

## **THE CARES ACT PROVIDES CRITICAL, NEWLY-FUNDED RELIEF FOR SMALL BUSINESSES**

Recent federal legislation and regulation is intended to provide economic relief to small businesses facing shutdowns and dramatic decreases in revenue as a result of the 2019 novel coronavirus (COVID-19) pandemic. Congress has just provided billions of dollars in new, desperately-needed funds for these vital programs – and small business *must act quickly* to take advantage of these new opportunities that are now available.

**Eric B. LaMons**

The Schulman Law Firm LLP  
The Cunard Building  
25 Broadway  
New York, New York 10004  
<http://www.djslf.com>  
Email: [eric@djslf.com](mailto:eric@djslf.com)  
Direct: 646.688.5214  
Cell: 917.751.4755

## Introduction

On March 27, 2020, following the passage of two earlier economic stimulus bills, the U.S. Congress passed, and the President signed, the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), which became effective immediately. On April 2nd, the Small Business Administration (SBA) issued its first Interim Final Rule, followed by the second Interim Final Rule on April 15<sup>th</sup>, and the third Interim Final Rule on April 17<sup>th</sup>, each providing additional guidance and regulation pursuant to the application of the CARES Act. On April 24, 2020, Congress passed and the President signed the Paycheck Protection Program on Health Care Enhancement Act (Pub. L. No. 116-139, H.R. 266), which became effective immediately and provides, among other things, billions of dollars in additional funding for certain programs under the CARES Act whose existing funds had been exhausted.

Pursuant to the CARES Act and subsequent regulations and legislation, the primary forms of economic relief provided to small businesses discussed below are as follows:

- The Paycheck Protection Program (PPP) provides loans from the SBA of up to \$10 million at 1% interest to cover payroll costs and certain other monthly expenses. The principal and interest is subject to potential 100% forgiveness;
- The Economic Injury Disaster Loan (EIDL) Program provides low-interest loans from the SBA of up to \$2 million to help restore necessary working capital or liquidity that has been lost, until normal operations can resume;
- A grant of \$10,000 as an emergency advance within three days of applying for an EIDL, which will never need to be repaid, even if the EIDL application is denied;
- A debt relief program deferring for six months the payments otherwise owed under pre-existing non-disaster related SBA loans; and
- An employee retention tax credit (for employers who do not obtain a PPP loan) of up to \$5,000 of payroll taxes per employee as well as deferral of payment of employer-side Social Security payroll tax payments, with 50% owed on December 31, 2021 and the remaining 50% owed on December 31, 2022.

Most of these benefits are provided on a *first-come, first-serve* basis until the funding runs out – as the initial funding already has. So, with an additional \$310 billion in new funding just added on April 24, 2020, and applications now being accepted again, it is incumbent on businesses to act quickly.

## A. The Paycheck Protection Program (PPP)

Title I, Section 1102 of the CARES Act amends Section 7(a) of the Small Business Act to authorize the SBA to issue a new type of loan under a new Paycheck Protection Program.

### ➤ *Key Provisions of the PPP*

1. The covered period for this program begins on February 15, 2020 and ends on June 30, 2020, the date by which any application must be made;
2. Loans issued under the PPP are backed 100% by the federal government, protecting lenders from any risk;
3. An eligible business can, per Section 1102, obtain a loan in the amount of **2.5 times its monthly payroll expenses**, up to \$10 million total;
  - a. This is calculated based on the monthly average of total payroll expenses incurred over the year prior to the issuance of the loan, although eligible salaries are capped at \$100,000 per employee, as discussed below;
  - b. This loan can additionally include any outstanding loan amounts made under the EIDL between January 31, 2020 and the date on which such a loan may be refinanced as part of the PPP
4. **The loan proceeds can be used to pay:**
  - a. **“Payroll costs”** as defined in Section 1102 to include payments of or for:
    - Salary, wages, commissions, or tips (capped at \$100,000 on an annualized basis for each employee, as prorated for the covered period, and excluding compensation for employees residing outside the U.S.)
    - Group health care benefits, including insurance premiums
    - Vacation, parental, family, medical, or sick leave (except to the extent there is a credit for such benefits allowed under the Families First Coronavirus Response Act)
    - Severance benefits;
    - Retirement benefits, and
    - State or local taxes assessed on employee compensation
  - b. **Rent**, under lease agreements in force before February 15, 2020
  - c. **Utilities**, for which service began before February 15, 2020

