Paycheck Protection Program Legal Update for Tax-Exempt Organizations

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CURRENT STATUS

On April 24, 2020, President Trump signed the Paycheck Protection Program and Healthcare Enhancement Act (PPP Enhancement Act), adding an additional $310 billion to the previously exhausted $349 billion in funds allotted for small business entities (including tax-exempt organizations organized under Section 501(c)(3) and Section 501(c)(19) of the Internal Revenue Code) and additional funds to various relief programs under the Coronavirus Aid, Relief, and Economic Security (CARES) Act. The original CARES Act created the Paycheck Protection Program through a modification and expansion the Small Business Administration (SBA) 7(a) loan guarantee program.

The passage of the Paycheck Protection Program and Health Care Enhancement Act means that more funds should be available, at least for those who have already applied to the PPP and are currently waiting in queue. As of June 2, 2020, at least $120 billion remained in PPP funds.

On June 5, 2020 the President signed a further amendment to the PPP, the Paycheck Protection Program Flexibility Act (PPPFA) of 2020, which brings additional changes discussed in additional detail below.

QUALIFICATIONS AND REQUIREMENTS SUMMARY

To be eligible for a PPP loan, a prospective tax-exempt applicant must notably, among other criteria:

i. be a 501(c)(3) or 501(c)(19) tax-exempt organization that was in operation on February 15, 2020. Faith-based organizations are eligible regardless of whether they provide secular social services.
ii. together with its affiliates, have 500 or fewer employees (including full time and part-time employees) or have less than the higher size standard of number of employees set by the Small Business Administration for the industry in which it operates.

1. Volunteers who do not receive compensation are not considered employees, but student workers do count as employees.
2. Normally an organization must count both its own employees and the employees of its affiliates in determining whether it qualifies for PPP funds.However, even if an organization is otherwise disqualified from receiving PPP funds because it is affiliated with other organizations that, together, have more than the maximum permissible number of employees, it can qualify for an exception from the affiliation rules if the affiliation is based on a religious teaching or belief or is otherwise a part of the exercise of religion.

Applicants should further pay special attention to the certifications required of them that “[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant” and that the funds will be used for authorized purposes. The Treasury Department has stated it intends to audit certain borrowers with an eye toward these certifications, among others, including each borrower who received PPP loans in amounts over $2 million. Recipients of PPP loans under $2 million or less, however, are presumed to have completed the necessity certification in good faith.

CURRENT LOAN DETAILS AND FORGIVENESS GUIDELINES

An eligible applicant may apply for a loan up to the lesser of (i) $10 million and (ii) 2.5 times the organization's average monthly payroll costs for its U.S. employees during either calendar year 2019 or the one-year period prior to the loan date (though an applicant that was not in business on or prior to June 30, 2019, may instead use its average monthly payroll costs for the period January 1, 2020 through February 29, 2020). The interest rate on PPP loans is one percent and there is no processing fee to the borrower nor any pre-payment penalty. Loans made before June 5, 2020 were available for fixed two-year terms, but following the passage of the PPPFA may be extended to a term of up to five years (and may have a term of up to ten years) upon mutual agreement of the Borrower and Lender. Loans made on or after June 5, 2020 will all have a fixed five-year term. The PPP will be available through at least June 30, 2020, subject to available program funds.

A loan would be eligible for forgiveness by application to the lender to the extent it is used on certain eligible costs during a set window following the funding date of the loan. Under the original Cares Act, that spending window lasted eight weeks from funding, but the PPPFA extended the end date of the window to the earlier of 24 weeks from funding or December 31, 2020.If the PPP loan was made before June 5, 2020 borrowers can, however, opt back into the eight week window if they so choose.

If a borrower submits to its lender a loan forgiveness application within 10 months after the end of its loan forgiveness covered period, the borrower will not have to make any payments on principal or interest on its loan before the date on which SBA remits the loan forgiveness amount on its loan to its lender (or notifies its lender that no loan forgiveness is allowed). If no loan forgiveness application is submitted, the borrower must begin making payments 10 months after the expiration of the loan forgiveness covered period. This is in contrast to the pre-PPPFA rules which only allowed for six months of deferral.

