

What's Next with PPP: Realities and Practicalities

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Agenda

- Overview of Congressional Action and Current State of Play
- The Good Faith “Necessity” Certification - FAQs and Evolving Guidance
- The Loan Forgiveness Process
- Tax Benefits Available or Impacted by PPP Loans
- Key Considerations for Boards and Management in Assessing Risks
- The Enforcement Landscape



Overview of Congressional Action and Current State of Play

Robert Mangas

Co-Managing Shareholder, Washington, D.C.

Federal Legislation Relating to COVID-19

- **March 6:** Coronavirus Preparedness and Response Supplemental Appropriations Act (\$8.3 B)
- **March 18:** Families First Coronavirus Response Act (over \$100 B)
- **March 27:** Coronavirus Aid, Relief and Economic Security (CARES) Act (\$2.2 Trillion)
- **April 24:** Paycheck Protection Program and Healthcare Enhancement Act (\$480 billion)
- Heroes Act? (\$3 Trillion) (passed House on **May 15**)




PPP Legislative Timeline

- **3/11:** President Trump calls for \$50 billion “economic loan” program
- **3/12:** Sen. Rubio announces bill to expand SBA 7(a) program by \$50 billion
- **3/18:** Sens. Rubio, Collins introduce \$300 billion small business relief plan
- **3/19:** Sen. McConnell introduces text of CARES Act, with \$300 billion expansion of 7(a) program; 4x monthly expenses; up to 500 employees
- **3/22:** CARES Act redesigned to include \$350 billion Paycheck Protection Program; 2.5x payroll; coordinated with SBA categories; adds self-employed
- **3/24:** CARES Act enacted

PPP Legislative Timeline (cont.)

- 4/7: Sec. Mnuchin seeks an additional \$250 billion in PPP funding
- 4/16: SBA stops accepting new applications
- 4/19: Treasury says \$300 billion “should be sufficient to reach almost everybody”
- 4/20: Democratic leaders want \$60 billion set aside for small banks
- 4/21: Agreement on PPP: \$310 billion, \$60 billion set aside for small lenders
- 4/24: Paycheck Protection Program and Healthcare Enhancement Act signed
- 5/12: Heroes Act text released: \$60 billion set aside replaced with 25% for employers with 10 or fewer employees, 25% for nonprofits; 25% for CFIs; adds local news media, all nonprofits, bankrupt hospitals; additional provisions on covered period for loan applications and loan forgiveness, 75/25 rule, safe harbor if cannot rehire, interaction with retention tax credit
- 5/15: House passes Heroes Act, 208 to 199



**Hot Topic:
The Good Faith “Necessity”
Certification –
FAQs and Evolving
Guidance**

A Group Discussion



The FAQs

FAQ 31

- Whether large companies with *adequate sources of liquidity* to support the business' ongoing operations qualify for a PPP loan?
- Reference to certifications
 - Affiliation
 - Economic necessity: “[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant” in a manner that is not significantly detrimental to the business
- Repayment safe harbor extended to May 18, 2020

FAQ 46

- Loans less than \$2 million total – certification will be deemed to have been made in good faith
- Loans greater than \$2 million
 - Borrower must have adequate basis for making certification
 - Subject to review
 - If lacking, SBA will seek repayment of the outstanding PPP balance and there will be no forgiveness
 - If repaid, SBA will not pursue administrative enforcement or referrals to other agencies

Next Steps

- If you do not meet the specific rules on affiliation or cannot justify the need, or have serious doubts about your position, consider returning the funds
- If you are uncertain whether you meet the rules, but believe you have a **good faith basis** for your interpretation of the rules that you believe justifies retaining the funds then:
 - Clearly document your analysis;
 - Be prepared to pay back; and
 - Be prepared for possible reputational risk.

Continuing Issues

- How will SBA review borrowers' required good-faith certification concerning the necessity of their loan request?
- What does necessary mean?
- What does other sources of liquidity that are not significantly detrimental to the business mean?
- What should companies consider when deciding whether to keep allocated PPP funds?
- Is the \$2 million limit on audits really a safe harbor?

The Loan Forgiveness Process

Lee Ann Anderson

Shareholder, Washington, D.C.

&

Jennifer S. Zucker

Shareholder, Washington, D.C.

