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**President Signs CARES Act into Law. Expands SBA Loan Programs to Allow for Paycheck Protection Program Loans to Assist Businesses**

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On March 27, 2020, President Trump signed the Coronavirus Aid, Relief, and Economic Security Act (CARES Act). The CARES Act is designed to assist Americans hurt by unprecedented restrictions on business activity that Federal, State and local governments have mandated, in response to the coronavirus (COVID-19) pandemic. The CARES Act is intended to provide direct financial aid to American families and businesses, including payroll and operating expense support for small businesses, and loan assistance for distressed industries.

**GENERAL REVIEW OF THE CARES ACT PAYCHECK PROTECTION PROGRAM:**

The CARES Act creates a new Small Business Administration (SBA) loan program designated as the “Paycheck Protection Program.” The Paycheck Protection Program will be implemented through an expansion of the SBA’s existing Section 7(a) program and will offer employers the opportunity to secure low-interest loans in amounts of up to \$10 million. If employers use those loans to continue funding payroll, rent, mortgage interest and utilities, a portion of the loan may be permanently forgiven. The attorneys of Schenck Price Smith & King are prepared to provide you with critical guidance on how to apply for such loans and adhere to any guidelines required to achieve maximum forgiveness of those loans.

Paycheck Protection Program loan proceeds may be used for the following purposes:

- Payroll support (including paid sick or medical leave)
- Employee salaries
- Mortgage, rent and utility payments
- Insurance premiums
- Other qualified debts

Borrowers who have incurred certain expenses during an eight week period following origination of the Paycheck Protection Program loan, may be eligible for loan forgiveness, to the extent that the loan proceeds were applied to:

- Payroll costs
- Interest accrued on an eligible mortgage prior to February 15, 2020
- Rental payments pursuant to a lease that was in effect prior to February 15, 2020

- Certain utility costs for service that commenced prior to February 15, 2020.

Loan forgiveness is tied to employee retention and continued employee compensation. If an employer fails to retain employees or reduces employee compensation beyond certain benchmarks set forth in the CARES Act, the amount of loan forgiveness will be reduced.

The CARES Act also offers certain subsidies for existing SBA Section 7(a) loans and departs from standard SBA loan requirements, in several respects, including the following:

- No personal or collateral guaranty will be required
- No certification by Borrower that it is unable to obtain credit elsewhere
- There will be a requirement that the Borrower certify that the loan is necessary due to circumstances created by the COVID-19 pandemic
- The Borrower must certify that the loan proceeds will be used for a purpose permitted under the CARES Act
- The Borrower must also certify that it is not receiving funds from another SBA program for the same purposes for which the Borrower has applied under the CARES Act
- CARES Act loans will have a term not to exceed ten years
- The interest rate on a CARES Act loan shall not exceed 4% and interest payments are deferred for up to one year
- No prepayment penalty shall be applied to a CARES Act loan.

#### **QUALIFICATION:**

In order to qualify for a CARES Act loan, the applicant must be a business that employs 500 or fewer employees. Notwithstanding this requirement, if the applicant's industry has an SBA size standard that permits more than 500 employees, the applicant may be eligible for a CARES Act loan. The applicant must have been operational, at that size, on February 15, 2020. The SBA size standards consider business combinations under common control (50% ownership or control) to be affiliates whose combined numbers will be used to determine the 500 employee maximum permitted by the CARES Act. A significant exception to that rule applies to hospitality and restaurant businesses, franchisees, and recipients of Small Business Investment Company (SBIC) investment.

Simply put, the 500 employee maximum for those businesses is applied on a local or regional basis. For example, a restaurant chain or franchise with more than 500 total employees may qualify for CARES Act loans for specific franchises or restaurant locations within a given locality or region. We can help you determine if your specific business location may qualify for a CARES Act loan, even if your total employee count exceeds the 500 employee maximum.

#### **SIZE STANDARDS:**

In establishing size standards, the SBA looks at several critical factors. First, size standards should vary from industry to industry to account for differences among industries. Second, a small business concern cannot be dominant in its field of operation, nationally. Third, the policy

decisions of the Agency should assist small businesses as a means of encouraging and strengthening their competitive position in the economy.

The SBA's size standards methodology examines the structural characteristics of an industry as a basis to assess industry differences and the overall degree of competitiveness of an industry and of firms within the industry. The SBA reviews all size standards and adjusts them, as necessary, every five years based on the analysis of industry and Federal contracting factors in accordance with the Small Business Jobs Act of 2010 (the Jobs Act) (Public Law 111-240, 124 Stat. 2504, Sept. 27, 2010).

