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MEMORANDUM

FROM: Quattlebaum, Grooms & Tull PLLC
DATE: March 30, 2020
SUBJECT: Paycheck Protection Program

The Paycheck Protection Program (“PPP”) is a new loan program within 7(a) Loan Program of the U.S. Small Business Administration (“SBA”). The PPP was created under the Coronavirus Aid, Relief and Economic Security Act (“CARES Act”) which was signed into law on March 27, 2020. The purpose of the PPP is to get liquidity to qualifying businesses and to encourage such businesses to keep employees on their payroll. Under the PPP, the SBA will guarantee 100 percent of the amounts loaned by participating lenders to certain small business, nonprofit organizations, veterans organizations and tribal businesses (“qualifying businesses”). Qualifying businesses will be eligible to participate in the PPP during the “covered period” from February 15, 2020 through June 30, 2020 (“covered loans”).

Qualifying Businesses

The PPP increased the eligibility for Section 7(a) loans for certain small businesses and nonprofit organizations. Under the CARES Act, in addition to “small business concerns” as currently defined under the Small Business Act (15 U.S.C. 632) that are normally eligible to participate in SBA Section 7(a) loans, the following are eligible for covered loans:

- Business concerns, including nonprofit organizations, veterans organizations, and tribal business concerns, which employ less than 500 employees (unless the applicable SBA size standard for the industry in which the business operates allows greater than 500 employees);
- Sole proprietors, independent contractors, and eligible self-employed individuals (as such term is defined in Section 7002(b) of the Families First Coronavirus Response Act), subject to the receipt of supporting documentation such as payroll tax filings reported to the Internal Revenue Service, Form 1099-MISC, and income and expenses from the sole proprietorship; and

- Business concerns in the Accommodation and Food Service Section, according to the North American Industry Classification System (“NAICS”) Code 72 with more than one physical location, where each location employs less than 500 employees.

Generally, for the purposes of determining whether a potential borrower satisfies the number of employees standard, the SBA’s affiliation rules under 13 C.F.R. 121.103 provide that the employees of the borrower and its affiliates will be aggregated. However, under the CARES Act, those rules are expressly waived for the following:

- Business concerns operating in NAICS Code 72 (“Accommodation and Food Services”) that have up to 500 employees per location (see the table below for certain examples of such business concerns);
- Business concerns operating as franchises with an SBA-assigned franchise code identifier; and
- Business concerns that receive financial assistance through the Small Business Investment Company (“SBIC”) program.

Examples of Business Concerns having an NAICS Code 72

Hotels (except Casino Hotels) and Motels

721120	Casino Hotels
721191	Bed-and-Breakfast Inns
721199	All Other Traveler Accommodation
721211	RV (Recreational Vehicle) Parks and Campgrounds
721214	Recreational and Vacation Camps (except Campgrounds)
721310	Rooming and Boarding Houses, Dormitories, and Workers’ Camps

Subsector 722—Food Services and Drinking Places

722310	Food Service Contractors
722320	Caterers
722330	Mobile Food Services
722410	Drinking Places (Alcoholic Beverages)
722511	Full-Service Restaurants
722513	Limited-Service Restaurants
722514	Cafeterias, Grill Buffets, and Buffets
722515	Snack and Nonalcoholic Beverage Bars

Terms of the Loans

The maximum amount of any loan under the PPP is the lesser of: (a) the average total monthly payroll costs incurred in the one-year period before the date on which the loan is made multiplied by 2.5, plus the amount of any eligible Economic Injury Disaster Loans (“EIDL”) to be refinanced into the covered loan; or (b) \$10 million.

For the purposes of the loans, “payroll costs” means the sum of any payments of any compensation with respect to employees that is a:

- salary, age, commission or similar compensation;
- payment of a cash tip or equivalent;
- payment for vacation, parental, family, medical or sick leave;
- allowance for dismissal or separation;
- payment required for the provisions of group health care benefits, including insurance premiums;
- payment of any retirement benefit; or
- payment of state or local tax assessed on the compensation of employees.

