



## Alerts

### COVID-19 Relief Bill Creates Second Paycheck Protection Program

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*Hinshaw Alert*

*Editorial note: in a prior version of this alert, we incorrectly stated the amount that a first time PPP borrower can receive under the new PPP program. The maximum amount for a new PPP borrower is the lesser of 2.5 times monthly payroll costs or \$10,000,000. We apologize for the error.*

On December 28, 2020, President Trump signed the Consolidated Appropriations Act. Over 5,000 pages in length, the Act included revisions and additions to the Paycheck Protection Program (PPP). The new PPP will (1) accept applications from eligible borrowers that did not receive a PPP loan under the earlier program; (2) permit qualifying businesses that received a PPP loan under the earlier program to receive a second PPP loan—known as a second draw loan; (3) allow existing PPP borrowers who are ineligible for a second draw to spend any remaining PPP funds on permitted expenses, which includes additional forgivable expenses; and (4) change PPP rules for existing PPP borrowers, new PPP borrowers, and second draw borrowers in areas such as eligibility, forgivable expenses, and loan forgiveness.

Key sections of this legislation provide:

- More than \$284 billion to the SBA for PPP and allocates \$20 billion for Economic Injury Disaster Loan (EIDL) Grants to businesses in low-income communities.
- \$15 billion in dedicated funding in the form of grants to be made to shuttered live venues, independent movie theaters, and cultural institutions (a Shuttered Venue Operator Grant).
- \$12 billion to help business in low-income and minority communities.
- \$120 billion to be used so that workers will receive supplemental unemployment benefits of \$300 per week from December 26, 2020 to March 14, 2021.

The Act also extends (1) the employee retention tax credit; (2) the Pandemic Unemployment Assistance program, while also expanding coverage to individuals who are self-employed, as well as gig workers, and others in nontraditional employment; and (3) the Pandemic Emergency Unemployment Compensation program, which provides additional weeks of federally funded unemployment benefits to individuals who exhaust their regular state benefits.

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## PPP Provisions

### First-Time Borrowers

First-time borrowers from the following groups will be eligible to participate in the new PPP loan program, as long as they comply with all the PPP rules:

- Businesses with 500 or fewer employees that are eligible for other Small Business Administration (SBA) 7(a) loans
- Sole proprietors, independent contractors, and eligible self-employed individuals
- Not-for-profits, including churches
- Accommodation and food services operations—those with North American Industry Classification System (NAICS) codes starting with 72—with fewer than 300 employees per physical location

### Section 501(c)(6) Business Leagues

For the first time, Section 501(c)(6) business leagues such as chambers of commerce, visitors' bureaus, and "destination marketing organizations" will be allowed to secure PPP loans. To qualify, these entities must have 300 or fewer employees and must not receive more than 15% of their receipts from lobbying. In addition, their lobbying activities must comprise no more than 15% of the organization's total activities and have cost no more than \$1 million during the most recent tax year that ended prior to February 15, 2020.

### Destination Marketing Organizations

A destination marketing organization will be eligible for a PPP loan if:

- The organization receives less than 15% of its receipts from lobbying
- Lobbying does not comprise more than 15% of the total activities of the organization
- The costs of any applicable lobbying activities did not cost more than \$1,000,000 during the most recent tax year
- The organization employs 300 or fewer employees
- The organization is exempt under Internal Revenue Code Section 501(a) or is a quasi-government entity or political subdivision of a state or local government

### News Organizations

News organizations such as newspapers and broadcast news businesses are now eligible to apply for PPP funding. They may not employ more than 500 employees at each physical location or meet the applicable SBA size standard. This allows broadcast stations licensed by the Federal Communications Commission (FCC) and newspaper businesses with multiple locations to secure PPP loans.

### Second Draw Borrowers

Previous PPP recipients may apply for another loan of up to \$2 million, provided that they:

- Have 300 or fewer employees;
- Have used or will use the full amount of their first PPP loan; and
- Can demonstrate they suffered a 25% gross receipts decline in any 2020 quarter compared with the same quarter in 2019.



