FEDERAL DISASTER RELIEF PROGRAMS FOR SMALL BUSINESSES

There are several federal disaster relief programs available to businesses impacted by COVID-19, and we have been tracking all of the recent legislation (See FAQ for Employers Relating to COVID-19). Below are some frequently asked questions about the following programs:

- Traditional 7(a) Small Business Administration (SBA) Loans
- Paycheck Protection Program under the Coronavirus Aid, Relief and Economic Security Act (CARES Act)
- Economic Injury Disaster Loans (EIDL)
- SBA Express Bridge Loans

Q: How is the Paycheck Protection Program different from traditional 7(a) SBA loans?

A: The Paycheck Protection Program expands the SBA's traditional 7(a) loan program and eligibility requirements to include any business concern, nonprofit organization, veterans organization, or tribal business concern that has no more than 500 employees. The Paycheck Protection Program also expands the eligibility of 7(a) loans to individuals who operate under a sole proprietorship or as an independent contractor and to eligible self-employed individuals. The program includes other attractive features, including a six-month payment deferral option and the ability for portions of the loan to be forgiven.

Q: Who is eligible for loans under the Paycheck Protection Program?

A: In general, any business concern, nonprofit organization, veterans organization or tribal business concern that (i) together with its affiliates, has no more than the greater of 500 employees or, if applicable, the size standard established by the SBA for the industry in which the business concern operates, (ii) was in operation on February 15, 2020, and (iii) had employees or independent contractors for whom the business concern paid salaries, compensation, and payroll taxes. Cannabis companies are not eligible for the Paycheck Protection Program or other SBA loans.

Applicants are eligible to apply for loans under the Paycheck Protection Program until June 30, 2020.

Q: Do the SBA affiliation rules apply to loans under the Paycheck Protection Program?

A: Yes. On April 2, 2020, the SBA issued its Interim Final Rule, which provides that businesses eligible for loans under the Paycheck Protection Program will be subject to the SBA's existing affiliation rules. Then on April 3, 2020, the SBA issued a supplemental Interim Final Rule and a supporting guidance document to provide clarity on how the affiliation rules will apply to businesses. The new SBA guidance confirms that, in most cases, borrowers will be considered together with their affiliates for purposes of determining eligibility for loans under the Paycheck Protection Program.

Pursuant to 13 CFR 121.301(f), affiliation occurs when one entity controls or has the power to control another entity, or when a third party controls both entities. Control does not have to be exercised; merely the power to control will suffice for purposes of determining affiliation.

The recent SBA guidance clarifies that affiliation will exist under any of the following circumstances:

- **Ownership:** When an entity owns or has the power to control more than 50% of the other entity's voting interests. A minority shareholder may also be in control if it has the power to prevent a quorum or block action by the board of directors or shareholders.

- **Stock options, convertible securities, and agreements to merge:** When stock options, convertible securities, and agreements to merge (including agreements in principle) affect one entity's control over another entity.

- **Management:** When a CEO or president of one entity also controls the management of another entity; when a single individual that controls the board of directors or management of one entity also controls the board of directors or management of another entity; or when an entity controls the management of another entity through a management agreement.

- **Identity of interest:** When close relatives have identical or almost identical business or economic interests.

The recent SBA guidance also clarifies that the affiliation rules are waived for the following businesses:

- Businesses with fewer than 500 employees at each physical location in the food services and hospitality industries (NAICS code 72 designation);
- Franchises assigned a franchise identifier code by the SBA; and
- Businesses that receive SBIC financing.

Q: Do I need to demonstrate financial hardship to qualify for the Paycheck Protection Program?

A: No, there is no financial hardship requirement. Applicants are only required to make a good faith certification that (i) the uncertainty of current economic conditions makes necessary the loan request to support the ongoing operations of the applicant, and (ii) the funds will be used to retain workers and maintain payroll or make mortgage payments, lease payments, and utility payments.

Q: How much can I borrow under the Paycheck Protection Program?

