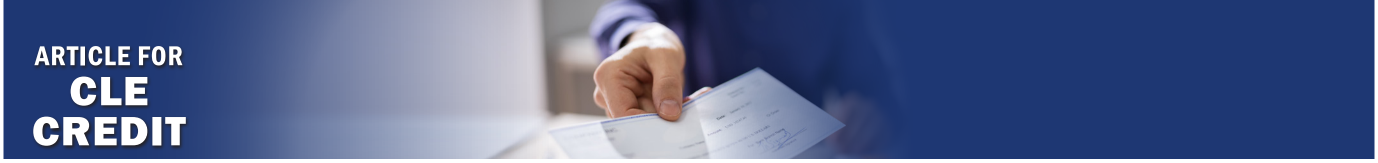


Practical Pointers – Paycheck Protection Program Loans

BY DARA J. GOLDSMITH, ESQ. AND AMANDA NETUSCHIL, ESQ.

The events of the past two years have been difficult for all of us. The practice of law has changed as we know it because of the COVID-19 pandemic. We now Zoom and use programs like Bluejeans and Google Meetings to meet with clients, attend meetings, and appear in court. Many of us rarely darken the doorstep of a courthouse, or at least with far less frequency than before March 2020.

Sensing the issues that would be created by a global pandemic and shutting down the U.S. economy, Congress enacted multiple economic relief packages in spring 2020, including the Coronavirus Aid, Relief, and Economic Security (CARES) Act. CARES originally set aside $349 billion for small business relief, to be administered by the Small Business Administration (SBA) through the use of a Paycheck Protection Program (PPP).[1] According to FederalPay.org, there were 11,768,689 total PPP loans and 4,318 lenders, and the average PPP Loan was $67,866.00. The first round of PPP loans opened on April 3, 2020, and closed April 16, 2020,[2] and many small businesses missed the short window to apply for the first round of loans, as some banks chose to handle larger loans applied for by larger companies. The second round of PPP loans allocated an additional $320 billion and included limitations designed to help small businesses that needed help, rather than large businesses or successful or growing small businesses. The second round of PPP loans closed on August 8, 2020.[3] With more than 11 million loans funded in the U.S., chances are that you know someone with a PPP loan or two, and that someone could be you or a client (a borrower).

The PPP program was designed to help small business owners whose income was slashed as a result of the pandemic cover expenses associated with the payroll costs, rent, utilities, employee benefits, and even uninsured property damage costs caused by looting or vandalism in 2020.[4] While waiting for PPP loans or other assistance, many business owners tapped into or drained their personal savings or retirement funds to try to keep their businesses afloat. Some of these businesses survived, others did not.

Almost any business could qualify for the first round of PPP loans, including but not limited to the following: sole proprietors, independent contractors, self-employed persons, most businesses, 501(c)(3) non-profit organizations, and 501(c)(19) veterans' organizations. Some larger successful businesses were able to satisfy the requirements in the first round and received PPP loans. After being reported in the media, some of these entities repaid the loans immediately. To qualify for the second round of PPP loans, a prior borrower who would or had used the full amount of the original PPP loan must have had no more than 300 employees and must have demonstrated at least a 25 percent reduction in gross receipts between comparable quarters in 2019 and 2020. The same requirements applied to a first-round borrower, as well as a similarly situated new borrower.[5] The funds for the second loan could be used for a variety of reasons including: payroll costs, including sick leave and health insurance; interest on loans; rent; and utilities.[6]

The PPP loans were not only a lifeline to continue scaled-back operations or funding during a full shutdown, but they were also relatively easy to qualify for, had no/nominal front-end costs, came with a guaranteed low interest rate and other favorable terms. The PPP loans have an interest rate of 1 percent and a maturity date of between two years and five years. Loans that were issued after June 5, 2020, have a maturity of five years.[7]

Given the ease and speed of loan funding, there were bound to be borrowers who stretched the truth to qualify for loans. Desperate times may have called for desperate measures. Some borrowers might not have been 100 percent honest on the PPP loan application. Even during a global pandemic, it is illegal to make false statements to a financial institution, so if a borrower lied on a PPP loan application, the borrower could be charged with a federal crime. Pursuant to 18 U.S.C. §1014, if convicted, a hefty fine may be imposed upon the borrower, along with imprisonment for up to 30 years.

