

# BURR ALERT

## Senate Passes CARES Act for Business Relief Amid Coronavirus Pandemic

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The Senate passed the largest-ever economic recovery legislation, dubbed the Coronavirus Aid, Relief, and Economic Security Act (the “CARES Act” or the “Act”) in response to the coronavirus pandemic late in the evening on March 25, 2020. The bill passed the Senate unanimously and will now move to the House of Representatives.

This alert is intended to serve as a primer on the relief provided to various businesses in the Act. It also includes a note on certain aspects of the Act which are relevant to businesses in the real estate industry. We anticipate guidance in the coming days to clarify the various provisions of the Act.

### Small Business Relief:

The CARES Act adds a new program to the arsenal of Small Business Administration (“SBA”) Section 7(a) loans: the paycheck protection program (“PPP”). The PPP is intended to provide greater benefits to a greater number of recipients than existing SBA Section 7(a) loan programs. It is important to note that these PPP loans, as with other Section 7(a) loans, are made by private lenders.

- Available for limited time period: PPP loans are only available from February 15, 2020 until June 30, 2020 (the “Covered Period”).
- Full Federal Backing: Loans under the PPP are 100% guaranteed by the SBA.<sup>1</sup>
- Maximum Interest Rate: 4%
- Increased Eligible Recipients: These PPP loans will be available for small business concerns (those businesses already typically capable of participating in the SBA Section 7(a) loan programs), non-profit organizations, veterans organizations, Tribal business concerns and any business concern, in each case, which employs no more than (i) 500 employees or (ii) the size standard in number of employees as established by the SBA for the particular industry in which that business concern, non-profit organization, veterans organization<sup>2</sup> or Tribal business concern operates, whichever is greater. In addition, individuals operating under a sole proprietorship, independent contractors and certain self-employed individuals are eligible. Special rules apply in the SBA Section 7(a) loan regulations with regard to counting employees

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<sup>1</sup> Lenders must agree to deferral of the PPP loan as described herein. Typically, under Section 7(a), the SBA guarantees only up to 85% of loans of \$150,000 or less, and only up to 75% of loans of greater than \$150,000.

<sup>2</sup> The Act specifically contemplates that affiliation rules to determinate employee number will apply with respect to non-profit organizations and veterans organization, “in the same manner as with respect to a small business concern.”

for these purposes, some of which are modified by the Act for those businesses in the restaurant and hospitality industries.

- Additional eligibility relief for restaurant and hospitality industries and certain other businesses:
  - During the Covered Period, any business concern “assigned a North American Industry Classification System code beginning with 72 at the time of disbursal” is eligible for a PPP loan so long as it does not employ more than 500 employees at single physical location.
  - Typically, affiliates of a business concern are included in calculating number of employees. However, for those restaurant and hospitality industry businesses, as well as business concerns that are franchises and “assigned a franchise identifier code” by the SBA and any business concern receiving financial assistance from a small business investment company, as contemplated in 15 U.S.C. 681 et seq., the requirement to take into account affiliate employees is waived.
- Borrower Requirements: An eligible recipient is subject to certain requirements:
  - Certification: A borrower must certify to the following: (i) that uncertain economic conditions make the loan necessary for on-going operations, (ii) acknowledge that the funds will be used to retain workers and maintain payroll or make mortgage, lease or utility payments, (iii) that the borrower does not have another SBA Section 7(a) loan pending to accomplish these same purposes, and (iv) affirm that the borrower has not received any duplicative funds under SBA Section 7(a) from February 15, 2020 until December 31, 2020.
  - Waiver of Certain SBA Section 7(a) Requirements: During the Covered Period, it is *not* required that a small business concern be unable to obtain credit elsewhere to obtain a PPP loan. Also, during the Covered Period, no personal guarantee or collateral is required to obtain a PPP loan.
- Maximum SBA Section 7(a) Loan Amount: During the Covered Period, the maximum SBA Section 7(a) loan amount is the lesser of: (i) \$10,000,000 or (ii) the amount derived from a formula to reflect the average of monthly payroll payments, multiplied by 2.5, and increased by existing outstanding economic injury disaster loans that may be refinanced during the Covered Period. For non-seasonal employers, the monthly average of payroll payments is determined based on the preceding year.
- Permissible Uses of Loan: In addition to other permissible uses for SBA Section 7(a) loans, these PPP loans may be used for the following purposes during the Covered Period: payroll costs, costs related to continuing certain employee benefits, costs of salaries and other compensation, payments of mortgage interest, rent, utilities, and interest on any debt obligation incurred prior to the Covered Period.

