

New PPP Changes in the Stimulus Bill: Second PPP Loan for Hardest-Hit Existing PPP Borrowers, Additional Categories of Forgivable Expenses, Tax Deductibility for Expenses Paid with PPP Proceeds, Lender Liability Limitations, Simplified Forgiveness Application for Loans of $150,000 or Less, and Other Changes

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On December 27, the President signed the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act (Act) addressing changes to the rules regarding PPP loans, including making a supplemental PPP loan available to many PPP borrowers and increasing the types of business expenses that can be forgiven.

Among many other changes discussed in detail below, the Act provides the following key changes in regard to the PPP program:

- Funding to allow the hardest-hit small businesses to receive a second forgivable Paycheck Protection Program (PPP) loan (Second Draw Loan).
    - Eligibility would be limited to small businesses with 300 or fewer employees that have sustained a 25 percent revenue loss in any quarter of 2020.
- Forgivable expenses are expanded to include supplier costs and investments in facility modifications and personal protective equipment to operate safely.
- Business expenses paid for with the proceeds of PPP loans are tax deductible, consistent with Congressional intent in the CARES Act.
- Limitations on lender liability are clarified.
- EIDL grants no longer reduce the allowed forgiveness amount of PPP loans.
- Borrowers may apply to obtain loan amounts they had previously returned or had not taken.

- Loan forgiveness process is simplified for borrowers with PPP loans of $150,000 or less.

This Alert will first discuss the standards and requirements for Second Draw Loans. It will then discuss changes to requirements for PPP loans generally (note that unless otherwise indicated, the changes to PPP loans generally also apply to Second Draw Loans). Finally, this Alert will discuss the simplified forgiveness process for loans of $150,000 or less.

Second Draw PPP Loans

The Act provides for a "Second Draw Loan" that PPP borrowers may apply for beyond their original PPP loan. A borrower may receive only one Second Draw Loan. Many of the requirements are the same as a regular PPP loan. Note that, along with the provisions of the Act specifically applying to Second Draw Loans set out in this section, the provisions of the Act applicable all PPP loans set forth in the next section below (Provisions of the Act Applying to PPP Loans Generally, Including Second Draw Loans) also apply to Second Draw Loans.

Second Draw Down Loan Amount

The maximum loan amount is the lesser of:

- $2 million; or
- For most entities, at the election of the eligible entity, either (1) the average total monthly payment for payroll costs incurred or paid by the eligible entity during the 1-year period before the date on which the loan is made; or (2) calendar year 2019; multiplied by 2.5.
    - For seasonal employers, the average total monthly payments for payroll costs incurred or paid by the eligible entity during (at the election of the eligible entity) (1) a 12-week period beginning February 15, 2019, or March 1, 2019, and ending June 30, 2019, or at the election of the eligible recipient, (2) any consecutive 12-week period during the period beginning on February 15, 2020 and ending on December 31, 2020; multiplied by 2.5;
    - For new entities that did not exist during the 1-year period preceding February 15, 2020, the sum of the total monthly payments by the eligible entity for payroll costs paid or incurred by the eligible entity as of the date on which the eligible entity applies for the covered loan divided by the number of months in which those payroll costs were paid or incurred; multiplied by 2.5.
    - For entities classified as NAICS 72 (Accommodation and Food Services), the product of (at the election of the eligible entity) the average total monthly payment for payroll costs incurred or paid by the eligible entity during (1) the 1-year period

before the date on which the loan is made; or (2) calendar year 17 2019, at the election of the eligible entity, by 3.5.

- If an Accommodation and Food Services entity has more than one physical location:
  - Its total Second Draw Loan amounts may only be $2 million; and
  - It may have only 300 total employees, as opposed to 500 employees under the rules for an original PPP loan.

90 Day Limitation of $10 Million

The total amount of loans an entity, including affiliates, may receive as an original PPP loan and as a Second Draw Loan in any 90 day period is $10 million.

Eligibility

To receive a Second Draw Loan, an entity must have received a regular PPP loan and is expected to use all the regular loan proceeds before the date it is expected to receive the Second Draw Loan. Entities may obtain only one Second Draw Loan.

