

CARES Act Summary and Analysis

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CARES Act – H.R. 748

Sweeping legislation to respond to the COVID-19 pandemic was cleared by Congress and signed into law by President Trump on March 27, 2020. The Coronavirus Aid, Relief, and Economic Security Act (“the CARES Act” or “the Act”) authorizes more than \$2 trillion to battle COVID-19 and its economic effects, including immediate cash relief for individual citizens, loan programs for small business, support for hospitals and other medical providers, and various types of economic relief for impacted businesses and industries.

Title I – Keeping American Workers Paid and Employed Act

The Paycheck Protection Program: The Paycheck Protection Program enacted under the CARES Act provides increased loan amounts for eligible small businesses for payroll obligations, emergency grants to cover immediate operating costs, and a mechanism for loan forgiveness where the small business can demonstrate that the loan proceeds were used for payroll and related costs. Title I provides \$349 billion for relief during the covered period from February 15, 2020 to June 30, 2020 through a number of changes to the loan programs that currently exist and are administered by the Small Business Administration (SBA).

Small Businesses: So-called Section 7(a) loans are the primary SBA vehicle for providing capital to small businesses. Small businesses¹ are defined by the Act to include business concerns, nonprofit organizations, veterans organizations or tribal businesses provided that such entity employs not more than the greater of (i) 500 employees (which includes full time and part time employees) or, if applicable, (ii) the size standard in number of employees established by the SBA for the industry in which such entity operates.

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Source: The Reed Smith Coronavirus team includes multidisciplinary lawyers from Asia, EME and the United States who stand ready to advise you on these issues or others you may face related to COVID-19. For more information on the legal and business implications of COVID-19, visit the Reed Smith Coronavirus (COVID-19) Resource Center or contact Reed Smith at COVID-19@reedsmith.com.

¹The term “small business concern” has the meaning given to such term in 15 U.S.C. section 636.

Section 7(a) Borrowers: An eligible recipient applying for a covered loan under the CARES Act must make a good faith certification, that, among other things: (i) the current economic conditions and uncertainty make the loan request necessary to support the recipient's business operations; (ii) the funds from such covered loan will be used to retain workers, maintain payroll, or make mortgage, lease or utility payments; (iii) the recipient does not have another loan application pending under the CARES Act; and (iv) the recipient has not received amounts under the CARES Act for the same purpose before December 31, 2020 and was in operation as of February 15, 2020.

Loan Forgiveness: Any portion of the Section 7(a) loan used to maintain payroll, provided workers stay employed through to the end of June 2020, will be forgiven in an amount equal to the sum of the following costs incurred and payments made during the eight-week period beginning on the date of the origination of a covered loan: (i) payroll costs; (ii) interest payments on mortgages; (iii) covered rent obligations; and (iv) covered utility payments. The amount of forgiveness may not exceed the principal amount made available under the covered loan. Small businesses and other eligible entities will be able to apply if they experienced impacts related to the COVID-19 pandemic between February 15, 2020 and June 30, 2020. Loan forgiveness applies only to Section 7(a) loans and does not apply to EIDLs (discussed below).

Economic Injury Disaster Loans (EIDLs): The Act expands the SBA's EIDL program. EIDLs are loans available to small business borrowers that have suffered economic injury as a result of a pandemic or other disaster. Eligibility for an EIDL is limited to small business. The small business qualification attributes discussed above for Section 7(a) loans are generally applicable to EIDLs; however, it does not appear that the relief from affiliation rules (such as for borrowers in the accommodation and food services industries) for Section 7(a) loans applies to EIDLs. In addition to being a small business, the EIDL borrower must (i) be located in a declared disaster area; (ii) have suffered "substantial economic injury"⁴ as a direct result of a declared disaster; and (iii) not own property subject to a federal judgment lien. EIDL amounts are generally limited to \$2 million. Personal guaranty requirements are waived for loans of \$200,000 and less. The Act does not specify any changes to existing collateral requirements (collateral is generally required for EIDLs of more than \$25,000), so it would appear that they continue to apply.



The CARES Act authorizes more than \$2 trillion to battle COVID-19 and its economic effects, including immediate cash relief for individual citizens.

