AMERICANS FOR PROSPERITY FOUNDATION

April 23, 2020

Submitted Via Regulations.gov

Jovita Carranza
Administrator
U.S. Small Business Administration
409 3rd St, SW
Washington, DC 20416

Re: U.S. Small Business Administration Business Loan Program; Paycheck Protection Program Interim Final Rule, No. SBA-2020-0019, RIN 3245-AH35

Dear Administrator Carranza:

I write on behalf of Americans for Prosperity Foundation ("AFPF"), a 501(c)(3) nonpartisan organization that educates and trains citizens to be advocates for freedom, creating real change at the local, state, and federal levels.[1] AFPF appreciates the opportunity to comment on the Small Business Administration's ("SBA") interim final rule implementing the Paycheck Protection Program. *See* 85 Fed. Reg. 20817 (the "Interim Final Rule").

AFPF believes that it is important to deliver timely, targeted, and temporary relief to those experiencing hardship like lost jobs or shuttered businesses as a result of government action. AFPF has concerns about the extent to which the Paycheck Protection Program ("PPP"), created by Sections 1102 and 1106 of the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act" or "the Act"), Pub. L. 116-136, has achieved this result. The government's public-health-related actions responding to the COVID-19 pandemic have necessitated the PPP, which is supposed to provide a much-needed lifeline to small businesses and their employees. The PPP is intended to protect the livelihoods of many Americans who are struggling financially through no fault of their own, coupled with government-imposed disruptions on everyday life and commerce, including government-mandated closures of businesses. At a minimum, programs like the PPP should be equitably and effectively administered.

AFPF has serious concerns that Section III.2.b.iii of the Interim Final Rule irrationally and unfairly closes off PPP eligibility to small businesses that are partially owned by individuals who have had any contact with the criminal justice system. This prohibition applies even if they are merely accused of a crime, irrespective of the nature of the alleged or proven conduct at issue, and regardless of whether such conduct reflects on the creditworthiness or legitimacy of the business. AFPF believes that, as currently drafted, this provision of the Interim Final Rule is contrary to the text, structure, and purpose of the CARES Act. This bright-line limitation on eligibility for critical PPP support also raises due-process concerns as applied to those merely charged with crimes,

[1] *See* AMERICANS FOR PROSPERITY FOUNDATION, https://americansforprosperityfoundation.org/.

including misdemeanors. This arbitrary limitation on eligibility for critical financial support is poor public policy with an overbroad sweep that harms otherwise deserving small businesses and their employees. Accordingly, as detailed below, AFPF respectfully urges the SBA to immediately remove Section III.2.b.iii from the Interim Final Rule or, at a minimum, amend the Interim Final Rule to narrowly tailor any criminal-justice-related limitations on eligibility to target the types of conduct bearing on the creditworthiness and legitimacy of the applicant business.

I. Relevant Statutory and Regulatory Background

The CARES Act states that any business with under 500 employees is eligible for loans made under the program: "Sec. 1102.7(a) Loan Program . . . b) *Increased Eligibility For Certain Small Businesses And Organizations*.— (1) In General— During the covered period, *any business concern*, private nonprofit organization, or public nonprofit organization which employs not more than 500 employees shall be eligible to receive a loan made under section 7(a) of the Small Business Act[.]"[2] As evidenced by Section 1102's text, Congress intended to make PPP relief broadly available to *any* legitimate business, to benefit their employees.

Nonetheless, the Interim Final Rule appears to have imported and broadened eligibility barriers established by an SBA regulation initially promulgated in 1996,[3] as well as related SBA guidance. The Interim Final Rule states that "[b]usinesses that are not eligible for PPP loans are identified in 13 CFR 120.110 and described further in SBA's Standard Operating Procedure (SOP) 50 10, Subpart B, Chapter 2[.]"[4] 13 C.F.R. § 120.110(n) broadly bars businesses with partial owners or key employees who have had contact with the criminal justice system from obtaining loans, stating that "[t]he following types of businesses are ineligible . . . [b]usinesses with an Associate who is incarcerated, on probation, on parole, or has been indicted for a felony or a crime of moral turpitude[.]"[5] "Businesses engaged in any illegal activity" are independently ineligible for SBA loans.[6] SBA's Standard Operating Procedure (SOP) 50 10, Subpart B, Chapter 2 goes even further, broadening the universe of what SBA refers to as "Businesses with an Associate of Poor Character," which it has deemed ineligible for loans.[7]

