

COVID-19 Aid To Small Business Owners Trickles Out As SBA Clarifies CARES Act Rules For Sole Proprietors

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Entrepreneurs

How to break \$1M in revenue in a business staffed only by the owners

Robert W Lederhilger III got his hopes up when he heard the Coronavirus Aid, Relief and Economic Security Act (CARES) Act was offering relief to small businesses hurt by the COVID-19 crisis. His white label web hosting company, Enterprise Service Level, a single member LLC in Bradenton, Fla. that tackles projects with the help of three contractors, applied for a \$10,000 advance from the Small Business Administration's Economic Injury Disaster Loan (EIDL) on March 29, when the SBA was still indicating that advances would come within three days of a successful application.

Yesterday, Lederhilger finally received \$1,000 advance from the EIDL in his bank account. He also applied through his bank for a Paycheck Protection Program (PPP) Loan, another part of the \$2 trillion CARES Act designed to help companies keep paying people during the crisis. The PPP loans are forgivable if used for payroll and other designated costs.

"Looking back, I understand we're dealing with the government here," says Lederhilger. "They're not quite as efficient as we'd like them to be. I believe Congress did try to help small business, and the SBA was overwhelmed."

But Lederhilger realizes his company's situation is more fortunate than the many small businesses that were shuttered completely by the COVID-19 crisis. After two strong months in January and February, his sales started flattening in March, and the trend continued in April, says Lederhilger.

"There are a lot of small businesses in way different positions," he says. "I feel terrible for them. That's why I was hopeful these programs would help."

Yesterday, the SBA issued a guidance on the PPP program that addressed a number of questions sole proprietors have had on the PPP. They have been able to apply for the PPP program on Friday, April 10, but many have been confused about how it applies to them. The guidance is called "[Business Loan Program Temporary Changes: Paycheck Protection Program—Additional Eligibility Criteria and Requirements for Certain Pledges of Loans.](#)"

Among the key points clarified:

- **The maximum amount eligible for forgiveness:** The guidance defines these as payroll costs including salary, wages and tips, up to \$100,000 of annualized pay per employees (up to \$15,385 per individual), as well as covered benefits for employees, excluding the owners. These benefits include healthcare expenses, retirement contributions and state taxes on employee payroll, such as unemployment insurance premiums.

To prevent the PPP from turning into a windfall for businesses with low overhead, a self-employed owner's forgiveness is limited to a proportionate share of eight weeks of net profit from the owner's 2019 Form 1040 Schedule C.

- **How to calculate the business owner's compensation if they have no employees :** This is calculated based on 2019 net profit, based on the 2019 Form 1040 Schedule C (line 31). Amounts over \$100,000 are subtracted.

- * **How business partners may handle PPP applications:** The guidance says that a partner in a partnership cannot submit a separate PPP application as a self-employed individual. The self-employed income of partners must be record as a payroll cost, up to \$100,000 annualized, on a PPP application.

The EIDL program offers loans as large as \$2 million, with an advance up to \$10,000. They come with a 3.75% interest rate for businesses and 2.75% for nonprofits. The maturity is 30 years, with the first payment deferrable for one year.

The Paycheck Protection Loans, which can be as large as \$10 million, have a 1% interest rate and a maturity of 2 years. They are forgivable if a minimum of 75% of the funds received are used for payroll over the eight-week period after the loan is signed and the remaining for specified operating expenses, such as rent, mortgage and utilities. The first payment can be deferred for six months.

The SBA has been sending out emails this week clarifying the amount that is available applicants for the EIDL advances.

"To ensure that the greatest number of applicants can receive assistance during this challenging time, the amount of your Advance will be determined by the number of your pre-disaster (i.e., as of January 31, 2020) employees. The Advance will provide \$1,000 per employee up to a maximum of \$10,000," the SBA notice states.

Mounting despair

Many small business owners whose income and ability to work have been cut off by shelter-in-place rules are still waiting with growing desperation for aid to arrive from the government.

The application process for sole proprietors on Friday was bumpy by many accounts.