⁴13 C.F.R. Section 123.300(a) (a substantial economic injury means that a business concern is unable to meet its obligations as they mature or to pay its ordinary and necessary operating expenses. Loss of anticipated profits or a drop in sales is not considered substantial economic injury for this purpose).

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The Small Business Owner's Guide to the CARES Act

CARES Act Small Business FAQ

What types of businesses and entities are eligible for a Payment Protection Program (PPP) loan?

- Businesses and entities must have been in operation on February 15, 2020.
- Small business concerns, as well as any business concern, a 501(c)(3) nonprofit organization, a 501(c)(19) veterans organization, or Tribal business concern described in section 31(b)(2)(C) that has fewer than 500 employees, or the applicable size standard in number of employees for the North American Industry Classification System (NAICS) industry as provided by SBA, if higher.
- Individuals who operate a sole proprietorship or as an independent contractor and eligible self-employed individuals.
- Any business concern that employs not more than 500 employees per physical location of the business concern and that is assigned a NAICS code beginning with 72, for which the affiliation rules are waived.
- Affiliation rules are also waived for any business concern operating as a franchise that is assigned a franchise identifier code by the Administration, and company that receives funding through a Small Business Investment Company.

How is the loan size determined?

Depending on your business's situation, the loan size will be calculated in different ways (see below). The maximum loan size is always \$10 million.

- If you were in business February 15, 2019 – June 30, 2019: Your max loan is equal to 250 percent of your average monthly payroll costs during that time period. If your business employs seasonal workers, you can opt to choose March 1, 2019 as your time period start date.
- If you were not in business between February 15, 2019 – June 30, 2019: Your max loan is equal to 250 percent of your average monthly payroll costs between January 1, 2020 and February 29, 2020.
- If you took out an Economic Injury Disaster Loan (EIDL) between February 15, 2020 and June 30, 2020 and you want to refinance that loan into a PPP loan, you would add the outstanding loan amount to the payroll sum.

What costs are eligible for payroll?

- Compensation (salary, wage, commission, or similar compensation, payment of cash tip or equivalent)
- Payment for vacation, parental, family, medical, or sick leave
- Allowance for dismissal or separation
- Payment required for the provisions of group health care benefits, including insurance premiums
- Payment of any retirement benefit
- Payment of State or local tax assessed on the compensation of employees

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What costs are not eligible for payroll?

- Employee/owner compensation over \$100,000
- Taxes imposed or withheld under chapters 21, 22, and 24 of the IRS code
- Compensation of employees whose principal place of residence is outside of the U.S.
- Qualified sick and family leave for which a credit is allowed under sections 7001 and 7003 of the Families First Coronavirus Response Act

What are allowable uses of loan proceeds?

- Payroll costs (as noted above)
- Costs related to the continuation of group health care benefits during periods of paid sick, medical, or family leave, and insurance premiums
- Employee salaries, commissions, or similar compensations (see exclusions above)
- Payments of interest on any mortgage obligation (which shall not include any prepayment of or payment of principal on a mortgage obligation)
- Rent (including rent under a lease agreement)
- Utilities
- Interest on any other debt obligations that were incurred before the covered period

What are the loan term, interest rate, and fees?

For any amounts not forgiven, the maximum term is 10 years, the maximum interest rate is 4 percent, zero loan fees, zero prepayment fee (SBA will establish application fees caps for lenders that charge).

How do I get forgiveness on my PPP loan?

You must apply through your lender for forgiveness on your loan. In this application, you must include:

- Documentation verifying the number of employees on payroll and pay rates, including IRS payroll tax filings and State income, payroll and unemployment insurance filings.
- Documentation verifying payments on covered mortgage obligations, lease obligations, and utilities.
- Certification from a representative of your business or organization that is authorized to certify that the documentation provided is true and that the amount that is being forgiven was used in accordance with the program's guidelines for use.

What happens after the forgiveness period?

Any loan amounts not forgiven are carried forward as an ongoing loan with max terms of 10 years, at a maximum interest rate of 4%. Principal and interest will continue to be deferred, for a total of 6 months to a year after disbursement of the loan. The clock does not start again.

Where should I go to get a PPP loan from?

