

## Analysis of Funding Streams in the CARES Act

### Funding Stream 1: \$367 Billion for Small Business Administration (UPDATED April 5, 2020)

#### Who oversees small business loans?

- The [Small Business Administration](#) (SBA) is the primary federal agency that supports small businesses and entrepreneurs.

#### What types of loans are currently available through the SBA?

- The SBA works with lenders to provide loans to small businesses. The agency does not lend money directly to small business owners. Instead, it sets guidelines for loans made by its partnering lenders, community development organizations, and micro-lending institutions.
- There are three common financial assistance programs overseen by SBA – the “7(a) loan program”, the “7(b) loan program” and the Small Business Investment Company (SBIC) financial assistance program.
- The 7(a) loan program is SBA’s primary program for providing financial assistance – in the form of loans – to small businesses. In order for a small business to be eligible, the business must, in addition to other requirements:
  - Be registered as a for-profit business;
  - Not employ more than a certain number of employees or exceed stated revenue thresholds; and
  - Be physically based in the US.
- Section 7(b) of the Small Business Act includes the Economic Injury Disaster Loan (EIDL) program, which distributes loans in amounts up to \$2 million for certain small businesses and non-profits facing economic injury as a result of declared emergencies like the coronavirus (COVID-19).
- The SBIC program allows licensed privately-operated investment funds to provide financing to eligible small businesses in the form of loans, debt securities, equity securities, guarantees or purchase of securities in a small business.

#### What is new for small businesses under the latest stimulus bill?

- The Coronavirus Aid, Relief, and Economic Security (CARES) Act creates a new 7(a) loan program, known as the Paycheck Protection Program (PPP). Congress initially is appropriating \$349 billion of funding for this new program.
- The legislation also modifies and increases funding for the existing EIDL program under Section 7(b).
- The legislation relaxes participation requirements, meaning more business will be deemed “small” and eligible for economic assistance.
- The legislation provides funding for deferments of loans in place.
- The legislation establishes a program to provide training and resources to small businesses affected by coronavirus.

### What is the PPP Loan?

- The PPP Loan provides to recipients up to the lesser of (i) 2.5x the average total monthly payroll costs during *the year preceding application* plus any amounts loaned to the recipient under the EIDL program this year, or (ii) \$10 million.
  - “Payroll costs” include salaries, wages, commissions, cash tips, payment for vacation, parental or sick leave, allowance for dismissal or separation, payment of group healthcare benefits, payment of retirement benefits, and payment of state and local tax assessed on compensation.
  - “Payroll costs” exclude compensation (i.e. salary, wages, commissions or cash tips) in excess of \$100,000 on an annualized basis for each employee, taxes imposed or withheld under Chapters 21, 22 or 24 of the Internal Revenue Code during the period from February 15, 2020 to June 30, 2020, compensation for non-U.S. domiciled employees, amounts paid to an independent contractor, and family or sick leave wages for which a credit has been received under the Families First Coronavirus Response Act.
  - NOTE: SBA has been inconsistent in interpreting the phrase “the year preceding application.” The SBA guidance has interpreted this phrase as both (x) the twelve months preceding application and (y) “the preceding calendar year” (i.e., calendar year 2019). Consult the application form provided by your PPP lender for further guidance.
- PPP Loan Terms:
  - Complete payment deferral (including principal, interest and fees) for 6 months; however, interest will continue to accrue over this period.
  - Maturity: 2 years after the funding of the loan
  - Interest Rate: 1.00% fixed rate
  - Prepayment: The loan may be prepaid at any time with no penalties, premiums or fees
  - Collateral: None
  - Personal Guarantees: None; however, using the proceeds for fraudulent purposes will subject the applicant to criminal liability
- If an employer receives a PPP Loan, the employer will not be eligible for the employee payroll retention tax credit under Section 2301 of the CARES Act.

### What are the permitted uses of the PPP Loans?

- The proceeds of the PPP Loans may be used for:
  - Payroll costs (subject to the limitations on “payroll costs” set forth above);
  - Interest related to mortgage obligations incurred prior to February 15, 2020;
  - Rent under lease agreement in force prior to February 15, 2020; and
  - Utilities costs, for which service began prior to February 15, 2020.
- If a borrower uses any portion of the PPP Loans for unauthorized purposes, SBA will direct the borrower to repay that portion of the PPP Loans.
  - The knowing use of funds for unauthorized purposes will subject the borrower to additional liability such as charges for fraud (including against any shareholder, member or partner of the borrower that uses such funds for unauthorized purposes).