If a eligible participant is self-employed or organized as a sole proprietorship, “payroll costs” means the sum of payments of any compensation to or income of a sole proprietor or independent contractor that is a wage, commission, income, net earnings from self-employment or similar compensation and that is an amount not more than \$100,000 in one year, as prorated for the covered period.

Payroll costs do not include: (a) the compensation of an individual employee in excess of an annual salary of \$100,000, as prorated for the covered period; (b) taxes imposed or withheld under Chapter 21 (Social Security and Medicare taxes, employee and employer portion), Chapter 22 (railroad retirement tax), or Chapter 24 (withholding obligations from employees) or the Internal Revenue Code of 1986; (c) any compensation of an employee whose principal place of residence is outside of the United States; or (d) qualified sick leave wages and qualified family leave wages, in each case, for which a credit is allowed under the Families First Coronavirus Response Act.¹

Thus, for purposes of illustration, if a loan is made on April 1, 2020, and the average monthly payroll costs for a qualifying business for the period between April 1, 2019 to April 1, 2020 were \$1,500,000.00, the maximum loan amount would be \$3,750,000.00.

An eligible recipient may use the proceeds of the covered loan for:

¹ The Families First Coronavirus Response Act (“FFCRA”) applies to private employers with fewer than 500 employees (with a few exceptions) and expands paid leave for covered employees in circumstances related to COVID-19. FFCRA requires employers to provide two weeks of paid sick leave at the employee’s regular rate of pay (up to \$511 per day and \$5,110 in the aggregate) if the employee is unable to work (or telework) because: (1) the employee is subject to a quarantine order related to COVID-19; (2) the employee has been advised by a health care provider to self-quarantine; or (3) the employee is experiencing symptoms of COVID-19 and seeking medical treatment related to the symptoms. FFCRA requires employers to provide two weeks of paid sick leave at 2/3 the regular rate of pay (up to \$200 per day and \$2,000 in the aggregate) if the employee is unable to work (or telework) because: (1) the employee is caring for an individual subject to a quarantine order or who has been advised to self-quarantine; (2) the employee is caring for a child whose school or daycare is unavailable; or (3) the employee is experiencing any other condition “substantially similar” to the specifically listed conditions. FFCRA has varying rules for full versus part-time employees and labor provided by temporary agencies. The leave granted by FFCRA is in addition to any pre-existing paid leave benefits offered by the employer. Employers are prohibited from requiring employees to exhaust other paid leave benefits before using FFCRA benefits. Employers providing benefits under FFCRA will qualify for a dollar-for-dollar reimbursement through tax credits for wages paid under FFCRA. Employers may also receive a tax credit for qualified health plan expenses allocated to COVID-19 related leaves. Employers are required to post a notice of FFCRA rights in a prominent location. A copy of the poster can be downloaded here: <https://www.dol.gov/newsroom/releases/whd/whd20200324>

- Payroll costs;
- Costs related to the continuation of group health care benefits during periods of paid sick, medical or family leave, and insurance premiums;
- Employee salaries, commissions or similar compensations;
- Payments of interest on a mortgage obligation;
- Rent (including rent under a lease agreement)
- Utilities; and
- Interest on any other debt obligations that were incurred before February 15, 2020.

Additionally, the CARES Act provides the interest rate for a loan is not to exceed 4 percent, and there is no prepayment penalty for any payment made on a covered loan. Payments under any covered loans and all other 7(a) loans are to be deferred for 6-12 months, and the SBA is directed to issue guidance on the terms of this deferral. Any portion of the principal amount of a covered loan that is not forgiven (under the process summarized below) will be subject to a maximum maturity of 10 years from the date of the loan forgiveness application and will continue to be guaranteed by the SBA. The forgiven portion of a loan will not be treated as taxable income from cancelled indebtedness for 2020.

Loan Forgiveness

A borrower is eligible for loan forgiveness for a portion of the loan in the amount equal to the following payments made during the eight-week period after the loan's origination date:

- Payroll costs, not including compensation in excess of \$100,000 per year for an individual employee;
- Interest payments on mortgages evidencing indebtedness incurred before February 15, 2020;
- Rent payments for properties under a lease in force before February 15, 2020; and
- Utility payments in service prior to February 15, 2020.

