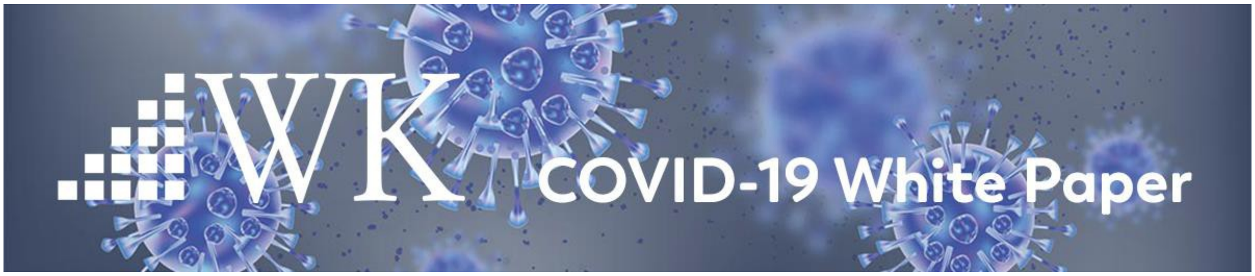

Business Responses to COVID-19 After the CARES Act and the Families First Act

Editor's Note: As we navigate these uncertain times, there is no "one-size-fits-all" approach to help businesses and their owners to identify financial management strategies made possible by recent United States government action in the response the international COVID-19 pandemic. Please contact your WK advisor to determine what options and opportunities might be best for your business in both a short-term and long-term sense.

COVID-19, though medical in nature, has had a devastating impact on businesses and the individuals who own or are employed by those businesses. There is much confusion and concern, and business owners find themselves asking "What is the best course of action?" as it relates to maintaining long-term business viability and ensuring the welfare of those they employ.

There are, unfortunately, no easy answers, and the optimal decisions will be different in each situation. In addition, business owners have new tools at their disposal, in the form of provisions found in the Coronavirus Aid, Recovery, and Economic Security Act (CARES Act), and the Families First Coronavirus Relief Act (Families First Act). This article identifies common situations businesses are facing and examines the tools and strategies available to navigate those situations effectively.

The situations and suggestions that follow ignore those cash-flow-enhancement provisions that are generally applicable in any situation. These include:

- deferring significant 2019 income tax payments and Q1 2020 estimates, enhanced to include amounts that would otherwise be paid Q2 2020, until July 15, 2020;
- working with current lenders to evaluate a modification of existing loans (e.g., interest-only for a period to preserve current assets);
- carrying 2018 – 2020 tax losses to prior years to recover previously paid taxes, as well as other changes that allow businesses to more quickly recognize the tax benefits associated with loss years; and
- expensing costs for qualified improvement property that was previously depreciated over 39 years, including retroactively to 2018.

These provisions will be useful in helping a business maintain cash flow, but as they generally do not require a decision between alternative courses of action, we will ignore them for the purposes of this article. Visit WK's website for our previous articles and alerts that address these topics.

Generally speaking, the most significant opportunity for most businesses with 500 or fewer employees, subject to some industry-specific exceptions, is the Paycheck Protection Program (PPP) administered through the Small Business Administration (SBA). In many instances this program can be used to strengthen current cash flow, by allowing businesses to access a loan that is subject to eventual forgiveness if qualifications are met. This strategy is not compatible with all other tools and resources, as noted in the following examples, so thought will need to be given to the optimal strategy given your business' specific situation.

Situation 1: Your business is continuing to operate, but you are concerned about taking care of your employees.

We have talked with many business owners whose businesses are continuing to operate somewhat normally (which is becoming fewer as new stay-at-home orders are issued), but they have questions about how to most effectively take care of their employees.

If your business has employees who are individually unable to work or telework due to six different situations related to COVID-19, the Families First Act requires your business to provide up to 10 days of paid sick leave, at two different levels of pay, depending on the reason leave is required. Additionally, if an employee is unable to work or telework due to a child's school or daycare closure related to COVID-19, you are required to provide 12 weeks of FMLA, of which the last 10 weeks are required to be paid leave at two-thirds of an employee's regular pay, up to a maximum of $200 per day. These provisions are effective April 1, 2020.

