Memorandum

Date: April 3, 2020

To: NALCAB Membership & Partners

From: NALCAB Policy Team

Re: Initial Analysis of the Federal Paycheck Protection Program Regulation

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The Paycheck Protection Program (PPP), authorized in the recent CARES Act, makes available approximately $350 billion through the Small Business Administration's (SBA) 7(a) loan program structure for eligible lenders to make loans to businesses to support payroll and certain limited operating costs for an 8 week period beginning on the date of origination of the loan.

On the evening of Thursday April 2, the SBA published a regulation that provides some clarity about how lenders should administer this program and leaves some very important details as yet unclear. We want to share what we know based both on what we are reading in the regulation and our communications with colleagues in the financial services industry.

It is good that the Senate and House Small Business Committees moved quickly to put in place a program to deliver emergency financial relief to small businesses and the people they employ. It is also good that the Treasury and SBA moved rapidly to publish a regulation to implement the program. In a letter to Administration officials, however, Committee Chairwoman Nydia Velazquez' office has expressed concern that many feels about the chaotic and confusing public communications about this program.

NALCAB's primary focus with regard to the PPP is **how to ensure these resources make it to underserved businesses and microbusinesses** in the communities we serve. This is consistent with the intent of the law. The CARES Act states, "It is the sense of the Senate that the Administrator should issue guidance to lenders and agents to ensure that the processing and disbursement of covered loans prioritizes small business concerns and entities in underserved and rural markets, including veterans and members of the military community, small business concerns owned and controlled by socially and economically disadvantaged individuals, women, and businesses in operation for less than two years."

The program structure for the Paycheck Protection Program established by the Treasury Department and SBA makes it very difficult for underserved small business to get rapid access to these resources.

Challenges **:** There are not enough eligible lenders in the SBA 7a system that have a track record of providing access to capital for underserved businesses, as described in the CARES Act. The regulation makes access to the PPP far more difficult for 1099 contractors in particular because they are required to apply by themselves and cannot be included in the application of the businesses that "employs" them or is their primary source of income. The large majority of eligible lenders are publicly communicating that they will only serve their existing client base. Most of those eligible lenders that do in fact have a strong track record in this regard, are smaller and do not have the capacity to serve beyond their existing client base. In particular, they do not have access to sufficient cash to process the PPP product at scale, even if they can work out the staff and systems capacity challenge. Relying on the secondary market for capital adds cost and time to this process that could be avoided if the SBA and Treasury provided the liquidity directly. Given the very tight timeline to process these applications (June 30), the people who are left to the end of the line may not get served, even if they are eligible and there is sufficient funding.

***Solution*:** SBA should provide "Delegated Authority" to additional lenders with a focus on those that have a specialized track record of opening access to capital for underserved businesses and microbusinesses, including 1099 contractors.

***Solution*:** SBA should directly provide liquidity to eligible lenders with assets less than $750 million. SBA could begin by providing these smaller authorized providers of the PPP product with sufficient cash up front to cover 15 days of anticipated deployment to be held in a segregated account. SBA should then provide cash based on documentation of actual deployment taking into account when a provider is rapidly scaling their operation. This will eliminate the need for time consuming and expensive secondary market transactions and allow the SBA time to process payments without creating a cash payment bottleneck. Providers of the PPP product would return any repayments they recover from borrowers to SBA on a quarterly basis.

***Solution*:** SBA should change the regulation to allow businesses to include in their applications amounts to pay 1099 contractors that primarily rely on that business for their income, as determined by the business owner and documented through an attestation.

***Solution*:** Congress should extend the period during which loans can be processed until Dec. 31, 2020 (not to be confused with the covered period for forgivable expenses – that is a different question).

The Paycheck Protection Program regulation released by SBA and Treasury does not provide sufficient detail about the mechanics of how forgiveness will be authorized for the PPP product.

***Challenges*:** The regulation and system being developed to deploy the PPP product is appropriately designed to allow lenders to make loans quickly. A significant potential pitfall for businesses is to secure a loan quickly without fully understanding the terms and being stuck with debt later that they thought would be forgiven. The regulation published on April 2 offers cursory guidance on the mechanics for obtaining loan forgiveness and indicates, "SBA will issue additional guidance on loan forgiveness."

***Solution*:** It is critical that this additional guidance be issued as immediately as possible so lenders can provide full disclosure to business owners about what documentation will be required on the back end to allow the loan to be forgiven, as long as it is spent on eligible purposes.