A: In most cases, applicants can borrow up to 250% of their average total monthly payroll costs during the one-year period before the date of the loan, plus the amount of any eligible EIDL to be refinanced into the Paycheck Protection Program loan. However, the eligible payroll costs for each employee are capped at $100,000 for each employee with an annual salary above $100,000. The proceeds of a loan under the Paycheck Protection Program can be used to cover eligible payroll costs, costs related to group health benefits, payments of mortgage interest, rent and utilities, and interest on any other debt obligation incurred before February 15, 2020. The Interim Final Rule clarifies that independent contractors do not count as employees for purposes of a borrower's loan calculation or loan forgiveness because independent contractors have the ability to apply for a Paycheck Protection Program loan themselves.

Q: What are the terms of a loan under the Paycheck Protection Program?

A: Pursuant to the SBA's Interim Final Rule, the loans will have a maturity of two years, will bear interest at 1%, and payments of principal may be deferred for six months.

Q: How do I apply for the Paycheck Protection Program?

A: The Paycheck Protection Program is administered by the existing network of approved SBA lenders. We recommend that you contact your existing lender or contact a local bank or credit union to see if they are participating in the program. You can find local SBA-approved lenders through the SBA's Find a Lender search. You can download the lender application form here. No personal guarantee will be required, no collateral needs to be pledged, and the participating lenders may not charge any fees.

Q: How much of a Paycheck Protection Program loan can be forgiven?

A: The amount eligible to be forgiven under a Paycheck Protection Program is the sum of the following costs incurred during the first eight weeks after the loan is originated: eligible payroll costs (capped at $100,000 per employee); payment of interest on a mortgage incurred before February 15, 2020; payment of rent on a lease in force before February 15, 2020; and payment for access to electricity, gas, water, transportation, telephone, or internet which began before February 15, 2020. The SBA's Interim Final Rule clarified that not more than 25% of the loan forgiveness amount may be attributable to non-payroll costs. Amounts forgiven under the Paycheck Protection Program are excluded from the borrower's gross income for federal income tax purposes. If the full principal amount of the Paycheck Protection Program loan is forgiven, the borrower is not responsible for the interest accrued in the eight-week period.

The amount eligible to be forgiven is reduced (but not increased) in proportion to any reduction in the number of employees employed by the borrower during either (at the election of the borrower) (i) the period from February 15, 2019 to June 30, 2019, or (ii) the period from January 1, 2020 to February 29, 2020. In addition, the amount of loan forgiveness is reduced by the amount of any reduction in compensation of any employee with an annualized salary of less than $100,000 by more than 25% of the compensation of that employee during the most recent full quarter during which the employee was employed before the eight-week period.

However, the amount of loan forgiveness will not be reduced if the borrower rehires the employees previously laid off or eliminates the wage reductions by June 30, 2020.

Q: How do I seek forgiveness of my Paycheck Protection Program loan?

A: A borrower seeks loan forgiveness by submitting an application to the servicing lender that includes the following documents and certifications:

- Documentation verifying the number of full-time employees on payroll and pay rates for the relevant pay periods, including:
  - payroll tax filings reported to the IRS, and
  - state income, payroll, and unemployment insurance filings.
- Documentation verifying payments on other covered costs, i.e., payments on covered lease obligations or mortgage interest, and covered utility payments, including payment receipts, transcripts of accounts, or other documents.
- Certification from an authorized representative of the borrower that:
  - the documentation presented is true and correct, and
  - the amount for which forgiveness is requested was used to retain employees, make payments on a covered rent obligation, make interest payments on a covered mortgage obligation, or make covered utility payments.
- Any other documentation the SBA determines necessary.

The lender is required to issue a decision on the loan forgiveness application within 60 days after receiving the application.

Q: Can I apply for both a Paycheck Protection Program loan and an Economic Injury Disaster Loan?

