THE IGNOMINIOUS LIFE OF THE PAYCHECK PROTECTION PROGRAM

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The COVID-19 pandemic gravely endangers the health of millions of Americans. Private and public safety measures adopted to reduce infection, however, are also a source of existential risk. As U.S. infection rates increased in early March 2020, unemployment and business dislocation surged. The bipartisan Coronavirus Aid, Relief, and Economic Security Act (CARES Act) represents the first and largest federal attempt to manage economic fallout from the pandemic. The Paycheck Protection Program (PPP) is a lynchpin of the CARES Act. The PPP seeks to mitigate unemployment and closures in several vulnerable sectors of the economy including among tens of millions of small businesses, not-for-profits, and self-employed individuals. The PPP has disbursed over $500 billion to these sectors, providing a lifeline to millions of employees. Nevertheless, media, lawmakers and economists have criticized the PPP for inefficiently or inequitably distributing funds. This Article is the first work of legal scholarship that explains and examines the PPP. As a case study, this Article also provides insight into the design of economic interventions and their limitations, as well as how the lawmaking process generates a narrative allocating responsibility for social trauma.

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I.
INTRODUCTION

The challenges that COVID-19 poses for lawmakers seeking to reduce economic dislocation from the pandemic are unprecedented in two respects.[1] First, downturns are typically linked to shocks coursing into the economy through specific channels, such as spikes in oil prices, deterioration of real estate markets, or increases in interest rates.[2] When disruption flows into the economy through a discrete channel, interventions may be more targeted and less costly. In contrast, the current decline stems from ubiquitous vulnerability to viral infection, which implicates a broad gamut of social and economic in-person interactions. Second, unlike prior downturns, this one has its origins in natural phenomena rather than an asset bubble, macroeconomic policy, war, or other consequences of human decision-making. The magnitude and complexity of the crisis pose grave challenges for policymakers. But human disinvolvement from creation of the crisis poses a unique challenge for politicians, who have to define their intervention to constituents seeking to parse traumatic events in crisp moral terms.

The bipartisan Coronavirus Aid, Relief, and Economic Security Act (CARES Act) represents the federal government's initial, massive response to COVID-19. The CARES Act provides over two trillion dollars in economic support. This Article addresses the Paycheck Protection Program (PPP) component of the CARES Act, which seeks to allay payroll losses and dislocation among small businesses, not-for-profits, self-employed individuals,[3] tribal business concerns, veterans' organizations and certain food and hospitality businesses. Under the CARES Act, the PPP allocated $349 billion to support these sectors in

1. MICHAEL H. CECIRE, CONG. RES. SERV., IN11228, COVID-19: FEDERAL ECONOMIC DEVELOPMENT TOOLS AND POTENTIAL RESPONSES 10 (2020) (noting challenges in developing programs to support businesses in the circumstances of a nationwide pandemic); Zachary Warmbrodt, *Trump Signs Revamp of Small Business Aid Into Law but Problems Loom,* POLITICO (June 5, 2020, 12:22 PM), https://www.politico.com/news/2020/06/05/trump-signs-small-business-aid-revamp-303316 ("But the new law is by no means the last major change in store for the program, which has been subject to an evolving set of rules since the Small Business Administration and Treasury Department hurriedly launched it on April 3.").

2. This is not true of natural disasters such as wildfires, hurricanes and earthquakes; however, these are localized rather than national and thus do not lead to losses of comparable magnitude.

3. For brevity, the term "self-employed" includes sole proprietors and independent contractors.

the form of loans, which are generally eligible for forgiveness.[4] As of July 2020, the PPP had financed over 4.8 million small businesses and other organizations.[5] Notwithstanding its broad uptake, the program's implementation generated a barrage of criticism from lawmakers, the press and some economists.[6]

This Article is the first legal scholarship to explain and examine the PPP. As a case study, this Article also provides insight into the design of economic interventions and their limitations as well as how the lawmaking process generates a narrative allocating responsibility for social trauma. Prior policy responses to economic crises had the benefit of identifiable human contributors (e.g., militant foreign powers, Wall Street bankers, policy wonks setting interest rates), with debate then ensuing over the extent of these contributors' responsibility.[7] The unique nature of the current crisis, however, provides a relatively ahuman backdrop for the lawmaking process, thus allowing its artificial, narrative-building function to come into relief.

The remainder of this Article is divided into five parts. Part II discusses populist lawmaking to provide a framework for assessing responses to the PPP. Part III provides background on the economic impact of COVID-19 as Congress was drafting the CARES Act. Part IV narrates the initial implementation of the PPP. Part V explores and responds to common criticisms of the PPP. Part VI concludes.

Two themes recur in Parts IV and V. First, the messy conclusion to the first round of PPP funding resulted from the program's inadequate funding, broad qualification standards, and decentralized design.

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4. An additional $310 billion were allocated to the PPP under the Paycheck Protection Program and Health Care Enhancement Act (the "Enhancement Act") discussed below.

5. Press Release, U.S. Dep't of the Treas., SBA and Treasury Announce Release of Paycheck Protection Program Loan Data (July 6, 2020), https://home.treasury.gov/policy-issues/cares-act/assistance-for-small-businesses/sba-paycheck-protection-program-loan-level-data.

6. Jonathan O'Connell, Jeanne Whalen, Jeff Stein & Erica Werner, *Following Messy Start, Enormous Paycheck Protection Program Shows Signs of Buttressing Economy*, WASH. POST (June 10, 2020, 8:13 AM), https://www.washingtonpost.com/business/2020/06/09/how-effective-is-ppp-small-business/ ("[After] igniting a public firestorm that outraged tens of thousands of business owners . . . the PPP has directed more than $530 billion to 4.5 million companies, and economists, business leaders, White House officials and lawmakers from both parties think it helped stabilize the economy.").

7. *See* Howell E. Jackson & Steven L. Schwarcz, *Protecting Financial Stability: Lessons from the Coronavirus Pandemic*, HARV. BUS. L. REV. (forthcoming 2021) ("The root cause of the last financial crisis was a pattern of errors in prior market expectations about the capacity of individual borrowers to sustain mortgage payments and the sustainability of continuously rising housing prices.").

