

BANKING & FINANCE LAW ALERT

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JACK MEADOWS

614.227.2101

jmeadows@porterwright.com

JACK BEELER

614.227.1959

jbeeler@porterwright.com

CASSANDRA RICE

937.449.6713

crice@porterwright.com

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SBA loan eligibility FAQs

The Coronavirus Aid, Relief and Economic Security Act (CARES Act) offers new financial relief for small businesses, which my colleague [Cassandra Rice](#) detailed in this [Law Alert](#). Certain government programs, including SBA loan programs, are reserved for “small businesses.” In order to qualify for those programs, a business must satisfy both the SBA’s definition of a “small business concern” as well as the size standards for a small business.

What is a small business concern?

- 13 C.F.R. § 121.105(a)(1) provides that “a business concern eligible for assistance from SBA as a small business is a business entity organized for profit, with a place of business located in the United States, and which operates primarily within the United States or which makes a significant contribution to the U.S. economy through payment of taxes or use of American products, materials or labor.”
- Business concerns may be in the following legal forms:
 - an individual proprietorship
 - limited liability company
 - corporation
 - joint venture (if no more than 49 percent participation in the joint venture is by foreign business entities)
 - association
 - trust
 - cooperative

What is a small business size standard?

- A small business size standard is the largest size that a business may be to remain classified as a small business for SBA purposes.

- Size standards vary by industry.

How does SBA calculate small business size standards?

- Size standards are calculated by the number of employees or annual receipts.

How does SBA calculate the number of employees for a business?

- The SBA does not look only at full-time employees. 13 C.F.R. § 121.106 provides the method for calculating a business's number of employees.
- SBA counts all individuals employed on a full-time, part-time, or other basis, including employees obtained from a temporary employee agency, professional employee organization or leasing concern.
- SBA will consider the totality of the circumstances, including criteria used by the IRS for Federal income tax purposes, in determining whether individuals are employees of a concern.
- Volunteers are not considered employees.
- The average number of employees of the concern is used (including the employees of its domestic and foreign affiliates) based upon numbers of employees for each of the pay periods for the preceding completed 12 calendar months.

How does SBA calculate annual receipts?

- The SBA does not merely look at annual sales. 13 C.F.R. § 121.104 provides the method for calculating a business's annual receipts.
- Receipts means all revenue, in whatever form received or accrued from whatever source, including from the sales of products or services, interest, dividends, rents, royalties, fees, or commissions, reduced by returns and allowances.
 - Receipts equal the total income (or gross income) plus the cost of goods sold.
- Receipts exclude net capital gains or losses; taxes collected for and remitted to a taxing authority if included in gross or total income, such as sales or other taxes collected from customers and excluding taxes levied on the concern or its employees; proceeds from transactions between a concern and its domestic or foreign affiliates; and amounts collected for another (such as deposits received by a travel agent, real estate agent, advertising agent, conference management service provider, freight forwarder or customs broker).
- Receipts are averaged over a business's latest three complete fiscal years or (except in the Business Loan and Disaster Loan Programs) five complete fiscal years to determine the average annual receipts. If a business hasn't been in business for five years, multiply its average weekly revenue by 52 to determine its average annual receipts.

What if my business is affiliated with a larger company?

- Per 13 C.F.R. § 121.105, a business will not be treated as a separate business concern if a substantial portion of its assets and/or liabilities are the same as those of a predecessor entity.
- In such a case, the annual receipts and employees of the predecessor will be taken into account in determining size.
- 13 C.F.R. § 121.103 provides the method for determining whether an affiliation exists between businesses:
 - Generally, “concerns and entities are affiliates of each other when one controls or has the power to control the other, or a third party or parties controls or has the power to control both.”
 - Thus, subsidiaries are affiliated with their parent companies, and brother-sister companies are considered to be affiliated.

What if my business already has a loan with a lender?

- If your business is already borrowing from a lender under a credit agreement, you should double check the credit agreement to determine if incurring more debt from SBA loans is permitted.
- If SBA loans are not considered permitted indebtedness under the credit agreement, then small businesses should work with their lenders to obtain their consent for an SBA loan.
- While waiting for lender approval to incur additional debt, small businesses should continue to pursue SBA financing.

How does the Coronavirus Aid, Relief, and Economic Security (CARES) Act increase eligibility for SBA loans?

- Under the CARES Act, small businesses would continue to be eligible under the above standards, but the Act also expands eligibility for “covered loans” under the new program to all businesses with 500 employees or less.
- Independent contractors will now be eligible for SBA loans.
- Nonprofit organizations may now be eligible.
- Businesses that are assigned a North American Industry Classification System (NAICS) code beginning with 72 (i.e., hotels, restaurants and other hospitality industry companies) are eligible if they have 500 or less employees per physical location.
- The CARES Act waives the provisions applicable to affiliations under 13 C.F.R. § 121.103 for any business concern:
 - With 500 or less employees that is assigned a NAICS code beginning with 72 (i.e., hotels and restaurants);
 - Operating as a franchise that is assigned a franchise identifier code by the SBA; or
 - Receiving financial assistance from a small business investment

company (SBIC) licensed under Section 301 of the Small Business Investment Act of 1958 (15 U.S.C. § 681).

- SBIC's are privately-owned investment companies that are licensed by the SBA. They provide small businesses (particularly start-up companies) with financing opportunities.

SBA calculates a business's industry according to 13 C.F.R. §121.107. SBA considers "the distribution of receipts, employees and costs of doing business among the different industries in which business operations occurred for the most recently completed fiscal year."

Examples of Size Standards for Certain Industries

- Chicken Egg Production: \$16.5M in annual receipts
- Electric Power Distribution: 1,000 employees
- Commercial and Institutional Building Construction: \$39.5M in annual receipts
- Breweries: 1,250 employees
- Surgical and Medical Instrument Manufacturing: 1,000 employees
- Supermarkets and Other Grocery (except Convenience) Stores: \$35M in annual receipts
- Colleges, Universities and Professional Schools: \$30M in annual receipts
- Full-Service Restaurants: \$8M in annual receipts
- Automobile Manufacturing: 1,500 employees
- Most types of agriculture: \$1M in annual receipts
- General Warehousing and Storage: \$30M in annual receipts
- Beauty Salons: \$8M in annual receipts
- Other Miscellaneous Nondurable Goods Merchant Wholesalers: 100 employees

Helpful Resources

- A table detailing the Small Business Size Standards by NAICS Industry can be found [here](#).
- The [SBA website has a tool](#) that allows businesses to check to see if they qualify as a small business.

For more information contact [Jack Meadows](#), [Cassandra Rice](#), [Jack Beeler](#) or any member of [Porter Wright's Banking & Finance practice group](#).