January 5, 2021

COVID-19 "Phase IV" Stimulus

Latest Stimulus Legislation Provides Additional Coronavirus Relief

SUMMARY

On December 27, 2020, President Trump signed into law the 2021 Consolidated Appropriations Act (the "*Act*"). The Act provides approximately $900 billion in coronavirus pandemic-related relief, and, among other measures, provides one-time payments of $600 for individuals earning up to $75,000 annually ($1,200 for couples earning up to $150,000), authorizes emergency community development programs, lengthens temporary suspensions and modifications of several banking-related provisions, and authorizes approximately $325 billion in relief for small businesses that have been affected by the pandemic. The Act was adopted on December 21.[1] This memorandum summarizes key financial services-related provisions of the Act, including those relating to the Small Business Administration's Paycheck Protection Program (the "*PPP*").

The Act reauthorizes and appropriates up to $284.5 billion for the PPP,[2] for both first-time and second-time borrowers. Portions of that amount are set-asides for certain types of lenders: $15 billion for community financial institutions, including community development financial institutions and minority depository institutions and $15 billion for insured depository institutions, credit unions, and members of the Farm Credit System with less than $10 billion in consolidated assets. At least $35 billion will be reserved for first-time PPP borrowers, with $15 billion of that amount set aside for first-time borrowers that are either (1) businesses with fewer than 10 employees or (2) businesses that request a loan under $250,000 and that are located in a low- or moderate-income neighborhood.[3] Similarly, $25 billion is set aside for the same categories of small second-time borrowers.[4]

The Act revises the PPP in several notable respects, including by:

- extending the covered period for loan disbursements to March 31, 2021;

- developing a process through which a small business or non-profit can receive a second PPP loan of up to $2 million, if the entity has fewer than 300 employees and can demonstrate a reduction in gross receipts of 25% when compared to a corresponding financial quarter of 2019;
- creating a simplified PPP loan forgiveness application for loans under $150,000;
- revising the lender "hold harmless" provision to incorporate good-faith reliance and expand the statutes addressed;
- expanding the list of eligible PPP expenses to include covered operations, uninsured property damage resulting from public disturbances, covered supplier costs, and covered worker protection expenditures;
- repealing the provision of the Coronavirus Aid, Relief, and Economic Security Act (the "*CARES Act*") requiring the deduction of any Economic Injury Disaster Loan advance from a borrower's forgiveness amount, even if the borrower has already received forgiveness;
- prohibiting publicly listed companies from receiving funds under the PPP;
- modifying the exemptions from the SBA affiliation rules; and
- confirming explicitly that agent fees are required to be paid only for services for which the lender directly contracts with the agent.

In addition to these, and other, updates to the PPP, the Act establishes new emergency measures aimed at combatting the economic effects of the pandemic, including, among other measures, the appropriation of $12 billion for the creation of a new Emergency Capital Investment Program and to support the Community Development Financial Institutions Fund.

The legislation also extends several temporary regulatory suspensions and modifications for banking institutions enacted under the CARES Act,[5] including:

- temporary relief from compliance with the Current Expected Credit Losses accounting standard, which is extended through January 1, 2022;
- temporary relief from compliance with the Troubled Debt Restructuring loan classification, which is extended through January 1, 2022; and
- continued increased access to the National Credit Union Administration's Central Liquidity Facility, which is extended through December 31, 2021.

The Act also rescinds $429 billion of unobligated CARES Act funding designated for Treasury and certain Federal Reserve facilities and provides that, after December 31, 2020, and subject to limited exceptions, the Federal Reserve may not make any loan, purchase any obligation, asset, security, or other interest, or make any extension of credit through any program or facility established under Section 13(3) of the Federal Reserve Act in which the Treasury Secretary made a loan, loan guarantee, or other investment pursuant to Section 4003(b)(4) of the CARES Act. Additionally, funding from the Exchange Stabilization Act may not be used for "any program or facility established under Section 13(3) of the Federal Reserve Act . . . that is the same as . . . any program or facility in which . . . an investment [was made] pursuant to Section 4003(b)(4) of the CARES Act, except the Term Asset-Backed Securities Loan Facility." The

Federal Reserve's ability to establish facilities under Section 13(3), as that authority existed before the CARES Act was enacted, remains unchanged.

BACKGROUND

The legislation is the latest federal response to the pandemic. The first of these, the CARES Act, was signed into law on March 27, 2020, and authorized up to $500 billion in loans, loan guarantees, and other investments in support of eligible businesses, states, and municipalities,[6] and temporarily suspended or amended, or authorized temporary changes to, certain regulatory provisions applicable to banking institutions. The CARES Act also established the PPP, initially a $349 billion lending program for eligible small businesses, administered by the Small Business Administration (the "*SBA*") under Section 7(a) of the Small Business Act.

With respect to banking organizations, Subtitle A of Title IV of the CARES Act, designated as the Coronavirus Economic Stabilization Act of 2020 ("*CESA*"):

- authorized the Federal Deposit Insurance Corporation (the "*FDIC*") to establish an emergency guarantee program, which could be used to increase deposit insurance limits, and similarly permitted the National Credit Union Administration (the "*NCUA*") to increase deposit insurance limits;
- authorized the Office of the Comptroller of the Currency (the "*OCC*") to exempt specified transactions from lending limits applicable to national banks;
- required the Federal Reserve, the FDIC, and the OCC (collectively, the "*federal banking agencies*") to decrease temporarily the "Community Bank Leverage Ratio" pursuant to which certain community banks are deemed to be in compliance with otherwise applicable leverage and risk-based capital requirements;
- suspended the Troubled Debt Restructuring loan classification, which established accounting and reporting obligations applicable to the categorization by financial institutions of loan modifications as "troubled debt restructurings";
- provided the option for banking institutions to delay the implementation of the Current Expected Credit Losses accounting standard ("*CECL*");
- enabled enhanced access for credit unions to the NCUA's Central Liquidity Facility; and
- established a number of consumer financial protections, including with respect to credit reporting, mortgages, foreclosures, and evictions.

As noted above, the Act continues the suspension of the troubled debt restructurings relief, the delay of the CECL, and the enhanced access for credit unions to the Central Liquidity Facility (each, as discussed further below).