Second, lawmakers and media exploited program failings in building a populist narrative. Criticisms of the program have in many cases missed the mark, blaming program participants (i.e., lenders and borrowers) for outcomes that were caused largely by the design of the program. This Article, however, does not train its sights on the design of the PPP. Although noting where the architecture of the PPP could have been improved, this Article contends that there simply were not well-developed policy tools available to lawmakers in March 2020 for efficiently staunching the torrent of unemployment claims. Where lawmakers did fall short, however, was in reacting to the program's shortfalls with populist pandering. This pandering was visible in Congressional and agency rhetoric, as well as enforcement and oversight reactions to the program's perceived performance.[8]

II.
Populist Lawmaking

Populist policies contrast with policies favoring elite interests as well as policies reflecting experts' prescriptions.[9] The distinction between elitist policies (i.e., policies favoring those at the top of a social power structure, such as regressive tax cuts) and expert policies (i.e., policies designed to maximize aggregate social welfare without favoring particular sub-groups) is significant.[10] For purposes of this Article,

8. Lawmaking and policymaking, in this Article, refer not only to the writing of statutes and regulations but also softer or more tacit exercises of power, such as press releases, policy statements, setting of enforcement priorities, and information collection for supervisory purposes. When a lawmaker acts through any of these channels, regulated parties may adjust their behavior whether to avoid reputation risk, to react to (perceived) enforcement risk, or simply to align themselves with lawmakers.

9. In practice, there may be overlap between distrust of experts and antipathy to elites. The great majority of voters do not engage in sophisticated analysis before forming opinions as to whether a policy represents a fair, omnibus compromise or represents the results of experts catering to elite interests. In the absence of a well-informed opinion, voters may resort to general skepticism and an insistence on their own interests being reflected in lawmaking. Thus, populist hostility to expert policy may represent the results of a second-best heuristic that opts to over- rather than under-advocate in the absence of discernible first-best solutions. In that regard, Professor Edward Glaeser identifies "the twin political risks of subversion, where private companies capture policy [i.e., capture of policies by elites through corruption or otherwise] . . . and political favoritism, where public leaders use government policy to pursue their own pet objectives, such as populism." Edward L. Glaeser, *The Political Risks of Fighting Market Failures: Subversion, Populism and the Government Sponsored Enterprises*, 4 J. Legal Analysis 41, 42 (2012).

10. *See* Mark J. Roe, *A Political Theory of American Corporate Finance*, 91 Colum. L. Rev. 10, 33 (1991) ("populism . . . refer[s] to a widespread attitude that large institutions and central accumulations of economic power are inherently undesirable and should be reduced, even if the concentration serves a useful productive function."); Cass R. Sunstein, *The Laws of Fear*, 115 Harv. L. Rev. 1119, 1120 (2002)

"populist" policies refer to those that differ from expert policies, leaving aside difficult debates as to how policy impacts on individuals should be measured and aggregated.[11] Within this frame, it became meaningful to label and criticize lawmaking as "populist" around the turn of the twentieth century when policy analysis by economists and others became professionalized.[12]

Populism has surged across the globe, perhaps most notably with the election of Donald Trump in the United States.[13] Globalism and rising inequality, as well as economic and social changes, have unleashed a groundswell of discontent. In parallel, digital media has increasingly enabled laypersons to express their view-points, leading to unfiltered democratization of (dis)information. Populism, however,

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(reviewing PAUL SLOVIC, THE PERCEPTION OF RISK (2000)) ("Good technocrats emphasize that ordinary people are frequently ill-informed and urge that the task of regulators is to follow science and evidence, not popular opinion."). Populism shapes law beyond financial and business-related subjects, as explained in a wide array of scholarship from political scientists and others; *see also* Tomasz Tadeusz Koncewicz, *Understanding the Politics of Resentment: Of the Principles, Institutions, Counter-Strategies, Normative Change, and the Habits of Heart*, 26 IND. J. GLOBAL LEGAL STUD. 501, 507–08 (2019) (discussing how resentment shapes populist policies). *See generally* Elizabeth Garrett, *Money, Agenda Setting, and Direct Democracy*, 77 TEX. L. REV. 1845 (1999); JAN-WERNER MULLER, WHAT IS POPULISM? (Penguin Books 2016); ERNESTO LACLAU, ON POPULIST REASON (Verso Books 2005); ELISABETH GERBER, THE POPULIST PARADOX: INTEREST GROUP INFLUENCE AND THE PROMISE OF DIRECT LEGISLATION (Princeton Univ. Press 1999).

11. For a general defense of welfarist approaches to policymaking, see Louis Kaplow & Steven Shavell, *Any Non-Welfarist Method of Policy Assessment Violates the Pareto Principle*, 109 J. POL. ECON. 281 (2001).

12. Ajay K. Mehrotra, *"Render Unto Caesar . . .": Religion/Ethics, Expertise, and the Historical Underpinnings of the Modern American Tax System*, 40 LOY. U. CHI. L.J. 321, 360–65 (2009) (examining how a professional group of policy-makers and analysts emerged at the turn of the twentieth century thereby distinguishing populist from elite views of lawmaking). *See, e.g.*, Robert Rabin, *Federal Regulation in Historical Perspective*, 38 STAN. L. REV. 1189, 1205–06 (1986) (discussing populist discontents in the late 1800s calling for the regulation of railroads and other government interventions into the economy). Arguably, prior to the formation of a professional class of policy experts, judges (especially those with lifetime or other protracted appointments) were the primary body assessing and tailoring legislation to improve its social consequences.

