## NEWS ALERT

# TAX GROUP

## *UPDATED*
## CARES Act – Understanding the Requirements and Benefits of the Obtaining Paycheck Protection Program Loans

By Marc T. Finer | April 9, 2020

*Since this Client Alert was originally issued on March 31, 2020, the Small Business Administration, in coordination with the U.S. Treasury Department, has issued additional guidance clarifying certain aspects of the Paycheck Protection Program. This updated Client Alert incorporates this additional guidance as of April 8, 2020.*

On March 27, 2020, President Trump signed the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act") into law. The CARES Act includes a new small business loan program under which the Small Business Administration ("SBA") and its network of lending financial institutions may provide 100% federally-backed loans up to an aggregate amount of $349 billion to eligible businesses to help pay their operational costs like payroll, rent, health benefits, insurance premiums, and utilities for up to 8 weeks. The loan program – called the Paycheck Protection Program – covers loans granted under the program during the period from February 15, 2020 through June 30, 2020 (the "Covered Period").

Businesses that are eligible to participate in the Paycheck Protection Program include:

- Businesses with up to 500 employees or which meet the applicable employee-based size standard for the relevant industry as provided by current SBA regulations;
- Businesses which meet the applicable revenue-based size standard for the relevant industry as provided by current SBA regulations;
- Businesses that satisfy both tests of the SBA's "alternative size standard" as of March 27, 2020: (1) the business's maximum tangible net worth is less than or equal to $15 million and (2) the business's average net income after deducting federal income taxes (note that this calculation excludes any carryover losses) for the two full fiscal years prior to the application date is less than or equal to $5 million;
- Businesses in the food service or accommodation industry with more than one location but no more than 500 employees at each location;
- Certain nonprofits (Section 501(c)(3) and 501(c)(19) tax-exempt organizations); and
- Certain eligible independent contractors, self-employed individuals and sole proprietors.

SBA affiliation rules generally apply for purposes of determining loan eligibility under the employee-size based, revenue-size based and alternative-size based standards.

For purposes of applying the employee-based size standard, applicants may generally calculate their number of employees by using their average number of employees in the (i) 12 month period prior to the date of the loan application, (ii) 12 completed calendar months prior to the date of the loan application or (iii) calendar year 2019.

The features of the loans made under the Paycheck Protection Program include:

- Subject to certain conditions described below, the full principal amount of the loan and any accrued interest is forgivable.

- No collateral or personal guarantee is permitted. Additionally, there is no recourse against any individual, shareholder, member, or partner of an eligible loan recipient for non-payment, unless the loan proceeds are used for unauthorized purposes.

- Interest on the loan is 1%.

- No prepayment penalty.

- Maximum loan amount (capped at $10MM) is 2.5 times the borrower's average total monthly payroll costs using data from either the 12 previous months or from the calendar year 2019.

  "Payroll costs" do not include: (1) cash compensation of an individual employee in excess of an annual salary of over $100,000 (excluding noncash benefits), prorated for the Covered Period; (2) compensation of employees whose principal place of residence is outside of the United States; (3) qualified sick and family leave for which a credit is allowed under the Families First Coronavirus Response Act, (4) employer-side federal payroll taxes, and (5) payments made to an independent contractor or sole proprietorship.

- Loan proceeds may be used to pay the following expenses:

  - Payroll Costs:

    - Compensation to employees, such as salary, wages, commissions, cash, etc.;

    - Paid leave (other than qualified sick or family leave wages for which a tax credit is allowed under the Families First Coronavirus Response Act);

    - Severance payments;

    - Payments for group health benefits, including insurance premiums;

    - Payments for retirement benefits;

    - Payments of state and local taxes assessed on compensation of employees; and

    - Compensation to sole proprietorships or independent contractors (including commission based compensation) up to $100,000 in 1 year, prorated for the period February 15, 2020 through June 30, 2020.

  - Group health care benefits during periods of paid sick, medical or family leave, and insurance premiums;

  - Salaries, commissions, or similar compensations;

  - Mortgage interest;

  - Rent/lease agreement payments;

  - Utility payments; and

  - Interest on any other debt incurred prior to February 15, 2020.

- All loan payments (principal, interest and fees) are deferred for six (6) months. However, interest will continue to accrue during the deferment period.

