

PROVISIONS OF THE CARES ACT APPLICABLE TO THE 7(a) LOAN PROGRAM

This NAGGL summary was prepared based solely on the language of the CARES Act. It is our understanding that Congress intends to provide information regarding congressional intent, and that both SBA and Treasury are writing guidance to implement the statute. The forthcoming guidance may provide details regarding program implementation not specifically set out in the statute. However, no written guidance has been issued as of 3/29/2020 when this summary was prepared. NAGGL will provide additional information as soon as it becomes available.

As points of reference as you and your institution review the statute:

- Section 1112 requires SBA to make payment on new and existing 7(a) loans for six months
- The entirety of the new **Paycheck Protection Program** can be found by referring to the following three separate sections:
- Section 1102 generally provides the parameters of the program and limited processing guidance;
- Section 1106 generally provides guidance regarding loan forgiveness; and
- Section 1109 generally provides program management authority for the Department of the Treasury.

And finally,

- Section 1107 provides **funding** for all provisions of the statute.

7(a) BORROWER PAYMENTS FOR 6 MONTHS **[Section 1112]**

This is an incredibly critical section of the final CARES Act. It provides six months of payments for all 7(a) borrowers—existing and new—which are not deferments, but rather full payments of principal and interest to the lender for which the borrower will never be responsible for again. This will be immediate and much needed relief for borrowers in the 7(a) portfolio.

While this section of the statute is very straightforward, SBA will need to provide guidance to lenders as to the mechanics of how these provisions will apply. The congressional intent and NAGGL's

encouragement has been that the guidance should be simple and clear; the statute states that these payments shall be made by SBA beginning with the next payment due on the loan after the bill is enacted. However, without SBA guidance as of 3/29/2020 and many borrowers' next payment date approaching, NAGGL is hopeful that SBA will issue this guidance immediately. NAGGL will provide additional information as soon as it becomes available.

- **Payment Relief:** SBA is required to pay the principal, interest, and any associated fees owed on a 7(a) loan in regular servicing starting with the next payment due for both existing and new borrowers. There are three scenarios outlined that cover all possibilities with clear guidance:
 - **Existing borrower not on deferment:** six months of payments of principal, interest, and any associated fees begin with the next payment due on the loan;
 - **Existing borrower on deferment:** six months of payments of principal, interest, and any associated fees beginning with the next payment due on the loan after the deferment period; and
 - **New borrower:** six months of payments of principal, interest, and any associated fees beginning with the first payment due on the loan, but only for new loans made within the first six months starting from the date of enactment (3/27/2020).

- **Eligibility:** Any loan made under the 7(a) program, including Express and Community Advantage loans. The payments are also applicable to any loan guaranteed by SBA in the 504 program [*NAGGL assumes this refers to the debenture portion only*], and to any loan made by a microlender.
 - Important to note: those loans made under the new Paycheck Protection Program (outlined below) are not eligible to receive payments.

In addition, the statute does not require the lender or borrower to meet any threshold requirements, proven, or documented to receive payments. However, SBA must provide guidance to detail the mechanics of how these payments will be made.

- Sense of Congress: All borrowers are assumed to be “adversely affected by COVID-19” and all relief payments are deemed appropriate for all borrowers, creating a very clear, bright-line for lenders and removing the burden from lenders to determine if a borrower is eligible in any way—all borrowers are deemed eligible.
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- **Timing of Payment:** SBA is required to begin making payments no later than 30 days after the date on which the first payment is due.

- **Application of Payment:** The payments made by SBA are required to be applied to the loan as if the payments had been made by the borrower.
- **Loans Sold on the Secondary Market:** Payments on loans sold on the secondary market are to be treated exactly the same as a loan not sold—there is no difference in how payments are required to be applied.
- **Relationship with Deferments:** Provisions in this section to provide payments are not to be seen as deferments in any way—they are government-provided loan payments. In addition to this relief, the Administration is called upon to encourage lenders to provide deferments either before or after this payment relief in order to work with borrowers when appropriate.
- **Coordination with Federal and State Regulators:** SBA is required to communicate and coordinate with federal and state regulators to encourage regulators to not require lenders to increase their reserves because of their receipt of payments from the SBA.
[It is unclear how the regulators will respond to this provision; the statute only requires that SBA communicate and coordinate, but does not require that the regulators comply with SBA's encouragement regarding reserves. Stay tuned for further guidance.]
- **Limits on Extending Maximum Loan Maturity Waived:** If a lender provides a deferral to a borrower at any time in the 1-year period following the date of enactment (3/27/2020) and extends the maturity of the loan as a result, SBA is required to waive any statutory limits on maximum loan maturities for that loan.
- **Extension of Lender Site Visit Requirements:** Recognizing that due to the potential for higher loan volume, travel restrictions, and the inability to access some properties altogether during the current pandemic, SBA is required to provide extended time to current lender site visit requirements when necessary to:
 - No more than 60 days after an adverse event, other than a payment default, which causes a loan to be classified as in liquidation, though SBA may extend this amount of time at its discretion; and
 - No more than 90 days after a payment default.

