

PPP Updates – Restrictions, Eligibility, Loan Amount Calculations & Penalty-Free Repayment Option

The recently enacted *Paycheck Protection Program and Health Care Enactment Act* (PPPHEA) allocated \$310 billion in additional funding for the U.S. Small Business Administration's (SBA) Paycheck Protection Program (PPP) and added enhanced oversight and new restrictions. The SBA resumed accepting PPP applications from participating lenders beginning on April 27, 2020, at 10:30 a.m. Eastern time. The legislation provides the SBA with an additional \$2.1 billion for administration and oversight of COVID-19 response programs. See BKD's [update](#) for additional details.

There were several other important updates released on April 24, 2020:

- The SBA issued a fourth [interim final rule](#)¹ clarifying eligibility requirements and incorporating previously issued FAQ items into official SBA regulation. The fourth interim rule includes updates that restrict eligibility for hedge funds, clarify eligibility for 501(c)(3) nonprofit hospitals and employee stock ownership plans (ESOP), expand eligibility for gaming organizations and curb eligibility in bankruptcy situations. The fourth interim rule is effective immediately, although a 30-day comment period will follow publication in the Federal Register.
- The SBA issued an eighth update to its [FAQ](#) to address eligibility for agricultural enterprises, U.S. residency considerations and housing allowances.
- The U.S. Department of the Treasury issued [instructions](#) on how to calculate the maximum PPP loan amount by business type:
 - Self-employed with and without employees
 - Self-employees and income reported on Schedule F
 - Partnerships
 - S corporations and C corporations
 - Nonprofit organizations and nonprofit religious organizations

PPP loans were very attractive to borrowers since the full principal amount was forgivable under certain criteria; however, the first round of funding drew widespread criticism. Because of the program's quick rollout, ambiguous language and changing criteria, government scrutiny and oversight have increased. Both the interim final rule and FAQ refine the borrower certification requirement and provide a mechanism to return funds already distributed without penalty for entities that may have applied for aid in conflict with the revised guidelines.

Some of the sworn certifications required to obtain these loans remain ambiguous, and there is still little guidance as to what some of these terms mean. We recommend prospective applicants seek legal counsel with any questions about eligibility for the program.

While a lending institution may incorrectly approve an ineligible PPP loan application, the borrower bears ultimate responsibility to demonstrate financial need, eligibility and use of the proceeds.

Borrower Certification – Assessing Adequate Liquidity Sources & Safe Harbor

This interim rule codifies the SBA April 23, 2020, FAQ update to include the following:

“In addition to reviewing applicable affiliation rules to determine eligibility, all borrowers must assess their economic need for a PPP loan under the standard established by the CARES Act and the PPP regulations at the time of the loan application. Although the CARES Act suspends the ordinary requirement that borrowers must be unable to obtain credit elsewhere, borrowers still must certify in good faith that their PPP loan request is necessary. Specifically, before submitting a PPP application, all borrowers should review carefully the required

¹Initial program guidelines were issued on April 3 (see [SBA Releases Details on Paycheck Protection Program](#)). A second interim rule was issued on April 14 with frequently asked questions, and a third interim rule was issued on April 20 covering eligibility for sole proprietorships (see [New SBA PPP Rules & FAQ](#)).

certification that “current economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant.” **Borrowers must make this certification in good faith, taking into account their current business activity and ability to access other sources of liquidity sufficient to support ongoing operations in a manner that is not significantly detrimental to the business.** For example, **it is unlikely that a public company with substantial market value and access to capital markets will be able to make the required certification in good faith**, and such a company should be prepared to demonstrate to SBA, upon request, the basis for its certification. Lenders may rely on a borrower’s certification regarding the necessity of the loan request. **Any borrower that applied for a PPP loan prior to this guidance and repays the loan in full by May 7, 2020, will be deemed by SBA to have made the required certification in good faith.”**

The SBA determined that this safe harbor is necessary and appropriate to help ensure that borrowers promptly repay PPP loan funds that the borrower obtained based on a misunderstanding or misapplication of the required certification standard.

As noted in the initial rules, knowingly making a false statement to obtain an SBA guaranteed loan is punishable under the law, including imprisonment of not more than five years and/or a fine of up to \$250,000 and, if submitted to a federally insured institution, by imprisonment of not more than 30 years and/or a fine of not more than \$1 million. See [Appendix](#) for a list of borrower certifications required.

Eligibility

Hedge Funds & Portfolio Companies

Hedge funds and private equity (PE) firms are primarily engaged in investment or speculation, and such businesses are ineligible to receive a PPP loan. The SBA does not believe that Congress intended for these types of businesses, which are generally ineligible for section 7(a) loans under existing SBA regulations, to obtain PPP financing.

The affiliation rules apply to portfolio companies of PE firms², and there is a reminder that the applicant must certify “current economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant.”

501(c)(3) Nonprofit Hospitals

501(c)(3) nonprofit hospitals exempt from tax under 501(a) are not ineligible for PPP loans solely because they are owned by a governmental entity, so long as less than 50 percent of its funding is from state or local government sources (not including Medicaid). The SBA determined that this exception to the general ineligibility (13 CFR 120.110(j)), of government-owned entities was warranted.

