

New Guidance Issued for Self-Employed Applicants for PPP Loans

The Small Business Administration (“SBA”) and U.S. Department of the Treasury (“Treasury”) have issued new [guidance](#) for self-employed persons who seek to apply for forgivable loans under the Paycheck Protection Program (“PPP”).

If You Have Self-Employment Income from an Entity Taxed as a Partnership – Apply as a Partnership

The guidance states that persons with self-employment income from an entity that is taxed as a partnership must apply at the partnership level. A partner active in the business may report self-employment income as “payroll costs” on the partnership’s application but may not apply separately as a self-employed person.

The SBA and Treasury state that limiting a partnership or LLC taxed as a partnership to a single application is necessary to ensure that as many eligible borrowers as possible are able to participate and to avoid additional administrative issues.

If You Have No Self-Employment Income on Your 2019 Tax Return – You Cannot Apply Until Later

Until there is further guidance, only self-employed persons who showed self-employment income on a Schedule C to their *2019 tax return* will be eligible for PPP loans.

The 2019 return does not need to be filed with the IRS at the time of the application (given that deadlines were automatically extended to July 15) but it needs to be completed and provided to the lender.

Those persons who were in operation as a self-employed enterprise on February 15, 2020 but were not in operation in 2019 will be eligible but will need a different means to verify self-employment income. The SBA and Treasury state that they will “issue additional guidance” to address that issue.

Your “Payroll Costs” if You Are Self-Employed -- Based on Schedule C “Net Profit” (Line 31)

Solo Enterprise. If your enterprise is completely solo – or if you only use independent contractors and have no employees – then your “payroll costs” for purposes of your PPP loan is your “Net Profit (or Loss)” reported on Line 31 of Schedule C of your 2019 tax return.

If the number is negative (meaning “Net Loss”), then you are not eligible for apply for any amount of PPP loan as a solo enterprise.

If the number is positive (meaning “Net Profit”), then that number – divided by twelve – will be treated as your average monthly “payroll costs.” Even though your solo enterprise will not actually have any “payroll,” the statutory term that will apply is “payroll costs.”

As with “payroll costs” generally, the amount is capped at \$100,000 (annualized) per person. So if Line 31 is greater than \$100,000, it will be reduced to \$100,000.

Despite language in the statute, the guidance indicates that self-employed persons will not be permitted to add back costs for health insurance and retirement contributions. Only amounts reported on Line 31 will count as “payroll costs” for the self-employed person.

Employees. If you are self-employed but have employees, then you may add the payroll costs for those employees to the Line 31 number. Again, any salary per person is capped at \$100,000 (annualized). With respect to employees, however, you may add health insurance costs and retirement contributions, which can bring a per-person total over \$100,000. You may also include state and local (but not federal) taxes.

Those payroll costs may be added to the Line 31 Net Profit amount. If you have employees, then you will be eligible even if you report a “Net Loss” on Line 31 but *you cannot subtract* the negative number. A “Net Loss” on Line 31 will be counted as “zero.”

Maximum Loan Amount. Once you calculate your average monthly “payroll costs” (which will include your “Net Profit” as if it were “payroll”), you multiply that amount by 2.5 to determine your maximum loan amount.

How You Can Use Loan Proceeds – Includes “Replacement of Owner Compensation”

The self-employed person may use the loan proceeds to replace eight weeks of “Net Profit” based on the 2019 Schedule C figure.

The loan can also be used to pay employee payroll costs, if any, plus:

- business-related rent;
- utilities used for the business (electric, telephone, internet and gas costs for a business vehicle);
- interest on business-related debt secured by a mortgage or security interest (including vehicle loan interest for a business vehicle); and
- refinancing a disaster loan received prior to April 3, 2020 (of which there will be few given the delays related to the disaster loan program).

The costs for expenses other than payroll must be expenses that were reported as expenses on Schedule C of your 2019 tax return. The amounts do not need to correspond (assuming you can verify your spending during the eight-week period), but if you did not report utilities as an expense during 2019 then you cannot use PPP loan proceeds on utilities.

For the loan to be forgivable, no less than 75 percent of the proceeds must be used for “payroll costs” – which includes owner compensation replacement based on eight weeks’ worth of 2019 “Net Profit” (8/52 of the Line 31 amount). The remaining 25 percent can be used for the other purposes listed above, although certain interest on business debt will not be forgivable.

For self-employed persons with no employees, however, the SBA and Treasury have imposed a “cap” as well. The forgivable portion of the loan used for “replacement of owner compensation” is limited to eight weeks of Net Profit.

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If your business has few expenses of the type listed (rent, utilities, interest), then you may end up with a non-forgivable balance to repay, since approximately 10 weeks of Net Profit can be borrowed but only eight weeks will be forgivable.

Amounts recouped via tax credits for paid sick leave or emergency family leave under the Families First Coronavirus Response Act cannot also be the basis of a forgivable PPP loan.

It is not clear from the guidance how the self-employed person is to account for the “owners compensation replacement” funds, but it would be advisable to place the funds in a separate account so you can demonstrate when necessary that the funds were used in accordance with the guidance.

If you need additional assistance with your PPP loan application or forgiveness calculation, Vandennack Weaver attorneys can help at 402-504-1300 or www.vwattys.com.