[SBA will likely need to issue guidance here to outline how they will view when extended time is

necessary and what lenders will need to provide to obtain the SBA extension, if anything, since the statute gives SBA some degree of discretion in this section.]

- **Funding:** \$17 billion is provided by Congress for SBA to make payments on all eligible 7(a), 504, and microloan loans.

GENERAL 7(a) LOAN PROGRAM CHANGES

TEMPORARY INCREASE TO SBA EXPRESS PROGRAM MAXIMUM SIZE [Section 1102(c)]:

- Maximum loan size for an SBA Express Loan is increased from \$350,000 to \$1 million effective 3/27/2020 (date of enactment of the CARES Act) through 12/31/2020
- Maximum authorized loan size will revert to \$350,000 on 1/1/2021

[Paycheck Protection Program loans are not considered to be SBA Express loans]

RESCISSION OF INTERIM FINAL RULE [Section 1102(e)]:

- The Interim Final Rule issued by SBA on 2/10/2020, *Express Loan Programs; Affiliation Standards*, is permanently rescinded and none of its provisions shall have any force or effect on any 7(a) loan.
- All policy addressed in the Interim Final Rule now reverts to the regulations in effect prior to March 11, 2020.

PAYCHECK PROTECTION PROGRAM

The Paycheck Protection Program (PPP), part of the CARES Act, will provide capital to small businesses to help them meet their short-term ongoing expenses, including payroll costs and other costs as specified in the statute. PPP borrowers will not be required to repay the portion of the loan that is used for the purposes specifically allowed by the statute. That concept is referred to in the statute as loan forgiveness. Loan funds used for purposes not included in the statute must be repaid.

PAYCHECK PROTECTION PROGRAM [Sections 1102, 1106 & 1109]:

- **Program Administration:** co-management by the Small Business Administration (SBA) and the Department of Treasury (Treasury)
- **Program Duration (“covered period”):** 2/15/2020 – 6/30/2020
- **Program Authorization Cap:** Authorizes \$349 billion to be shared by both PPP loans and all 7(a) loans during the covered period; the \$30 billion authorization cap for 7(a) loans does not apply during the covered period but will resume for 7(a) lending after the covered period
- **Program Appropriation:** Provides funding for PPP loans only at \$349 billion
[Note: the funding is not shared with all 7(a) lending; 7(a) loans still retain \$99 million in funding from FY2020 appropriations; only the authorization cap is shared by both PPP and 7(a) loans]
- **SBA Guaranty:** 100%
- **SBA Upfront Guaranty Fee:** Waived
- **SBA Ongoing Fee:** Waived between date of enactment and 6/30/2020; 55 basis points beginning 7/1/2020
[NAGGL has flagged for Congress that statutory language requires reinstatement of ongoing fee after 6/30/2020: stay tuned for additional guidance]
- **Origination Fee Paid to Lenders:** For PPP loans only, SBA will pay lender a loan origination fee based on loan size –
 - 5% of loan amount for loans of \$350,000 and less
 - 3% of loan amount for loans over \$350,000 up to \$2 million
 - 1% of loan amount for loans \$2 million and over

SBA is required to pay this fee within 5 days after loan disbursement.

[NAGGL has flagged for Congress that lenders do not report to SBA that a loan has been disbursed until they file their monthly 1502 report at the end of the month within which the loan was disbursed: stay tuned for additional guidance]

- **Agent Fee Limits:** SBA is authorized set fee limits for the fees that agents may charge applicants for assisting with the preparation of applications
- **Maximum Interest Rate:** 4% for life of loan, and guidance could set it lower

