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COVID-19 NEWS OF INTEREST

SBA Clarifies Rules for Paycheck Protection Program

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On Thursday, April 2nd and Friday, April 3rd, the Small Business Administration ("SBA") released two interim final rules regarding the Paycheck Protection Program ("PPP"). The first interim final rule provided an overview on and clarification of the general requirements under the PPP and the second addressed the rules of affiliation as they apply to the PPP. Along with the second interim rule, the SBA and Department of the Treasury issued a fact sheet providing guidance on the application of the SBA's affiliation rules to the PPP.

The rules and fact sheet largely affirmed the existing SBA regulations as they previously applied to Small Business Act Section 7(a) loans. In particular, the guidance did not waive or abrogate the affiliation rules beyond the limited waivers provided for in the CARES Act. In other ways, the new guidance expands upon previous guidance and regulations issued by the SBA, potentially causing confusion among applicants reviewing the statute, the SBA regulations, the guidance, and the application form for a consistent set of standards.

Nonetheless, the guidance did clarify a number of the rules governing eligibility and terms of the PPP described below.

First Come, First Served

The funding for the PPP is currently capped at $349 billion. The PPP will be open until either June 30, 2020 or when the $349 billion in funding is exhausted. Treasury has urged businesses to apply early as they expect a high rate of applications.

Eligibility Standards

Despite ambiguity in the interim final rule on general requirements, the SBA has provided informal guidance that there are three ways for a business to qualify for the PPP, subject to application of the affiliation rules:

1. Having no more than 500 employees.

2. Meeting the applicable size standard, either number of employees or annual receipts, for the industry in which the business operates, based on the business' North American Industry Classification System ("NAICS") code.

3. Meeting the Alternative Size Standard, meaning the business has a maximum tangible net worth of no more than $15 million and the business' average net income after federal income tax for the past two years is no more than $5 million.

Rules on Affiliation

The SBA has not changed or eased the rules of affiliation for Section 7(a) business loans, except for the three waivers of the affiliation rules explicitly granted for PPP loans in the CARES Act.

Determinations of affiliation are generally based on whether a business or third party has, or can exercise, control over another business. Treasury has released guidance on four tests for affiliation which apply to participants in the PPP, essentially repeating the existing affiliation rules applicable to Section 7(a) loans in 13 C.F.R. § 120.301, including:

- A business that owns more than 50 percent of another business' voting equity would be affiliated with that business.

- A minority shareholder will be considered an affiliate if it has the power under the concern's charter, by-laws, or shareholder's agreement to prevent a quorum or otherwise block action by the board of directors or shareholders.

- Affiliation arises where the CEO or President of the applicant also controls the management of one or more other concerns. Affiliation also arises where a single individual, business or entity controls the management of the applicant through a management agreement.

Counting Employees

The guidance clarifies that for purposes of calculating size for eligibility for the loan, applicants should only consider employees whose principal place of residence is in the United States. Under the SBA's rules of affiliation, the size of foreign affiliates will be added to the size of the applicant, but under the new guidance, applicants should count only employees of foreign affiliates whose residence is in the United States.

Clarification on the Treatment of Independent Contractors

Independent contractors are not considered employees and do not count for purposes of an applicant's PPP loan calculations or loan forgiveness. The SBA stated that this was due to the fact that independent contractors can separately apply for a PPP loan.

Additional Restrictions on Uses of the Loan Funds and Forgiveness

Based on the interim final rule released for general requirements:

- At least 75% of the PPP loan must be used for payroll costs; and
- Not more than 25% of the loan forgiveness amount may be attributable to non-payroll costs.

Changes to Maturity Date on a PPP Loan

The maturity rate on a PPP loan is now two years. This was changed from 10 years as the SBA and Treasury expect that the temporary economic dislocations caused by the pandemic will abate well before the two-year maturity date.

Interest Rate on PPP Loans

The Administrator has set the interest rate for a PPP loan at 1%.

Loan Deferment

The loan deferment period for a PPP loan will be for six months after the day the loan has been disbursed.

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