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Paycheck Protection Program Updates

Economic Aid Act Amendments and Second Draw Loans

Presented to the



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Agenda

- Overview of PPP Changes Under Economic Aid Act
- Overview of Second Draw Loans

Economic Aid Act

- On December 27, 2020, the Economic Aid Act (Act) became law.
- Act extends the authority to make PPP loans through **March 31, 2021**.
- Act also revises certain PPP requirements.
- The SBA published updated regulations on January 6, 2021 which incorporated the changes made by the Act into existing PPP guidance.
- These regulations apply to loan applications, including requests for increases and applications for forgiveness following the enactment of the Act.
- The regulations also apply to loan forgiveness applications submitted before enactment where the SBA has not remitted the forgiveness payment.

Who is Eligible for a First Draw PPP Loan?

- Borrower (together with all affiliates, if any) are:
 - A small business concern under revenue-based size standard established by SBA or under SBA alternative size standard.
 - Independent contractor, eligible self-employed individual, sole proprietor.
 - Business concern, tax-exempt nonprofit under 501(c)(3) and certain other entities that have no more than the greater of 500 employees, or if applicable, the size standard number of employees established by the SBA.
 - Housing co-op, eligible 501(c)(6) or eligible destination marketing organization that employs no more than 300 employees.
 - Certain other entities listed in the regulations.
- Must have been in operation on February 15, 2020 and either had employees who were paid salary and payroll taxes or paid independent contractors (could also qualify as a self-employed individual, independent contractor or sole proprietor with no employees).

Who is Not Eligible?

- Hedge funds and private equity firms,
- Businesses in bankruptcy*,
- Businesses engaged in illegal activity,
- Households,
- Businesses owned at least 20% by certain criminals,
- Businesses that receive grants under the shuttered venue operator grant program,
- Certain entities related to the executive branch or legislative branch,
- Generally, publicly traded entities,
- Businesses that have been delinquent or defaulted on other SBA loans, and
- **An entity that has permanently closed.**

What is the Maximum Loan Amount?

- The maximum loan amount for a first draw loan is \$10 Million or the amount using the payroll-based formula described in the Act, if less.
- Under this formula, the maximum loan amount is $2.5 \times$ average monthly payroll costs.
- To determine average monthly payroll costs, borrowers in 2021 may generally use any of the following in the calculation:
 - Average monthly payroll in 2019,
 - Average monthly payroll determined based on 1-year period before loan is made, or
 - Average monthly payroll in 2020.
- The maximum loan amount for a single corporate group for first draw loans is \$20 Million. This limit applies even where there is a waiver of the affiliation rules for other purposes.

What Qualifies As Payroll Costs?

- The Act clarified the definition of payroll costs.
- Payroll costs consist of compensation to employees (whose principal place of residence is the United States) in the form of:
 - salary, wages, commissions, or similar compensation,
 - cash tips or the equivalent (based on employer records of past tips or, in the absence of such records, **a reasonable, good-faith employer estimate of such tips**),
 - payment for vacation, parental, family, medical, or sick leave,
 - allowance for separation or dismissal,
 - payment for the provision of employee benefits consisting of group health care or group life, disability, vision, or dental insurance, including insurance premiums, and retirement,
 - payment of state and local taxes assessed on compensation of employees,
 - for an independent contractor or sole proprietor, wages, commissions, income, or net earnings from self-employment, or similar compensation.

What Does Not Qualify As Payroll Costs?

- Any compensation of an employee whose principal place of residence is outside of the United States,
- The compensation of an individual employee in excess of \$100,000 on an annualized basis, as prorated for the period during which the payments are made or the obligation to make the payments is incurred,
- Federal employment taxes imposed or withheld during the applicable period, including the employee's and employer's share of FICA taxes, and income taxes required to be withheld from employees, and
- Qualified sick and family leave wages for which a credit is allowed under sections 7001 and 7003 of the Families First Coronavirus Response Act.

How Can a PPP Loan be Used?