A: Yes, a business may apply for a loan under the Paycheck Protection Program in addition to an EIDL grant, provided that the loan proceeds are not used for the same purpose. If a borrower received an EIDL from January 31, 2020 through April 3, 2020, the borrower can still apply for a Paycheck Protection Program loan. If the EIDL loan was not used for payroll costs, it will not affect the borrower's eligibility for a Paycheck

Protection Program loan. If the EIDL loan was used for payroll costs, the borrower's Paycheck Protection Program loan must be used to refinance the EIDL loan. Proceeds from any advance of up to $10,000 under the EIDL loan will be deducted from the loan forgiveness amount on the borrower's Paycheck Protection Program loan.

Q: What are Economic Injury Disaster Loans, and who is eligible to apply?

A: EIDLs are provided under the existing Small Business Act that was modified by the CARES Act. During the period from January 1, 2020 until December 31, 2020, EIDLs are available for businesses or cooperatives with fewer than 500 employees, sole proprietors or independent contractors, or Employee Stock Ownership Plans (ESOPs), or tribal small business concerns with fewer than 500 employees, together with its affiliates. The CARES Act eliminates the requirements that (i) the borrower provide a personal guarantee for loans up to $200,000, (ii) the eligible business must be in operation for one year prior to the disaster, and (iii) the borrower must be unable to obtain financing from other sources.

The proceeds of an EIDL may be used to pay for fixed debts, payroll, accounts payable, and other obligations that cannot be met because the disaster's impact. EIDLs will have a maturity of up to 30 years and will bear interest at 3.75% for small businesses or 2.75% for private nonprofits. An EIDL borrower may receive a $10,000 emergency advance within three days after applying for an EIDL grant. The $10,000 advance is not required to be repaid, even if the application is denied. EIDLs are administered by the SBA, and eligible businesses can apply here. There is no fee to apply, and there is no penalty if a business is approved for a loan but declines to accept it.

Q: What is the Express Bridge Loan (EBL) Pilot Program, and where can I find more information?

A: The EBL Pilot Program authorizes SBA Express Lenders to provide expedited SBA-guaranteed bridge loan financing on an emergency basis in amounts up to $25,000 for disaster-related purposes to small businesses while those small businesses apply for EIDL financing. More information about the EBL Pilot Program can be found here.

Q: What if my business is too large for an EIDL or a loan under the Paycheck Protection Program?

A: On April 9, 2020, the Treasury and Federal Reserve each issued a press release announcing the Main Street Business Lending Program, a program that will provide direct low-interest loans to businesses, including mid-sized businesses, distinct from the loans offered to small businesses under the Paycheck Protection Program. The Main Street Business Lending Program is expected to officially launch within the coming weeks, and the following summary is subject to change as the Federal Reserve issues additional guidance.

Q: What kinds of loans will be included in the Main Street Business Lending Program?

A: The Main Street Business Lending Program will consist of two new loan facilities: (i) the Main Street New Loan Facility and (ii) the Main Street Expanded Loan Facility. The Main Street New Loan Facility will include new loans originated on or after April 8, 2020. The Main Street Expanded Loan Facility will include upsized tranches to increase the size of loans originated before April 8, 2020. In conjunction with its press release, the Federal Reserve published term sheets for the Main Street New Loan Facility and the Main Street Expanded Loan Facility.

Q: Who is eligible to receive loans under the Main Street Business Lending Program?

A: To be eligible to receive a loan under the Main Street Business Lending Program, the business (including a nonprofit organization) must:

- Have no more than 10,000 employees or no more than $2.5 billion in 2019 annual revenues.
- Be created or organized in the United States or under the law of the United States with significant operations in and a majority of its employees based in the United States.

Q: What loans are eligible for the Main Street Business Lending Program?

