CARES Act Paycheck Protection Program: Overview for Participating Lenders

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On March 27, 2020, President Trump signed into law the Coronavirus Aid, Relief, and Economic Security Act (CARES Act)—summarized in a previous alert—which amends and expands the U.S. Small Business Administration's (SBA) flagship 7(a) Loan Program to create the Paycheck Protection Program (PPP). Congress has committed $349 billion in emergency funding to the PPP in order to assist certain eligible borrowers adversely impacted by the COVID-19 pandemic cover their near-term operating expenses, while also providing a strong incentive for employers to retain employees during the crisis. Under the PPP, the SBA will guarantee 100% of covered loans made by participating lenders to eligible borrowers and will permit loan forgiveness up to 100%, subject to certain employment and compensation conditions.

On March 31, 2020, the SBA and the Treasury Department released initial guidance (the Initial Guidance) and on April 2, 2020, the interim final rule (the Interim Final Rule) on the PPP, both providing further key details regarding how the SBA plans to administer the loan program. Given the fluid nature of these developments, lenders are strongly encouraged to seek advice from their legal adviser before participating in the PPP program.

This alert provides a brief overview of the PPP and answers certain preliminary questions to help guide lenders contemplating whether participation is appropriate.

PPP Overview

- ***Eligible Borrowers:*** Businesses, nonprofit organizations, veterans' organizations and tribal businesses with up to 500 employees or, if applicable, the SBA-size standard for the business' industry. Employee count includes those employed on a full-time, part-time or other basis. PPP also extends eligibility to individuals who operate under a sole proprietorship, as an independent contractor and certain self-employed individuals. Relaxed eligibility requirements for businesses in certain industries, including the hospitality and food service industries.

- ***Maximum Covered Loan Amount:*** $10 million cap, determined by a formula generally based on the borrower's previous year's payroll costs.

- ***Covered Period:*** PPP loans are available to eligible borrowers who qualify retroactively from February 15, 2020 through June 30, 2020.

- ***Permitted Loan Uses:*** Generally, a borrower can use the PPP funds to cover: (a) payroll costs; (b) costs related to the continuation of group health care benefits; (c) employee salaries; (d) mortgage interest payments; (e) rent; (f) utilities; and (g) interest on any other debt obligations that were incurred before the covered period. Per the interim final rule, at least 75% of the PPP funds must be used for payroll costs.

For a more comprehensive analysis of the PPP's borrowing requirements, please see our previous alert.

Who Is Eligible To Lend Under the PPP?

Initially, PPP loans will be disbursed through the existing network of SBA-certified lenders that participate in the SBA's 7(a) Loan Program. These lenders will be given delegated authority to quickly process PPP loans. In addition, all federally insured depository institutions, federally insured credit unions and Farm Credit Systems institution are eligible to participate.

A broad set of additional regulated lenders, approved by the SBA and the Secretary of the Treasury, will be permitted to enroll in the SBA's 7(a) Loan Program and make PPP loans as well. The SBA has established a streamlined application process to quickly facilitate the approval of new lenders. New lenders will need to submit their application to DelegatedAuthority@sba.gov to apply with the SBA.

When May Lenders Begin Making PPP Loans?

Existing SBA-certified lenders can begin to process loan applications for small businesses and sole proprietorships on April 3, 2020 and for independent contractors and self-employed individuals on April 10, 2020. New lenders will be permitted to make PPP loans as soon as they are approved and enrolled in the SBA's 7(a) Loan Program.

What Are The Basic Loan Terms?

- General: All loan terms will be the same for every borrower, regardless of the lender.
- Interest Rate: Fixed rate of 1%.
- Maturity: Two years, with no prepayment penalties or fees.

Are PPP Loans Subject To SBA Guarantee Fees?

No, the SBA will waive all guaranty fees, including upfront and annual servicing fees, with respect to PPP loans.

Will Lenders Receive Fees For Making PPP Loans?

