

CARES Act: Small Businesses

March 27, 2020

On March 27, 2020, Congress passed and President Donald Trump signed into law the \$2.2 trillion "Coronavirus Aid, Relief, and Economic Security Act" (CARES Act) legislation aimed to provide economic relief from coronavirus effects on individuals, families, small businesses and severely impacted sectors of the U.S. economy.

The CARES Act includes many provisions for small business, including:

(I) the paycheck protection program,

(II) economic injury disaster loans (EIDLs) and emergency grants,

(III) loan payment subsidies, and

(IV) education, training and assistance grants to small business development centers, women business centers and minority business centers.

1. Paycheck Protection Program

The CARES Act includes a new "paycheck protection program" which amends section 7(a) of the Small Business Act (15 U.S.C. 636(a)) (SBA Act) to significantly increase funding, expand flexibility and ease and speed access to loans and loan guarantees through the SBA's loan guaranty program.

Covered loans, loan guarantees and covered period: "Covered loans" under the paycheck protection program are loans made under the program during the "covered period" (February 15, 2020 - June 30, 2020). The Administrator (Administrator) of the Small Business Administration (SBA) is generally permitted to guarantee covered loans under the same terms, conditions and processes as applicable to loans covered under section 7(a) of the SBA Act. The CARES Act permits the Administrator and the Secretary of the Treasury (Secretary) to authorize additional lenders to make covered loans.

Covered loans are to bear interest not to exceed 4%. Covered loans with remaining balances after loan forgiveness in accordance with the loan forgiveness features of the CARES Act (see "[Limited loan forgiveness for covered loans](#)" below) will continue to be guaranteed by the Administrator and have a maximum maturity of 10 years from loan forgiveness application date.

Certain loans made during the period of January 31, 2020, to the date on which covered loans may be made available under the paycheck protection program may be refinanced as part of a covered loan.

Eligibility for covered loans: Eligibility for loans under the paycheck protection program during the covered period includes the following:

- Any business concern, 501(c)(3) non-profit organization, 501(a) veterans organization or tribal business concerns described in section 31(b)(2)(C) of the SBA, which employs not more than the greater of 500 employees or the size standard in number of employees for the industry established by the Administrator (for this purpose all full time and part-time employees and others employed on any other basis are counted)

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- Certain individuals (sole proprietors, independent contractors and eligible self-employed individuals as defined in the Families First Coronavirus Response Act)

Of special note, accommodation and food services businesses (those with NAISC codes beginning with 72) with multiple physical employment locations are now eligible for covered loans provided that the business concern does not employ more than 500 employees per physical location.

During the covered period, the affiliation provisions of the SBA Act are waived as to eligibility for a covered loan for accommodation and food services businesses, franchise businesses assigned a franchise identifier code by the Administrator, and businesses receiving financial assistance under section 301 of the Small Business Investment Act.

The only two factors to be considered by the lender in evaluating a prospective borrower's eligibility for a covered loan are whether the prospect was in operation as of February 15, 2020, and had employees paid salaries and payroll taxes or paid independent contractors reported on federal tax 1099 forms.

An eligible recipient must make a good faith certification that the uncertainty of current economic conditions makes the loan request necessary to support ongoing operations; that the funds will be used to retain workers and maintain payroll or make mortgage, lease or utility payments; that the eligible recipient does not have an application pending for a covered loan for the same purpose and duplicative of amounts applied for or received under a covered loan; and during the period of February 15, 2020 – December 31, 2020, that the eligible recipient has not received amounts under the payroll protection program for the same purpose and duplicative of amounts applied for or received under a covered loan. The eligible recipient must also maintain an average monthly number of full-time equivalent (FTE) employees during the covered period of not less than the number during the applicable period described below under "*Maximum loan amount of covered loans and express loans.*"

With regard to the paycheck protection program, certain other SBA 7(a) loan requirements have been suspended during the covered period including the inability of the business concern to obtain credit elsewhere, the requirement for a personal guarantee and the requirement for collateral.

These changes are expected to substantially increase eligibility and availability and streamline the application process for covered loans.