- “Payroll Costs” are generally defined as 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; 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. For sole proprietors or independent contractors, it is the sum of payments of any compensation to or income of a sole proprietor or independent contractor that is a wage, commission, income, net earnings from self-employment, or similar compensation and that is in an amount that is not more than \$100,000 in 1 year, as prorated for the covered period.
- “Payroll Costs” exclude:
  - The compensation of an individual employee in excess of an annual salary of \$100,000, as prorated for the Covered Period;
  - Taxes imposed or withheld under chapters 21, 22, or 24 of the Internal Revenue Code of 1986 during the Covered Period;
  - Any compensation of an employee whose principal place of residence is outside of the United States;
  - Qualified sick leave wages for which a credit is allowed under section 7001 of the Families First Coronavirus Response Act (Public Law 116–127); or
  - Qualified family leave wages for which a credit is allowed under section 7003 of the Families First Coronavirus Response Act (Public Law 116–127)
- What are other permissible uses of a PPP Loan?: Section 1102(a)(2)(F) of the Act, in providing the above uses of the proceeds of a PPP loan, provides that such uses are “in addition to the allowable uses of a loan made under this subsection.” As drafted, the Act contemplates that this provision will go into 15 U.S.C. 636(a). This subsection (a) of 15 U.S.C. 636 provides that the SBA is empowered to provide “loans for plan acquisition, construction, conversion, or expansion, including the acquisition of land, material, supplies, equipment, and working capital, and to make loans to any qualified small business concern . . . for purposes of this chapter.” This suggests the general uses for PPP loans seem very broad. However, there is no guidance here, and it is important to note that any amounts not paid to payroll and qualified mortgage, rent and utility expenses will generally not be included in determining the amount of the PPP loan that may be forgiven.
- Deferral: During the Covered Period, the SBA will require lenders to provide deferral for the payment of principal, interest and fees on all PPP loans for not less than 6 months and up to 1 year. The SBA has authority to purchase these PPP loans in the secondary market if a lender cannot provide deferral. You should expect more guidance here.

- Loan Forgiveness: SBA Section 7(a) loans made during the Covered Period are eligible for forgiveness in an amount equal to the sum of: (i) payroll costs, (ii) interest paid on a covered mortgage obligation (which does not include prepayment or payment of principal), (iii) payment on covered rent obligation and (iv) any covered utility payment. The amount forgiven cannot exceed the principal amount.
  - Reduction in Forgiveness Amount: The amount permitted to be forgiven is proportionately reduced by (i) a reduction in employees or (ii) by a reduction in the salaries/wages paid to employees during the Covered Period, with only employees who were not paid more than \$100,000 during 2019 counting for purposes of (ii). An exception is made with regard to this reduction for businesses that re-hire employees or increase salaries back to pre-existing levels by the end of the Covered Period.
  - Documentation: A business will need to retain records to apply for loan forgiveness to verify compliance, including payroll tax filings, certain state tax filings, unemployment insurance filings, and any payments of covered obligations. Forgiveness is explicitly disallowed unless documentation is provided to verify compliance.
  - No Additional Gross Income from Forgiveness: Any such loans forgiven will not be included in the business's gross income for U.S. tax purposes.
- Loans with Balances Remaining after Forgiveness: A PPP loan may have a balance remaining after eligible amounts are forgiven. If so, that balance is guaranteed by the SBA under its Section 7(a) rules,<sup>3</sup> and it will have a maximum maturity date of 10 years from the date on which the borrower applies for loan forgiveness.
- Coordination with Economic Injury Disaster Loans:
  - Refinancing: An economic injury disaster loan made from January 1, 2020 through the end of the Covered Period may be refinanced into a PPP loan
  - No Duplication of Benefits: A recipient of an economic injury disaster loan during the period from January 31, 2020 until the end of the Covered Period may seek a PPP loan so long as that economic injury disaster loan is "for a purpose other than paying payroll costs and other obligations set forth as permissible uses for PPP loans.

It is extremely important to note that a number of these provisions will require guidance from the SBA, and until that guidance is given, there is uncertainty as to how this relief will operate. This guidance will be very important to both the private lenders that will extend these PPP loans and the businesses that need them.

Additional Small Business Relief Includes:

- EIDL Grant: Small businesses may be awarded up to \$10,000 as a grant when applying for an economic injury disaster loan. Entities eligible for these EIDL grants include: (i) businesses with not more than 500 employees, (ii) individuals operating as sole proprietorships or as

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<sup>3</sup> Typically, under Section 7(a), the SBA guarantees only up to 85% of loans of \$150,000 or less, and only up to 75% of loans of greater than \$150,000.

independent contractors, (iii) cooperatives with not more than 500 employees, (iv) ESOPs with not more than 500 employees, or (v) Tribal small business concerns with not more than 500 employees. The SBA will cease to have authority to permit such grants on December 31, 2020.

