CONGRESS PASSES 'CARES' ACT; DETAILS ON PAYCHECK PROTECTION LOANS

Congress has passed, and sent to the President for signature, the "Coronavirus Aid, Relief and Economic Security Act" legislation, commonly known as the CARES Act. The CARES Act is 880 pages long, and consists of several different Divisions and Titles. Division A Title I of the CARES Act increases authorized commitments for SBA Business loans to $349 billion under section 7(a) of the Small Business Act.

The CARES Act amends the Small Business Act by creating a new Business Loan Category under Section 7(a) of the SBA called the Paycheck Protection Program. The SBA either directly, or through currently approved lenders in the private sector will have the ability to make loans to businesses, thus side-stepping the current process to more quickly provide funding.

Paycheck Protection Program

For the period from February 15, 2020 to June 30, 2020 (covered period), the law allows the SBA to provide 100% federally-backed loans up to a maximum amount to eligible businesses to help pay operational costs like payroll, rent, health benefits/insurance premiums, interest, and utilities.

Eligible Loan Recipients

Eligible businesses for the new program include any "small business concerns" as currently defined under the SBA, as well as any business concern, nonprofit organization, veterans organization, or Tribal business if it employs not more than the greater of —

•500 employees (includes full-time, part-time, and those employed on other bases), measured on the date the loan proceeds are disbursed; or

•If applicable, the size standard in number of employees established by the Administration for the industry in which the entity operates.

There are special eligibility rules for businesses in the hospitality and dining industries. For businesses with more than one physical location, if 500 or fewer employees are employed per location AND assigned to "accommodation and food services" (NAICS sector 72), the business is eligible to receive a loan.

Sole proprietors, independent contractors, and eligible self-employed individuals (as defined in Congress's last COVID-19 bill, the Families First Coronavirus Response Act (Families First Act)) are eligible for loan recipients, subject to some documentation requirements to substantiate eligibility.

Maximum Loan Amount

The maximum loan amount is the lesser of:

1. The Sum of:

•2.5 times the average total monthly payroll costs incurred in the one-year period before the loan is made (or for seasonal employers the average monthly payroll costs for the 12 weeks beginning on February 15, 2019, or from March 1, 2019 to June 30, 2019), PLUS

•The outstanding amount of a loan made under the SBA's Disaster Loan Program between January 31, 2020 and the date on which such loan may be refinanced as part of this new program;
OR

2. Upon request, for businesses that were not in existence during the period from February 15, 2019 to June 30, 2019

•2.5 times the average total monthly payroll payments from January 1, 2020 to February 29, 2020, PLUS

•The outstanding amount of a loan made under the SBA's Disaster Loan Program between January 31, 2020 and the date on which such loan may be refinanced as part of this new program OR

3. $10 million.

General Loan Provisions

•No collateral or personal guarantee is required for a loan.

•The interest rate on loans under the program is not to exceed 4%.

•Loan proceeds not forgiven (see below) are payable over 10 years starting with the date of the application for loan forgiveness.

•There will be no fee associated with the loans and no prepayment penalty for any payments made.

•The Administrator has no recourse against any individual, shareholder, member, or partner of an eligible loan recipient for non-payment, unless the individual uses the loan proceeds for unauthorized purposes (see discussion below of permitted uses).

•Cannot be denied based on "credit elsewhere" meaning availability of credit from non-federal sources

In evaluating eligibility of borrowers, a lender must consider whether the borrower was operating on February 15, 2020 and had employees or independent contractors from whom the borrower paid.

A loan made under the SBA's EIDL Program on or after January 31, 2020, may be refinanced as part of a covered loan under this new program as soon as these new loans are made available. The CARES Act specifically allows SBA EIDL recipients with economic injury disaster loans made since January 31, 2020 for purposes other than the permitted loan uses under this program to receive assistance under this program.

Use of Proceeds

In general, businesses may, in addition to uses already allowed under the SBA's Business Loan Program, use the loans for:

•Payroll costs (excludes individual employee compensation above $100,000 per year, prorated for the covered period; certain federal taxes; compensation to employees whose principal place of residence is outside of the US; and sick and family leave wages for which credit is allowed under the Families First Act);

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

•Salaries, commissions, or similar compensations;

•Payments of interest on mortgage obligations;

• Rent/lease agreement payments;

•Utilities; and

•Interest on any other debt obligations incurred before the covered period.

Loan Forgiveness and Payment Deferral Relief

The CARES Act requires lenders to provide payment deferment relief (for principal, interest, and fees) for impacted borrowers for six months to one year. Lenders are required to provide such relief during the covered period.

In addition, the program loans qualify for the CARES Act's broader loan forgiveness provisions in Section 1106. Specifically, indebtedness is forgiven in an amount (not to exceed the principal amount of the loan) equal to the following costs incurred and payments made during the covered period:

•Payroll costs;

•Interest payments on mortgages;

•Rent; and

•Utility payments.

Forgiveness amounts will be reduced for any employee cuts or reductions in wages.

The reduction in forgiveness for reduced number of employees is calculated as follows:

•Total loan principal,

• Multiplied by a fraction calculated as:

o The average number of full-time equivalent employees (FTE) for the 8-week period beginning on the date of the origination of a covered loan,

o Divided by the average number of FTE for the period from February 15, 2019 thru June 30, 2019 (or at the election of the borrower, the average number of FTE for the period January 1, 2020 through February 29, 2020).

•For example, assume the following fact pattern:

Average FTE for 8-week period = 90
Average FTE for period February 15, 2019 thru June 30, 2019 = 100
Average FTE for the period January 1, 2020 thru February 29, 2020 = 80
Loan Principal = $500,000
Loan Principal forgiveness = $450,000, calculated as follows:
$450,000 = $500,000 (loan principal) x (90/100)

The reduction in forgiveness for reduced wages is calculated as follows:

•Reduction in total salary or wages of any employee during the covered 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 period (for purposes of this paragraph, "employee" is limited to those employees who did not receive during any single pay period during 2019 a salary or wage at an annualized rate of pay over $100,000).

There is relief from these forgiveness reduction penalties for employers who rehire employees or make up for wage reductions by June 30, 2020.

There is also a required process to apply for loan forgiveness. Borrowers seeking forgiveness of amounts must submit to their lender –

•Documentation verifying full-time equivalent employees (FTEE) on payroll and their pay rates;

•Documentation on covered costs/payments (e.g., documents verifying mortgage, rent, and utility payments);

•Certification from a business representative that the documentation is true and correct and that forgiveness amounts requested were used to retain employees and make other forgiveness-eligible payments; and

•Any other documentation the Administrator may require.

Forgiveness amounts that would otherwise be includible in gross income, for federal income tax purposes, are excluded.

Borrower Requirements

There are very few borrower requirements to obtain a loan under the new program. Those requirements include a good-faith certification that:

•The loan is needed to continue operations during the COVID-19 emergency;

•Funds will be used to retain workers and maintain payroll or make mortgage, lease, and utility payments;

•The applicant does not have any other application pending under this program for the same purpose; and

•From February 15, 2020 until December 31, 2020, the applicant has not received duplicative amounts under this program.