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Payroll Protection Plan Epilogue

Douglas David Klein[1], Zion Kang[2]

[1]*Adjunct Professor, New Jersey City University, United States, dougkleinteacher@gmail.com*
[2]*Student, Jeju International School, Korea, zokang222@gmail.com*

ABSTRACT: The Paycheck Protection Program (PPP), part of the CARES Act passed by the United States Congress in 2020, was instituted as a response to social distancing restrictions during the COVID pandemic that shut down large parts of the American economy. The purpose of PPP was to provide small businesses (and corporations with 500 employees and less) with easy-access loans to help make essential operating payments such as rent, utilities and payroll. If PPP funds were properly used as promised, then the amount borrowed would be forgiven - meaning the loan would be converted to a grant and the borrowed funds would never have to be repaid. The PPP was rolled out in two phases: April 2020 and January 2021. This paper will address if the program worked as envisioned - what was the PPP's ultimate effectiveness? Did it really save jobs and businesses from failing? This paper will also research the percentage of fraudulent or criminal PPP loans - was there widespread fraud, abuse and misuse of the easy-access funds?

KEYWORDS: Paycheck Protection Program, effectiveness, fraud, abuse, businesses, jobs, loans

Introduction

The Paycheck Protection Program (PPP) provided loans for small businesses to keep employees on their payroll and to keep the business itself viable after social distancing restrictions and shutdowns were ordered by state and local governments. The PPP was established in April, 2020 under the Coronavirus Aid, Relief and Economic Security Act (CARES Act). Originally, under CARES, 75% of the PPP loan had to be used for employee related expenses, including wages, salaries, benefits (including vacation and parental, family, medical, or sick leave) and the state and local taxes on compensation. This provision was amended to 60% in June 2020 (Calzacorta 2021).

The PPP loan application and guidelines for approval process were overseen by the Small Business Administration, a division of the US Department of Commerce. However, the loans themselves were funded by commercial banks and then guaranteed by the SBA (Brumberg 2020). The PPP was rolled out in two phases: April 2020 and January 2021. The April stage funded $525 billion dollars in loans that were meant for companies that had no cash cushion and little access to additional capital. Roughly 5.2 million loans were funded to companies from April to August, 2020. The First Draw PPP Loans were intended to be used to help fund payroll costs (including benefits), mortgage interest, rent, utilities, and worker protection costs related to COVID-19, uninsured property damage costs caused by looting or vandalism during 2020, and certain supplier costs and expenses for operations (Stewart 2020).

The basic concept was that the SBA would forgive loans from borrower repayment e.g., the Federal government pays the banks back - if all employee retention criteria were met, and the funds were used for eligible expenses. However, loan forgiveness is not simple 1) the process that borrowers needed to complete to become eligible for forgiveness was hard to find 2) when a loan is forgiven, it creates IRS income tax reporting issues, namely the borrower cannot claim as a business deduction expenses that were paid for with PPP funds (normally, forgiven loans must be reported as income, but in this case, the forgiven loans would not be reportable) (Ransom 2020).

Terms and Conditions (from the SBA)

PPP loans had an interest rate of 1%. Loans issued prior to June 5, 2020 have a maturity of two years. Loans issued after June 5, 2020 have a maturity of five years. Loan payments will be deferred for borrowers who apply for loan forgiveness until SBA remits the borrower's loan forgiveness amount to the lender. If a borrower does not apply for loan forgiveness, payments are deferred 10 months after the end of the covered period for the borrower's loan forgiveness (between 8 weeks and 24 weeks).

No collateral or personal guarantees were required. Neither the government nor lenders will charge small businesses any fees (SBA 2020). If the funds were properly used from the 1st Draw, small businesses could apply for a 2nd Draw if PPP funds were still available (Gregg 2020).

By September 2020, Congressional Committee investigations found that some loans went to wealthy individuals or companies that were owned by politically powerful and well-connected borrowers (Madore 2020). The investigations also found that some loans were fraudulent, with borrowers engaging in criminal intent (Madore 2020). In Jan, 2021, the SBA released a document "Myth vs. Fact" to dispel beliefs that the PPP was wrought with waste and fraud (SBA Office of Capital Access, 2021). The agency announced all loans "are being reviewed" and outlined the process the SBA has in place for loan approvals, including a manual review for all requests of $2 million and more (SBA Office of Capital Access 2021).