### Will the PPP Loans be forgiven?

- Applicants can receive loan forgiveness in an amount not to exceed the principal amount of indebtedness related to the PPP Loans, equal to the sum of the applicant's payroll (subject to the limitations on "payroll costs" set forth above), rent, mortgage interest and utility costs incurred and payments made during the 8-week period following the origination of the loan if they maintain the same number of FTEs during such 8-week period as compared to the FTE count during a statutorily defined reference period in the past; the loan forgiveness is scaled down proportionally with any decrease in FTEs during such covered period or if any FTE salaries of employees making less than \$100,000 annually are decreased by more than 25%.
- NOTE: No more than 25% of the forgiven amount may be for non-payroll costs.
- Re-Hiring: For purposes of the loan forgiveness calculation, applicants have until June 30, 2020 to restore their full-time employment and salary levels for any changes made between February 15, 2020 and April 26, 2020.
- In order to request loan forgiveness, applicants must submit a request to the lender that is servicing the loan. The request will include documents that verify the number of full-time equivalent employees and pay rates, as well as the payments on eligible mortgage, lease, and utility obligations.
- The lender must make a decision on loan forgiveness within 60 days.
- Loans that are forgiven will not constitute cancellation of indebtedness income, and thus will not be taxable, to the borrower.
- If an employer receives a PPP Loan that is forgiven, the employer will not be eligible for payroll tax deferral under Section 2302 of the CARES Act.

### Do I qualify for the PPP Loan?

- In addition to traditional small businesses under SBA rules (eligibility criteria can be found [here](#)), eligible entities include any business (including nonprofits, veterans organizations and Tribal businesses) that employs 500 or fewer employees (unless the applicant's primary industry is subject to a higher employee-based size standard, in which case the applicant must be "small" under that higher [standard](#)). Certain self-employed workers and independent contractors are eligible, too.
  - Example: Applicant A's primary industry is subject to a 250-employee size standard but actually employs 350 employees. Applicant B's primary industry is subject to a 1,000-employee size standard but actually employs only 750 employees. Both applicants would qualify under the CARES Act paycheck protection assistance:
    - Applicant A qualifies because, even though it otherwise would not be "small" under its NAICS code for traditional SBA financial assistance, it is "small" for purposes of the CARES Act because it employs fewer than 500 employees.
    - Applicant B qualifies because, even though it employs more than the 500-employee limit established in the CARES Act, it operates in an industry with a higher employee-based size standard and it qualifies as "small" under that standard.
- Congress has also provided that businesses in the hospitality, food and beverage industry with more than one business location qualify ***provided*** that no single location has more than 500 employees.
- In addition, the SBA's usual "affiliation" rules are waived for (x) businesses primarily engaged in the hospitality, food and beverage industry employing not more than 500 employees, (y) registered franchises, and (z) businesses receiving financial assistance from a licensed SBIC.

- Affiliation rules: Affiliated companies are counted for purposes of determining whether a business satisfies the requirement of having 500 or fewer employees (or the traditional applicable size standard). More information on how SBA determines “affiliation” can be found at [Section 121.103 of 13 CFR](#).
  - NOTE: As of April 3, 2020, SBA intends to promptly issue additional guidance with regard to the applicability of the affiliation rules to PPP Loans.
- Furthermore, eligibility for borrowers requires:
  - that the business was in operation on February 15, 2020; and
  - the business has paid employees or paid independent contractors and payroll taxes.

#### What is the modified EIDL Program?

- The legislation modifies the existing disaster relief program to respond to the economic impact of COVID-19.
- SBA will waive certain requirements, including that an applicant needs to have been in business for a 1-year period before the disaster (so long as it has been in business since at least January 31, 2020) or the \$200,000 personal guarantee on advances and loans, and the obligation to first seek credit elsewhere before applying for funds provided under the program.
- **Note:** this program does not include the employee-by-location allowance offered in the PPP Loan for hospitality and food and beverage franchisees.
- Underwriting requirements are relaxed.
- EIDL loans must be paid back (other than any advance “emergency grant,” not to exceed \$10,000, applied for within 3 days after SBA receives the application).

#### Can I access both programs?

- Possibly. Businesses that receive a PPP Loan cannot receive an EIDL loan for the same purpose. However, businesses that have incurred an EIDL loan in 2020 may be able to refinance that loan into the PPP Loan, which becomes forgivable if the business has sufficient qualifying salary, utility and rent/mortgage expenses. Furthermore, the EIDL modifications extend to the end of 2020, so they are available to cover emergency expenses that occur after the June 30 expiration of the PPP Loan program.
- NOTE: If a business used an EIDL loan for payroll costs and then incurs a PPP Loan, the business must use the PPP Loan to refinance its EIDL loan. Proceeds from any advance up to \$10,000 on the EIDL loan will be deducted from the loan forgiveness amount on the PPP Loan.

