

## The CARES Act Paycheck Protection Program: Special Considerations For Not-for-Profit Organizations

By: Carl Koerner and Ryan J. Udell  
*Corporate and Securities Alert*  
4.2.20

The recently enacted multi-trillion dollar Cares Act has expanded Small Business Administration (SBA) business loans by creating a Paycheck Protection Loan Program (PPP), which offers forgivable loans to businesses impacted by the pandemic.

Historically, SBA business loans have only been available to small businesses which are operated for profit; the SBA regulations have excluded not-for-profit organizations (NFPs). Lobbying groups representing NFPs during the drafting of the legislation argued that NFPs were being equally hard hit by the pandemic and represented over 10% of the U.S. workforce. That effort led to the inclusion of NFPs in the definition of eligible borrowers under the PPP.

Eligibility is limited to 501(c)(3) entities and has not been extended to all of the other categories of NFPs, such as fraternal organizations, social clubs and business leagues. The SBA is expected to issue regulations regarding the PPP in the upcoming days (it has 15 days from enactment to issue the same), but in the interim since existing SBA business loan regulations that are not waived or amended by the Act never anticipated NFP applicants, there are several issues that arise when applying existing regulations to NFP borrowers which are highlighted below.

While these issues may preclude some NFPs from eligibility, so long as an NFP does not make any factually false statements, there does not appear to be any downside to applying under the PPP. There are no fees charged and, at worst, the application might be rejected. But it is just as likely that rules will be interpreted more favorably (or based on further SBA guidance not apply) to applicants because of the pressing need to maintain jobs and continue the payment of wages. If you are involved with an NFP, and you satisfy the basic eligibility requirement of less than 500 employees, before reading further, make sure your PPP application is underway.

### Religious Organizations

NFP advocates who participated in the legislative process have stated that their clear understanding is that the extension of the PPP to NFPs includes religious organizations. The SBA regulations exclude from eligibility "businesses principally engaged in teaching, instructing, counseling or indoctrinating religion or religious beliefs, whether in a religious or secular setting." SBA comments published in connection with the last significant rewriting of these regulations stated that the purpose of the regulation was to comport with constitutional requirements related to the Establishment Clause of the Constitution, which prohibits Congress from making a law "respecting an establishment of religion". Whether the SBA will waive that regulation, interpret it generously to borrowers or disregard it entirely is unclear.

### Affiliations

As noted, eligibility in the PPP is limited to entities with fewer than 500 employees. The SBA has permitted small businesses engaged in certain NAICS business activity classifications to exceed 500 employees. And the affiliation rule is waived for, among other limited areas, businesses engaged in the hospitality industry. But the NAICS codes typical for NFPs do not have higher employee limits. For purposes of determining number of employees, the NFP is aggregated with any other entities affiliated with it. The CARES Act specifically provides that SBA affiliation regulations under 13 CFR 121.103 shall also apply to NFPs.

Generally, affiliates are entities controlling, controlled by or under common control of each other. For business enterprises, control can be found based upon stock or other security ownership, board representation or contractual arrangements. But the regulations also permit a finding of control based upon affiliations of management where officers, managing members or partners control the management of more than one concern. Some NFPs are local establishments who have been organized under a charter or other arrangement with a national body. Will the powers that the national body can exercise over its local constituents be one that requires aggregation of all of the local organizations as affiliates? A similar analysis would apply to a religious institution that is part of a larger religious movement. The power of the movement to designate, approve or even remove clergy or other staff may lead to a finding of affiliation. The SBA has previously adopted regulations that recognize the independence of franchisees from their franchisor and other franchisees for purposes of the small business concern requirements. A similar approach would seem appropriate when considering NFPs that are part of larger umbrella organizations. Captive private foundations established by business enterprises or wealthy individuals who retain control would be expected to be aggregated.

## Criminal History

SBA regulations exclude from eligibility businesses with an officer, director or key employee who is incarcerated, on probation, on parole or has been indicted for a felony or a crime of moral turpitude. The application released by the SBA asks the following questions of applicants who are individuals and all "...20% or greater owners of the business..." with the caution that an affirmative answer to either will cause the loan to be rejected:

- Are you presently subject to an indictment, criminal information, arraignment, or other means by which formal criminal charges are brought in any jurisdiction, or presently incarcerated, on probation or parole?
- Within the last 7 years, for any felony or misdemeanor for a crime against a minor, have you: 1) been convicted; 2) pleaded guilty; 3) pleaded nolo contendere; 4) been placed on pretrial diversion; or 5) been placed on any form of parole or probation (including probation before judgment)?

There are many NFPs that have been formed expressly to assist individuals to avoid behaviors that can result in criminal prosecution or to rehabilitate individuals who have been convicted of crimes. Substance abuse programs are an obvious example. Oftentimes some of their most effective leaders are beneficiaries of the organization's programs. The measuring period according to the SBA regulations begins six months before the date of the loan application. The challenge will be to find a path that allows the NFP to answer these application questions truthfully, but without answering either in the affirmative which will result in immediate rejection by lending institutions and an SBA inundated with tens of thousands of applications and pressure to act on them.

If you have questions or would like more information, please contact Carl Koerner ([koernerbj@whiteandwilliams.com](mailto:koernerbj@whiteandwilliams.com); 212.631.4403) or another member of the Corporate and Securities Group.

As we continue to monitor the novel coronavirus (COVID-19), White and Williams lawyers are working collaboratively to stay current on developments and counsel clients through the various legal and business issues that may arise across a variety of sectors. Read all of the updates [here](#).

This correspondence should not be construed as legal advice or legal opinion on any specific facts or circumstances. The contents are intended for general informational purposes only and you are urged to consult a lawyer concerning your own situation and legal questions.