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SBA Clarifies Treatment of Foreign Affiliates for 500-Employee Calculation

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The Paycheck Protection Program (PPP) requires borrowers to certify that “[t]he applicant (1) is an independent contractor, eligible self-employed individual, or sole proprietor; or (2) employs no more than the greater of 500 employees or, if applicable, the size standard in number of employees established by the SBA in 13 C.F.R. 121.201 for the applicant’s industry. There has been confusion among some borrowers as to whether employees of foreign affiliates should be included in the 500-employee calculation.

On May 18, 2020, the SBA issued an Interim Final Rule clarifying the treatment of foreign affiliates for a borrower’s 500-employee calculation:

Question: *Are employees of foreign affiliates included for purposes of determining whether a PPP borrower has more than 500 employees?*

Answer: *Yes. The CARES Act specifies that an entity is eligible for a PPP loan only if it is (1) a small business concern, or (2) a business concern, nonprofit organization described in section 501(c)(3) of the Internal Revenue Code, veterans organization described in section 501(c)(19) of the Internal Revenue Code, or Tribal business concern described in section 31(b)(2)(C) of the Small Business Act that employs not more than the greater of 500 employees, or, if applicable, SBA’s employee-based size standard for the industry in which the entity operates.*

SBA’s affiliation regulations provide that to determine a concern’s size, employees of the concern “and all of its domestic and foreign affiliates” are included. 13 C.F.R. 121.301(f). Therefore, to calculate the number of employees of an entity for purposes of determining eligibility for the PPP, an entity must include all employees of its domestic and foreign affiliates, except in those limited circumstances where the affiliation rules expressly do not apply to the entity. (Emphasis added) Any entity that, together with its domestic and foreign affiliates, does not meet the 500-

employee or other applicable PPP size standard is therefore ineligible for a PPP loan.

*However, as an exercise of enforcement discretion due to reasonable borrower confusion based on SBA guidance (which was later resolved through a clarifying FAQ on May 5, 2020), **SBA will not find any borrower that applied for a PPP loan prior to May 5, 2020 to be ineligible based on the borrower's exclusion of non-U.S. employees from the borrower's calculation of its employee headcount if the borrower (together with its affiliates) had no more than 500 employees whose principal place of residence is in the United States.*** (Emphasis added) *Such borrowers shall not be deemed to have made an inaccurate certification of eligibility solely on that basis. Under no circumstances may PPP funds be used to support non-U.S. workers or operations.*

This Interim Final Rule makes clear that, to calculate the number of employees for purposes of determining a borrower's eligibility for the PPP, the borrower must include all employees of BOTH its domestic and its foreign affiliates.

As a result, borrowers who applied for a PPP loan prior to May 5, 2020 and based their employee headcount eligibility only on employees employed by their domestic affiliates, not their foreign affiliates, this new guidance provides assurance that the borrower will not be found to have made an inaccurate certification of eligibility solely on that basis.

Finally, this Interim Final Rule reminds borrowers that PPP loan proceeds may only be used for U.S. workers and operations.

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