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SPECIAL ALERT FOR BUSINESSES ON

The Coronavirus

Economic Relief for Your Business With CARES Act Loan Program

On March 27, 2020, Congress enacted the Coronavirus Aid, Relief, and Economic Security Act (the “CARES Act”), which provides certain economic relief to businesses, organization and employees impacted by the rapidly expanding COVID-19 pandemic.

Among other things, the CARES Act creates a new loan program guaranteed by the U.S. Small Business Administration (the “SBA”) for the purpose of funding forgivable loans to eligible businesses and organization to assist them in continuing to pay payroll expenses and certain other eligible business expenses. Like many other SBA loan programs, loans may be made to eligible applicants by lenders participating in the SBA’s loan program. Below is a brief summary of the new loan program that may be of particular interest to businesses and organizations contending with the economic fallout from the pandemic.

Payroll Protection Loans

Pursuant to Section 1102 of the CARES Act, certain businesses, non-profit organizations, and self-employed individuals may immediately apply for loans fully guaranteed by the SBA to cover certain payroll related costs and other eligible costs incurred in connection with the operation of such business or organization (defined as a “covered loan”). The new law specifically sets aside \$349,000,000,000 to fund covered loans made under the new program through June 30, 2020.

Significantly, the interest rate that may be imposed on a covered loan cannot exceed 4%, payment of principal, interest, and fees on a covered loan may be deferred for a period of at least six (6) months and up to one (1) year after the loan is made, and the entire principal amount of the loan is eligible to be forgiven.

Who is Eligible?

Under the new law, for the period beginning on February 15, 2020 through June 30, 2020 (defined as the “covered period”), businesses, nonprofit organi-

zations, veteran organizations, certain Tribal business concerns, and self-employed individuals (an “Eligible Recipient”) are eligible to apply provided that:

- The business or organization employs less than 500 employees, which includes individuals employed on a full-time, part-time or other basis;
- If applicable, the size standard established by the SBA for the particular industry in which the applicant operates.

Moreover, businesses with more than one (1) physical location and assigned a North American Industry Classification System code beginning with “72” (Accommodation and Food Services) are also eligible to the extent they do not employ more than 500 employees per physical location.

Applicants seeking a covered loan must make a “good faith certification” in the application that the uncertainty of the current economic conditions make it necessary to request a covered loan to support its ongoing operations. However, there is a presumption that any business or organization has so been affected if it was operating on February 15, 2020.

Permitted Uses of Loan Proceeds

Eligible Recipient’s may apply for a “covered loan” to fund payment of the following eligible expenses:

- “Payroll costs”;
- Payment of interest of any mortgage obligation;
- Rent (including rent under a lease agreement);
- Utility costs;
- Interest on any other debt obligations that were incurred prior to February 15, 2020.

Eligible “payroll costs” include: (i) salary, commission and other similar compensation arrangements; (ii) vacation, sick, medical, or family and parental leave; (iii) costs related to the continuation of health care benefits, including insurance premiums; (iv) retirement benefits; and (v) payment of any State or local taxes assessed on the compensation of employees.

“Payroll costs” specifically does not include the amount of compensation of any individual employee in excess of an annual salary of \$100,000 (prorated for the covered period), certain federal taxes, and compensation paid to any employee whose principal place of residence is outside of the United States. A similar limitation is imposed with respect to wages and earnings for sole proprietors that earn in excess of \$100,000 for one year, prorated for the covered period.

Maximum Amount of Loan

The amount of a covered loan made to an Eligible Recipient under the new program cannot exceed:

- i. 250% of the average total monthly payments for “payroll costs” incurred for the prior year; or
- ii. \$10,000,000.

To the extent an Eligible Recipient was not in business for the period between February 15, 2019 through June 30, 2019, the otherwise Eligible Recipient may use its average “payroll costs” for the period beginning on January 1, 2020 and ending on February 29, 2020 for purposes of determining the amount of the covered loan it is eligible for, subject to the cap of \$10,000,000. There are also special rules for seasonal employers.

Deferment and Other Loan Terms

Significantly, payment of principal, interest, and all SBA fees on a covered loan **are completely deferred** for a period of at least six (6) months and up to one (1) year after the loan is made if a business or organization was operating on February 15, 2020.