- Payroll costs,
- Costs related to the continuation of group health care, life, disability, vision, or dental benefits during periods of paid sick, medical, or family leave, and group health care, life, disability, vision, or dental insurance premiums,
- mortgage interest payments (but not mortgage prepayments or principal payments),
- rent payments,
- utility payments,
- interest payments on any other debt obligations that were incurred before February 15, 2020,
- refinancing an SBA EIDL loan made between January 31, 2020 and April 3, 2020,

How Can a PPP Loan be Used?

- Covered operations expenditures (payments for any business software or cloud computing service that facilitates business operations, product or service delivery, the processing, payment, or tracking of payroll expenses, human resources, sales and billing functions, or accounting or tracking of supplies, inventory, records and expenses),
- Covered property damage costs (costs related to property damage and vandalism or looting due to public disturbances that occurred during 2020 that was not covered by insurance or other compensation),
- Covered supplier costs, and
- Covered worker protection expenditures.
- Important: At least **60% of loan proceeds** must still be used for payroll costs.

Can the PPP Loan be Forgiven?

- The amount of loan forgiveness can be up to the full principal amount of the loan and any accrued interest.
- Eligible borrower will not be responsible for any loan payment if the borrower uses all of the loan proceeds for forgivable purposes and employee and compensation levels are maintained or, if not, an applicable safe harbor or exemption applies.
- Payroll costs that are qualified wages taken into account in determining the Employer Retention Credit are not eligible for loan forgiveness.

Loan Forgiveness and Covered Period

- Amount of loan forgiveness depends, in part, on total payroll costs (including employer contributions for group health, life, disability, vision and dental insurance), payments of interest on mortgage obligations incurred before February 15, 2020, rent payments on leases dated before February 15, 2020, utility payments for service that began before February 15, 2020, covered operations expenditures, covered property damage costs, covered supplier costs, and covered worker protection expenditures **over the loan forgiveness covered period.**
- The “**loan forgiveness covered period**” is the period beginning on the date the lender *disburses the PPP loan* and ending on any date selected by the borrower that occurs during the period (i) beginning on the date that is 8 weeks after the date of disbursement and (ii) ending on the date that is 24 weeks after the date of disbursement.

60% Requirement

- To receive full loan forgiveness, a borrower must use at least 60% of the PPP loan for payroll costs, and not more than 40% of the loan forgiveness amount may be attributable to nonpayroll costs.
- Example 1:
 - Borrower receives a \$100,000 PPP loan.
 - During the covered period the borrower spends \$54,000 (or 54%) of its loan on payroll costs.
 - As borrower used less than 60% of its loan on payroll costs, the maximum amount of loan forgiveness the borrower may receive is \$90,000 (with \$54,000 in payroll costs constituting 60% of the forgiveness amount and \$36,000 in nonpayroll costs constituting 40% of the forgiveness amount).

First Draw Loans - \$150,000 or Less

- An eligible borrower that received a loan of \$150,000 or less is not, at the time of application for loan forgiveness, required to submit any application or documentation in addition to the certification and information required by SBA.
- Such borrowers must retain records relevant to the form that prove compliance with the PPP requirements.
 - With respect to employment records, for the 4-year period following submission of the loan forgiveness application, and with respect to other records, for the 3-year period following submission of the loan forgiveness application.
- All other borrowers must follow the existing requirements for loan forgiveness applications and records retention. SBA may review and audit PPP loans of \$150,000 or less and access any records the borrower is required to retain.

First Draw Loans - \$150,000 or Less

- Borrower must sign and submit to the lender a certification that:
 - Provides a description of the employees the borrower was able to retain because of the loan,
 - The estimated amount of the covered loan spent by the eligible employer on payroll costs, and
 - The total loan value.
- Borrower must also attest that it accurately provided the certification and complied with the PPP requirements.
- The SBA is to provide the certification form within 24 days after enactment of the Act.

Deduction of EIDL Advance Amounts

- Act repealed requirement for SBA to deduct EIDL Advance Amounts from forgiveness amount.
- Thus, the EIDL Advance Amounts will not impact loan forgiveness amount.

Loan Terms

- No collateral is required.
- No personal guarantees are required.
- Interest rate is 1%, calculated on a non-compounding, non-adjustable basis.
- Credit elsewhere test does not apply.
- 5-Year maturity.

May a First Loan be Increased?