All current SBA 7(a) lenders are eligible lenders for PPP. The Department of Treasury will also be in charge of authorizing new lenders, including non-bank lenders, to help meet the needs of small business owners.

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Economic Injury Disaster Loans & Emergency Economic Injury Grants

These grants provide an emergency advance of up to \$10,000 to small businesses and private non-profits harmed by COVID-19 within three days of applying for an SBA Economic Injury Disaster Loan (EIDL). To access the advance, you first apply for an EIDL and then request the advance. The advance does not need to be repaid under any circumstance, and may be used to keep employees on payroll, to pay for sick leave, meet increased production costs due to supply chain disruptions, or pay business obligations, including debts, rent and mortgage payments.

Are businesses and private non-profits in my state eligible for an EIDL related to COVID-19?

Yes, those suffering substantial economic injury in all 50 states, DC, and the territories may apply for an EIDL.

Who is eligible for an EIDL?

Those eligible are the following with 500 or fewer employees:

- Sole proprietorships, with or without employees
- Independent contractors
- Cooperatives and employee owned businesses
- Tribal small businesses

Small business concerns and small agricultural cooperatives that meet the applicable size standard for SBA are also eligible, as well as most private non-profits of any size.

Who is eligible for an Emergency Economic Injury Grant?

Those eligible for an EIDL and who have been in operation since January 31, 2020, when the public health crisis was announced.

How long are Emergency Economic Injury Grants available?

January 31, 2020 – December 31, 2020. The grants are backdated to January 31, 2020 to allow those who have already applied for EIDLs to be eligible to also receive a grant.

If I get an EIDL and/or an Emergency Economic Injury Grant, can I get a PPP loan?

Whether you've already received an EIDL unrelated to COVID-19 or you receive a COVID-19 related EIDL and/or Emergency Grant between January 31, 2020 and June 30, 2020, you may also apply for a PPP loan. If you ultimately receive a PPP loan or refinance an EIDL into a PPP loan, any advance amount received under the Emergency Economic Injury Grant Program would be subtracted from the amount forgiven in the PPP. However, you cannot use your EIDL for the same purpose as your PPP loan. For example, if you use your EIDL to cover payroll for certain workers in April, you cannot use PPP for payroll for those same workers in April, although you could use it for payroll in March or for different workers in April.

How do I apply for an economic injury disaster loan?

To apply for an EIDL online, please visit <https://disasterloan.sba.gov/ela/>. Your SBA District Office is an important resource when applying for SBA assistance.

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IRS COVID-19-Related Tax Credits for Required Paid Leave Provided by Small and Midsize Business FAQs

The Families First Coronavirus Response Act (the “FFCRA”), signed by President Trump on March 18, 2020, provides small and midsize employers refundable tax credits that reimburse them, dollar-for-dollar, for the cost of providing paid sick and family leave wages to their employees for leave related to COVID-19.

The FFCRA gives businesses with fewer than 500 employees (referred to throughout these FAQs as “Eligible Employers”) funds to provide employees with paid sick and family and medical leave for reasons related to COVID-19, either for the employee’s own health needs or to care for family members. Workers may receive up to 80 hours of paid sick leave for their own health needs or to care for others and up to an additional ten weeks of paid family leave to care for a child whose school or place of care is closed or child care provider is closed or unavailable due to COVID-19 precautions. The FFCRA covers the costs of this paid leave by providing small businesses with refundable tax credits. Certain self-employed individuals in similar circumstances are entitled to similar credits.

What tax credits does the FFCRA provide?

The FFCRA provides businesses with tax credits to cover certain costs of providing employees with required paid sick leave and expanded family and medical leave for reasons related to COVID-19, from April 1, 2020, through December 31, 2020.

When can employers start claiming the credits?

Eligible Employers may claim tax credits for qualified leave wages paid to employees on leave due to paid sick leave or expanded family and medical leave for reasons related to COVID-19 for leave taken beginning on April 1, 2020, and ending on December 31, 2020.

Eligible Employers will claim the credits on their federal employment tax returns (e.g., Form 941, Employer’s Quarterly Federal Tax Return), but they can benefit more quickly from the credits by reducing their federal employment tax deposits. If there are insufficient federal employment taxes to cover the amount of the credits, an Eligible Employer may request an advance payment of the credits from the IRS by submitting a Form 7200, Advance Payment of Employer Credits Due to COVID-19. The IRS expects to begin processing these requests during April 2020.

