

# Insights

## **SBA Guidance on Change of Ownership for PPP Borrowers**

---

October 8, 2020

By: Robert A. Greising and Corben A. Lee

On October 2, 2020, a Procedural Notice issued by the SBA (the "Notice") became effective that provides information and procedures addressing requirements for approval of changes of ownership for an entity that has received funds under the Paycheck Protection Program ("PPP"). The Notice put in place a procedure for SBA approval and lender notice and approval that had not been in effect before. Prior to the Notice, these types of issues would only be addressed in any contractual provisions within the underlying lending documents. The Notice details the process for notice to the lender, prior approval by the lender and, if necessary, SBA approval in the event a change of ownership will occur with respect to a borrower under the PPP.

The Notice defines a "change of ownership" as the occurrence of one of the following: (1) at least 20% of the common stock or ownership interest of the borrower is sold or otherwise transferred, in one or more transactions (including to an affiliate or an existing owner of the entity); (2) the borrower sells or otherwise transfers at least 50% of its assets (determined by fair market value) in one or more transactions; or (3) the borrower is merged with or into another entity. Please note, the change of ownership concept captures plans for reorganization and ownership succession already in place and not just new transactions with third parties.

The Notice establishes different procedures depending on whether the PPP note is fully satisfied or not. As you can imagine, if the PPP note is fully satisfied prior to the change of ownership, no restrictions will apply to the change of ownership and the borrower will have no reporting obligation to the lender or the SBA. However, if the PPP note is not fully satisfied prior to the change of ownership, the Notice details instances when a lender can approve the change of ownership and SBA approval is not required.

For changes of ownership in this circumstance that are structured as a sale of stock, an asset sale or a merger, the borrower may complete the change of control transaction with lender prior approval but without the prior approval of the SBA if: (1) the sale or transfer is of 50% or less of the common stock or fair market value of its assets; or (2) prior to the closing of the transaction, the borrower completes a forgiveness application reflecting its use of all of the PPP funds, submits it to the lender, establishes an interest bearing escrow account with the lender and deposits funds in such account equal to the outstanding balance of the PPP loan.

Following the completion of the forgiveness process, the escrow funds must first be disbursed to repay any remaining PPP loan balance (if any remains after the forgiveness process is completed). Any remaining escrow funds will be returned to the designated recipient under the escrow terms.

If the change of ownership involves a sale of more than 50% of the ownership or involves an asset sale but the borrower fails to submit the forgiveness application and establish the escrow, approval by the SBA is required prior to the change of ownership. The borrower will need to submit to the lender the notice of the proposed change of ownership transaction, with copies of the transaction documents. Then, the lender must submit the request to the SBA and include the following documents and information: (1) the reason that the borrower cannot fully satisfy the PPP note or cannot deposit escrow funds; (2) details of the proposed transaction; (3) a copy of the executed PPP note; (4) the letter of intent and the purchase or sale agreement setting forth the responsibilities of the borrower, seller and buyer; (5) disclosure of whether the buyer has an existing PPP loan, and, if so, the SBA loan number; and (6) a list of all owners of 20 percent or more of the buyer. The SBA can also impose, as a condition of its approval, additional measures it deems appropriate to minimize the risk of the proposed transaction.

Further, the SBA's approval of any change of ownership that is an asset sale is conditioned on the buyer assuming all of the obligations of the seller under the PPP loan, which undertaking must be included in the transaction documents. The SBA will review and provide a determination within 60 calendar days of receipt of a complete request.

Additional requirements will apply for a change of ownership regardless of whether or not SBA approval is required. For instances regarding a stock sale or merger, the borrower (or, if applicable, the successor to the borrower) will remain subject to all obligations under the PPP loan. If the purchaser or successor to the borrower also has its own PPP loan, it will need to establish protocols for segregating and tracking the PPP funds and uses to demonstrate that both loans comply with the PPP requirements and limitations.

For lenders, the Notice also establishes several affirmative obligations on the lender to facilitate the change in ownership approval process and communications with the SBA. If an escrow account is required, the lender must notify the SBA of the location of the escrow account and its balance within 5 business days of closing. Also, in addition to the submission by the lender noted above, for stock transfers or mergers, the lender must give notice to the SBA within 5 business days of the closing of the identity of the new owners, new ownership percentages, tax ID numbers of those holding more than 20% of the equity of the business and the escrow information noted above if an escrow is required. These notices must be given even if SBA approval is not required.

Finally, the Notice brings up a number of lingering questions that will hopefully be clarified in future guidance from the SBA. For example, what happens if a lender allowed a change of ownership prior to this guidance? What recourse do you have if your lender is not accepting applications yet? What if the lender did not have the contractual right to approve or receive notice of a change of ownership? What are the consequences of failure to obtain the SBA's approval? What if your transaction needs to close sooner than 60 days? Is there a process for expediting review and approval? What are the standards for approval? Will the borrower be able to supplement the lender's submission to advocate for approval? Is SBA approval ministerial after determining that the requirements are met or is it merit based that allows the SBA to consider the impact of the change of ownership on the PPP loan or the PPP policies? Will the SBA approval process for the change of ownership be done in



tandem with review and approval of the forgiveness application? What are the lender's responsibilities to process the forgiveness application in coordination with the change of ownership approval process? As a result of these numerous questions, we will continue to monitor developments in the SBA's guidance.

Krieg DeVault is committed to helping you and your business during these unprecedented times. With your needs in mind, we have established a COVID-19 Resource Center to assist you through this process.

If you have any further questions, comments or concerns, please feel free to contact **Robert A. Greising, Corben A. Lee** or a member of our **Business, Acquisitions & Securities team**.