- Greater general access to all Section 7(b) economic injury disaster loan programs: The foregoing businesses described above are also permitted to seek relief under Section 7(b) loan programs generally, as are private non-profit organizations, small business concerns (as defined by the SBA), and small agricultural cooperatives.
- Subsidization of all SBA Section 7(a) Loans (other than PPP loans):<sup>4</sup> The SBA will pay the principal, interest and any fees with respect to such loans that: (i) were made prior to the Act's enactment and are not in deferment, for a 6-month period beginning on the next payment due date; (ii) were made prior to the Act's enactment and are in deferment, for the 6-month period beginning with the next payment due date after the deferment period ends; and (iii) were made during the period beginning with the date of the Act's enactment and ending on the date 6 months after its enactment, for that 6-month period beginning with the first payment due date of that loan.
- Increase of Express Loan limits: An Express Loan is a special type of SBA Section 7(a) loan, which typically is capped at \$350,000. Under the Act, this cap is increased to \$1,000,000. This increase is set to expire on January 1, 2021.

Again, it is important to note that Congress has directed the SBA to come out with guidance that will be significant for these small businesses and lenders.

### Relief for Large and Mid-Market Businesses:

Title IV of the CARES Act includes the "Coronavirus Economic Stabilization Act of 2020," which includes \$500 billion in funds for relief to businesses that are not otherwise eligible for SBA relief. The Secretary of the Treasury will oversee the use of these funds to make loans, loan guarantees and other investments.

#### Direct Loans for Specified Industries

Of this \$500 billion, certain amounts are earmarked for "direct loans" to businesses in specified industries: (i) up to \$25 billion is earmarked for loans and loan guarantees to passenger air carriers and related business, (ii) up to \$4 billion is earmarked for loans and loan guarantees to cargo air carriers, and (iii) up to \$17 billion is earmarked for loans and loan guarantees for "businesses critical to maintaining national security."

- The Secretary has discretion in determining eligibility for these direct loans, but the Act provides that such direct loans must: (i) be made to an eligible business for which credit is not reasonably available; (ii) be "prudently incurred;" (iii) be sufficiently secured or made at an interest rate reflective of the risk; (iv) be for as short a duration as practicable (and no more than 5 years at most); (v) be conditioned on no stock buybacks (unless otherwise required under contractual obligation that pre-exist the Act) until 12 months after such loan or loan guarantee is not

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<sup>4</sup> Loans from the SBA to state development companies under 15 U.S.C. 695 et seq. and SBA loans or grants extended under Section 7(m) are also subsidized.

outstanding; (vi) be conditioned on no payment of dividends or other distributions until 12 months after such loan or loan guarantee is no longer outstanding; (vi) be conditioned upon the business maintaining its March 24, 2020 employment levels to the extent practicable until September 30, 2020 (and in no case to reduce employment levels by more than 10% from such date); (vii) be conditioned on certification that the business is U.S.-organized and domiciled and has significant operations and employment based in the United States; and (viii) be conditioned on the fact that the business must have incurred or is expected to incur losses due to the coronavirus that will jeopardize its business.

- These loans are also subject to the business complying with limitations on compensation of highly-compensated individuals (here, those individuals with total compensation in excess of \$425,000 based upon the 2019 calendar year).
- The Secretary must receive warrants or equity interests in these businesses (or, a senior debt instrument, at the Secretary's discretion). The Secretary will not exercise any voting power with respect to these instruments, but will maintain and dispose of them to benefit the government and taxpayers.
- These Direct Loans cannot be forgiven.

#### Federal Reserve Relief for Other Eligible Businesses:

All remaining amounts are available for use by the Secretary to make loans, loan guarantees or other investments in and otherwise support the Federal Reserve's existing systems to maintain financial liquidity and stability and lend to eligible businesses, as well as states and municipalities.<sup>5</sup> The Federal Reserve system will be used to (i) purchase obligations or other interests from issuers, (ii) purchase obligations, including in the secondary market, and (iii) make loans (including loans and advances secured by collateral).

- The Secretary may determine to make loans directly to eligible businesses pursuant to an available Federal Reserve system program ("Reserve Direct Loans") under the following conditions: (i) that business entity will not repurchase any equity interest in that business that is listed on a national securities exchange (or any parent company of that business) while the loan is outstanding and for 12 months thereafter (except to the extent required by a contract that pre-exists the Act); (ii) that the business will not pay dividends or otherwise make any distributions with respect to the common stock of the business until 12 months after the loan is no longer outstanding; and (iii) that no officer or employee of that business whose total 2019 compensation exceeded \$425,000 will receive amounts in excess of such amount received in 2019 or receive any severance pay or other benefits which exceed twice the maximum total compensation received by such officer or employee in 2019.<sup>6</sup>
- The Secretary has discretion to waive the requirements in (i)-(iii) for these Reserve Direct Loans to "protect the interests of the Federal Government."

