

## Paycheck Protection Program highlights numerous oversight concerns even as the SBA makes first disclosures

By Corey Runkel and Rosalind Z. Wiggins

Original post [here](#).

The [Coronavirus Aid, Relief, and Economic Security \(CARES\) Act](#), which passed on March 27, established the Paycheck Protection Program (PPP), the US government's largest and most controversial program put in place to address the economic impacts of the COVID-19 virus. [Since April 3](#), the PPP has issued nearly [4.9 million loans](#) guaranteed by the Small Business Administration (SBA). As of June 30, banks and other private lenders have extended \$521 billion in government-guaranteed, forgivable loans under the program. The government's support measures have enjoyed [popularity](#) with taxpayers compared to those enacted during the Global Financial Crisis (GFC). However, the PPP has been under constant scrutiny from Congress and industry critics since implementation. In response to such criticism and changing economic conditions, both Congress and the SBA have repeatedly modified the program.

At least seven oversight bodies have responsibility for ensuring that the PPP is administered according to its Congressional mandates. These include the Pandemic Response Accountability Committee (PRAC), composed of [20 standing federal inspectors general](#) (IGs); the SBA IG; and the newly-created Special Inspector General for the Pandemic Response (SIGPR), which is tasked with tracking and evaluating loans and loan guarantees made by the Department of Treasury. The PPP is also subject to oversight by the Government Accountability Office and three congressional committees on small businesses. More detail about the PPP oversight bodies appears at the end of this blogpost.

A number of PPP oversight bodies have criticized the SBA for not releasing sufficiently detailed information about the PPP loans to enable it to properly perform their duties; they have specifically asked for loan-level details so they can properly analyze the efficacy of the program and determine whether it is meeting its statutory mandates. Other issues raised are listed below:

1. disclosure of detailed loan information
2. insufficient incentives for lender due diligence
3. differential accessibility for large and small borrowers
4. failure to implement statutory priorities
5. confusing eligibility criteria and limited application diligence
6. integrity of the loan forgiveness process
7. auditing processes.

This post will elaborate on the issues above, compare PPP oversight thus far with oversight during the Global Financial Crisis (GFC), and discuss greater implications for transparency of the government's COVID crisis programs.

## Design of the Paycheck Protection Program

The goal of PPP is to make loans that help “[businesses keep their workforce\[s\] employed during the Coronavirus \(COVID-19\) crisis](#).” Eligible SBA-approved lenders facilitate loans to small businesses that the Treasury guarantees. Under the SBA and Treasury’s original rules, the government would forgive a loan so long as the borrower used at least 75% of lent funds for payroll expenses. The program began processing loans [just seven days](#) after Congress passed the CARES Act. After nearly two weeks of loan processing, the SBA had [approved](#) more than 1.6 million loans through nearly 5,000 lenders, a massive increase over its normal volume. As of [June 30](#), lenders have extended more than \$521 billion of the total \$659 billion appropriated for the government guarantees. On that same day, Congress [voted](#) to extend the PPP until August 8. At the time of the vote, the PPP had \$139 billion available.

## Major issues and challenges

### *Disclosure of detailed loan information*

The disclosure of loan recipients has been a primary issue raised by oversight authorities. Several PRAC inspectors general wrote a [letter](#) to several members of Congress in early June expressing concern that an opinion from the Treasury General Counsel would exempt PPP loans from PRAC’s inspection, which they argued was contrary to how they interpreted their statutory duties. At stake in disclosure are the specific businesses and activities funded by potentially hundreds of billions of public dollars, some of which are known to have landed in the bank accounts of publicly traded corporations with other viable lending sources, and in small businesses connected to members of Congress.

The SBA made its first [PPP disclosures](#) on July 6; however, it released loan-level data including business names, addresses, NAICS codes, zip codes, business type, demographic data, non-profit information, jobs supported, and loan amount ranges only for loans of \$150,000 or larger. For loans of less than \$150,000, the exact amounts were disclosed, but the borrowers were anonymized and identified by zip code, industry, and business type.