Certain businesses, however, are barred from accessing a second PPP loan. This includes businesses that:

- Have securities listed on a national securities exchange;
- Are ineligible under 13 CFR 120.110, unless explicitly permitted to receive a PPP loan under the SBA's guidance or related federal legislation;
- Are primarily engaged in political or lobbying activities;
- Have significant operations in the People's Republic of China or Hong Kong; or
- Receive a Shuttered Venue Operator Grant.

Any person required to submit a registration statement under Section 2 of the Foreign Agents Registration Act of 1938 is also barred from receiving a second PPP loan.

## Existing Borrowers Not Eligible for Second Draw

Businesses that are ineligible for a second draw PPP loan—other than those barred from participating as described above—may take advantage of the expanded permitted uses for PPP loans, which are also eligible for forgiveness. As described below, all PPP loan borrowers will be able to use PPP funds for certain covered operations expenditures, property damage costs, supplier costs, and covered worker protection expenditures, all of which will be eligible for loan forgiveness.

## Maximum Amounts of PPP Loans

Second draw borrowers are eligible to receive loans in an amount equal to the lesser of the amount of the borrower's average total monthly payment for payroll costs incurred or paid during either (1) the one-year period before the loan was made or (2) the calendar year 2019, multiplied by 2.5; or \$2,000,000.

PPP borrowers with NAICS codes starting with 72 (hotels and restaurants) can get up to 3.5 times their average monthly payroll costs, up to the \$2 million maximum.

For most first-time borrowers, the maximum amount of a loan is the lesser of the amount determined pursuant to the formula set forth above in the first bullet point, or \$10,000,000.

## Increase in Existing PPP Loan Amount

In addition to the amount received in its first PPP loan, a business may be able to receive an increase in funds. A borrower may increase the amount of its first PPP loan if (1) the borrower returned certain funds or (2) the borrower did not accept the maximum funds offered under its successful PPP loan application. These borrowers are eligible to receive the difference between such amounts and the maximum loan amounts previously approved by the SBA and PPP lenders.

## Payroll Expense Requirement

As with the existing program, in order to be eligible for full loan forgiveness under the new program, PPP borrowers will have to spend no less than 60% of the funds on payroll over a covered period of either eight or 24 weeks. Under a clarification to the rules, borrowers may elect a covered period, which commences on the loan origination date and ends on a date that falls between eight and 24 weeks after the date of the loan's origination. Borrowers may now choose their own covered period and calculate loan forgiveness amounts based on the covered period.



## Permissible Expense

As was the case under the original program, expenses eligible for loan forgiveness include payroll, rent, covered mortgage interest, and utilities. The new PPP program also makes the following forgivable:

- **Covered operations expenditures**, which include:
  - Payments for any business software or cloud computing service that facilitates business operations, payroll and other recordkeeping and accounting functions.
- **Covered property damage costs**, which include:
  - Payments in connection with property damage, vandalism or looting due to public disturbances that occurred in 2020 and that were not covered by insurance or other compensation.
- **Covered supplier costs**, which include:
  - Payments made to a supplier of goods under a contract in effect before February 15, 2020, for the supply of goods that are essential to the operations of the business.
- **Covered worker protection expenditures**, which include:
  - Any operating or capital expenditures incurred in connection with the COVID-19 guidance issued by the federal government from March 1, 2020 to December 31, 2020 (e.g., social-distancing guidelines). This may include items such as funds spent creating a drive-through window facility and installing a new air filtration system, as well as funds spent on health screenings and the purchase of personal protective equipment. This does not, however, include residential real estate or intangible property.

The above provisions are applicable to loans made before, on, or after December 27, 2020. Such expenses will be included on applications for loan forgiveness. Consequently, PPP borrowers may use funds delivered under a prior PPP loan but not yet spent to pay for the above-listed items.