When will employers start to receive tax credits?

After qualified leave wage payments have been made, Eligible Employers may receive payment of the credits in accordance with applicable IRS procedures.

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What documentation must an Eligible Employer retain to substantiate eligibility to claim the tax credits?

Eligible Employers claiming the credits for qualified leave wages (and allocable qualified health plan expenses and the Eligible Employer's share of Medicare taxes), must retain records and documentation related to and supporting each employee's leave to substantiate the claim for the credits, and retain the Forms 941, Employer's Quarterly Federal Tax Return, and 7200, Advance of Employer Credits Due To COVID-19, and any other applicable filings made to the IRS requesting the credit.

What is the amount of the refundable tax credits available to Eligible Employers?

The credits covers 100 percent of up to ten days of the qualified sick leave wages and up to ten weeks of the qualified family leave wages (and any qualified health plan expenses allocable to those wages) that an Eligible Employer paid during a calendar quarter, plus the amount of the Eligible Employer's share of Medicare taxes imposed on those wages. Qualified sick leave and qualified family leave under the FFCRA are in addition to employees' preexisting leave entitlements. See the Department of Labor's Families First Coronavirus Response Act: Questions and Answers for rules regarding required FFCRA paid sick leave and expanded family and medical leave and other leave entitlements. Eligible Employers may only claim a credit for qualified leave wages.

Example: An Eligible Employer pays \$10,000 in qualified sick leave wages and qualified family leave wages in Q2 2020. It does not owe the employer's share of social security tax on the \$10,000, but it will owe \$145 for the employer's share of Medicare tax. Its credits equal \$10,145, which include the \$10,000 in qualified leave wages plus \$145 for the Eligible Employer's share of Medicare tax (this example does not include any qualified health plan expenses allocable to the qualified leave wages). This amount may be applied against any federal employment taxes that the Eligible Employer is liable for on any wages paid in Q2 2020. Any excess over the federal employment tax liabilities is refunded in accord with normal procedures. The Eligible Employer must still withhold the employee's share of social security and Medicare taxes on the qualified leave wages paid.

How do Eligible Employers claim their credits?

Eligible Employers will report their total qualified leave wages (and allocable qualified health plan expenses and the Eligible Employer's share of Medicare tax on the qualified leave wages) for each quarter on their federal employment tax return, usually Form 941, Employer's Quarterly Federal Tax Return. Form 941 is used to report income tax and social security and Medicare taxes withheld by most Eligible Employers from employee wages, as well as the Eligible Employer's own share of social security and Medicare taxes.

In anticipation of receiving the credits, Eligible Employers can fund qualified leave wages (and allocable qualified health plan expenses and the Eligible Employer's share of Medicare tax on the qualified leave wages) by accessing federal employment taxes related to wages paid between April 1, 2020, and December 31, 2020, including withheld taxes, that would otherwise be required to be deposited with the IRS. This means that in anticipation of claiming the credits on the Form 941, Eligible Employers can retain the federal employment taxes that they otherwise would have deposited, including federal income tax withheld from employees, the employees' share of social security and Medicare taxes, and the Eligible Employer's share of social security and Medicare taxes with respect to all employees. The Form 941 will provide instructions about how to reflect the reduced liabilities for the quarter related to the deposit schedule.

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What if an Eligible Employer does not have enough federal employment taxes set aside for deposit to cover its obligation to cover qualified leave wages?

If an Eligible Employer does not have enough federal employment taxes set aside for deposit to cover its obligation to provide qualified leave wages (and allocable qualified health plan expenses and the Employer's share of Medicare tax on the qualified leave wages), the employer may request an advance of the credits by completing Form 7200, Advance Payment of Employer Credits Due to COVID-19. The Eligible Employer will account for the amounts received as an advance when it files its Form 941, Employer's Quarterly Federal Tax Return, for the relevant quarter.

