

Insights

SBA Issues Additional Interim Guidance on Paycheck Protection Program Clarifying Treatment of Self-Employment and Partner Income

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On April 14, 2020, the U.S. Small Business Administration (the "SBA") issued a second interim final rule (the "Second PPP Interim Final Rule") related to the Paycheck Protection program (the "PPP") offered under the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act"). This latest guidance provides eagerly awaited information for individuals with self-employment income, including partners in a partnership or members in an LLC taxed as a partnership, and supplements initial guidance issued by the SBA in the initial interim final rule issued on April 2nd (the "First PPP Interim Final Rule") (covered by our previous alert found [here](#)). The Second PPP Interim Final Rule also addresses eligibility issues for certain businesses and requirements for certain pledges of PPP loans. While its provisions are effective immediately, public comments are solicited on all aspects of the Second PPP Interim Final Rule.

Self-Employment Income and Treatment of Partnerships Under the PPP Loans

The Second PPP Interim Final Rule clears up a few lingering issues that were not resolved when the April 2nd guidance contained in the First PPP Interim Final Rule was released. The SBA clarified that individuals with self-employment income (reported on Form 1040, Schedule C) are eligible for a PPP loan if they were in operation on February 15, 2020, have a principal place of residence in the U.S., and file (or will file) a Form 1040 Schedule C for 2019.

Perhaps most notably, the guidance expressly provides that partners in a partnership (or members in an LLC taxed as a partnership) should NOT submit a separate PPP loan application for themselves as self-employed individuals. Instead, the self-employment income of such individuals, up to the \$100,000 annualized income cap, should be reported as a "payroll cost" on a PPP loan application filed by the partnership.

In addition to clarifying the threshold question of whether partner self-employment income should be included as a payroll cost of the partnership, the SBA provided instructions for calculating the maximum borrowing amount of a partnership under the PPP loan rules.

- For partnerships with employees, the maximum PPP loan amount is calculated as the sum of:
 - a) Partner net profit income from 2019 Form 1040, Schedule C, Line 31 (if not yet filed, compute the value using the form and instructions) up to \$100,000 per partner; plus
 - b) 2019 gross wages and tips paid to partnership employees using 2019 Form 941 Taxable Medicare wages and tips (line 5c-column 1) from each quarter plus any pre-tax employee contributions for health insurance or other fringe benefits excluded from Taxable Medicare wages and tips, up to \$100,000 per employee; plus
 - c) Employer 2019 health insurance contributions, retirement contributions, and state and local taxes assessed on employee compensation (i.e., SUTA),

- Next, the sum of a, b, and c above is divided by 12, to calculate average monthly amount.
- Finally, this average monthly amount is multiplied by 2.5.

Note: Partnerships with no employees would simply skip step "b" above, in calculating the maximum loan amount. In addition, the outstanding amount of any SBA Economic Injury Disaster Loan ("EIDL") made between January 31, 2020 and April 3, 2020 that the applicant wishes to refinance may be added to the amount calculated as well (whether or not the applicant has employees). If the EIDL was used for payroll costs, it must be refinanced by the PPP loan.

Use of PPP Loan Proceeds By Individuals with Self-Employment Income

The Second PPP Interim Final Rule sets forth a list of approved uses of PPP loan proceeds for individuals with self-employment income filing a 2019 Form 1040, Schedule C (including partners or LLC members), including:

- "Owner compensation replacement" (calculated as described above);
- Employee payroll costs (as defined in the First PPP Interim Final Rule);
- Mortgage interest (but not principal) on any business mortgage obligation on real or personal property, business rent payments, and business utility payments, provided the taxpayer was entitled to claim a deduction for such expenses on their 2019 Form 1040, Schedule C;
- Interest payments on any other debt obligations incurred before February 15, 2020 (but note: such amounts are NOT eligible for PPP loan forgiveness); and
- Refinancing an EIDL made between January 31, 2020 through April 3, 2020

Loan Amount Eligible for Forgiveness

While the amount of the PPP loan forgiven can be the full principal amount plus accrued interest, the actual amount forgiven will depend on the total proceeds spent over the covered period on:

- Payroll costs up to \$100,000 of annualized pay per employee (for eight weeks, a maximum of \$15,385 per individual) and covered benefits for employees (but not owners), including health care, retirement, and state and local taxes on employee payroll (e.g., unemployment insurance);
- Owner compensation replacement (calculated based on 2019 net profit, as described above *(limited to eight weeks' worth of 2019 net profit, excluding any qualified leave supporting a credit under the Families First Coronavirus Response Act)* (covered by our previous alert found [here](#));
- Payments of interest on mortgage obligations on real or personal property incurred before February 15, 2020 (to extent deductible for federal tax purposes);
- Rent payment on lease agreement in force before February 15, 2020 (to extent deductible for federal tax purposes);
- Utility payments under agreement dated before February 15, 2020 (to extent deductible for federal tax purposes);

Note: The limitation of owner net profit to 8 weeks' worth of 2019 net profit is explained by the overarching focus of the CARES Act of keeping workers paid, rather than permitting windfalls.

Other Guidance

In addition to the issues summarized above, the Second PPP Interim Final Rule provides the following:

- Documentation must be submitted to the PPP lender supporting employee wages (Form 941), business rent, business mortgage interest payments, and owner self-employed income (2019 Form 1040, Schedule C).
- Eligible businesses owned by directors or shareholders of a PPP lender may apply for a PPP loan through such lender, provided the director or shareholder is not also an officer or key employee of the lender.
- Business that receive revenue from legal gaming are eligible for a PPP loan, subject to certain qualifications.
- The requirements for loan pledges under 13 CFR 120.434 ("SBA Regulations") do not apply to PPP loans pledged for borrowings from a Federal Reserve Bank or advances by a Federal Home Loan Bank. This would mean, for example, that the SBA would not have to approve loan documents or require a multi-party agreement among the SBA, the lender and others.

If you have any further questions, comments or concerns, please feel free to contact **Kendall A. Schnurpel**, **Robert A. Greising**, or a member of our **Business, Acquisitions & Securities team**.