- Regulations provide the following borrowers can reapply or request an increase in their first draw PPP loan amount:
 - If a borrower returned all of a PPP loan, the borrower may reapply for a PPP loan in an amount the borrower is eligible for under current PPP rules.
 - If a borrower returned part of a PPP loan, the borrower may reapply for an amount equal to the difference between the amount retained and the amount previously approved.
 - If a borrower did not accept the full amount of a PPP loan for which it was approved, the borrower may request an increase in the amount of the PPP loan up to the amount previously approved.
 - Any request for an increase must be submitted electronically in E-Tran on or before March 31, 2021, and is subject to the availability of funds.
- The lender may make a single additional disbursement of the increased loan proceeds.

Special Rules Regarding Increase

- January 13, 2021 – SBA Procedural Notice - First Draw Paycheck Protection Program Loan Increases After Enactment of the Economic Aid Act
- If an eligible borrower received a first draw loan, the lender reported to SBA before December 27, 2020 that the borrower fully repaid the loan, and SBA has not remitted a forgiveness payment to the Lender on that loan, the **borrower may reapply** for a new first draw loan.
- Reapplication procedure depends on whether lender reported the loan to SBA as “cancelled” or “paid in full” as a result of the borrower’s repayment before December 27, 2020. Reapplication procedure applies only to those loans reported as “cancelled” or “paid in full” by the lender because the borrower returned the full amount of the original loan amount prior to December 27, 2020.
- The SBA guidance clarifies – any first draw loan reported as “paid in full” by a lender due to SBA’s remittance of a forgiveness payment in any amount to the lender is not eligible for a reapplication. **However, the borrower may be eligible for a Second Draw PPP Loan.**

Second Draw Loans

Second Draw Loans

- Generally, the second draw loans are subject to the same requirements as the first draw loans, but there are a number of differences.
- Eligibility for second draw loans is narrower.
- Lower employee count threshold and revenue decline requirements apply.

Eligibility Based on Employee Count

- Any single business entity that is assigned a NAICS code beginning with 72 (including hotels and restaurants) and that employs not more than 300 employees per physical location is eligible to receive a second draw PPP loan.
- In addition, SBA's affiliation rules do not apply to any business entity that is assigned a NAICS code beginning with 72 and that employs not more than a total of **300** employees.
 - As a result, if each hotel or restaurant location owned by a parent business is a separate legal business entity, each hotel or restaurant location that employs not more than 300 employees is permitted to apply for a separate PPP loan provided it uses its unique EIN.

General Eligibility

- An applicant is eligible for a second draw loan if it is a business concern, independent contractor, eligible self-employed individual, sole proprietor, nonprofit organization eligible for a first draw loan, veteran's organization, Tribal business concern, housing cooperative, small agricultural cooperative, eligible 501(c)(6) organization or destination marketing organization, or an eligible nonprofit news organization that:
 - Previously received a first draw loan in accordance with the applicable eligibility criteria,
 - Has used, or will use, the full amount of its first draw loan (including the amount of any increase on such first draw loan) on authorized uses on or before the expected date on which the second draw loan will be disbursed;

General Eligibility

- Employs 300 employees or less (but if an applicant has more than one physical location and employs not more than 300 employees per physical location, it is eligible if it is assigned a NAICS code beginning with 72 at the time of loan disbursement and otherwise meets the eligibility criteria); and
- Experienced a reduction in revenue in calendar year 2020 measured as follows:
 - Had gross receipts during the 1st, 2nd, 3rd, or 4th quarter in 2020 that demonstrate at least a 25% reduction from the borrower's gross receipts during the same quarter in 2019.
 - Special rules apply where the borrower was not in business in certain quarters of 2019.
 - If a borrower was in business all 4 quarters of 2019, the borrower is deemed to have experienced the revenue reduction if it had a reduction in annual receipts of 25% or more in 2020 compared to 2019 and the borrower submits copies of its annual tax forms substantiating the decline.

Gross Receipts

- “Gross receipts” includes all revenue in whatever form received or accrued (in accordance with the entity’s accounting method) from whatever source, including from the sales of products or services, interest, dividends, rents, royalties, fees, or commissions, reduced by returns and allowances.
- Generally, receipts are considered “total income” (or in the case of a sole proprietorship, independent contractor, or self-employed individual “gross income”) plus “cost of goods sold,” and excludes net capital gains or losses.