Maximum loan amounts of covered loans and express loans: The maximum loan amount for covered loans during the covered period is the lesser of \$10 million or an amount equal to the sum of:

- 2.5 times the average total monthly payment for eligible payroll costs incurred during the one-year period before the covered loan date (except in the case of seasonal employers, the eligible recipient may elect for the period to be the 12-week period beginning February 15, 2019, or March 1, 2019 - June 30, 2019, and in the case of an otherwise eligible recipient of a covered loan that was not in business during the period of February 15, 2019 - June 30, 2019, can instead elect the period of January 1, 2020 - February 29, 2020); and
- The outstanding amount of a loan that was made during the period of beginning January 31, 2020, and ending on the date on which covered loans are available to be refinanced under a covered loan.

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Eligible payroll costs include the following:

- *Payments of employee compensation* (salary or wages; cash tips or equivalent; vacation, parental family, medical or sick leave; allowances for dismissal or separation; payments for group health care benefits (including insurance premiums); retirement benefits and state and local taxes assessed upon compensation of employees)
- *Payments to a sole proprietor or independent contractor* (wages, commissions or similar compensation of not more than \$100,000 in a year (prorated for the covered period))

Eligible payroll costs do not include any of the following:

- Annual compensation of an individual exceeding \$100,000 (prorated for the covered period)
- Certain taxes imposed or withheld (chapters 21, 22 or 24 of the Internal Revenue Code)
- Compensation of any employee whose principal residence is outside the United States
- Qualified sick leave and family leave wages credited under the Families First Coronavirus Response Act

The maximum loan amount for SBA express loans has been increased from \$350,000 to \$1 million. The increase in the maximum amount for express loans will be automatically repealed effective January 1, 2021.

Permitted uses of the proceeds of covered loans: The permitted uses of the covered loans proceeds during the covered period include the following:

- Payroll costs (see above description of eligible and ineligible costs); continuation of group health benefits during paid sick, medical or family leaves (and insurance premiums); employee salaries, commissions and similar compensation
- Mortgage, rent and utilities payments made during the covered period under agreements in existence at the start of the covered period
- Interest on any other debt incurred *before* the covered period.

Waiver of loan guarantee fees during the covered period: SBA loan guarantee fees are waived during the covered period. SBA loan guarantee fees for loans with maturities exceeding 12 months are based on a graduated percentage 2% - 3.75% depending on the loan guarantee amount, and SBA loan guarantee fees for loans with maturities of one year or less are 0.25%.

Complete loan payment deferrals of up to one year: Lenders are required to provide complete payment deferrals for impacted borrowers (in this case, eligible borrowers in operation on February 5, 2020, which have a covered loan application that is approved or pending approval on or after the date of enactment of the CARES Act) for a period of not less than six months and not more than one year. The SBA is to provide payment deferral process guidance to lenders within 30 days of the enactment of the CARES Act.

In order to implement the payment deferral provisions in the case where an investor declines to approve a requested deferral for a covered loan sold on the secondary market, the SBA is required to purchase the covered loan so the impacted borrower may receive the deferral of not less than six months and not more than one year. The deferral

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provisions also provide that covered loans are not eligible to be sold in the secondary market until the loan recipient has requested loan forgiveness (see “*Limited covered loan forgiveness*” below) and the Administrator has determined the forgiveness amount. Any remaining balance of the covered loan may then be sold on the secondary market.

Limited loan forgiveness for covered loans: Eligible recipients of a covered loans will be eligible for forgiveness of indebtedness on the loans (not to exceed the principal amount of the financing) equal to the payments made during the eight-week period beginning on the origination date of the covered loan (covered period) in an amount equal to the total amount of the following payments:

- Payroll costs (see eligible and ineligible payroll costs outlined under “*Maximum loan amount of covered loans and express loans*” above)
- Interest on any covered mortgage obligation (real or personal property incurred before February 15, 2020)
- Any covered rent obligations (rent under a leasing arrangement in force before February 15, 2020)
- Any covered utility payment (electricity, gas, water, transportation, telephone or internet access which service began before February 15, 2020)

Reductions in loan forgiveness amounts for employment and compensation reductions: The forgivable amounts are to be reduced for reductions in employment (numbers of employees) and compensation levels during the covered period subject to the re-hires exemption described below.