Gaming

The third interim final rule excluded any legal gaming entity that derived certain thresholds of revenue from legal gaming revenues. This interim rule supersedes those limitations and now entities receiving legal gaming revenue are eligible regardless of revenue size or percentage of revenue from gaming. The normal SBA gaming restriction in 13 CFR 120.110(g) is not applicable to PPP loans.

Businesses that received illegal gaming revenue remain ineligible.

²The affiliation rules are waived if the borrower receives financial assistance from an SBA-licensed small business investment company (SBIC) in any amount for financing in the form of loans, debt with equity features, equity and guarantees. Affiliation is waived even if the borrower has investment from other non-SBIC investors.

Business Participation in ESOPs

The SBA clarified that a business's participation in an ESOP does not result in an affiliation between the business and the ESOP as the shares of the company are not directly held by employees while employed with the company (the employee generally receives the shares in his or her personal account only upon the cessation of employment with the company, including retirement, disability, death or termination).

Bankruptcy

Any applicant or owner of the applicant involved in a bankruptcy proceeding at the time of application or any time before the loan is disbursed is ineligible for PPP funding. If the bankruptcy proceedings commence between the application date and the funding date, the applicant is required to notify the lender and cancel the application. Failure to do so will be regarded as a use of PPP funds for unauthorized purposes, which is one of the borrower certifications (see [Appendix](#)). Lenders may rely on the applicant's representation regarding involvement in a bankruptcy proceeding.

Agricultural Enterprises

The PPPHEA expanded eligibility for disaster loans to agricultural enterprises. The SBA [FAQ](#) update released on April 24, 2020, expands PPP eligibility to agricultural producers, farmers, ranchers and cooperatives under the following conditions:

- The business has 500 or fewer employees, **or**
- The business fits within the revenue-based sized standard, which is average annual receipts of \$1 million

Agricultural producers, farmers and ranchers also can qualify for PPP loans as a small business concern if their business meets SBA's alternative size standard:

- Maximum net worth of the business is not more than \$15 million, **and**
- The average net income after federal income taxes (excluding any carryover losses) of the business for the two full fiscal years before the date of the application is not more than \$5 million

For all of these criteria, the applicant must include its [affiliates](#) in its calculations.

As long as other PPP eligibility requirements are met, small agricultural cooperatives and other cooperatives may receive PPP loans.

Other Items

Housing Allowance

The cost of a housing stipend or allowance provided to an employee as part of compensation counts toward payroll costs. Payroll costs include all cash compensation paid to employees, subject to the \$100,000 annual compensation per employee limitation.

U.S. Residency

PPP applicants and lenders may consider IRS regulations (26 CFR §1.121-1(b)(2)) when determining whether an individual employee's principal place of residence is in the United States.

Conclusion

BKD will continue to follow this developing situation. As with most topics related to COVID-19, changes are being made rapidly. Please note that this information is current as of the date of publication. Visit [BKD's COVID-19 Resource Center](#) to learn more. If you have questions about these changes, contact your **BKD Trusted Advisor™** today.

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Appendix – Borrower Certifications

What certifications need to be made?

On the PPP application, an authorized representative of the applicant must certify in good faith to all the below:

- The applicant was in operation on February 15, 2020, and had employees for whom it paid salaries and payroll taxes or paid independent contractors, as reported on a Form 1099-MISC
- Current economic uncertainty makes this loan request necessary to support the applicant's ongoing operations
- The funds will be used to retain workers and maintain payroll or make mortgage interest, lease and utility payments; I understand that if the funds are knowingly used for unauthorized purposes, the federal government may hold me legally liable such as for charges of fraud
- Documentation verifying the number of full-time equivalent employees on payroll, as well as the dollar amounts of payroll costs, covered mortgage interest payments, covered rent payments and covered utilities for the eight-week period following this loan, will be provided to the lender
- Loan forgiveness will be provided for the sum of documented payroll costs, covered mortgage interest payments, covered rent payments and covered utilities. No more than 25 percent of the forgiven amount may be for nonpayroll costs
- During the period beginning on February 15, 2020, and ending on December 31, 2020, the applicant has not and will not receive another loan under this program
- I further certify that the information provided in this application and the information provided in all supporting documents and forms is true and accurate in all material respects. I understand that knowingly making a false statement to obtain a guaranteed loan from SBA is punishable under the law, including under 18 USC 1001 and 3571 by imprisonment of not more than five years and/or a fine of up to \$250,000; under 15 USC 645 by imprisonment of not more than two years and/or a fine of not more than \$5,000; and, if submitted to a federally insured institution, under 18 USC 1014 by imprisonment of not more than 30 years and/or a fine of not more than \$1 million
- I acknowledge that the lender will confirm the eligible loan amount using tax documents I have submitted. I affirm that these tax documents are identical to those submitted to the IRS. I also understand, acknowledge and agree that the lender can share the tax information with SBA's authorized representatives, including authorized representatives of the SBA Office of Inspector General, for the purpose of compliance with SBA loan program requirements and all SBA reviews