

## SBA Issues New Guidance on Paycheck Protection Program

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Following last Friday's passing of the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), businesses are eager to obtain much-needed relief, but there are uncertainties about which forms of relief are available to them. Questions remain as to whether and to what extent rules applicable to existing Small Business Administration (SBA) loan programs or other existing rules relating to issues such as how to calculate small business size or number of employees, whether entities are affiliates, how much information is required to be disclosed, how to calculate the amount of funding that can be obtained, and other matters apply to the CARES Act's Paycheck Protection Program (PPP).

In an effort to address some of these outstanding questions, the SBA issued a preliminary version of an "interim final rule" which provides some guidance on the implementation of the small business assistance provisions relating to the PPP. We anticipate the interim final rule will be published in the Federal Register in the coming days.

In addition, although a PPP loan application had been provided earlier this week, on the evening of April 2 an updated loan application was released. On the morning of April 3, the SBA still had the old application form on its site, but it was updated at approximately 9:20 am EDT with the Treasury form. It is important that applicants ensure they are not looking at the wrong form, as there are substantive differences between the two.

The "interim final rule" does not resolve all questions, and in fact creates some ambiguity. With loan applications already being submitted as of today, April 3, 2020 and the SBA's statement in no uncertain terms that loans will be issued on a first-come, first-served basis, there is a need for all due deliberate speed to file. Many applicants were already completing applications based on the existing guidance and loan application, and when they received the "interim final rule" and updated application were working to adjust their applications in the expectation that it would be issued on Friday, April 3. The "interim final rule" and updated PPP application are [available online](#).

### **Business Size**

The act provided that "small business concerns" under the Small Business Act were eligible borrowers. Under the Small Business Act, certain businesses are considered small business concerns if they have a number of employees and/or revenues that are at or below specified levels. The act also expanded the list of permissible borrowers to include certain entities which satisfied specified size standards. The act provided for calculation of small business size for these additional borrowers based on whether the entity has no more than the greater of either (i) "500 employees," or (ii) the business operates in a certain industry and meets the applicable SBA employee-based entity size standard. These size standards apply to businesses and any entity that is a 501(c)(3) tax-exempt nonprofit organization, a tax-exempt veterans organization under 501(c)(19) of the Internal Revenue Code, or a tribal business concern under 31(b)(2)(C) of the Small Business Act.

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The “interim final rule” does not track the definition of small business concern under the Small Business Act exactly. Instead, Article III, Section 2 titled “What Do Borrowers Need to Know and Do? . . . a. Am I eligible” refers to entities having “500 or fewer employees” or satisfying the “applicable SBA employee-based size standards” and being either a small business concern, a 501(c)(3) nonprofit, a veterans organization or a tribal business concern. It fails to expressly refer to SBA revenue-based size standards as being sufficient to be eligible for the PPP. Instead, it seems to require that all businesses other than the designated categories of nonprofits and tribal business concerns be a “small business concern” as defined in section 3 of the Small Business Act. This suggests that (i) applicants that operate under a revenue-based NAICS code and meet that small business size standard are only eligible if they have 500 or fewer employees (including employees of affiliates), (ii) designated 501(c)(3) and 501(c)(19) nonprofits and tribal business concerns are only eligible if they have 500 or fewer employees, and (iii) certain types of businesses -- sole proprietorship, independent contractor or eligible self-employed individual -- are also eligible for PPP loans if they meet standards identified in the act. Another section of the “interim final rule” expressly states that applicants are not eligible if they are not considered a “business” and refers to 13 C.F.R. § 121.100.

The “interim final rule” does provide that the affiliation rules under 13 C.F.R. § 121.301(f) will be used to determine the size of businesses seeking loans, unless the affiliation rules are specifically waived under the CARES Act. The “interim final rule” also states that, for eligibility affiliation determinations, “SBA intends to promptly issue additional guidance with regard to the applicability of affiliation rules at 13 CFR §§ 121.103 and 121.301 to PPP loans.” Thus, questions on the applicable standard for business size remain for applicants to solve, and it remains an open question as to whether exceptions to the affiliation rules will be proposed to better enable businesses backed by private equity to utilize the PPP.

### Ineligibility

The SBA’s “interim final rule” contains several provisions on ineligibility and refers the applicant to 13 C.F.R. § 120.110, as well as its Standard Operating Procedures (SOP) 50 10, Subpart B, Chapter 2, Eligibility for 7(a) Guaranty Loan Program, for determining whether its business is ineligible for a PPP loan.