Unfortunately, the Interim Final Rule appears to go even farther. Section III.2.b.iii states that "[y]ou are ineligible for a PPP loan if, for example: An owner of 20 percent or more of the equity of the applicant is incarcerated, on probation, on parole; presently subject to an indictment,

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[2] 15 U.S.C. § 636(a)(36)(D)(i)(I)-(II), amended by Section 1102, CARES Act, Pub. L. 116-136 (emphasis added).

[3] *See* 61 Fed. Reg. 3226, 3239-3240 (Jan. 31, 1996).

[4] 85 Fed. Reg. 20811, 20812 (Apr. 15, 2020). To our knowledge, neither the regulation nor the related SBA guidance has been challenged in court.

[5] "Associate" is defined by 13 C.F.R. § 120.10 as: "(i) An officer, director, owner of more than 20 percent of the equity, or key employee of the small business; (ii) Any entity in which one or more individuals referred to in paragraphs (2)(i) of this definition owns or controls at least 20 percent; and (iii) Any individual or entity in control of or controlled by the small business (except a Small Business Investment Company ('SBIC') licensed by SBA)."

[6] 13 C.F.R. § 120.110(h).

[7] SBA SOP 50 10 5(K), § III.A.13, pp. 109-110 (Apr. 1, 2019). Importantly, SBA SOP 50 10 appears to recognize that what it calls "Businesses with an Associate of Poor Character" may well be legitimate enterprises that comply with applicable laws, as it includes a separate prohibition against providing benefits to "Businesses Engaged in any Illegal Activity." *Id.* at § III.A.8, pp. 107.

criminal information, arraignment, or other means by which formal criminal charges are brought in any jurisdiction; or has been convicted of a felony within the last five years[.]"[8]

II. Section III.2.b.iii of the Interim Final Rule is Arbitrarily and Unfairly Overbroad and Should Therefore Be Promptly Removed.

Section III.2.b.iii of the Interim Final Rule is irrationally overbroad, unfairly barring many small businesses—and their employees—who desperately need PPP loans from even applying. To begin with, it goes farther than 13 C.F.R. § 120.110(n) by barring a businesses 20 percent owned by individuals merely charged with unrelated misdemeanors (*e.g.*, DUI/DWI) from applying. The Interim Final Rule does not explain this apparent policy change,[9] which appears to contravene Congress's clear intention of *expanding* eligibility to obtain PPP loans. Categorically barring businesses partially or wholly owned by individuals who are merely *accused* of crimes violates basic norms of due process and is contrary to the presumption of innocence.

An additional flaw is that Section III.2.b.iii appears to target conduct entirely unrelated to any legitimate eligibility criteria in any way bearing on whether a small business is creditworthy or engaged in legitimate activities. Section III.2.b.i of the Interim Final Rule separately states that businesses that "are engaged in any activity that is illegal under Federal, state, or local law" are "ineligible for a PPP loan."[10] That provision—although perhaps overbroad as applied to businesses that may operate lawfully under state and local law, even though prohibited by federal law—at least attempts to further a permissible government purpose. In light of Section III.2.b.i of the Interim Final Rule, Section III.2.b.iii is, at a minimum, superfluous. Put simply, Section III.2.b.iii serves no necessary purpose. Tellingly, Section III.2.b.iii in no way cabins its reach to crimes plausibly bearing on creditworthiness (for example, prior convictions for fraud, identity theft, or embezzlement). As one court recently observed, "in regard to the CARES Act, *all business owners on probation are treated equally* [by SBA's Interim Final Rule] *in that all are ineligible for PPP funds*."[11] That makes no sense for a host of reasons, not least of which is the absence of any suggestion that there must be a nexus between the underlying criminal conduct and the activities of the business that wishes to apply for a PPP loan.

