

# SHERIN<sup>AND</sup> LODGEN

## Overview of the CARES Act

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## Topics To Cover

- Paycheck Protection Program (PPP) and Other Financing Programs (including EIDL loans)
- Expansion of Unemployment Insurance Benefits
- Tax Relief

## Disclaimer

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# PPP

- Expansion of existing SBA loan program
- Loans made by banks and credit unions, and are fully guaranteed by the SBA
- Approximately \$350 billion
- For small businesses

## PPP - Eligible Businesses

- *Eligible businesses are any business concern, nonprofit, veterans organization or tribal business that:*
  - *Was in business on February 15, 2020*
  - *Employs not more than 500 employees, subject to industry specific exceptions*
  - *For businesses in “accommodation and food services” sector, such a business will be eligible if it employs not more than 500 employees **per physical location***
  - *Under Section 121.106 of existing SBA Regs (on how to count employees), employees obtained from a temporary employee agency or professional employee organization count*
  - *Under Section 121.106 of existing SBA Regs, part-time and temps count same as full-time*
  - *Revenue caps – Michael to add details*

## PPP - Eligible Businesses

- Sole proprietors/independent contractors/self-employed persons may also be eligible. Example: Lift / Uber Drivers
- *SBA affiliation rules for commonly controlled companies (rules requiring employee numbers to be viewed on aggregate basis) are waived for (i) hotels and restaurants (500 employees per location) and (ii) any entity operating as a franchisee (meaning that the SBA won't aggregate employees employed by franchisor or other franchisees).*
- *Certain other industries have special sizing limits under the SBA (cookie and cracker manufacturing / electric power distribution: 1,000 employees).*

# Underwriting

- Much lower than usual SBA standards
- SBA will not require personal guarantees or collateral (although lenders may)
- SBA will not determine repayment ability (although lenders may)
- Main SBA underwriting concerns are:
  - Making sure business was operational on February 15, 2020 and had workforce (i.e., paid salaries, payroll taxes or paid independent contractors)

# Underwriting

- Certification required from borrower that:
  - Loan is necessary due to uncertainty of current economic conditions caused by global COVID-19 pandemic to support borrower's ongoing operations
  - Acknowledging that the funds will be used to retain workers and maintain payroll or make mortgage, lease and utility payments and
  - That the borrower does not have an application pending for a loan under another SBA program for the same use and has not received such a loan



## Amount of Loan

- Maximum PPP loan amount is the lesser of \$10 million or 250% of employers average monthly payroll costs during one-year period prior to loan.
- With respect to payroll costs, such term is broadly defined to include:
  - Salaries, wages, commissions or similar compensation
  - Cash tips or equivalent
  - Group health care benefits (premiums / leave)
  - Retirement benefits
  - State and local taxes assessed on compensation

## Amount of Loan

- Sole proprietors and independent contractors can get their net income from business up to \$100,000 (pro-rated for relevant period).
- Exclusions from payroll costs:
  - Compensation for any individual over \$100,000 (just excess – we think)
  - Federal payroll taxes and income tax withholdings
  - Comp for any employee whose principal residence is outside the US
  - Sick or family leave wages for which a credit is available under the Families First Coronavirus Response Act

# Allowed Uses of PPP Loan

- The Act provides that proceeds from a PPP loan may be used for:
  - Payroll costs
  - The costs of the continuation of group health care benefits, insurance premiums, salaries, commissions, etc.
  - Payment of interest on any mortgage obligation (but not principal) – effective 2/15/20
  - Rent – lease effective 2/15/20
  - Utilities – service effective 2/15/20
  - Interest (but not principal) on any debt obligation - effective 2/15/20

# Debt Forgiveness

- PPP debt forgiveness provisions convert loan into a grant
- Must spend loan on specified expenses (see prior slide) during 8 week period after the loan is originated
- Not more than loan amount (seems obvious)
- No adverse tax consequence from debt forgiveness
- “Strings attached....”

## Debt Forgiveness

- Look at amount of specified expenses during 8 weeks after PPP loan is disbursed
- Then, there may be 2 negative adjustments:
  - First for employee headcount (FTEs)
  - Second for reduction in total salary or wages of any employee during the 8 week period that is in excess of 25% of the total salary or wages of the employee during the most recent full quarter during which the employee was employed (assuming employee's annualized salary does not exceed \$100K).
  - To the extent FTE reduction or compensation reduction occurs between 2/15/2020 and 4/26/2020, the negative adjustments can be eliminated by “curing” the FTE reduction or compensation adjustment on or before June 30, 2020.

# Debt Forgiveness

- Not clear how the “cure” works
- Negative reduction in debt forgiveness re: FTEs works as follows:
  - A baseline is established by borrower choosing average number of FTEs per month by borrower during period (i) beginning on 2/15/19 and ending on 6/30/19 or (ii) 1/1/20 and ending on 2/29/20
  - Baseline is denominator
  - Numerator is average FTEs employed by borrower during 8-week covered period

# Debt Forgiveness

- Example:
  - Assume PPP Loan of \$1,000,000
  - Assume borrower's qualifying expenses are \$800K
  - Assume borrower's FTEs during 8 week period is 75% of baseline FTEs
  - Maximum amount of debt forgiveness is \$600,000, which is 75% of \$800,000
  - Assumes employer does not, on or before 6/30/20, "cure" the FTE reductions that occurred prior to 4/26/2020
  - For 25% comp reductions, the negative adjustment is dollar for dollar

# Loan Applications

- Treasury and the SBA have 15 days from the date on which the CARES Act was enacted (March 27, 2020) to provide rules to allow businesses to access funds.
- Secretary Mnuchin said on March 29, 2020 that he expects the rules to be available by April 3, 2020
- The necessary application forms for the PPP have not yet been released by the SBA. Expected to be similar to SBA form 1919
- Michael Kuhn to advise
- Timing? Next steps?



