CORONAVIRUS AID, RELIEF, AND ECONOMIC SECURITY ACT: MANUFACTURING IMPACTS

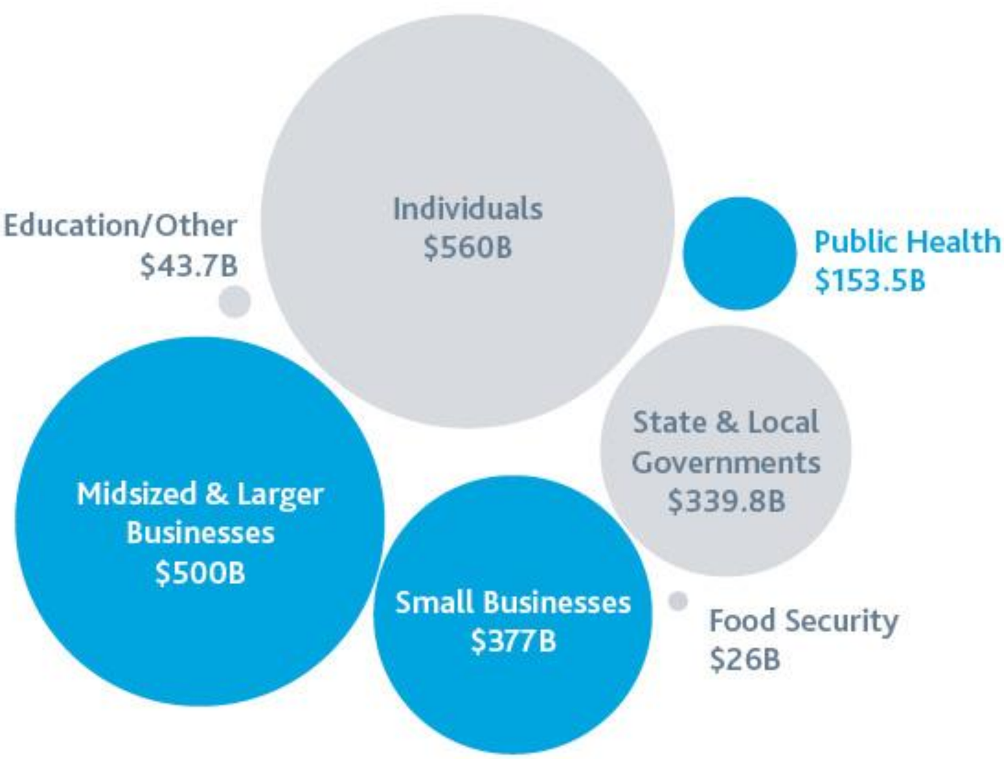
On Friday, March 27, President Trump signed the Coronavirus Aid, Relief, and Economic Security Act (also known as the CARES Act), a $2 trillion stimulus package intended to help mitigate the economic devastation caused by the novel coronavirus (COVID-19).

The stimulus is good news for manufacturers, many of whom are struggling given the current economic circumstances and stand to benefit financially from the package. However, the CARES Act also includes restrictions and responsibilities that manufacturers need to be aware of, especially manufacturers that produce supplies related to the healthcare industry, including ventilators, products like Personal Protective Equipment (PPE) and hand sanitizer, and medication.

We've summarized some of the key portions of the CARES Act for manufacturers.

Lending Programs

The CARES Act is comprised of multiple loan programs targeted at different groups impacted by COVID-19. The programs manufacturers may be eligible for are highlighted in the figure below.



SBA Payment Protection Program – $350B
Under the Small Business Administration (SBA) Paycheck Protection Program, specific funds totaling $350 billion have been set aside for small businesses, to be administered by SBA-approved lenders. Loan amounts for this provision may only be used for rent, insurance premiums, utility payments, mortgages, and payroll.