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<sup>5</sup> These systems exist under Section 13(3) of the Federal Reserve Act.

<sup>6</sup> Officers and employees whose total compensation exceeded \$3 million are subject to special rules. Their compensation may not exceed the sum of \$3 million plus 50% of the excess compensation over \$3 million.

- Business aided hereunder must be U.S.-organized and domiciled business with significant U.S. operations.
- These Reserve Direct Loans cannot be forgiven.

#### Facilities Targeted for Mid-Size Businesses:

The Secretary of the Treasury is instructed to endeavor to implement a program under the general Federal Reserve relief described above that will make loans to eligible business, including “to the extent practicable,” non-profit organizations and businesses with between 500-10,000 employees. The rate for such loans will be no higher than 2% annually, and payment will be deferred for 6 months after the loan is made (or such longer period as the Secretary determines). An eligible business would need to certify: (i) the loan is necessary for on-going operations, (ii) the funds will be used to retain at least 90% of its workforce, at full compensation and benefits, until September 30, 2020, (iii) the business intends to restore not less than 90% of its workforce that existed as of February 1, 2020, with all compensation and benefits, no later than 4 months after the termination of this public health emergency, as declared by the Secretary for the Department of Health and Human Services, (iv) the business is U.S.-domiciled with significant U.S. operations, (v) recipient is not a debtor in a bankruptcy proceeding, (vi) recipient is U.S.-organized, (vii) recipient will not pay dividends with respect to any common stock or re-purchase any of its equity securities listed on a national securities exchange (or any equity securities of the parent company of that business), (viii) recipient will promise not to outsource jobs offshore for term of the loan plus 2 years, (ix) recipient will promise not to abrogate any collective bargaining agreements for the term of the loan plus 2 years, and (x) recipient will promise to remain neutral in any union organizing efforts for the term of the loan.

#### Main Street Lending Program

The Federal Reserve may also establish a “Main Street Lending Program” or other program to support small and mid-sized businesses as it determines necessary or desirable and consistent with section 13(3) of the Federal Reserve Act.

#### Treatment of Federal Loans for Tax Purposes

The Act provides that any loan made by the Treasury pursuant to the Act is to be treated as indebtedness for U.S. tax purposes, without original issue discount. The Secretary is to issue regulations on the treatment of such loans, including providing that any issuance of warrants, stock options, or other equity interests in connection with these loans will not result in an ownership change under Section 382 of the Internal Revenue Code.

#### Significant Provisions for Real Estate Businesses:

Significant for businesses in the real estate industry, the Act also provides the following for the following actions.

#### Forbearance for Multifamily Mortgage Loans

From the date of enactment of the Act until the termination of the national emergency resulting from COVID-19, as declared by the President, or December 31, 2020, whichever is sooner (the “Available Forbearance Period”), a borrower on a federally backed multifamily mortgage loan may request a

forbearance, provided it was current on its payments as of February 1, 2020 and can confirm that it is currently experiencing financial hardship. The servicer, upon this request, will provide forbearance for up to 30 days and extend the forbearance for up to two additional 30-day periods upon the borrower's request, so long as that request is made during the Available Forbearance Period and at least 15 days prior to the end of the applicable 30-day period.

A borrower that receives forbearance cannot, for the duration of the forbearance, evict (or initiate eviction) of a tenant for the applicable property solely due to nonpayment of rent or other fees or otherwise charge late fees, penalties or other charges due to late payment of rent.

For these purposes, a federally backed multifamily mortgage loan is generally any loan that is secured by a residential multifamily real property designed principally for the occupancy of five or more families and is made, in whole or in part, or insured, guaranteed, supplemented or assisted in any way by the federal government or in connection with a HUD program, or is purchased or securitized by the Federal Home Loan Mortgage Corporation or Federal National Mortgage Association.

#### Temporary Moratorium on Eviction Filings

During the 120-day period beginning from the enactment of the Act, a lessor of any dwelling occupied by a tenant, whether under a residential lease, without a lease, or with a lease terminable under state law, that is on "covered property" may not initiate any eviction proceeding for nonpayment of rent and other fees or charge any fees, penalties or other charges due to nonpayment of rent.

Further, such a lessor may not require a tenant to vacate such a dwelling unit before the date that is 30 days after the date on which the lessor provides the tenant with a notice to vacate, which notice may not be issued until the expiration of the 120-day period mentioned above.

For these purposes, a "covered property" is any property that: (i) participates in a covered housing program (as defined at 34 USC 12491(a)), (ii) participates in the rural housing voucher program (as defined at 42 USC 1490r), (iii) has a federally backed mortgage loan, or (iv) a federal backed multifamily mortgage loan.

We will follow the Act as it progresses through the legislative branch and to the President's desk and will provide further information as guidance is made available.

#### **To discuss this further, please contact:**

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