The reduction based on the number of employees is to be determined by multiplying the forgiveness amount as described above by the quotient of (a) the average number of FTE employees per month employed during the covered period, divided by (b) the average number of FTE employees employed during February 15, 2019 through June 30, 2019 (except that if the eligible recipient was not in operation before that period, the measurement period is changed to January 1, 2020 through February 29, 2020 and in the case of a seasonal employer, the measurement period is February 15, 2019 - June 30, 2019). The average number of FTE employees is to be determined by the average number of FTE employees for each pay period within the month.

The reduction in compensation is to be the amount of any reduction in total salary or wages of any employee (other than an employee who received wages or salary at an annualized rate exceeding \$100,000 in any pay period during 2019) exceeding 25% of the total salary or wages during the most recent full quarter before the covered period.

The reductions in the loan forgiveness amount for reductions in numbers of FTE employees or compensation during the February 15, 2020, through 30 days after the date of enactment of the CARES Act do not apply if the eligible recipient has eliminated the reductions not later than June 30, 2020 (referred to as the “re-hire exemption”).

Loan forgiveness applicable to tipped employees: Eligible recipients with tipped employees (as described in the Fair Labor Standards Act) may receive forgiveness for additional wages paid to those employees.

Payment of forgiveness amount: The amount of forgiveness plus accrued interest is to be paid by the Administrator to the lender within 90 days of determination of the forgiveness amount. In addition, the Administrator is required to purchase the expected forgiveness amount from a lender as to particular covered loans or pools of covered loans if requested by the lender in a report as required by the forgiveness provisions. The Administrator is required to complete

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the purchase within 15 days after receipt of the required report from the lender.

Treatment of loan forgiveness amounts: The amounts forgiven are to be treated as cancellation of indebtedness by a lender for purposes of the SBA Act and will not be included in gross income for federal tax purposes.

Applications for loan forgiveness: An eligible recipient seeking loan forgiveness must submit an application to the originating lender of the covered loan. Applications must be accompanied by certain required documentation and the applicant must certify that the requested loan forgiveness was used to retain employees make interest payments on covered mortgage obligations, covered rent obligations or to make covered utility payments. Decisions by lenders are required within 60 days of receipt of the application.

2. EIDLs and Emergency Grants

The CARES Act expands the group of individuals and entities eligible for EIDLs and emergency grants.

Eligible entities and covered period: The parties eligible for economic injury disaster loans (EIDLs) under section 7(b)(2) of the SBA Act have been expanded during the covered period to include the following individuals and entities:

- A business with not more than 500 employees
- Any individual operating as a sole proprietorship or independent contractor
- A cooperative with not more than 500 employees
- An ESOP (as defined under the Small Business Act)
- A tribal business concern

The covered period for these loans and emergency grants is January 31, 2020 - December 31, 2020.

Certain requirements otherwise applicable to EIDLs under section 7(b)(2) of the SBA Act do not apply to loans made in response to COVID-19 during the covered period. These include:

- All personal guarantees on advances and loans not exceeding \$200,000
- The requirement that the applicant must be in business at least one year for a business not in operation on January 31, 2020
- The requirement that the applicant be unable to obtain credit elsewhere

The requirements for the evaluation of the creditworthiness of an applicant for an EIDL during the covered period may also be limited by a lender to the applicant's credit score (and the lender need not require tax returns or transcripts) or other appropriate methods to determine ability to repay.

Emergency EIDL grants (advances): An eligible entity that applies for an EIDL during the covered period may request an advance not to exceed \$10,000 to be made within three days after submitting the application. The advance may be used, in addition to any other allowable purpose under section 7(b)(2) of the SBA Act, for any of the following:

- Providing COVID-19 related sick leave

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- Maintaining payroll during disruptions or substantial slowdowns
- Meeting increased material costs due to supply chain interruptions
- Rent or mortgage payments
- Obligations that cannot be met due to revenue losses

Notably, the CARES Act provides that the recipient of such an advance is not required to repay any amount of the advance.

3. Loan Payment Subsidies

The CARES Act provides for loan payment subsidies for covered eligible loans.