PPP [applications](#) included provisions notifying applicants that loan data would likely be disclosed pursuant to Freedom of Information Act requests. Secretary Mnuchin also originally agreed with this in April, but FOIA requests were rebuffed, triggering a [lawsuit](#) by several media organizations. Secretary Mnuchin’s [position](#), based on a Treasury counsel opinion, was that for small businesses such information is “confidential” and “proprietary.” Following [demands](#) from the House Select Subcommittee, and lagging SBA cooperation noted in the GAO report, the administration on [June 19](#) retreated from that position, [announcing](#) the current, two-tiered disclosure model.

A June 23 YPFS [blogpost](#) noted that, while 75% of approved funding passed through loans of \$150,000 or larger, 86% of PPP borrowers were lent less than \$150,000. The Treasury’s new standard leaves a wealth of information undisclosed despite applicants’ acknowledgment that such information would be disclosed. Several oversight bodies and members of Congress continue to push for release of all PPP recipient names and loan details.

The SBA’s limited disclosure is problematic for a number of reasons. The failure to collect information and limited disclosure will possibly limit the ability of oversight authorities to properly fulfill their roles analyzing programs and their efficacy. Senator Ben Cardin made this point at the June 10 hearing on the PPP: “One reason we would like to get more granular data is

so we can understand the scope of the issues” (2:12). And even after the SBA’s recent disclosure of redacted information, Senator Chuck Schumer continues to push for full disclosure of the names of all recipients so that the effectiveness of the program can be properly assessed.

A Treasury OIG report dated May 18 raised a similar point with respect to the Treasury’s failure to provide a mechanism for recipients to report regarding use of the funds received from the Coronavirus Relief Fund, which provided \$150 billion to states, tribal governments and municipalities for COVID related expenses: “This position negatively impacts our office’s ability to efficiently and effectively carry out oversight responsibilities.”

Second, limited disclosure under the PPP and other programs creates two levels of disclosure under programs established with CARES Act funds. The Federal Reserve has established under Section 13(3) of the Federal Reserve Act several lending programs using \$195 billion of CARES Act funds from the Treasury. Section 13(3) requires that the Fed make an initial report, followed by monthly [updates](#) to Congress upon the establishment of a new program. Although the law requires the Fed to include the identities of participants and details of loans in such reports, Fed Chairman Powell may request that they be kept confidential.

For four facilities receiving Treasury equity support with CARES Act funds, the [Fed’s April announcement](#) states that it will publish the reports including the names and details of participants; amounts borrowed and interest rate charged; and overall costs, revenues, and fees. See a [YPFS blogpost](#) on this announcement. A month later the [Fed announced](#) that it would make similar disclosures with respect to the Term Asset-Backed Securities Loan Facility and the Paycheck Protection Program Liquidity Facility (PPPLF), programs not covered by the CARES Act disclosure and reporting rules. The Fed stated that it was making these more liberal disclosures because it “remains committed to providing the public and Congress with detailed information about our efforts to support households and businesses during this unprecedented time.”

Third, at stake is the question of possible favoritism and impropriety if the names of recipients and other loan details are not made public. A recent Politico [report](#) connected four members of Congress with PPP loans. And on [July 6 the SBA released its first set of PPP loan data](#); the release revealed more loans to businesses related to members of Congress and senior executive-branch officials, as well as to other entities that did not appear to be the small “mom-and-pop” shops often associated with the program.

To be clear, the CARES Act does not prohibit lawmakers from applying for or accepting PPP funds. SBA standard policy requires lawmakers with significant stakes in businesses applying for SBA loans to receive individual approval from the SBA’s Standards of Conduct Committee. But the Washington Post [reported](#) that in April SBA Administrator Jovita Carranza waived these requirements for members of Congress, SBA officials, and their families.

Section 4019 of the CARES ACT provides a conflict of interest provision that prohibits any company in which the President, Vice President, an executive department head, Member of Congress, or their immediate family member has a substantial interest in from benefiting from programs funded with Title IV funds and programs, which are funds targeted to the aviation industry and used to support Federal Reserve lending programs. The provision doesn’t extend to the PPP and its Title I, under which it is authorized, does not contain a similar provision. Nevertheless, the appearance of impropriety is important.

