period or the Alternative Payroll Covered Period, as applicable, or incurred during such period and paid on or before the next regular billing date (even if such date falls outside of the Covered Period or the Alternative Payroll Covered Period, as applicable). • The Interim Rule clarifies that bonuses or "hazard pay" to an employee during the Covered Period (or Alternative Payroll Covered Period, as applicable) are eligible for loan forgiveness to the extent such employee's total cash compensation does not exceed \$100,000 on an annualized basis. Similarly, the forgiveness amount with respect to owner-employees and self-employed individuals cannot exceed the lower of 8/52 of 2019 compensation or \$15,385 per individual in total across all businesses.
Procedure:	• *Generally*. PPP borrowers may apply for loan forgiveness as early as eight weeks following the initial date of disbursement. Upon receipt of a completed Forgiveness Application, the lender will have 60 days to review and issue a decision with respect to the aggregate forgiveness amount, upon which lender must request payment from the SBA. So long as such determination does not require further SBA review, the SBA will remit the applicable forgiveness amount to the lender, plus any interest accrued through the payment date within 90 days of the lender's initial determination.

	In the event that a PPP loan is deemed ineligible for forgiveness, in whole or in part, the borrower is responsible for repayment of all or the remaining balance of the loan on or before the two year maturity date thereof. The Interim Rule is careful to note that the foregoing process applies only to those Forgiveness Applications not under review by the SBA prior to the lender's decision on the Forgiveness Application. • *Forgiveness Applications Reviewed* by SBA. All PPP loans, regardless of amount, are subject to review by the SBA, at any time and in its sole discretion. Per the Interim Rule, the scope of the SBA's review will largely focus on eligibility determinations, proper use and deployment of PPP loan proceeds and entitlement to forgiveness. o With respect to eligibility, the SBA may review any eligibility determination for compliance with the provisions of the CARES Act, prior SBA rules and related guidance and the terms, information and certifications included in borrower's PPP loan application. o In connection with eligibility review, the SBA may also review whether the loan amount was properly calculated and whether the proceeds thereof were deployed in accordance with CARES Act guidelines (as detailed and clarified by subsequent SBA guidance). o With respect to PPP loan forgiveness, the SBA may review whether a borrower is entitled to forgiveness in the amount claimed on the Forgiveness Application. • In each of the foregoing cases, borrowers will have the opportunity to respond to the SBA, either directly or through its lender, and provide any additional information in support of its position. In the event the SBA determines that borrower is ineligible for a PPP loan, that the loan amount was not properly calculated, or that the forgiveness amount claimed on the Forgiveness Application is improper, the SBA may seek repayment of the outstanding PPP loan balance or pursue "other available remedies". A borrower may appeal any such determination, the specifics of which will be addressed in subsequent SBA guidance.
Adjustments:	Forgiveness amounts are subject to decrease in the event that an applicant (i) reduces its full-time employees, or (ii) decreases salaries and wages by more than 25% for employees making less than $100,000 per year, in each case, during the Covered Period or the Alternative Payroll Covered Period, as applicable, as compared to the periods below. For purposes of determining the workforce reduction amount, the CARES Act uses a "full-time equivalent employee" ("FTE") standard, which is calculated based on the average weekly full-time equivalent employees.

	• *Workforce Reduction*: Workforce reduction during the Covered Period or the Alternative Payroll Covered Period, as applicable, is measured against the period from February 15, 2019 to June 30, 2019 or January 1, 2020 to February 29, 2020 at the borrower's option. For seasonal employers, the applicable measurement period is either of the foregoing periods or the consecutive 12-week period between May 1, 2019 and September 15, 2019. A borrower's aggregate forgiveness amount will be reduced if the average number of full-time equivalent employees during the Covered Period (or Alternative Payroll Covered Period, as applicable) is less than the average number employed during the applicable reference period. o *Full-Time Equivalent Employees*: For purposes of calculating average FTE, the Interim Rule defines a "full-time equivalent employee" as an employee who works an average of forty hours or more per week. For those employees who work less than forty hours, the Interim Rule permits borrowers to elect one of the following calculation options: (A) the ratio of the average number of hours paid per week per individual employee to 40, or (B) full-time equivalency of 0.5 for all part-time employees. While borrower retains discretion, it must apply the selected method consistently to all part-time employees for the Covered Period (or Alternative Payroll Covered Period, as applicable). o The Forgiveness Application provides that the aggregate forgiveness amount will not be reduced for headcount reductions related to: (A) any position for which the borrower has made a good-faith, written offer to rehire an employee during the Covered Period (or Alternative Payroll Covered Period, as applicable), which was rejected by such employee, or (B) any employee who, during the applicable period, (1) was fired for cause, (2) voluntarily resigned, or (3) voluntarily requested and received a reduction of their hours. • C*ompensation Reduction*: Compensation reduction is measured against the employee's most recent full quarter prior to the PPP loan disbursement and applies only to those employees whose salary at no time exceeded $100,000 (annualized). This reduction calculation is performed on a per employee basis, not in the aggregate. In the event that salary/hourly wage levels are ultimately restored, then the applicable reduction may be eliminated. *"Savings" Clause:* Borrowers have until June 30, 2020 to restore (i) any reduction in FTEs that occurred between February 15, 2020 and April 26, 2020 (the "safe harbor period") to at least the number of FTEs employed on February 15, 2020, and (ii) any reduction in salary or wages for each employee in excess of 25% during the safe harbor period in order to regain eligibility for forgiveness of the entire PPP loan amount. If an employee does not accept a rehire offer on comparable terms during the cure period or if the employee is fired for cause, voluntarily resign or requests a schedule reduction, there will not be a reduction in forgiveness. Any replacement of employees by other employees (in the same quantity), will not impact forgiveness.