Eligible Entities:

- Any business concern, nonprofit organization, veterans organization, Tribal business concern, eligible self-employed individual, sole proprietor, independent contractor, or small agricultural cooperative that:
  - That on or before the expected date on which the Second Draw Loan is disbursed to the borrower, has used, or will use, the full amount of the original PPP loan;
  - If a business concern, meets the annual receipts requirements for PPP borrowers generally;
  - If not a small business concern, meets the alternative size requirements for PPP borrowers generally;
  - Has 300 or fewer employees
  - Has at least a 25% reduction in gross receipts in quarter in 2020, measured as followed:

- Comparing the first, second, or third quarter in 2020 (or, only with respect to an application submitted on or after January 1, 2021, fourth quarter in 2020) to the same quarter in 2019.
- If the entity was not in business during the first or second quarter of 2019, it had at least a 25% reduction in gross receipts in the third or fourth quarter in 2020 as compared to the same quarter in 2019;
- If the entity was not in business during the first, second or third quarter of 2019, it had at least a 25% reduction in gross receipts in the fourth quarter in 2020 as compared to the same quarter in 2019;
- If the entity was not in business during 2019, but was in operation on February 15, 2020, it had at least a 25% reduction in gross receipts in the second or third quarter in 2020 as compared to the first quarter in 2020.

Ineligible Entities - The following types of entities are not eligible:

- Publicly traded corporations;
- Entities which are "ineligible businesses" under 13 CFR 120.110(b) through (j) and (l) through (s);
- Entities engaged in political or lobbying activities, advocacy organizations or think tanks;
- Entities in which a Chinese entity has an ownership interest of 20% or more, or a resident of China is a member of the board of directors;
- Persons or entities that receive a grant under Section 24 of the Economic Aid to Hard-Hit Small Businesses, Non-profits, and Venues Act;
- Persons required to register as a foreign agent.

Certification Required

As with the original PPP loan, an applicant for a Second Draw Loan must certify that economic uncertainty makes the loan request necessary to support the applicant's ongoing operations. Given that the applicant will now have been operating for several months during the COVID crisis, care should be taken by the applicant to be certain it can establish that economic necessity.

Forgiveness Amount and Categories

At least 60% of the forgiveness amount must be payroll costs.

The forgiveness amount may include the expense categories previously allowed for PPP loans:

- Payroll costs;
- Any payment of interest on a mortgage obligation (which shall not include any prepayment of or payment of principal on a mortgage obligation);
- Rent;
- Utility payments.

Additionally, the following new categories of expenses are forgivable:

- Operations expenditures, including defined software and computing costs, processing of payrolls, and various back office support functions;
- Property damages and vandalism costs related to public disturbances in 2020 that are not covered by insurance;
- Supplier costs based on contractual obligations in effect at the date of the loan, and which are essential for business operations;
- Worker protection expenditures related to compliance with worker safety and health mandates related to the COVID emergency;
- Group life, disability, vision, and dental insurance are expressly listed as payroll costs.

Lender Eligibility

Lenders who are eligible to make regular PPP loans may also make Second Draw Loans.

SBA Fee Waiver

The SBA will not charge a guarantee fee or a yearly fee for a Second Draw Loan.

Fund Set Asides for Certain Businesses

The Act stipulates that available funds for Second Draw Loans must be set aside for certain types of businesses, including small entities with no more than 10 employees as of February 15, 2020, community financial institutions, insured depository institutions with consolidated assets of less

than $10,000,000,000, credit unions with consolidated assets of less than $10,000,000,000; and institutions of the Farm Credit System chartered under the Farm Credit Act of 1971 (12 U.S.C. 2001 et seq.) with consolidated assets of less than $10,000,000,000 (not including the Federal Agricultural Mortgage Corporation).

Provisions of the Act Applying to PPP Loans Generally, Including Second Draw Loans

Clarification of Certain Categories of Eligible Borrowers

The Act clarifies that these entities are eligible for PPP loans if they meet the other PPP eligibility requirements:

- Destination marketing entities, defined as including 501(c) corporations; and state and local government instrumentalities engaged in promoting or marketing communities and facilities to businesses and leisure travelers or engaged in and deriving the majority of its operating budget from revenue attributable to providing live events.
- News organizations that are licensed broadcasters with no more than 500 employees or non-profits that are public broadcasting entities, that meet certain limitations and conditions;
- Housing cooperatives;
- Farm Credit Institutions (defined as an institution of the Farm Credit System chartered under the Farm Credit Act of 1971; and does not include the Federal Agricultural Mortgage Corporation).
- There are specific provisions for the calculation of maximum loan amount income for farmers and ranchers with or without employees.

