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Summary of CARES Act

March 26, 2020

CARES Act (Coronavirus Aid, Relief, and Economic Security Act)

Below is a summary of certain provisions of HR 748, the bill approved by the Senate on March 25, 2020. Please note that the legislation still requires review and approval by the House and signature by the President and the provisions are subject to change. The summary focuses primarily on provisions directed at assistance for businesses, nonprofits, and their employees.

ASSISTANCE FOR SMALL BUSINESSES, NONPROFITS, AND SOLE PRACTITIONERS

1. Grants and Loans from the Small Business Administration

A major focus of the legislation is geared towards providing financial assistance to help businesses keep workers on the payroll during the physical and economic shutdown. These financial assistance provisions include a massive $350 billion Paycheck Protection Program (PPP), administered through the Small Business Administration, that will provide eligible entities with loans to cover the costs of payroll, healthcare benefits, mortgage interest, rent, utilities, and certain other obligations. The maximum amount of each loan is $10 million, with the actual permitted amount tied to the borrower's payroll costs[1] (and effectively limited to 2.5x the average monthly payroll incurred over the 1-year period prior to the loan, with exceptions for seasonality). The covered loan period begins on February 15, 2020 and ends on June 30, 2020. When paired with an eight-week loan forgiveness program, the PPP will effectively serve as a federal grant to eligible entities to keep employees on the books (or rehire employees that were recently laid off[2]) for at least a near-term period. The loan forgiveness will not be treated as gross income for tax purposes.

Importantly, the PPP specifically targets businesses in the hospitality and restaurant industries that would ordinarily not qualify as "small businesses" under governing SBA guidelines. Specifically, it waives the small business requirements for those industries to allow entities to potentially benefit from the PPP so long as they have no greater than 500 employees in a physical location, even if they are otherwise part of a larger company or affiliated with/franchises of a larger company. These waivers do not apply to other retail entities.

As importantly, the PPP expands beyond small businesses to include other organizations, including nonprofits and sole practitioners or self-employed individuals and waives personal guarantee and collateral requirements that would otherwise apply.

Of particular interest to lenders, the bill provides an avenue for lenders that are not currently authorized to make loans under Section 7(a) of the Small Business Act to be approved to make loans under the PPP and relieves lenders from having to make troubled debt restructuring (TDR) disclosures for any loans modified under the PPP to address COVID-19 related difficulties.

The PPP serves as an alternative to the SBA-administered Economic Injury Disaster Loan Program (EIDL Program) that was passed by Congress a couple of weeks ago. The legislation also expands the EIDL program to include sole practitioners and includes $10 billion in funding that would provide an immediate grant of up to $10,000 to entities that choose to pursue assistance under the earlier EIDL Program.

For those small businesses that are already the recipients of SBA loan assistance, the legislation offers $17 billion to fund a six-month subsidy for those loans.

2. Tax Code Adjustments Impacting Businesses

In addition to expanded unemployment benefits and tax rebates for individuals, the legislation provides targeted adjustments to the tax code for businesses. Again, to encourage businesses to keep workers on the payroll, the legislation provides a refundable payroll credit to those employers whose operations were either suspended due to a shutdown order or whose gross receipts declined by more than 50% during a calendar quarter. The legislation also defers the employer share of payroll taxes over a two-year period in subsequent tax years (2021 and 2022).

Again, the legislation includes targeted relief for particularly affected industries. For one, it corrects a technical error from the 2017 Tax Cuts and Jobs Act that mandated certain retail qualified improvement property expenses be depreciated over the 39-year life of the building, and it instead allows these expenses to be written off in one year. This provision will help businesses in the hospitality, restaurant, and retail industries by allowing them to amend their 2018 and 2019 tax return as well as continue to invest in their properties.

The legislation also adjusts the tax code to allow for certain net operating losses to be carried back to the previous five years which could potentially allow taxpayers to eliminate their tax liability or obtain refunds for tax paid in those years and temporarily removes the 80% taxable income limitation for years before 1/1/21 to allow for such losses to fully offset the taxpayer’s taxable income. Again, this will particularly help industries experiencing significant losses this year.

