On Wednesday, March 25, 2020, the U.S. Senate unanimously approved the Coronavirus Aid, Relief, and Economic Security Act or the “CARES Act”. Among other things, the CARES Act amends the Small Business Act to allocate an additional $349 billion for forgivable 7(a) loans (each such loan a “Loan” and, collectively, the “Loans”) under the newly established “Paycheck Protection Program” (the “Program”) to provide certain small businesses with crucial financing during the crisis surrounding the COVID-19 pandemic.1

Because the Small Business Administration (“SBA”) has delegated authority to authorized lending institutions to administer the Program without the approval of the SBA, the role of banks and other qualified lenders is essential to the success of the Program. The SBA is actively seeking to authorize new lending institutions (those not previously authorized) as authorized providers of the Loan. This includes both bank and certain qualified non-bank lenders. This summary outlines key considerations lending institutions should take into account when considering whether to participate in the Program as lenders.

Delegated Authority
The SBA has delegated to participating lending institutions the authority to administer Loans and make their own determinations on borrower eligibility and creditworthiness.2 However, instead of using repayment eligibility to approve the loan, lenders shall consider whether the potential borrower was operational on February 15, 2020 and whether the potential borrower had employees (for whom the borrower paid salaries and payroll taxes) or independent contractors reporting on a FORM-1099.3 Supporting this limited creditworthiness evaluation, once the Loan is issued by the lender, the SBA will guarantee 100% of the principal amount of the Loan.4 Prior to the passage of the CARES Act, a typical 7(a) loan was only guaranteed by the SBA in amounts up to 75% or 85%.

Loan Terms
Under the Program, eligible lenders can now issue these Loans in amounts based on a formula which ties the loan amount to payroll costs incurred by the borrower, up to a maximum amount of $10 million.5 Borrowers must use the proceeds of the Loan only for certain enumerated purposes, including payroll costs, group health care benefits, mortgage interest payment and interest payments on debt existing prior to February 15, 2020.6

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2 See id. at § 1102(a)(2)(36)(F)(i).
3 See id. at § 1102(a)(2)(36)(F)(ii).
4 See id. at § 1102(a)(1)(B)(F).
5 See id. at §1102(a)(2)(36)(E).
6 See id. at §1102(a)(2)(36)(F).
The Program specifically waives any requirements that a borrower provide a personal guarantee or collateral to secure the Loan.\(^7\) In fact, the Loans are expressly nonrecourse against any individual shareholder, member or partner of a borrower for non-payment of the Loan, except to the extent loan proceeds are used for an unauthorized purpose. However, given that the Loans are 100% guaranteed by the SBA, the lender would not be required to pursue a borrower in any event. Even though the covered period for the Program only runs through June 30, 2020\(^8\), this SBA guaranty continues for life of the Loan, even with respect to any loan balance that remains outstanding after June 30, 2020.\(^9\)

One key benefit to borrowers is that Loan proceeds used to pay payroll, mortgage interest, rent and utilities between February 15, 2020 and June 30, 2020 are forgivable in full without being treated as income to the borrower. The Program provides that the SBA will pay lenders for 100% of the forgiven Loan amount within 90 days of the date of loan forgiveness (with interest for the date from forgiveness through the date of payment). The CARES Act expressly provides that no lender will be subject to claims or penalties by the SBA for forgiving payments on a Loan if lender bases such forgiveness on full documentation received by the lender from borrower evidencing forgivable payments.

Other terms of the Loans include the requirements that (a) a lender must defer all loan payments for a period of at least six (6) months but not greater than one (1) year,\(^10\) and (b) interest on the Loans cannot exceed 4.00% per annum.\(^11\) The Loans are also not supported by collateral and not guaranteed by the borrower.

The Program caps the processing fees that a participating lender can charge the borrower at amounts set by the SBA and waives all fees that would normally be charged by the SBA. The SBA will reimburse lenders for processing fees as follows within 5 days after disbursement of a covered Loan in the amount of:

- 5.0% for Loans of up to $350,000,
- 3.0% for Loans between $350,000 and $2,000,000, or
- 1.0% for Loans of $2,000,000 or more.\(^12\)

In addition, covered Loans issued under the Program may be sold on the secondary market, and no fees are payable to the SBA when these Loans are sold. However, if any transferee declines to honor the deferral of payments by the borrower for the required 6-12 month period prior to June 30, 2020, the SBA will be required to purchase the Loan.\(^13\)

Finally, to incentivize lenders, the Program states that the risk weight of a covered loan is 0% for any federal banking agency or national credit union regulatory authority that uses risk-based capital requirements.\(^14\)

**Becoming an Authorized Lender for the Program**

In order to become a qualified SBA lender for the Program, lending institutions should contact a lender relations specialist at their local SBA district office (to locate this office, they can use the following link: [https://www.sba.gov/local-assistance/find/](https://www.sba.gov/local-assistance/find/)).

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7 See id. at §1102(a)(2)(36)(F)(v).
8 See id. at §§ 1101, 1107.
9 See id. at § 1102(a)(2)(36)(K).
10 See id. at § 1102(a)(2)(36)(M).
11 See id. at § 1102(a)(2)(36)(L).
12 See id. at § 1102(a)(2)(36)(P)(ii).
13 See id. at § 1102(a)(2)(36)(M)(iii).
14 See id. at § 1102(a)(2)(36)(O)(i).
In order to participate, lenders must meet the following requirements:

- Have a continuing ability to evaluate, process, close, disburse, service, and liquidate small business loans;
- Be open to the public to issue loans (and not be a financing subsidiary, engaged primarily in financing the operations of an affiliate);
- Have continuing good character and reputation, and otherwise meet and maintain the ethical requirements as identified in 13 CFR Part 120.140; and
- Be supervised and examined by a state or federal regulatory authority, satisfactory to the SBA, which includes supervision by the SBA for SBIC funds.

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.

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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.