In response to criticism on the matter, Senator Rubio countered that “Congress plays no role in who gets a loan and who doesn’t.” Since the PPP offers funds to all who meet its eligibility criteria, he argued, it contrasts with competitive contract awards (where award decisions have to be made); such awards have historically been at the center of corruption cases.

However, for any program, a blanket waiver should raise concern. The SBA waiver neutralizes the application of its usual ethics review process. There is no evidence in the statute that Congress intended this. Further, it creates a duality of standards under the Act. Arguably, Congress’s inclusion of section 4019, was meant to do just the opposite--to create a more equal process of ethics review under the Cares Act for companies affiliated with government officials.

On top of the questionable blanket waiver, failure to disclose details of loans only furthers a sense of unfairness and a lack of integrity in the process. Even the disclosure of details that call into question whether the funds have been distributed in accordance with statutory mandate would allow for an airing of the facts and review by oversight authorities and the public.

#### *Insufficient incentives for lender due diligence*

PPP loans are distributed to borrowers through SBA-approved lending financial institutions, which receive a fee for each loan processed. Per [Section 1102\(2\)\(36\)\(O\)\(i\)](#), PPP loans receive 0% risk weight in the capital requirements of eligible lenders. In the [June PRAC report](#) (p. 41), the SBA Inspector General expressed the concern that SBA’s 100% participation in the loans would cause lenders to “not exercise due diligence in originating loans, thereby increasing the risk of potential financial losses to SBA.” In other words, the diffusion of loans through thousands of lenders could set up a principal-agent problem whereby lenders are incentivized by the fees on each loan origination to approve as many loans as possible and there were few incentives to ensure borrower quality. The IG went on to recommend that the SBA implement “proper controls in the loan approval phase to ensure eligibility of participants.”

#### *Differential accessibility for large and small borrowers*

As loan approvals began, [reports](#) filtered out that large and publicly traded borrowers had received loans quicker and easier than had small and new borrowers.

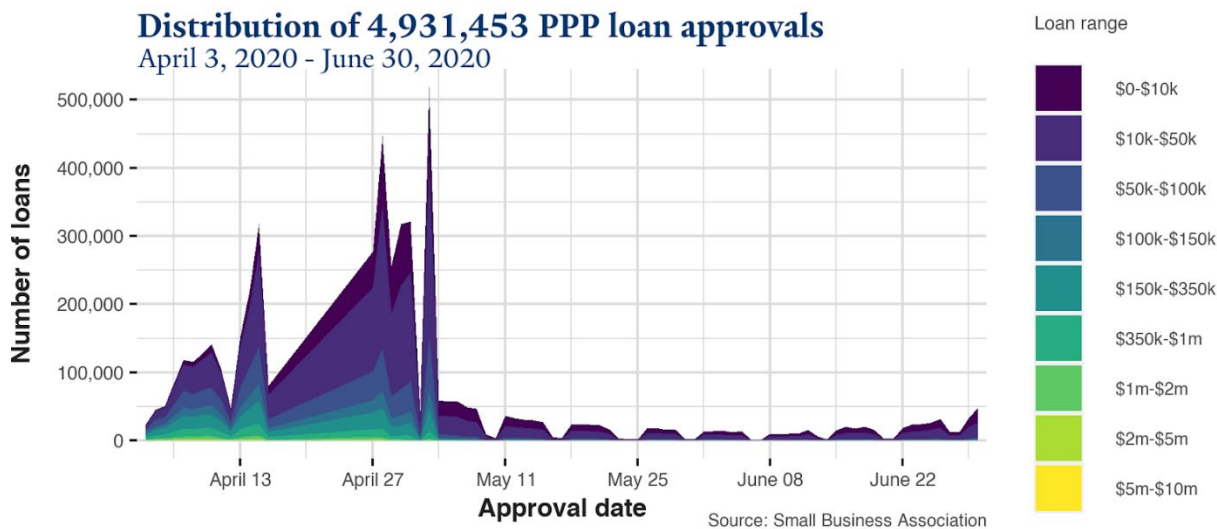
Lawmakers inveighed against differential treatment of businesses trying to borrow from the PPP in letters addressed to Secretary Mnuchin and SBA Administrator Carranza. Missouri Senator Joshua Hawley [warned](#) in an early letter that the program was becoming a vector for “corporate greed” with two tiers of borrowers. He alleged that large and existing clients of lenders received loans larger, faster, and easier than small and new borrowers. Democratic Representatives later made [similar claims](#) in letters addressed to the SBA as well as to several of the largest lenders.