Covered loans eligible for subsidies: The covered loans eligible for subsidies are the following:

- Loans guaranteed under section 7(a) of the SBA Act including specifically the Community Advantage Pilot Program but excluding loans under the paycheck protection program
- Loans under Title V of the Small Business Investment Act
- Loans made by intermediaries to a small business concern under section 7(m) of the SBA Act

Subsidies for covered loan payments: The Administrator is required to pay principal, interest and associated fees owed on a covered loan in a regular servicing status to be applied against the loans as follows:

- For the 6-month period beginning with the next payment due for a covered loan made before the enactment of the CARES Act which *is not on deferment*
- For the 6-month period beginning with the next payment due after deferment for a covered loan made before enactment of the CARES Act which *is on deferment*
- For the 6-month period beginning with the first payment due for a covered loan made during the period of the date of enactment of the CARES Act through the date that is six months after enactment

The subsidies are to be paid by the administrator not later than 30 days after the date the first payment is due.

Other requirements: The Administrator is required to communicate and coordinate with federal and state banking authorities to encourage them to not increase lender reserves on account of receiving subsidy payments. The Administrator is also required to waive maximum loan maturity requirements for covered loans in the case of lender deferrals and extensions during the one year period following the CARES Act enactment date of the CARES Act and extend lender site visit requirements if necessary due to travel restrictions or difficulties from the COVID-19 pandemic.

4. Grants to Resource Partners, Resource Partner Associations and Minority Business Centers for Education, Training and Advising Services to Covered Small Business Concerns

The CARES Act increases funding for coronavirus education, training and advising of small businesses through small business development, women's business and minority business centers.

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Grants to resource partners: The CARES Act provides for grants that may be awarded to resource partners to provide education, training and advising to covered small business concerns. The “resource partners” eligible for the CARES Act grants are “small business development centers” and “women’s business centers” (as each is defined in the SBA). There are 63 lead small business development centers and more than 100 women’s business centers in the US. See <https://www.sba.gov/offices/headquarters/osbdc/about-us> for more information about small business development centers and see <https://www.sba.gov/offices/headquarters/wbo> for more information about women’s business centers.

Grants to resource partner associations: Grants may also be made under the CARES Act to “resource partner associations.” These are associations representing resource partners to establish a hub for COVID-19 information including online platform and training programs for resource partners.

Grants to minority business centers: Grants may also be made to “minority business centers” of the Minority Business Development Agency of the Department of Commerce to provide education, training and advising to covered small business concerns. For additional information about the Minority Business Development Agency, see <https://www.mbda.gov/>.

Covered small business concerns: Covered small business concerns are small business concerns under the SBA Act that are located in an area that is “substantially affected by COVID-19.” Substantially affected by COVID-19 is defined to mean that the covered small business concern has experienced supply chain disruptions, staffing challenges, decreases in sales or customers, or a closure.

Permitted uses of CARES Act grants: The grants awarded under the CARES Act are to be used for education, training and advising of covered small business employees on COVID-19 business practices to mitigate the economic effects of COVID-19 or similar occurrences, including the following:

- Accessing and applying for capital and business resiliency resources from the SBA and other Federal sources
- COVID-19 and other communicable diseases hazards and transmission prevention
- The potential and mitigation of effects on supply chains and the distribution and sale of products of COVID-19
- Telework practices to reduce possible transmission of COVID-19
- Remote customer service practices
- Risks and mitigation of cyber threats from those practices
- Mitigation of effects of reduced travel or outside activities relating to COVID-19

No matching funds are required for CARES Act grants: Matching funds are not required for these CARE Act grants. Also, and more broadly, during the three-month period beginning on the effective date of the CARES Act, any requirement for matching funds from non-Federal sources under the Women’s Business Center Program (section 29(d)(1) of the Small Business Act) is waived for any recipient of such assistance.

Goals and Metrics for CARES Act grants: The goals and metrics for the grants are to be developed taking into consideration the spread of COVID-19 or similar occurrences affecting covered small business concerns in the areas covered by the resource partner particularly in rural or economically distressed areas; the use of the permitted grant funding (with flexibility in responding to unique situations); and encouraging resource partners to develop and provide

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services to covered small business concerns.

This is part of a series of our COVID-19 alerts providing clients with practical advice on measures they can take to navigate through these troubled times. Please contact the authors or your Miller Canfield attorney with further questions.

This information is based on the facts and guidance available at the time of publication, and may be subject to change.