



The National Voice of the State Credit Union System

**NASCUS L&R Committee Special Call
CARES Act and SBA's Payment Protection Program
Q&A with Venable LLP**

Friday, April 10, 2020

Transcript

Neither the April 10, 2020 NASCUS Legislative and Regulatory Affairs Committee conference call, nor this transcript of the call, represent legal advice. No opinions expressed in this transcript are official regulatory interpretations of any state or federal regulatory agency. For formal answers to any questions related to the COVID-19 response, reader should individually consult qualified legal counsel.

The transcript has been edited for brevity and clarity.

Bright Knight - Welcome to this special Legislative & Regulatory Affairs Committee call. A couple of administrative items before we get started. If everyone could mute their phone lines. I want to make sure everyone can hear the information that we will have today. Thank you to everyone who has sent us questions, we have sent those along. Please continue to send us your questions during and after the call.

We are recording this call for members who are unable to make the call. For those of you in states who require consent before you participate in this type of call, your continued participation in this call will be taken as consent. So, everyone please be aware that we will be recording the call for future playback for other members.

Disclaimer: There are a lot of legal compliance, regulatory interpretive questions that were sent. And there are a lot of legal and interpretive issues to be discussed today. NASCUS is providing this call as a service to our members, to help you begin to understand the complexities, the conflicting information that is out there. We are, however, not presenting legal advice. We do not speak for any specific regulatory agency, state or federal, in terms of regulatory forbearance. I think when we get started with our guests from Venable, they'll probably talk with you a little bit about the conditions around their remarks. But just so everyone understands, this is informational. It is not formal, legal or regulatory advice. With that, we are going to move forward.

We are very fortunate to have with us on the phone this afternoon representatives from the Venable law firm. Venable is one of the firms that NASCUS works with from time to time. We've talked with Venable around issues like marijuana banking, BSA, other issues impacting the credit union system. And we were having conversations with our guests today, last week, about the CARES Act, the stimulus package, the PPP, and that began a conversation that culminated in an opportunity today, where they were gracious enough to say that they are going to participate in, what might be a series of conference calls to answer questions around these issues as we move through the pandemic planning.

We have with us two partners from the DC office, Laura Biddle and Ed Wilson. All of the questions you've sent to us, we've sent to them. I think what we'll hear on this call are definitive answers to some questions. We're going to hear in some areas where there is no firm answer yet. But I think everything we hear today is going to help us further navigate this issue. With that, a reminder to put our phones on mute. And thank you again, Laura and Ed, for making yourself available to our members.

Laura Biddle – Welcome all. Thank you all for joining, Welcome to the madness that is PPP. We're a week in now, and it is a fast-moving train, and it continues to evolve and change. We have a whole task force at Venable dealing with these issues every day. So, hopefully, we can be useful. We thought we'd start with just a summary of the PPP, to level set. Talk about where we stand now with Congress, what the next steps are and the recent Federal Reserve's liquidity facility, related to the PPP, and then jump right into your questions. Hopefully, we can get into as many of those as possible in the next hour.

Ed Wilson – Hello. This is Ed Wilson. I think you can tell the difference in our voices. I'd like to start by giving a disclaimer similar to NASCUS'. We are here for informational purposes. We can't pretend to know all the actual issues that go into these great questions we've gotten. My job is to set the table a little bit, to give you a background, to level set as Laura said. And then to turn quickly into your questions. Because we figure that's probably the best use of our time.

Let's start with the PPP, a summary of the Payroll Protection Program:

It's defined for small businesses. And this will answer some of the questions along the way. There are some waiver exceptions in the act that talk about employers having no more than 500 employees, but that does not exclude all the other small businesses that qualify under the different NAICS codes that can have many more employees than 500, depending upon the type of small business, both in terms of asset size and employee size. That depends very much on the business. So, if you have a specific question there, the way to go there is to go to the SBA guidance or to consult with your local counsel.