In order to qualify for a loan under this program, your company must employ 500 workers or fewer (both full-time and part-time), *or* they must meet the industry size standard set forth by the SBA. The SBA's size standard for auto manufacturers, for example, is 1,500 employees or fewer.

The maximum amount for these loans is 2.5 times the average total monthly payroll costs for the prior 12 months, or up to $10 million. The interest rate may not exceed 4%. Businesses can also defer payment of the principal, interest and fees for six months to one year.

One of the biggest appeals of the SBA Paycheck Protection Program is that the loans are forgivable, assuming certain conditions are met. The SBA can grant forgiveness up to the total amount borrowers spend of up to eight weeks of payroll costs and mortgage interest, rent, and utility payments between February 15 and June 30, 2020, if the borrower retains its employees and does not reduce salary levels more than 25%. Loan forgiveness is prorated for organizations that do not maintain payroll. The CARES Act provides an exception to the reduction if the eligible entity re-hires employees and/or eliminates the reduction in salaries by June 30, 2020. Forgiven amounts do not need to be reported as taxable income. The Treasury Department is anticipating that not more than 25% of the forgiven amount may be for non-payroll costs.

The application is available through the Treasury Department's website here. You will need to complete the PPP loan application and include your payroll information. Once complete, submit to an approved lender by June 30, 2020.

Small businesses, nonprofits, and sole proprietorships can apply for and receive loans to cover their payroll and other certain expenses through existing SBA lenders starting on April 3, 2020. Independent contractors and self-employed individuals can apply starting April 10, 2020.

SBA Economic Injury Disaster Loans
The SBA's Economic Injury Disaster Loan (EIDL) program gets an honorable mention here since the CARES Act temporarily expands eligibility to all businesses with 500 employees or fewer. The program offers up to $2 million in economic aid to small businesses, at an interest rate of 4% or less. Loans smaller than $200,000 can now be approved without a personal guarantee. In addition, the CARES Act removes the requirement that borrowers must demonstrate they have not been able to secure credit elsewhere.

Companies can also request an emergency grant cash advance of up to $10,000, to be funded within three days of the SBA's receipt of the loan application. The grant does not need to be repaid, even if the candidate isn't ultimately approved for a loan.

Manufacturers can apply for loans under both SBA programs as long as they don't cover the same expenses.

You can apply directly for an EIDL loan via the SBA's online portal.

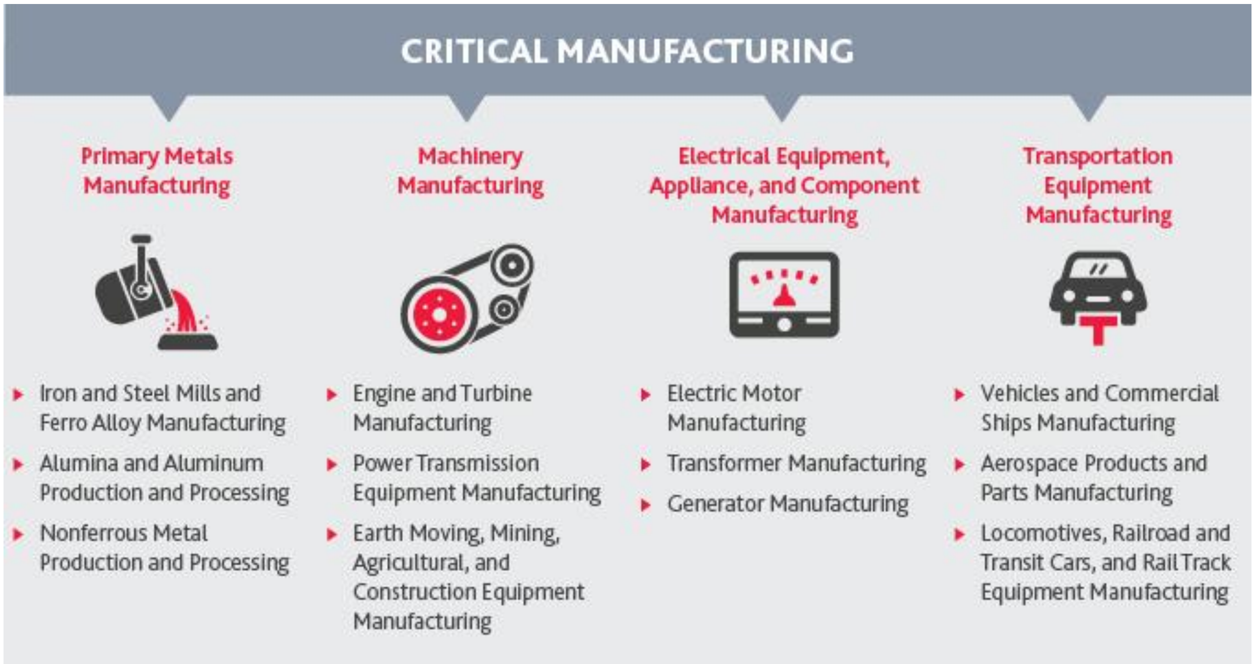
Midsized & Larger Businesses – $500B
The Treasury will have $500 billion at its disposal to give loans to eligible businesses as part of the economic stabilization plan included in the CARES Act. The $500 billion will be allocated as follows:

The terms and conditions of these loans are delineated between the $46 billion for air carriers and businesses deemed critical to national security, and the $454 billion allocated for other businesses, states and municipalities. The former will be provided directly via the Secretary of the Treasury, while the latter will be allocated via programs and facilities established by the Board of Governors of the Federal Reserve program—which means requirements relating to loan collateralization, taxpayer protection and borrower solvency under the Federal Reserve Act also apply. The process to get a loan will also likely be lengthier, as these programs and facilities have not yet been established.

The $454 billion does explicitly include a loan program for midsized businesses—defined as organizations with between 500 and 10,000 employees, for which annualized interest rates cannot exceed 2%. No interest payments are due within the first six months of the loan.

It's worth noting that the Department of Homeland Security cites "critical manufacturing" as one of 16 critical industry sectors vital to U.S. national security, in addition to the chemical sector and defense industrial base. As a result, many manufacturers may be eligible for the $17 billion allocated for national security businesses.

Unlike the SBA Paycheck Protection Program, these loans are not forgivable. The loans also come with public disclosure requirements, which will be overseen by a Special Inspector General for Pandemic Recovery appointed by the President.



Tax Provisions

The CARES Act also introduces several tax changes, including credits, payment delays and increases to interest deductions that have immediate implications for manufacturers' total tax liability:

- Employee Retention Credit for Employers Subject to Closure due to COVID-19 – This tax credit against applicable employment taxes amounts to 50% of "qualified wages with respect to each employee."
- Delay of Payment of Employer Payroll Taxes – Employers may delay their 2020 payroll taxes, to be paid in full within two years.
- Modification for Net Operating Losses – Tax losses from 2018-2020 can be applied retroactively five years to offset income.
- Modifications of Limitation on Business Interest – Businesses may increase their interest deductions for 2019 and 2020. Previously, the maximum interest deduction was 30% EBITDA. It has been raised to 50% EBITDA.

Labor Provisions

The most important labor provisions for manufacturers are those regarding paid leave and unemployment insurance. Under the CARES Act, there is a cap on the payments an employer must pay for emergency paid leave. Employers can also elect to receive an advance tax credit on paid leave. If they do not elect to receive the tax credit, they will be reimbursed on the back end.

Unemployment insurance is available to both the unemployed and the underemployed. State short-term compensation programs will make it possible for employers to preserve pro-rated unemployment benefits for employees when reducing their hours.

Industry Partnerships

$50 million is reserved for the Hollings Manufacturing Extension Partnership (MEP), for the purposes of helping manufacturers respond to COVID-19. MEP provides resources to small and medium-sized manufacturers.