	In order to avoid duplicate penalties, the Interim Rule further clarifies that the wage/salary reduction applies only to the portion of the decline in employee salary and wages that is not attributable to the FTE reduction.
Unauthorized Use of Proceeds:	In the event that PPP loan proceeds are used for an unauthorized purpose, the entirety of the loan amount used for such improper purpose must be repaid in full. If funds are knowingly used for an unauthorized purpose, the applicant will be subject to additional liability, including charges for fraud. If funds are used for an unauthorized purpose by a shareholder, member or partner of the applicant, the SBA will have recourse against such shareholder, member or partner for the unauthorized use.
Document Retention:	The Forgiveness Application and Forgiveness Instructions require borrowers to retain all PPP loan supporting documentation for a period of six years after the date that the loan is forgiven or repaid in full. Such information includes payroll documentation, documentation supporting borrower's certifications as to the economic necessity of the PPP loan, documentation delivered in connection with, and in support of, borrower's loan forgiveness application and any other records demonstrating material compliance with PPP requirements.

WHAT ARE THE TAX IMPLICATIONS OF OBTAINING A PPP LOAN?

Credits and Deductions:	A borrower is not entitled to payroll tax credits under the CARES Act for employee payments if they have a PPP loan. Any employer may defer payment of the employer's share of social security taxes for wages starting on March 27, 2020 through December 31, 2020. The deferred taxes will be due 50% by December 31, 2021 and 50% by December 31, 2022. The proceeds of PPP loans are used to pay salary, rent and certain other operational expenses, which would normally be tax deductible for a business. In the event a loan is forgiven, the borrower will not recognize income upon cancellation of the debt. In that case, allowing a tax deduction for the salary, rent and other expenses paid by the borrower would produce a tax windfall to the borrower. In recognition of this special situation, the IRS released Notice 2020-32, which states that no deduction should be allowed for such expenses if the repayment of the loan is forgiven.

APPLICATION AND ADDITIONAL GUIDANCE	
Application:	The SBA-approved Borrower Application Form can be found here. All applications should be submitted directly to the applicant's lender (not to the SBA). As demonstrated by the first round of applications, PPP funds are expected to be in high demand and will likely exhaust quickly.
SBA Guidance:	The SBA, in consultation with the Department of Treasury, is continuously releasing additional guidance with respect to the PPP. An up to date listing of all SBA interim final rules, frequently asked questions and supplemental guidance, can be found here, under the heading "Program Rules".
Additional Assistance:	We are continuing to monitor as additional guidance is released by the SBA and Department of Treasury and will provide updates to this guide as appropriate. Our attorneys are available to answer any questions and assist in determining how best to navigate these relief measures for the benefit of your business.

For additional information on the COVID-19 pandemic, the CARES Act and the Paycheck Protection Program, please visit the Resource Center on our website:

Resource Center

CONTACTS

Samantha Epstein
Associate
TEL: 646-563-8928
M: 516-526-3127
sepstein@coleschotz.com

Philip Hirschfeld
Associate
TEL: 646-563-8955
M: 917-763-6704
phirschfeld@coleschotz.com

Jennifer Horowitz
Member
TEL: 201-525-6214
M: 917-561-4466
jhorowitz@coleschotz.com

Roger Iorio
Member
TEL: 201-525-6312
M: 201-248-1526
riorio@coleschotz.com

Christopher Kula
Member
TEL: 646-563-8929
M: 646-563-7929
ckula@coleschotz.com