So, who qualifies? Anyone who either meets the standards under Part 1 of the CARES Act. And we'll refer to two parts of the CARES Act. Part 1 and Part 4. Part 4 is the SBA Fed Reserve programs. Section 1, Part 1 is the Small Business Act programs. Who qualifies? Small businesses. Those that are defined under Section 7(a). There are consumer lending programs under the Small Business Act; those that fit under the 500 and fewer. Why was that done? It was clearly done to maximize the number of employees who could receive aid. I think Congress faced a choice: It could either throw everyone into unemployment or it could say we want small businesses to keep their employees. We'll pay the small businesses to pay the employees. And that led to some really interesting discussions, which are going on to this day because there's going to be a new bill. And how do you change it? One of the major changes was for all the hospitality industry folks to say, if you have multiple places, multiple outlets, franchises, that have under 500 employees, per location, each one may apply. Again, maximizes the amount of funds going directly to employees. There was some initial confusion on foreign ownership. Foreign owners need not apply was the original word from the original lender's document and borrower's documents put out by the SBA. That was changed to say are your employees in the U.S., basically? And that goes back to the initial purpose which was to get money into employees' hands. I think the Administration was very worried they were going to get slammed by giving money to foreign companies, until somebody, somebodies, convinced them no, the money is not going to a foreign company, it's going to the U.S. employees, so they changed it. Also, for the first time, it allowed nonprofits into the SBA loan program. As a result our firm, which really represents more nonprofits than almost any law firm in the country had a lot of rounds pegs in square hole, as we looked at the SBA forms.

So where do we stand now? Current funding of loans. Let's talk macro first and then micro. Macro: \$350B, about \$150B has been committed. I don't pretend to say \$150B has been disbursed because it hasn't. We have calls every night at 9 and twice during the week in the mornings, and we're hearing just dribs and drabs of our clients being funded. So, we understand this is a big thing to swallow and get to working correctly. So that's both macro and micro.

So what's going to happen next? I was reading the paper yesterday, the Senate majority leader tried to push a very short bill yesterday, just to increase the amount of money in this program by another \$250B. The Democrats in the House said that will never pass here. We have other things—not talking the politics, those are just the facts. We have a very substantial regulatory practice and the people in the practice are getting calls, routinely. For example, I was on a call this morning with Sarah Donovan, one of our good legislative folks. Sarah had gotten calls from her two friends on Hill and asked what should be in the new bill. So, they are actively reaching out saying how do we make this work to make sure our economy can get back to life once this is over. How do we keep our employees/citizens with having enough money?

And with that as background, I want to turn this back to Laura who has a whole host of questions. Laura took all the questions that Brian gave us. Some of these, you should know, we read and said we don't have a clue, so we said we'd have another part to this call next Wednesday, for the ones we can't get to.

Laura Biddle:

We put [the questions] in categories. We have:

- Borrower Eligibility
- Lender Eligibility
- Loan Terms and Process
- Documentation
- Forgiveness
- Guarantee
- Miscellaneous COVID-related

BORROWER ELIGIBILITY

Question (Laura): All the guidance discusses small businesses having less than 500 employees. Can't some businesses with 500+ employees qualify for PPP?

Answer (Ed): This is a question I tried to answer in the introduction. There are two segments to this—there's the CARES Act that has 500 employees or less and then there's the traditional SBA—what is a small business. And that depends on what the line of business is, what its assets are, who owns it. There's something called the affiliation rules. Affiliation rules which apply at most places. For e.g., someone told me they have 400 employees in Orlando FL. I asked who owns you? They said we're owned by a French company. I asked how many employees does that have? They said we have 7,000. I said, well, I think we have a problem because those 7,000 employees in a company that is publicly traded in France are going to be imputed to this small entity owner in Orlando, so it will not qualify. So, there are two segments to this: If this company had been a stand-alone business, *in its line of business* in Orlando, it could have had 1,200 employees and qualify. [Traditional definition of U.S. small business] is not limited to 500.

Question (Laura): Seasonal businesses—how do these businesses calculate payroll, as solely owned enterprises, where do contractors fit in?

Answer (Ed): Seasonal business are calculated over a 12-month period, unfortunately. So it really does lower it. And we're trying to get some relief from that in the next bill, but I'm not sure it's going to happen. Wholly-owned enterprises--you're on the same 12-month calculation. Where do contractors fit in? By and large, they don't. We've had a few companies call us and ask us can they include their service

workers who wouldn't ordinarily be part of their workforce, if they hadn't contracted out that function? And unfortunately, independent contractors have to apply for PPP loans in their own capacity.

Question (Ed): May Board members apply for loans from their own institutions in their personal capacity as a business owner? Does Treasury, SBA plan to allow more flexibility in their guidelines. That's really two questions.

