

## The CARES Act

# Relief for Small Businesses

*Prepared by Wagner Law Group*

### **March 27, 2020**

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act, or CARES Act (the “Act”) was passed. The bill is expected to provide relief for eligible small business through a loan guarantee program, the postponement of certain tax payments, and a tax credit. The Act states that the Administrator at the Small Business Administration (SBA) should issue guidance to lenders and agents to ensure that processing and disbursement of covered loans prioritizes:

- Small business concerns;
- Entities in underserved and rural markets (including veteran communities and members of the military community);
- Small business concerns owned by socially and economically disadvantaged individuals;
- Women; and
- Businesses in operation for less than two years.

## **I. Small Business Loans**

### **a. Eligible Employers**

Under the Act’s loan program, a business concern (including self-employed individuals), non-profit organization described in Code Section 501(c)(3), veterans organization or Tribal business concern can obtain loans from local SBA lenders through the SBA’s 7(a) loan guarantee program between February 15, 2020 and June 30, 2020 if they have fewer than 500 employees, or if greater, the size standard of employees established for that industry. To determine the 500-employee threshold, the term “employee” includes those employed on a full-time, part-time or other basis, such as seasonal or temporary.

A business concern receiving this loan may not also receive an emergency disaster loan. The Internal Revenue Service (IRS) has the authority to establish a loan program for employers with between 500 and 10,000 employees, but if such a program were established, employers receiving such loans would be subject to conditions related to union activity and collective bargaining agreements.



A business concern that has several locations is an eligible employer if there are 500 or fewer employees at each location and the business classification is accommodation and food services.

#### **b. Maximum Loan Amount**

The maximum amount of the loan for businesses will be the average total monthly payments for Payroll Costs (defined below) incurred during the one-year period before the date on which the loan is made, multiplied by 2.5. For a seasonal employer, the maximum amount is the average total monthly payments for Payroll Costs for the period from February 15, 2019 (or March 1) to June 30, 2019 multiplied by 2.5. If a business was not in operation between February 15, 2019 and June 30, 2019, the maximum loan amount will be the average total monthly Payroll Costs incurred between January 1, 2020 and February 29, 2020 multiplied by 2.5.

A loan made on or after January 31, 2020 under the SBA's Disaster Loan Program may be refinanced as part of a covered loan.

In no event may the maximum loan amount exceed \$10 million.

#### **c. Payroll Costs**

Loans can be used to cover Payroll Costs, mortgage payments, rent, and utilities incurred between February 15, 2020 and June 30, 2020. It also includes interest on any other debt obligations incurred before February 15, 2020.

Payroll Costs include:

- Wages, salaries, and commissions;
- Paid vacation, parental, family, medical or sick leave;
- Severance pay;
- Cost of group healthcare benefits (including premiums);
- Payments for retirement benefits; and
- Payments for state or local taxes on employees' compensation.

If an employee makes more than \$100,000 annually, the loan can only cover wages up to \$100,000 (which would be a prorated over the period from February 15, 2020 to June 30, 2020).

Eligible expenses do not include amounts for qualified sick leave or qualified family leave for which a tax credit is allowed under the Families First Coronavirus Response Act, and compensation for employees whose principal residence is outside of the United States.

#### **d. Loan Forgiveness**

A portion of loan described above may be forgiven. To the extent that a loan is used to cover the following costs incurred between February 15, 2020 and June 30, 2020, it may be forgiven:

- Payroll Costs;
- Payment of interest on any covered mortgage loan obligation (does not include prepayment of or payment of principal of a mortgage); and



- Payment on any covered rent obligation.

The amount of the loan that may be forgiven will be reduced by any losses in employees or reductions in wages.

If the reduction is due to fewer employees, the reduction is, generally, calculated as follows:

- The maximum available forgiveness amount for the business multiplied by:
- The average number of "full-time equivalent employees" per month during the covered period divided by either:
  - The average number of full-time equivalent employees per month employed from February 15, 2019 to June 30, 2019; or
  - The average number of full-time equivalent employees per month employed from January 1, 2020 until February 29, 2020.

Special rules apply for seasonal employers and tipped employees.

For reductions in wages, the forgiveness amount is reduced by the amount of any reduction in total salary or wages of any employee during the covered period that is in excess of 25% of the employee's salary or wages during the most recent full quarter of employment before the covered period. For purposes of any reduction in forgiveness due to wages, the term "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 greater than \$100,000.

However, the amount of the forgiveness reduction will be calculated without taking into consideration any reduction in the number of full-time equivalent employees or a reduction in the salary of one or more employees during the period beginning on February 15, 2020 and 30 days following enactment of the CARES Act if:

- The employer eliminates the reduction in full-time equivalent employees by June 30, 2020; or
- In the event of a salary reduction, the reduction is eliminated by June 30, 2020.

Amounts forgiven are not subject to taxation as cancellation of indebtedness income.