“The biggest roadblock freelancers are facing is not having an existing business checking account with lenders,” Rafael Espinal, executive director of the Freelancers Union,” said in an email on Monday. “Most banks have made having a business account with an open date of February 15th or before a requirement to apply for the loans. Freelancers are left with trying to find smaller lenders that are open to take new clients. Also, because it’s a program with limited funds and freelancers were allowed to apply 1 week after it was made available to small businesses, it’s possible many will be left out. We will have to wait and see.”

To clear up some of the confusion, MBO Partners, a provider of back-office services to the self-employed, launched a [calculator](#) on its website to help the self-employed calculate what their likely aid would be through the EIDL and PPP programs.

“We call on the government – specifically the SBA and/or Treasury department – to help ensure that all workers have equal access to the programs and benefits access to the programs and benefits promised under the CARES Act,” said Gene Zaino, chairman of MBO Partners, a provider of back office services to independent workers that also studies the self-employed workforce, in an email. “To date, independents — America’s smallest businesses — have been challenged as they try to take advantage of initiatives like the Paycheck Protection Program, which rolled out to independent contractors just a few days ago on April 10. This workforce is large, powerful, and cannot be forgotten: there are 41 million independent workers in the United States at present, contributing \$1.28 trillion in value to the U.S. economy annually.

Know Your Customer laws are one reason banks have not moved as quickly as many small business owners would like, say many experts. Fraud has often been a problem in large-scale lending programs, and banks are responsible for making sure the money doesn’t get into the hands of criminals—or businesses that don’t show signs of legitimate activity, such as actual revenue.

“A lot of the fraud is happening with smaller businesses and sole proprietors,” says Christina Camacho, founder and CEO of Ivy Lender, which created a COVID-19 SBA Loan Marketplace, which delivers applications to SBA-approved lenders.

Unanswered questions

The latest guidance addresses some of the most common questions sole proprietors have been asking small business groups but still does not seem to address the situation of self-employed owners who take a combination of a paycheck and an owner’s draw—a common practice for those whose income fluctuates from month to month. They may take a modest

paycheck the business can constantly cover from month to month but rely heavily on distributions from their income. It doesn't appear that this additional distribution income is included in income calculations.

"There are many unanswered questions," said Gerri Detweiler, education director of NAV, a financial technology firm that is processing loan applications. "These business owners are really lost. When they see the administration talk about the number of loans being made, all they can see is a dwindling pot of money."

Progress to date

The Treasury Department says that through April 13, the SBA has guaranteed 1,035,086 loans under the PPP. It is unclear how many EIDL loan advances have been disbursed.

One grassroots effort, the [COVID Loan Tracker](#), offers crowdsourced information on how small business owners are faring. Among more than 9,000 small businesses that applied as of 6 am today, 5% reported receiving PPP loans, and 3.5% received EIDL advances.

J. Kirk McGill, a CPA and attorney in the Denver, Colo., area, helped some of his clients apply for aid from the SBA. As of Tuesday, one five-employee firm received a \$5,000 EIDL advance; another business with one owner-employee received a \$1,000 advance, according to McGill.

"No client has received an actual EIDL loan, or even so much as an email to discuss the loan application," McGill said in an email. "Clients also report the SBA pulled their credit report multiple times for the same EIDL loan, which has damaged their credit."

Two of his clients have received PPPs, he added. "Both had existing bank relationships at small banks," he said in his note. "No client has received a PPP loan from a major institution or from a bank with which they did not have a previous relationship," McGill said.

Evan Kulak, a wealth advisor and principal at Polaris Portfolios in Chicago, said his firm helped 25 clients, generally firms from 10 to 50 employees, apply for the EIDL and associated cash advance. "None of them got anything," he said, as of Tuesday.

What the picture will be for America's smallest businesses remains to be seen. There are nearly 26 million nonemployer firms with no payroll—representing the vast majority of small businesses—and their fate will have a huge effect on the economy.

Steve King, partner at Emergent Research, a firm in Lafayette, Calif., that studies the independent workforce, said one of his biggest concerns is whether they will be able to get enough help from the loan programs quickly enough to avoid closure. His firm has done an analysis of [closure scenarios](#) that can only be described as heartwrenching. "For a lot of these people, unemployment is the better alternative," says King.

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