Answer to the first question. I had a call from a bank client that called me yesterday, with a string of emails from three of their peer banks. All of them have, apparently, had directors, who, with their own businesses, have applied for the PPP at the banks where they sit on the board and they weren't flagged until actually it was approved. The answer: A lot of them were looking to Reg O (Insiders), and the loan was perfectly in compliance with Reg O. But what does that mean the PPP? The PPP is part of the 7(a) program so the 7(a) program, overall, will apply and there's a provision in the SBA regulation, applying to all 7(a) loans, that prohibits conflicts of interest and requires that when a conflict is identified that the lender (the CU) notify the SBA ASAP. So, the client is contacting their local SBA office to provide notice. They haven't funded yet and are trying to get some clarity on how they can unwind this, as we speak.

2nd part of Q is on whether there are plans to provide more flexibility.

Ed: Regarding borrower guidelines, let me give you a real example from the franchise world. Under the new qualifying companies that are 500 or less employees, in any one place, that are considered franchises on the SBA list. Well, there are franchises and franchises. If a franchisee pays all of its own employees directly, clearly it qualifies. The franchisor pays employees at the corporate level, then is reimbursed by the franchisee through its franchise payments. Those are the sorts of questions the SBA is getting and sorting out. Can SBA call it on its own or does it need to go back for legislative relief? So we're seeing changes and no one knows where it's going to come out yet.

Question (Laura): Regarding eligible borrower, I've heard conflicting opinions on which types of nonprofits are eligible. Specifically, some of the written information provided by SBA suggests that any entity that can provide satisfactory evidence from the state that the nonrevenue producing organization or entity is a non-profit, one organized and practicing under state law is an eligible borrower. How broadly can we reasonably interpret that? Is a town or municipality organized under state law eligible? How about a library or HOA homeowners' association?

Answer (Ed): I have been involved in this through my church. What the SBA and lender should be looking for is a federal tax-exempt letter--something in stated declaration or affirmation or copy of IRS letter that says, "Yes I am nonprofit--a 501(c)(3). But I wouldn't get into "Is a town or municipality, under state law, eligible?" They are eligible for different things. This really goes to nonprofit corporations formed under, with a tax-exempt status, 501(c)(3).

Question (Ed): Can certain criminal violations render a borrower ineligible? Is the lender expected to verify certain criminal history or can we rely upon representations of the borrower?

Answer (Laura): No, you are not expected to verify criminal history. To do that you'd have to run a background check within the time period provided. There's not enough time and you also have the certification of the borrower on which you're permitted to rely. That said, if there's something very obvious, like you know that this person has a criminal record, then that would give you reason to not rely on it (the borrower's certification) and you would not process it that way (as reliable).

Answer (Ed): Laura and I discussed what can we rely on, as lenders? How careful do we have to be? I want to give you a little comfort on that. And this is for those who have pulled down the regulatory

capital rule, paycheck protection program lending facility, that was published in the Federal Register, the day before yesterday, on page 7 of 31. I am going to quote it: "The SBA reimburses PPP lenders for any amount of a covered loan that is forgiven. PPP lenders are not held liable for any representations made by PPP borrowers, in connections with the borrower's request for PPP covered loan forgiveness." That is a theme that comes up over and over again. The SBA is looking for you to exercise good judgment. Yes, they see lenders as the front line of defense, but they also know that his is moving very fast. As Laura said, as long as you are exercising good judgment. As long as someone doesn't come in who you know has been arrested 20 times and says, "I don't have a criminal record." Except for something like that where you're being willfully blind or very negligent, we don't see this as an issue.

Question (Laura): We are encountering some members' borrowers operate different, unrelated businesses in separate corporate entities. I.e., restaurants in one entity and one carpet cleaning as another line of business. Both entities are entirely owned by husband and wife. Are both entities permitted to apply for a PPP loan?

Answer (Laura): Yes. The point is really to get money to the employees of these individual businesses, not to be concerned with husband-wife control of multiple companies.

