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# Hughes Hubbard & Reed

## Paycheck Protection Program – SBA Guidance

### Client Advisories

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The Small Business Administration (the “SBA”), in consultation with the Department of the Treasury, has been providing, on an ongoing basis, additional guidance concerning the implementation of the Paycheck Protection Program (“PPP”) under the Coronavirus Aid, Relief, and Economic Security Act (the “CARES Act”).

The following is a summary of guidance provided with respect to the SBA’s review of borrowers’ certification concerning the economic necessity of their PPP loan application, as well as clarifications regarding (i) borrower eligibility, and (ii) the scope of Payroll Costs under the PPP. Note this recent guidance also provided clarifications with respect to other matters that affect borrowers and lenders.

For Hughes Hubbard’s detailed review of the PPP, please refer to this [client advisory](#).

### **Review of PPP Loans**

PPP borrowers are required to certify in good faith that the current economic uncertainty makes their loan request necessary to support their ongoing operations. Such good-faith certification must take into account the borrower’s access to other sources of liquidity that would be sufficient to support their ongoing operations in a manner that is not significantly detrimental to the borrower.

To ensure that PPP loans are limited to eligible borrowers in need, the SBA announced that it will review the certifications of necessity made by certain PPP borrowers, as follows:

### **Safe Harbors**

- Any borrower that, together with its affiliates, received PPP loans with an original principal amount of less than \$2 million will be deemed to have made the certification of concerning the loan’s necessity in good faith.

- In addition, any borrower that received a PPP loan in excess of \$2 million but repays its loan in full by May 18, 2020, will be deemed to have made the certification of necessity in good faith.

### **Loans in excess of \$2 million**

- The SBA will review all loans in excess of \$2 million, as well as other PPP loans as appropriate (other than loans protected by the safe harbors), following the lender's submission of the borrower's loan forgiveness application.
- Borrowers with loans greater than \$2 million that do not satisfy the safe harbors may still have an adequate basis for making the required good-faith certification, based on their individual circumstances.
  - The SBA provided, as an example, that a public company with substantial market value and access to capital markets is unlikely to be found to have had an adequate basis for making the certification of necessity.
- If the SBA determines in the course of its review that a borrower lacked an adequate basis for the certification of necessity, the SBA will seek repayment of the outstanding PPP loan balance and will inform the lender that the borrower is not eligible for loan forgiveness.
- If the borrower repays the loan after receiving notification from the SBA, the SBA will not pursue administrative enforcement or referrals to other agencies based on its determination with respect to the certification of necessity.

### **Eligibility Standards - Borrower's Size**

The SBA clarified that a business may be eligible for a PPP loan if it meets any of the following size tests:

- it has less than 500 employees or meets the SBA employee-based or revenue-based size standard corresponding to its primary industry;
- it satisfies the existing statutory definition of a "small business concern"; or
- it met both SBA "alternative size standard" tests as of March 27, 2020:
  - its maximum tangible net worth is not more than \$15 million; and
  - the average net income after Federal income taxes (excluding any carry-over losses) of the business for the two full fiscal years before the date of the application is not more than \$5 million.

### **Affiliation**

The SBA confirmed that borrowers are required to apply SBA's affiliation rules under 13 C.F.R. 121.301(f), as set forth in the [SBA's Interim Final Rule on Affiliation](#). A borrower must certify on the Borrower application form that it is eligible to receive a PPP loan, and that certification means that borrower:

- is a "small business concern"; or
- meets the applicable SBA employee-based or revenue-based size standard; or
- meets the tests in SBA's "alternative size standard", after applying the affiliation rules, if applicable.
  - Note that SBA's existing affiliation exclusions apply to the PPP (i.e. exclusions under 13 C.F.R. 121.103(b)(2)).

The guidance indicates that the affiliation rule based on ownership continues to apply and that may affect businesses backed by venture capital and private equity funds (13 C.F.R. 121.301(f)(1)). The SBA will deem a minority shareholder in a business to control the business if the shareholder has the right to prevent a quorum or otherwise block action by the board of directors or shareholders. If a minority shareholder irrevocably gives up

on those rights, then it will no longer be an affiliate of the business (assuming no other relationship triggers the affiliation rules).

## **Scope of Payroll Costs**

The SBA clarified that the following personnel-related expenses may be included in “Payroll Costs” for purposes of the PPP:

- Cost of employee vacations, and parental, family, medical, and sick leave.
- Non-cash benefits such as employer contributions to defined-benefit or defined-contribution retirement plans, even for employees earning more the \$100,000.

Amounts paid to an independent contractor or sole proprietor, however, are excluded from Payroll Costs, given that they may be eligible to apply for a loan directly.

## **Payroll Provider Documentation**

The SBA clarified that payroll documentation provided by a payroll provider or by a Professional Employer Organization that indicates the amount of wages and payroll taxes reported to the IRS by the payroll provider for the borrower’s employees will be considered acceptable PPP loan payroll documentation.

- Relevant information from a Schedule R (Form 941), Allocation Schedule for Aggregate Form 941 Filers, attached to the payroll provider’s Form 941, Employer’s Quarterly Federal Tax Return, should be used if available;
- Otherwise, the borrower should obtain a statement from the payroll provider documenting the amount of wages and payroll taxes.

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