#### Should I apply for PPP or EIDL Loans?

- It depends on your circumstances, but the PPP Loans will be beneficial in many cases if you anticipate that the funds will allow you to maintain your current payroll, especially because all or a portion of the PPP Loan may be forgivable; however, it is a temporary program and only covers expenses through June 30, 2020. Funds borrowed under the EIDL existing loan program must be repaid, but terms are flexible and it covers injuries through the end of the year.

**When will these programs become available?**

- The EIDL program is currently available.
- PPP Loans:
  - Starting April 3, 2020, small businesses and sole proprietorships can apply for and receive loans to cover their payroll and other certain expenses through existing SBA lenders.
  - Starting April 10, 2020, independent contractors and self-employed individuals can apply for and receive loans to cover their payroll and other certain expenses through existing SBA lenders.
  - Please note, in either case, we encourage applicants to reach out to lenders immediately to begin the application process as there may be significant delays in funding due to the high demand for these programs.

**How long will the PPP last?**

- The program is open until June 30, 2020, but we are encouraging borrowers to apply as quickly as possible since the PPP Loans are “first come, first served” and lenders will need time to process the loans.
- NOTE: A borrower can only apply for one PPP Loan, so borrowers should apply for the maximum amount available.

**What can I do now?**

- For PPP Loans: Reach out to your existing relationship depository bank immediately to determine if they are an existing SBA 7(a) lender. Most banks have said they will only offer PPP Loans to their existing customers. To the extent a borrower does not have a relationship with an existing SBA 7(a) lender, a list of the top 100 most active SBA 7(a) lenders can be found [here](#).
- For EIDL Loans: Go to the [SBA website](#) to apply.
- Complete the relevant Application Form (current as of April 5, 2020):
  - For PPP Loans: <https://home.treasury.gov/system/files/136/Paycheck-Protection-Program-Application-3-30-2020-v3.pdf>
  - For EIDL Loans: 7(b) Loan Application (SBA Form 5): [https://www.sba.gov/sites/default/files/files/serv\\_da\\_all\\_loanapp\\_2\\_0\\_0\\_3.pdf](https://www.sba.gov/sites/default/files/files/serv_da_all_loanapp_2_0_0_3.pdf)
- Other items to be submitted with your application:
  - Payroll Documentation (including any of the following: payroll processor records, payroll tax filings, or, if the borrower doesn't have such records, any other supporting documentation, such as bank records, sufficient to demonstrate the qualifying payroll amount)
  - Business tax returns (previous three years)
- NOTE: E-signatures and e-consents are permitted.

**Additional Information Regarding the PPP (current as of April 5, 2020):**

- An overview of the program can be found [here](#).
- A Borrower Information Fact Sheet can be found [here](#).

- A Lender Information Sheet can be found [here](#).

## Funding Stream 2: Treasury's Business Stabilization Loan Fund

This \$500 billion fund will allow the Secretary of the Treasury to provide loans and loan guarantees to support credit facilities that will be established by the Federal Reserve.

### Who is eligible for the Treasury program?

- Businesses that have not otherwise received adequate economic relief in the form of loans or loan guarantees provided under this Act are eligible.

### How is this fund allocated?

- Congress authorized \$46 billion to be directed to the following industries: passenger air carriers and some related industries; cargo air carriers; businesses important to maintaining national security.
- The remaining \$454 billion, as well as any amounts available but not used for direct lending, are available for loans, loan guarantees, and investments in support of the Federal Reserve's lending facilities to businesses, states, and municipalities.

### Who is eligible for a direct lending loan?

Entities applying for a direct lending loan must meet the following criteria:

1. Alternative financing is not reasonably available to the business;
2. The loan is sufficiently secured or made at an interest rate that reflects the risk of the loan and, if possible, not less than an interest rate based on market conditions for comparable obligations before the coronavirus outbreak;
3. The duration of the loan shall be as short as possible and shall not exceed 5 years;
4. Borrowers and their affiliates must agree not to engage in stock buybacks, unless previously contractually obligated, or pay dividends until one year after the date of repayment of the loan;
5. Borrowers must commit to maintain their employment levels as of March 24, 2020 until September 30, 2020, to the extent practicable, and in any event to retain no less than 90 percent of their employees as of March 24, 2020;
6. A borrower must certify that it is a U.S.-domiciled business and its employees are predominantly located in the U.S.;
7. The loan cannot be forgiven; and
8. In the case of borrowers critical to national security, their operations are jeopardized by losses related to the coronavirus pandemic.