Answer (Ed): If you go to the Venable website, you'll see a client alert "Afflicted by Affiliations," which explains the affiliation rules by the SBA. In this game, the question is posed: The restaurant is one entity under the SBA and the carpet cleaning business is another. But for the small business rules, they're combined. So do we have an issue here? This is exactly why we gave a disclaimer at the beginning. We don't know how large the restaurant is, how the cleaning business is. We're assuming each one qualifies as a small business and that together they would still qualify under the various rules--under the size, the capital assets test, they'd be okay. This is why we say we're giving informational advice and not legal advice.

Question (Ed): Small CU asked me if they can take payroll deferment talked about in the CARES Act. Someone thinks the CU can since it just defers some social security payments until 2021 and 2022.

Answer (Ed): I'm not sure that's correct, that's a different act that does that. They think they can address what credit unions as an employer can and can't take advantage of. They have less than 500 employees. And even in this issue, it doesn't matter how many employees. But I'm not confident in that statement. Let's take out the social security payments. Let's take the payroll protection loan here. Any small business can apply. So, if the question is can a credit union apply, the answer is yes. And what do we do with that becomes a factual issue, and we'd rather talk to somebody specifically about it. We got a little confused. *[Editorial Clarification: Federally-insured credit unions are eligible to apply as PPP lenders but not as PPP borrowers. As employers, credit unions are eligible for another program under Section 2302 of the CARES Act that allows employers to defer the deposit and payment of the employer's share of social security taxes.]*

LENDER ELIGIBILITY

Question (Laura): Must a credit union be a registered SBA lender to offer the PPP?

Answer (Laura): If you're already a registered SBA lender, you automatically are permitted to make PPP loans. If you're not a registered as a 7(a) lender, you can submit online their lender agreement and then once that's received, you're eligible to make the loan. It's the [non-SBA] lenders that they recently released standards for, and [non-SBA lenders] actually have to be approved ahead of time before they can start lending. So just go online, the form is there, submit it through the portal and you're good to go.

LOAN TERMS & PROCESS

Q: Concerning the expected payment terms of PPP loans, after the initial 6-month deferral period, there is inconsistency among those opining on the topic. Some in the legal and CU communities are of the opinion that it is up to the lender to determine a specific payment schedule, with the lender having the power to grant several options including but not limited to (a) interest only until maturity; (b) P & I fully amortized over the remaining 18 months until maturity; or (c) a balloon payment at maturity. Others are of the opinion that the required payment terms are to amortize the principal and accrued interest over 18 months commencing at the end of the 6-month deferral period until maturity. Any comment that could be provided on that point would be helpful.

Answer 1 (Laura): This is another area where we have to look at the general SBA 7(a) regulations. The PPP provides for the maturity date, and then the deferral and the interest rate, but not necessarily the repayment terms. And that's something that's done by the credit union, itself, within the parameters of the larger SBA 7(a) program.

Answer 2 (Ed): I'm hoping we'll get better guidance on this yet, because where we've landed on this so far is that while no payments are due for 6 months, following the disbursement (so that begins the 6 month period) and that's the complete disbursement, not the partial (we think, but we're not sure), interest will continue to accrue during that period for the 6 months. There's no penalty we can find for pre-payment. But after that I would look at the current SBA rules, and that gives you a lot of flexibility. Then, let's keep an eye out for guidance because we're finding a lot of the questions are going back to SBA and we're a feeder of questions to the SBA, and I'm sure we're not the only ones, and we're all trying to characterize what we know and what we don't know.

Question. The loan payments are deferred for 6 months. Does the 24-month amortization begin after the 6-month period or is it an 18-month re-payment loan? This would presume some portion of the loan isn't forgiven.

Answer (Laura): The term alone is 24 months, or 2 years, with a 6-month deferral. During that time it accrues interest. As Ed was saying, this is an area where no guidance has been given, but that's the logical way to read that and to argue.

Answer (Ed): The disbursal of the approved funds should occur no later than 5 days after approval. However, the funds that are disbursed periodically, when is the last timeframe for distribution to the borrower? If you're a lender, on this side of the question, I'm going to say it should occur no later than 5 days after approval. But, we've been finding in the last two weeks that reality gets in the way of legislative requirements, so it doesn't always happen in legislative timeframe or in the SBA's timeframe. On the periodic distribution of funds, if they're going to be disbursed periodically, we need to keep in mind what the reason for this loan is. These loans stand in the place of unemployment insurance payments, so if you're doing it periodically, then you might want to be doing it within a borrower's payroll requirements.

