Sea Grant
Law Center

CARES Act Tip Sheet for Self-Employed Individuals

This document was prepared on April 23, 2020. Guidance regarding financial relief for the impacts of COVID-19 is rapidly changing. Please check appropriate state and federal websites frequently for the most updated information.

I'm a self-employed individual who has lost business due to the COVID-19 pandemic. What relief programs are available to me under the CARES Act?

Self-employed individuals are eligible to apply for three relief programs under the CARES Act: the Paycheck Protection Program (PPP), the Economic Injury Disaster Loan Program (EIDL), and Pandemic Unemployment Assistance (PUA).

- The PPP is a forgivable loan meant to cover 8 weeks of payroll and other allowable business expenses.
- EIDL provides low interest loans to small businesses affected by COVID-19.
- PUA provides unemployment assistance beyond standard state benefits.

How do I know which program is right for me?

Paycheck Protection Program

The PPP is designed to provide a direct incentive for small businesses who have been affected by COVID-19 to keep their workers on the payroll. SBA will forgive loans if all employees are kept on the payroll for eight weeks and the money is used for payroll, rent, mortgage interest, or utilities. To be forgiven, the business must use at least 75% of its loan on payroll expenses. Loan payments are deferred for six months following the date of the disbursement of the funds, and will be subject to a 1% interest rate.

The program is currently closed. Congress is in discussions on a new bill to provide additional funding that may reopen the program. Contact your bank as soon as possible so you are prepared for the next round of funding, if appropriated by Congress.

Eligibility Requirements for Self-Employed Individuals:

- In operation on February 15, 2020.

    - *If you have no employees: You must submit an invoice, bank statement, or book of record showing this with your application.*
    - *If you have employees: You must submit a payroll statement or similar documentation from the pay period covering Feb. 15, 2020 to show this.*
- Have self-employment income (e.g., independent contractor or sole proprietor).
    - *If you have no employees: You must submit a Form 1099-MISC, bank statement, or book of record to show you are self-employed.*
- Principal place of residence is the United States.
- Filed or will file a Form 1040 Schedule C for 2019.
    - *For businesses with and without employees: You must provide this form with your application, even if you have not yet submitted your 2019 taxes.*
    - *Business with employees need to submit additional documentation:*
        - *2019 Form 941 (or similar payroll processor records); state quarterly wage unemployment insurance tax reporting forms for each 2019 quarter (or similar payroll processor records); and evidence of any retirement and health insurance contributions.*

The PPP has some significant limitations. First, it has a very short coverage period (loan funds must be spent within 8 weeks) and will only run through June 2020. Second, the program is underfunded. Even if Congress authorizes additional funds for the program, the money is likely to go very quickly. Third, it is not designed for businesses with minimal payroll costs. A PPP loan may not be helpful for a business that needs funds to cover non-payroll costs. Finally, it is important to remember that with the PPP, the funding is provided as a loan. Some, but not necessarily all, of the loan can be forgiven depending on how the funds are used.

<u>Loan Calculation:</u>
To determine maximum loan amount if you have **no employees**:
- Start with 2019 IRS Form 1040 Schedule C line 31 net profit amount (max. $100,000). <u>*Ineligible for loan if amount is zero.*</u>
- Divide by 12 to determine average monthly net profit.
- Multiply by 2.5 to determine maximum loan amount.
- Add the outstanding amount of any EIDL made between 1/31/20 – 4/3/20, less any EIDL COVID-19 advance.

So let’s say that you make an average of $35,000 per year at your business, and this is the net profit amount you entered on line 31. Your max loan amount would be approximately $7,291 ($35,000/12 x 2.5).

You could then use those funds to pay your salary over the eight-week period following the date of the disbursement of the funds. That's approximately $911 per week. You would need to keep accurate records demonstrating that the PPP funds were used to cover payroll costs.

If you are an independent contractor and your business **has employees that receive W-2s**, the loan calculation is different. To determine maximum loan amount if you have employees:

- Compute 2019 Payroll by adding:
    - 2019 IRS Form 1040 Schedule C line 31 net profit amount (max. $100,000). <u>*Ineligible for loan if amount is zero.*</u>
    - 2019 IRS Form 941 Taxable Medicare wages & tips (line 5c– column 1) minus any amounts to an individual employee in excess of $100,000 or to any employee with a principal place of residence outside the US.
    - 2019 employer health insurance contributions (Form 1040 Schedule C line 14), retirement contributions (Form 1040 Schedule C line 19), and state and local taxes assessed on employee compensation.
- Divide by 12 to determine average monthly payroll.
- Multiply by 2.5 to determine maximum loan amount.
- Add the outstanding amount of any EIDL made between 1/31/20 – 4/3/20, less any EIDL COVID-19 advance.

<u>Loan Forgiveness:</u>
Self-employed individuals can only use their PPP loan amount for certain expenses. The loans are meant to maintain existing operations and payroll. They are not intended for business expansion. Allowable expenses include:

- Owner compensation replacement, which is limited to a pro-rated amount of your net profit from 2019 IRS Form 1040 Schedule C line 31;
- Employee payroll costs for all employees whose principal place of residence is the United States;
- Mortgage interest, rental, and utility payments that you did or could deduct on your 2019 Form 1040 C;
- Interest payments on other debt incurred before February 15, 2020, *but these payments will not be forgivable as discussed below*; and
- Refinancing an SBA EIDL loan made between January 31, 2020 and April 3, 2020.