- d. **Interest on mortgage obligations** incurred before February 15, 2020<sup>1</sup>
5. The loan has a maximum term of **two years**, and there are no prepayment penalties or fees
6. Per the first Interim Final Rule, the loan has a **fixed interest rate of 1%**
7. **Loan payments and interest payments are deferred for six months**, although interest will still accrue during this six-month period
8. Up to 100% of the principal of the loan and the accrued interest may qualify for **loan forgiveness** if particular requirements, described below, are satisfied

➤ ***Eligibility for a PPP Loan***

**A Qualified Business** (or qualified tax-exempt non-profit, veteran organization, or tribal business concern) is one that:

1. Has **500 or fewer employees** (with exceptions for companies in the hospitality/dining industry)<sup>2</sup> regardless of whether the business qualifies as a small business under normal SBA standards
  - a. **Affiliation rules** apply to calculate this number, so the number of employees includes employees of the company's affiliates.
  - b. Per the SBA, companies or entities are affiliates of each other when one controls or has the power to control the other(s) or when a third party (or parties) control or have the power to control each of them. It does not matter if control is actually exercised, only if such control exists. Such control exists where:
    - A party owns or has the power to control more than 50% of a company's voting equity, or has the power to prevent a quorum or otherwise block action by the board of directors or shareholders;
    - A party holds stock options, convertible securities, or a merger agreement (including an agreement in principal) that would provide such control, as if the rights granted have been exercised;

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<sup>1</sup> If the company or entity received an EIDL loan between January 31, 2020 and April 3, 2020, and that loan was used for payroll costs, the company or entity can apply for a PPP loan, but the proceeds must be used to refinance the EIDL loan.

<sup>2</sup> Sole proprietors, independent contractors, and self-employed persons also qualify if they meet the other qualifications. In addition, businesses in the hospitality and dining industries, even with more than 500 employees, can still qualify for a PPP loan and are not subject to the affiliation rules if they (a) have more than one location, (b) employ no more than 500 people per location, and (c) are assigned a code under the North American Industry Classification System (NAICS) beginning with 72, applicable to the accommodation and food services sector. Affiliation rules are also waived for (a) a business operating as a franchise that has been assigned by franchise identifier code and (b) a company that receives funding through a Small Business Investment Company.

- The CEO, President, or other management of a party have control over the management or board of directors of the company; or
  - Where there is identity of interest between close relatives with substantially identical business or economic interest (such as being in the same or similar industry in the same geographic area).
2. Was in operation on February 15, 2020
  3. Has paid salaries and payroll taxes to employees (or paid independent contractors) whose principal place of residence is the United States
    - a. The payroll calculation for determining the amount of the loan will be based solely on such employees (or independent contractors)
  4. Has been substantially impacted by the public health restrictions related to the Covid-19 pandemic such that “current economic uncertainty makes this loan request necessary to support [its] ongoing operations”
    - a. This requires mere certification, not documentation
  5. Will use the loan proceeds to “retain workers and maintain payroll or make mortgage interest payments, lease payments, and utility payments” consistent with PPP requirements
  6. Has not already received a loan between January 31, 2020 and April 3, 2020 under the Small Business Act for the purpose of paying payroll costs and other allowable uses for loans under the PPP
    - a. In other words, a business cannot receive more than one loan for this same purpose
  7. Is not, and any individual owning 20% of its equity is not, subject to an indictment, criminal information, arraignment, or otherwise facing criminal charges, or presently incarcerated, on probation, or on parole
  8. No owner of the business has been convicted, plead guilty, plead no contest, placed on pretrial diversion, or placed on parole or probation for a felony

➤ ***Forgiveness of a PPP Loan***

1. Title I, Section 1106 of the CARES Act provides for potential **forgiveness** of PPP loan proceeds used for by the borrower to pay “payroll costs”, as well as the qualified rent, utility, and interest on mortgage payments (as defined and described above, from Section 1102 of the act), subject to particular requirements.
2. The “covered period,” for purposes of loan forgiveness under this program, is the eight-week period starting on the origination date of the PPP loan.