Question: What's the last timeframe for distribution to a borrower?

Answer: Depends on how you characterize the loan, but to me, this is supposed to be a real short-term hit, so it should be more than a couple of months. But we haven't seen anything that says everything has to be disbursed by X day. [Editorial Clarification: SBA interim final rule says last disbursement must be made within 2 months.]

Question (Laura): Will the SBA consider revising its 5-day loan disbursement requirements? There is a lack of clarity about the disbursement of PPP loans, and there's concern that a 5-day window may be too short of a window with processing demands. Perhaps, as soon as the loan becomes available?

Answer (Laura): Not a lot of clarity on this and we have to consider the intense volume of loans that are going through the system. We hope SBA will be thinking of this, but for now, we don't have clarity.

Question (Laura): What it means that the PPP loan has to be partially funded in 5 days and wholly funded in 2 weeks? I'm not sure I'm prepared to answer the question.

Question (Ed): The next one is similar: Will the repayment remain 2 years on the unforgiven portion of the loan balance or will the remaining loan amount be amortized during over a longer time period.

Answer: It's a 2-year loan, unless there are some changes in it, that's where we are at the current time, but we're monitoring it like everyone else.

Question: Have the closing requirements for the SBA loans been extended to 10 days?

Answer (Ed): Everyone I know is trying to do, both lending and borrower side, are trying to do things quickly and in good faith. No time limits have been extended formally, but reality is getting in the way of legal requirements, just because of the facts of life. So, that's the best answer we have for that, unless we see something in the next few days that says it. I don't know why we would see formal extensions.

Clarification: (Bill Buchanan, Delta Community Credit Union.) The FAQs that were updated on April 8th, Question #20, the last sentence on the last page did, in fact, increase the disbursement period to 10 days.

Ed: You're right, Bill. You've got that right. I appreciate the correction, Bill. I think that's a good example of there's so much information coming out that we can't always keep it together.

Question. (Ed) The CU started uploading PPP loans on the SBA portal last Friday. The following Tuesday they were told they had to be funded in 5 days, which was extended to 10. Is the 10-day funding requirement for all approved PPP loans or just the ones approved?
[Ed asks Bill to answer since he has FAQs in front of him].

Bill Buchanan: It is 10 days regardless of whenever you received the approval.

Ed: Thank you for your help. Greatly appreciate it. Don't mute your phone!

DOCUMENTATION

Question(Laura): Will a non-SBA note impact the availability of these loans in a secondary market?

Answer (Laura) No. Most of our FI's clients use their own note. So long as it meets the SBA requirements and doesn't include anything that would conflict with the PPP, there shouldn't be a problem there.

Question: *[Ed & Laura, decide to summarize a group of related questions.]* **What documents are required to satisfy it? Do we have to use SBA Note Form 147, which appears to be the same awful document used for 7(a) loans since 2002?**

Answer (Ed): I have to say that I'm stunned that you don't appreciate the great writing involved in Form 147. I'm being facetious. It's well known that that's why most of Laura's clients have developed their own forms.

Answer (Laura): Here's a summary of where we are: The PPP has certain requirements. The SBA produced its own note and put it on the site for the overall 7(a) program. As long as the loans and documentation meet those requirements, there's nothing new and different, with respect to documenting a PPP loan.

Question (Laura). **Does the SBA expect and/or prohibit lender from including commercially reasonable default language?**

Answer (Laura): That should not be a problem. You still have a loan, you still have indebtedness, and there's nothing in the PPP that would prohibit that. It also helps alleviate your risk.

Answer (Ed): We find very few people use the SBA loan form, and we see these are pretty much normal commercial terms in making sure that both what the SBA allows you to do and what SBA prohibits you from doing are both included.

FORGIVENESS

Question. *It appears in the act that the SBA is not required to purchase 100% of the PPP loan, if the borrower has failed to meet the purpose requirements set forth in the act which is obviously outside of the control of the lender. In such event, where does that leave the lender in the event the borrower is unable to pay the loan in accordance to its terms or at maturity?*

Answer (Laura): This one, and some of the others, are confusing or melding together the concept of forgiveness and guarantee. If the borrower fails to meet their purpose requirements, that will impact the borrower's forgiveness and [the loan] will not qualify for forgiveness. That doesn't impact the guarantee—as long as the lender has done everything according to the program. Has the lender done everything they're supposed to be doing? The lender is not responsible for the borrower's misdeeds with the funds.