Public Company Ineligibility

On or after the date of the Act, publicly traded corporations are not eligible for an original PPP loan or a Second Draw Loan.

Conflict of Interest Ineligibility

- If certain members of the Federal Executive Branch or Congress, or their spouses, directly or indirectly hold a controlling ownership or equity interest in an entity, the entity may not obtain a new PPP loan on or after the date of the Act.

- For loans obtained before the date of the Act, the entity shall disclose such a conflict of interest to the SBA if, either before or after the date of the Act, it applied for or applies for forgiveness of the loan.

Definition of Seasonal Employer

For all past and future PPP loans, "season employer" is defined as an entity that does not operate for more than 7 months in a calendar year; or during the preceding calendar year, had gross receipts for any 6 months of that year that were not more than 33.33 percent of the gross receipts of the employer for the other 6 months of that year.

Forgiveness of Additional Expenses

For existing and future loans where forgiveness has not already been granted before the enactment of the Act, the additional expense categories discussed in the section above on Second Draw Loans are now allowed to be forgiven:

- Operations expenditures, including defined software and computing costs, processing of payrolls, and various back office support functions;
- Property damages and vandalism costs related to public disturbances in 2020 that are not covered by insurance;
- Supplier costs based on contractual obligations in effect at the date of the loan, and which are essential for business operations;
- Worker protection expenditures related to compliance with worker safety and health mandates related to the COVID emergency;
- Group life, disability, vision, and dental insurance are expressly listed as payroll costs.

Covered Period

The "covered period" for determination of full time employee equivalent, payroll, etc., is extended from December 31, 2020 to March 31, 2021.

Deductibility of Forgiven Expenses

To undo a previous IRS interpretation, the Act provides that for any PPP loan, forgiven expenses are tax deductible even if excluded from gross income. This applies to any present or future PPP loan, even if forgiveness has already been granted.

Entities in Bankruptcy



The Act makes temporary changes to the Bankruptcy Code to enable debtors or trustees to apply for PPP loans, subject to approval of the Bankruptcy Court. The changes will take effect when the SBA Administrator submits a written determination to the Director of the Executive Office for United States Trustees stating that if debtors or trustees meet other PPP requirements, they may obtain PPP loans.

Liability Protection for Lenders

The Act clarifies lenders' liability protections in regard to any PPP loan, regardless of when made and regardless of when forgiveness was or will be granted. A lender may rely on a borrower's certification that it has complied with PPP requirements and submitted the certifications and documents required. If the borrower provided such a certification and made such submissions, no enforcement action may be brought against a lender under any Federal, State, or other criminal or civil law or regulation, and no lender shall be subject to penalties based on loan forgiveness, origination or guarantee, provided that:

- The lender acted in good faith relating to loan origination or forgiveness; and
- All statutory and regulatory requirements related to the lender are met.

This applies to any past, present or future PPP loan, even if forgiveness has already been granted.

Date of Operation for Loan Eligibility

To be eligible for a PPP loan, an entity must have been in operation on February 15, 2020.

Borrower May Choose Any Forgiveness Covered Period Between 8 and 24 Weeks

For loans where forgiveness is provided after the date of the Act, the borrower is not limited to a choice of 8 weeks or 24 weeks for the covered period for which it seeks forgiveness – the borrower may choose any length of time between 8 weeks and 24 weeks after the origination of the loan.

Inability to Restore Employee Headcounts

For loans made on or after the date of the Act, the time period for determining that no reduction in forgivable payroll costs is required based on the inability to rehire an employee or hire a comparable new employee, or to return to previous level of business activity due to COVID-related government requirements, is moved from December 31, 2020 to the last date of the borrower's selected covered period.

Eligibility for Increased Loan Amount

If a borrower is eligible for an increased covered loan amount as a result of any interim final rule that allows for covered loan increases, the borrower may submit a request for an increase in the loan amount even if the initial loan amount has been fully disbursed.