Other code adjustments include the deferral of the excess business loss limitations for pass-through businesses and sole proprietors, which is now only effective for tax years beginning after December 31, 2020; an increase to the business interest expense limitations (from 30% to 50% of EBITDA) to allow for additional interest deductions in taxable years beginning in 2019 or 2020; and the ability to accelerate the recovery of corporate AMT credits.

Lastly, the limitations related to charitable contributions have also been relaxed for both businesses and individuals. For cash contributions made during 2020, corporations are able to deduct up to 25% of taxable income.

3. Other Provisions Impacting Individuals

As noted above, the limitations related to charitable contributions have also been relaxed for individuals. For cash contributions made during 2020, individuals can deduct up to 100% of adjusted gross income. In addition, in 2020, taxpayers who do not itemize their deductions may deduct cash gifts to public charities of up to $300.

ASSISTANCE FOR CORPORATIONS

1. Corporate Lending Facilities

The other major component of the legislation is $500 billion in loans and other assistance to larger businesses. In addition to specific direct lending relief for airlines, cargo air carriers, and "businesses important to maintaining national security," the legislation provides Treasury (under its 13(3) program) with $454 billion to enable significant lending assistance to eligible businesses, municipalities, and states through Federal Reserve programs and facilities. The assistance comes with certain strings, including a requirement to maintain and retain at least 90% of employees, a ban on stock buybacks and dividends on common stock for a year after the loan is repaid, and limits on high-level executive compensation increases and severance packages (discussed below); and each loan must be sufficiently secured or made using a market-based interest rate (using pre-market Covid-19 standards). Participants will be subject to mandatory reporting and oversight by both a special inspector general and a Congressional oversight board.

One of the conditions to the assistance above involves restrictions on executive and officer compensation for the 1-year period after the loan or loan guarantee is no longer outstanding. The compensation limits vary based on the employee or officer's total compensation paid in 2019. If the employee or officer received more than $425,000 in total compensation in 2019, then during the 1-year period, that individual's total compensation during the 1-year period is limited to the same amount of total compensation she or he received in 2019. In addition, any severance is limited to two times the maximum total compensation that person received in 2019. For employees and officers who received more than $3,000,000 in 2019, the individual's compensation during the 1-year period is limited to $3,000,000 plus one-half of the amount of total compensation received in 2019 over $3,000,000. For these purposes, "total compensation" is defined broadly to include salary, bonuses, stock awards and other financial benefits.

Of particular relevance to mid-sized corporations and nonprofits, the legislation directs Treasury to "endeavor to implement" a special 13(3) facility targeted at providing financing to lenders that make direct loans to nonprofits and businesses with 500 to 10,000 employees – subject to certain conditions, including that the funds must be used to retain 90% of the workforce with full compensation and benefits through Sept. 30, 2020, a ban on stock buybacks and dividends on common stock until the loan is repaid and the recipient will not outsource or offshore jobs until two years after the loan is repaid.

2. Real Estate Financing

The legislation seeks to provide protection against certain foreclosures and evictions. (Note that these provisions are in addition to any protections enacted by states and municipalities.)

Foreclosures are prohibited for a 60-day period beginning on March 18, 2020 for any mortgage loan purchased by Fannie Mae or Freddie Mac, insured by HUD, the VA or USDA, or made directly by the USDA. Furthermore, any borrower with such loans experiencing financial hardship due to COVID-19 may apply for and receive forbearance on that loan for a period of up to 180 days, which period may be extended for up to 180 additional days.

Multifamily landlords with federally-backed mortgage loans (i.e. loans to real property designed for 5 or more families purchased, insured, or assisted by Fannie Mae, Freddie Mac, or HUD) that are experiencing financial hardship due to COVID-19 are eligible for up to a 90-day forbearance but may not evict or charge late fees to tenants for the duration of the forbearance period.

More broadly, any landlord with a mortgage that is insured, guaranteed, supplemented, protected, or assisted by HUD, Fannie Mae, Freddie Mac, or certain other programs is temporarily prohibited for 120 days from eviction filings or late fees or other penalties for nonpayment of rent.