Members of the Senate Committee on Small Business & Entrepreneurship raised concerns during a June 10 [hearing](#) that this misalignment would foster a divide of the sort described by Senator Hawley. Committee Chair Marco Rubio defended the PPP, [saying](#) that “these bumps in the road were and are the price of a successful program.” Rubio went on to argue that the need for relief necessitated the velocity of loan approvals.

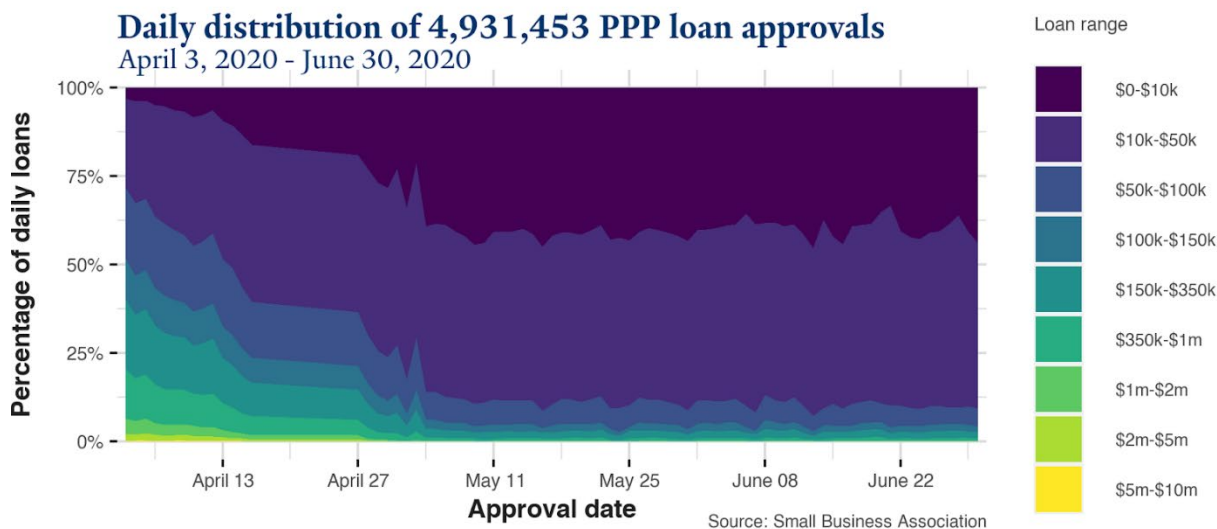
The eligibility of several publicly traded corporations that applied for PPP funds was controversial. Bloomberg [reported](#) that \$38.5 billion in PPP funds have been canceled since the program’s launch, after a mix of realizations that loans would not be forgiven or that assistance was not necessary. Such [returns](#) came in the wake of press coverage that included Secretary

Steven Mnuchin [insisting](#) that they were not the program’s targeted audience (and could face prosecution). Yet, on other occasions, the Secretary has not addressed why the PPP was not administered in a manner to target the markets prioritized by Congress.

**Figure 1.** Most approved loans came early in the PPP’s initial run.



**Figure 2.** Large loans made up a disproportionate amount of early approvals.



In aggregate, large loans may be closer to the exception than the rule. SBA data show that loans of \$1,000,000 or more makeup just 1.7% of loan approvals. As shown below, the vast majority of loan approvals were for loans smaller than \$150,000.

