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How PPP Loans Work for Sole Proprietors and Freelancers

It's fairly simple, but the money is going fast



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It's become increasingly clear PPP loans are the hot ticket in the new CARES Act. Hundreds of thousands of officially “incorporated” small businesses **with**

employee payroll expense have already applied for a PPP loan and the money is starting fund (not to mention run out!)

For unincorporated freelancers and sole proprietors **it's been more frustrating**. Until yesterday, no one (including the banks) really understood how PPP loans might work for self-employed folks without employees. That all changed with recently-released guidance from the SBA.

Here is an oversimplified summary of how PPP loans work for sole proprietors and freelancers *without employees*:

Point 1 — The loan is based on 2019 Schedule C income:

1. In fact, a copy of the 2019 Schedule C tax form must be included with the PPP loan app, *even if the applicant hasn't filed their 2019 tax return yet*. This ruling will favor those who already compiled their business tax information for 2019, or better yet filed their 2019 tax return.
2. If 2019 Schedule C income is \$0 or less, a proprietor without employees is **not eligible for a PPP loan**.

Point 2 — The amount of the PPP loan is calculated as follows:

1. Take Line 31 of 2019 Schedule C. If Line 31 is more than \$100,000, use \$100,000.
2. Divide the number by 12 to get average monthly Schedule C net income.
3. Multiply that number by 2.5. This is the amount of the loan.
4. **EXAMPLE:** let's say Line 31 is \$150,000. The loan amount is \$100,000 divided by $12 \times 2.5 = \$20,833$. This example happens to be the maximum loan amount any sole proprietor will be eligible for.

Point 3 — Eventual forgiveness of the PPP loan is calculated as follows:

1. 8 weeks worth of 2019 Schedule C income is forgiven (apparently automatically). For example, if a proprietor had the maximum \$100,000 Schedule C income, the “automatic” forgiveness would $8/52 \times \$100,000 = \$15,384$.
2. In addition, during the 8 weeks following funding of the loan, any business expenses for utilities (including business vehicle gas), rent and interest would be forgiven, up to the remaining unforgiven amount of the loan.

BOTTOM LINE: In simple terms, for a sole proprietor without employees, the maximum loan is \$20,833, of which \$15,384 is apparently automatically forgiven. The remaining \$5,449 can be forgiven if spent on business utilities, rent and interest.

Point 4 — The new SBA guidance also addressed partnerships without payroll expense.

If you have such a partnership, **the *partnership* must apply for the PPP loan.** The loan amount is based on the combined self-employment income of the general active partners up to a maximum of \$100,000 per partner.

For example, take a partnership with \$500,000 in total self-employment income and 3 partners. The maximum loan is \$300,000 divided by $12 \times 2.5 = \$62,500$.

It is presumed (**but not specifically spelled out**) that forgiveness would follow the same vein as forgiveness for sole proprietors. 8 weeks worth of the \$300,000 of self-employment income would be forgiven. Using the above example that would be $8/52 \times \$300,000 = \$46,154$ forgiven.

If partners are not comfortable trusting in automatic forgiveness, it might be wise to issue guaranteed payments (the equivalent of wages) to the partners in

the amount of the expected SE income forgiveness (again, \$46,154 in this example). That would create an audit-able cash trail to support forgiveness.

Like sole proprietor loans, the remainder of the loan could also be forgiven if spent on utilities, rent and interest within 8 weeks of receiving the loan.

Final Thoughts

With these new SBA guidelines, hopefully the banks will be able to quickly and efficiently process loans to self-employed individuals. Unfortunately, though, it appear it will be a matter of days until the initial PPP money runs out. Self-employed PPP loan applicants should act fast or hope Congress acts soon to replenish the PPP loan pool.

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