### Who is eligible for the Federal Reserve's lending facilities?

There is no restriction on the ability of any business to apply for support through the Federal Reserve's lending facilities, which facilities will have access to the residual \$454 billion plus any amounts not lent directly by Treasury. Businesses may only apply for these funds if they agree to the following criteria:

1. agreement not to pay dividends or engage in buybacks of the borrower entity's own equity or the equity of any parent company, in either case until one year after the loans have been repaid; and
2. agreement to comply with the executive compensation limitations applicable to individuals making more than \$425,000 and to individuals making more than \$3 million per year, which limitations are described below.

The Secretary may waive these requirements, but is required to make himself available to testify before the Senate Banking and House Financial Services Committee regarding the reasons for any such waiver.

### What if I am a non-profit or a business that employs between 500-10,000 employees?

- The Secretary will endeavor to implement a **special credit facility** through the Federal Reserve targeted specifically at non-profit organizations and businesses between 500 and 10,000 employees, subject to additional loan criteria and obligations, including:
  - The funds received must be used to retain at least 90 percent of the recipient's workforce, with full compensation and benefits, through September 30, 2020;
  - The recipient will not outsource or offshore jobs for the term of the loan plus an additional two years;
  - The recipient will not abrogate existing collective bargaining agreements for the term of the loan plus an additional two years; and
  - The recipient must remain neutral in any union organizing effort for the term of the loan.
- **Note:** The Secretary is authorized to create this facility without restriction to the Federal Reserve's existing authority to create a Main Street Lending Program. This Program would not be required to have all of the above restrictions and may ultimately be the principal way that the CARES Act resources are channeled to provide relief to medium-sized businesses.

### If I accept this loan, what executive compensation obligations will apply?

- The Secretary may enter into an agreement with an eligible business only if, between March 1, 2020 and March 1, 2022, no employee or officer making greater than \$425,000 in 2019:
  - Receives a raise in compensation; or
  - Receives severance pay or benefits exceeding twice the maximum total compensation received by the employee in 2019.
- Additionally, employees of a borrower whose compensation exceeds \$3 million per year will be required to reduce their compensation.

### Where do I get more information?

- Treasury is expected to issue additional guidance imminently.



### Funding Stream 3: Tax Credits and Other Potentially Beneficial Tax Considerations

The CARES Act includes a number of potentially beneficial tax provisions for businesses, some of which apply generally across industries, while others are targeted to benefit specific industries (e.g., hospitality).

#### Section 2301 – Employee retention credit for employers subject to closure due to COVID-19.

- Provides a refundable payroll tax credit to qualifying employers on a dollar-for-dollar basis equal to 50% of qualifying wages paid by such employers to employees during the COVID-19 crisis, resulting in a maximum potential net credit of \$5,000 per employee.
- The credit is available to employers whose (i) operations were fully or partially suspended due to a COVID-19-related government shutdown order (and only during periods in which its operations are fully or partially suspended), or (ii) gross receipts for a given quarter beginning after December 31, 2019 declined by more than 50 percent when compared to the same quarter in the prior year.
- The credit is based on qualified wages paid to the employee. Qualified wages include an allocable share of health benefits paid by an employer on behalf of the employee.
- Any family or sick leave wages for which a credit has been received under the Families First Coronavirus Response Act do not count as qualified wages for purposes of this credit.
- For employers who had an average of more than 100 FTEs during 2019, qualified wages are wages paid to employees when those employees are not providing services to the employer due to the COVID-19-related circumstances described above (i.e. (i) and (ii) in the second bullet).
- For eligible employers who had an average of 100 or fewer FTEs during 2019, all employee wages qualify for the credit, whether the employer is open for business or subject to a shut-down order.
- The credit is provided for wages paid or incurred from March 13, 2020 through December 31, 2020.

#### Section 2302 – Delay of payment of employer payroll taxes.

- Allows employers and self-employed individuals to defer payment of the employer share of the Social Security tax they otherwise are responsible for paying to the federal government with respect to their employees.
- As a general matter, employers are responsible for paying a 6.2-percent Social Security tax on employee wages.
- Section 2302 provides that employers can defer the tax due from the date of enactment of the Act through December 31, 2020.
- The provision requires that the deferred employment tax be paid over the following two years, with half of the amount required to be paid by December 31, 2021 and the other half by December 31, 2022.

**Section 2307 – Technical amendment regarding qualified improvement property.**

- Enables businesses to take an immediate deduction for costs associated with improving facilities instead of having to depreciate those improvements over the 39-year life of the building.
- The provision, which corrects an error in the Tax Cuts and Jobs Act, not only increases companies' access to cash flow by allowing them to amend a prior year return, but also incentivizes them to continue to invest in improvements as the country recovers from the COVID-19 emergency.