Number, Dollar Amount, and Distribution of Paycheck Protection Program Loans, as of June 12, 2020				
Amount of loan (dollars)	Number of approved loans	Approved dollars (\$)	Percent of approved loans (%)	Percent of approved dollars (%)
150,000 and less	3,926,477	136,683,699,300	85.8	26.7
150,001 - 350,000	370,507	83,240,884,629	8.1	16.2
350,001 - 1,000,000	197,277	112,238,433,258	4.3	21.9
1,000,001 - 2,000,000	52,586	72,856,742,215	1.1	14.2
2,000,001 - 5,000,000	24,734	73,523,496,712	0.5	14.4
More than 5 million	4,807	33,728,428,031	0.1	6.6
<b>Total</b>	<b>4,576,388</b>	<b>512,271,684,145</b>	<b>100</b>	<b>100</b>

Source: Small Business Administration | [GAO-20-625](#)

### *Failure to implement statutory priorities*

Section 1102(a)(36)(P)(iv) of the CARES Act requires the agency to issue guidance to lenders prioritizing small business concerns and entities in “underserved and rural markets.” In a [May 8 report](#), the SBA Office of the Inspector General (OIG) noted that the SBA had not yet issued guidance to lenders directing them to prioritize loans to these markets. In a June 10 [Congressional hearing](#), members questioned why the SBA had still not issued such guidance, but received no explanation from Secretary Mnuchin or SBA Administrator Carranza (at 52:00).

As a result, lenders were not notified to target these priority areas. The extent to which entities in underserved and rural areas participated in the program is unknown since the SBA [opted](#) not to collect demographic information from prospective borrowers. It did include the option to provide such information on its application for loan forgiveness. The result is that it will be difficult for the agency to determine how much of the PPP funds went to the entities that Congress had intended lenders to prioritize.

### *Confusing eligibility requirements and limited application diligence*

In order to implement the program quickly, the SBA relied on a limited application process, which was shortened after borrowers complained about the burden of the original application. Applicants self-certified that key loan eligibility requirements were met rather than provide detailed documentary evidence to support their claims. Treasury and the SBA say this was done to speed processing of an unprecedented number of applications.

A [June 25 GAO report](#) warned that “reliance on applicant self-certifications can leave a program vulnerable to exploitation by those who wish to circumvent eligibility requirements or pursue criminal activities.” The report also noted that frequent changes in the SBA guidance had led to confusion and “raised program integrity concerns.” It [concluded](#) that the agency should draw up oversight plans detailing how it would address potential risks and review PPP loans of all sizes.

Speed also apparently resulted in confusion regarding the actual criteria for PPP loans, as SBA issued guidance on a rolling basis: “18 interim final rules and 17 updates to its frequently asked questions [FAQs], as of June 15, 2020” (GAO pp.35, 241-2). These rules and FAQs addressed topics such as eligibility, payroll cost calculation, and loan forgiveness, but were at times confusing rather than clarifying and were issued at times that made compliance

challenging for lenders and borrowers (GAO pp.241-2). For example, the guidelines for how independent contractors and self-employed persons could borrow were issued only two days before the first tranche of funding was exhausted (GAO pp.243-4).

Legislators [have questioned some of the SBA's decisions](#) to streamline the application process in the interest of speed. A similar point was also considered by oversight authorities who reviewed the government's decisions regarding assistance to AIG during the Global Financial Crisis. Then, the [Congressional Oversight Panel](#) summarized its conclusion like this:

Through a series of actions, including the rescue of AIG, the government succeeded in averting a financial collapse, and nothing in this report takes away from that accomplishment. But this victory came at an enormous cost. Billions of taxpayer dollars were put at risk, a marketplace was forever changed, and the confidence of the American people was badly shaken. (page 9.)

Likewise, it will be the role of the PPP oversight authorities to consider whether the trade-offs made have been appropriate and effective in getting the PPP funds into the hands of the intended recipients.

#### *Integrity of the loan forgiveness process*

Since the start of PPP lending, Congress has significantly expanded eligibility for loan forgiveness.

First, the [Paycheck Protection Program Flexibility Act](#) lowered from 75% (as originally set by the SBA) to 60% the minimum portion of a loan spent on retaining or rehiring employees to qualify for forgiveness. The prior threshold of 75% had also been a forgiveness “cliff” -- that is, if 74.9% of the loan had been spent on payroll, the borrower would receive no forgiveness. The act changed this provision, creating a schedule of loan forgiveness amounts depending on the percentage of funds used for payroll expenses.