13. Martin Loughlin, *The Contemporary Crisis of Constitutional Democracy*, 39 OXFORD J. LEGAL STUD. 435, 444 (2019) ("Claiming to express the authentic voice of the people, populists are critical of constitutional devices that filter majority views through such institutional sieves as electoral colleges, unelected second chambers, expert commissions, judicial scrutiny mechanisms and transnational networks.").

has shaped policy for decades across diverse areas such as antitrust,[14] tax,[15] banking,[16] executive compensation,[17] securities and business

14. *See*, *e.g.*, Joshua Wright & Aurelien Portuese, *Antitrust Populism: Towards a Taxonomy*, 25 STAN. J. L. BUS. & FIN. 131, 134 (2020) ("[A]ntitrust populism entails both the rejection of rigorous economic analysis in favor of politically-driven competition enforcement, as well as suspicion of the role of experts and independent agencies on antitrust matters."); Timothy J. Muris & Jonathan E. Nuechterlein, *Chicago and Its Discontents*, 87 U. CHI. L. REV. 495, 498 (2020) ("populist[s] . . . dispense with consumer welfare as the primary focus of antitrust [and] have no clear conceptual objectives other than reining in large global companies that displace smaller, more local, and less efficient companies"); William E. Kovacic, *The Chicago Obsession in the Interpretation of US Antitrust History*, 87 U. CHI. L. REV. 459, 473 (2020) (responding to critiques of "populist" theories of antitrust law); Barak Orbach, *Antitrust Populism*, 14 N.Y.U. J. L. & BUS. 1, 6 (2017) ("The essence of populism is an effort to disrupt the existing social order by solidifying and mobilizing the animosity of 'the people' against the 'corrupt elites' and the 'establishment.'"); Robert Skitol, *The Shifting Sands of Antitrust Policy: Where It Has Been, Where It Is Now, Where It Will Be in Its Third Century*, 9 CORNELL J. L. & PUB. POL'Y 239, 244, 248 (1999) (comparing "populist" and "Chicago" schools of antitrust analysis); Brent W. Huber, *Target Corporations, Hostile Horizontal Takeovers and Antitrust Injury Under Section 16 of the Clayton Act After Cargill*, 66 IND. L.J. 625, 631–32 (1991) ("[S]cholars have labeled these non-economic goals 'populist' because they are concerned primarily with concentrations of wealth and power rather than the efficient allocation of resources.").

15. *See*, *e.g.*, Arthur J. Cockfield, *Shaping International Tax Law and Policy in Challenging Times*, 54 STAN. J. INT'L L. 223, 236–38 (2018) (discussing how populism complicates international tax cooperation and how disclosures of elite tax avoidance support populist distrust); Erik M. Jensen, *The Taxing Power, The Sixteenth Amendment, and the Meaning of Incomes*, 33 ARIZ. ST. L.J. 1057, 1098–1102 (2001) (discussing populist pressures the income tax satisfied); Steven A. Bank, *Origins of a Flat Tax*, 73 DENV. U. L. REV. 329, 339 n.60 (1996) ("The populist movement is an example of the view that the government and the rich conspire against the poor in times of great disparity causing the poor to become desperate and threaten violence."); Jennifer Arlen & Deborah M. Weiss, *A Political Theory of Corporate Taxation*, 105 YALE L.J. 325, 331–32 (1995) (examining whether popular misconceptions of corporations may explain double taxation). *See generally* Meredith R. Conway, *Money, It's a Crime: Share It Fairly, but Don't Take a Slice of My Pie!: The Legislative Case for the Progressive Income Tax*, 39 J. LEGIS. 119 (2015) (discussing how realities and perceptions of a progressive income tax have been used to mollify popular discontent).

16. Federico Lupo-Pasini, *The Rise of Nationalism in International Finance: The Perennial Lure of Populism in International Financial Relations*, 30 DUKE J. COMP. & INT'L L. 93, 138–39 (2019) (discussing tension between populists and technocrats, particularly with respect to central bank governance); Andra Ghent, *How Do Case Law and Statute Differ? Lessons from the Evolution of Mortgage Law*, 57 J. L. & ECON. 1085, 1116 (2014) (finding that courts tend to be less receptive to populist pressure than legislators in the context of mortgage law); Gyung-Ho Jeong, Gary J. Miller & Andrew C. Sobel, *Political Compromise and Bureaucratic Structure: The Political Origins of the Federal Reserve System*, 25 J. L. ECON. & ORG. 472, 493 (2008) (examining how negotiation between interest groups created a Federal Reserve that was insulated from democratic accountability); Clark Hildabrand, Note, *The Geographic (Un)representativeness of the Federal Reserve Board of Governors*, 34 YALE

law.[18]

Professors Jacob Gersen and Matthew Stephenson model potential adverse effects of populism using a framework of "over-accountability."[19] Casting citizens as principals and politicians as agents,[20]

L. & POL'Y REV. 155, 163 (2015) (discussing how regional interests negotiated between more and less inflationary structures for the Federal Reserve).

17. Omari S. Simmons, *Taking the Blue Pill: The Imponderable Impact of Executive Compensation Reform*, 62 S.M.U. L. REV. 299, 306 (2009) ("For lawmakers, the matrix of executive compensation reforms operates like a blue pill, keeping corporate constituencies, especially populist groups, in a state of blissful ignorance, foregoing a deeper analysis that reveals the reality of lawmaker opportunism and manipulation."); William W. Bratton, Book Note, *The Tournament over Executive Compensation* 93 CALIF. L. REV. 1557, 1577–88 (2005) (reviewing LUCIAN BEBCHUK & JESSE FRIED, PAY WITHOUT PERFORMANCE: THE UNFULFILLED PROMISE OF EXECUTIVE COMPENSATION (2004)) (exploring risk of populist intervention in the area of executive compensation); Paul Mahoney, *The Origins of the Blue-Sky Laws: A Test of Competing Hypotheses*, 46 J. L. & ECON. 229, 237 (2003) ("The Populist movement as a formal political program was dead by the time of the blue-sky laws[; h]owever, populist rhetoric and ideas—particularly the antipathy to financiers that predated the Populist movement—survived in agricultural areas."); Kevin J. Murphy, *Politics, Economics, and Executive Compensation*, 63 U. CIN. L. REV. 713, 727 (1995) (examining how lawmakers propose legislation reflecting populist discontent with executive compensation).