3. **For forgiveness of *entire* loan principal, three requirements must be met.** The amount of forgiveness will be reduced to the extent any of these requirements are inadequately satisfied.

A. The employer must use at least **75%** of the total loan proceeds **for payroll costs** and not more than **25%** of the total loan proceeds **for non-payroll costs** (using the same definition of “payroll costs” described above). To the extent the employer’s use of loan proceeds for non-payroll costs exceeds 25% of the total, the amounts used in excess of that percentage will not be forgiven.

- In no event can more than 25% of the forgiven amount be for non-payroll costs.

B. **The employer must maintain and must not reduce its number of full-time employees during the eight-week covered period.** Per Section 1106, the lender will compare:

- (i) The average number of full-time, or equivalent, employees employed by the employer per month during the covered period with
- (ii) At the employer’s election, either (a) the average number of full-time, or equivalent, employees employed by the employer per month during the same period last year, meaning February 15, 2019 through June 20, 2019 OR (b) the average number of full-time, or equivalent, employees employed by the employer per month during the period from January 1, 2020 through February 29, 2020.

To the extent, if any, that the first is less than the second, the amount of loan forgiveness will be reduced. For example, if the employer only maintains 90% of its full-time employees during the covered period as compared to previous periods, the employer will only be eligible for, at most, 90% loan forgiveness, subject to the other limitations.

C. **The employer must maintain and must not reduce below a certain level the amount of salary and wages it pays certain employees during the eight-week covered period.** Per Section 1106, the lender will focus on employees who made \$100,000 or less on an annualized basis in 2019 and compare:

- (i) The amount of salary and wages paid by the employer to such employees during the covered period with

- (ii) The amount of salary and wages paid by the employer to such employees during the most recent full quarter before the covered period.

To the extent, if any, that the first is more than 25% less than the second, the amount of loan forgiveness will be reduced by the corresponding dollar amount. In other words, the dollars that the employer did not pay to such employees in excess of the allowable 25% reduction will be taken from the amount of loan forgiveness.

4. **Please note**, however, that if the employment or salary levels fell below the requisite thresholds listed above between February 15, 2020 and April 26, 2020, the employer still has until June 30, 2020 to restore them to appropriate levels and thereby avoid reduction of the amount of loan forgiveness.
  - a. For example, if an employer rehires employees that had previously been laid off at the beginning of the covered period, the employer will not be penalized.
5. Any employer seeking loan forgiveness must submit to the lender (and so should maintain) documentation and information including at least:
  - a. Documentation verifying the number of full-time employees, or the equivalent, on the payroll and the pay rates during the relevant periods above (such as payroll tax, income, and unemployment insurance filings);
  - b. Documentation verifying payments made for applicable rent, utilities, and mortgage interest payments during the relevant periods above; and
  - c. Certification from a representative of the employer verifying the accuracy of all such documentation and certifying the loan proceeds were only used for authorized purposes.
6. The lender must issue a decision within 60 days of receiving an application seeking loan forgiveness from a borrower.
7. Any amounts forgiven are treated as cancelled indebtedness, and interest will only be owed to the extent it has accrued upon the amount, if any, of unforgiven principal. If all the principal is forgiven, the borrower owes no interest.
8. Any principal forgiven will be excluded from gross income for federal tax purposes as well.
9. Loan principal that is not forgiven, and interest accruing on such unforgiven principal, must be repaid with a term of no more than ten (10) years from the origination date.