After popular outcry on social media and stories of fraud appeared in the media, the SBA released the names of all companies who applied for PPP - but it didn't mean the business actually received PPP loans, simply applied (O'Connell 2020). 75% of all PPP loans went to a business with 9 or fewer employees and 87% of loans were for $150,000 or less. The SBA reported that $130 billion from the first phase of PPP went unclaimed. Ultimately, PPP supported 51 million employees (SBA Office of Capital Access 2021).

By the end of January, 2021, the US national employment rate was 6.7% and the SBA says that the PPP helped to achieve this statistic. In an attempt to have funds distributed in rural locations and minority neighborhoods, the SBA and the US Treasury Department executed an aggressive outreach campaign to ensure PPP participation by Community Development Financial Institutions (CDFIs), Minority Depository Institutions (MDIs), and minority, women, veteran, or military-owned lenders due to their existing presence in underserved communities. The SBA and Treasury's claim that their outreach campaign to underserved communities worked: As of August 8, 2020, when the PPP Phase 1 closed to new loan applications, 432 MDIs and CDFIs had participated from across the country, providing over 221,000 loans for more than $16.4 billion (SBA Myths and Facts 2021).

PPP delivered $133 billion of loans to businesses in Historically Underutilized Business Zones, accounting for more than 25 percent of all PPP funding. What's more, a review of census tracts showed 28 percent of the U.S. population lives in low- and moderate-income census tracts, and when matched against the distribution of PPP loans, 27 percent of the PPP funds went to low and moderate income communities, which is in line with their representation in the population (Borawski and Schweitzer 2021).

Not surprisingly, the Federal government declared the PPP a success. But what was the extent of fraud and abuse? In September, 2020, the US Justice Department charged 57 people with trying to steal a total of $175 million in taxpayer-backed coronavirus pandemic loans (Gregg 2020). The funds were disbursed with relatively little vetting, and businesses were allowed to certify their own eligibility (Gregg, 2020). This fact made the illegal activity easier to accomplish for criminals who saw the PPP as an opportunity. The $175 million that applicants attempted to steal has entailed a known loss of $80 million to the government, officials said. The Justice Department was able to recover $30 million (Rochelle 2021).

It's not easy to forgive

By October of 2020, it became clear to borrowers that the administrative process of having the PPP loans forgiven was not easy to accomplish. There were hundreds of thousands of PPP borrowers, and that meant a crush of forgiveness applications for personnel to receive and acknowledge. In these modern times, borrowers expect to find a web portal on the lender's website to complete the forgiveness form. Will the banks have the manpower to develop the online form on time? Will the software work as designed? How about the small regional and minority owned financial institutions - will they have the resources to deliver online forgiveness applications? (Ransom 2020)

Moving on from the questions on how the forgiveness process will be administratively offered to the borrowers - how will the hundreds of thousands of applications be processed efficiently by the lenders in a timely manner? Banks - just like any other employer - staff their businesses based on normal business volume. The national lobbying and interest of banks - the American Banking Association - submitted a formal letter summarizing their concerns about processing forgiveness in January 2021 (Nicholls 2021).

How and when to apply for loan forgiveness?

1. The first step in the process of having your PPP loan converted to the forgiveness stage is to contact the lender and complete the correct form (SBA Form 3508 or the shortened versions SBA Form 3508EZ or SBA Form 3508S)

2. The 2nd step is compiling the documentation the SBA requires:

Payroll documentation for all payroll periods that overlapped with the period covered by the PPP, including bank account statements or third-party payroll provider reports documenting the amount of cash compensation paid to employees. Also required are the payroll tax forms (or equivalent third-party payroll service provider reports) for the periods that overlap with the PPP, typically, Form 941 and State quarterly business and individual employee wage reporting and unemployment insurance tax filings reported, or that will be reported, to the relevant state (SBA.gov 2021).

As noted above, non-payroll expenses deemed essential and intrinsic to keeping a business open were covered. Property damage because of rioting was also covered. The SBA also advised borrowers to follow up with lenders to submit additional documentation as requested in a timely manner. If SBA undertakes a review of your loan, your lender will notify you of the review and the SBA loan review decision. You have the right to appeal certain SBA loan review decisions. Your lender is responsible for notifying you of the forgiveness amount paid by SBA and the date on which your first payment will be due, if applicable (SBA.gov 2021).

How well did the process work?