A: To be eligible under the Main Street Business Lending Program, the loan must meet the following criteria:

- Four-year maturity.
- Principal and interest payments deferred during the first year.
- Adjustable rate of SOFR (secured overnight financing rate) plus 250-400 basis points (i.e., 2.5% to 4.0%).
- Maximum loan size:
  - For the Main Street New Loan Facility - the lesser of (i) $25 million or (ii) an amount that, when added to the business' existing outstanding and committed, but undrawn debt, does not exceed four times the business' 2019 EBITDA (earnings before interest, taxes, depreciation, and amortization).
  - For the Main Street Expanded Loan Facility - the least of (i) $150 million, (ii) 30% of the business' existing outstanding and committed, but undrawn bank debt, or (iii) an amount that, when added to the business' existing outstanding and committed, but undrawn debt, does not exceed six times the mid-sized business' 2019 EBITDA.
- Minimum loan size of $1 million.
- Prepayment of the loan permitted without penalty.

Q: What certifications must be made by the business regarding the loan under the Main Street Business Lending Program?

A: The business will be required to make the following certifications:

- The business is not a debtor in a bankruptcy proceeding.
- The business will commit to refrain from using the proceeds of the loan to repay other loan balances.
- The business will commit to refrain from repaying other debt of equal or lower priority, with the exception of mandatory principal payments, unless the business has first repaid the loan under the Main Street Business Lending Program in full.
- The business will not seek to cancel or reduce any of its outstanding lines of credit with the lender or any other lender.
- The business requires financing due to the exigent circumstances presented by the COVID-19 pandemic, and that, using the proceeds of the loan, it will make reasonable efforts to maintain its payroll and retain its employees during the term of the loan.
- The business meets the EBITDA leverage condition discussed above.

- The business will not make dividends or distributions with respect to the business' common stock or buy back the company's listed securities until 12 months after the loan is repaid (except pursuant to a previously existing contractual obligation).
- The business will not outsource or offshore jobs for the term of the loan plus two years after the loan is repaid.
- The business will not abrogate existing collective bargaining agreements for the term of the loan plus two years after the loan is repaid.
- The business will remain neutral in any union organizing effort during the term of the loan.

Q: Will a loan under the Main Street Business Lending Program be eligible for forgiveness or reduction, similar to a loan under the Paycheck Protection Program?

A: No, unlike loans under the Paycheck Protection Program, the CARES Act prohibits the reduction or forgiveness of the principal amount of any loan made to an eligible business pursuant to a program or facility established by the Federal Reserve.

Q: Will a loan under the Main Street Business Lending Program be subject to the SBA affiliation rules, similar to a loan under the Paycheck Protection Program?

A: No, Title IV of the CARES Act does not impose the SBA's affiliation rules for businesses that receive a loan, loan guarantee, or other investment under a Federal Reserve program or facility.

Q: Is the SBA offering any other debt relief to small businesses during the COVID-19 pandemic?

A: As part of SBA's debt relief efforts, the SBA will automatically pay the principal, interest, and fees of current 7(a), 504, and microloans for a period of six months. The SBA also will automatically pay the principal, interest, and fees of new 7(a), 504, and microloans issued prior to September 27, 2020.

In addition, the SBA is offering automatic deferral through December 31, 2020 for current SBA Serviced Disaster (Home and Business) Loans that were in "regular servicing" status on March 1, 2020. Interest will continue to accrue on the loans, but the deferment will not cancel any recurring payments on the loan. Borrowers that established recurring payments online are responsible for canceling those recurring payments. Borrowers that wish to continue making regular payments during the deferment period may continue remitting payments during the deferment period. The SBA will apply those payments normally as if there was no deferment. After the automatic deferment period, borrowers will be required to resume making regular principal and interest payments. Borrowers that canceled their recurring payments will need to reestablish the recurring payment.

If you have any questions concerning this alert, please contact:

Daniel L. Phillips
Shareholder
Email
214.922.4174

J. Daniel Boysen
Attorney
Email
214.922.4193

Hallett & Perrin, P.C. provides this information as a service to clients and friends for educational purposes only. It should not be construed or relied on as legal advice or to create an attorney-client relationship. Readers should not act upon this information without seeking advice from an attorney.