The PPP was launched on April 3, 2020,[7] and, within two weeks, the initial $349 billion in funding had been exhausted. In light of the unmet demand for PPP loans, and at the urging of the SBA and the Treasury Department, the Paycheck Protection Program and Health Care Enhancement Act was enacted on April 24, 2020, and increased by $310 billion the amount authorized for the SBA to commit for loans under the PPP, bringing the total to $659 billion.[8] On June 5, 2020, President Trump signed into law the Paycheck Protection Program Flexibility Act of 2020, (the "*Flexibility Act*") which made significant changes to the PPP, including among other modifications: (1) establishing a minimum maturity of five years for all loans made after the enactment of the Flexibility Act; (2) extending the eight-week "covered period" for expenditures that qualify for forgiveness; (3) requiring borrowers to use only 60% (down from 75%) of the loan proceeds for payroll costs,[9] and up to 40% (up from 25%), for other permitted purposes, as a condition to obtaining forgiveness of the loan; and (4) delaying from June 30, 2020 to December 31, 2020 the date by which employees must be rehired to avoid a reduction in the amount of a loan eligible for forgiveness. In the absence of any subsequent legislation, the authorization for the issuance of new loans under the PPP lapsed on August 8, 2020. Since the passage of the CARES Act, the SBA, in consultation with the Treasury Department, has issued, and continues to issue, regulations, guidance, and forms implementing the PPP.

The Act represents the first comprehensive legislative response to the pandemic since the spring, and the first major legislative update to the PPP since the Flexibility Act. Because of the process involved in passage of the Act, there is only very limited legislative history. Accordingly, as with the CARES Act and the original PPP, interpretation of statutory provisions may require further reliance on regulations, forms, and guidance issued by the SBA and the Treasury Department. For further information on the CARES Act and the PPP, please refer to our previous Memoranda to Clients on March 29, 2020, March 30, 2020, April 23, 2020, June 6, 2020, and our COVID-19 Updates & Guidance web page.

KEY UPDATES TO THE PAYCHECK PROTECTION PROGRAM

This memorandum summarizes key initial takeaways with respect to the Act's revisions to the existing PPP framework. Of particular note, the SBA Administrator (the "*Administrator*") is directed to promulgate implementing regulations no later than 10 days after the date of enactment, unless otherwise noted in the Act.[10] This requirement presents a significant implementation challenge for the SBA.

Extension of the covered period. The covered period,[11] or the period during which borrowers may receive initial and "second draw" PPP loans, has been extended to March 31, 2021.[12]

Additional expenses eligible for forgiveness. The Act retains the PPP's requirement that at least 60% of expenses must be attributable to payroll costs in order for the borrower to be eligible for full forgiveness,[13] but significantly expands the types of other expenses that are eligible for forgiveness under the PPP. The expansion of eligible expenses applies both to initial PPP loans and PPP "second draw" loans, as explained further below. In addition to payroll costs and covered mortgage, rent, and utility obligations, eligible expenses now include: (1) "covered operations expenditures"; (2) "covered property damage costs"; (3) "covered supplier costs"; and (4) "covered worker protection expenditures."[14]

- "Covered operations expenditures" include payments for "any business software or cloud computing service that facilitates business operations, product or service delivery, the processing, payment, or tracking of payroll expenses, human resources, sales and billing functions, or accounting or tracking of supplies, inventory, records and expenses."[15]

- "Covered property damage costs" include costs related to property damage due to "public disturbances" that occurred during 2020 that are not covered by insurance.[16]
- "Covered supplier costs" include payments for supplies "essential to the operations of the entity" and made pursuant to contracts relating to perishable goods or entered into before the loan forgiveness covered period.[17]
- "Covered worker protection expenditures" include costs incurred in order to comply with COVID-19-related requirements or guidance issued by the Department of Health and Human Services, the Centers for Disease Control, the Occupational Safety and Health Administration, or state and local governments.[18]

The Act applies the expanded set of eligible expenses to any loan made "before, on, or after the date of enactment of the Act,"[19] but excludes such loans for which a borrower "received forgiveness before the date of enactment of [the] Act."[20] It is unclear whether a borrower will be considered to have "received forgiveness" upon submission of a loan forgiveness application to a lender or approval of the application by the lender, or if a loan will be considered forgiven only upon the expiration of the SBA's 90-day review period (or earlier, if payment is remitted to the lender sooner).[21] Allowing a borrower to revise a forgiveness application during the time that a lender or the SBA is considering an application for approval or denial does not appear to be expressly contemplated or prohibited by the Act.

Second Draw Loans. The Act permits PPP borrowers to receive a second PPP loan if they have used, or will use, the full amount of their initial PPP loan before the date they would receive the second PPP loan.[22] We refer to these second PPP loans as "second draw loans." The Act notes that the Administrator "may guarantee covered loans to eligible entities under the same terms, conditions, and processes" as initial PPP loans, unless otherwise provided in the Act.[23] The disbursement of loans under the PPP second draw loan program will end on March 31, 2021, the date on which the funding authorization will expire.[24]

For most borrowers, a PPP second draw loan may be up to 2.5 times the borrower's average monthly payroll costs,[25] but may be up to 3.5 times the average monthly payroll costs for borrowers in the hospitality and food services industries (i.e., those that have been assigned a North American Industry Classification System ("*NAICS*") code beginning with 72).[26] For both categories of borrower, however, the loan amount is capped at $2 million.[27]

Not all borrowers who were eligible for an initial PPP loan will be eligible for the second draw loan program. Eligible borrowers under the PPP second draw loan program are limited to businesses, nonprofit organizations, housing cooperatives, veterans organizations, tribal businesses, eligible self-employed individuals, sole proprietors, independent contractors, or small agricultural cooperatives[28] that have 300 or fewer full-time and part-time employees. The 300 employee cap is a reduction from the 500 employee limit for initial PPP loans. In calculating the number of employees, the SBA's affiliation rules would appear to continue to apply in the same manner as under the original PPP (with certain modifications), which broadly defines affiliation and includes in the calculation employees of each affiliate of the business.[29] Borrowers in the hospitality and food services industries with more than one physical location would still qualify if they employ not more than 300 employees per physical location and are not publicly listed entities.[30] In addition to the size and affiliate limitations set forth above, a borrower must demonstrate at least a 25% reduction in gross receipts in any given quarter of 2020 relative to the corresponding 2019 quarter.[31] Further, if the entity was not in operation during 2019, but was in operation as of February 15, 2020, gross receipts during the second, third, or fourth quarter of 2020 must demonstrate not less than a 25% reduction from the gross receipts of the entity from the first quarter of 2020.[32]