Determining the Amount of Allocable Qualified Health Plan Expenses

“Qualified health plan expenses” are amounts paid or incurred by the Eligible Employer to provide and maintain a group health plan (as defined in section 5000(b)(1) of the Internal Revenue Code (the “Code”)), but only to the extent that those amounts are excluded from the gross income of employees by reason of section 106(a) of the Code.

Generally, the tax credits for qualified sick leave wages and qualified family leave wages are increased by the qualified health plan expenses allocable to each type of qualified leave wages. Qualified health plan expenses are properly allocated to the qualified sick or family leave wages if the allocation is made on a pro rata basis among covered employees (for example, the average premium for all employees covered by a policy) and pro rata on the basis of periods of coverage (relative to the time periods of leave to which such wages relate).

Does the amount of the qualified health plan expenses include both the portion of the cost paid by the eligible Employer and the portion paid by the employee?

The amount of qualified health plan expenses taken into account in determining the credits generally includes both the portion of the cost paid by the Eligible Employer and the portion of the cost paid by the employee with pre-tax salary reduction contributions. However, the qualified health plan expenses should not include amounts that the employee paid for with after-tax contributions.

An Eligible Employer who sponsors more than one health plan for its employees (for example, both a group health plan and a health flexible spending arrangement (health FSA), or more than one plan covering different employees, how are the qualified health plan expenses for each employee determined?

An Eligible Employer who sponsors a fully-insured group health plan may use any reasonable method to determine and allocate the plan expenses, including (1) the COBRA applicable premium for the employee typically available from the insurer, (2) one average premium rate for all employees, or (3) a substantially similar method that takes into account the average premium rate determined separately for employees with self-only and other than self-only coverage.

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If an Eligible Employer chooses to use one average premium rate for all employees, the allocable amount for each day an employee covered by the insured group health plan is entitled to qualified leave wages could be determined using the following steps:

1. The Eligible Employer's overall annual premium for the employees covered by the policy is divided by the number of employees covered by the policy to determine the average annual premium per employee.
2. The average annual premium per employee is divided by the average number of work days during the year by all covered employees (treating days of paid leave as a work day and a work day as including any day on which work is performed) to determine the average daily premium per employee. For example, a full-year employee working five days per week may be treated as working 52 weeks x 5 days or 260 days. Calculations for part-time and seasonal employees who participate in the plan should be adjusted as appropriate. Eligible Employers may use any reasonable method for calculating part-time employee work days.
3. The resulting amount is the amount allocated to each day of qualified sick or family leave wages.

Example: An Eligible Employer sponsors an insured group health plan that covers 400 employees, some with self-only coverage and some with family coverage. Each employee is expected to have 260 work days a year. (Five days a week for 52 weeks.) The employees contribute a portion of their premium by pre-tax salary reduction, with different amounts for self-only and family. The total annual premium for the 400 employees is \$5.2 million. (This includes both the amount paid by the Eligible Employer and the amounts paid by employees through salary reduction.)

For an Eligible Employer using one average premium rate for all employees, the average annual premium rate is \$5.2 million divided by 400, or \$13,000. For each employee expected to have 260 work days a year, this results in a daily average premium rate equal to \$13,000 divided by 260, or \$50. That \$50 is the amount of qualified health expenses allocated to each day of paid sick or family leave per employee.

For an eligible Employer who sponsors a health savings account (HSA), or Archer Medical Savings Account (Archer MSA), are contributions to the HSA or Archer MSA included in the qualified health plan expenses?

The amount of qualified health plan expenses does not include Eligible Employer contributions to HSAs or Archer MSAs. Eligible Employers who sponsor a high deductible health plan (HDHP) should calculate the amount of qualified expenses in the same manner as an insured group health plan, or a self-insured plan, as applicable.

For an eligible Employer who sponsors a health reimbursement arrangement (HRA), a health flexible spending arrangement (health FSA), or a qualified small employer health reimbursement arrangement (QSEHRA) are contributions to the HRA, health FSA, or QSEHRA included in the qualified health plan expenses?

The amount of qualified health plan expenses may include contributions to an HRA (including an individual coverage HRA), or a health FSA, but does not include contributions to a QSEHRA. To allocate contributions to an HRA or a health FSA, Eligible Employers should use the amount of contributions made on behalf of the particular employee.