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Community Association Loan Eligibility: Paycheck Protection Program (PPP) and Economic Injury Disaster Loans (EIDL) under the Coronavirus Aid, Relief, and Economic Security (CARES Act)

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The Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act") was signed into law on March 27, 2020, providing emergency assistance to businesses, families and individuals impacted by the COVID-19 pandemic. The CARES Act provides significant relief for small businesses by providing $350 billion in Small Business Administration ("SBA") loan funding, subsidies and guaranties, and an additional $10 billion for the existing Economic Injury Disaster Loan ("EIDL") program. But where homeowner associations are concerned, the big question is: **Are homeowner associations considered businesses?**

Paycheck Protection Program

One of the benefits provided to businesses under the CARES Act is the Paycheck Protection Program ("PPP"). This program allows certain businesses to apply for a loan of up to 2.5 times the business's average total monthly payments for payroll costs during the one-year period before the PPP Loan is made.

A business's payroll costs eligible for a PPP loan may include the following:

- Payroll costs[1] (including compensation, vacation and leave payments, allowance for dismissal or separation, cash tips, healthcare benefits, retirement benefits, state or local taxes based on compensation, and similar items)
- Employee salaries, commissions, or similar compensation
- Payments of interest on any mortgage obligation (specifically excluding any principal and prepayments)
- Rental payments
- Utility costs
- Interest on any other debt obligations (incurred prior to covered period)

Subject to the caveats discussed below, if you believe your association will need funds to cover any of the above listed costs, your association should apply for a PPP loan as soon as possible.

In the few days since the CARES Act was passed, there has been much debate within the legal and banking communities about homeowner associations' eligibility for PPP loans, and the criteria remain subject to interpretation by participating lending institutions. The issues hinge on the definition of businesses eligible for PPP loans in the CARES Act and under standard Small Business Administration ("SBA") lending criteria, as well as the required certification that must be made by a representative of the association.

The funds allocated to PPP loans under the CARES Act are to be loaned on a "first-come, first-served" basis, so it is imperative that loan applications be made as soon as possible, even if there is some uncertainty about an association's eligibility. PPP Loans are being made available through existing SBA-certified lenders, as well as additional lenders that the SBA determines have the necessary qualifications. The period in which PPP Loans may be requested runs from February 15, 2020, through June 30, 2020. PPP Loans will be subject to forgiveness under certain circumstances.

In determining eligibility for a PPP Loan, a lender will consider whether the applicant (i) was in operation on February 15, 2020, and (ii) whether the applicant had employees for whom the applicant paid salaries and payroll taxes or paid independent contractors as reported on a 1099. Note, however, that pursuant to guidance issued on April 2, 2020, independent contractors do not count as employees for purposes of calculating loan amounts or for loan forgiveness. Additionally, an association will be ineligible for a PPP Loan if it has ever obtained a guaranteed loan from the SBA or any other Federal agency that is currently delinquent or has defaulted within the last seven years and caused a loss to the government.

Applications for a PPP Loan should be made through a participating lending institution. Applicants must submit SBA Form 2483 (Paycheck Protection Program Application Form) and such documentation as necessary to establish eligibility, such as payroll processor records or payroll tax filings. Borrowers without such documentation must provide other supporting documents to demonstrate the qualifying payroll amount. Interested borrowers should also have readily available their most recent Federal Income Tax Returns, financial statements and similar relevant materials.

In addition to the above-listed documentation, in order to obtain a PPP Loan, an applicant must make a good faith certification (i) that current economic conditions make the loan necessary to support ongoing obligations, (ii) acknowledging that funds will be used to retain workers and maintain payroll or to make mortgage, lease or utility payments, and (iii) that the applicant does not have an existing application pending with the SBA for (or has not received) a loan for the same purpose. **The certification should be approved by the Board of Directors of your association and signed by an officer or Board member. Your association should consult with legal counsel for purposes of preparing the required certification and necessary approvals.**