Even if Section III.2.b.iii served a legitimate purpose as applied to businesses wholly owned by individuals who have had contact with the criminal justice system, that still would not justify its application to businesses that are, for example, 20 percent or even 50 percent owned by

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[8] 85 Fed. Reg. 20811, 20812 (Apr. 15, 2020).

[9] "Agencies are free to change their existing policies as long as they provide a reasoned explanation for the change. When an agency changes its existing position, it 'need not always provide a more detailed justification than what would suffice for a new policy created on a blank slate.' But the agency must at least 'display awareness that it is changing position' and 'show that there are good reasons for the new policy.'" *Encino Motorcars, LLC v. Navarro*, 136 S. Ct. 2117, 2125-26 (2016) (cleaned up).

[10] *Id.*

[11] *United States v. Steven*, No. 19-10087, 2020 U.S. Dist. LEXIS 67631, at *14 (D. Kan. Apr. 17, 2020) (emphasis added) (denying motion for early termination of probation). The court noted SBA's "regulation here is clear that business owners on probation are not eligible for PPP funds." *Id.* at *9. The defendant pled guilty to a misdemeanor charge relating to his personal gambling activities. *See* Amy Renee Leiker & Chance Swaim, *Brandon Steven pleads guilty to gambling charge, forfeits more than $1 million*, THE WICHITA EAGLE (June 19, 2019), https://bit.ly/3eHlwFc.

such individuals. The following hypothetical illustrates this point: how is it fair to prohibit a small restaurant owned by five siblings, each of whom has a 20 percent interest, from obtaining a critical PPP loan because the "wild child" of the bunch was recently charged with a DUI or simple possession of a controlled substance? How would that accusation in any way bear on the legitimacy of the underlying business? How would denying a family business on this basis be equitable to the owners who have not even had any contact with the criminal justice system? Or, for that matter, the employees, who need to earn a paycheck to feed their families, and for whose benefit the PPP was established? Categorically denying businesses the ability to apply for PPP loans on the basis of individuals' unrelated contacts with the criminal justice system is nonsensical.

Section III.2.b.iii is also plain wrong, as the individuals it impacts have either paid their debt to society, are currently paying it, are presumed to be innocent of pending charged crimes. In many instances, individuals who have made past mistakes have done everything possible to rehabilitate themselves and build up legitimate businesses[12]—they deserve a second chance and should not be punished for circumstances over which they have no control, which were created by the government's response to the COVID-19 outbreak. Nor should their employees or co-owners.

The CARE Act's text, structure, and purpose in no way suggests that Congress intended for the SBA to consider any of the factors set forth in Section III.2.b.iii when determining loan eligibility criteria,[13] or even granted SBA statutory authority to do so.[14] Section III.2.b.iii is contrary to law, arbitrary and capricious, and in excess of SBA's statutory authority under the CARES Act. Section III.2.b.iii wrongly harms highly deserving individuals who most desperately need PPP relief. Accordingly, SBA should immediately remove this wrongful bar on PPP loan eligibility from the Interim Final Rule.

Thank you for your time and attention. If we can provide any additional information or otherwise be of further assistance, please do not hesitate to contact me via email (mpepson@afphq.org) or telephone (202.603.1678).

Respectfully submitted,

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[12] *See, e.g.*, Jill Colvin, *Criminal Records Shut Small Biz Owners Out of Aid Program*, AP (Apr. 21, 2020), https://bit.ly/3cFCrGA.

[13] "[A]n agency rule would be arbitrary and capricious if the agency has relied on factors which Congress has not intended it to consider, entirely failed to consider an important aspect of the problem, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could not be ascribed to a difference in view or the product of agency expertise." *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983).

[14] SBA is a creature of statute, which possesses only those powers that Congress chooses to confer upon it. *See La. Pub. Serv. Com v. FCC*, 476 U.S. 355, 374 (1986); *Lyng v. Payne*, 476 U.S. 926, 937 (1986).