Lender Fees From SBA

For loans made on or after the date of the Act, the SBA shall pay lenders the following fees:

- for a covered loan of not more than $50,000, the lesser of:
    - 50 percent of the balance of the financing outstanding at the time of disbursement of the covered loan; or
    - $2,500; and
- 5 percent for a covered loan of more than $50,000 and not more than $350,000,;
- 3 percent for a covered loan of more than $350,000 and less than $2,000,000; and
- 1 percent for a covered loan of not less than $2,000,000.

Interest Calculation

For loans made on or after the date of the Act, interest is to be calculated on a non-compounding, non-adjustable basis. Lenders and borrowers on loans made prior to the Act may agree to adopt this method of calculation.

Agent Fees

The Act resolves an issue about payment of agent fees that has led to a number of class actions against lenders for alleged failure to pay the fees of borrowers' agents:

- If a borrower knowingly engages an agent to assist with obtaining a PPP loan, the borrower is responsible for paying the agent's fees, and PPP loan proceeds cannot be used to pay the agent;
- A lender is only responsible for paying an agent's fees in regard to services for which the lender directly contracted with the agent.

Obtaining PPP Loan Proceeds That Were Returned or Not Taken

For borrowers of PPP loans who as of the date of the Act have not yet received forgiveness, and

the borrower:

- Returned amounts disbursed under its PPP loan, the borrower may apply for a new loan equal to the difference between the amount retained and the maximum amount applicable.

- Did not accept the full amount of the PPP loan for which the borrower was approved, the borrower may, subject to general PPP requirements, apply for a modification of the loan amount to the maximum amount applicable.

SBA Nonrecourse on Refinances

For all PPP loans, the SBA shall not have recourse against any individual shareholder, member, or partner of a borrower for non-payment of a PPP loan to the extent that the PPP loan was used to refinance an existing loan.

No Personal Guaranty

For all PPP loans, the prohibition against personal guarantees during the covered period is extended to apply for the entire life of the loan. There is no provision regarding how to implement this requirement on loans that previously had personal guarantees.

Payment Deferral

For all PPP loans, the lender and investor payment deferral requirements during the covered period now apply during the entire life of the loan.

EIDL Grant Does Not Reduce Amount of PPP Forgiveness

Originally, if a PPP borrower obtained an Economic Injury Disaster Loan $10,000 emergency grant, that amount was deducted from the amount of PPP forgiveness the borrower could receive. The Act repeals that requirement – the EIDL grant does not reduce the allowable amount of PPP loan forgiveness. The Act requires the SBA to issue rules addressing how all entities are to be treated equally in this regard, including those that previously obtained forgiveness without the amount of the EIDL.

Lobbying Expense Ban

PPP loan proceeds may not be used for lobbying purposes.

Simplified Loan Forgiveness for Loans of $150,000 or Less

Borrowers applying for a loan of $150,000 or less may use a simple, one page form the SBA is

charged with developing within 7 days of the enactment of the Act. The form will require the borrower to provide only:

- The number of employees whose jobs were preserved due to the PPP loan;
- The amount of loan proceeds spent on payroll costs;
- The total amount of the loan;
- An attestation that its certification was accurate, that it has complied with PPP requirements, and that it is maintaining required records.

However, the borrower may be required to submit documentation to support its claimed payroll cost forgiveness.

After the lender submits the forgiveness application to SBA, SBA may choose to audit the loan. If it does so and determines that there is fraud, ineligibility or other material noncompliance with program requirements, it may modify the amount of the loan or the amount of forgiveness.

Instead of submitting otherwise required documents, the borrower is to retain all employment records and other records relevant to expense forgiveness.

Buchalter's Commercial Finance Group has organized its attorneys to create in-depth expertise in every aspect and requirement of the PPP. Buchalter's Commercial Finance Group is comprised of attorneys with extensive transactional and regulatory expertise, and is one of the largest firms on the West Coast providing sophisticated counseling to both creditors and borrowers. Thus, our commercial finance attorneys are uniquely positioned to advise clients on the PPP. Please feel free to contact any of the attorneys in Buchalter's Commercial Finance Group if you have questions regarding the PPP or would like to discuss the various options and details under the program.



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