A [previous YPFS blogpost](#) details these changes. As revised, the PPP now more closely resembles the [fixed-cost supports](#) that many countries have enacted to help businesses in affording rent, mortgage payments, utilities, and other overhead expenses. Nonpayment of such costs may cause businesses to close permanently, precluding the SBA goal that such businesses maintain their workforces.

The Act also amended the time period borrowers had to use PPP funds in order to qualify for loan forgiveness. Originally, borrowers had to use funds within 8 weeks of receipt. Now borrowers can choose whether to use an 8-week period or a 24-week period to apply for forgiveness. The extension of the covered period under the PPPFA allows borrowers to use the loan proceeds to cover eligible expenses over a longer period of time but also creates a second chance for borrowers that might have failed to comply with the original terms of their loans. A [YPFS blog](#) discusses this change.

In the same act, Congress indicated that an employer should not be penalized if it cannot retain or rehire employees due to compliance with requirements or guidance issued by health authorities. The policy change responded to feedback from borrowers, but it arguably weakens the incentives for [employers to retain employees](#).

A related concern is that the SBA's original [five-page](#) loan forgiveness application also relies on extensive self-certifications for key criteria. Additionally, the agency introduced a simplified [three-page](#) “EZ” loan forgiveness application that requires even less information.

Without sufficient or verified information being collected, there is the risk that the SBA will forgive some loans that should not be forgiven.

### *Auditing Processes*

Although Secretary Mnuchin originally stated that all loans under the program would be subject to audit, he later reversed this position. The SBA has already [announced](#) that it will likely not look closely at borrower eligibility or forgiveness for loans smaller than \$2 million, which comprise 79.3% of PPP loans as of [June 27](#). Only approximately 30,000 loans that represent about 21 percent of the approved dollar amount of PPP loans (as of June 12) would be subject to audit under this standard.

The [GAO Report](#) has asked what the review plans are for loans of \$150,000 or less and has cautioned that “because of the number of loans approved, the speed with which they were processed, and the limited safeguards, there is a significant risk that some fraudulent or inflated applications were approved.” It also warned that the announced limited review guidelines have “increased the likelihood that borrowers may misuse loan proceeds or be surprised they do not qualify for full loan forgiveness.”

### **Comparisons with Global Financial Crisis oversight**

The oversight approach represented by the PPP is difficult to compare directly to the interventions the Department of Treasury employed during the GFC, reflecting to some extent the different natures of the two crises. During the Global Financial Crisis, the federal government did not provide direct support to small businesses; GFC-era programs focused on providing [market liquidity](#) and on maintaining financial institution solvency. Because of this, most funds went to large, mostly financial, institutions. The majority of funds were disbursed through Federal Reserve programs (and all of which were repaid).

However, oversight committees and observers criticized the Fed during the GFC for disparate treatment of some borrowers, refusing to reveal details of loans -- including borrower identities -- and the absence of written guidance for its loan procedures. Overall, these perceived weaknesses threatened taxpayer acceptance and generated suspicion of the Fed and the programs, despite their arguable success in preserving financial stability. In 2010, through [the Dodd-Frank Act](#), Congress required the Fed to publish transaction data one year after closing an emergency facility; the Fed’s current practices go beyond this requirement.

[Signed into law](#) on October 3, 2008, the other major government intervention during the GFC, Treasury’s Troubled Asset Relief Program (TARP), primarily [funded](#) loans to, and investments in, financial institutions and car manufacturers -- institutions with significant experience in financial compliance. Of the [\\$443.9 billion](#) spent under TARP, only \$368 million was [allocated](#) to small businesses outside the financial sector. Similar to PPP, the federal government’s primary recourse against the financial risks of TARP was audits, fines, and litigation. The Special Inspector General for the TARP launched [criminal investigations](#) that succeeded in recouping monies from TARP recipients that had used the funds as part of accounting and securities fraud schemes (p.7).