PPP – A Quick Review

- As noted at the top, there are various proposals to change substantially the terms of the program, including extensions of time periods, revisions to the 75% rule, and revisions to loan terms. We are discussing the law as it exists today.
- 2.5 x Average Monthly Payroll
- PPP loans have a term of two years, bear interest at 1% per annum and require no principal payments for the first six months, although interest accrues.
- Must be used 75% for payroll costs for US-resident employees

Payroll Costs

- Salary, wage, commission or similar compensation (up to \$100,000 per employee)
- Cash tips or equivalent
- Payment for vacation, parental, family, medical, or sick leave (other than qualified family or sick leave wages for which a credit is allowed under Sections 7001 or 7003 of the Families First Coronavirus Response Act)
- Allowance for dismissal or separation
- Payment required for the provision of group health care benefits, including insurance premiums
- Payment of any retirement benefit
- Payment of state or local tax assessed on the compensation of employees

Forgivable Uses

- Forgivable uses
 - During the 8 weeks beginning from when you received your first installment on the PPP loan
 - You must incur and pay 75% or more on payroll costs
 - You may incur and pay no more than 25% on
 - Payment of interest on a mortgage entered into prior to Feb. 15, 2020 (but not on principal prepayments),
 - Any rent payment under a rental agreement or lease entered into prior to Feb. 15, 2020
 - Utilities (for which service commenced prior to Feb. 15, 2020)

Utilities

- Electricity
- Gas
- Water
- Transportation (waste removal?)
- Telephone
- Internet Access

Allowable Uses

- Other allowable (but not forgivable) uses (up to 25%)
 - Costs related to the continuation of group health care benefits during periods of paid sick, medical or family leave (other than qualified family or sick leave wages for which a credit is allowed under Sections 7001 or 7003 of the Families First Coronavirus Response Act), and insurance premiums
 - Payment of interest on any mortgage obligation (but not on any prepayment of principal)
 - Rent
 - Utilities
 - Interest on any other debt incurred before Feb. 15, 2020
- Uses other than allowable uses could result in a fraud prosecution!

How Do I Apply for Forgiveness?

- Through your bank after the end of the eight-week period (or after June 30, 2020 if you are relying on the hire back provisions described below).
- Use the Treasury Department's forgiveness application form (detailed instructions and worksheets).
- Documentation Requirements
- Consider keeping the loan proceeds in a segregated account
- Further guidance from the SBA and/or the Treasury Department may include changes or further details on the current rules
- Future legislation may also alter the forgiveness program

How Do I Calculate the Forgivable Amount?

- Your forgiveness amount may be reduced as follows:
 - If, during the eight-week period (or alternative payroll covered period) from when you receive your first installment of your PPP loan, your full-time equivalent (FTE) count is lower than:
 - Your average FTE count during the period Feb. 15, 2019 through June 30, 2019, or
 - Your average FTE count during the period Jan. 1, 2020 through Feb. 29, 2020,
 - Then your forgiveness may be adversely impacted unless you rehire a sufficient number of employees for any changes you made between February 15, 2020 and April 26, 2020 to equal the average FTEs of your chosen measurement period before June 30, 2020.

Forgiveness Continued

- FTE count is not reduced for employees who turned down a good faith written offer of rehire, and
 - Employees fired for cause during the covered period (or alternative)
 - Employees who voluntarily left employment during the covered period (or alternative), or
 - Employees who voluntarily reduced their hours
- For employees who made less than \$100,000 in 2019, if you reduce salaries during the eight-week period (or alternative payroll covered period) by more than 25% (as compared to January 1, 2020 to March 31, 2020), your forgiveness may be reduced by the amount of salary reduction on a dollar-for-dollar basis in excess of 25%, unless the salary is restored by June 30, 2020.

Calculating Average FTE

- Average FTE: Calculation of the average full-time equivalency (FTE) during the Covered Period or the Alternative Payroll Covered Period
- For each employee, enter the average number of hours paid per week, divide by 40, and round the total to the nearest tenth (but not > 1.0)
- Borrowers can choose a simplified method that assigns a 1.0 for employees who work 40 hours or more per week and 0.5 for employees who work fewer hours

Additional Thoughts

- In order to be eligible for forgiveness, and consistent with requirements for the use of PPP loan proceeds, you must have spent 75% of your PPP loan on payroll costs, and not more than 25% of the amount you are requesting for forgiveness can be for things other than payroll cost.
- If your entire loan is not forgiven, the remaining amount is converted to a term loan bearing 1% interest and a total two year term (starting from when you received funds). The interest accrued during the first six months of the loan that accrued on that amount also will be owed.
- If your whole loan is forgiven, the accrued interest is also forgiven.
- The loan forgiveness is not taxable for Federal income tax purposes, but may be for state and local tax purposes.