18. Stephen Bainbridge, *Corporate Purpose in a Populist Era*, 98 NEB. L. REV. 543, 547 n.17 (2020) (discussing definitions of populism, and adapting the definition that Mark Roe developed, namely, that populism is the "widespread attitude that large institutions and accumulations of centralized economic power are inherently undesirable and should be reduced, even if concentration is productive"); Camden Hutchison, *Progressive Era Conceptions of the Corporation and the Failure of the Federal Chartering Movement*, 2017 COLUM. BUS. L. REV. 1017, 1032–39 (2017) ("As a general matter, anti-corporate populists were often vague in explaining the benefits of their proposals, which often entailed unacknowledged conflicts between the economic interests of consumers and investors."); Stephen Bainbridge, *Dodd-Frank: Quack Federal Corporate Governance Round II*, 95 MINN. L. REV. 1779, 1785–86 (2011) (explaining how economic and financial crises lead to federal interventions in corporate law that reflect popular outrage instead of measured policy analysis); Christopher M. Bruner, *Corporate Governance Reform in a Time of Crisis*, 36 IOWA J. CORP. L. 309, 333 (2011) (explaining that "the emergence of so thoroughly shareholder-centric a set of [reform] proposals in the wake of the [2008] crisis is best understood as one reflection of a much broader populist backlash against managers"); Marcel Kahan & Edward Rock, *Symbiotic Federalism and the Structure of Corporate Law*, 58 VAND. L. REV. 1573, 1588–1589 (2005) (discussing how Delaware's preeminent position in setting corporate governance standards is at risk from post-scandal or crisis populist pressure to federalize corporate law). *See generally* MARK J. ROE, STRONG MANAGERS, WEAK OWNERS (1994); Robert A. Prentice & David B. Spence, *Sarbanes-Oxley as Quack Corporate Governance: How Wise is the Received Wisdom?*, 95 GEO. L.J. 1843 (2007); Roberta Romano, *The Sarbanes-Oxley Act and the Making of Quack Corporate Governance*, 114 YALE L.J. 1521 (2005).

19. Jacob E. Gersen & Matthew C. Stephenson, *Over-Accountability*, 6 J. LEGAL ANALYSIS 185 (2014) [hereinafter *Over-Accountability*]. The article claims that problems of over-accountability do not necessarily stem from principals' irrationality. However, many of the examples discussed in the article rely on bounded rationality in

Gersen and Stephenson analyze dynamics where increasing political accountability may lead to undesirable policy results.[21] Traditional views of political action and popular instincts view politicians as lacking sufficient accountability to the population they govern. In contrast, Gersen and Stephenson demonstrate that there are a range of undesirable behaviors that may arise from *too much* accountability:

> [P]rincipals [i.e., voters] are at an informational disadvantage relative to their agents [i.e., elected politicians] in two respects. First, . . . agents have better information about the likely consequences of different courses of action . . . . Even after a decision is made, the principal may be unsure whether the agent did the right thing. . . . Second, the principals are often uncertain about their agents' preferences and abilities. In the conventional political economy jargon, they are uncertain as to each agent's "type," where "type" is a catchall term that might include a variety of relevant characteristics including values, motivations, and competence at predicting consequences and implementing policies effectively. All else equal, a rational principal will prefer an agent who is a better type. . . . The action which a perfectly-informed principal would want the agent to take is not necessarily the action that would most effectively convince imperfectly-informed principals that the agent is a good type.[22]

Gersen and Stephenson's analysis formalizes when politicians may choose suboptimal policies to cater to under-informed voters, including several scenarios where over-accountability leads to the selection of a policy based on the relative popularity of sub-groups. Inter alia, the model explains why politicians may choose to pander to the populace with policies that serve to demonstrate that the politicians are not captured by elite interests at the expense of foregoing optimal policy choices.[23]

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the form of principal irrationality or absence of means to credibly transmit information from agents to principals. Thus, the paper presents a model where principals exhibit failings due to relative inexpertise in understanding optimal policy choices ex ante and judging their agents' decisions ex post*; see also* Lars Frisell, *A Theory of Self-Fulfilling Political Expectations*, 93 J. PUB. ECON. 715, 716–17 (2009) (providing a model of how voter distrust may lead to populist governments).

20. For earlier work from economics developing the principal agent model, see, for example, Stephen Ross, *The Economic Theory of Agency: The Principal's Problem*, 63 ECON. REV. 134 (1973).

21. *Over-Accountability*, *supra* note 19, at 186 ("[A]ccountability also has a dark side . . . . recent work in political economy has identified and elucidated an important class of situations in which effective accountability mechanisms can decrease, rather than increase, an agent's likelihood of acting in her principal's interests").

22. *Id.* at 190–191.

23. *Id.* at 188.

As further developed below, the PPP provides a rarely clean environment for isolating populist strains in lawmaking. In the typical case where human conduct (rather than a virus) precipitates an economic crisis, policies addressing the resulting trauma also represent judgment calls that attribute blame across groups of involved individuals. Numerous examples may be drawn from the preceding few decades, such as the savings and loan crisis, the Dot Com bubble bursting, the 9/11 terrorist attacks, and the 2008 financial crisis. Reasonable onlookers may debate whether policy responses to these events identified appropriate transgressors and to what extent the policy responses accurately apportioned blame. Because of this space for debate, it is generally difficult to determine whether punitive aspects of interventions represent, on the one hand, well-calibrated means for acknowledging the harm that was inflicted or threatened by the transgressors, or on the other hand, populist strategies where lawmakers excessively flog culpable decision-makers to demonstrate an uncorrupt allegiance to the masses.

COVID-19, however, did not stem from human misconduct and its devastating impact on the economy—especially among smaller enterprises—is not plausibly attributable to misconduct by elites. In analyzing the implementation of the PPP and various lawmakers' subsequent castigation of large businesses and other elite bodies involved in the program, this Article reveals top-down strategies by members of Congress and agency officials that power a populist narrative. Evidence of professionalized scapegoating surfaced in this Article, in turn, provides basis for a broader skepticism of the good faith and independence of politicians and political appointees.[24]

III.
Economic Background

In the pandemic's initial phase, COVID-19 threatened supply chains and exports to the extent the U.S. economy interacted with China and other affected regions.[25] The domestic economy significantly slowed as the risk of infection within the U.S. grew. Concerns

24. *See generally* David E. Pozen, *Constitutional Bad Faith*, 129 Harv. L. Rev. 885 (2016); Cass R. Sunstein, David Schkade, Lisa M. Ellman & Andres Sawicki, Are Judges Political?: An Empirical Analysis of the Federal Judiciary (2006).

