



April 2020

COVID-19: New SBA Loans for Small Businesses—Maybe a Great Deal

The COVID-19 pandemic has upended all aspects of life around the world, including the world of business here in the U.S.

If your business is struggling, you may be able to get some help from the federal Small Business Administration (SBA), which is authorized to provide loans to small businesses on an as-needed basis.¹

There are two types of relief you can apply for—read on.

Economic Injury Disaster Loans

Traditionally, low-interest SBA Economic Injury Disaster Loans (EIDLs) have been available to small businesses following a disaster declaration; these are authorized by Section 7(a) of the Small Business Act.²

EIDLs are commonly granted on a local level following a natural disaster (such as a hurricane or a tornado). But right now they are authorized for small businesses in all U.S. states and territories due to the COVID-19 pandemic.

Currently, each disaster loan provides up to \$2 million to pay fixed debts, payroll, accounts payable, and other bills. The interest rate is fixed at 3.75 percent for small businesses and 2.75 percent for non-profits. EIDLs can be repaid over a period of up to 30 years.³

Additionally, due to COVID-19, the SBA is providing advances of up to \$10,000 on EIDLs for businesses experiencing a temporary loss of revenue. Funds are available within three days after applying, and the loan advance does not have to be repaid.⁴

Small business owners can apply for an EIDL and advance here:
<https://covid19relief.sba.gov/#/>

New Paycheck Protection Program

The Paycheck Protection Program (PPP) is an expansion of the existing 7(a) loan program, authorized by the recently passed Coronavirus Aid, Relief, and Economic Security Act (CARES Act).⁵

Who's Eligible?

You are covered if your business was in operation as of February 15, 2020, and you had either (a) employees for whom you paid salaries and payroll taxes or (b) 1099-MISC independent contractors.⁶

Small businesses that employ 500 or fewer employees, including sole proprietors, independent contractors, certain non-profits, veterans' organizations, tribal businesses, and self-employed workers, are all eligible for PPP relief.⁷

“Self-employed” workers are who you would think they are, the sole proprietors who file Schedule C with their Form 1040. IRC Section 1402 identifies them as those who regularly carry on a trade or business within the meaning of tax code Section 1402.⁸

Update April 4, 2020: SBA Guidance Conflicts with CARES Act (see sidebar below)

Update April 8, 2020: What If I Work by Myself with No Employees (see sidebar 2 below)?

How Much Aid Is Available?

Small businesses can borrow 250 percent of their average monthly payroll expenses during the one-year period before the loan is taken, up to \$10 million.⁹

For example, if your monthly payroll average is \$10,000, you can borrow \$25,000 ($\$10,000 \times 250$ percent). At \$1 million, you can borrow \$2.5 million.

The law defines “payroll costs” very broadly as

- employee salaries, wages, commissions, or “similar compensation,” up to a per-worker ceiling of \$100,000 per year;

cash tips or the equivalent;

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- payment for vacations and parental, family, medical, or sick leave;
- allowance for dismissal or separation;
- payment for group health benefits, including insurance premiums;
- payment of any retirement benefit; or
- state or local tax assessed on employee compensation.¹⁰

What's specifically *not* included in payroll costs:

- Annual compensation over \$100,000 to any individual employee
- Compensation for employees who live outside the U.S.
- Sick leave or family leave wages for which a credit is already provided by the Families First Coronavirus Response Act (P.L. 116-127)¹¹

How Much of the Loan Is Forgiven?

Principal amounts used for payroll, mortgage interest, rent, and utility payments during an eight-week period (starting with the loan origination date) will be forgiven.¹²

If the full principal is forgiven, you are not liable for the interest accrued over that eight-week period—and, as an added bonus, the canceled amounts are not considered taxable income.¹³

Warning: Payroll Cuts Affect Loan Forgiveness

Because the whole point of the PPP is to help keep workers employed at their current level of pay, the loan forgiveness amount decreases if you lay folks off or reduce their wages.¹⁴

1. If you keep all your workers at their current rates of pay, you are eligible for 100 percent loan forgiveness.
2. If you reduce your workforce, your loan forgiveness will be reduced by the percentage decrease in employees.

Example. Last year, you had 10 workers. This year, you have eight. Your loan forgiveness will be reduced by 20 percent.

You are allowed to compare your average number of full-time equivalent employees employed during the covered period (February 15, 2020, to June 30, 2020) to the number employed during your choice of¹⁵

- February 15, 2019, to June 30, 2019, or

January 1, 2020, to February 29, 2020.

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3. If you reduce, by more than 25 percent (as compared to the most recent full quarter before the covered period) the pay of a worker making less than \$100,000 annually, your loan forgiveness decreases by the amount in excess of 25 percent.¹⁶

Example. Last quarter, Jim was earning \$75,000 on an annual basis. You still have Jim on the payroll but have reduced his salary to \$54,750 annually. Jim's pay has decreased by 27 percent, so the amount of your PPP loan forgiven is reduced by the excess 2 percent.

The good news: If you have already laid workers off or made pay cuts, it's not too late to set things right. If you hire back laid-off workers by June 30, 2020, or rescind pay cuts by that date, you remain eligible for full loan forgiveness.¹⁷

When Are Payments Due?

Any non-forgiven amounts are subject to the terms negotiated by you and the lender, but the maximum terms of the loan are capped at 10 years and 4 percent interest.