The SBA has been posting information, data and statistics on the PPP since April 2020 at this site https://www.sba.gov/funding-programs/loans/covid-19-relief-options/paycheck-protection-program/ppp-data

Data as of May 24, 2021

Table 1. PPP Loans Issued, Forgiven and Under Review

Total 2020 PPP volume	5.2 million loans for $521.2 Billion - 70% of all loans were for less than $50,000
Loans Forgiven	3.3 million loans for a total of $279.4 Billion
PPP Loan amount NOT forgiven	$1 billion
PPP Loans Under review	145,000 loans representing $81.5 Billion
Applications not yet received	1.7 million loans representing $159.1 billion

Source: Small Business Administration

But owners had to wait months for clarity on how to apply for forgiveness. By the Fall of 2020, there were still not clear guidelines on how to file for forgiveness. And when the new year of 2021 began, there was still plenty of confusion (Cowley 2020).

Putting the question of loan forgiveness aside...was PPP a success?

Not according to Raj Chetty, a leading American labor economist and professor at Harvard University. In a paper he co-wrote for the National Bureau of Economic Research, the $600 billion spent should have had a much greater boost in the economy (Chetty and Stepner 2020). In terms of saving people's jobs, the program spent vastly more money than the number of jobs it saved," economist Michael Stepner, one of the paper's co-authors. About 90% of those workers whose paychecks were paid out of the fund were not at risk of being laid off in the first place, according to the analysis. The bulk of the funds were allocated to businesses in the professional, scientific and technical services industries — sectors in which employees can typically telecommute (Chetty and Stepner 2020).

And small business owners questioned how the program's logic - in order to receive a loan, the business owner had to keep workers employed (Chetty and Stepner 2020). But there weren't enough customers to pay the businesses' other bills. It's possible that the loans were attractive to those business owners who knew their payrolls would remain unchanged. "If they weren't going to lay employees off anyway, they are just getting a grant from the government. That made the loans particularly attractive to firms that knew they could keep employees on payroll," Stepner said (Chetty and Stepner 2020).

Other Economic Studies

Other studies performed by academics were less critical than the NBER report. A widespread study conducted by MIT in July 2020 concluded that the PPP increased employment by 2.3 million workers (Autor, Cho 2020). Preliminary July 22, 2020. This study utilized employer data provided by the largest US payroll processing firm ADP, representing anonymized payroll information of 26 million employees across all industries. The MIT study found that small firms eligible for PPP loans evinced the same decrease in employment as large firms in the early days of the pandemic - March and April of 2020. But after the PPP became active, small firms showed a quicker and larger employment recovery to pre-pandemic levels: "We estimate that through the end of May the PPP increased the level of employment at eligible firms by between 2 percent and 4.5 percent" providing some empirical evidence that the premise behind the legislation was working in practice (Autor, Cho 2020).

Conservative Academic Perspective

In a paper entitled "Has the Paycheck Protection Program succeeded" economists Glenn Hubbard, Professor of Finance and Economics at the Columbia Business School, and Michael R. Strain, Director of Economic Policy Studies at the American Enterprise Institute, concluded that the first phase of PPP appeared to be a success. Though they did caution that it was too early to declare a conclusive judgment, Hubbard and Strain found that small firms that received PPP loans were in better financial health than larger companies that received no PPP funds. (Hubbard and Strain, 2020)

This thesis was based on corporate data provided by Dun and Bradstreet, one of the largest and oldest aggregators of business information in the US. Noting that 47% of all private sector jobs are with an employer with 500 employees or less, Hubbard and Strain compared firms that applied for PPP loans of at least $150,000 and researched the following:

- Were they still in business?
- Where they paying bills on time?
- Did they maintain pre-pandemic employment levels?

The data evinced that the smaller firms eligible for PPP loans were in fact healthier by September 2020 based on all three metrics delineated above. Thus, they concluded that the

PPP succeeded in its short-term goals of allowing smaller businesses to maintain employment connections with workers while absorbing the sudden shock of plummeting or zero revenues. (Hubbard and Strain 2020).

Incidents of Fraud

When the PPP was first announced in April 2020, there were fears of widespread fraud. A year later, the Project on Government Oversight (POGO) - after reviewing comprehensive statistics from the Department of Justice and the Small Business Administration, found that only 209 people were charged with theft and fraud up to April 2, 2021. The total amount allegedly stolen according to POGO was $445 million. Since the total SBA PPP funding was $755 BILLION, the alleged fraud is .0006% of the total funded - a very low ratio (Scwellenback and Summers 2021).