$10 million is reserved for the National Network of Manufacturing Innovation (also known as “Manufacturing USA”), for the purposes of helping manufacturers respond to COVID-19. They engage over 1,900 member organizations.

Medical Device and Biopharmaceutical Manufacturers

There are special provisions of the CARES Act intended for businesses and workers involved in the biopharmaceutical and medical device production industries.

Biopharmaceutical and medical device manufacturers will need to be aware of new rules and regulations set forth by the CARES Act, some of which include:

- **Compliance with the medical supply chain security report.** The National Academies of Sciences, Engineering, and Medicine will be carrying out a report on the security of the U.S. medical supply chain, considering issues of national security and the potential for increasing domestic manufacturing of certain medical supplies. As part of the report, the National Academies may consult with medical product manufacturers. Manufacturers should be prepared to comply with the report and watch for its findings once released.

- **Ensure compliance with new manufacturing reporting requirements related to drug shortages.** The responsibilities for manufacturers to report on drug shortages has been expanded. For example, manufacturers will now be required to maintain and implement a risk management plan and prepare annual reports for each drug they produce as listed in the Federal Food, Drug, and Cosmetic Act.

- **Notification of discontinuance or interruption of medical device manufacturing.** Devices that could have an impact on public health and safety during a public health crisis must be more closely monitored. Manufacturers are now responsible for reporting supply chain disruptions and discontinuations.

Provisions to Increase Supply of Products to Help Fight COVID-19

Certain supplies, specifically hand sanitizer, PPE and cleaning products, are useful in combating the spread of COVID-19. The U.S. is currently suffering from a shortage of many such supplies. The CARES Act includes provisions intended to increase the availability of these products to protect public health.

- **Alcohol** – There will be a temporary exception from excise tax for any alcohol that is used to produce hand sanitizer.
- **PPE and Hand Sanitizer** – Many of the funds being made available to various institutions, including the Smithsonian Institutes and the TSA, can be used for the purchase of PPE, hand sanitizer, and cleaning products. The demand for these products, while high already, will likely continue to grow as government assistance becomes available for their purchase.

Takeaways

- Manufacturers should now assess the need for financial relief that is being provided through this $2 trillion CARES Act. There are several very favorable loan options and tax savings strategies that manufacturers of all sizes can benefit from. The underlying theme with these loans and tax benefits is to maintain employee levels so be sure to understand these options before making decisions to reduce headcount.
- For manufacturers who are able to keep facilities open, either by pivoting production or being classified as essential, employee health and safety must come first. Asking employees to take their temperature multiple times a day, to avoid interacting with other teams and to restrict themselves to their own workspace, and ensuring they know they won't be penalized for taking time off in light of a potential exposure, are all important steps employers can take to reduce the likelihood of COVID-19 spreading through their facilities.
- Manufacturers may consider pivoting their production to high-demand items like hand sanitizer or medical devices, which can help alleviate severe shortages of products necessary to fight COVID-19 and keep their operations running. Some manufacturers, such as perfume and alcohol manufacturers, may already have supplies and equipment necessary to produce hand sanitizer. If you are considering pivoting your production, there are several questions you should be asking yourself first. Do you have the necessary expertise to produce the new product, or will you need to hire new workers with specialized knowledge? Are you aware of any new restrictions and/or regulations that you'd be subject to if you produce this new product? Do you have access to the resources necessary to produce this product?
- Biopharmaceutical manufacturers should increase visibility in their supply chains to comply with new supply chain regulations in the CARES Act. Does your supply chain have blind spots? If so, several technological tools are available to help. Smart logistics, Cloud-based GPS, and Radio Frequency Identification technologies (RFID) are just a few tools that manufacturers can use to shed light on the hidden parts of the supply chain, hopefully reducing the likelihood of unwelcome surprises.