Also, payments are deferred for at least six months and up to one year from the loan origination date.¹⁸

What If You Already Applied for an EIDL for Coronavirus-Related Reasons?

No problem—if you took out an EIDL on or after January 30, 2020, you can refinance the EIDL into the PPP for loan forgiveness purposes, but you can't double-dip and use the loans for the same purposes.

Any remaining EIDL funds used for reasons other than the stated reasons above are a regular (albeit low-interest) loan that needs to be repaid.

How to Apply for a PPP

Unlike EIDLs, which run directly through the SBA, PPP loans go through approved third-party lenders. Talk to your bank or your local SBA office (given the current demands on the SBA, your bank may be a better place to start).

There's no fee to apply, and your burden for demonstrating need is low. In addition to the appropriate documentation regarding your finances, you need only make a good-faith showing that¹⁹

- the loan is necessary to support your ongoing business operations in the current economic climate;
- the funds will be used to retain workers and maintain payroll or make mortgage payments, lease payments, and utility payments; and

you do not have a duplicate loan already pending or completed.

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If You're Going to Apply, Do It Now

The law allocates \$349 billion for PPP relief²⁰—a huge amount, but one that will presumably be in very high demand given the devastating effects of the COVID-19 pandemic.

There's no guarantee that more funding will be forthcoming, so act now to claim your share if you are eligible. It may be a while before the processes to grant these loans are actually up and running, but get things rolling at your end ASAP.

If you are in dire straits right now, you may additionally want to go ahead and apply for an EIDL loan and advance, as the machinery is already set up for those.

Sidebar—SBA Guidance Conflicts with CARES Act

The law clearly states that the payroll includes independent contractors. Check the citations.

The SBA in its new interim final rule interpreting the law said this:²¹

- Amounts paid to independent contractors do not count for the PPP payroll because they can apply for their own PPP loans.²²

- Similarly, independent contractors don't count for PPP loan forgiveness purposes.²³

In ordinary times, the law rules over guidance.

For this SBA loan, you go to the bank which likely is going to ignore the law and follow the SBA guidance (after all this is an SBA loan).

Does the SBA Guidance Go Against the Intent of the Stimulus or Prevent Double Dipping?

We believe the SBA guidance goes against not only the law but also the Congressional intent to keep small businesses alive so they can participate and accelerate the recovery.

Example. John operates a proprietorship that pays 15 people on a 1099. If the SBA is right and the law is wrong, then John gets no money to continue paying the 15 people. If he pays them, he goes bankrupt.

Sure, the 15 people can obtain loans on their own. They may even have employees of their own.

But we think the original intent of the law was to keep John in business so he could help generate a speedy recovery from this mess. If John is out of business, so are his 15 workers.

You can comment to SBA about this "interim final guidance" and perhaps influence a change.²⁴

Sidebar 2: What If I Work by Myself with No Employees?

Good news. If you file a Schedule C with your Form 1040 and have no employees, you qualify for the PPP loan and forgiveness program. Freelancers, gig workers, real estate sales professionals, carpenters, hair dressers, retailers, and others who operate one-person Schedule C businesses qualify.

Don't procrastinate. You can apply for your PPP loan with your bank or other SBA lender beginning Friday, April 10, 2020. Do it. When the PPP money runs out, the PPP loan program dies (temporarily). Lawmaker will resurrect it with more money with a round two.

Example. Harriet works for herself and has no employees. She had 2019 Schedule C net income of \$130,000. The PPP caps her Schedule C income at \$100,000. On a monthly basis, that's \$8,333. Harriett can qualify for an SBA loan of 2.5 times that amount, or \$20,833.

Under the rules, Harriet gets to keep at least 8/52 (\$15,385) of this money (not pay it back to the lender). And the best part, the money Harriet gets to keep is tax-free to Harriett.²⁵

[Client Letter on This Article for Use by Tax Pros. Click Here.](#)

1 15 USC Section 636(a).

2 Ibid.

- 3 <https://www.sba.gov/disaster-assistance/coronavirus-covid-19>.
 - 4 <https://www.sba.gov/page/coronavirus-covid-19-small-business-guidance-loan-resources#section-header-2>.
 - 5 CARES Act, Section 1102.
 - 6 Ibid., Section 1102(a)(2).
 - 7 Ibid.
 - 8 Ibid; FFCRA, Section 7002(b).
 - 9 CARES Act, Section 1102(a)(2).
 - 10 Ibid.
 - 11 Ibid.
 - 12 Ibid., Section 1106(b).
 - 13 Ibid., Section 1106(h)(2)(i).
 - 14 Ibid., Section 1106(d)(2).
 - 15 Ibid., Section 1106(d)(2)(A)(ii)(I).
 - 16 Ibid., Section 1106(d)(3)(A).
 - 17 Ibid., Section 1106(d)(5)(B).
 - 18 Ibid., Section 1102(a)(2).
 - 19 Ibid.
 - 20 Ibid., Section 1102(b)(1).
 - 21 Docket No. SBA-2020-0015, 13 CFR Part 120, RIN 3245-AH34.
 - 22 Ibid, Section III(2)(h).
 - 23 Ibid, Section III(2)(p).
 - 24 Ibid, p. 2.
 - 25 Ibid., Section 1106(h)(2)(i).
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