Tax Benefits Available or Impacted by PPP Loans

Marvin Kirsner

Shareholder, Boca Raton

Tax Benefits Potentially Impacted as a Result of a PPP Loan

- Employee Retention Tax Credit
- Payroll Tax Deferral
- Paid Medical Leave and Paid Family Leave Tax Credit
- EIDL loans

Employee Retention Tax Credit

- 50% refundable tax credit
- Qualified wages paid to employees
- Governmental closure order or significant decline in gross receipts
- \$5,000 maximum credit per employee
- Can reduce workforce and/or pay
- No limit on size of company (but better for companies of up to 100 employees)
- H.R. 6800 would expand benefits of credit

No Employee Retention Credit if Company Receives PPP Loan

- No credit if PPP loan received
- Extends to members of aggregated group
- Current understanding – Any company which shares common owners of more than 50%
- Under this definition, if one portfolio company of PE fund receives PPP loan, all other port co's would be ineligible for PPP loan.
- If PPP loan is returned by SBA safe harbor deadline, company may claim the credit (FAQ # 45)

Payroll Tax Deferral

- Allows company of any size to defer payment of employer's share of social security tax (6.2%)
- Effective for wages paid after March 27, 2020
- Half of deferred tax due Dec. 31, 2021, and other half due Dec. 31, 2022
- No deferral allowed after all or part of PPP loan has been forgiven.
- May continue to defer taxes which accrued prior to forgiveness date (see IRS Payroll Tax Deferral FAQ # 4)

Paid Medical Leave and Paid Family Leave Tax Credit

- Companies with 500 employees or less
- Required to pay 10 days COVID-19 related sick leave (\$511/day or \$200/day)
- Employer gets 100% tax credit
- Not impacted by PPP loan
- However, amount of leave paid should not count as payroll for PPP forgiveness (since it is reimbursed to employer by the credit)

EIDL

- Loans do not impact other tax benefits
- EIDL grants would be reported as income unless further guidance to the contrary is issued

Tax Issues of PPP Loan

- Forgiveness of loan is not taxable for federal income tax purposes
- Would still be taxable for state tax purposes in many states (CARES Act language did not amend § 108 of Tax Code)
- No deduction for wages and rent paid with PPP loan proceeds (IRS Notice 2020-32)
- This nondeductibility is controversial – Does not appear to be intent of Congress



Key Considerations for Boards and Management in Assessing Risks

David C. Peck

Shareholder, Fort Lauderdale

Board Considerations

Now Famous (or Infamous) SBA PPP Certification Language:

- “[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant.”
- Taking into account “their current business activity and their ability to access other sources of liquidity sufficient to support their ongoing operations in a manner that is not significantly detrimental to the business.”

Board Considerations (cont'd)

Board of Directors/Managers – Should Review and/or Consider:

- Historical practices
- Applicable State Law(s) or Statutes
- Governing Documents (Charter, Bylaws, LLC Operating or Shareholders Agreements, Investor Agreements)
- Lender or Loan Document Requirements

Board Considerations (cont'd)

With Management's Input, Assess the Operational Needs
Such As:

- Market and economic conditions and projected impact on revenues, pre-COVID forecasts
- Projections for the duration of adverse effects of COVID, both temporary and/or long-term
- Operational and financial effects of COVID, governmental measures and restrictions

Board Considerations (cont'd)

- Impact on customers – For example, revenues, bad debt or extended payment scenarios, changes in demand, competitive environment
- Impact on suppliers and vendors – How will supply chains be affected and what is the impact or alternative sources for the business
- Risks of breaches or defaults under existing obligations – For example, financing and credit agreements, leases, and supply agreements

Board Considerations (cont'd)

What Liquidity Options Are Available:

- Current balance sheet and projections
- Borrowing under existing facility(ies) or other access to other lenders
- Additional investment(s) from current equity holders

Absent the PPP Loan, how long does the business project its available capital will last?