In addition to the extremely low interest rate to entice borrowers to keep their businesses open or to pay employees during a shutdown, a PPP loan may qualify to be forgiven, in part or in its entirety.[8] 15 U.S.C. §9005(b) provides that a PPP loan recipient can be forgiven for an amount spent on: (1) payroll costs, (2) any payment of interest on any covered mortgage obligation, (3) any payment on any covered rent obligation, and (4) any covered utility payment.[9] Once a borrower seeks forgiveness, the borrower's loan payments are stayed until the SBA has completed giving the loan forgiveness information to the lender.[10]

To qualify for loan forgiveness, the following requirements must be met during the eight- to 24-week covered period after the PPP loan disbursement: (1) the employee compensation levels were maintained, (2) the loan proceeds were spent on payroll costs and other eligible expenses, and (3) at least 60 percent of the proceeds were spent on payroll costs.[11] A borrower may only apply for forgiveness once all funds have been depleted, and up and until the maturity of the loan.[12] If the loan has been fully paid, it cannot be forgiven.[13]

If a borrower does not apply for forgiveness within 10 months after the last day of the covered period, the PPP loan will cease to be deferred, and instead, payments will have to begin to a particular lender.[14] In what instances would a borrower fail to apply for forgiveness? Suppose the borrower dies or loses capacity. While there is no clear guidance from the SBA at this time, the duly appointed personal representative, guardian, or attorney-in-fact should garner the necessary information along with documentation of their authority and submit the application for forgiveness. Accordingly, in canvassing probate and guardianship matters, it is important to determine if the decedent/proposed protected person had any PPP loans. If the personal representative, guardian, or attorney-in-fact is not sure, contact the SBA with proof of authority and seek direction.

Buying and selling businesses now has an added complication. Does/did that business have a PPP loan? Has that loan been forgiven, or has the borrower applied for forgiveness? Is the loan being knowingly assumed by the new business owner? Even if the borrower sells the business, the borrower is still responsible for the loan, and the lender must be notified of proposed ownership change.[15] These issues should be addressed in the representations and warranties of any asset or stock/membership sale agreement to avoid issues and surprises in the future. It is important to involve and get approval from the lender.

Once the borrower is within the correct timeframe to apply for forgiveness, a protocol[16] needs to be followed to seek forgiveness. Some loan-forgiveness requests are handled through the lender and others directly through the SBA.[17] The necessary steps are beyond the scope of this article and are form and data driven.[18] Seek advice and input from the borrower's CPA, as many CPAs assist clients with loan-forgiveness processing.

Once a borrower has submitted the correct forms, they will need to monitor the status of forgiveness. The SBA will notify the borrower of the loan's review, if they undertake a review, and the borrower even has the opportunity to appeal certain loan-review decisions conducted by the SBA. The borrower's specific lender is the one responsible for notifying the borrower of the forgiveness amount paid by the SBA and the date on which the borrower's first payment will be due if the forgiveness amount does not cover the borrower's loan fully.[19]

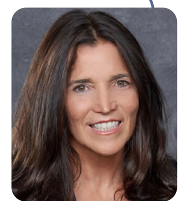
A borrower whose loan is not fully forgiven may attempt to augment the materials provided to support the borrower's request for forgiveness. If that does not result in forgiveness and the borrower believes that loan should be forgiven, the borrower may appeal the decision within 30 days. The appeal will be assigned to an administrative law judge for review.[20]

If the borrower does not qualify for forgiveness because the monies were not used for a proper purpose or simply do not satisfy the formula, the borrower may be eligible for relief under the Bankruptcy Code.[21] These loans were not created to become an added burden during an already troublesome time, and as such, the system created for the loans provides ample opportunity for the loan to be forgiven. If the SBA does not fully pay off the borrower's loan, the remaining balance may be erased through bankruptcy.[22] If the borrower receives a bankruptcy discharge, the borrower is no longer responsible for paying back the borrower's debt. The borrower will get a fresh start.

It is still important to heed the potential dangers that exist if seeking to use bankruptcy to eliminate the PPP loans. If the proper documents were not maintained to reflect the borrower's financial condition at the time of the PPP loan, the borrower could run into problems.[23]

Another developing area of law is how to handle PPP loans in the event of divorce. *Forbes* magazine briefly addressed this issue, stating that it was important for all appropriate accounting measures to have been taken to reflect how the loan funds were applied and what portion, if any, was forgiven or needs to be repaid. Accurate accounting is important because of impact on joint tax filling, or how it should be treated in appraisal of business in connection with divorce.

The PPP loans were created to help businesses during these devastating times, and more questions will continue to arise regarding the PPP loans. The analysis of these loans and the ramifications of the borrower's actions and inaction will continue to develop over time. The implications of these loans on borrowers, their family, assignees, personal representatives, and business associates is a developing area of the law.



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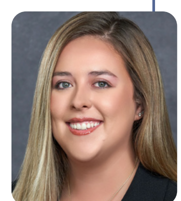

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ENDNOTES:

1. https://www.americanactionforum.org/research/tracker-paycheck-protection-program-loans/
2. *Id.*
3. *Id.*
4. https://www.sba.gov/funding-programs/loans/covid-19-relief-options/paycheck-protection-program
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6. *Id.*
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12. *Id.*
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