



## Saving Our Small Businesses: Congress Reaches Agreement on New Forgivable Paycheck Protection Loans to Small Businesses

By: Michael R. Wilson, Marisa Murillo and Natalie M. Jersak

Just before midnight Eastern Time on Wednesday, March 25, 2020, the U.S. Senate unanimously approved the Coronavirus Aid, Relief, and Economic Security Act or the "CARES Act" after releasing the final text of the CARES Act late Wednesday evening. If passed by the U.S. House of Representatives (which is expected by Friday, March 27, 2020) and signed into law by the President, the CARES Act will provide significant financial relief to small businesses, individuals and certain sectors of the U.S. economy that have been hit hardest by the COVID-19 pandemic.

Title I of the CARES Act focuses on supporting U.S. small businesses by, among other things, amending the Small Business Act to establish the "Paycheck Protection Program" (the "Program"), which is designed to incentivize workforce continuity during the ongoing pandemic by providing forgivable 7(a) loans to eligible businesses (each such loan a "Loan" and, collectively, the "Loans").<sup>1</sup> The Paycheck Protection Program will lend up to an aggregate amount of \$349 billion during the period beginning retroactively on February 15, 2020 through June 30, 2020 (the "Covered Period").<sup>2</sup>

### Small Business Eligibility

In order to be eligible for Loans under the Program, a business must be either (a) a small business concern (as defined in the Small Business Act), which were already eligible for 7(a) loans under the Small Business Act prior to passage of the CARES Act, or (b) any business concern, nonprofit organization, veterans organization, or Tribal business concern employing not more than the greater of 500 employees (full-time, part-time or otherwise<sup>3</sup>) or the size standard in number of employees for the industry in which the entity operates as established by the Small Business Administration (the "SBA").<sup>4</sup> The SBA's size standards as published in August 2019 can be found on the SBA's website [here](#). Note that this test is based solely on number of employees and not revenue.

The CARES Act provides for an express waiver of the SBA affiliation rules aggregating affiliates for purposes of meeting size standards for businesses that receive financial assistance from Small Business Investment Companies (SBIC funds), businesses in accommodations and food, and franchises with an SBA franchise identifier code.<sup>5</sup> While the CARES Act requires that the SBA affiliation rules do apply to nonprofit organizations and veterans organizations, it does not apply such affiliation rules to the category of "any business concern". The CARES Act also makes eligible accommodations and food businesses with multiple physical locations each having fewer than 500 employees.<sup>6</sup>

The CARES Act waives the typical requirement under the 7(a) program that the borrower is unable to obtain credit elsewhere for Loans under the Program.<sup>7</sup>

Instead of determining a borrower's creditworthiness and ability to repay the Loan, lenders are required to only consider (a) whether the borrower was in operation on February 15, 2020 and (b) if the borrower either had employees to whom it paid salaries and payroll taxes or paid independent contractors.<sup>8</sup> Borrowers

1 Coronavirus Aid, Relief, and Economic Security Act, H.R. 748, 116th Con. (2020) § 1102.

2 *Id.* at §§ 1101, 1107.

3 *See id.* at § 1102(D)(v).

4 *See id.* at § 1102(D)(i).

5 *See id.* at § 1102(D)(iv).

6 *See id.* at § 1102(D)(iii).

7 *Id.* at § 1102(a)(2)(36)(I).

8 *See id.* at § 1102(a)(2)(36)(F)(ii).



must certify to its lender that, among other things, a Loan is necessary in light of the economic uncertainty created by COVID-19.<sup>9</sup>

Recipients of economic injury disaster loans (“EIDLs”) from the SBA for COVID-19-related purposes are unable to receive Loans under the Program.<sup>10</sup>

While the CARES Act permits a broad range of small businesses to participate in the Program, the Senate included a statement of intent for the SBA to issue guidance for lenders to prioritize Loans to small business concerns and entities in underserved and rural markets, including veterans and members of the military communities, small business concerns owned and controlled by socially and economically disadvantaged individuals, women and businesses in operation for less than 2 years.<sup>11</sup>

### Authorized Uses

The proceeds of Loans under the Program may be used only for the following purposes: payroll costs, group health care benefits during periods of paid sick, medical or family leave and insurance premiums, employee compensation, mortgage interest payments, rent, utilities and interest on debt incurred prior to February 15, 2020.<sup>12</sup> Payroll costs expressly exclude: (a) compensation of an individual employee in excess of an annual salary of \$100,000 as prorated for the Covered Period, (b) withholding taxes, (c) compensation of persons whose principal place of residence is outside of the US, and (d) qualified sick leave and family leave for which a credit is allowed under the “phase 2” bill.<sup>13</sup>

### Distinguishing Loan Terms

Perhaps the most notable feature of the Program is that borrowers are eligible for forgiveness of indebtedness on their Loan in an amount equal to the sum of payroll costs, mortgage interest, rent payments, and utility payments made by the borrower during the Covered Period.<sup>14</sup> Forgiveness amounts will be considered canceled indebtedness by a lender and are not deemed income to the borrower.<sup>15</sup> The amount of forgiveness available to the borrower will be reduced by both (1) a percentage related to the number of employees laid off during the Covered Period as compared to the same period during the prior year or during January and February 2020 (with a cure for employees rehired by June 30, 2020), and (2) an amount related to reductions in salaries and wages of employees in excess of 25% during the Covered Period (with a cure for salaries and wages restored by June 30, 2020).<sup>16</sup> Borrowers must provide their lenders with complete documentation of the calculation of their forgiveness amounts.

