



About the Firm

Shapiro Sher was founded in 1972 with the mission of providing outstanding legal counsel for businesses of all sizes. Based in Baltimore, the Firm is nationally recognized for its practices in business law, litigation, bankruptcy, banking, and creditors' rights.

Shapiro Sher's banking lawyers provide experienced counsel in connection with all aspects of commercial loans. Chaired by **Scott Foley**, the firm's **Banking & Financial Services Group** regularly represents regional and community banks, credit unions, finance companies, and other financial institutions in the Mid-Atlantic and in transactions throughout the country.

The banking group includes partner **Pat Gill**, who represents financial institutions in connection with re-documenting troubled loans and structuring, negotiating, documenting, and closing commercial finance transactions. Attorneys in the group also advise financial institutions regarding under-performing and distressed loans. The group routinely handles loan modifications, workouts, restructurings, short and long-term forbearance agreements, and bankruptcy litigation. Because the group has extensive experience in the origination of loans and in workout situations, it is prepared to provide efficient representation at every stage in the lending process.

With decades of experience in the banking industry, Mr. Foley and the firm's other seasoned banking attorneys appreciate the potential hazards facing clients in the commercial loan process, and strive to protect lenders' interests throughout the lifecycle of the loan.

THE PAYCHECK PROTECTION PROGRAM: UNINTENDED RISKS FOR LENDERS

By Scott W. Foley, Pat Gill, and Wes Parker

Launched April 3, 2020, the Small Business Administration's (SBA) Paycheck Protection Program (PPP) enacted under the CARES Act provides favorable and potentially forgivable loans to eligible small businesses affected by the Covid-19 pandemic. While the PPP has been designed to provide much-needed financial relief to small businesses throughout the country, it does expose their lenders to certain risks.

The SBA provided its interpretation of the PPP under its interim final rules (Rules) issued on April 2. Subsequently, the SBA in consultation with the Department of Treasury (Treasury) provided further guidance concerning the PPP by way of its Frequently Asked Questions (FAQs) originally issued on April 7, which are being updated on an ongoing basis. As participating financial institutions continue to process PPP loan approvals while simultaneously addressing an unprecedented number of requests for loan deferrals under existing credit facilities, lenders should be mindful of certain pitfalls associated with navigating the PPP and its evolving rollout. To help mitigate the risks, lenders should be cognizant of the obligations imposed on them by the program and implement sound procedures to ensure compliance with the PPP loan process, including the not-too-distant loan forgiveness process.

Loan Forgiveness, Generally

Although there is minimal guidance to date on the loan forgiveness process, in less than eight short weeks after closing a PPP loan, a lender should be prepared to process loan forgiveness applications. Loan forgiveness is available to borrowers under PPP loans for amounts incurred and payments made during the eight week period following the first disbursement of loan proceeds (Covered Period) on certain (i) payroll costs, (ii) interest payments on mortgages incurred before February 15, 2020, (iii) rent payments on leases in effect before February 15, 2020, and (iv) utility payments for which service began before February 15, 2020; provided however, not more than 25% of the loan forgiveness amount may be attributable to non-payroll costs. Also, certain reductions may apply to the loan forgiveness amount as a result of changes to a borrower's number of employees or reduction in employee wages.

The originating lender will be responsible for collecting the necessary loan forgiveness documentation and applications from its borrowers and issuing a decision on the applications for forgiveness within sixty (60) days



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of receiving such application. However, even before the borrower submits its application for loan forgiveness, the lender may request that the SBA purchase the expected forgiveness amount as early as week seven of the Covered Period. Such requests should take the form of an application to the SBA for the expected forgiveness amount of the PPP loan or a pool of PPP loans and shall include:

- The PPP Application Form (SBA Form 2483) and any supporting documentation submitted therewith;
- The PPP Lender's Application for 7(a) Guaranty (SBA Form 2484) and any supporting documentation;
- A detailed narrative explaining the assumptions used in determining the expected forgiveness amount, the basis for those assumptions, alternative assumptions considered, and why alternative assumptions were not used;
- Any information obtained from the borrower since the loan was disbursed that the lender used to determine the expected forgiveness amount, which should include payroll tax filings, cancelled checks, and other payment documentation; and
- Any additional information the Administrator of the SBA may require to determine if the expected forgiveness amount is reasonable.