➤ ***Application for a PPP Loan***

1. A business is not required to pledge any collateral for the loan
2. No personal guarantee is required for the loan
3. A borrower does not need to make any attempt to receive the funds elsewhere before making the application for a PPP loan
4. An employer seeking a PPP loan must submit to any bank or lender approved to make SBA loans:
  - a. **SBA Form 2483 (the Paycheck Protection Program Application Form,** available at: <https://www.sba.gov/sites/default/files/2020-04/PPP-Borrower-Application-Form-Fillable.pdf>)
    - This form includes all required certifications, authorizations and information indicating, among other things, that
      - The employer meets eligibility requirements;
      - The employer will comply with all rules and requirements of the PPP as set forth above, including will use the loan proceeds solely for authorized purposes;
      - The employer will provide the lender with documentation of its payroll costs and employment information for the eight-week period following the origination of the loan; and
      - All information in the application and supporting documentation is accurate and complete.
  - b. **Documentation of its payroll costs,** as such costs are described above and defined in Section 1102, sufficient to determine and verify the appropriate amount of the loan; and
  - c. Documentation of any currently outstanding EIDL loan sought to be refinanced.
5. Lenders can automatically approve loans under the PPP without SBA consent
6. There are no loan fees paid to the SBA, and the SBA pays the origination fees to the lender, so the borrower should pay minimal or no fees to the lender.
7. **Please note** that, prior to the passage of the April 24, 2020 legislation, the SBA indicated that the initial funds had been exhausted. However, the most recent legislation has specifically provided substantial additional funding for this program, and the SBA *has now begun accepting applications* again. Notably, many small businesses are finding substantial delays and some are waiting longer than expected to receive loan proceeds after submitting applications, which simply adds to the urgency to submit new applications as soon as possible.



**B. Economic Injury Disaster Loans and  
Emergency Economic Injury Grants**

Title I, Section 1110, of the CARES Act expands the scope of the Economic Injury Disaster Loan Program (EIDL) authorized under Section 7(b)(2) of the Small Business Act. The CARES Act expands the loans available to small businesses and provides for the issuance of emergency grants to small businesses in further response to the COVID-19 pandemic. The April 24, 2020 legislation has provided an additional \$60 billion to fund the EID loan program and an additional \$10 billion to fund the emergency grants authorized by the CARES Act.

Many lenders are combining applications for the emergency grant \$10,000 EIDL loans together with their applications for PPP loans, but a small business can apply directly to the SBA for that grant, so long as funds are remaining to fund the program.

➤ ***Key Provisions of the Expanded EIDL Program***

1. This EIDL Program generally provides loans to eligible small businesses located in a declared disaster area and impacted by the natural or other disaster to obtain relief from the disaster's impact.
2. Section 1110 expands the EIDL to allow eligible small businesses impacted by the COVID-19 pandemic during the period from **January 31, 2020 to December 31, 2020** to obtain relief through low-interest loans.
  - This is the current “**covered period**” for purposes of applying the EIDL
3. The loans are offered at a fixed rate of **3.75% interest** for for-profit companies (and 2.75% interest for non-profit organizations).
4. The loans are offered at a maturity term of up to **30 years**.
5. Principal and interest payments on an EIDL can be **deferred for up to 1 year**.
6. The SBA guarantees up to 100% of the EIDLs
7. The EIDL offers loans in an amount **up to \$2 million**.<sup>3</sup>
  - Per Section 1110, the SBA can also issue “small dollar loans” to applicants based solely on either (i) an applicant's credit score or (ii) an appropriate alternative method to determine the applicant's ability to repay the loan.

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<sup>3</sup> Prior to the passage of the April 24, 2020 legislation, the SBA had announced that, due to overwhelming demand and insufficient funding, it would only be able to issue EID loans in the amount of \$15,000 each for the next two months. However, the additional funding in the latest legislation may change that policy.

8. The amount of a company's particular loan is based upon the company's **actual economic injury suffered as a result of the COVID-19 pandemic during the covered period**, as determined by the SBA on a case-by-case basis.
  - The loan proceeds are to be used to cover financial obligations and operating expenses, such as payroll, rent, mortgage payments, and other costs that the company could have met had the disaster not occurred.
  - The loan proceeds are *not* to be used for things like refinancing, making loan payments on other federal debts, to repair physical damages, to pay IRS tax penalties, or to pay out dividends.
9. A small business *can* seek and obtain a loan from **both the PPP and the EIDL**, but only to the extent the funds from each loan are **used for different purposes**.

