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May 20, 2020

Jovita Carranza  
Administrator  
Small Business Administration  
409 3<sup>rd</sup> St., SW  
Washington, DC 20416

Re: SBA Administrative Docket, SBA-2020-0020-0001 (Comments on Interim Final Rule, *Business Loan Program Temporary Changes: Paycheck Protection Program – Additional Eligibility Criteria and Requirements for Certain Pledges of Loans*)

Dear Administrator Carranza,

I write on behalf of the Office of the Massachusetts Attorney General to provide comments concerning the U.S. Small Business Administration's ("SBA") Paycheck Protection Program Interim Final Rule concerning sole proprietorships, additional eligibility criteria, and loan pledge requirements ("Third Interim Final Rule," or "Third IFR"). Last week, we provided comments regarding the initial Interim Final Rule, SBA Administrative Docket, SBA-2020-0015-0001, which incorporated a May 6, 2020 letter from Attorney General Healey and 23 other state attorneys general to Congressional leaders urging a variety of reforms for the PPP. We reiterate those comments for purposes of this docket, but also wish to raise certain other criticisms and suggestions for incorporation into the Third IFR's administrative record, as set forth below:

1. Limiting Loans for Investment Partnerships. While the Third IFR largely focuses on sole proprietorships, it also makes certain statements regarding the eligibility of partners and partnerships. In section III(1)(a) of the Third IFR, the SBA specifies that partnership members, if applying through their partnerships, can obtain PPP loans even if the partnership has no employees. The provision notes that "self-employment income of general active partners may be reported as a payroll cost, up to \$100,000 annualized, on a PPP loan application filed by or on behalf of the partnership." To avoid confusion, the SBA should provide a clearer statement in this regulation regarding what types of partnerships are entitled to these government-guaranteed (and likely government-forgiven) loans. For instance, the SBA should be clearer regarding whether a group of investors who created a partnership and pooled money to actively invest in the stock market would be entitled to receive up to \$100,000 each from the PPP. Such loans do not serve the PPP's central purpose of helping struggling small businesses and their employees,

and the SBA should take steps to avoid any confusion regarding their eligibility. For similar reasons, the SBA should clearly address the eligibility of other types of partnerships for government-guaranteed loans. An example would be a lucrative boutique law firm that normally generates over \$1 million annually for each partner, but which is suffering from some drop in revenue during the pandemic. The purposes of the PPP would not be served by making loans (which, if they are forgivable, are effectively taxpayer funded grants) available to such partnerships. PPP regulations addressing partnership eligibility should specify safeguards to ensure that businesses generating ample funds do not receive PPP money to supplement partners' profits.

2. Limiting Loans for Highly Paid Employees That Continue to be Highly Paid During the Pandemic. A similar issue arises regarding how self-employed individuals can calculate payroll for purposes of the PPP. As noted in section III(1)(b) of the Third IFR, such individuals are directed to use the "2019 IRS Form 1040 Schedule C line 31 net profit amount. . . if this amount is over \$100,000, reduce it to \$100,000." The language used by the SBA here is confusing. It might be interpreted to mean that a self-employed individual making an annualized \$1 million, even during the pandemic, is entitled to receive a taxpayer-funded PPP loan for part of that salary and have that loan forgiven. To remove any appearance that the SBA has been inappropriately applying PPP funds, the agency should review prior PPP loan submissions to determine whether highly paid, self-employed individuals are seeking PPP loans and have been granted PPP loans. The SBA should also amend the Third IFR to make plain that forgiveness may not be available where a self-employed individual's net profit during the relevant eight-week period made the loan unnecessary.<sup>1</sup> The SBA could evaluate whether a simple test is appropriate to enforce this standard, such as barring loan forgiveness for sole proprietors when income or net profit exceeded a certain baseline.
3. Covering Commercial Insurance Premiums. Section III(1)(d)(iii) of the Third IFR indicates that a self-employed individual can use PPP loan proceeds to pay certain business automobile expenses, including "interest on an auto loan . . . and the cost of . . . gas you use driving your business vehicle." We have heard from a number of small businesses that would like to use a portion of their PPP loan proceeds to pay their commercial automobile insurance premiums. If the SBA intends to cover automobile-related expenses, it should consider including expressly in the regulation that PPP loans may be used to cover auto insurance. Moreover, because the underlying legislation authorizing the PPP, the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act"), directs that PPP loan proceeds can be used for items allowed under section 7(a) of the Small Business Act<sup>2</sup>, small business borrowers should be allowed to use some of the