Question: **I see the loan forgiveness as a potential source of significant dispute between lenders and borrowers, specifically in the event that forgiveness is partially or wholly denied to a borrower. The most likely and readily available outlet complaint will be the lender. In that regard what role and degree of responsibility is lender going to be expected to have in the process of applying for forgiveness?**

Answer (Laura): To be clear, the SBA will be giving the decision on forgiveness. The CU will file the report as set forth in the interim final rule. The specifics aren't out there on that yet of what it will look like. In the initial matter, you want to make sure there's a very good payroll record. You submit the forgiveness request and then the SBA makes the decision. I think there's more to come on that, and I hope we will be able to give more clarity on that next week.

Question (Laura): If the business fails in the 6 month deferral period, will the loan be forgiven or will the lender take the loss?

Answer (Laura): I think again that's confusing the two (forgiveness and guarantee). Assuming the lender did everything that was required of the lender, under the 7(a) rule and the PPP, the guarantee should not be impacted and presumably the loan would be forgiven, assuming the borrower did everything they were supposed to do and the SBA review the record to make the determination.

Answer (Ed): We found this question to be pretty interesting because it brings a couple of different issues into play. It says, "If the business fails..." Well, is the person asking the question assuming the business didn't do what it was supposed to do with the money? It did not use the money to pay its employees, and instead decided to take a long vacation to Grand Cayman? If the business fails, can the loan be forgiven? Well, that depends on other facts. The lender shouldn't take the loss because the loan is guaranteed. As Laura stated we have to be careful about confusing forgiveness versus guarantee, which leads us to the next question.

Question (Ed): What is the date to begin collecting documents from borrowers to support loan forgiveness?

Answer (Ed): Laura made a real good comment to me when we were discussing this. She said that date ought to be right now. There ought to be a good conversation at the time money is disbursed, you need to be collecting these documents right now. And they are your payroll records, in particular. Laura, anything to add?

Answer (Laura): No--we're still waiting for more guidance of what that's going to look like. And that's the next question in this line of forgiveness questions.

Question. (Ed) Loan forgiveness seems to be conditioned upon submission of a report. What's expected?

Answer: We assume the government is going to give us a form. And, it's not yet out.

GUARANTEE

Question. (Laura) Guarantee. The program specifies that the loans are 100% guaranteed as long as the lender complies with the PPP rules and requirements. Given that the guarantee is of critical importance for a loan that is unsecured and absent a personal guarantee, what is the degree of error/tolerance that can be expected before the SBA is impaired or denied?

Answer (Laura): You follow the requirements under the PPP. You get the required certifications from the borrower. Unless there's some source of willfulness, not validating, not doing your own calculation of the payroll amounts, or negligence in reviewing the applications, it's unlikely that the guarantee will be jeopardized.

Question (Laura): What do you see as potential areas where errors of the lenders couldn't negate the SBA guarantee?

Answer (Ed): These are normal sorts of major screw-ups. As I read earlier, out of the government's release on the second set of regulations: "PPP lenders are not held liable for misrepresentations made by PPP borrowers, in connection with the borrower's request PPP-covered loan forgiveness." What that's saying is unless it is completely false, unless you're passing through anything any reasonable person would know is not true, you are not going to be held responsible. I don't know what else I can say about that. I can't guarantee you won't ever be caught on something. But, our conversations with people on the Hill about the bill, as they were drafting it, is they're not looking to hold lenders liable. They're looking to get this money out quickly and have financial institutions use their normal good judgment. And that lead to a series of questions in this regard.

[Interruption due to someone shuffling papers.]

Question: Borrower fraud misrepresentation--when would the credit union be responsible for taking the loan loss?

Answer (Ed): I don't know how to answer that question because we could go on forever. We're all good thinkers and we are worried about making sure that our institutions are protected and that we get this right. When we'd talk to people on The Hill about question regarding lenders being worried about being held liable. The standard response was that Congress was not looking for lender liability. Congress was looking to get money quickly to employees and we're asking the lenders to just make good a faith effort to ask questions and make sure people aren't just being openly fraudulent. One example: If somebody comes to you and says that they own a small business and it sits right across from the financial institution's main office, and if you look out outside your front door and you ought to be able to see it and it's not there, well, that's something...

