

# SBA Issues New Guidance for PPP Borrowers Looking to Sell Their Business or Engage in Other “Changes of Ownership”

by Anthony J. Zeoli

A FREEBORN & PETERS LLP CLIENT ALERT

Since the inception of the Paycheck Protection Program (the “PPP”), there has been a lot of ambiguity as to the requirements for PPP borrowers looking to engage in M&A transactions and equity sales. To resolve the ambiguity, on October 2, 2020, the Small Business Administration (the “SBA”) released new guidance, in the form of [Procedural Notice No. 5000-20057](#) (the “Notice”), which provides much needed clarity around the specific requirements for lenders or the SBA to provide consent to PPP borrowers looking to engage in such transactions and the resulting treatment of the underlying PPP loan.



## **Background**

Many PPP lenders developed their own PPP loan forms based on prior SBA loan documents that contain provisions stating that the borrower will be in default of the loan if it merges, reorganizes, consolidates or otherwise has a change of control without the PPP lender’s approval. On top of that, under traditional 7(a) loans, the SBA’s prior approval is required in connection with any of the foregoing transactions while the loan is outstanding and it was unclear whether PPP loans would be subject to the same approval requirements. These provisions led most banks to take the position that both the PPP lender’s approval, and the approval of the SBA, were required for a PPP borrower to engage in any of these transactions while its loan remained outstanding. There was (and as of this alert still is) no clear process for requesting the approval of a PPP lender or the SBA to conduct any of the subject transactions. Even if a PPP borrower could navigate that process with a willing PPP lender, it could take weeks to months to obtain the requisite approvals.

Some PPP lenders even went so far as to say that a PPP borrower could not engage in any of these transactions until it filed its forgiveness application and the SBA issued its final determination on forgiveness. Given many PPP lenders still haven’t started taking forgiveness applications and that the SBA has up to 60 days to make its determination with respect to an application, waiting until both of these events have occurred could take months.

This backdrop has resulted in significant concern in the M&A community and has led many PPP borrowers to significantly delay their intended transactions. Those PPP borrowers for whom delaying these transactions was not economically or otherwise an option were forced to proceed by either repaying their PPP loan, or closing the transaction knowing that the closing might adversely affect the potential forgiveness of their PPP loans. While the Notice doesn’t answer all of the questions around these transactions it goes a long way in clearing up many of the uncertainties.

## **What's in the Notice?**

The Notice clarifies the requirements for completing a “change of ownership” (*as defined therein and discussed below*) and the treatment of the related PPP loan. As the definition of “change of ownership” is broad enough to cover the majority of M&A transactions and significant equity sales/transfers, the Notice provisions are extremely relevant to, and welcomed by, PPP borrowers and other M&A deal participants.

**Change of Ownership.** Under the Notice a “change of ownership” includes any of the following:

- The sale or transfer of 20% or more of the PPP borrower’s equity interests;<sup>1</sup>
- The sale or transfer of 50% or more of the PPP borrower’s assets (*as measured based on the fair market value of the assets*); and
- The merger of the PPP borrower with, or into, another entity.

**General Provisions.** Regardless of the level of approvals is required (*as discussed below*), the following will apply to any “change of ownership” by a PPP borrower prior to their PPP loan being fully forgiven or paid off:

- A PPP borrower contemplating a “change of ownership” must, prior to closing, give written notice to their PPP lender describing the proposed transactions, together with copies of the proposed transaction documents.
- The PPP borrower (*and, in the event of a merger of the PPP borrower into another entity, the successor to the PPP borrower*) will remain responsible for:
  - the performance of all obligations under its PPP loan;
  - all certifications made in connection with its PPP loan application (*including the certification of economic necessity*);
  - compliance with all other applicable requirements with respect to its PPP loan; and
  - obtaining, preparing, and retaining all required PPP forms and supporting documentation and providing the same to the PPP lender/SBA as requested.
- Where a PPP borrower is acquired by, or merged into, another PPP borrower, the new owners/successor entity will be responsible for segregating and delineating PPP funds and expenses and providing documentation to demonstrate compliance with PPP requirements by each PPP borrower.
- The PPP lender will be required to provide certain details regarding the closing of a “change of ownership” (*including an identification of the new owners and, where applicable, the amount of escrow funds held*) to the SBA within 5 business days of its closing.

