Insight

The HEALS Act and the Paycheck Protection Program

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Executive Summary

- Senate Republicans have set out their position for the next round of COVID-19 relief legislation in the $1 trillion Health, Economic Assistance, Liability Protection, and Schools (HEALS) Act.
- The HEALS Act, like the House Democrats' HEROES Act but unlike previous relief packages, is light on financial services policy with the exception of proposed changes to the Paycheck Protection Program (PPP), the most effective aspect of the CARES Act.
- The Republicans' proposal would allow firms to take a second PPP loan, provides an additional $190 billion in funding for the program, and would make a number of program changes simplifying the PPP process. Surprisingly, however, Senate Republicans would only allow a narrow set of firms to apply for a second PPP loan.

Introduction

On July 28, Senate Republicans announced a series of bills that together make up the Health, Economic Assistance, Liability Protection, and Schools (HEALS) Act, a $1 trillion statement of intent setting out their priorities for the next round of COVID-19-related federal aid, and a direct response to the $3 trillion HEROES Act issued by House Democrats. These bills represent the starting point of debate for the eventual bicameral relief bill.

Unlike in the CARES Act, financial services policy has taken something of a back seat in the HEALS proposal, as it did in HEROES. It does, however, come as no surprise that Senate Republicans are seeking to update and provide additional funding for the Paycheck Protection Program (PPP), the highly successful small-business loans program administered by the Small Business Administration (SBA) and Treasury. The PPP distributed $531 billion in a single month and was the largest source of support for the economy for the month of April. Recent data indicate that the PPP may have saved as many as 3.2 million jobs.

Despite these successes the PPP has encountered operational difficulties and negative press ranging from the unjustified (as some businesses were deemed "inappropriate" despite qualifying per Congress's construction of the program) to the justified (little information about the mechanism of forgiveness eventually giving way to contradictory information). As a result of these concerns, and the limitations of the program, over $130 billion of funding remains available.

Within the HEALS Act, Republicans have proposed the Continuing Small Business Recovery and Paycheck Protection Program Act, introduced by Senator Marco Rubio, chairman of the Senate Committee on Small Business and Entrepreneurship, and Senator Susan Collins. The bill would allow qualifying businesses to obtain a second PPP loan and would provide an additional $190 billion in funding to the program, in addition to making a number of program changes.

The Current State of the PPP

The CARES Act set aside $349 billion for the relief of small businesses, to be administered by the SBA in the form of the PPP. The SBA commenced the PPP on April 3, 2020, and closed the program on April 16, 2020, on the exhaustion of the $349 billion appropriated by Congress. Congress later provided an additional $310 billion for the PPP in H.R.266, the Paycheck Protection Program and Health Care Enhancement Act. This bill brought the total funds available to the SBA and the PPP to $659 billion. The PPP program was due to expire at midnight on June 30 with funds remaining, but just hours before the expiration of the program, Congress authorized an extension through August 8. Over $130 billion in funding remains available to the program.

The HEALS Act's Proposed Changes

The Continuing Small Business Recovery and Paycheck Protection Program Act has four major components.

PPP Second Draw Loans

The bill would provide an additional $190 billion in funding to the PPP to support PPP loans extended both to first-time borrowers but now also to second-time borrowers. Second-time borrowers must, however, satisfy new criteria to qualify. Where first-time borrowers must only meet SBA small business requirements (broadly speaking, firms with under 500 employees), to be eligible for a second PPP loan firms must have under 300 employees. Likewise, where first-time firms need only "attest" that they have suffered financial hardship as a result of the pandemic, second-time borrowers must "demonstrate" a 50 percent reduction in gross revenues. Finally, where first-time firms might receive a loan calculated on payroll up to $10 million, the maximum loan size for a second time borrower equals 2.5 times average total monthly costs up to a maximum of $2 million. Borrowers cannot receive a second loan where the loan amount when added to the first loan would exceed $10 million. Finally, the bill carves out $25 billion for borrowers with fewer than 10 employees and $10 billion set aside for loans made by community lenders.

Expands the SBA 7A Loan Program

The bill would authorize $100 billion in long-term, low-cost loans for "seasonal businesses and businesses located in low-income communities" via an expansion of the SBA's existing 7A loan program. To be eligible firms must qualify as SBA small businesses but must also demonstrate a 50 percent reduction in gross revenues. The maximum value of loans offered would be twice the borrower's annual revenue, capped at $10 million. These loans would be entirely guaranteed by the SBA and have a maturity of 20 years with a fixed 1 percent interest rate to the borrower.

PPP Program Improvements

The bill would make a number of program improvements to the PPP, most notably a simplified loan-forgiveness process (at least the third time this process will have been "simplified," for anyone counting). A wider range of expenditures would become forgivable, including for the provision of protective equipment to workers. The bill would also once again expand eligibility of the program to include some 501(c)(6) organizations, but not professional sports teams or political campaigns, and has terms providing favorable PPP loan calculations for farmers and ranchers.

Small Business Growth and Domestic Production Investment Facility

The bill would establish a Small Business Growth and Domestic Production Investment Facility. This facility would provide $10 billion in long-term debt with equity features to registered SBA Small Business Investment Companies (SBICs) that invest in small businesses with significant revenue losses from COVID-19, manufacturing startups in the domestic supply chain, and in low-income communities.

Analysis

Allowing companies to obtain a second PPP loan is a policy position with broad support in Congress and is highly likely to be included in the final version of the bill. Perhaps more surprising is the narrowness of the degree to which Republicans would construct eligibility requirements. Restricting eligibility to firms with fewer than 300 employees and a 50 percent reduction in revenue is oddly limiting for a program that has demonstrated such success and still has funds available. Trade groups including the National Restaurant Association have already indicated that the program as suggested is simply not flexible enough to allow for program takeup, frustrating the very purpose of the expansion. A 50 percent reduction in revenue for most firms would likely indicate that the business is no longer a going concern loan notwithstanding. To what extent would Congress be betting on the wrong horses?

Even more curious is the requirement that impacted firms "demonstrate" the reduction in gross revenue. The CARES Act did everything it could to streamline the process of obtaining a loan by only requiring borrowers to attest their need. Here Republicans would seemingly require the need for evidence, perhaps in the belief that the time pressure is not as significant and higher standards are necessary to prevent fraudulent applications. As with the previous number of rounds of PPP lending, the participation of banks will be key. Banks will need to find capacity and not be turned off by complex loan terms – and the Fed will once again have to buy these loans as quickly as possible.

Conclusions

It does not seem like an overstatement that the PPP was the most effective and consequential relief mechanism of the CARES Act, as three months later other relief programs, most notably emergency relief provided by the Fed, continue to stumble out the gate. Although the program has its flaws, and philosophical questions remain about the initial decision to provide relief in the form of forgivable loans rather than grants, the PPP has been wildly effective. Allowing firms to take a second loan, providing additional funding to the program, and making it easier for a wider range of firms to apply using a simplified process represent the most sensible steps Congress can take.