Over the years, SBA has adopted a broad range of size standards – manufacturing industry standards ranged from 250 employees to 1,500 employees; other industry size standards ranged from \$0.10 million to \$38.5 million in average annual receipts. SBA establishes its size standards for industries using the latest NAICS industry definitions, developed by the Office of Management and Budget (OMB) in collaboration with U.S. Census Bureau, other U.S. Federal Statistical Agencies, and Statistical Agencies of Canada and Mexico.

The most recent [SBA Table of Size Standards](#) was adopted by the SBA on August 19, 2019. It is not clear, at this point, whether the size standards will be further amended as part of the CARES Act. The SBA's website, also has a [Size Standards Tool](#) that may be helpful in assessing what size standards apply to your business.

#### **FORGIVENESS:**

CARES Act loans include an unusual and significant feature. If the applicant strictly complies with certain requirements, the CARES Act loan will be partially forgiven. That forgiveness, as mentioned earlier, would be based upon certain expenses incurred during the initial eight weeks following the funding of the CARES Act loan, including payroll costs, rent, utilities, mortgage interest payments and other qualified expenses related to leases, mortgages, utility contracts etc. that were in effect on February 15, 2020. Eligible payroll costs are limited to compensation of \$100,000 or less.

The amount of any loan forgiveness will be affected by any significant reduction in employee compensation or reduction in workforce. Reduction in employee compensation in excess of 25% for any individual employee will adversely impact a claim for loan forgiveness. Nonetheless, the CARES Act will not penalize employers who rehire workers previously laid off, if they have a reduced payroll at the commencement of the period designated for forgiveness. Forgiveness of a portion of the CARES Act loan will not be recognized as taxable income for federal income tax purposes. Any amount not forgiven at the end of one year will remain due and payable as a loan, at a maximum interest rate of 4% for a term not to exceed ten years.

CARES Act loans will be offered by the same lenders who now participate in the SBA's Section 7(a) loan program. Applications for forgiveness will also be processed by those lenders. The lenders will be required to approve or deny applications for loan forgiveness within 60 days following receipt of the Borrower's application. If the lender determines that a partial loan forgiveness is warranted, the SBA is authorized to reimburse the lender for the principal amount

of the forgiven portion of CARES Act loan, together with accrued interest, not later than 90 days following the lender determination.

**LOAN AMOUNT:**

No CARES Act loan shall exceed the lesser of \$10 million or a loan amount equal to 2.5 x Total Monthly Payments for Payroll Costs for the year immediately preceding the CARES Act loan. The CARES Act loan may also include the remaining balance of a loan made under the SBA's Disaster Loan Program between January 31, 2020 and the date that such loan may be refinanced under the CARES Act.

**DURATION OF THE CARES ACT:**

The eligible period for submitting a loan application under the CARES Act is the period commencing February 15, 2020 and ending December 31, 2020.

**FEDERAL GUARANTY:**

The federal government currently guaranties Section 7(a) loans at the rate of 75% for loans in excess of \$150,000 and 85% for loans equal to or less than \$150,000. The federal government will guaranty CARES Act loans at a rate of 100% through December 31, 2020.

**EXPANSION OF SBA PROGRAM:**

The Department of Treasury is authorized by the CARES Act to expand the pool of lenders authorized to offer SBA loans, in recognition of this national emergency.

**EFFECT ON EXISTING SBA LOANS:**

For a six month period, commencing on the next payment due date, the SBA will pay principal, interest and other fees due and owing on certain existing SBA Section 7(a) loans. If your loan is currently in deferment, you would be entitled to an additional six month period of deferment commencing on the next payment date. Except for Paycheck Protection Program loans, loans made during the six month period following enactment of the CARES Act will also be eligible for a six month deferment.

**OTHER DISASTER RELIEF AVAILABLE:**

Prior to enactment of the CARES Act, certain legislation was enacted to address the COVID-19 pandemic. That prior legislation also included disaster assistance loans that may offer assistance to your business. For instance, the Coronavirus Preparedness and Response Supplemental Appropriations Act greatly expanded the Economic Injury Disaster Loan (EIDL) program. You should be aware that a Borrower receiving a CARES Act loan is precluded from receiving an EIDL loan for the same purpose.

The EIDL loan program has several beneficial features, not the least of which is the availability of an emergency grant that allows an eligible business to request an advance on the EIDL of up to

\$10,000. That advance would not need to be repaid, even if the business is eventually denied an EIDL.

The SBA will be developing rules to implement the legislation which will be forthcoming in the days/weeks ahead to provide additional guidance which we will continue to monitor. The attorneys at Schenck Price Smith & King, LLP have studied the CARES Act and other relevant emergency legislation and welcome your inquiries. We will assist you in determining how best to assess the various benefits and eligibility requirements for each program. Please feel free to contact our attorneys to assess your best course of action in this trying time.

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