If a borrower applies for a PPP second draw loan of less than $150,000, the borrower may certify that it has met the gross receipt reduction requirement, and then subsequently submit documentation supporting such certification on or before the date on which the borrower applies for forgiveness.[33] It is unclear how the requirement to "produce adequate documentation that the eligible entity met [the] revenue loss standard" will interact with the simplified loan forgiveness application for borrowers with initial PPP loans of less than $150,000 (as further discussed below). Borrowers that receive initial loans of less than $150,000 are not required to produce *any* documentation,[34] raising the possibility that borrowers with PPP second draw loans of less than $150,000 may be subject to an alternative forgiveness process, at least with respect to the second draw loan, even if the same borrower holds both an initial and a second draw loan of less than $150,000 each.

The second draw loan program also excludes those businesses that are generally ineligible under the existing 7(a) lending program (except for nonprofit businesses and certain religiously oriented businesses),[35] entities primarily engaged in political or lobbying activities, entities affiliated with entities organized under the laws of the People's Republic of China or the Special Administrative Region of Hong Kong (or entities that have a director that is a resident of the People's Republic of China), and entities required to register under the Foreign Agents Registration Act, as well as entities that receive a grant under the Shuttered Venue Operator Grant program.[36] A lender already approved to make loans under the PPP may (but does not appear obligated to) make PPP second draw loans on the same terms and conditions as initial PPP loans, unless as otherwise provided in the Act or unless the relevant requirements have changed pursuant to subsequent regulations, guidance, and forms issued by the SBA.[37]

As previously noted with respect to initial PPP loans, borrowers of PPP second draw loans are eligible for a loan forgiveness amount equal to the sum of their payroll costs and their covered mortgage, rent, and utility payments, covered operations expenditures, covered property damage costs, covered supplier costs, and covered worker protection expenditures incurred during the loan forgiveness covered period. As with initial PPP loans, at least 60% of expenses must be payroll expenses in order to qualify for full forgiveness.[38] For both types of loan, a borrower will be able to elect a loan forgiveness covered period that begins at loan origination and ends on a date of the borrower's choosing between eight and 24 weeks after loan origination.[39]

Expanded pool of eligible borrowers. The pool of borrowers eligible for initial PPP loans has been expanded to include housing cooperatives, some types of 501(c)(6) organizations, destination marketing organizations, FCC license holders, and certain state colleges and universities.[40] Further, any entity, including FCC license holders and state colleges and universities that are also considered public broadcasting entities, are now eligible to receive PPP loans if the entity is majority-owned or controlled by a newspaper publisher or broadcasting entity (i.e., those entities that have been assigned a NAICS code beginning with 511110 or 5151), and the borrower certifies in good faith that the PPP loan will be used to support expenses related to "locally focused or emergency information."[41] To qualify, a prospective media-related borrower may not employ more than 500 individuals (or an alternative size standard established by the Administrator) at any one location.[42] FCC license holders and other borrowers that now qualify under the Act are also exempt from general SBA affiliation rules, provided that such prospective borrowers do not employ more than 500 employees per location (or the size standard established by the Administrator) and such prospective borrowers are majority-owned or controlled by a newspaper publisher or broadcasting entity.[43]

Publicly listed businesses now expressly ineligible to receive PPP funds. Businesses that issue securities listed on a national securities exchange are now ineligible to receive PPP funds.[44] This prohibition does not appear to exclude borrowers with affiliates listed on national exchanges; however, the Act expressly states that this provision will not apply to affiliates of any entity described in Section 317 of the Act (e.g., the corporate parent of an FCC license holder).[45]

Ability of borrowers to request an increased loan amount. The Act provides that the Administrator must, within 17 days after the enactment of the Act, issue rules or guidance to ensure that borrowers that returned a portion of an initial PPP loan can reapply for the amount of such loan that was returned, or can request a loan modification to increase the amount of the loan to the maximum amount for which such borrower was initially approved.[46] This process is not related to a borrower's ability to receive a PPP second draw loan and is not part of the second draw program. Although it seems that this provision may be intended to provide relief for those businesses that were unable to use the proceeds of the initial PPP loan for permitted purposes during the applicable period after disbursement, it is unclear whether this provision could also apply to borrowers that may have returned funds due to an inability to certify previously that economic uncertainty made the PPP loan request necessary to support the ongoing operations of such borrower.[47] The Act also allows borrowers to ask for increased funds due to changes to any interim final rule, even if the initial loan amount has been fully disbursed.[48] The Act allows borrowers to receive additional funds if they have already applied for, but not yet received, forgiveness on the day before the date of enactment of the Act.[49] Borrowers that received forgiveness before the enactment of the Act are not allowed to request additional funds.[50]

Simplified PPP loan forgiveness application. The SBA is directed to issue a one-page, streamlined loan forgiveness application, within 24 days of the enactment of the Act, for borrowers that have an existing PPP loan, or will obtain a PPP loan, in an amount of not more than $150,000.[51] In completing the form, the borrower must attest that it qualifies for forgiveness, has complied with PPP requirements, and will retain documents to prove compliance with such requirements.[52] These borrowers must retain relevant records related to employment for four years and all other records for three years.[53] The Administrator retains the right to audit any streamlined applications.