The amount of the loan that is not forgiven shall have a maximum maturity of ten years. Lenders must provide deferment relief for the payment of principal, interest and fees on the loan for at least six months, and not more than one year. Interest on the loan cannot exceed 4%.

#### **e. Requesting a Loan**

To be eligible for the loan, the borrower must:

- Certify that, due to the uncertain economic conditions that currently exist, the loan is necessary to support the ongoing operations;
- Acknowledge that the funds will be used to retain employees and maintain payroll or make mortgage payments, lease payments, and utility payments;

- Certify that the borrower has not received any other loan for the same purpose and duplicative amounts; and
- Certify that the borrower does not have a loan application pending for the same purpose and duplicative amounts.

A self-employed individual must also submit documentation necessary to establish the individual as eligible (e.g., payroll tax filings filed with the IRS, Forms 1099-MISC, and income and expenses from the sole proprietorship as determined by the Administration).

## II. Economic Injury Disaster Loan (EIDL) Grants

Between January 31, 2020 and December 31, 2020, the Act expands eligibility for access to EIDL grants to businesses with 500 or less employees, any individuals who operate as sole proprietors or independent contractors, cooperatives with 500 or less employees, ESOPs with less than 500 employees that wholly own a business, and tribal concerns.

Any EIDL loans made in response to COVID-19 before December 31, 2020 will not require personal guarantees on advances and loans below \$200,000. In addition, the requirement that the applicant needs to have been in business for at least one year period before the disaster will be waived, except that no waiver will be made for a business that was not in operation on January 31, 2020. Furthermore, the requirement that the applicant not be able to obtain credit elsewhere is also waived.

During the covered period, the SBA may approve and offer EIDL loans based solely upon the applicant's credit score or use an alternative approach to determine an applicant's ability to repay.

The Act also establishes an emergency grant to allow an eligible entity that has applied for an EIDL loan to request an advance of the loan of not more than \$10,000, which the SBA must distribute in 3 days.

The advance payments may be used for providing paid sick leave to employees who are unable to work due to COVID-19; maintaining payroll; meeting increased costs to obtain materials unavailable from the applicant's normal sources; making rent or mortgage payments; and repaying obligations that cannot be met due to revenue losses.

## III. Deferral of Payroll Taxes

A business may defer the "employer share" of the payroll taxes it would otherwise pay to the federal government until December 31, 2020. The amount deferred must be paid in two installments. One-half of the deferred amount must be paid by December 31, 2021, and the remaining half by December 31, 2022.

If a business's loan (described above) is forgiven, the business will not be eligible to also defer payment of the "employer share" of the payroll taxes.

## IV. Payroll Tax Credit

A business that fully or partially shuts down its operations due to orders from an applicable government authority, or experiences a 50% reduction in its revenue, may



receive an advance-refundable credit on its payroll taxes up to 50% of the first \$10,000 of wages paid to employees during the period between March 13, 2020 and December 31, 2020. Wages include amounts paid by the employer to provide and maintain group health plan coverage. Non-profit organizations are also eligible to receive this tax credit.

With respect to the payroll tax credit, if an employer employs 100 or more employees, the employer will receive a tax credit for wages and contributions for health care coverage to paid to employees who are not performing any services for the employer. If an employer employs fewer than 100 employees, it can receive the tax credit on all wages and contributions for health care coverage.

If an employer takes a loan (as described above), the employer cannot receive this payroll tax credit even if the loan is forgiven.

## V. Net Operating Loss Deduction Relief

The Act provides two forms of temporary net operating loss (NOL) deduction relief for taxpayers with NOLs in 2018, 2019, and 2020 by temporarily reversing two changes to the Code made under the Tax Cuts and Jobs Act of 2017. The change likely to have the greatest effect is a provision of a 5-year carryback of NOLs. One ancillary benefit of this relief is that corporate taxpayers were subject to a higher maximum rate of corporate income taxes prior to 2018 (35 % rather than the current 21 %). Businesses wishing to take advantage of this relief will need to discuss the effect on other tax deductions businesses claimed on the years to which the NOL is being carried back. Second, since 2018, the Tax Cut and Jobs Act of 2017 capped the NOL deduction at 80% of taxable income. The Act repeals this limitation and permits taxpayers to claim the full NOL deduction. These two provisions will immediately allow affected taxpayers to file amended federal income tax returns and claim a tax refund.

## VI. Student Loans

Between the date of enactment and December 31, 2020, an employer may contribute up to \$5,250 towards an employee's student loan obligation, and that amount will be excludible from income. The \$5,250 exclusion would be reduced by any other educational assistance payments under Section 127 of the Code.

## VII. Conclusion

Employers should carefully review the loan program, the EIDL grants, the deferral of the payroll tax, the payroll tax credit, and the NOL deduction relief to determine if their businesses are eligible for the financial assistance and how such assistance may impact their businesses' finances today and in the future.

Furthermore, Employers who have already laid off employees or reduced salaries due to the COVID-19 emergency may want to reconsider their actions in order to take full advantage of the loan program.

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