A different program known as the Economic Injury Disaster loan, also supervised by the Small Business Administration, had a much higher rate of fraud. The POGO study found that over $580 million was seized back by the SBA, representing 23,000 loans found to be fraudulent. Since only $202 billion is EID loans were issued, the ratio of .003%, 20 times higher than the fraud rate of PPP loans (Schwellenback and Summers 2021).

Will the number of jobs saved ever be counted?

One year after Congress created the Paycheck Protection Program, taxpayers don't know how many jobs were saved by the nearly $1 trillion in forgivable loans issued to businesses during the pandemic (Wire 2021). And economists and government watchdog groups say they probably never will — because the government didn't count. The PPP was pitched as a way to save millions of jobs threatened during the COVID-19 recession. But the Small Business Administration under President Trump — and now under President Biden — hasn't tracked figures on jobs that were saved, despite a legal requirement to do so (Wire 2021). "No one will actually know except for the recipients whatever happened with the loan and with the jobs," said Sean Moulton, senior policy analyst at the Project on Government Oversight, a watchdog group (Wire 2021). The SBA's initial estimate of 50 million jobs "supported" by the PPP was quickly dismissed as wildly inaccurate. Treasury Department economists place the number closer to 19 million, while economists studying the program estimate it's between 2 million and 5 million (Wire 2021).

More than 8.7 million forgivable loans worth $961 billion have been made so far. And Joseph Biden signed a two-month extension at the start of his Presidency, allowing the SBA to accept applications for $79 billion in loans through May 31. SBA officials told Congress they expect the money to be exhausted by the end of April (Wire 2021).

In April 2020, just days after the program began issuing loans, the Trump administration's Office of Management and Budget instructed the agency not to ask loan recipients to report back on the estimated number of jobs created or retained (Wire 2021).

The budget office said "centrally available economic data" would provide sufficient information to produce the report. Its memo did not say where those data would come from, how they would be verified or why the budget office did not want the businesses to provide the information (Wire 2021).

In January, the agency's inspector general emphasized in a report that reliable information on the number of jobs saved was not available because the SBA did not collect it. "SBA officials and national leaders do not have enough information to make informed decisions or determine to what extent the PPP met national program objectives. Additionally, SBA cannot accurately report jobs retained by PPP borrowers" (Wire 2021).

Moulton said applications for forgiveness would provide only a snapshot of current conditions, not the five years of jobs data that Congress specifically asked for in the CARES Act to verify whether the loans kept people in their jobs in the long term. Employees who were paid using the loan could have been laid off as soon as the money ran out, he said (Wire 2020). No one disputes that the program probably helped thousands of small businesses survive. The scope of how many closed and how many stayed open will become more obvious as tax filings and bankruptcy data become available in time, economists say (Wire 2021).

Eric Zwick, an economist at the University of Chicago's business school who has studied the program, said Congress could have modified the program in the early months of the pandemic after seeing how much money was going to businesses that weren't in regions or industries facing economic peril because of shutdowns. Congress waited until December to prioritize loans for businesses with fewer employees and with major drops in revenue. "You could have had the same program, just as [beneficial], possibly for half the price," Zwick said (Wire 2021).

UC Berkeley law professor Robert Bartlett, who surveyed businesses in Oakland during the pandemic, found that how much the loan contributed to a business' expectation of survival depended largely on how many people it employed (Wire 2021). Microbusinesses of fewer than five employees needed their people to continue working in order to stay open and thus benefited the most from payroll support, Bartlett said. They were 20% more likely to say they expected to be open in six months because of the loan (Wire 2020). But for businesses with more than five employees, layoffs were the best way to manage cash flow, and they needed rent help from the government more than payroll support, Bartlett said. Though the PPP delayed layoffs for a few months, the businesses reported that the loans did not have a lasting effect on their ability to survive the next six months (Wire 2020).

The PPP lapsed in August, but Congress in December approved a second round of loans, tightening eligibility requirements to focus support on the smallest, hardest-hit firms and those with the greatest drops in revenue. Only businesses with fewer than 300 employees could apply for a second loan, and money was set aside for particularly small and minority-owned businesses (Warmbrodt 2021). It also created direct grants for performing venues and restaurants, which the SBA expects to make available this month. Businesses applying for PPP loans still need not report the number of jobs saved (Warmbrodt 2021).

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