Title I of the CARES Act: The Paycheck Protection Program and Loan Forgiveness Provisions

Client Alert

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Among the many significant provisions of the Coronavirus Aid, Relief and Economic Security Act (CARES Act), signed into law on March 27, 2020, are the paycheck protection program and the terms and conditions for loan forgiveness included under Title I of the Act - the "Keeping American Workers Paid and Employed Act."

The following summarizes these two critical provisions of Title I, which offer a positive financial opportunity for many employers that should be seized upon quickly.

Paycheck Protection Program

Section 1102 of Title I authorizes $349,000,000,000 for small business disruption loans. These loans will be administered by the Small Business Administration (SBA) and funded through SBA lenders, with regulations and guidance to be forthcoming from the SBA by April 26, 2020.

- Who Can Apply and Application Deadline
  - Generally speaking, during the period beginning on February 15, 2020 and ending on June 30, 2020, any business concern, nonprofit organization, veterans organization, or Tribal business concern is eligible to receive a covered loan if it employs not more than 500 employees, whether employed on a full-time, part-time or other basis.
  - There are additional specific provisions for sole proprietorships, independent contractors and self-employed individuals, for employers with more than one location, and for the relaxation of affiliation rules
  - As these loans must be originated by June 30, time is of the essence to gather the required information and submit an application through your bank's SBA department.
- Determining Eligibility
  - Lenders will determine eligibility by evaluating whether the business was in operation on February 15, 2020, had employees for whom the borrower paid salaries and payroll taxes, or paid independent

contractors.

- Loan Size
  - For businesses operating between the period of February 15, 2019 and June 30, 2019, the maximum loan is the lesser of $10,000,000 or the sum of (i) the product obtained by multiplying the average total monthly payments for payroll costs incurred during the 1-year period before the date on which the loan is made by 2.5 plus (ii) certain loans previously made beginning January 31, 2020. The time period is subject to adjustment for seasonal businesses.
  - For businesses that were not operating between February 15, 2019 and June 30, 2019, the maximum loan is the lesser of $10,000,000 or 250% of average monthly payroll costs for the period between January 1, 2020 and February 29, 2020.

- Payroll Costs
  - Payroll costs include: (i) compensation (salary, wages, commissions or similar compensation, payment of cash tips or equivalent; (ii) payment of vacation, parental, family, medical or sick leave; (iii) allowance for dismissal or separation; (iv) payment for group health care benefits, including insurance premiums; (v) payment for retirement benefits; and (vi) payment of any state and local tax assessed on the compensation of employees.
  - Payroll costs do not include: (i) compensation to an employee in excess of $100,000; (ii) taxes imposed or withheld under chapters 21, 22 and 24 of IRS code during the covered period; (iii) compensation for employees whose principal residence is outside US; (iv) qualified sick leave wages and qualified family leave wages for which a credit is allowed under sections 7001 and 7003 of the Families First Coronavirus Response Act.

- Use of Loan Proceeds
  - Loan proceeds may be used for: (i) payroll costs; (ii) costs related to group health care benefits during periods of paid sick, medical or family leave and insurance premiums; (iii) employee salaries, commissions or similar compensation (subject to the exclusions referred to above); (iv) rent (including rent under a lease agreement); (v) utilities; (vi) interest on any mortgage obligations (but not principal or loan prepayments); (vii) interest on any other debt obligations incurred before February 15, 2020; and (viii) certain other permitted purposes, such as working capital and equipment purchases; however, that portion is not subject to the loan forgiveness provisions of the program.

- Loan Terms - Generally
  - The loan is for a maximum period of 10 years from the date of the application for loan forgiveness, unless it is forgiven pursuant to the loan forgiveness provisions of the legislation.
  - Interest may not exceed 4%; there are no loan fees to the borrower, or prepayment fees or charges; there is no requirement to show an inability to obtain credit elsewhere; there are no guaranties or other collateral requirements; and the loan is non-recourse.
  - Applications are self-certified. To the extent that the loan is not forgiven, then there will be a deferment of the obligation to repay the loan that may range from a minimum of 6 months to a year.