Yes, the SBA will pay processing fees to lenders within five days after the disbursement of the covered loan. Fees will be calculated at the following rates, based on the balance of the financing outstanding at the time of final disbursement:

- 5% for loans $350,000 and under;
- 3% for loans greater than $350,000 and up to $2 million; and
- 1% for loans greater than $2 million.

Lenders are prohibited from collecting any fees from applicants.

What Are The Underwriting Requirements?

Per the Initial Guidance, lenders will be required to verify the following information with respect to each borrower:

- The borrower was in operation on February 15, 2020;
- The borrower had employees for whom it paid salaries and payroll taxes; and
- The dollar amount of the borrower's average monthly payroll costs.

In addition, lenders must be sure to comply with applicable Bank Secrecy Act requirements.

Are Personal Guarantees and/or Collateral Required?

No. No personal guarantee or collateral is required in order for a borrower to obtain a PPP loan. In fact, the SBA has no recourse against any individual shareholder, member or partner of an eligible borrower for nonpayment of any covered loan, *unless* the loan proceeds are used for impermissible purposes. Moreover, per the Initial Guidance, if loan proceeds are used for fraudulent purposes, criminal charges will be pursued.

Are Lenders Required To Provide Payment Deferments for PPP Loans?

Yes. Per the Initial Guidance, the first payment will be deferred for six months. However, interest will continue to accrue during this period.

In addition, 7(a) lenders are encouraged to provide payment deferments on, and extend the maturity date of, existing SBA-backed loans, in order to avoid balloon payments or other requirements that would increase debt payments due to the deferments. To achieve these existing loan deferments, the SBA will pay lenders the deferred principal, interest and associated fees that are owed during the covered period for a six month-period, beginning with the first payment due on the covered loan. Moreover, the CARES Act contemplates the SBA will coordinate with the FDIC, OCC and state bank regulators to not require lenders to increase their reserves on account of deferment and receipt of SBA payments.

How Will PPP Loans Be Treated for Capital Purposes?

For purposes of regulatory capital requirements, loans will receive a risk weight of 0%.

Who May Be An Agent And How Are Agents Compensated?

Per the Initial Guidance, agents are authorized representatives and can be any of the following:

- Attorneys;
- Accountants;
- Consultants;
- Someone who prepares an applicant's application for financial assistance and is employed and compensated by the applicant;
- Someone who assists a lender with originating, disbursing, servicing, liquidating or litigating SBA loans;
- A loan broker; or
- Any other individual or entity representing an applicant by conducting business with the SBA.

Agents are compensated out of lender fees and will be paid directly by the lender. Agents will be paid per the following fee structure:

- 1% for loans $350,000 and under;
- 50% for loans greater than $350,000 and up to $2 million; and
- 25% for loans greater than $2 million.

Can PPP Loans Be Sold On The Secondary Market?

Yes. Per the Initial Guidance, PPP loans can be sold in the secondary market. For PPP loans sold into the secondary market, the SBA will not collect any fee for any guarantee sold. If the related investor does not approve a permitted deferment, the SBA is required to repurchase the loan and provide the deferral.

How Are Lenders Reimbursed For The Loan Amounts That Are Forgiven?

After a borrower applies for loan forgiveness, with detailed documentation verifying employment numbers, payroll and certain other expenses, lenders will have 60 days to determine whether to grant (and the amount of) the loan forgiveness. This amount, including accrued interest through the date of payment, will be remitted by the SBA to the lender within 90 days of the lender's determination. The amount of loan forgiveness may not exceed the principal amount of the PPP loan. If a lender requests that the SBA advance purchase any forgiven amounts, then the SBA will remit the forgiven amount within 15 days. Further, if a lender receives the appropriate verified documentation from a borrower, the lender will be held harmless from enforcement actions or other penalties imposed by the SBA.

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VORYS COVID-19 TASK FORCE

Vorys attorneys and professionals are counseling our clients on a myriad of others issues related to the outbreak. We have established a comprehensive COVID-19 Task Force, which includes attorneys with deep experience in the niche disciplines that we have been and expect to continue receiving questions regarding coronavirus. Learn more and see the latest updates from the task force at vorys.com/coronavirus.