➤ ***Eligibility for EIDLs***

1. An entity eligible for such a loan **is an entity** located anywhere in the United States that has been negatively impacted economically by the circumstances of the COVID-19 pandemic and that is, per Section 1110:
  - A small business concern or non-profit organization already eligible for an EIDL prior to the implementation of the CARES Act;
  - A business with 500 or fewer employees (calculated as described above with the affiliate rules applied);
  - An individual who operates as a sole proprietor, with or without employees, or as an independent contractor;
  - A cooperative with 500 or fewer employees;
  - An Employee Stock Ownership Plans (ESOPs) (as defined in Section 3 of the Small Business Act) with 500 or fewer employees; or
  - A tribal small business concern.
2. Businesses are not qualified for an EIDL if, for example, the business:
  - Derives more than a third of its annual revenue from gambling activities
  - Is in the business of lobbying
  - Is a government entity
  - Is engaged in any illegal activity, or derives revenue from sexual depictions or products

➤ *Application for an EIDL under the Expanded Program*

1. No personal guarantee is required.
2. The business is not required to have been in operation for the one-year period prior to the disaster (unless the business was not in operation on Jan. 31, 2020).
3. A borrower does not need to make any attempt to receive the funds elsewhere before making the application for an EIDL
4. An employer seeking a PPP loan can apply to a lender or go directly to the SBA website at <https://www.sba.gov/page/disaster-loan-applications> to find a link to submit such an application directly to the SBA.
  - The application will require the applicant to:
    - Verify that eligibility requirements are satisfied
    - Provide basic information about the operating expenses, revenue, contact information, employee information, and other information to indicate the financial need for the loan based on hardship suffered as a result of the circumstances of COVID-19 epidemic
    - Provide bank account information if the applicant is seeking an emergency grant, described below
  - The application will also require the applicant to submit an IRS Form 4506-T authorizing the IRS to provide the SBA with the applicant's relevant tax return information.
1. **Please note** that, prior to the passage of the April 24, 2020 legislation, the SBA indicated that it was no longer accepting applications for EIDLs or emergency grants because the existing funds had been exhausted. However, the most recent legislation has specifically provided substantial additional funding for each of these programs, and the SBA should begin accepting applications again.

➤ *Emergency Grants of Advances Under the Expanded EIDL*

1. Any small business (or other eligible entity) making an application for the EIDL loan during the covered period (which currently lasts until Dec. 31, 2020) can simultaneously request an emergency grant.
2. Such an emergency grant:
  - Will be in an amount of **up to \$10,000**
  - Can be used for any costs for which the EIDL proceeds can be used, while specifically including payment of:

- i. Payroll costs to retain employees during business disruption or slowdown, or to pay sick leave to employees unable to work;
  - ii. The increased production costs resulting for supply chain disruptions;
  - iii. Rent or mortgage payments; or
  - iv. Repaying obligations that cannot be met due to loss of revenue.
- Will be provided within three (3) days of submitting the EIDL application;
3. Any entity eligible for an EIDL is eligible for such an emergency grant.
4. The emergency grant does not need to be repaid under any circumstances, even if the EIDL application is denied.

### C. Small Business Debt Relief Program

The CARES Act also provides for a Small Business Debt Relief Program, funding in the amount of \$17 billion. This program applies to three types of non-disaster SBA loans into which small business may have entered prior to the COVID-19 pandemic that remain outstanding, or that small businesses may enter into anytime between now and September 27, 2020, the date six months after the CARES Act became law.

These three types of non-disaster SBA loans are:

- A loan pursuant to Section 7(a) of the Small Business Act, typically called a “7(a) loan”, *excluding PPP loans*, to obtain working capital, providing up to \$5 million to purchase a business, to refinance debt, to purchase furniture or supplies, etc.;
- A loan pursuant to the SBA’s 504 Loan Program, made available through Certified Development Companies (CDCs), typically known as a “504 loan”, providing up to \$5.5 million to obtain commercial real estate and other fixed assets like buildings and heavy equipment or machinery;
- A loan pursuant to SBA’s Microloan Program, providing up to \$50,000 to help start-ups establish themselves and expand.

For small businesses holding outstanding debt pursuant to any or all of these types of loans, or who take on such debt by September 27, 2020, **the SBA will automatically pay six months of loan payments, including principal, interest, and fees**, owed on all such loans.