- Loan Forgiveness Rules

The principal amount of the loan plus accrued interest is eligible for loan forgiveness up to an amount equal to the total costs incurred or paid for the following expenses during the 8-week period starting with the loan origination date (the "Covered Forgiveness Period"):

- Payroll costs;
- Interest payments on mortgages on real or personal property incurred prior to February 15, 2020 ("covered mortgages");
- Rent obligations on a lease agreement in force before February 15, 2020 ("covered rent payments"); and
- Utility payments (electricity, gas, water, transportation, telephone or internet access) for which service began before February 15, 2020 ("covered utility payments").

NOTE: Loan amounts used to satisfy interest on pre-February 15, 2020 debt obligations that are not covered mortgages are not eligible for forgiveness.

NOTE: 75% of the forgiven amount must be used to cover payroll costs. Only 25% of the forgiven amount may be used for payments of covered rent payments, covered utility payments and interest on covered mortgages.

The loan forgiveness amount is excluded from taxable income.

The amount of loan forgiveness will be reduced for (1) any employee cuts or (2) reductions in salary/wages above a certain amount.

*Reduction in Loan Forgiveness Amount for Fewer Full-Time Employees*

The reduction in the amount of loan forgiveness resulting from the termination of employees is calculated as follows:

(A) The maximum available loan forgiveness amount

*multiplied by a percentage obtained by dividing*

(B) The borrower's average number of full-time employees ("FTEs") per month (calculated by the average number of FTEs for each pay period falling within a month) during the Covered Forgiveness Period

By

At the election of the borrower

a. The average number of FTEs per month employed from February 15, 2019 to June 30, 2019, or

b. The average number of FTEs per month employed from January 1, 2020 until February 29, 2020

*Reduction in Loan Forgiveness Amount for Reduction in Salaries/Wages*

For reductions in salaries/wages, the loan forgiveness amount is reduced dollar-for-dollar by the amount of any reduction in total salary/wages of any employee during the Covered Forgiveness Period that is in excess of 25% of the employee's salary/wages during the employee's most recent full quarter of employment before the Covered Forgiveness Period. "Employee" is limited to any employee who did not receive during any single pay period during 2019 a salary or wages at an annualized rate of pay over $100,000.

*Relief from Loan Forgiveness Reduction Penalties*

Relief from the debt forgiveness reduction penalties is available for employers who rehire employees or make up for salary/wage reductions by June 30, 2020. Specifically, reductions will be determined without regard to otherwise applicable reductions in workforce or salaries/wages if the reductions occurred between February 15, 2020 and 30 days following the enactment of the CARES Act (April 26, 2020) if:

- Workforce Reductions: the borrower reduces the number of FTEs between February 15, 2020 and April 26, 2020, as compared to February 15, 2020, and not later than June 30, 2020, the borrower has eliminated the reduction in FTEs, or

- Salary/Wage Reductions: there is a salary/wage reduction between February 15, 2020 and April 26, 2020, as compared to February 15, 2020, for one or more employees and that reduction is eliminated by June 30, 2020 (it is unclear whether this is intended to be limited to employees who made $100,000 or less during 2019).

➢ Loan term is two years.

➢ To be eligible for a loan under the Paycheck Protection Program, an applicant must provide good faith certifications including:

(i) The applicant was in operation on February 15, 2020 and had employees for whom it paid salaries and payroll taxes or paid independent contractors;

(ii) The uncertainty of current economic conditions makes the loan request necessary to support its ongoing operations;

(iii) Acknowledging that the loaned funds will be used to retain workers and maintain payroll or mortgage payments, lease payments and utility payments;

(iv) The applicant will provide to the lender documentation verifying the number of full-time equivalent employees on the applicant's payroll as well as the dollar amounts of payroll costs, covered mortgage interest payments, covered rent payments, and covered utility payments for the Covered Forgiveness Period following the loan;

(v) Acknowledging that not more than 25% of the forgiven amount may be for non-payroll cost; and

(vi) During the period beginning on February 15, 2020 and ending on December 31, 2020, that the borrower has not and will not receive another loan under the Paycheck Protection Program.

At the outset, the existing network of approved SBA lenders will administer the program, although the SBA is expected to expand its list of lenders over time. The specific documentation required will be dictated by the individual lenders, but businesses planning to apply should begin assembling at least the following material.

- documentation verifying the number of FTEEs on payroll and pay rates for the applicable periods, including payroll tax filings; and state income, payroll, and unemployment insurance filings; and

- documentation verifying payments on mortgage or lease obligations and utilities.

*If you have any questions regarding the Paycheck Protection Program or how it might affect your business, please contact:*
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