Although the provisions relating to the simplified PPP forgiveness application also apply to PPP second draw loans,[54] as previously mentioned, second-time borrowers with loans of not more than $150,000 must also submit documentation supporting the gross receipt reduction certification on or before the date on which they apply for forgiveness, which may lead to operational difficulties in standardizing a simplified loan forgiveness application for first-time and second-time borrowers.[55]

Modifying the hold harmless provision. The Act adds a good faith obligation on the lender and requires compliance with all federal, state, and local requirements applicable to a lender. The implications of this new language are not clear, but a good-faith standard appears to be generally consistent with guidance previously issued by the SBA.[56] Of most importance, the Act continues to state that a lender may rely on any certification or documentation submitted by an initial or second draw PPP loan applicant, provided that such certification or documentation:

> (A) is submitted pursuant to all applicable statutory requirements, regulations, and guidance related to initial or second draw PPP loan[s] . . . and (B) attests that the applicant has accurately provided the certification or documentation to the lender in accordance with the statutory requirements, regulations, and guidance described in [condition] (A).[57]

A lender will not be subject to an enforcement action or any penalties relating to loan origination or forgiveness if the lender relies on the above-mentioned certification or documentation, and such lender (1) "acts in good faith relating to loan origination or forgiveness of the initial or second draw PPP loan based on that reliance," and (2) "all other relevant Federal, State, local, and other statutory and regulatory requirements applicable to the lender are satisfied with respect to the initial or second draw PPP loan."[58] Unlike the CARES Act, the bar against enforcement actions is not limited to those enforcement actions taken under Section 47(e) of the Small Business Act (15 U.S.C. § 657t(e)).[59]

Bankruptcy-related provisions. The Act establishes special procedures related to PPP borrowers that are in bankruptcy and authorizes debtors in possession or trustees to obtain initial or second draw PPP loans if approved by the bankruptcy court.[60] These provisions will take effect on the date the Administrator determines certain debtors in bankruptcy to be eligible for PPP initial and second draw loans[61] and will expire two years after the date of enactment of the Act.[62]

EIDL grants are now eligible for forgiveness. Section 1110 of the CARES Act had required PPP borrowers that also received an EIDL Advance to deduct the amount of their EIDL Advance from their PPP forgiveness amount, with the potential of leaving many borrowers with a $10,000 stub payment left to be repaid under their PPP loan.[63] The Act repeals this provision of the CARES Act, thereby making EIDL Advance amounts eligible for forgiveness under the PPP.[64] Within 15 days of the date of enactment of the Act, the Administrator must issue rules to “ensure the equal treatment” of borrowers that completed loan forgiveness applications before the passage of the Act and were therefore denied forgiveness on EIDL Advances.[65] The Act also includes a $20 billion appropriation for EIDL Advance grants.[66]

Agent fees. The Act expressly limits agent fees payable by lenders to those “fees to an agent for services for which the lender directly contracts with the agent.”[67] This language applies retroactively to the beginning of the PPP, confirms numerous recent judicial decisions, and would appear to have the potential to curtail remaining (or new) litigation concerning alleged agents seeking fees from lenders for allegedly helping small business borrowers obtain loans under the PPP. Also, in a departure from the SBA’s regulatory requirements, which provided that agents may not collect fees from borrowers,[68] if a borrower has “knowingly retained an agent,” such fees will be paid by the borrower (but shall not be paid out of the proceeds of a loan).[69]

COMMUNITY DEVELOPMENT INVESTMENT

The Act provides for two emergency programs aimed at revitalizing and providing long-term financial products, service availability, and investments in, low- and moderate-income and minority communities that have disproportionately suffered from the impacts of the pandemic.

Capital investment program. Section 308 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989[70] (“*FIRREA*”) established the following goals for banking regulators:

- to preserve the number of minority depository institutions (“*MDI*”);
- to preserve minority character in cases of merger or acquisition of an MDI;
- to provide technical assistance to prevent insolvency of institutions not now insolvent;
- to promote and encourage creation of new minority depository institutions; and
- to provide for training, technical assistance, and educational programs.

Banking regulators have historically taken steps to preserve and encourage minority ownership of insured financial institutions in furtherance of these goals. However, the number of MDIs has decreased substantially in the last decade.

Aligned with the goals of Section 308 of FIRREA, and in response to the pandemic, the Act provides for a $9 billion emergency capital investment fund, administered by the Treasury Secretary through a newly established emergency capital investment program (the “*Emergency Capital Investment Program*”), to support the efforts of “low- and moderate-income community financial institutions” to, among other things, provide loans, grants, and forbearance for small businesses, minority-owned businesses, and consumers, especially in low-income and underserved communities, including those communities that may be disproportionately impacted by the economic effects of the pandemic.[71] Of the $9 billion, $4 billion will be set aside for eligible institutions with less than $2 billion in total assets, of which $2 billion will be set aside for institutions with less than $500 million in total assets.[72]

The Treasury Secretary is required to begin accepting applications under the Emergency Capital Investment Program within 30 days after the date of enactment of the Act.[73] Only low- and moderate-income community financial institutions will be eligible to participate in the program.[74] The Treasury Secretary may establish additional criteria for participation as the Secretary deems appropriate in furtherance of the goals of the Emergency Capital Investment Program.[75]

"Low- and moderate-income community financial institutions" means any financial institution that is either a CDFI or an MDI and that is (1) an insured depository institution that is not controlled by a bank holding company or savings and loan holding company that is also an eligible institution[76], (2) a bank holding company, (3) a savings and loan holding company, or (4) a federally insured credit union. A "CDFI" is a community development financial institution, as defined in Section 103 of the Community Development Banking and Financial Institutions Act of 1994.[77] An "MDI" is an entity that is (1) a minority depository institution, as defined in Section 308 of FIRREA,[78] (2) considered to be a minority depository institution by the appropriate federal banking agency or the NCUA, or (3) listed in the Federal Deposit Insurance Corporation's Minority Depository Institutions List published for the Third Quarter of 2020.