13 C.F.R. § 120.110 provides that the following types of businesses are ineligible for SBA business loans, and the SOP 50 10 provides additional guidance as to what businesses are captured by these categories:

- a. Nonprofit businesses (for-profit subsidiaries are eligible) [The SBA’s interim final rule recognizes that this basis for ineligibility is abrogated for nonprofits by the text of the CARES Act for purposes of the PPP.]
- b. Financial businesses primarily engaged in the business of lending, such as banks, finance companies and factors (pawn shops, although engaged in lending, may qualify in some circumstances)
- c. Passive businesses owned by developers and landlords that do not actively use or occupy the assets acquired or improved with the loan proceeds (except Eligible Passive Companies under § 120.111)
- d. Life insurance companies
- e. Businesses located in a foreign country
- f. Pyramid sale distribution plans
- g. Businesses deriving more than one-third of gross annual revenue from legal gambling activities
- h. Businesses engaged in any illegal activity
- i. Private clubs and businesses which limit the number of memberships for reasons other than capacity
- j. Government-owned entities (except for businesses owned or controlled by a Native American tribe)
- k. Businesses principally engaged in teaching, instructing, counseling or indoctrinating religion or religious beliefs, whether in a religious or secular setting
- l. Loan packagers earning more than one third of their gross annual revenue from packaging SBA loans

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- m. Businesses with an associate who is incarcerated, on probation, on parole, or has been indicted for a felony or a crime of moral turpitude
- n. Businesses in which the lender or CDC, or any of its associates owns an equity interest
- o. Businesses which:
  - 1. Present live performances of a prurient sexual nature
  - 2. Derive directly or indirectly more than de minimis gross revenue through the sale of products or services, or the presentation of any depictions or displays, of a prurient sexual nature
- p. Unless waived by SBA for good cause, businesses that have previously defaulted on a federal loan or federally assisted financing, resulting in the federal government or any of its agencies or departments sustaining a loss in any of its programs, and businesses owned or controlled by an applicant or any of its associates which previously owned, operated, or controlled a business which defaulted on a federal loan (or guaranteed a loan which was defaulted) and caused the federal government or any of its agencies or departments to sustain a loss in any of its programs. For purposes of this section, a compromise agreement shall also be considered a loss
- q. Businesses primarily engaged in political or lobbying activities
- r. Speculative businesses (such as oil wildcatting)

Note, however, that contrary to 13 C.F.R. § 120.110(a) and the SOP, above, the CARES Act and the “interim final rule” provide that 501(c)(3) nonprofits are identified as eligible to apply for a loan.

### Terms of the PPP Loan

The CARES Act indicated that PPP loans would have a maturity of up to 10 years and an interest rate not greater than 4%, while prior guidance issued by the Treasury Department referred to a 0.50% interest rate and a term of two years. The “interim final rule” confirms that the maturity date of the loan is two years, and the interest rate on the loan will be 1% or 100 basis points.

### Required Certifications and Penalties

The prior version of the PPP application required 20% or greater owners of the applicant to join in making a number of certifications relating to the applicant, its business and owners, and its use of loan proceeds. This created complications for 20% owners – for example a passive 20% owner may have no basis for making such certifications. In a welcome change, the updated PPP application no longer requires 20% or greater owners to join in making such certifications. It does require an identification of ownership in other businesses – “Is the applicant or any owner of the applicant an owner of any other business, or have common management with, any other business? If yes, list all such businesses and describe the relationship on a separate sheet identified as addendum A.”

The updated PPP application adds several additional certifications. Of particular note, an applicant is now required to certify that it is eligible to receive a PPP loan “under the rules in effect at the time this application is submitted that have been issued” by the SBA.

Additionally, the “interim final rule,” as well as the revised application, provides penalties for false statements, as borrowers will have to certify to the following in the PPP loan application. The “interim final rule” states:

I understand that knowingly making a false statement to obtain a guaranteed loan from SBA is punishable under the law, including under 18 USC 1001 and 3571 by imprisonment of not more than five years and/or a fine of up to \$250,000; under 15 USC 645 by imprisonment of not more than two years and/or a fine of not more than \$5,000; and, if submitted to a federally insured

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institution, under 18 USC 1014 by imprisonment of not more than thirty years and/or a fine of not more than \$1,000,000.

Accordingly, a careful reading of the rules as issued and available guidance, as well as best efforts to address questions accurately, will be important.

### Lenders

The SBA rule covers borrowers' eligibility and borrowing calculation matters. The Department of Treasury provides information on both borrower and lender matters, and has updated its website with a "final application form."

As with all things coronavirus related, this is an ever-evolving matter. The "interim final rule" once issued will be open for comment until 30 days from its release on the Federal Register.

We will continue to track the SBA and Department of Treasury activities and guidance issued for implementing the CARES Act, and will report back on additional details, including any additional guidance on affiliation rules under the PPP. If you have any questions related to PPP loan eligibility or applications, please contact the authors of this alert, or your Stinson counsel.

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