In addition, this program:

- Permits banks and other lenders to extend the duration of existing loan terms and
- Provides an extension for certain reporting requirements.

**D. The Employee Retention Tax Credit and Deferral of Employer Payroll Taxes**

For small businesses that are not eligible for, or otherwise do not receive any loan from the PPP, Title II, Section 2301 of the CARES Act provides an Employee Retention Tax Credit to potentially provide an alternative source of relief. In addition, Section 2302 allows small businesses to delay paying the employer portion of certain payroll taxes.

➤ ***Key Provisions of the Employee Retention Tax Credit***

1. An employer is eligible to take this credit if it:
  - a. Was carrying on a trade or business during the calendar year 2020, and
  - b. For any calendar quarter in 2020, either:
    - (i) The operation of such trade or business is “fully or partially suspended” due to “orders from an appropriate governmental authority limiting commerce, travel, or group meetings” due to the COVID-19 pandemic
      - A partial suspension is triggered even if a business’s operations can continue in some form, but not at their normal capacity.
    - OR
    - (ii) There was a “significant decline in gross receipts,” meaning a decrease in gross receipts of 50 percent or more as compared to the gross receipts for the same quarter in 2019.
      - The “significant decline” ends with the first 2020 quarter after a 2020 quarter in which the gross receipts are greater than 80% of the gross receipts for the corresponding quarter in 2019.
2. Eligible employers can take this credit against applicable employment taxes in an amount equal to:
  - 50% of up to \$10,000 in “qualified wages” paid per employee after March 12, 2020.
  - In other words, it is a **tax credit of up to \$5,000 in “qualified wages” paid per employee** during a period of economic hardship described in 1(b) above.

3. For an employer for which the average number of **full-time employees** during 2019 was **greater than 100**, “**qualified wages**” are the wages paid to an employee for time that the employee is not providing services due to one of the economic hardships described in 1(b) above.
4. For an employer for which the average number of **full-time employees** during 2019 was **100 or fewer**, “**qualified wages**” are the wages paid to *any* employee during a period of economic hardship described in 1(b) above.
5. “Qualified wages” include amounts paid by the employer to provide group healthcare insurance so long as such amounts are excluded from the gross income of employees.
6. An employer can claim this Employee Retention Tax Credit by either:
  - a. Reducing its employment tax deposits by the amount of the credit, and accounting for such reduction in deposits using the IRS Form 941 (Employer’s Quarterly Federal Tax Return) for the quarter, OR
  - b. Submitting IRS Form 7200 (seeking Advance Payment of Employer Credits Due to COVID-19) to request advance payment of the credit.
7. If for any quarter the amount of this credit exceeds the employer portion of Social Security tax owed on all wages paid to all employees, the excess amount is an overpayment to be refunded to the employer.
8. Again, an employer cannot take this credit if it has received a PPP loan.

➤ ***Delay of Payment of Employer Payroll Taxes***

1. Section 2302 of the CARES Act allows employers to defer the payment of certain taxes for a “payroll tax deferral period.”
2. The particular taxes subject to such deferral are employer-side Social Security payroll taxes (and half of SECA tax liability for those self-employed).
3. The “payroll tax deferral period” provides that the employer’s payment of such taxes, otherwise due from March 27, 2020 to January 1, 2021, will be considered timely so long as the employer:
  - a. pays half (50%) of such taxes by December 31, 2021 and
  - b. pays the remaining half (50%) by December 31, 2022.
4. An employer cannot take such tax deferral if it has obtained any forgiveness for a PPP loan, pursuant to Sections 1106 of the CARES Act as described above.

For any questions or concerns, or for more information, please contact:

**Eric B. LaMons**

Email: [eric@djslf.com](mailto:eric@djslf.com)

Direct: 646.688.5214

Cell: 917.751.4755

*or*

**Dan J. Schulman**

Email: [djs@djslf.com](mailto:djs@djslf.com)

Direct: 646.688.5214

Cell: 646.263.3199

The Schulman Law Firm LLP  
The Cunard Building  
25 Broadway  
New York, New York 10004  
<http://www.djslf.com>