25. James K. Jackson, Andres B. Schwarzenberg, Martin A. Weiss, & Rebecca M. Nelson, Cong. Res. Serv., R46270, Global Economic Effects of COVID-19 10 (2020) [hereinafter, CRS, Global Economic Effects]. ("The drop in economic activity, initially in China, has had international repercussions as firms experienced delays in supplies of intermediate and finished goods through supply

with contagion drove private as well as public actors to adopt measures curtailing in-person interactions. These responses impacted business activity, with severity varying across industries and regions.[26] For example, customers avoided cruises, airlines, restaurants, and entertainment venues where patronage involved mixing with potentially infectious strangers. As travel declined, hospitality and related industries were also hit hard (e.g., hotels, travel agencies). Expectations of decreased transportation, production, and other economic activity led to a rout in energy markets, with oil prices collapsing.[27] Manufacturing facilities were closed to reduce infection risk, with General Motors, Ford and Fiat Chrysler temporarily shutting down U.S. facilities.[28] Other industries, such as financial services, technology companies, and resource extraction, however, were less affected, and some businesses were even buoyed in the drastically changed circumstances.[29]

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chains."). For example, looking back on its fiscal quarter ending on March 28, 2020, Apple explained:

> During February 2020, following the initial outbreak of the virus in China, [Apple] experienced disruptions to its manufacturing, supply chain and logistical services provided by outsourcing partners, resulting in temporary iPhone supply shortages that affected sales worldwide. Also, the Company's sales of its products in China were adversely affected as public health measures and other actions to curb the spread of the virus, including the temporary closure of [Apple's] retail stores and channel partner points of sale, were put in place.

Apple Inc., Quarterly Report (Form 10-Q) at 25 (April 30, 2020).

26. CRS, Global Economic Effects at 45 ("A decline in economic activity of 30% or more was recorded in motor vehicles and parts, recreation, food services and accommodation and transportation sectors, reflecting the quarantine measures adopted across the country. In contrast to the other sectors of the economy, food and beverage consumption increased by 25% as a result of the switch by individuals from eating at restaurants and other commercial food service establishments to preparing and eating food at home.").

27. Brian Sullivan, *Oil Prices Could Go Negative Again for Reasons Beyond Just Storage*, CNBC (Apr. 28, 2020, 8:30 AM), https://www.cnbc.com/2020/04/28/oil-prices-could-go-negative-again-for-reasons-beyond-just-storage.html [https://perma.cc/24JU-C7MF].

28. Phil LeBeau & Noah Higgins-Dunn, *General Motors, Ford and Fiat Chrysler to Temporarily Close All US Factories Due to the Coronavirus*, CNBC (Mar. 18, 2020, 4:56 PM), https://www.cnbc.com/2020/03/18/general-motors-ford-and-fiat-chrysler-to-close-all-us-factories-due-to-the-coronavirus-sources-say.html [https://perma.cc/72ZH-3MYA].

29. Many financial services firms recognized anticipatory losses on their credit portfolios. And across industries, non-essential workers typically stayed at home until health measures lifted. Relatedly, the designation of "essential" businesses required necessarily somewhat arbitrary and imprecise line drawing, leading to political frictions. *See* Marisa Fernandez and Courtenay Brown, *The Randomness of "Essential" Businesses*, Axios (Apr. 20, 2020), https://www.axios.com/coronavirus-essential-businesses-22e0edfc-d838-4c2a-81eb-9fb81303ee13.html.

The impact of health measures on the nation's economy became severe by early to mid-March, particularly due to the uncertainty gripping medium- to long-term planning. As recognized in releases implementing the PPP, small businesses were heavily affected:

> With the COVID-19 emergency, many small businesses nationwide are experiencing economic hardship as a direct result of the . . . health measures that are being taken to minimize the public's exposure to the virus. These measures, some of which are government mandated, are being implemented nationwide and include the closures of restaurants, bars, and gyms. In addition, based on the advice of public health officials, other measures, such as keeping a safe distance from others or even stay-at-home orders, are being implemented, resulting in a dramatic decrease in economic activity as the public avoids malls, retail stores, and other businesses.[30]

Not just the closure of businesses or their emptying due to concerns for employee and customer welfare posed existential challenges. As employment collapsed and spending slowed, the strength of the overall economy came into question due to expected lower business revenues over the medium term.[31] Furthermore, uncertainty related to potential availability of vaccines and treatments as well as future waves of infection and responses thereto made business planning diffi-

30. Business Loan Program Temporary Changes; Paycheck Protection Program, 85 Fed. Reg. 20,817 (Apr. 15, 2020) (to be codified at 13 C.F.R. pt. 121) [hereinafter Affiliates Rule].

31. Contemporaneous estimates indicate that the pandemic and related health policies may reduce global growth by a staggering two percent per month while conditions persist, with deeper impacts on global trade. CRS, GLOBAL ECONOMIC EFFECTS, *supra* note 25. More importantly, analysis fails to provide a firm basis to estimate the long-term impacts of the pandemic. *Id.* As Congressional Research Service explained:

> Initially, the economic effects of the virus were expected to be short-term supply issues as factory output fell because workers were quarantined to reduce the spread of the virus through social interaction. The drop in economic activity, initially in China, has had international repercussions as firms experienced delays in supplies of intermediate and finished goods through supply chains. Concerns are growing, however, that the virus-related supply shock is creating more prolonged and wide-ranging demand shocks as reduced activity by consumers and businesses lead to a lower rate of economic growth. As demand shocks unfold, businesses experience reduced activity and profits and potentially escalating and binding credit and liquidity constraints. While manufacturing firms are experiencing supply chain shocks, reduced consumer activity through social distancing is affecting the services sector of the economy, which accounts for two-thirds of annual U.S. economic output. In this environment, manufacturing and service firms have tended to hoard cash, which affects market liquidity. In response, central banks have lowered interest rates where possible and expanded lending facilities to provide liquidity to financial markets and to firms potentially facing insolvency.