For borrowers that have already had their PPP loans forgiven, the above-listed items are not forgivable. Essentially, borrowers may not retroactively file another loan forgiveness application based on the above-listed items.

In a situation where a borrower has completed a forgiveness application but the applicant has not been approved, it is unclear whether the borrower may re-file the loan forgiveness application to add the expenses described above.

## Tax Deductibility for PPP Expenses

In April, the IRS issued Notice 2020-32, which stated that no deduction would be allowed under the Internal Revenue Code for an expense that is otherwise deductible if the payment of the expense results in forgiveness of a PPP loan. The IRS' position was that since the income associated with the forgiveness is excluded from gross income for purposes of the Code under Section 1106 of the CARES Act, such expenses could not be deducted.

Then, in November, the IRS issued Revenue Ruling 2020-27, which stated that a taxpayer computing taxable income on the basis of a calendar year could not deduct eligible expenses in its 2020 tax year if, at the end of the 2020 tax year, the taxpayer had a reasonable expectation of reimbursement in the form of loan forgiveness at a future date on the basis of eligible expenses paid or incurred during the covered period.

The Act has effectively reversed the IRS' position. It specifies that "no deduction shall be denied, no tax attribute shall be reduced, and no basis increase shall be denied, by reason of the exclusion from gross income provided" by Section 1106 of the CARES Act. This provision applies to loans under both the original PPP and the new one.

## Eligible Entities in Bankruptcy Proceedings

The legislation amends the federal bankruptcy statutes to permit debtors or trustees to obtain a PPP loan. The applicable bankruptcy court must approve a PPP loan to any such debtor and requires any PPP funds to be given a super priority claim in the bankruptcy process.



## Other Terms

The new COVID-19 relief bill also:

- Creates a simplified forgiveness application process for loans of \$150,000 or less. A borrower will automatically receive forgiveness if it signs and submits to the lender a certification (to be prepared by the SBA that will not be more than one page in length) that includes a description of the number of employees the borrower was able to retain because of the loan, the estimated total amount of the loan spent on payroll costs, and the total loan amount. The SBA is directed to create the simplified application form within 24 days of the bill's enactment and may not require additional materials unless necessary to substantiate revenue loss requirements or satisfy relevant statutory or regulatory requirements.
- Repeals the requirement that PPP borrowers deduct the amount of any EIDL advance from their PPP forgiveness amount.
- Includes set-asides of \$25 billion to support first- and second-time PPP borrowers with 10 or fewer employees and first-time PPP borrowers that have recently been made eligible provided such borrowers comply with all of the program rules.

## Lenders

### Lender Held Harmless

A PPP lender may rely on all documentation and certifications submitted by a borrower and will not be subject to an enforcement action for any falsehoods in said documentation if the lender (1) acts in good faith relating to loan origination or forgiveness and (2) complies with all relevant federal, state, local, and other statutory and regulatory requirements.

### Agent Fees

Under the original program, disputes arose between PPP lenders and agents for PPP borrowers as to who would pay the agent's fees. Under the new legislation, a PPP lender will only be responsible for paying fees to an agent for services for which the lender directly contracts with the agent. This applies to the original PPP as well as the second draw program described above.

### Lender Fees

There are three tiers of fees payable to lenders for making the loans:

- For loans up to \$50,000, the lender fee is the lesser of 50% of the principal amount or \$2,500.
- For loans between \$50,000 and \$350,000, the lender fee is 5%.
- For loans \$350,000 and above, the lender fee is 3%.

### Interest Rate and Term

The interest rate under new program loans will be 1%. The term will be five years.

### Set Asides

The following set asides have been established for certain PPP lenders:

- \$15 billion for PPP loans (initial and second draw) issued by community financial institutions, including community development financial institutions (CDFIs) and minority depository intuitions (MDIs).



- \$15 billion for PPP loans (initial and second draw) issued by depository institutions with under \$10 billion in assets.