



## **Congress Passes the CARES Act**

To help keep small businesses afloat, the CARES Act provides that businesses with fewer than 500 employees, including sole proprietors and nonprofits, will have access to nearly \$350 billion in loans through the Small Business Act during the “covered period,” which runs from February 15, 2020 through June 30, 2020. The loans, which are referred to as “paycheck protection loans” and are fully guaranteed by the federal government through December 31, 2020 (returning to an 85% guarantee for loans greater than \$150,000 after that date), are generally limited to the LESSER OF:

- the sum of
  - 1) average monthly “payroll costs” for the 1 year period ending on the date the loan was made (an alternative calculation is available for seasonal employers) multiplied by 2.5, and
  - 2) any economic disaster loan taken out after January 31, 2020 that has been refinanced into a paycheck protection loan, and
- \$10 million.

### ***Payroll costs are the sum of the following:***

- wages, commissions, salary, or similar compensation to an employee or independent contractor,
- payment of a cash tip or equivalent,
- payment for vacation, parental, family, medical or sick leave,
- allowance for dismissal or separation,
- payment for group health care benefits, including premiums,
- payment of any retirement benefits, and
- payment of state or local tax assessed on the compensation of employees,



## ***Payroll costs do not include:***

- the compensation of any individual employee in excess of an annual salary of \$100,000,
- payroll taxes,
- any compensation of an employee whose principal place of residence is outside the U.S., or
- any qualified sick leave or family medical leave for which a credit is allowed under the new Coronavirus Relief Act passed last week.

*Example. ABC Co. applies for a paycheck protection loan on April 15, 2020. The business had \$1.2 million in payroll costs for the period April 15, 2019 through April 15, 2020, for a monthly average of \$100,000. ABC Co. is entitled to a fully guaranteed federal loan —assuming it's made before December 31, 2020 — equal to the LESSER OF:*

- *\$250,000 (\$100,000 in average payroll costs \* 2.5), or*
- *\$10 million.*

The loans will have a maximum maturity of 10 years and an interest rate not to exceed 4%.

## ***Proceeds may be used to cover:***

- Payroll
- mortgage payments
- rent
- utilities, and
- any other debt service requirements

The standard fees imposed under Section 7 of the Small Business Act are waived, and no personal guarantee is required by the business owner.

An additional provision in the CARES Act provides for possible deferment of repayment of the loans for a period of at least six months, but not to exceed a year.



## ***Loan Forgiveness of Paycheck Protection Loans***

A separate section of the CARES Act calls for a portion of the paycheck protection loans to be forgiven on a tax-free basis. The amount to be forgiven is the sum of the following payments made by the borrower during the 8-week period beginning on the date of the loan:

- payroll costs (as defined above)
- mortgage interest,
- rent,
- certain utility payments.

To seek forgiveness, a borrower must submit to the lender an application that includes documentation verifying the number of employees and pay rates, and cancelled checks showing mortgage, rent, or utility payments.

*Example. Continuing the previous example with ABC Co, in the first 8 weeks after the business borrows the \$250,000, the business pays \$200,000 in payroll costs, mortgage interest, and utility payments. ABC Co. is eligible to have \$200,000 of the \$250,000 loan forgiven. The forgiveness will not create taxable income. In addition, because of the deferment rules in the CARES Act, any payments due on the remaining \$50,000 will not be due for six months.*

There is a provision, however, that reduces the amount that may be forgiven if the employer either:

- Reduces its workforce during the 8-week covered period when compared to other periods in either 2019 or 2020, or
- Reduces the salary or wages paid to an employee who had earned less than \$100,000 in annualized salary by more than 25% during the covered period.

This reduction can be avoided, however, if the employer rehires or increases the employee's pay within an allotted time period.