

U.S. Insight: Chapter 11 Debtors Excluded from SBA Loan Program during the COVID-19 (Coronavirus) Pandemic?

The widespread coronavirus has largely slowed economic activity across the globe. As many businesses weigh their options to navigate through this economic downturn, the prospect of bankruptcy protection rapidly becomes a consideration. In order to counteract the secondary economic effects of COVID-19, the federal government passed the CARES Act (the “Act”) to bridge the gap for companies teetering on the edge of insolvency. Notably, the Small Business Administration (the “SBA”) assumed the role of providing loans to qualifying companies pursuant to the Paycheck Protection Program (“PPP Loans”).

PPP Loan Qualifications Tightened by SBA

On April 24, 2020, the SBA tightened the qualifications required to obtain approval for PPP Loans by releasing an interim rule that clarified: “[i]f the applicant or the owner of the applicant is the debtor in a bankruptcy proceeding, either at the time it submits the application or at any time before the loan is disbursed, the applicant is ineligible to receive a PPP loan.”

Thus, it appears that the U.S. government is definitively not providing PPP Loan assistance to chapter 11 debtors. Further, the rule states, “[i]f the applicant or the owner of the applicant becomes the debtor in a bankruptcy proceeding after submitting a PPP application but before the loan is disbursed, it is the applicant’s obligation to notify the lender and request cancellation of the application.” This solidifies the notion that the SBA does not support loans to chapter 11 debtors.

The bar on companies already involved in chapter 11 may uproot their plans to weather this economic downturn. For example, Hidalgo County Emergency Service Foundation, an emergency medical services company based in southern Texas that filed for chapter 11 protection on October 8, 2019 (“Hidalgo”) (Case No. 19-20497 (Bankr. S.D. Tex.)), is relying on PPP Loan funding in order to continue paying its employees and running its business; a common struggle many U.S. companies are facing during the coronavirus pandemic and the resulting adverse effect on the economy. The security that this loan offers is under threat by the SBA. In response, Hidalgo and others retaliated.

Chapter 11 Debtors Challenge the SBA

Hidalgo recently obtained a temporary restraining order against the SBA. This effectively nullified the language on the PPP Loan application asking “[i]s the Applicant or any owner of the Applicant . . . presently involved in any bankruptcy?” Pursuant to

the Bankruptcy Court's order, Hidalgo was given a second opportunity to apply for and procure the PPP Loan. In an analogous case, on April 28, 2020, Cosi, Inc. filed a motion for a temporary restraining order requesting, among other things, an injunction against the SBA following its denial of relief under the Act. An expedited hearing is set to be heard in the Bankruptcy Court for the District of Delaware on April 30, 2020. Similarly, Ravn Air Group Inc., an Alaskan airline that filed for chapter 11 protection on April 5, 2020, structured much of its plan of reorganization around obtaining debtor-in-possession financing pursuant to the Act, but was denied the loan and filed a chapter 11 plan of liquidation on April 27, 2020.

The future remains uncertain for chapter 11 debtors, but the SBA's recent bankruptcy bar highlights the importance of hiring professional and knowledgeable bankruptcy lawyers to best navigate companies, such as Hidalgo, Cosi and Ravn Air Group, through insolvency both in and out of chapter 11.

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Please feel free to contact Curtis' Restructuring and Insolvency partners if you have any questions on this important development:



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