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CARES Act to Provide Needed Aid to Small Businesses Dealing with Uncertainty and Disruption

Legal Alert

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The "Coronavirus Aid, Relief, and Economic Security Act" was signed into law by the President on March 27th in an attempt to curtail the massive economic fallout that is likely to result from the near complete shutdown of American commerce amid the COVID-19 pandemic. This comprehensive bill provides financial resources that augment the individual states' responses. This alert will explain some of the relief provided by the CARES Act that affect businesses grappling with these difficult times. It provides only a summary of the highlights of the Act and should generally apprise you of the programs available.

The CARES Act allocates an additional $349 billion to loans and grants through the Small Business Administration (SBA). For small and midsize businesses, the most significant result of the Act is to amend Section 7(a) of the Small Business Act to create the Paycheck Protection Program (PPP). The PPP provides loans of up to two and a half times a borrower's average monthly payroll expenses (over the last twelve months) in order to pay employee wages, benefits, insurance premiums, mortgage, rent, and utility payments. "Payroll expenses" include employee pay, leave (vacation, sick, parental, family, etc.), and health insurance and premiums, but is subject to limitations for high earning employees. This program is designed to encourage and incentivize businesses with less than 500 employees to retain their labor force. Eligibility standards focus on whether the business was operational before the crises, not its ability to repay. The CARES Act also waives the "credit elsewhere" test and no longer requires a personal guarantee for PPP loans. All PPP loans have a maximum interest rate of 4%, but as shown below, some or all of these loans may be forgiven. Furthermore, the CARES Act provides that the SBA will pay principal and interest on existing and new SBA loans for six months.

PPP loans are eligible for forgiveness upon meeting certain standards and this canceled indebtedness will not be recognized as income. The SBA will forgive the amount that the borrower spent during the first eight weeks after receiving funds on: (i) payroll costs as defined above; (ii) interest on existing mortgages (iii) payments of existing rents; and, (iv) payments of existing utility service. Since the CARES Act is attempting to prevent job losses, a borrower's eligibility to have its loan forgiven is proportionally reduced by any reduction in employees compared to the prior year. A borrower's loan forgiveness is also reduced if an employee's pay is decreased beyond 25% of his or her previous year's pay. However, if an employer has already laid off or reduced an employee's pay, it can reinstate that employee prior to June 30, 2020 without suffering a reduction in forgiveness.

In addition to the PPP, the CARES Act expands the availability of Economic Injury Disaster Loans (EIDLs) and expands the business entities eligible to receive them. The CARES Act waives the need for personal guarantees for EIDLs less than $200,000 and approval is based strictly on the applicant's credit score. Any applicant for an EIDL can also request up to $10,000 in an Emergency Grant that the SBA must distribute within three days. The advance payment through the Emergency Grant may not need to repaid but must be used to: (i) pay sick leave to employees; (ii) maintain payroll; (iii) meet increased costs to obtain materials;

(iv) make rent or mortgage payments; or (v) repay obligations that cannot be paid due to revenue losses. Emergency funds or EIDLs that convert to SBA loans through the PPP can be forgiven as stated above.

The Act also provides valuable tax credits of 50% of the first $10,000 of wages paid by employers to each employee during the crisis. To be eligible, an employer must have had its operations fully or partially suspended due to a shut-down order or had its gross receipts decline by more than 50% compared to the same quarter last year. There are different rules concerning what wages are qualified depending on the number of employees a particular business employs. In addition to the tax credit, an employer or self-employed individual can defer payment of the employer share of Social Security tax and allows such payments to be made over two years with half due by the end of 2021 and other half due at the end of 2022. Additionally, the CARES Act expands the ability of businesses to offset operating losses and retroactively apply them to previous years (carry-back NOLs).

In addition, the CARES Act provides for tax credits for employers who pay the required enhanced leave for employees affected by COVID-19. Employers can receive tax credits for up to $511 per day per employee when they pay employees under sick leave. Much more information regarding paid leave can be found in Adam Gersh’s three part employer’s guide: Part 1 | Part 2 | Part 3.
The CARES Act requires the SBA to promulgate rules promptly that should provide some more details on the available funds, process, and administration of these loans. Interested borrowers should contact the SBA here. Additionally, funds are available at the state and local level and will be the topic of another Flaster Greenberg post in the near future.

Finally, the CARES Act expanded the number of businesses that can seek Chapter 11 bankruptcy relief under the recently enacted Small Business Reorganization Act of 2019 (SBRA). For the next year, the SBRA is available to businesses that owe less than $7.5 million in total debt, which is nearly three times higher than the original SBRA limitation. The SBRA, like a more traditional chapter 11 bankruptcy, allows a debtor to reorganize its balance sheet with the intention of setting forth a bankruptcy plan that will allow the company to operate profitably in the future. The advantage of the SBRA is that it is designed to provide a streamlined process, reduce costs, and provider a quicker exit from bankruptcy as compared to the traditional Chapter 11 bankruptcy where its cost can be a significant barrier to entry. Although businesses rarely want to consider bankruptcy, it can prove to a significant step toward regaining solvency and emerging from this crisis.

If your company is one of the millions struggling with this disruption, it should consider whether it can utilize the funds available in order to meet the short-term liquidity crunch. As always, Flaster Greenberg's attorneys are available to assist you and we are here to help your company through this difficult time. The next section contains important links that can provide assistance to businesses.

COVID-19 Resources

- Flaster Greenberg COVID-19 Resource Page
- U.S. Small Business Administration Disaster Loan Assistance
- Pennsylvania COVID-19 Resource Page
- Pennsylvania Department of Community and Economic Development Resources
- Philadelphia Small Business Loans

- Philadelphia Industrial Development Corporation COVID-19 Resources
- New Jersey COVID-19 Resource Page
- New Jersey Small Business Development Corporation COVID-19 Resources
- New York State COVID-19 Resource Page
- New York City COVID-19 Business Resources
- Delaware COVID-19 Support for Businesses
- Delaware Small Business COVID-19 Support

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