Id. at 10.

cult. Business decisions are not made exclusively by reference to current conditions but also take expected future conditions into account. As businesses adapted plans to operate during a downturn, layoffs and other cost cutting strategies were being considered and put into place. While the extent of expected hardship varied greatly, a solid majority of U.S. businesses generally and small businesses specifically had reason to consider layoffs, furloughs, salary reductions and other measures to reduce compensation expense.[32]

As unemployment claims mounted to unprecedented levels in the middle of March and stock markets sank to levels unobserved for a heady three years, the U.S. Department of Labor sent guidance to state labor agencies asking to hold unemployment claims data until Thursday, March 26, 2020.[33] In the meantime, legislative staffs and lobbyists scrambled to assemble a bailout package for affected individuals and businesses. The CARES Act passed the Senate on March 25, passed the House on March 26, and was signed into law by the 45th President on Friday, March 27. That day capped an exceptionally traumatic week in markets, as the S&P 500 slid to less than 70 percent of its highpoint in February. Figure 1 shows the S&P 500 index during the relevant period (graphed on the left axis) and initial unemployment claims (graphed on the right axis). As reflected in Figure 1, U.S. equity markets began to recover after the CARES Act passed.

32. For further discussion of the effects COVID-19 and related health measures had on the economy, see Section V.B, *infra*.

33. Veronica Stracqualursi & Annalyn Kurtz, *Trump Administration Asking States to Delay Release of Unemployment Numbers*, CNN (Mar. 20, 2020, 1:51 PM), https://www.cnn.com/2020/03/20/politics/labor-department-states-unemployment-numbers-coronavirus/index.html.

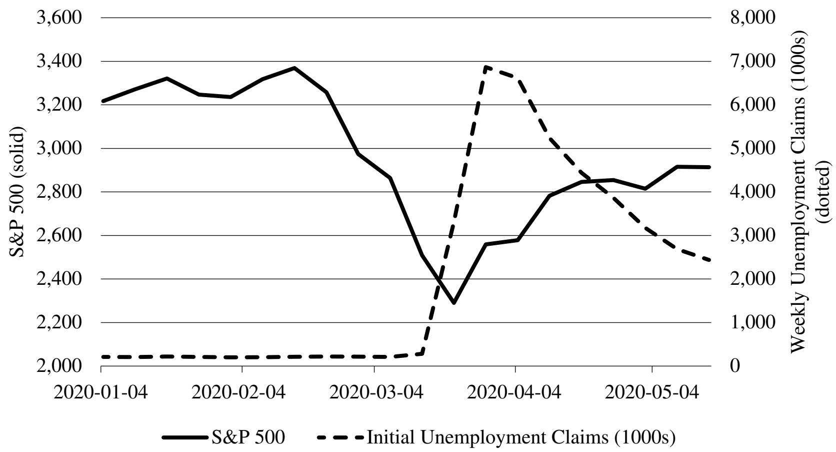

FIGURE 1: S&P 500 INDEX AND INITIAL UNEMPLOYMENT CLAIMS[34]

The bipartisan CARES Act authorized over two trillion dollars in relief to affected businesses and individuals.[35] Of that, $349 billion were allocated for making loans under the Paycheck Protection Program (PPP).[36] The PPP, as its name suggests, is aimed at reducing layoffs, furloughs and other threats to American paychecks. Notably, the PPP was not intended to support those who had been laid off or otherwise lost work due to COVID-19 related health measures. That support was provided by separate components of the CARES Act. Rather, the PPP was designed as one of several measures aimed at keeping the engines of production running while the economy idled. As discussed in more detail below, subsequent legislation increased the funding available to the program from $349 billion to $659 billion.

IV.
DESIGN AND IMPLEMENTATION OF THE PAYCHECK PROTECTION PROGRAM

As is typical when legislation is crafted, the CARES Act adapts preexisting legal machinery to achieve policy objectives. Prior to the PPP, the Small Business Administration (SBA) subsidized small business capital formation through providing a federal guarantee of private loans from banks and other lenders pursuant to Section 7 of the Small

34. Claims graphed thanks to data from FEDERAL RESERVE ECONOMIC DATA, https://fred.stlouisfed.org (last visited May 1, 2021).

35. The Federal Reserve had earlier initiated extensive measures to stabilize U.S. financial markets and signal political resolve to see the U.S. economy through.

36. CARES Act § 1107(a)(1).

Business Act.[37] The PPP grafts onto this framework, contemplating that a network of private lenders would distribute program funds among eligible participants pursuant to SBA guidance.[38]

The program is designed to be an attractive source of funding for typical enterprise expenses with a focus on payroll.[39] Under the CARES Act, PPP loans are federally guaranteed, have origination fees covered by the federal government, and most importantly, are conditionally forgivable.[40] Forgiveness entails that the loan is repaid by the federal government rather than the borrower. Rulemaking added an important feature conditioning loan availability and forgiveness on at least 75 percent of the proceeds being put towards payroll.[41]

In understanding statutory and administrative design decisions affecting the PPP, it is important to appreciate the difficult timeline and challenging working environment in which lawmakers crafted the program. The PPP was scheduled to go into effect a week from its adoption on Friday, April 3. A week is an extraordinarily brief period for the SBA to issue guidance and for lenders to adopt an underwriting process for PPP loans. Moreover, during that week, many agency and lender employees were working from home, while potentially also juggling childcare responsibilities.[42] The April 3 deadline was an ambitious goal made plausible only by the immense stakes as millions of

37. Business Loan Program Temporary Changes; Paycheck Protection Program—Revisions to Loan Forgiveness, 85 Fed. Reg. 38304, 38305 (June 26, 2020) (to be codified at 13 C.F.R. pt. 120) ("CARES Act [includes] provisions authorizing SBA to temporarily guarantee loans under a new 7(a) loan program titled the 'Paycheck Protection Program.' ").

38. For brevity, this Article refers to the SBA as administering the program although the Treasury is also involved, primarily in a consultative function.