However, the amount of loan forgiveness is capped at the principal amount of the loan and will be subject to reduction if the borrower reduces the number of employees, employee salaries or both during the eight-week period following the origination of the loan, as follows:

- Loan forgiveness is reduced by multiplying the forgiveness amount by the quotient of the borrower's average number of full-time employees per month during the eight weeks following the origination of the loan by either (at the election of the borrower) (a) the borrower's average number of full-time employees per month employed during the period beginning on February 15, 2019, and ending on June 30, 2019, or (b) the average number of the borrower's full-time employees per month employed during the period beginning on January 1, 2020 and ending on February 29, 2020. The average number of full-time employees is determined by calculating the average number of full-time equivalent employees for each pay period falling within a month.
- Loan forgiveness will be reduced by an reduction in total salary or wages of any employees earning \$100,000 or less on an annualized basis for 2019 during the eight-week period following the origination of the loan that is in excess of 25% of the total salary or wages of such employee during the most recent full quarter during which the employee was employed before such period.

However, there is relief from these forgiveness reduction penalties for employers that by June 30, 2020 restore their employee count and employee salaries to the levels in effect on February 15, 2020.

Applicable Lenders

Initially, loans will be disbursed by banks that currently participate in the SBA's 7(a) Loan Program. However, the CARES Act allows the Department of Treasury to establish a process by which lending institutions that are not currently authorized to offer SBA loans will be able to participate. SBA approved lenders will have the delegated authority to process, close, and service a covered loan without SBA review. PPP loans will not require lenders to reserve additional capital with respect to the principal amount of such loans under the risk-based capital requirements of federal banking agencies or the National Credit Union Administration Board.

Application Process for a PPP Loan

A lender approved to make loans under the PPP is deemed to have been delegated authority by the SBA to make and approved covered loans. A lender is required to consider if the applicant was in operation on February 15, 2020 and had employees for whom the borrower paid salaries and payroll taxes or paid independent contractors, as reported on a Form 1099-MISC. During the covered period, the CARES Act waives (i) the PPP loan application and certain other fees, (ii) the need for a personal guarantee or collateral, and (iii) the requirement that a small business concern demonstrate that it was unable to obtain credit from nonfederal sources on reasonable terms and conditions. As such, PPP loans are unsecured and nonrecourse to the borrower, unless the loan proceeds are utilized for nonpermitted purposes.

However, the applicant is required to make a good faith certification:

- That the uncertainty of current economic conditions makes necessary the loan request to support the ongoing operations of the applicant;
- Acknowledging that funds will be used to retain workers and maintain payroll or make mortgage payments, lease payments and utility payments;
- That the applicant does not have an application pending for a loan under the PPP for the same purpose and duplicative of amounts applied for or received under a covered loan; and
- During the period beginning on February 15, 2020 and ending on December 31, 2020, that the applicant has not received amounts under the PPP for the same purpose and duplicative of amounts applied for or received under a covered loan.

Reimbursement of Lenders for Processing

No later than 5 days after the disbursement of a covered loan, the SBA is required to reimburse the lender at a rate, based on the balance of the financing outstanding at the time of disbursement of the covered loan, of:

- 5% for loans up to \$350,000;
- 3% for loans greater than \$350,000 and less than \$2 million;

- 1% for loans of \$2 million or greater.

An agent that assists an applicant to prepare an application for a covered loan is not permitted to collect a fee in excess of the limits established by SBA.