Question: In the event a lender miscalculates in determining the loan amount and the amount is funded in excess, what are the repercussions to the lender? I.e., Is just the excess amount not guaranteed or is the entire guarantee compromised?

Answer (Ed): I don't think we have specifics on this, but our thought is it is just the excess amount that is not guaranteed. But, again, lenders are expected to get the math right. So, if you ask us about where there's going to be focus on lenders, it's getting the math right. Laura, do you agree?

Answer (Laura): Yes, and it's one of the specific things the FAQs point out is they need to be checking the numbers. That's considered part of the review and it's part of your responsibility under the PPP.

MISCELLANEOUS COVID-RELATED

Question: (Ed) The lender has responsibility to pursue the collection prior to submitting the reimbursement request under an SBA guarantee. To what degree is a lender going to have to have collection responsibility for these loans as a condition precedent to seeking reimbursement under SBA guidance?

Answer (Ed): It's not [a condition precedent to collect]. If you go through the FAQs, you'll see that the loan is going to be forgiven if the borrower submits the right kind of information and the entire amount is guaranteed, just from the fact of making the loan. I had a little trouble understanding this question. I think there's something underlying to this question that I'm not getting.

Question (Ed): Loan underwriting. The program requirements specify that the lender may rely on the information without independent verification. However, there appears to be some gray area--potential pitfalls in the event the SBA later determines that the lender's reliance provided wasn't reasonable.

Answer (Ed): This goes back to what degree of tolerance. I can't draw you a bright line. And we all know, there's going to be some look-back issues after this is all over. But if you've made a good faith effort, we see that you're not going to be dinged for these things. That is where we are coming up. And that is where the FAQs are coming out.

Question (Ed): In the event the reimbursement request is denied, is the lender going to be provided any appeal process or any other recourse?

Answer (Laura): This is looking back at the same SBA's 7(a) process.

Question (Ed): If the loans are sold, will the servicing responsibility be with the lender or the borrower? If lender, what will be our servicing responsibility?

Answer (Laura): I'm not sure I know the answer to that. So, we'll put that off unless you have a thought on that, Ed.

Answer (Ed): We did have one thought on that, as a business matter. The Federal Reserve Board has come out with a new program to buy these loans. It's not going to do it directly. It will--like it did with the bond buying program where they contracted with Black Rock--it will have someone here. As a matter of good business, whoever ends up buying the loan will want to do the servicing. Otherwise, there will be a lot of credit unions and financial institutions around the country with servicing responsibility but without actual responsibility for the debt itself. So that's where we think it will come out, but we haven't seen it. We suspect it will come out in the regulations that come out, particularly in the comments.

Question: Who is responsible if a borrower is ineligible due to criminal convictions, too many employees?

Answer (Ed): If those facts are withheld from you, by the borrower, then you're not going to be [responsible]. That will be a borrower problem--not a lender problem. Same as if there is an impermissible use. We know there will be people who will misuse these funds, but we don't see that will be a lender issue, unless they're rubbing your nose in it.

The other thing we got questions on was the how does the PPP tie together, and we've touched on this with other SBA programs. But there are economic injury disaster loans, debt relief loans, and we can put those together, but they're covered well in the FAQs, so I'm not sure we want to burn a lot of time here.

The other thing we wanted to bring forth are the 6-month duration loan modifications. And this is a move by all the regulators to say if someone comes to you and their loan is current, you can give them a 6-month loan duration modification, and it does not count as a distressed loan restructuring. A lot of our financial institution clients are finding that they're looking at that and saying that that ought to be

helpful. Of course, they're worried that that's what the Feds and NCUA, OCC is saying now, but what are they going to say in 6 months? What we're saying here is that good documentation ought to control.

LIVE QUESTIONS & FOLLOW-UPS

Ed: While we're waiting for questions to come in, Laura and I just received one from our people who are monitoring what's going on in "COVID-4"--the 4th bill that will come out, is that the hotel and restaurant franchisors have asked that there be significant changes in how they're treated under the CARES Act, so that more of their folks can qualify for the PPP loans. They want them extended, they want them additional \$600B and they want businesses to be able to receive multiple PPP loans. Up to 3 is what they're suggesting. So, this is an example of the problems we're seeing with the bill. And they're also asking for changes in how the money is calculated, how the funds are calculated. To go back to the earlier question about someone who has seasonal employees. How do you do it? So, this is a moving target.