39. Omitting some nuance, for purposes of the PPP, payroll expenses consist of compensation to U.S. employees in the form of salary, wages, commissions, or similar compensation; cash tips; payment for vacation, parental leave, family, medical or sick leave; allowance for separation or dismissal; payment for the provision of employee benefits consisting of group health coverage, including insurance premiums, and retirement; payment of state and local taxes assessed on compensation of employees. Business Loan Program Temporary Changes; Paycheck Protection Program, 85 Fed. Reg. 20811, 20813 (Apr. 15, 2020) (to be codified at 13 C.F.R. pt. 120) [hereinafter April 2 Rule].

40. Coronavirus Aid, Relief, and Economic Security Act, Pub. L. No. 116-136, § 1106, 134 Stat. 281 (2020) [hereinafter CARES Act].

41. In June, the Paycheck Protection Program Flexibility Act of 2020 (the "Flexibility Act") retroactively reduced the amount of proceeds that had to be spent on payroll from 75% to 60%. Paycheck Protection Program Flexibility Act of 2020, Pub. L. No. 116–142, 134 Stat. 641 (2020) [hereinafter Flexibility Act].

42. *See* O'Connell et al., *supra* note 6 ("Many of the Paycheck Protection Program's initial problems can be traced to its hurried creation in the frenzied days and nights of negotiation that led to the passage of the Cares Act, which was rushed together at breakneck speed to arrest the economy's sudden free-fall.").

Americans filed for unemployment. Figure 2 shows a timeline of key events in the initial rollout of the PPP.

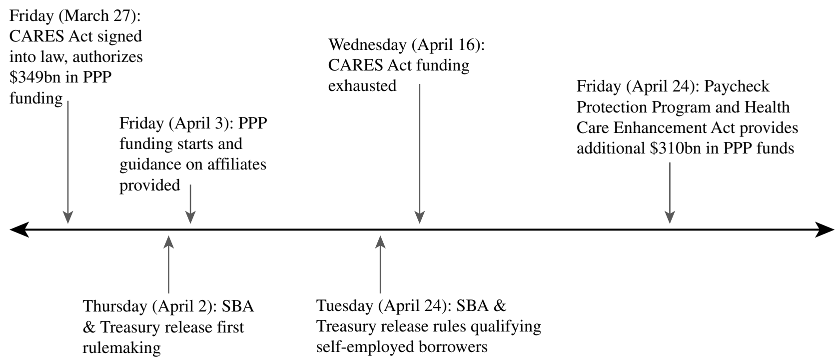

FIGURE 2: TIMELINE SHOWING PPP INITIATION[43]

Subsequent subsections develop on the timeline, discussing the implementation of the PPP in more detail.

A. *Initial SBA Rulemaking on April 2 Establishes Key Program Terms*

The SBA promulgated the first rule implementing the PPP on April 2. For brevity, this rule will be referred to as the April 2 Rule.[44] Given that borrowing under the program was due to begin a day later on April 3 and that the program was due to expire on June 30, this initial rule dispensed with both the typical notice and comment process as well as any post-publication delay in effectiveness.[45] The April 2 rule generally made the program more attractive to lenders while, perhaps inadvertently, significantly limiting larger firms from partici-

43. April 2 Rule, 85 Fed. Reg. at 20,811 (March 27); Affiliates Rule, 85 Fed. Reg. at 20,817 (April 2); Business Loan Program Temporary Changes; Paycheck Protection Program–Additional Eligibility Criteria and Requirements for Certain Pledges of Loans, 85 Fed. Reg. at 21,747 (April 14); Sarah Hansen, *The $350 Billion Small Business Loan Program Is Officially Out of Money. Lawmakers Can't Agree on What Happens Next*, FORBES (Apr. 16, 2020, 11:26 A.M.), https://www.forbes.com/sites/sarahhansen/2020/04/16/the-350-billion-small-business-loan-program-is-officially-out-of-money-lawmakers-cant-agree-on-what-happens-next (April 16); Curtis R. Hearn, William W. Horton, R. Christian Johnsen & Meredith Guthrie Maxwell, *Senate Passes Paycheck Protection Program and Health Care Enhancement Act*, NAT'L L. R. (Apr. 22, 2020), https://www.natlawreview.com/article/senate-passes-paycheck-protection-program-and-health-care-enhancement-act (April 24).

44. April 2 Rule, 85 Fed. Reg. at 20,811 (implementing Sections 1102 and 1106 of the CARES Act).

45. Section 1114 of the CARES Act authorizes issuance of regulations implementing the PPP without regard to notice requirements.

pating in the program. The remainder of this Subsection III.A discusses how the April 2 Rule sculpted the statutory terms of the PPP.

i. Lenders Exempted from Independent Diligence Efforts to Establish Borrower Qualification

This first rule had to address concerns from lenders relating to the diligence they were expected to undertake before funding PPP loans. Initially, the SBA considered tasking participating lenders not only with implementing the new, albeit simple, program in a matter of days but also independently confirming each borrower's eligibility.[46] Requiring lenders to perform independent diligence so as to confirm borrower eligibility posed four issues. First and second, eligibility for the program was a key concern for lending decisions as it impacted the availability of both the federal guarantee and federally funded loan forgiveness. Third, if a lender assisted with a fraudulent loan application, the lender could also be subject to liability alongside the borrower.[47] And fourth, many lenders were keen to avoid a diligence requirement so as not to compete in a race to the bottom. Before April 2, a contest was brewing to maximize federally funded fees from low-risk lending under the PPP. This contest would put pressure on robust underwriting standards, and some major banks decided the game would not be worth the candle if they were to race with more aggressive lenders[48] while being subject to liability for borrower-initiated

46. *See* Pete Schroeder & David Henry, *Thousands of U.S. Banks May Sit Out Small-Business Rescue Plan on Liability Worries: Sources,* REUTERS (Apr. 1, 2020, 10:43 PM), https://www.reuters.com/article/us-health-coronavirus-stimulus-banks-exc/thousands-of-u-s-banks-may-sit-out-small-business-rescue-plan-on-liability-worries-sources-idUSKBN21K075 [https://perma.cc/9B2A-EMNM].

47. O'Connell et al., *supra* note 6 ("Treasury was not planning to waive strict criminal penalties for lenders who did not thoroughly vet their new customers [but banks] warned that leaving the rules in place would require a level of vetting they couldn't quickly provide.").