Loan Forgiveness Applications

Borrowers seeking loan forgiveness with respect to a covered loan are required to submit to the lender servicing the loan an application along with certain documents and certifications. The documentation includes:

- Documentation verifying the number of full-time equivalent employees on payroll and pay rates for the relevant periods, including payroll tax filings reported to the Internal Revenue Service and state income, payroll and unemployment insurance filings;
- Documentation verifying payments on covered mortgage obligations, payments on covered lease obligations, and covered utility payments, including cancelled checks, payment receipts, transcripts of accounts, or other documents;
- A certification from a representative of the borrower that:
 - The documents presented are true and correct; and
 - The amount of the requested forgiveness was used to retain employees, make interest payments on a covered mortgage obligation, make payments on a covered rent obligation, or make covered utility payments;
- Any other documentation that the SBA determines is necessary.

The lender will be the decision maker as to the forgiveness application and is required no later than 60 days after the application to issue such decision. If a lender receives the required documentation that verifies that the borrower used the proceeds on payroll costs, covered mortgage obligations, payments on covered lease obligations or covered utilities payments during the covered period, the lender will not be subject to any penalties by the SBA relating to loan forgiveness. Further, if such documentation is received, an enforcement action may not be taken against the lender under section 47(e) of the Small Business Act relating to the loan forgiveness.

Additional Guidance and Regulations

Pursuant to the terms of the CARES Act, the SBA is to issue additional regulations to implement the PPP within 15 days of enactment.

Expansion of EDIL under CARES Act

The CARES Act has allocated \$10 billion in additional funds for the Economic Injury Disaster Loans (“EDIL”) and expanded the SBA’s authority to make EDILs.

Caution: A Borrower cannot Obtain an EDIL and PPP Loan for the Same Purpose

An applicant cannot obtain both a PPP loan and an EDIL for the same purpose. A borrower who has received an EIDL between January 31, 2020, and the date on which the PPP loan is made

available can still receive a PPP loan, but only if the EIDL was for a purpose other than the purpose of the PPP loan.

EDILs may be Refinanced under PPP

For purposes of the formula used to determine the maximum amount of a PPP loan, the size of the loan may be increased by the outstanding amount of an EIDL between January 31, 2020, and the date on which the PPP loan is made available, with the EIDL to be refinanced under the PPP loan.

Expansion of Eligible Recipients

The CARES Act expands eligibility for access to EDIL to include tribal businesses, cooperatives, and ESOPs with fewer than 500 employees or any individual operating as a sole proprietor or an independent contractor between January 31, 2020 and December 31, 2020. Private non-profits are also eligible for both grants and EIDLs.

No Personal Guarantee or “Credit Elsewhere”

The CARES Act requires that for any EIDLs made in response to COVID-19 before December 31, 2020, the SBA shall waive (i) any personal guarantee on advances and loans below \$200,000, (ii) the requirement that an applicant needs to have been in business for the 1-year period before the disaster (iii) and the “credit elsewhere” requirement typical of SBA loans.

Higher Maximum EDILs

The maximum amount available to eligible small business concerns is \$2 million through an EDIL, but the actual loan amount is limited to the economic injury as determined by the SBA (less business interruption insurance or other recoveries such as potential contributions available from the business concern and/or its owner(s) or affiliates).

Reduced Underwriting Scrutiny

Between January 31, 2020 and December 31, 2020, the CARES Act gives the SBA authority to approve and offer EIDL loans based solely on an applicant’s credit score or use an appropriate alternative method for determining applicant’s ability to repay.

Advance Requests

Caution: the SBA is directed to consider EDIL advances when determining loan forgiveness, if the applicant refinances the EDIL into a loan under the PPP. Under the CARES Act, entities who have applied for an EIDL due to COVID-19 may request an advance on that loan of not more than \$10,000, which the SBA must distribute within 3 days. Further, applicants shall not be required to repay advance payments, even if subsequently denied for an EIDL. In conjunction with disbursing such advance payment, the SBA shall waive: (i) any personal guarantee on advances and loans below \$200,000, (ii) the requirement that an applicant needs to have been in business for the 1-year period before the disaster, (iii) and the “credit elsewhere” requirement. This approval shall take the form of a certification under penalty of perjury by the applicant that they are eligible. An advance

payment may be used for providing paid sick leave to employees, maintaining payroll, meeting increased costs to obtain materials, making rent or mortgage payments, and repaying obligations that cannot be met due to revenue losses.