Board Considerations (cont'd)

Documentation of the Board's and Management's thoughtful consideration and assessment of:

- The uncertainties the company is facing;
- The support needed for the company's operations; and
- The ability to access other sources of liquidity to provide needed support that is not significantly detrimental to the business

The Enforcement Landscape

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Attorney General William P. Barr Urges American Public to Report COVID-19 Fraud

FOR IMMEDIATE RELEASE

Friday, March 20, 2020

Attorney General William P. Barr Urges American Public to Report COVID-19 Fraud

Attorney General William P. Barr is urging the public to report suspected fraud schemes related to COVID-19 (the Coronavirus) by calling the National Center for Disaster Fraud (NCDF) hotline (1-866-720-5721) or by e-mailing the NCDF at disaster@leo.gov .

This week, Attorney General Barr directed all U.S. Attorneys to prioritize the investigation and prosecution of Coronavirus-related fraud schemes. In a follow-up memorandum issued March 19, Deputy Attorney General Jeffrey Rosen further directed each U.S. Attorney to appoint a Coronavirus Fraud Coordinator to serve as the legal counsel for the federal judicial district on matters relating to the Coronavirus, direct the prosecution of Coronavirus-related crimes, and to conduct outreach and awareness.

Two Charged in Rhode Island with Stimulus Fraud

FOR IMMEDIATE RELEASE

Tuesday, May 5, 2020

Two Charged in Rhode Island with Stimulus Fraud

First in the Nation to be Charged with Fraudulently Seeking CARES Act SBA Paycheck Protection Loans

Two businessmen have been charged in the District of Rhode Island with allegedly filing bank loan applications fraudulently seeking more than a half-million dollars in forgivable loans guaranteed by the Small Business Administration (SBA) under the Coronavirus Aid, Relief, and Economic Security (CARES) Act.

What DOJ Prosecutors Look For

- Knowing / Willful false statements and fraud
- The law does not criminalize inadvertent mistakes, good faith confusion

BUT...

- Conscious effort not to learn the truth may create liability
- Accuracy should be assessed at each step of process / with each certification

Excerpts– Forgiveness Certifications

I understand that if the funds were knowingly used for unauthorized purposes, the federal government may pursue recovery of loan amounts and/or civil or criminal fraud charges.

The Borrower has accurately verified the payments for the eligible payroll and nonpayroll costs for which the Borrower is requesting forgiveness.

The information provided in this application and the information provided in all supporting documents and forms is true and correct in all material respects. I understand that knowingly making a false statement to obtain forgiveness of an SBA-guaranteed loan is punishable under the law, including 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 thirty years and/or a fine of not more than \$1,000,000.

The tax documents I have submitted to the Lender are consistent with those the Borrower has submitted/will submit to the IRS and/or state tax or workforce agency. 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 ensuring compliance with PPP requirements and all SBA reviews.

Title: Form 3508 Forgiveness Form (Documents Required to Be Maintained)

The Form identifies 4 specific items plus the following catchall language:

“All records relating to the Borrower’s PPP loan, including documentation submitted with its PPP loan application, documentation supporting the Borrower’s certifications as to the necessity of the loan request and its eligibility for a PPP loan, documentation necessary to support the Borrower’s loan forgiveness application, and documentation demonstrating the Borrower’s material compliance with PPP requirements. The Borrower must retain all such documentation in its files for six years after the date the loan is forgiven or repaid in full, and permit authorized representatives of SBA, including representatives of its Office of Inspector General, to access such files upon request.”

Risk of Enforcement

- Very fact-specific
- Subject to changes in legal landscape (which has been very dynamic)

Civil Enforcement – False Claims Act

- Statutory penalties and potential treble damages for knowing submission of false claims to gov't
- “Knowing” includes deliberate ignorance and reckless disregard of truth
- Lower standard of proof than criminal enforcement
- Recovery available against individuals
- Role of whistleblowers

FAQ 46 and Criminal / Civil Enforcement

- Statement of how SBA will prioritize and deploy its audit resources
- Does not bind DOJ or private parties
- May give rise to defenses but does not eliminate enforcement risk
- Role of business decision about necessity

Mitigating Enforcement Risk

- Understand facts and legal restrictions before signing any certification (at application, request for forgiveness, etc.)
- Maintain supporting paperwork
- Maintain compliance mechanisms (audits, reports)
- Be aware of public statements (e.g., SEC filings) and internal statements about finances (e.g., financial health, payroll, employee retention)
- Address internal whistleblower complaints



Questions?

For more information,

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