Another key distinguishing term of the Program is that the requirements for personal guarantees and collateral are expressly waived and are not required to obtain Loans during the Covered Period.<sup>17</sup> In fact, the Loans are expressly nonrecourse against any individual shareholder, member or partner of an eligible recipient of a Loan for non-payment of the Loan, except to the extent proceeds are used for an unauthorized purpose.

### Other Loan Terms

The maximum amount for which Loans may be issued is the lesser of (i) \$10,000,000 and (ii) 2.5 times the average total monthly payments for payroll costs incurred during the 1-year period before the date the Loan is made.<sup>18</sup>

The interest rate on the Loans is capped at 4% per annum.<sup>19</sup> Any amount outstanding after forgiveness is granted pursuant to the CARES Act will have a maximum maturity of ten (10) years from the date on which the borrower applies for Loan forgiveness under the CARES Act.<sup>20</sup> Moreover, lenders are required to

<sup>9</sup> See *id.* at § 1102(a)(2)(36)(G).

<sup>10</sup> *Id.* at §1102(a)(2)(36)(Q).

<sup>11</sup> See *id.* at § 1102(a)(2)(36)(P).

<sup>12</sup> See *id.* at §1102(a)(2)(36)(F).

<sup>13</sup> See *id.* at §1102(a)(2)(36)(A).

<sup>14</sup> See CARES Act, *supra* note 1 at § 1106(b).

<sup>15</sup> See *id.* at § 1106(c).

<sup>16</sup> See *id.* at § 1106(d).

<sup>17</sup> *Id.* at § 1102(a)(2)(36)(J).

<sup>18</sup> This amount will vary for seasonal borrowers and borrowers not in business during the period beginning on February 15, 2019 and ending June 30, 2019. See *id.* at § 1102(a)(2)(36)(E).

<sup>19</sup> See *id.* at § 1102(a)(2)(36)(L).

<sup>20</sup> See *id.* at § 1102(a)(2)(36)(K).



provide complete payment deferment for a period of not less than six (6) months, nor greater than a period of one (1) year.<sup>21</sup>

It is also important to note that the CARES Act requires waiver of the upfront and annual fees typically due to the SBA under the Small Business Act.<sup>22</sup> Additionally, there will be no prepayment penalties for any payment made on a Loan.<sup>23</sup>

The maximum loan amount for "Express Loans" has also been increased under the CARES Act to \$1,000,000, up from the prior maximum of \$350,000.<sup>24</sup> "Express Loans" are an expedited version of loans provided under Section 7(a) for which the turnaround time for a response to the application is given within 36 hours.<sup>25</sup>

### Lender Considerations

Authorized lenders under the Program have delegated authority to make determinations on borrower eligibility and creditworthiness, subject to the criteria that, for purposes of determining creditworthiness, they must only consider (a) whether the borrower was in operation on February 15, 2020 and (b) if the borrower either had employees to whom it paid salaries and payroll taxes or paid independent contractors. Such authorized lenders administer the Loans directly in accordance with the Small Business Act as amended by the CARES Act, without being required to coordinate with the SBA in the same way as they would with the normal 7(a) loan program.<sup>26</sup>

While a typical 7(a) loan is guaranteed by the SBA in an amount up to 75% or 85% of the outstanding amount of the loan (depending on the amount outstanding), the CARES Act increases the SBA's guarantee of the Loans provided under the Program during the Covered Period to 100%.<sup>27</sup> This guarantee also includes payment from the SBA to the lender of 100% of the forgiven loan amount (discussed above).<sup>28</sup>

Due to the unprecedented magnitude and scale of COVID-19, the CARES Act expressly notes additional lenders are actively being sought for authorization to administer Loans under the Program.<sup>29</sup> Locke Lord will be publishing additional guidance for lending institutions' participation in the Program soon.

Your regular Locke Lord contact and the authors of this article would be happy to help you navigate the CARES Act and the related amendments to the Small Business Act as they relate to the Paycheck Protection Program or otherwise.

For more information on the matters discussed in this *Locke Lord QuickStudy*, please contact the authors.

**Michael R. Wilson** | 312-201-2522 | [michael.wilson@lockelord.com](mailto:michael.wilson@lockelord.com)

**Marisa Murillo** | 312-443-0294 | [marisa.murillo@lockelord.com](mailto:marisa.murillo@lockelord.com)

**Natalie M. Jersak** | 617-239-0336 | [natalie.jersak@lockelord.com](mailto:natalie.jersak@lockelord.com)

Please visit our [COVID-19 Resource Center](#) often for up-to-date information to help you stay informed of the legal issues related to COVID-19.

<sup>21</sup> See *id.* at § 1102(a)(2)(36)(M).

<sup>22</sup> See *id.* at § 1102(a)(2)(36)(H).

<sup>23</sup> See *id.* at § 1102(a)(2)(36)(R).

<sup>24</sup> See *id.* at §1102(i).

<sup>25</sup> *Types of 7(a) loans*, U.S. SMALL BUSINESS ADMINISTRATION, <https://www.sba.gov/partners/lenders/7a-loan-program/types-7a-loans#section-header-4> (last visited: March 20, 2020).

<sup>26</sup> See *id.* at § 1102(a)(2)(36)(F)(ii).

<sup>27</sup> See *id.* at § 1102(a)(1)(B)(F).

<sup>28</sup> See *id.* at § 1106(c)(2).

<sup>29</sup> See *id.* at § 1102(a)(2)(36)(F)(iii).



Practical Wisdom, Trusted Advice.

[www.lockelord.com](http://www.lockelord.com)

Atlanta | Austin | Boston | Brussels | Chicago | Cincinnati | Dallas | Hartford | Hong Kong | Houston | London | Los Angeles  
Miami | New Orleans | New York | Princeton | Providence | San Francisco | Stamford | Washington DC | West Palm Beach