

OBSERVATIONS

CARES Act – Business Tax Provisions 3

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The CARES Act was signed by the President on Friday and is now law. The Act has numerous provisions, one of which is the Paycheck Protection Program (PPP). PPP will provide loans to businesses for payroll and certain other costs. The big bonus is that these loans can be forgiven in the future.

Mechanically, the Act amends the Small Business Administration statute (15 U.S.C. 14A), specifically, Section 636. PPP is added as subsection 36 to Section 636 (a).

The following is our reading of the Bill and is subject to any administrative interpretation issued by the Small Business Administration. This blog will review how much can be borrowed and who is eligible.

Maximum Amount of Loan

The PPP provides for loans to cover payroll, rent, interest and utility expenses. However, the measurement of the amount of the loan is solely payroll.

The general rule is that the maximum loan is the lesser of 250% of the average monthly payroll costs for the prior year or \$10,000,000.¹ There are some exceptions (discussed below). Note that the loan may also include amounts for SBA disaster loans made after January 31, 2020.

In detail, average monthly payroll costs are the average total monthly payments by the applicant:

- for payroll costs (see definition below)
- incurred during the 1-year period (note that it is essentially an accrual calculation, i.e. the liability was incurred in the 1 year period)
- before the date on which the loan is made (this means that when the loan application is filed, there may have to be some estimate of the costs).

The term ‘payroll costs’² 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.

¹ Section 1102 (a)(2) of the Act, which adds subsection 36 (E) beginning page 17

² Section 1102 (a)(2) of the Act, which adds subsection 36 (A), page 10

- 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; or
- Payment of State or local tax assessed on the compensation of employees.

Note:

- there is a cap for employees who make more than \$100,000;
- the employee must reside in the United States
- self-employed individuals are included in the coverage³

The rules are modified for seasonal and startup businesses.

Seasonal businesses can determine average monthly costs using the 12 week period beginning either February 15, 2019 or March 1, 2020 (applicant's election).

If the business is a startup, i.e. was not in business between February 15, 2019 and June 30, 2019, then the average monthly payroll costs are determined by reference to the period January 1, 2020 to February 29, 2020.

In summary: loans are available to cover payroll costs plus certain other expenses (e.g. rent, interest, utilities); however, the amount of the loan is based solely on payroll costs. Assuming flat and level payroll costs that would translate to approximately 25% of the loan available for the non-payroll eligible expenses.

Who is Eligible?

The Act defines an 'eligible recipient' as: "an individual or entity that is eligible to receive a covered loan"⁴. A 'covered loan' is "a loan made under this paragraph during the covered period."⁵

Any business concern, nonprofit organization, veteran's organization, or Tribal business concern with no more than 500 employees is eligible.⁶ A 'nonprofit organization' means an organization that is described in section 501(c)(3) and exempt from taxation under section 501(a)⁷.

There is a required certification that must accompany the loan application, which must contain, among other representations, the representation:

That the uncertainty of current economic conditions makes necessary the loan request to support the ongoing operations of the eligible recipient⁸

³ See Maloney & Kennedy Blog CARES Act: Business Tax Provisions 2

⁴ Section 1102 (a)(2) of the Act, which adds subsection 36 (A), page 10

⁵ Ibid, page 9

⁶ Ibid, page 14

⁷ Ibid, page 10

The economic upheaval has been such that most businesses have been impacted and/or will soon be impacted. The purpose of the Act is to ensure that companies/organizations will not have any more layoffs. Presumably, therefore, this certification standard will be very liberal.

The fact that the company has access to other business loans will apparently not be a consideration.

During the covered period, the requirement that a small business concern is unable to obtain credit elsewhere, as defined in section 3(h), shall not apply to a covered loan.⁹

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

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⁸ Ibid, page 23

⁹ Ibid, page 24