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<sup>1</sup> The PPP application requires a certification that may be designed to address this necessity issue, but the SBA should also include this information in the rule. A standard in the rule could help to prevent unnecessary subsequent disputes regarding forgiveness standards. Such safeguards are especially important given that a borrower seeking less than \$2 million is currently deemed to have made the required certification in good faith. *See* Small Business Administration, Frequently Asked Questions, at Question 46 (May 13, 2020).

<sup>2</sup> Section 7(a) allows various general business expenses, which would generally include business insurance costs. *See* 15 U.S.C. sec. 636(a) ("Loans to small business concerns; allowable purposes; qualified business; restrictions and limitations. The Administration [SBA] is empowered to . . . make loans to any qualified small business concern, . . . for purposes of this chapter. . .").

PPP proceeds to pay not just commercial automobile insurance premiums, but other necessary insurance premiums as well.

4. Clarification Regarding the 75% Rule. Our office has previously suggested that some flexibility on the 75% payroll requirement may be appropriate in certain types of business situations. Even where the rule applies, there is a lack of clarity regarding self-employed PPP borrowers. Section III(1)(b) of the Third IFR indicates that self-employed individuals can use a snapshot of prior profit in lieu of actual salary for determining the size of an available PPP loan.<sup>3</sup> However, section III(1)(e) notes that “at least 75 percent of the PPP loan proceeds **shall be** used for payroll costs” (emphasis added). The SBA should make clear whether the 75% threshold can be met by payments calculated from the net profit as described in section III(1)(b). This appears to be the case, as stated in section III(1)(f) regarding forgiveness (“For individuals with self-employment income who file a Schedule C, the Administrator [of the SBA], in consultation with the [Treasury] Secretary, has determined that it is appropriate to limit loan forgiveness to a proportionate eight-week share of 2019 net profit, as reflected in the individual's 2019 Form 1040 Schedule C.”), but making the point clearer throughout the regulation would be preferable.
5. Avoiding the Appearance of Impropriety. In our office’s previous comments to the SBA, we noted the importance of treating all applicants fairly and we discussed the need for a strict “first-come, first-served” policy. It is important that the SBA and its authorized lenders avoid all appearances of impropriety. Section III(2)(a) of the Third IFR explicitly allows bank (or other lender) directors and certain bank owners (holders of less than 30 percent equity in the bank or other lender) to fund their own side businesses through PPP loans secured at the bank. *See* Section III(2)(a) of the Third IFR (“SBA ... shall not apply to prohibit an otherwise eligible business owned ... by an outside director [of an SBA-authorized lender] or holder of a less than 30 percent equity interest in a PPP Lender from obtaining a PPP loan from the PPP Lender on whose board the director serves or in which the equity owner holds an interest”). The provision does demand that the lender show no favoritism towards the director/owner’s side business, *see id.* (“[such loans can be funded] **provided that** the eligible business owned by the director or equity holder **follows the same process as any similarly situated customer**” (emphasis added)), and notes that “[f]avoritism by the Lender in processing time or prioritization of the director’s or equity holder’s PPP application is prohibited.” *Id.* However, this admonition may well prove to be insufficient. The integrity, and the public’s view of the integrity, of the PPP program is exceedingly important. Given that such businesses could simply apply through another SBA authorized lender, the SBA should consider barring these types of transactions except in very narrow or exceptional circumstances that do not raise any appearance of impropriety.

We thank you for considering our comments as set forth above. Please feel free to contact us should you have any questions.

Sincerely,  
  
Glenn Kaplan, Chief

Insurance & Financial Services Division

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<sup>3</sup> If the self-employed borrower has employees, then the snapshot of prior profit can be added to payroll costs associated with the employees. *See* Third IFR, at sec. III(1)(b).