Among other requirements, to participate in the Emergency Capital Investment Program, low- and moderate-income financial institutions must:

- submit an application; and
- develop a plan to maintain or expand significant lending or investment activity in low- and moderate-income minority communities, especially those disproportionately impacted by the pandemic, and to minorities with significant unmet capital or financial services needs.[79]

Investments under the Emergency Capital Investment Program will take the form of purchases of preferred stock and, in some cases, other financial instruments from eligible institutions, with terms and conditions to be determined by the Treasury Secretary in accordance with specified requirements and restrictions.[80]

The authority to make new capital investments in low- and moderate-income community financial institutions will terminate six months after the date on which the national emergency concerning the coronavirus outbreak, declared by President Trump on March 13, 2020, terminates (the "*Coronavirus Emergency Termination Date*").[81]

Emergency Support through the CDFI Fund. The Community Development Financial Institutions program provides monetary awards and training opportunities to invest in and build the capacity of CDFIs. CDFIs are financial institutions that primarily serve individuals and/or communities that have been underserved by traditional financial institutions. The Act provides for $3 billion in emergency support funds (the "*Emergency Support Funds*") to the CDFI Fund to provide grants and other financial and technical assistance to CDFIs, including CDFI loan funds, as they serve consumers, small businesses, and nonprofits responding to the pandemic.[82]

Of the Emergency Support Funds, $1.25 billion will be available until September 30, 2021 to award grants and financial assistance to CDFIs to respond to the economic impact of the pandemic.[83] These funds will be made available not later than 60 days after the date of enactment of the Consolidated Appropriation Act.[84]

The remaining $1.75 billion will be available until expended to provide additional grants and financial assistance to CDFIs to respond to the economic impact of the pandemic.[85] Of these funds, $1.2 billion are reserved for providing financial assistance, technical assistance, awards, training and outreach programs to recipients that are "minority lending institutions," a new category of CDFIs that predominately service minority communities and are either MDIs or meet other standards as determined by the CDFI Fund.[86]

The authority to make new Emergency Support Funds will terminate on the Coronavirus Emergency Termination Date.[87]

TEMPORARY PROVISIONS APPLICABLE TO BANKING INSTITUTIONS AND REGULATORS

As described below, the Act temporarily suspends or amends, or authorizes temporary changes to, certain provisions applicable to banking institutions and regulators.

A. TROUBLED DEBT RESTRUCTURINGS

Under U.S. generally accepted accounting principles ("*U.S. GAAP*"), a restructuring of debt constitutes a Troubled Debt Restructuring ("*TDR*") if the creditor, for economic or legal reasons related to the debtor's financial difficulties, grants a concession to the debtor that the creditor would not otherwise consider. Under U.S. GAAP, any loan modified in a TDR is treated as an impaired loan. Impaired loans must be evaluated under applicable accounting standards, including measuring impairment and determining whether to record a charge-off or establish reserves. Classification of a loan as a TDR must also be reflected in an institution's regulatory and financial reporting.

Under CESA, a financial institution may elect to (1) suspend requirements under U.S. GAAP for loan modifications related to the coronavirus outbreak that would otherwise be categorized as a TDR, and (2) suspend any determination of a loan modified as a result of the effects of the coronavirus outbreak as being a TDR, including impairment for accounting purposes. The purpose of this measure is to allow bank lenders to enter into forbearances and modifications with borrowers affected by the coronavirus outbreak without suffering adverse accounting and, by extension, regulatory capital consequences.[88]

The Act extends the temporary TDR relief under CESA through January 1, 2022 and clarifies that the TDR relief provision applies to "insurance companies" as well as "financial institutions."[89]

B. CURRENT EXPECTED CREDIT LOSS METHODOLOGY

In June 2016, the Financial Accounting Standards Board issued Accounting Standards Update ("*ASU*") No. 2016-13, which introduced the CECL methodology for estimating allowances for credit losses.[90] Under U.S. GAAP, CECL replaces an "incurred loss" approach to the recognition of credit losses on financial assets measured on an amortized cost basis with a "forward-looking" approach based on the expected credit loss over the life of the instrument. For Securities and Exchange Commission ("*SEC*") reporting companies with fiscal years ending December 31, the CECL methodology generally became effective beginning with the first quarter of 2020.[91] There has been ongoing concern that application of the CECL methodology has had and could continue to have consequences for some banks' financial reporting, capital ratios and lending capacity during the coronavirus outbreak.[92]

CESA provided that, notwithstanding any other provision of law, no insured depository institution, credit union, bank holding company, or any affiliate thereof is required to comply with ASU 2016-13, including the CECL methodology, during the period beginning on CESA's enactment date (March 27, 2020) and ending on the earlier of the date on which the national emergency concerning the coronavirus outbreak declared by the President terminates or December 31, 2020.

The Act extends the temporary relief from ASU 2016-13, including the CECL methodology, under CESA through January 1, 2022.[93]

C. NATIONAL CREDIT UNION ADMINISTRATION'S CENTRAL LIQUIDITY FACILITY

The NCUA's Central Liquidity Facility (the "*CLF*") is a mixed-ownership government corporation that is owned by member credit unions and that serves as a liquidity lender to credit unions experiencing unusual or unexpected liquidity shortfalls. CESA temporarily increased the availability of the CLF through December 31, 2020, including by permitting certain expansions to corporate credit union membership and by removing a limitation on the NCUA from approving an application for credit with the intent to expand credit union portfolios.

The Act extends the temporary expansions to the NCUA CLF under CESA through December 31, 2021.[94]

CARES ACT LENDING FACILITIES & LENDING AUTHORITY

As noted above, the CARES Act provided $500 billion in funding for the Treasury and the Federal Reserve to establish temporary lending facilities that expired on December 31, 2020. To date, a large portion of these authorized funds has not been expended. The Act requires the immediate rescission of $429 billion of such unobligated funds.[95] Other than certain (1) administrative expenses, (2) funds made available for the Special Inspector General for Pandemic Recovery, and (3) funds made available for the Congressional

Oversight Commission established under Section 4020 of the CARES Act, any remaining unobligated funds made available pursuant to Section 4027 of the CARES Act will be permanently rescinded on January 9, 2021.[96] The Act also confirms that the authority to make loans, loan guarantees or other investments under Section 4003(b) of the CARES Act terminated as of December 31, 2020.[97] Additionally, after December 31, 2020, the Federal Reserve may not make any loan, purchase any obligation, asset, security, or other interest, or make any extension of credit through any program or facility established under Section 13(3) of the Federal Reserve Act[98] in which the Treasury Secretary has made a loan, loan guarantee, or other investment pursuant to Section 4003(b)(4)[99] of the CARES Act. There is an exception for any loan submitted to the Main Street Lending Program's lender portal if submitted on or before December 14, 2020, provided, further, that the Program purchases a participation interest before January 8, 2021.[100] Finally, congressional authorization will be required if, in the future, the Treasury Secretary intends to use Exchange Stabilization Act funds to support any "program or facility established under Section 13(3) of the Federal Reserve Act . . . that is the same as any . . . program or facility in which the [Treasury] Secretary made an investment pursuant to Section 4003(b)(4) [of the CARES Act], except the Term Asset-Backed Securities Loan Facility."[101]