The amount of an approved PPP Loan shall be in an amount that is calculated by multiplying the average total monthly payments for payroll costs during the one-year period before the PPP Loan is made by 2.5 (although a PPP Loan shall be in the maximum amount of $10,000,000). PPP Loans will have a two-year term, and interest rates are set at 1.0%. Borrowers will not have to make any payments for six months following the date of the loan, but interest will continue to accrue. In addition to this low interest rate and deferred repayment period, to incentivize borrowers obtaining PPP Loans to use funds for the purposes specifically designated in the CARES Act, borrowers will be eligible for loan forgiveness in an amount equal to the amount spent by a borrower during the 8-week period after the loan origination date (not to exceed the amount of the PPP Loan) on the following items:

- Payroll costs (not including compensation above $100,000 for any individual)
- Interest payments on mortgages incurred prior to February 15, 2020 (specifically excluding any payment of principal)
- Rental payments under leases in force prior to February 15, 2020
- Utility payments for service beginning prior to February 15, 2020

Due to likely high subscription to the PPP program, not more than 25% of the forgiven amount shall be for non-payroll costs. The SBA will be issuing additional guidance on PPP Loan forgiveness in the coming weeks.

Economic Injury Disaster Loans (EIDL)

In addition the loans available pursuant to the PPP program, the CARES Act expands the SBA's EIDL program by providing long term, low interest loans and emergency cash advances to assist nonprofit organizations and small businesses experiencing a substantial economic injury as a result of the COVID-19 national disaster. A substantial economic injury has occurred when an association is unable to pay ordinary operating expenses or has reduced working capital, increased expenses, or cash shortages due to the national disaster.

An EIDL loan is intended to be used to supplement or substitute for lost working capital until an association returns to pre-disaster operations.

There are limited permissible uses for the proceeds of an EIDL, including: payment of fixed debts, payroll, accounts payable, and other operating expenses that cannot be paid because of the disaster's impact. EIDL proceeds cannot be used for the following purposes: expanding business operations, paying cash dividends and/or bonuses, or disbursing payments to officers and owners unless those payments are directly related to the performance of services for the business.

The amount of an EIDL can be up to $2,000,000, with the amount based upon the economic injury suffered by the association as a result of the disaster. The interest rate is 3.75% for a small business and 2.75% for non-profits. The maximum term of an EIDL is 30 years. The SBA will determine the repayment period and monthly payments based upon the applicant's financial condition. An EIDL will not be forgiven by the SBA. Loans with a principal balance in excess of $25,000 must be secured by some form of collateral, and community association assessment income streams qualify as collateral for EIDLs. The CARES Act waives the requirements for a personal guaranty when the EIDL is less than $200,000.

In addition to the underwritten EIDL loan, the CARES Act establishes that a qualifying business may request an emergency grant of not more than $10,000 when it applies for an EIDL. The grant is disbursed by the SBA within three days after receipt of the EIDL application. The CARES Act requires that the grant be used for one of the following purposes: providing sick leave to employees, maintaining payroll, meeting increased costs to obtain materials, making rent or mortgage payments, or repaying obligations that cannot be met due to revenue losses. The applicant is not required to repay the grant, even if the business is subsequently denied an EIDL. However, if the business also receives a PPP program loan, the grant will be subtracted from the amount of the PPP program loan that is eligible for loan forgiveness.

Your association may apply for an EIDL loan by following this link: https://covid19relief.sba.gov/#/

Winstead is Here to Help

Under the CARES Act, both the SBA and participating lending institutions are expected to develop and refine processes over the first two weeks of April. Winstead's attorneys have experience assisting clients with understanding and applying for the assistance programs discussed above.

For additional information directly from the SBA, please contact the SBA disaster assistance customer service center by phone (1-800-659-2955), e-mail (disastercustomerservice@sba.gov) or online (https://www.sba.gov/disaster/apply-for-disaster-loan/index.html).

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[1] It should be noted that homeowner associations' management companies are independently eligible for PPP loans, so an association's management fees paid directly to a management company are not eligible costs for a PPP loan to the association. If the association has employees of its own (not employees of the management company), then an association would likely be eligible for a PPP loan to cover its payroll costs.