A key requirement of PPP loans is that a minimum amount of loan proceeds must be used for specified payroll costs, with the remainder used for specified nonpayroll costs. This minimum payroll costs requirement was initially set at 75% but was reduced to 60% by the PPPFA. While borrowers are required to achieve this minimum spending threshold over the life of the loan, it is not a requirement that they spend the full 60% on payroll costs during their forgiveness window. However, the 60% requirement will be interpreted as a proportional limit on nonpayroll costs as a share of the borrower's loan forgiveness amount. For example, if a borrower receives a $100,000 PPP loan, and during the covered period the borrower spends $54,000 (or 54 percent) of its loan on payroll costs, then because the borrower used less than 60 percent of its loan on payroll costs, the maximum amount of loan forgiveness the borrower may receive is $90,000 (with $54,000 in payroll costs constituting 60 percent of the forgiveness amount and $36,000 in nonpayroll costs constituting 40 percent of the forgiveness amount). In addition, following the covered period, the Borrower will still need to spend an additional $6,000 of the loan on payroll costs on a non-forgivable basis.

Permitted non-payroll costs are defined as mortgage interest (but not principal), rent (of either real estate or personal property), and utilities, in each case for properties owned or leased, or service which was in effect on or prior to February 15, 2020. Loan forgiveness is subject to reduction, however, for certain changes in a borrower's employee headcount or any employee's compensation, in each case as compared against a certain reference period. However, certain safe harbors and exceptions to this reduction are available, which the PPPFA elaborated upon in stating that loan forgiveness amount is permitted to be determined without regard to the proportional reduction in the number of full-time employees if such employer is able to document an inability to (a) re-hire an individual who was an employee prior to February 15, 2020, (b) to hire similarly qualified employees on or before December 31, 2020, or (c) return to the same level of business activity as prior to February 15, 2020, due to compliance with certain requirements established or guidance issued by the Secretary of HHS, the Director of the CDC, or the OSHA that pertain to the maintenance of standards for sanitation, social distancing or any other worker or customer safety requirement related to COVID–19, in each case to the extent established or issued between March 1, 2010 and December 31, 2020.

FURTHER UPDATES, CHANGES, AND RESOURCES

The second batch of funds came with a notable change that may assist certain eligible tax-exempt organizations in accessing funds: a requirement that certain smaller lenders receive a set amount of funds. Under the PPP Enhancement Act, at least $30 billion must go to community development financial institutions, banks and credit unions with less than $10 billion in assets. Another $30 billion at least must go to banks and credit unions with assets between $10 billion and $50 billion. As many smaller financial institutions may be community-focused, the change could assist applicants of loans from these smaller institutions, which may include certain eligible tax-exempt organizations, by opening up access to funding that had been a challenge to access in the first round of funding under the CARES Act.

The SBA has also updated its guidance on the implementation of the PPP that, while not directly applicable to nonprofits, could result in more PPP funds being available as other applicants reassess their eligibility. Specifically, the updated guidance:

- Stresses the importance of the required necessity certification through several program FAQs (notably numbers 31, 37 and 46) which seem to have both slowed the pace of PPP applications and, in particular, discouraged certain larger potential applicants from applying for PPP loans. This, in turn, means more funding may be available for other applicants who have fewer financial resources, including tax-exempt entities.
- Introduces measures such as (1) pacing the numbers of loans processed electronically, (2) instituting a maximum dollar amount that any lending institution will be able to originate, (3) implementing operational standards to ensure that lenders access PPP resources based on their asset size, and (4) ensuring that the system continues to work on a first-come, first-served basis to ensure equitable access and system integrity.

A list of eligible lenders can be found here and more information on the application requirements and loan details may be found in this Goodwin Alert and on the SBA website.

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