But what worked during the GFC may not work for the PPP (or for other COVID-19 programs) due to the difference in borrower sizes. Litigation against the 86% of PPP borrowers that sought



less than \$150,000 would likely cost more than forgiving the disputed loan. These policy choices demonstrate the altered cost-benefit calculus of crisis oversight.

While greater loan underwriting and other pre-disbursement policies carry less risk, they are commensurately slower. The SBA leaned towards speed in the current situation, a position approved by some. Senator Rubio said at the June 10 hearing that, “the speed of the lockdown meant we needed to get funds to small businesses with urgency,” and speculated that, “without PPP’s temporary lifeline, tens of millions of Americans would have been permanently separated from their livelihoods and stripped of dignified work.” Several other members agreed with him. However, the June PRAC report explored this tension between speed and integrity, noting that “increased loan volume, loan amounts, and expedited loan processing timeframes may make it more difficult for SBA to identify red flags” (p. 41).

The minority of TARP funds that touched homeowners and small businesses can be useful in understanding what might have happened. Then, the [Home Affordable Modification Program](#) was encumbered by embedded oversight mechanisms that effectively reduced risk but also reduced coordination, accessibility, speed, and, hence, efficacy. Requiring only limited loan underwriting, as the Treasury and SBA have functionally done, has arguably allowed the agencies to distribute PPP loans before businesses go bankrupt.

However, it can also be argued that the SBA’s reliance on self-certifications, coupled with less stringent forgiveness criteria, and a limited audit processes, have potentially produced a program far from its original statutory intent. Despite the SBA’s heroic effort to process thousands of loans in a very short time period, which must be acknowledged, this type of confused administration is not likely to engender confidence in taxpayers that their money has been well-spent.

### **Major PPP Oversight Bodies**

As alluded to in the discussion above, at least seven oversight bodies have responsibility for reviewing the PPP. The CARES Act established two oversight bodies. The Pandemic Response Accountability Committee (PRAC), composed of [20 standing federal inspectors general](#) (IGs), is charged to “prevent and detect fraud, waste, abuse, and mismanagement” in all CARES Act-funded disbursements and guarantees to non-federal organizations. The SBA IG is part of this group. Soon to be added to the PRAC roster is the Special Inspector General for the Pandemic Response (SIGPR), tasked under [Section 4018\(c\)\(1\)](#) of the CARES Act with tracking and evaluating loans and loan guarantees made by the Department of Treasury.

Also overseeing the PPP are the Government Accountability Office, the House of Representatives’ ad hoc [Select Subcommittee on the Coronavirus Crisis, and the standing](#) Senate and House committees on small business.

**Figure 3.** Newly-created PPP Oversight Bodies

	Pandemic Response Accountability Commission (PRAC)	Special Inspector General for Pandemic Recovery (SIGPR)	House Select Subcommittee on the Coronavirus Crisis
Date established	March 27, 2020	March 27, 2020	April 23, 2020
Containing body	Council of the Inspectors General on Integrity & Efficiency	Department of Treasury	House Committee on Oversight & Reform
Scope	Funds disbursed to non-Federal entities used to address the coronavirus crisis	Treasury disbursements via CARES Act programs	“taxpayer funds and relief programs to address the coronavirus crisis”
Basis of authority	<a href="#">H.R. 748 Sec. 15010</a>	<a href="#">H.R. 748 Sec. 4018</a>	<a href="#">H.Res. 935</a>
Mandate	“prevent and detect fraud, waste, abuse, and mismanagement; and mitigate major risks that cut across program and agency boundaries”	“conduct [...] audits and investigations of the making, purchase, management, and sale of loans, loan guarantees, and other investments”	report on: efficacy, fraud, and efficiency of federal response; national preparedness; economic and health impacts; cooperation between federal branches and investigators
Funding	\$80,000,000	\$25,000,000	\$2,000,000
Report schedule	Biannually	Quarterly	As needed
Chair	Michael Horowitz	Brian Miller	James Clyburn (D-SC)
Can subpoena?	Yes		
Termination date	September 30, 2025	March 27, 2025	30 days after final report