Other notable terms of the new loan program include:

- There is no requirement the covered loan is secured by collateral;
- The covered loan shall be made on a “nonrecourse basis”, meaning that no individual, shareholder, member, or partner of an Eligible Recipient is personally liable for the covered loan;
- The failure of an Eligible Recipient to otherwise qualify for other loan programs (e.g. for credit reasons) does not apply to covered loans;
- The interest rate accruing on a covered loan shall not exceed 4%.
- The covered loan shall have a maximum maturity of ten (10) years (assuming the entire amount is not forgiven, as described below).

Loan Forgiveness

An Eligible Recipient **may apply to have the indebtedness of a covered loan forgiven**. Notably, the law specifically provides that the amount forgiven is not subject to cancellation of indebtedness income under the Internal Revenue Code, meaning Eligible Recipients will not have to pay any federal income tax on the amount of the covered loan forgiven.

The amount that is eligible to be forgiven is equal to the sum of the following costs incurred by the Eligible Recipient during the eight (8) week period after a covered loan is made:

- i. “Payroll costs”
- ii. Payment of any interest of a mortgage incurred prior to February 15, 2020;
- iii. Lease payments made under a lease agreement entered into prior to February 15, 2020;
- iv. Payments made for the provision of electricity, gas, water, transportation, telephone, or internet access and for which service began prior to February 15, 2020.

The amount that is forgiven amount is limited as follows:

- It shall not exceed the principal balance of the covered loan;
- It shall be reduced based on a percentage of the reduction of an Eligible Recipient’s full-time equivalent employees during the eight (8) week period after the covered loan is made, if any;
- It shall be reduced based on certain reductions in the total salary or wages of certain employees.

For purposes of determining the reduction based on an Eligible Recipient's employees, the amount is calculated by dividing:

- i. the average number of the Eligible Recipient's full-time equivalent employees during the eight (8) week period after a covered loan is made; by
- ii. the average number of the Eligible Recipient's full-time equivalent employees per month that were employed during the period of February 15, 2019 through June 30, 2019 or January 1, 2020 through February 29, 2020 (the Eligible Recipient has the option of determining which period to use).

For employers who have already laid off employees or taken steps to curtail wages in response to the pandemic, there is relief to the forgiveness reduction to the extent employees are rehired or made whole for wage reductions by June 30, 2020.

In addition, the amount eligible to be forgiven is further reduced by the decrease in total salary or wages of an employee during the eight (8) week period after the covered loan is made and which is in excess of 25% of the employee's total wages or salary for the most recent quarter. However, this only applies to employees that did not receive, during any single pay period in 2019, wages or salary at an annual rate of \$100,000 or more.

For purposes of illustration, let's assume an Eligible Recipient obtains a covered loan in the amount of \$1,000,000. Let's also assume the Eligible Recipient incurs \$1,000,000 in eligible expenses qualifying to be forgiven (such as payroll expenses, rent payment, and utility costs during that period).

In our hypothetical scenario, for the period of February 15, 2019 through June 30, 2019, the Eligible Recipient employed an average of 100 full-time employees. Thereafter, for the eight (8) week period after a covered loan is made, the Eligible Recipient employs on average 80 full-time employees, and there was no reduction in salary or wages for any full-time employee that made less than \$100,000 on an annualized basis in 2019. In that case, the total amount of the covered loan eligible to be forgiven is equal to \$800,000, calculated as follows:

- \$1,000,000, multiplied by
- .80 (80 full-time employees/100 full-time employees).

Finally, an Eligible Recipient seeking forgiveness of a covered loan is required to submit to the lender an application, which must include, among other things: (i) documentation verifying the number of full-time equivalent employees on payroll and pay rates for the required periods; and (ii) documentation substantiating expenses made that are eligible for forgiveness (such as lease, mortgage, and utility payments).

We anticipate additional guidance will be issued by the SBA to assist businesses and organizations seeking loans through the new program implemented by the CARES Act. Our experienced team of lawyers continue to be available to assist you as needed, including advising on eligibility and the application process.

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