Question (Bill Mellin, NY Credit Union Association) – If we make a loan to an individual under the PPP, and that individual does not follow through and goes out of business, and doesn't use the funds at all to keep his people employed, what happens to the lender at that time? They go out of business and maybe they can't even be found. They're just gone.

Answer (Laura): So they go out of business and can obviously no longer make the payments. Forgiveness is not a route the lender will need to take. Assuming the lender met all the other requirements as an SBA lender, the lender should be able to apply for the guarantee.

Bill Mellin: Again, as the lender, I want to go through the 7- 8 week period, and I want to request that the SBA purchase the remaining balance of my loan, and clearly, I don't want to continue owning this loan. I want to sell it to the SBA, but I can't find my borrower.

Ed: Your loan is still guaranteed.

Bill: Do I still have a loan on my books or do I have the opportunity to sell that loan to the SBA at that time?

Laura: You sell it to the SBA, going through the normal SBA 7(a) guarantee process.

Bill: So I don't have to have cooperation from my borrower in order to do that transaction?

Laura: You need the borrower's cooperation for forgiveness, but not for the guarantee.

Ed: I would put into your loan agreement that you can sell it. Why not get rid of that problem right up front?

Ed: Thanks for giving us a chance to answer that question. Things will get more interesting because the Federal Reserve is putting up a program to buy these loans, to essentially give you more capital so there can be more loans.

Question from Bill Lynch (BECU) – I hear the discussion. Lenders are expected to get the math right. I infer that means they have to not only properly calculate the numbers they are required to calculate with the inputs given to them, assuming those inputs are correct. And they need to review any borrower calculations for which they have the inputs and can perform the review. Is that the full scope of what they need to get right?

Just trying to clarify. Is this all the lender has to do with regard to getting the math right: First, take the inputs that the borrower gave and perform whatever lender calculations they need to perform correctly for their loan approval process. Second, review any calculations that the borrower has made and performed already to see if the borrower did those calculations correctly. That is the full scope of what the lender needs to get the math right?

Ed: I am going to add another one to that: If the borrower comes to you with a category way out of line with other categories—numbers in one category that are way out of line with others, then I think a reasonable person would have expected you to notice that. And I mean way out of line. I don't think it is a big deal, but when people want to know if I am going to be liable, if you aren't at least giving these things a little bit of a look, you are going to get some push back.

Laura: I agree. And talking to my other financial institution clients, they are doing their own form of underwriting, just to protect themselves. So you can rely on what the borrower gives you, but, you have to use good business sense and judgment, and ask "Does it look remotely right?" And if it's not, send it back and ask for clarification.

Bill L: So, it's like a classic Liar Loan back in 2006 with a cleaning person who makes \$100,000 a year. When you talk about "categories," you mean there is no way this income could be made from this kind of business.

Bill L: So, a related question – a faceless employee that is who unbeknownst and the managers is in collusion with the borrower. The CARES Act has prohibitions on what can be paid to a broker, but what if your own employee is receiving some kickback. What is the standard for policing your own employees? Strict liability, negligence, gross liability, or gross negligence?

Ed: I'm not sure that standard changes under this Act.

Laura: I agree—I don't think it does [change the standard of policing your own employees. You have to look to your own policy and procedures and requirements and make sure you're in compliance with those. I don't think this creates any additional requirement.

WRAP-UP

Brian Knight: We're coming to the end. However, there were additional questions related to making all these loans. What happens to the BSA requirements? There were also other questions that go beyond the PPP, like the Treasury checks that are coming. And kinds of ACH questions--what happens if it comes to a closed account? Do garnishments apply? Ed, you touched on the Federal Reserve standing up its liquidity facility... These are the next round of questions that we'll try to catch you the next installment these calls which will be next Wednesday.

For those of you still on the phone, feel free to continue emailing questions in and we will feed them over to Venable. And then watch your email for a notice of Wednesday's Round 2 when we will address those questions beyond PPP and finish off the PPP questions that we didn't get to or that have come in since then.

So for everyone. Thank you for participating in today's call. Thank you to Laura Biddle and Ed Wilson of Venable LLP for taking these questions on the fly.

Call ended.