3. Other Financing Provisions

The legislation also authorizes the FDIC to temporarily establish a debt guarantee program and authorizes NCUA to temporarily increase share insurance coverage for noninterest-bearing transaction accounts; provides nonbank financial companies with an exception to the OCC's lending limits aligned with the exception for financial companies and temporarily authorizes the OCC to exempt any transaction from the lending limits; temporarily reduces the Community Bank Leverage Ratio for qualifying community banks; allows financial institutions to elect to suspend requirements under U.S. GAAP for loan modifications related to the pandemic and suspend any determination regarding such modified loans; provides an option to insured depository institutions, bank holding companies, and affiliates to temporarily delay (but no later than 12/31/2020) measuring credit losses under the new Current Expected Credit Losses methodology; temporarily suspends the statutory limitation on the use of the Exchange Stabilization Fund for guarantee programs for the money market mutual fund industry; and temporarily enhances access to the Central Liquidity Facility.

OTHER ASSISTANCE IMPACTING CLIENTS

1. Relief Funding to States and Municipalities.

The legislation provides states and local governments with $150 billion in funding to offset expenses caused by the pandemic.

2. Appropriations to the Executive, Legislative, and Judicial Branches.

The legislation appropriates $340 billion to the federal government to deploy, much of which goes to state and local governments. Significant provisions include funding for hospitals ($100B) and educational institutions (including $14.25B in funding to higher education institutions), as well as funding for transit infrastructure grants ($25B). Smaller appropriations are specifically targeted at rental assistance for low-income, seniors, and other disadvantaged groups, including Section 8 voucher rental assistance ($1.25B), Section 202 elderly housing assistance ($50M), Section 811 disability housing assistance ($15M), and $1B in "project-based rental assistance" funding for reduced tenant payments as a result of the crisis. The appropriations also include funding for economic development grants for states and communities ($1.5B), child care and development block grants ($3.5B), community services block grants ($1B), community development block grants ($5B), and homeless assistance grants ($4B). Finally, appropriations also include $150M to the NEA and NEH to maintain continued access to cultural organizations and institutions of learning.

3. Changes Affecting Retirement Plans

Clients should be aware that the legislation includes other provisions affecting employers related to postponement of certain ERISA filing deadlines, retirement plan distributions, and delaying the due date for single employer pension plan contributions.

For example, the legislation expands the Secretary of Labor's authority to extend ERISA deadlines for up to a year in the event of a public health emergency declared by the Secretary of Health & Human Services.

The legislation also creates "coronavirus-related distributions" of up to $100,000 per participant from retirement plans, and such distributions are not subject to a 10% early withdrawal penalty. These distributions will be taxed over a 3-year period, or the participant may repay the distributions over a 3-year period. Participants may self-certify that they are eligible if they, a spouse or dependent have been diagnosed with coronavirus, or if they experience adverse financial consequences from coronavirus-related quarantine, furlough or layoff, from being unable to work or telework due to lack of child care, or from a closing or reduction of hours in the participant's own business.

The legislation also increases the maximum loan amount for retirement plans from $50,000 to $100,000, and allows loans calculated based on the full account balance, rather than 50% of the account balance. In addition, any outstanding retirement loan payments due through December 31, 2020, may be delayed for one year.

Furthermore, the legislation extends the due date for 2020 minimum required contributions for single-employer pension plans. The new due date is January 31, 2021, and the amount due is increased by interest accrued since the original due date, calculated at the plan's regular rate of return. Also, for purposes of Section 436 of the Code, the Act allows single employer pension plans to apply the most recently-ended plan year's adjusted funding target attainment percentage (AFTAP) on a going-forward basis, for plan years which include 2020.

The legislation also allows defined contribution plans and IRAs to suspend required minimum distributions due in 2020.

[1] Note payroll costs exclude certain compensation, including compensation to employees exceeding $100,000.

[2] Employers should be aware that another provision of the stimulus package provides some rehired employees who were let go after March 1, 2020 with access for paid family and medical leave, with limits on the paid and emergency sick leave amounts.