- **Prepayment Penalty (“Subsidy Recoupment Fee”):** NO prepayment penalty for any PPP loan
- **Maximum Loan Maturity:**
 - Statute is silent as to what maturity period should be established at the time of origination, but permits SBA to use regular 7(a) “terms, conditions and processes”
 - *[Stay turned for guidance from SBA regarding how this issue will be addressed]*
 - Statute specifies a 10-year maturity for any balance remaining after application of the forgiveness – SBA guaranty continues to apply
- **Eligible Lenders:**
 - All current 7(a) lenders AND
 - Additional lenders determined by SBA and Treasury to have the necessary qualifications to process, close, disburse and service loans guaranteed by SBA
 - Treasury, in consultation with SBA and Farm Credit Administration will establish criteria for participation by other entities that are not already SBA participating lenders
- **Delegated Authority:** Every lender approved to make PPP loans is authorized to process using delegated authority “subject to the provisions” of the program
- **Basic Eligibility:** Lender shall consider whether applicant –
 - Was in operation on 2/15/2020 AND
 - Had employees for whom it paid salaries and payroll taxes OR paid independent contractors (reported on a Form 1099-MISC)
- **Additional Eligibility Criteria:** The following entities are deemed eligible—
 - Small business concerns, including sole proprietorships, independent contractors and eligible self-employed individuals;
 - Self-employed individuals, independent contractors and sole proprietors must provide documentation to establish eligibility including payroll tax filings reported to IRS, Forms 1099-MISC, and income expenses from the sole proprietorship as deemed necessary by SBA and Treasury
 - *[NAGGL has flagged for Congress that the statute requires documentation that is not applicable to all forms of business organization: stay tuned for additional guidance]*
 - Nonprofit organizations as described in section 501(c)(3) of the IRS Code that are exempt from taxation under section 501(a) of the Code (excluding nonprofits receiving MEDICAID expenditures);
 - Veterans organizations (as described in section 501(c)(19) of the IRS Code that are exempt from taxation under section 501(a) of the Code); AND
 - Tribal business concerns
- **Eligible Business Size:** the greater of –
 - 500 employees OR
 - If applicable, the size standard in number of employees established by SBA for the industry in

which the business operates (13 CFR 121) EXCEPT

- For businesses in industries with NAICS codes beginning with 72 (accommodation and food services) that have more than 1 physical location, the 500 employee test applies to each individual location

[Stay tuned for additional guidance regarding size.]

- **Affiliation:**

- SBA Affiliation Regulations (13 CFR 121.103) apply *[program guidance may provide clarification]* EXCEPT:
 - Regulations are waived for covered loans under any of the three following circumstances—
 - Businesses with not more than 500 employees that operates under a NAICS codes beginning with 72 (accommodation and food services);
 - Businesses operating as a franchise **and** assigned Franchise Identifier Codes (FIC) by SBA *[Source for information would be the SBA Franchise Directory];*
 - Businesses that receive financial assistance from a company licensed under section 301 of the Small Business Investment Act of 1959 (a Small Business Investment Company)
- SBA Affiliation Regulations (13 CFR 121.103) also apply to nonprofit organizations and veterans organizations.

[Reminder: affiliation will be measured under the regulations that existed before March 11, 2020; the Interim Final Rule no longer applies because the statute rescinds it, as noted above.]

- **General Maximum Loan Size = lesser of –**

- \$10 million OR
- The sum of –
 - Applicant’s average total monthly payments for payroll costs *[See definition of payroll below]* for the 1-year period before the date on which the loan is made X 2.5 EXCEPT
 - For a seasonal employer, average total monthly payroll payments will be based on the 12 week period between 2/15/2019 and 6/30/2019
[The statute says “the 12 week period,” however, we recognize the time period provided is longer than 12 weeks—NAGGL has raised this concern with Congress; please stay tuned for further clarification.]
 - PLUS the outstanding amount of an SBA disaster loan made between 1/31/2020 and ending on the date on which covered loans are available to be refinanced under this program

- **Maximum loan size for a business not in business for the period beginning 2/15/2019 and ending 6/30/2019 = lesser of –**

- \$10 million OR
- The sum of the applicant’s average total monthly payments for payroll costs *[See definition of payroll below]* incurred during the period beginning 1/1/2020 to 2/29/2020 X 2.5

- **PLUS** the outstanding amount of an SBA disaster loan made between 1/31/2020 and the date on which covered loans are available to be refinanced under this program

- **Allowed Uses of Loan Proceeds** *[not all will be eligible for forgiveness]*:
 - Payroll costs
 - Costs related to continuation of group health care benefits during periods of paid sick, medical or family leave and insurance premiums
 - Employee salaries, commissions or similar compensations
 - Payment of interest on any mortgage obligation (excluding prepayment of, or payment of principal)
 - Rent
 - Utilities
 - Interest on any other debt obligation incurred before the covered period, and
 - Refinancing of a disaster loan made between 1/1/2020 and the date on which covered loans are made available to be refinanced