Gross Receipts

- Gross receipts do not include the following:
 - Taxes collected for and remitted to a taxing authority if included in gross or total income (such as sales or other taxes collected from customers and excluding taxes levied on the concern or its employees),
 - Proceeds from transactions between a concern and its domestic or foreign affiliates, and
 - Amounts collected for another by a travel agent, real estate agent, advertising agent, conference management service provider, freight forwarder or customs broker.
- All other items, such as subcontractor costs, reimbursements for purchases a contractor makes at a customer's request, investment income, and employee-based costs such as payroll taxes, may not be excluded from gross receipts.
- Gross receipts of a borrower with affiliates is determined by adding the gross receipts of affiliates.
- Forgiven first draw loans are not included.

Payroll Cost Calculation

- The maximum loan amount for a second draw loan is equal to the lesser of 2.5 months of the borrower's average monthly payroll costs or \$2M.
- The relevant time period for calculating a borrower's payroll costs for a second draw loan is the 12-month period prior to when the loan is made (if not self-employed), calendar year 2019 or calendar year 2020.
- For borrowers assigned a **NAICS code beginning with 72** at the time of disbursement, the maximum loan amount is equal to 3.5 months of payroll costs rather than 2.5 months.
- For businesses that are part of a single corporate group may not receive more than \$4M in second draw loans in the aggregate.

Affiliation

- Eligibility for second draw loans is governed by the same affiliation rules (and waivers) as first draw loans, with certain changes described below:
- The affiliation rules are waived with respect to eligibility for a second draw loan for:
 - Any business concern with not more than 300 employees that, as of the date on which the covered loan is disbursed, is assigned a NAICS code beginning with 72, and
 - Any business concern that employs not more than 300 employees, per physical location of such business concern and is majority owned or controlled by a business concern that is assigned a NAICS code beginning with 511110 or 5151 or any nonprofit organization that is assigned a NAICS code beginning with 5151.

Who is Not Eligible to Receive a Second Draw Loan?

- The following entities are excluded even if they otherwise meet the eligibility requirements:
 - Excluded from first draw loan eligibility,
 - Certain business concerns engaged in political or lobbying activities,
 - Certain business concerns created under the laws of PRC or Special Admin. Region of Hong Kong,
 - Any person required to submit a registration statement under Section 2 of Foreign registration Act,
 - Any person or entity that receives a grant for shuttered venue operators,
 - Certain entities related to the executive branch or legislative branch,
 - Generally, publicly traded entities,
 - An entity that already received a second draw loan,
 - **An entity that has permanently closed.**

Application Requirements for Second Draw Loan, Opening of SBA Portal for all PPP Loans

- Applicant must submit to the lender SBA Form 2483–SD (Paycheck Protection Program Second Draw Borrower Application Form) or the lender's equivalent form including the required certifications and the required documentation.
- The SBA PPP loan portal was fully reopened on Tuesday, January 19, 2021 to all participating PPP lenders to submit first and second draw loan applications to SBA.

Tax Issues

- Forgiven PPP loans amounts are excluded from Federal AGI. NYS follows the federal treatment.
 - If forgiven loan is excluded from Federal AGI it is also excluded from New York AGI. See <https://www.tax.ny.gov/pit/cares-act-faq.htm>.
- Act permits employers to deduct expenses paid with forgiven loan proceeds.
 - If the expenses related to the forgiven loan are deducted in computing Federal AGI, these deductions are automatically excluded from New York AGI.

Tax Issues

- Qualified wages taken into account in determining the employee retention credit may not be counted as payroll costs under the PPP, but employers may elect not to have wages count as qualified wages for purposes of the employee retention tax credit.
 - If a PPP loan is ultimately not forgiven, such election will not prevent the wages from counting as qualified wages for purposes of the employee retention credit.
 - In short, employers who receive PPP loans remain eligible for the employee retention credit with respect to wages that are not counted as forgiven payroll costs under the PPP.

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Thank you.