OTHER PROVISIONS

The Act contains several other notable provisions in addition to those discussed above, which include:

- clarification that (1) forgiven PPP loans and EIDL grants will not be included in taxable income, (2) deductions are allowed for expenses paid with the proceeds of forgiven PPP loans and EIDL grants, and (3) where the borrower is a partnership or S corporation, loan forgiveness will not reduce a partner's outside basis;[102]
- direct one-time payments of $600 for individuals earning up to $75,000 annually and $1,200 for couples making up to $150,000, as well as an additional amount of $600 for each eligible child dependent;[103]
- $120 billion in additional federal funding for unemployment insurance, extending the unemployment insurance expansion established under the CARES Act through March 14, 2021;[104]
- $15 billion in SBA grants to certain live venues, theaters, museums, and zoos to address the economic impact of the pandemic;[105] and
- continuation of debt relief payments of principal and interest on small business loans guaranteed by the SBA under the 7(a), 504, and microloan programs.[106]

* * *

ENDNOTES

[1] The Act was adopted in the U.S. Senate by a vote of 92 to 6, and in the U.S. House of Representatives by votes of 359 to 53 and 327 to 85. The first vote concerned all portions of the Act, except divisions B, C, E, and F. The second vote covered those remaining sections.

[2] Of the approximately $325 billion in total relief to small businesses, $284.45 billion is allocated to the PPP, $20 billion is allocated to certain borrowers under the EIDL Advance program, $15 billion is allocated to the Shuttered Venue Operator Grant program, $3.5 billion is allocated towards the Debt Relief program to assist borrowers of non-PPP SBA loans, and approximately $1.92 billion is allocated to implementing other loan programs administered by the SBA, including costs of implementing updates to such programs pursuant to the Act. Consolidated Appropriations Act, 2021, Div. N (the "*Act*"), H.R. 133, § 323(d)(1).

[3] *Id.* § 323(d)(1)(A)(iii).

[4] *See id.* § 323(d)(1)(A)(v). After 25 days from the enactment of the Act, the Administrator may adjust the set-aside amounts if (1) it is not reasonably expected that a given type of borrower or lender will receive, or make, the minimum amount of funds allocated to such category of borrower or lender and (2) it is reasonably expected that the total amount of loans guaranteed under the PPP will equal substantially all available funds. *Id.* § 328(d)(2)(B). It is not clear how lenders will monitor the participation of first-time borrowers and smaller first-time and second-time borrowers eligible for set-aside amounts, and the total amount of funds borrowed by such borrowers across the PPP.

[5] Pub. L. No. 116-136 (2020).

[6] The $500 billion appropriated under Subtitle A of Title IV of the CARES Act, the Coronavirus Economic Stabilization Act of 2020 ("*CESA*") included: (1) up to $25 billion for loans and loan guarantees for U.S. passenger air carriers and related businesses; (2) up to $4 billion for loans and loan guarantees for U.S. cargo air carriers; (3) up to $17 billion for loans and loan guarantees for businesses critical to maintaining national security; and (4) up to $454 billion, plus any amounts not used under the three preceding categories, for loans, loan guarantees, and other investments in connection with certain eligible programs or facilities established by the Board of Governors of the Federal Reserve System. 12 U.S.C. § 343(b)(1)-(4).

[7] Over the period following April 3, 2020, the SBA, in consultation with Treasury, has issued extensive rules and guidance for lenders and borrowers participating in the PPP in a number of formats.

[8] Pub. L. No. 116-139 (2020).

[9] The Flexibility Act may have been interpreted to require that a borrower use 60% of the loan amount for payroll costs in order to be eligible for forgiveness. *See* Flexibility Act, Pub. L. No. 116-142 § 3(b)(2) (2020). Shortly after the enactment of the Flexibility Act, in a joint statement by Secretary Mnuchin and Administrator Carranza, Treasury and the SBA clarified that if a borrower uses less than 60% of the loan amount for payroll costs, "the borrower will continue to be eligible for partial loan forgiveness, subject to at least 60% of the loan *forgiveness* amount having been used for payroll costs." Joint Statement by Treasury Secretary Mnuchin and SBA Administrator Carranza Regarding Enactment of the Paycheck Protection Program Flexibility Act (June 8, 2020) (emphasis added).

[10] The Act, § 303. In Section 303, the Administrator must issue regulations no later than 10 days after the date of the Act's enactment. However, other provisions of the Act have more specific timelines that appear to override the 10-day requirement. For instance, the Administrator shall complete a simplified application for loans of less than $150,000 within 24 days after the enactment of the Act. *See id.* § 307(a). Further, the Administrator must, within 17 days, issue rules or guidance for borrowers to receive approved but unfunded or returned portions of loans, *id.* § 312(b), and must issue rules relating to the repeal of the EIDL Advance deduction within 15 days of the Act's passage. *Id.* § 333(e).

ENDNOTES (CONTINUED)

11 Legislation and SBA regulations, forms, and guidance refer to two types of "covered periods": the "covered period" to receive a PPP loan and the "covered period" relevant to loan forgiveness calculations. The "covered period" to receive a PPP loan has been extended until March 31, 2021. The loan forgiveness "covered period" relating to forgiveness calculations means the period beginning on the date of loan origination and ending on a date of the borrower's choosing between eight and 24 weeks after loan origination.

12 The Act, § 343(a).

13 Flexibility Act, § 3(b)(2); Joint Statement by Treasury Secretary Mnuchin and SBA Administrator Carranza Regarding Enactment of the Paycheck Protection Program Flexibility Act (June 8, 2020).

14 The Act, § 304(a).

15 *Id*. § 304(b)(2)(A)(v).