The SBA has provided some guidance as of this date concerning loan forgiveness. The SBA in an April 14 Interim Rule has stated that the following can be forgiven for self-employed individuals. *Note that mortgage interest, rent, and utility payments must all be eligible business expenses that are deductible on Form 1040 Schedule C in order to be forgiven*.

- Payroll costs including salary, wages, and tips (up to $100,000 per employee), as well as covered benefits including health care expenses, retirement contributions, and state taxes imposed on employee payroll paid by the employer;
- Mortgage interest payments on real or personal property incurred before February 15, 2020;
- Owner compensation replacement, which is limited to 8 weeks of 2019 net profit (2019 IRS Form 1040 Schedule C line 31);
- Rent payments on any lease agreement entered into before February 15, 2020; and
- Utility payments under service agreements dated before February 15, 2020.

Economic Injury Disaster Loans

The SBA provides low-interest disaster loans to help businesses and homeowners recover from declared disasters. Applicants must be able to establish that the claimed economic injury is substantial and a direct result of the declared COVID-19 national emergency.

The program is currently closed. Congress is in discussions on a new bill to provide additional funding that may reopen the program. Contact your bank as soon as possible so you are prepared for the next round of funding, if appropriated by Congress.

Applicants may apply for a loan of up to $2 million to pay fixed debts, payroll, accounts payable, and other bills during the “covered period” of January 31 - December 31, 2020. The interest rate is 3.75% and the loans have a maximum 30-year repayment period.

Applicants may request an advance of $10,000, but note that as April 10, 2020, SBA local field offices have announced that this amount would be limited to $1,000 per employee, up to $10,000. An independent contractor with no employees may be eligible for a $1,000 advance.

EIDL applications must be submitted within nine months from the date of a governor’s disaster declaration.

Unemployment Assistance

Pandemic Unemployment Assistance (PUA) is available for individuals not qualified for regular unemployment benefits. This includes those who are self-employed, individuals seeking part-time employment, individuals lacking sufficient work history, or those otherwise not qualified for regular UC, extended benefits under state or federal law, or PEUC.

According to a Department of Labor Unemployment Insurance Program letter issued on April 5, 2020, the Pandemic Unemployment Weekly Benefit is to be calculated as set forth in 20 C.F.R.

625.6 and is increased by the $600 Federal Pandemic Unemployment Compensation (FPUC) payment. 20 C.F.R. 625.6(a)(2) states that "The self-employment income to be treated as wages for the purposes of computing the weekly amount … shall be the net income reported on the tax return of the individual as income from all self-employment that was dependent upon the performance of services by the individual."

Returning to your average $35,000 income, let's convert that to hourly wages by dividing by 2080 (work hours in a year). That gives you a $16.82 hourly rate. Multiply that by 40 hours for a work week and that's $673 per week. Maximum weekly benefit amounts vary by state, so your compensation may be limited by that.

The CARES Act authorizes PUA benefits from January 27 - December 31, and FPUC benefits from March 29 - July 31. Let's assume your state's maximum weekly benefit amount is $500 Your estimated unemployment benefits would be:

- $500 per week from January 27 - March 28
- $1,100 per week from March 29 - July 31 ($500 + $600)
- $500 per week from August 1 - December 31

So, thinking back to the PPP hypothetical above, unemployment benefits potentially provide more than PPP at least during the FPUC period; that is $1,100 vs $911. *Remember:* this will vary by state. But within the context of this hypothetical, unless you qualify for a PPP loan amount over $9,000, unemployment will likely pay more. Here's why. Let's work backwards from the $911 PPP benefit.

- $911 x 4 = $3,644 hypothetical average monthly net income.
- $3,644 x 2.5 = $9,110 maximum loan amount.
- That would require a net income amount over $43,728 ($3,644 x 12).

If you have no net income from self-employment, you are entitled to a weekly amount equal to 50% of the average weekly payment of regular compensation in the state. Let's say the average weekly payment in your state is $300. That means an individual with no net income from self-employment would be entitled to $150 (50% of $300) plus the $600 FPUC benefit for a total of $750 a week.

So, your estimated unemployment benefits would be:

- $150 per week from January 27- March 28
- $750 per week from March 29 - July 31 ($147.50 + $600)
- $150 per week from August 1 - December 31

Unemployment would be your only option in this situation, as individuals who report zero for their net income on 2019 Form 1040 Schedule C line 31 are ineligible for PPP loans.

What Can I Do Now?

Independent contractors and individuals may be best served by working through local lenders, who know them, their businesses, and their communities. Reach out to your local bank if you have a relationship with one or your nearest Small Business Development Center for assistance in gathering documentation and preparing your applications.

Self-employed individuals have successfully secured loans through these programs, but remember funds are very limited and this financing might not be the best option for everyone. For some individuals, filing for Pandemic Unemployment Assistance might make more sense.

Other Options

SBA 7(a) Loans: The 7(a) loan program is the SBA's primary program for providing financial assistance to small businesses. The terms and conditions vary by the type of loan. Information available at: https://www.sba.gov/partners/lenders/7a-loan-program/types-7a-loans

Employee Retention Credit: The CARES Act created a tax incentive for employers to continue paying their employee's wages during the COVID crisis: the Employee Retention Credit (ERC). The ERC is equal to 50% of qualified wages, but the maximum that can be claimed per employee is $5,000. The ERC is not available to employers who receive PPP loans. Additionally, the IRS has created a new form (Form 7200) that employers can file to immediately reduce their payroll taxes through the ERC and other COVID-related tax credits available at: https://www.irs.gov/forms-pubs/about-form-7200.