To minimize the cash "pinch" associated with requiring a business to provide this leave, the Families First Act provides payroll tax credits to reimburse businesses for leave paid under this Act beginning on April 1, 2020 and ending on December 31, 2020. If your business is already providing paid leave to employees for the specified COVID-19 reasons, your business is also eligible for reimbursement of the amount of leave it pays (beginning on April 1, 2020), up to the amounts required to be paid under the Families First Act. In other words, if you pay 100 percent of an employee's regular wage for a leave situation that only requires you to pay two-thirds of their normal wage under the Families First Act, you are only eligible for reimbursement of two-thirds of the leave payment.

Another option for funding employee payroll costs is PPP. This program provides loans to businesses to cover payroll, rent, utilities and interest payments. If the business maintains pre-COVID-19 employment levels and avoids significant reductions in employee compensation, any amount of the loan spent on payroll, rent, utilities and interest in the eight weeks following loan issuance is forgiven. The loan amounts are set at 2.5 times average monthly payroll over the last year, capped at $10 million, and the primary eligibility qualifications are that the business was operating on February 15, 2020 and that is has payroll expenses or payments to sole proprietors and independent contractors.

A final option to strengthen current cash flow is to delay payment of employer payroll taxes. As part of the CARES Act, employers can defer payment of employment taxes due from the date of enactment until December 31, 2020. Fifty percent of the deferred amount will be due on December 31, 2021, and the remaining 50 percent will be due on December 31, 2022.

It should be noted, however, that this deferral is not available to businesses that have indebtedness forgiven under the PPP. If the business is eligible for debt forgiveness under the PPP, that will produce a better overall outcome than the deferral of payroll taxes. However, if a business is not eligible for the PPP loan or choses to not participate in the PPP, this payroll tax deferral is a viable option to strengthen current cash flow.

Businesses in Situation 1 should first confirm qualification for the PPP and prepare their applications, then consider payroll tax payment deferral and the Generally Applicable provisions in the aforementioned order.

Strategies to choose from include:

1. **tax credits to provide post April 1, 2020 paid leave for leave necessitated by COVID-19;**
2. **a PPP loan that can be partially or fully forgiven; or**
3. **if a PPP loan is unavailable, businesses can defer payment of 2020 payroll taxes until 2021 and 2022.**

Strategies (1) and (2) can be used together, but you cannot receive duplicate tax benefits for them (e.g., reimbursed Emergency Sick Leave wages are not included in the wages paid under the PPP that are subject to loan forgiveness). Strategies (2) and (3) cannot be used in combination.

Situation 2: Your business is, or will soon be, unable to operate profitably due to the COVID crisis.

The typical decision business owners are wrestling with in this situation is whether to terminate employees now, or in the near term, to allow them to qualify for enhanced unemployment benefits, or to try to keep the employees on payroll and fund their pay using a combination of subsidized leave payments, payroll tax deferrals or credits and PPP loans.

One option is to shut down the business, temporarily lay off your employees and allow them to qualify for unemployment benefits during the business shutdown. If the business is unable to fund their pay at current levels due to lack of work/cash flow, this may provide the maximum compensation benefit to employees, but this strategy does come with the risks associated with laying off employees, including the possibility this layoff has a negative impact on employee engagement and morale, and the risk that employees find other employment in the meantime. These risks will be different for every situation, and communication with employees will be of the utmost importance.

During the COVID-related business shutdown, employees will not be eligible for Emergency Sick Leave or expanded paid FMLA under the Families First Act, even if the shutdown is mandated by federal, state or local directive. Affected employees will be able to draw enhanced unemployment benefits under the CARES Act. This assistance takes the form of weekly unemployment benefits at the normal state unemployment rate plus $600. This additional $600 weekly benefit is available through July 31, 2020.

Another option is to proceed as soon as possible with the PPP application to receive the benefits described above, allowing the business to weather the storm and keep employees on payroll until the situation improves. This could be used in combination with the tax credits to subsidize the enhanced leave options identified in Situation 1.

These two options, unemployment or PPP forgivable loans, would, at first glance, appear to be an “either/or” proposition, as the ability to have the Paycheck Protection Loans forgiven is reduced to the extent a business lays off or terminates employees and/or significantly reduces an employee’s pay.