16 *Id*. § 304(b)(2)(A)(vi).

17 *Id*. § 304(b)(2)(A)(vii).

18 *Id*. § 304(b)(2)(A)(viii).

19 *Id.* § 304(c)(1).

20 *Id.* § 304(c)(2).

21 *See* 85 Fed. Reg. 33004, 33005 (June 1, 2020) ("SBA will, subject to any SBA review of the loan or loan application, remit the appropriate forgiveness amount to the lender, plus any interest accrued through the date of payment, not later than 90 days after the lender issues its decision to SBA.").

22 The Act, § 311(a).

23 *Id*. § 311(a).

24 *Id*. § 323(a)(1)(B).

25 At the election of the borrower, the average payroll would be calculated by referring to the one-year period before which the loan is made, or by reference to fiscal year 2019. For seasonal employers, the amount will be calculated by referring to any 12-week period between February 15, 2019 and February 15, 2020. *See id*. § 311(a). The definition of "payroll costs" has been expanded to include group life, disability, vision, or dental insurance.

26 *Id*. § 311(a). Seasonal employers are to use the average total monthly payroll cost over any 12-week period between February 15, 2019 and February 15, 2020 when calculating the maximum amount of a covered loan.

27 *Id*.

28 *Id*.

29 *See* 13 C.F.R. § 121.103 for the SBA's affiliation rules. Under these rules, the SBA considers factors such as "ownership, management, previous relationships with or ties to another concern, and contractual relationships, in determining whether affiliation exists." The SBA will consider the totality of the circumstances in determining if a person is an affiliate of a business concern.

30 The Act, §§ 311(a), 342. Pursuant to the CARES Act, the affiliation rule is waived for businesses (1) in the hospitality and food services industries (and that employ not more than 300 employees, as modified by the Act), (2) that are franchises, as recognized by the SBA's franchise directory, or (3) that receive financial assistance from a company licensed under Section 301 of the Small Business Investment Act of 1958. 15 U.S.C. § 636(a)(36)(D)(iv).

31 The Act, § 311(a). The Act provides that if the entity was not in business during the first or second quarter of 2019, the third or fourth quarter of 2019 would be used as a benchmark, and if the entity

was not in business during the first, second, or third quarter of 2019, the fourth quarter of 2019 would be used as a benchmark. *Id.*

32 *Id.* Under the terms of the Act, it is not clear whether an entity that was not in existence in 2019 but was in operation by February 15, 2020 would, for purposes of the 25% reduction test, use an adjusted gross receipts amount to cover the entire first quarter of 2020, or use the actual gross receipts amount instead.

33 *Id*.

34 See *id.* § 307(a)(3).

35 *See* 13 C.F.R. § 120.110; the Act, § 311(a). Hedge funds and private equity firms were previously deemed to be speculative businesses, and thus ineligible, by the SBA. 85 Fed. Reg. 23450, 23451 (Apr. 28, 2020).

36 The Act §§ 311(a), 310(b). Though not eligible under the revised PPP, the Act also provides $15 billion in grants to certain live venue operators and promoters. *See id.* § 324.

37 *Id.* § 311(a).

38 In general, and subject to certain qualifications, exceptions and safe harbors, a forgiveness amount is reduced if a borrower spends less than the required thresholds on eligible expenses, does not retain the same average amount of full-time employees during the covered period when compared to a selected base period, and/or reduces an employee's salary or wage greater than 25% when compared to a base period. The second draw loan provisions of the Act appear to have codified the position of Treasury and the SBA (with respect to second draw loans) that if a borrower uses less than 60% of the loan amount on payroll expenses, a borrower is still eligible for partial forgiveness, but payroll expenses must be at least 60% of the loan forgiveness amount. *See supra*, n. 9; the Act, § 311(a) (to be codified as 15 U.S.C. § 636(a)(37)(J)(iv)).

39 *Id*. § 306.

40 *See id*. §§ 316–18.

41 *Id*. § 317(a)(2).

42 *Id*.

43 *Id*. § 317(b).

44 Though publicly traded companies were not prohibited from applying to the PPP, the SBA had issued an FAQ reminding borrowers that they "must certify in good faith that their PPP loan request is necessary" and that "[b]orrowers must make this certification . . . taking into account their current business activity and their ability to access other sources of liquidity sufficient to support their ongoing operations in a manner that is not significantly detrimental to the business." As an example, the SBA pointed to public companies, noting "it is unlikely that a public company with substantial market value and access to capital markets will be able to make the required certification in good faith." SBA FAQ No. 31.

45 The Act, § 342.

46 *Id*. § 312(b).

47 *See* FAQ No. 31; Borrower Application Form, SBA Form 2483 (June 24, 2020). Though subject to further rules or guidance to be issued by the SBA, Section 312(b) of the Act allows for a borrower that returned the entire amount of its loan to reapply for a covered loan.

48 The Act, § 312(c).

49 *Id*. § 312(a)(2).

50 *Id.*

51 *Id*. § 307(a)(3).

ENDNOTES (CONTINUED)

52 *Id*.

53 *Id*.

54 *Id.* § 311(a).

55 *Id*.

56 For example, the FAQs note that, when reviewing loan applications, “[l]enders are expected to perform a good faith review, in a reasonable time, of the borrower’s calculations and supporting documents concerning average monthly payroll cost.” FAQ No. 1. The CARES Act had included a robust hold harmless provision, providing that “[i]f a lender has received the documentation required . . . from an eligible recipient attesting that the eligible recipient has accurately verified [certain] payments,” “an enforcement action may not be taken against the lender . . . relating to loan forgiveness for th[ose] payments” and that “the lender shall not be subject to any penalties by the [SBA] relating to loan forgiveness for th[ose] payments.” The CARES Act, § 1106(h).

57 The Act, § 305(a). It is unclear whether, under the terms of the Act, each document must be submitted pursuant to all applicable requirements and include an attestation, or whether a document submitted as part of a borrower’s complete application would satisfy this standard.

58 *Id*.

59 The CARES Act, § 1106(h).

60 The Act, § 320(a). The SBA had previously prohibited borrowers from being “presently involved in any bankruptcy.” *See* SBA Form 2483; 85 Fed. Reg. 23451 (Apr. 28, 2020).