- Statute also permits any other permitted 7(a) use, but these uses will NOT be forgiven *[NAGGL has asked Congress to provide clarification on this point.]*

- **Definition of “Payroll”**

For individual employees, payroll = the sum of:

- Payments of any compensation to employees (salary, wages, commission or similar compensation) +
 - Payment of cash tip or equivalent +
 - Payment for vacation, parental, family, medical or sick leave +
 - Allowance for dismissal or separation +
 - Payment required for group health benefits (including insurance premiums) +
 - Payment of retirement benefit OR Payment of State or local tax assessed on the compensation of employees
- AND**
- For sole proprietor or independent contractor, the sum of payments of any compensation to or income that is a wage, commission, income, net earnings from self-employment or similar compensation and that is in an amount of not more than \$100,000/year as prorated for the covered period
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- Payroll shall **NOT** include –
 - Compensation of an individual employee in excess of an annual salary of \$100,000/year as prorated for the covered period
 - Taxes imposed or withheld under chapters 21, 22 or 24 of the IRS Code during the covered period
 - Any compensation of an employee whose principal place of residence is outside the U.S.
 - Qualified sick leave wages for which a credit is allowed under section 7001 of the

- Families First Coronavirus Response Act; or
 - Qualified family leave wages for which a credit is allowed under section 7003 of the Families First Coronavirus Response Act
- **Loan Deferment (principal and interest):**
 - For loans NOT sold in secondary market -- requires lenders to provide deferment of principal and interest for a period of not less than 6 months and not more than 1 year
 - For loans SOLD in secondary market – if investor declines to approve a deferment longer than 3 months, requires SBA to repurchase the loan from the secondary market so that the borrower can receive the same deferment as an unsold loan
 - SBA required to provide guidance within 30 days
- **Collateral:** No collateral will be required
- **Personal Guarantee:** No personal guaranty will be required BUT –
 - Government will have recourse against a shareholder, member or partner of a borrower company if loan proceeds are used for a purpose not authorized by the law
- **Required Borrower Certification at Time of Application:** Recipient must make a “good faith certification” *[Note that the Administration may provide a certification form or template]* –
 - Stating that uncertainty of current economic conditions makes loan request necessary to support ongoing operations
 - Acknowledging that funds will be used to retain workers and maintain payroll or make mortgage, lease and utility payments
[Allowed use of proceeds for refinancing disaster loans and for any other 7(a) purpose that are both permitted in statute are not included here; NAGGL has raised this point with Congress]
 - Stating that eligible recipient does not have another PPP application pending for same purpose AND
 - Acknowledging that the applicant may not receive another 7(a) loan for the same purpose through December 31, 2020
- **Secondary Market Sales:** PPP loans are eligible to be sold in the secondary market and no fees may be collected by SBA for any guaranty sold in the secondary market
[NAGGL has requested clarification as to what fees are intended to be included.]
- **EIDL Loans:** If a borrower received an EIDL loan between January 31, 2020 and the date on which PPP loans are made available, and if the EIDL loan was for a different purpose than PPP loans, then a borrower may receive a PPP loan.
[It is still unclear if a borrower could receive an EIDL loan after the date on which PPP loans are made available if for different purposes and NAGGL has requested clarification.]
- **Regulatory Capital Requirements:**
 - Risk Weight – zero risk weight (applies to all Federal Regulators, including NCUA)

- Temporary Relief from TDR Disclosures – after 3/13/2020 until regulators deem appropriate, an insured depository institution or credit union that modifies a PPP loan in a “troubled debt restructuring” will not be required to comply with Financial Accounting Standards Board Accounting Standards Codification Subtopic 310-40 (‘Receivables – Troubled Debt Restructurings by Creditors’)

LOAN FORGIVENESS [Section 1106]

PPP loan proceeds used for the purposes described below are eligible for “forgiveness” and the lender will receive payment from SBA equal to the amount of the forgiveness on each loan.