As the SBA continues to focus on getting approved PPP loans in the hands of eligible small businesses, lenders anxiously await additional guidance on the loan forgiveness process that the Rules state will be forthcoming. Given that participating lenders will be tasked with quickly shifting from originating the PPP loans to processing loan forgiveness applications, lenders should actively monitor the SBA's continuing guidance and be prepared to implement mechanisms to process loan forgiveness requests.

Mitigating Risks and Liability

In light of the mass PPP loan approvals and loan forgiveness decisions to be made by participating lenders on an expedited basis under the evolving PPP, the SBA attempted to provide certain assurances to lenders. The Rules provide that "[l]enders must comply with the applicable lender obligations set forth in this interim final rule, but will be held harmless for borrowers' failure to comply with program criteria." Similarly, subject to further guidance, it appears that a lender is entitled to rely upon the documentation submitted by the borrower in connection with loan forgiveness and is not required to conduct any verification thereof if the borrower submits documentation supporting its request for loan forgiveness and attests that it has accurately verified the payments for eligible costs.¹ Accordingly, when processing the requests for loan

¹ With respect to a lender's reliance upon the borrower's forgiveness application and attestation, the Rules specifically state "[t]he Administrator [of the SBA] will hold harmless any lender that relies on such borrower documents and attestation from a borrower. The Administrator [of the SBA], in consultation with the Secretary [of Treasury], has determined that lender reliance on a borrower's required documents and attestation is necessary and appropriate in light of section 1106(h) of the [CARES] Act, which prohibits the Administrator [of the SBA] from taking an enforcement action or imposing penalties if the lender has received a borrower attestation."



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forgiveness, the lender should ensure that the borrower submits a complete application with the required supporting documentation and certification.

While the Rules should provide lenders with some comfort that they may not be subject to enforcement action or the imposition of penalties by the SBA, such assurances obviously do not extend to potential claims from applicants or borrowers arising out of the participating lenders' involvement in the PPP. As a result, to further minimize risks during the life-cycle of the PPP loan process, lenders should consider incorporating additional PPP related procedures, including the following:

- Continued training of commercial lenders on communicating with applicants and borrowers during the PPP loan process;
- Fine-tuning the underwriting process if the program receives additional substantial funding;²
- Incorporating protective provisions in the PPP loan documents, including certain borrower representations, acknowledgements and indemnifications in favor of the lender;
- Documenting and preserving the actions taken by the lender, including acceptance or denial of an application; and
- Preserving communications with and documentation submitted by applicants and borrowers.

Due to the novelty of the PPP and the rapidly developing implementation thereof, participating lenders should balance their need to quickly process PPP loans and loan forgiveness requests in accordance with the criteria set forth in the Rules and related guidance, while still ensuring that they are aptly mitigating post-closing risks.

In response to inquiries during these challenging times, Shapiro Sher's Banking and Financial Services Group is monitoring the developing programs and policies affecting lenders and/or their borrowers under the PPP and the CARES Act. For more information about this or other banking law matters, please do not hesitate to contact any of the attorneys in our Banking and Financial Services Group.

Shapiro Sher provides this information as a service to clients and others for educational purposes only. It should not be construed or relied on as legal advice or to create an attorney-client relationship. Readers should not act upon this information without seeking advice from counsel.

² Although the Rules afford the lender certain protections by holding it harmless for the borrower's failure to comply with the PPP and by allowing the lender to rely upon the information and certifications submitted by the borrower with its application, the lender is nevertheless expected to satisfy certain underwriting obligations and perform a "good faith review," in a reasonable time, of the application. By way of example, the FAQs indicate that such a review of the borrower's submitted dollar amount of average monthly payroll costs would be satisfied by a "minimal review of calculations based on a payroll report by a recognized third-party payroll processor." If, however, the lender identifies errors or a material lack of substantiation in the borrower's application, the lender should work with the applicant to correct the problems. Despite the understandable inclination to assist borrowers in these uncertain times (especially existing customers), lenders should take caution to avoid the appearance of being the borrower's advisor while processing the application, including with respect to the borrower's completion of the application, so as to ensure that all information contained in the application and submitted in connection therewith is the borrower's work product.