

OBSERVATIONS

CARES Act – Business Tax Provisions 2

March 30, 2020

The CARES Act (Act) passed the House and was signed by the President on Friday. In theory, banks should be in business to lend under the Paycheck Protection Program (PPP) today, March 30. In summary, PPP allows banks to loan businesses enough funds to cover eight (8) weeks of payroll and certain other costs. Later, if the business can establish that the loan proceeds were in fact used for the designated expenses, the government will pay the loan on behalf of the business. The Program will be administered by the Small Business Administration. This blog will review what expenses are eligible under PPP.

Note: The CARES Act is 880 pages. As with most legislation, the Act amends existing statutes to incorporate these new provisions. For example, the Paycheck Protection Program is codified as an amendment to the Small Business Act. For now, we will make our citations to the CARES Act. The CARES Act, in its 880-page glory, is available on several internet sites. However, the first 83 pages are devoted to the PPP. The remaining portions of the Act addresses relief to individuals, the healthcare system, and distressed sectors of the economy. Additionally, there was a grab bag of a number of other provisions that have only minimal relevance to COVID-19. The following is our reading of the Act and is subject to any administrative interpretation issued by the Small Business Administration.

What Can the Loan Proceeds Be Used For?

During the covered period, an eligible recipient may use the proceeds of the covered loan for:

1. payroll costs;
2. costs related to the continuation of group health care benefits during periods of paid sick, medical, or family leave, and insurance premiums;
3. employee salaries, commissions, or similar compensations;
4. payments of interest on any mortgage obligation;
5. rent (for leases in place on February 15, 2020)¹;
6. utilities; and
7. interest on any other debt obligations that were incurred before the covered period.²

The language in the Act steps over itself somewhat because ‘payroll costs’ are defined to include #2 and #3.

¹ Section 1106 of the Act, page 42

² Section 1102 (a)(2) of the Act, page 20

What is the Covered Period?

The period beginning on February 15, 2020 and ending on June 30, 2020.³ However, see discussion below regarding loan forgiveness.

What Is a Covered Loan?

A loan made under the Paycheck Protection Program during the covered period.

What Are Payroll Costs?

The term ‘payroll costs’⁴ means the sum of payments of any compensation with respect to employees that is a;

- 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

Are there any limitations?

There are two limitations on the calculation of payroll costs⁵:

- Payments to an employee whose principal place of residence is outside of the United States will not qualify;
- Compensation of an individual employee in excess of an annual salary of \$100,000, as prorated for the covered period, will not qualify. Essentially, the maximum compensation per employee is \$1,923 per week (thus, a maximum of \$15,384 overall). The limitation refers to “compensation” and not payroll costs so it appears that in addition to the \$1,923 of compensation, the health insurance premiums, retirement, etc. will be allowed.

Are Owners and Self-Employed Individuals Covered?

Yes. The Act provides⁶ that payroll costs include:

the sum of payments of any compensation to or income of a sole proprietor or independent contractor that is a wage, commission, income, net earnings from self-employment, or similar compensation ...

The self-employed payroll costs are limited to the same \$100,000 annual proration that applies to employees.

However, note that payroll costs for the self-employed appear to be limited to wages, etc. while payroll costs for employees are the wages plus health insurance premiums, retirement, etc.

³ Ibid, page 10

⁴ Ibid page 10

⁵ Ibid, page 12

⁶ Ibid, page 12

Are Part-time or Season Employees Covered?

Yes. The term ‘employee’ includes individuals employed on a full-time, part-time, or other basis.⁷

Loan Forgiveness

A subsequent blog will have more extended discussion of the loan forgiveness rules. However, there could be some confusion arising over the definition of ‘covered period’. The borrowing provisions described above (covered in Section 1102 (a)(2) of the Act) referred to the covered period as February 15 to June 30. In fact, the more important time limitation is set forth in the Loan Forgiveness provisions.⁸

The amount of the loan that would be forgiven would be payments made in the ‘covered period’ defined as the 8 week period beginning on the date of the origination of a covered loan.⁹ In other words, although the loan may be granted referencing the February 15 to June 30 period, the amount of the loan to be forgiven will be based on the 8 week period starting when the loan originated.

There are clearly minefields to be avoided with this legislation. However, the benefits, viz. Government payment of payroll, rent and interest for 8 weeks, are very attractive.

We will be providing further blogs in short order addressing other issues of the Paycheck Protection Program.

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⁷ Ibid, page 17

⁸ Section 1106 of the Act

⁹ Ibid, page 41