Loan Forgiveness Terms and Conditions

Section 1106 of Title I provides terms and conditions for loan forgiveness under the CARES Act.

- Generally

- The amounts forgiven will be considered cancelled indebtedness but will be excluded from gross income.
- The expected forgiveness amount means the amount of principal a lender reasonably expects a borrower to expend during the 8-week period beginning on the date of the origination on the sum of: (i) payroll costs (as defined above); (ii) interest on a mortgage obligation (not including principal or a prepayment of principal) incurred in the ordinary course of business, on real or personal property, before February 15, 2020; (iii) payments of rent under a leasing agreement in force before February 15, 2020; and (iv) utility payments (electricity, gas, water, transportation, telephone, or internet access) for service that began before February 15, 2020.

- Forgiveness
  - To apply for loan forgiveness, the eligible recipient must submit to the lender an application with the materials listed below, and should expect to receive a response within 60 days:
    - Documentation verifying the number of full-time employees on payroll and pay rates (for the relevant period with respect to reductions discussed below), including payroll tax filings and state income, payroll and unemployment insurance filings;
    - Documentation, including cancelled checks, payment receipts, transcripts of accounts or other documents verifying payments on mortgage obligations, lease obligations and utility payments;
    - A certification from a representative of the eligible recipient authorized to make such certifications that the documentation is true and correct and the amount for which forgiveness is requested was used to retain employees, make interest payments on a covered mortgage obligation, make payments on a covered rent obligation, or make covered utility payments; and
    - Such other documentation as the administrator determines necessary.
  - The loan forgiveness cannot exceed the principal amount of the loan. The amount that may be forgiven is subject to reduction based on a reduction in the number of employees and the amount of any reduction in total salary or wages, as outlined below.
  - Reduction Based On Reduction in Number of Employees: The amount of the loan forgiveness will be reduced (but not increased) by multiplying the amount eligible for forgiveness by a quotient obtained by dividing the average number of full time equivalent employees per month employed by the eligible recipient during the 8-week period beginning on the date of the origination, by (at the election of the borrower):
    - The average number of full-time equivalent employees per month employed during the period beginning on February 15, 2019 and ending on June 30, 2019, or
    - The average number of full-time equivalent employees per month employed during the period beginning on January 1, 2020 and ending on February 29, 2020, or
    - For an eligible recipient that is a seasonal employer, the average number of full-time equivalent employees per month employed during the period beginning on February 15, 2019 and ending on June 30, 2019.
    - Full time equivalent employees are determined by calculating the average number of full-time equivalent employees for each pay period falling within a month.
  - Reduction Relating to Salary and Wages: The amount of loan forgiveness will also be reduced by the amount of any reduction in total salary or wages of any employee (who did not receive during any single pay period during 2019, wages or salary at an annualized rate of pay greater than $100,000) during the Covered 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 before the Covered Period. An eligible recipient with tipped employees may receive forgiveness for additional wages paid to those employees.

- Exemption for Re-Hires: The amount of loan forgiveness will be determined without regard to a reduction in the number of full time equivalent employees or a reduction in the salary of 1 or more employees that occurred during the period beginning on February 15, 2020 and ending on April 26, 2020.
  - if there is a reduction in full time equivalent employees during that period from what was existing on February 15, 2020, and the reduction is eliminated no later than June 30, 2020, or
  - if there is a reduction in salary or wages during that period from what was existing on February 15, 2020, and the reduction is eliminated no later than June 30, 2020.

The provisions of the CARES Act are very complex, and the above is intended to provide only a general overview of the legislation. We welcome your questions and are ready to work with you to evaluate your specific needs and discuss how you can best approach the financial opportunity that the Act affords.

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