**Cases in which NO approval is required.** In short, per the Notice there are no restrictions on a “change of ownership” if the borrower’s PPP loan is no longer outstanding. More specifically the Notice provides that no approval of the PPP lender or the SBA will be required in connection with a “change of ownership” by a PPP borrower if, prior to the closing:

- its PPP loan has been paid, in full; or
- the PPP borrower has completed the loan forgiveness process (*including receiving a final determination from the SBA*) and its PPP loan had been fully forgiven or the non-forgiven portion has otherwise been paid off, in full.

<sup>1</sup> The Notice provides that for purposes of determining whether the 20% threshold has been satisfied, all sales and other transfers occurring since the date of approval of the borrower’s PPP loan must be aggregated. However, special rules apply with respect to publicly traded PPP borrowers.

Cases that require the prior approval of the PPP lender ONLY (*SBA approval is NOT required*). A PPP borrower will only be required to obtain the prior approval of the PPP lender if the “change of ownership”:

- is structured as a merger or a sale/transfer of equity interests and:
  - the transactions involve the sale/transfer of 50% or less of the equity interests of the PPP borrower;<sup>2</sup> or
  - the PPP borrower: (a) has submitted a forgiveness application (*and all supporting documents*) to the PPP lender; and (b) has deposited with the PPP lender (*into an interest bearing escrow account controlled by the PPP lender*) an amount equal to the outstanding balance of its PPP loan;
- is structured as an asset sale and:
  - the transactions involve the sale/transfer of 50% or more of the assets of the PPP borrower (*as measured based on the fair market value of the assets*); and
  - the PPP borrower: (a) has submitted a forgiveness application (*and all supporting documents*) to the PPP lender; and (b) has deposited with the PPP lender (*into an interest bearing escrow account controlled by the PPP lender*) an amount equal to the outstanding balance of its PPP loan.

Cases that require the prior approval of BOTH the PPP lender and the SBA. For any proposed “change of ownership” that does not fall into one of the above categories, or where any of the applicable requirements cannot be satisfied, the PPP borrower will need to obtain the prior approval of both the PPP lender and the SBA. To obtain SBA approval the PPP borrower will need to submit a request to the SBA (*through the PPP lender*), which must include:

- the reason why the PPP borrower cannot either pay off the loan or satisfy the applicable requirements for PPP lender approval only (*including funding the required escrow amount*);
- a detailed description of the proposed transactions;
- a copy of its PPP loan promissory note;
- copies of any letter of intent or other agreements identifying the obligations of the PPP borrower and the other parties;
- a disclosure as to whether the buyer has an existing PPP loan (*and, if so, the respective SBA loan number*); and
- a list of all persons/entities holding 20% or more of the equity interests of the buyer.

The Notice also provides that: (a) the SBA may require additional risk mitigation measures as a condition to its approval of a particular “change of ownership;” (b) in order to get SBA approval for any “change of ownership” involving the sale/transfer of 50% or more of the assets of the PPP borrower, the buyer will be required to specifically assume all of the PPP borrower’s obligations under its PPP loan; and (c) the SBA will have up to 60 calendar days from the delivery of a fully completed request for approval to respond.

## **Conclusion**

While the Notice goes a long way in clarifying the prior ambiguities surrounding “change of ownership” transactions, it certainly does not resolve all of the surrounding issues. Most notably, many PPP lenders still have not started accepting PPP loan forgiveness applications. A PPP borrower looking to do a “change of ownership” who cannot submit its forgiveness application will be forced to obtain both the approval of the PPP lender and the SBA, which is a much more involved and elongated process. Moreover, as of the date of this alert, the actual administrative process for requesting the approval of a PPP lender or the SBA remains unclear. As such, a PPP borrower contemplating a “change of ownership” should reach out to their respective PPP lender as soon as possible in order to determine the process for obtaining the necessary approvals.

**We will continue to follow this and the other CARES Act programs and offer updates as further developments arise. If you have any questions, please contact Anthony Zeoli ([azeoli@freeborn.com](mailto:azeoli@freeborn.com)) or another member of the Freeborn CARES Act team.**

<sup>2</sup> The Notice provides that, for purposes of determining whether the 50% threshold has been reached, all sales and other transfers occurring since the date of approval of the borrower PPP loan must be aggregated.

## ABOUT THE AUTHOR



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Anthony Zeoli is a Partner in the Corporate Practice Group and the Leader of the Emerging Industries Team. He concentrates his practice in the areas of banking and commercial finance, securities, real estate, and general corporate law. Anthony's commercial finance practice includes the representation of borrowers and lenders in: secured and unsecured lending transactions; corporate reorganizations and restructuring; syndicated commercial financing transactions; and loan workouts.

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