A third option, however, that treats these two tools as a “both/and” strategy that may provide the best overall outcome, but it does have one significant risk, in addition to the previously identified risks. Specifically, a business could initially proceed with termination of its employees, allowing those employees to receive enhanced unemployment benefits during the shutdown. After a period of weeks, but no later than June 30, 2020, the business can rehire those employees and apply for benefits under the PPP.

This strategy works because the CARES Act will not reduce the benefit of the PPP (i.e., the ability to have the loan forgiven) if employees who have been terminated after February 15, 2020 are rehired, or if pay that has been reduced significantly after February 15, 2020 has been restored, by June 30, 2020. The employees and pay levels would need to be maintained for the eight weeks after the origination of the PPP loan.

The main additional risk associated with the combined option is that PPP funds may be completely tapped by the time the business attempts to access them. The downside of the shutdown-and-unemployment option, regardless of whether it is used in combination with the PPP, is that the employees may find other employment and are not available to return when the business is ready to reopen.

Finally, if a business has seen a significant downturn in revenue or has been forced to fully or partially suspend activities, that business is eligible for a credit against the old-age, survivors, and disability insurance (OASDI) portion of employer payroll taxes for 50 percent of qualified employee wages, up to a maximum of $5,000 per employee per quarter. Please see this chart for specific details.

It should be noted that wages subject to the credit do not include leave subject to tax credits under the Families First Act. Additionally, if the business receives a covered loan under the PPP, that business will not be eligible to take this tax credit. For most businesses, debt forgiveness under the PPP will generally produce a better overall outcome than the partial tax credit.

However, if a business is not eligible for the PPP loan or chooses to not participate in the PPP, this tax credit should be pursued if the conditions for eligibility are met.

Although this scenario assumes a total shutdown, another scenario could be a partial reduction in workforce to accommodate a reduction in business. If the partial reduction in workforce is expected to be long-term, that would likely reduce viability of the PPP forgivable loan option, unless the laid-off employees could be rehired by June 30, 2020. In a long-term layoff scenario, the 50 percent wage credit could be the optimal decision.

As with the full shut down, a business could continue with partial employment for a period of time and then rehire all employees and apply for the PPP loan, or the business could apply for the PPP loan at the outset as a means to maintain the current workforce.

Strategies to choose from include:

1. **shutdown/ laying off employees, allowing them to claim enhanced unemployment benefits;**
2. **a PPP loan that can be partially or fully forgiven; or**
3. **payroll tax credit for eligible wages paid to retain employees.**

Strategies (1) and (2) can be used together, but you must be mindful of the rules regarding timing of rehiring, as reducing employment levels generally causes a reduction in the amount of the Payroll Protection Loan that is eligible for forgiveness. Strategies (2) and (3) cannot be used in combination.

Situation 3: The business has been forced to temporarily shut its doors due to either a reduction in business or a mandated closure.

In this situation, the options are generally the same as in Situation 2. You could choose to pay the employees under your own sick leave or family and medical leave policy, but that leave would not be eligible for the payroll tax credits in the Families First Act. Additionally, if employees are being paid under your leave policy, they would not be eligible for the expanded unemployment benefits.

Thus, the better solution from a compensation standpoint would be to lay off employees and allow them access to the expanded unemployment benefits, subject to the previously identified risks. If the shutdown is not mandated by Federal, state, or local government, you could also try to immediately access PPP forgivable loans to allow you to rehire the employees immediately and reopen your doors.

Finally, you could lay off your employees for a period of time, allowing them to draw enhanced unemployment, and then rehire them and apply for the Paycheck Protection Program loans, being mindful of the rehire deadlines identified in Situation 2.

Strategies to choose from include:

1. **continued termination of employees, allowing them to claim enhanced unemployment benefits; or**
2. **a PPP loan that can be partially or fully forgiven.**

These two tools can be used together, but you must be mindful of the rules regarding timing of rehiring, as reducing employment levels generally causes a reduction in the amount of the Payroll Protection Loan that is eligible for forgiveness.

Summary

These are unprecedented times, and each business' situation is different. PPP loans appear to have the widest applicability for eligible businesses, but there may be competing factors that make other options more beneficial. A review of your specific situation will be key to navigating these decisions. Please contact your WK advisor to discuss your specific situation and potential solutions.

Our hope is that these ideas will help identify the main decision points and direct conversations and decisions for your business. One certainty in these uncertain times is that our primary focus in the coming days and weeks will be on helping you navigate this ever-more-challenging business environment.