61 The Act, § 320(f)(1).

62 *Id.* § 320(f)(2).

63 The CARES Act, § 1110(e)(6).

64 The Act, § 333(c).

65 *Id*. § 333(e).

66 *Id*. § 323(d)(1)(D).

67 *Id*. § 340(b)(1).

68 85 Fed. Reg. 20816 (Apr. 15, 2020).

69 The Act, § 340(b)(1).

70 12 U.S.C. § 1463 note (a).

71 The Act, §§ 520, 522.

72 *Id*. § 522.

73 *Id.*

74 *Id.* Institutions that are either (1) designated as being in “Troubled Condition” by the appropriate federal banking agency or the NCUA, as applicable, or (2) subject to a formal enforcement action from its primary federal regulator that addresses unsafe or unsound lending practices will be ineligible to participate in the Emergency Capital Investment Program. *Id.*

75 *Id*.

76 The requirements that an insured depository institution must not be controlled by “a bank holding company or savings and loan holding company that is also an eligible institution” may be aimed at preventing a corporate parent and subsidiary from both being considered an “eligible entity.”

77 The Act, § 522. Under Section 103 of the Community Development Banking and Financial Institutions Act of 1994, a “community development financial institution” is generally defined as a person that: (1) has a primary mission of promoting community development; (2) serves an

investment area or targeted population; (3) provides development services in conjunction with equity investments or loans, directly or through a subsidiary or affiliate; (4) maintains, through representation on its governing board or otherwise, accountability to residents of its investment area or targeted population; and (5) is not an agency or instrumentality of the United States or any State or political subdivision of a State. 12 U.S.C. 4702.

78 Under Section 308 of FIRREA, "MDI" means any depository institution that: (1) if privately owned, is 51% owned by one or more socially and economically disadvantaged individuals; (2) if publicly owned, 51% of the stock is owned by one or more socially and economically disadvantaged individuals; and (3) in the case of a mutual institution where the majority of the board of directors, account holders, and the community which it services is predominately minority. "Minority" for these purposes means any black American, Native American, Hispanic American, or Asian American. 12 U.S.C. § 1463 note (b)(2).

79 The Act, § 522.

80 *Id.*

81 *Id.*

82 *Id.* § 523.

83 *Id*. § 523(a)(1).

84 *Id*. § 523(a)(1)(B).

85 *Id*. § 523(a)(2).

86 *Id*. § 523(a)(2)(C).

87 *Id.*

88 For further information on TDR relief under CESA, *see* our Client Memorandum, "*Sweeping Stimulus Legislation Authorizes $500 Billion to Support Distressed Sectors of the Economy, Temporary Suspension or Modification of Certain Banking Provisions and Nearly $350 Billion to Support Small Businesses Through a Temporary Paycheck Protection Program in Response to the Coronavirus Outbreak*," dated March 29, 2020, *available at* https://www.sullcrom.com/sandc-publication-coronavirus-aid-relief-and-economic-security-act.

89 The Act, § 541.

90 For further information on the rules regarding the implementation of CECL, *see* our Client Memoranda, "*Bank Capital Requirements*: *Federal Banking Agencies Release Final Rule Regarding the Implementation of CECL, and Federal Reserve Provides Guidance on CECL and CCAR*," dated December 27, 2018, *available at* https://www.sullcrom.com/cecl-final-rule-on-phase-in-and-frb-guidance-on-cecl-and-ccar, and "*Client Alert*: *FASB Expected Credit Loss Methodology*," dated June 23, 2016, *available at* https://www.sullcrom.com/client-alert-fasb-expected-credit-loss-methodology.

91 For SEC filers, other than smaller reporting companies and emerging growth companies that use the extended transition period for complying with any new or revised financial accounting standards, CECL applies from the first fiscal year beginning after December 15, 2019, including interim periods within that fiscal year.

ENDNOTES (CONTINUED)

92 On March 27, 2020, the federal banking agencies issued an interim final rule providing eligible banking organizations that adopt CECL during 2020 the "option to delay for two years the estimated impact of CECL on regulatory capital, followed by a three-year transition period to phase out the aggregate amount of the capital benefit provided during the initial two-year delay (i.e., a five-year transition, in total)." The interim final rule seeks to delay the effect on regulatory capital of an estimated amount of the increase in the allowance for credit loss attributable to CECL, relative to the incurred loss methodology. Specifically, the interim final rule uses a 25% scaling factor to approximate the average after-tax provision for credit losses attributable to CECL, relative to the incurred loss methodology. Accordingly, an electing banking organization will use transitional amounts that reflect 100% of the "day one" impact of adopting CECL plus the quarterly changes that result from CECL, as measured using the scaling factor. *See* Joint Release, "*Regulatory Capital Rule: Revised Transition of the Current Expected Credit Losses Methodology for Allowances*," dated March 27, 2020, *available at* https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20200327a2.pdf. The agencies subsequently provided guidance on the interaction of the interim final rule and the optional deferral of CECL provided by CESA, and adopted a final rule, consistent with the interim final rule, in August 2020.

93 The Act, § 540.

94 *Id*. § 540(b).

95 *Id*. § 1003(a)(1).

96 *Id*. § 1003(a)(2).

97 *Id*. § 1005. The Act also sets the amount allocated to such programs to $0 on January 9, 2021. *Id.* § 1003(b)(1).

98 12 U.S.C. § 343(b)(3).

99 Section 4003(b)(4) of the CARES Act relates to loans, loan guarantees, and investments in programs or facilities established by the Federal Reserve for the purpose of providing liquidity to the financial system. This section does not capture: (1) loans and loan guarantees for passenger air carriers, certain eligible businesses approved to perform inspection, repair, replacement, or overhaul services, and ticket agents; (2) loans and guarantees to cargo air carriers; or (3) loans and guarantees for businesses critical to maintaining national security. 12 U.S.C. § 343(b)(1)-(3).

100 *Id.* § 1005.

101 *Id.*

102 *Id.* § 278.

103 *Id*. § 272.

104 Title II, Chapter 1, Subchapter I of the Act.

105 The Act, § 323(d)(1)(H).

106 *See id*. § 325.

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