[Suggestion has been made that SBA provide a template worksheet to guide calculation of the forgiveness amount and any required reductions]

- **Amount Eligible for Forgiveness:** A PPP borrower is eligible to have its loan forgiven by an amount equal to the following costs incurred and payments made during the covered period –
 - Payroll costs +
 - Interest payments on any covered mortgage obligation (excluding prepayment of or payment of principal) +
 - Payments on covered rent obligations +
 - Any covered utility payment
- **Note:** The statutory list does not include refinancing of EIDL loans as eligible for forgiveness, whereas EIDL refinancing is an eligible use of PPP proceeds and allowed to be included in the maximum loan size. *[NAGGL has requested clarification.]*
- **Reduction in Amount Paid Based on Reduction in Number of Employees:**
 - Amount of PPP loan forgiveness will be reduced (but NOT increased) by –
 - Multiplying the amount eligible for forgiveness by
 - Quotient obtained by dividing the average number of full-time equivalent employees per month employed by the eligible recipient during the covered period by either (borrower’s choice):
 - the monthly average number of full-time equivalent employees per month employed by the eligible recipient between 2/15/2019 and 6/30/2019, OR
 - the average number of full-time equivalent employees per month employed by the eligible recipient between 1/1/2020 and 2/29/2020

OR

If an eligible recipient is a seasonal employer, the calculation of the average number of full-time equivalent employees will be based on the number of full-time equivalent employees per month employed by the eligible recipient during the period between 2/15/2019 and 6/30/2020

- Average number of full-time equivalent employees is calculated based on employees for each pay period falling within a month
- **Reduction in Amount Paid Based on Salary and Wages:**
 - If the employees' wages were cut by more than 25% during the most recent full quarter before 2/15/2020, the amount of the debt forgiven will be reduced by that amount.
 - Covered employees include those who did not receive, during any single payment period in 2019, wages or salary at an annualized rate of pay in an amount in excess of \$100,000.
[Guidance has been requested to clarify whether such individuals are totally excluded, or only the amount of their salary or wages over \$100,000.]
 - Forgiveness amount may include additional wages paid to tipped workers
- **Exemption for Rehires:**
 - If certain conditions are met, the amount of the forgiveness will not be reduced because either there was a reduction in the number of employees or a reduction in the salaries of one or more employees of the PPP loan recipient for 30 days after enactment
 - The reduction in forgiveness amount will not apply if by 6/30/2020 the total number of full-time equivalent employees is not reduced
 - The reduction in forgiveness amount will not apply if by 6/30/2020 any reduction in salaries or wages is eliminated
- **Authority for Exemptions:** SBA and Treasury may draft regulations granting de minimis exemptions to the requirements that forgiveness amounts be reduced.
[NAGGL has requested for clarification.]
- **PPP Borrower Application for Forgiveness:** Borrower must provide documentation to the lender to support the forgiveness request including [no forgiveness may be approved without the required documentation] –
 - Documentation supporting verifying the number of full-time equivalent employees on payroll and pay rates for the periods specified
[NAGGL has requested needed clarification on the time periods to use since the referenced section in the statute refers to multiple different time periods];
 - Payroll tax filings reported to IRS and
 - State income, payroll and unemployment insurance filings
 - Cancelled checks, payment receipts, transcripts of accounts or other documents verifying payments on covered mortgage obligations, payments on covered lease obligations and covered utility payments;
 - Any other documentation deemed necessary by SBA; AND
 - Certification from an authorized representative of the borrower that
 - Documentation presented is true and correct
 - Amount for which forgiveness is requested was used for purposes eligible for forgiveness

- **Lender Processing:**
 - With 60 days of receipt of documentation from borrower, lender must issue a decision on the application provided by the borrower
- **“Hold Harmless”:** Lender may rely on the certification of the borrower that the documentation submitted in connection with the request for forgiveness has accurately verified the payments for payroll costs, covered mortgage obligations, covered lease obligations, or covered utility payments
- **SBA Payment:** SBA will reimburse lenders for amount of loan forgiveness in one of two ways –
 - Advance purchase – the lender or a secondary market purchaser may request payment of the principal amount of the expected forgiveness of an individual loan or a pool of loans
 - SBA has 15 days to pay
[although the statute is silent, it is presumed that, after the forgiveness amount is calculated the lender and SBA will reconcile balance on each loan and the amount of forgiveness to be applied will be calculated for each borrower]
 - OR
 - Payment after calculation of forgiveness – lender may request reimbursement from SBA for principal + interest after it has determined the amount of the forgiveness
 - SBA has 90 days after the lender determines the amount of forgiveness to pay the lender the amount of the forgiveness + interest through the date of payment
- **Treatment of Forgiveness:** Amounts forgiven shall be considered canceled indebtedness by a lender
- **Taxability:** Forgiveness amount will not be considered as income of the borrower and will not be taxed