# Loan Applications

- Contact banks
- Existing banks may give preference to existing customers
- If existing bank is not participating in PPP, look for SBA preferred lender
- Be patient
- Lender will probably not fund until SBA confirms they will guarantee it
- 60 days after application, lender required to make a decision on debt forgiveness
- Once SBA guarantees hit \$349 billion, a small business not already approved may not be able to get funding unless Congress expands program

# Loan Applications

- Get schedule of employees (confirming sizing is correct) and payroll costs documentation ready
- Prepare worksheet calculating loan amount
- P&L for 2019 (if available)

## Other Loans

- Economic Injury Disaster Loans (EIDL)
- EIDLs are made directly by the SBA
- Timing may be longer than PPP Loans (funding may take 4-6 weeks, but bridge loans are possible, up to \$25K)
- No sizing formulas
- \$2,000,000 cap.
- Money to meet financial obligations which could have been met but for COVID-19
- Up to 30 year term and 3.75% interest rate

## Other Loans

- Can't receive EIDL and PPP loan *for same purpose*
- But, *can* apply for both. OK to use PPP for payroll; EIDL for inventory
- Existing EIDL's can be refinanced with PPP loans
- Emergency advances of \$10K payable w/i 3 days
- No need to refund if application denied.
- \$10K is subtracted from debt forgiveness in PPP loans
- Money to meet financial obligations which could have been met but for COVID-19
- Up to 30 year term and 3.75% interest rate

## Other Loans

- We note that the Act provides for additional emergency loans to small and mid-size business
- Mid-size businesses have 500 to 10,000 employees
- These loans are not forgiven like PPP loans
- Funds are used to retain 90% of recipients workforce (different program have different requirements)
- No dividends or buybacks while loan is outstanding
- Lots of other requirements, we don't have time to cover

# Unemployment Benefits Expansion

- The CARES Act substantially increases the unemployment assistance available to laid-off or reduced hours employees
- Extends benefits for all eligible workers through December 31, 2020
- Allows workers to collect unemployment benefits who would not traditionally be eligible (for example, self-employed workers and independent contractors)
- In addition, until July 31, 2020, the federal government will pay “eligible recipients” an additional \$600 per week in excess of amounts otherwise paid under state programs

# Unemployment Benefits Expansion

- Finally, through December of 2020, the CARES Act provides 50% of the cost of any state “short-time compensation” programs, which are programs designed to allow employers to reduce their workforce without laying workers off
- Under such programs, employees who have had their hours reduced as a result of COVID-19 receive pro-rated unemployment benefits

# Tax Relief

- Employees are not taxed on:
  - Covid related reimbursements, including expenses to allow employees to work at home (Section 139)
  - An employer's direct payments of employee student loans up to 5,250 per year
- 4/15/20 filing and paying deadline delayed to 7/15. Note - Massachusetts does not permit C corporations and trusts to defer, only individuals. Some clients are going to double up on 6/15 estimates which were not delayed.



# IRA/qualified plans

- Corona related withdrawals:
  - Under 59.5 – withdrawals up to \$100,000 - no 10% penalty.
  - All taxpayers - no income tax deferred for up to 6 years. Three years to repay; amounts not repaid are taxable over the next 3 years.
- Waiver of required minimum distributions in 2020. Does not appear to apply to defined benefit plans
- Limit on loans from qualified plans increased from \$50,000 to \$100,000 for the period 3/27 – 9/27+/-.

# Tax Credits

- Tax credits for Covid mandated sick and family leave pay for employees who are not working:
  - Per employee limits are:
    - If employee is sick - \$511 per day for 10 days = \$5,111
    - If employee is a care provider 2/3 of salary up to \$200 per day for 10 days = \$2,000
- This does not apply if you obtain a Paycheck Protection Program (PPP) loan

# Tax Credits

- Employee retention credit –
- Who qualifies? Employers that have either (i) shut down or partially shut down or (ii) have had a 50% drop in sales, comparing 2020 quarters to corresponding 2019 quarters and (iii) do not take a PPP loan
- Qualifying employers are entitled to a credit for wages paid to retained employees
- The credit is 50% of wages per employee limited to \$10,000 of wages (max credit is \$5,000 per employee)
- For employers with over 100 employees the credit only applies to employees not working due to Covid related circumstances

## Other Changes

- The business interest limitation is increased from 30% of adjusted taxable income to 50% 2019-2021
- Repeal of 250,000/500,000 excess business loss limitation for 2018 - 2020
- IRS rebates - \$1,200 if single, \$2,400 if married plus \$500 for each qualifying child
- Rebates are phased-out based on taxpayer's income
- Single \$75,000 - \$150,000
- Married- \$99,000 – \$198,000
- A new \$300 charitable contribution deduction for taxpayers who do not itemize

## Other Changes

- Employers can defer the 6.2% Social security tax for payroll 3/27/20 -12/31/20
- Taxes deferred are due 50% on 12/31/21 and 50% on 12/31/22
- Businesses who obtain a PPP loan are not eligible for this deferral
- Five year carryback for 2018, 2019 and 2020 net operating losses (NOLs)
- Finally, the technical correction we have all been waiting for - businesses and landlords can claim bonus depreciation on qualifying leasehold improvements made since 2018

# Tax Planning

- With the retroactive technical correction of bonus depreciation, consider amending 2018 (and 2019 if filed) to claim bonus depreciation return or consider a change in method of accounting to claim bonus depreciation on 2020 tax returns. Partnership returns that could not or did not elect out of BBA (centralized audit procedures) cannot amend
- This probably does not apply to hotels and restaurants, but other businesses with sales under \$25,000,000 should consider switching from the accrual basis to cash basis