48. This discussion attempts to use "lender" instead of bank because the program did permit non-bank lenders to participate. *Id.* at 20815. Brian Thompson, *Banks and Fintech Companies Accepting Paycheck Protection Program Loan Applications*, FORBES (Apr. 9, 2020, 6:22 PM), https://www.forbes.com/sites/brianthompson1/2020/04/09/banks-and-fintech-companies-accepting-paycheck-protection-program-loan-applications-from-new-and-non-bank-customers [https://perma.cc/5KHC-8UVV]. Concerns were raised that bank lenders were favored due to slow approval of non-bank lenders such as FinTech companies. *See* Anne Sraders, *14 Years in 14 Days: Inside the Chaotic Rollout of the SBA's PPP Loan Plan*, FORTUNE (Apr. 29, 2020, 12:30 PM), https://fortune.com/2020/04/29/sba-ppp-paycheck-protection-program-loans-small-business-administration-inside-chaos/ ("Given their smaller client base, some argue the smallest of businesses might have had a better shot at getting funding had FinTechs been approved to lend sooner.").

fraud.[49] In adopting the April 2 Rule, the SBA changed its position, relieving lenders of the four forgoing concerns.[50]

The initial rulemaking requires borrowers to make certifications, returned to below, that are consistent with statutory conditions to receiving PPP loans. The April 2 Rule generally enables lenders to rely on those certifications, without undertaking diligence to verify their content:

> SBA will allow lenders to rely on certifications of the borrower in order to determine eligibility of the borrower and use of loan proceeds and to rely on specified documents provided by the borrower to determine qualifying loan amount and eligibility for loan forgiveness. Lenders . . . will be held harmless for borrowers' failure to comply with program criteria.[51]

As discussed below, the rule made other concessions towards enticing lenders to serve as plumbing for distributing PPP funds.[52]

ii. Limitation on Statutorily Contemplated Pool of Eligible Borrowers to Exclude Larger Businesses in Accommodation and Food Service Industries

The April 2 Rule substantially limited the set of eligible participants the CARES Act contemplated. As explored below, this limitation led to confusion that would engender a chorus of outrage concerning purportedly ineligible businesses benefiting from the loans.[53] To put this error in context, the CARES Act expands the range of businesses eligible for SBA-guaranteed loans under the rele-

49. *See* Schroeder & Henry, *supra* note 46.

50. Lee Richards, Daniel Zinman, David Daniels & Rachel Mechanic, *The CARES Act – Lenders Beware*, N.Y.U. L. PROGRAM ON CORP. COMPLIANCE AND ENF'T: COMPLIANCE & ENF'T (Apr. 27, 2020), https://wp.nyu.edu/compliance_enforcement/2020/04/27/the-cares-act-lenders-beware/ [https://perma.cc/4YQH-B982].

51. April 2 Rule, 85 Fed. Reg. at 20,811. Lenders can similarly rely on borrower certifications for purposes of determining eligibility for loan forgiveness. *Id.* at 20815–16.

52. For a discussion of an alternative that would have used the IRS, see John C. Coffee, Jr., *Wall Street CARES!: Who Gets the Hidden Subsidies under the CARES Act?*, CLS BLUE SKY BLOG (Apr. 15, 2020), https://clsbluesky.law.columbia.edu/2020/04/15/wall-street-cares-who-gets-the-hidden-subsidies-under-the-cares-act/ [https://perma.cc/BCZ3-XZJZ]. There are significant questions as to whether the IRS would have had the operational capacity to process and fund loan applications and forgiveness requests better than the network of private lenders leveraged through the PPP. If the IRS had administered the distribution of funds to beleaguered businesses directly, there would also be no private parties to blame in the event of a frustrating rollout. *See* Section V.D.ii.

53. *See* Sraders, *supra* note 48 ("[M]any small-business owners are frustrated that over 200 publicly traded companies received over $750 million in loans . . . .").

vant provision of the Small Business Act.[54] Pursuant to the CARES Act, PPP funds could support not-for-profits, tribal entities, veterans organizations, self-employed individuals, businesses with under 500 people irrespective of industry and "*any business concern that employs not more than 500 employees per physical location of the business concern [and is in the accommodation or food services industries]*."[55] One may argue whether the emphasized text represents successful lobbying by hotels, restaurants and other businesses hit hard by the COVID-19 related health measures, or something like an indifference on the part of legislative actors between layoffs affecting employees of chains versus stand-alone entities. These considerations will be resumed below. But in either case, the clear statutory language contemplates lending to large businesses in these industries so long as they had no more than 500 employees at any given location.

The April 2 Rule cheekily neglected this statutory language.[56] Instead, the rulemaking stated that of for-profit businesses, only those with 500 or fewer employees or businesses qualifying under *pre-existing* SBA guidelines were eligible for PPP funds. Subsequent guidance dated April 29, 2020 would acknowledge[57] that the 500-employee limit did not apply to certain businesses in the accommodation or food services industries. But as discussed below, this corrective guidance followed the exhaustion of funds in the first round of the PPP and the formation of a public narrative incorrectly informed by the blooper in the April 2 Rule.[58]

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54. Business Loan Program Temporary Changes; Paycheck Protection Program—Revisions to Loan Forgiveness, 85 Fed. Reg. 38,304 (June 26, 2020) (to be codified at 13 C.F.R. pt. 120).

55. 15 U.S.C. § 636(a)(36)(D)(iii).

56. April 2 Rule, 85 Fed. Reg. at 20,812 ("Am I eligible? You are eligible for a PPP loan if you have 500 or fewer employees whose principal place of residence is in the United States, or are a business that operates in a certain industry and meet the applicable SBA employee-based size standards for that industry; and (i) You are: A. A small business concern as defined in section 3 of the Small Business Act . . . and subject to SBA's affiliation rules . . . .").

57. *See* U.S. DEP'T OF TREAS., PAYCHECK PROTECTION PROGRAM LOANS FREQUENTLY ASKED QUESTIONS (FAQS) (2020) ("24. Question: How do the $10 million cap and affiliation rules work for hotels and restaurants (and any business assigned a North American Industry Classification System (NAICS) code beginning with 72)? Answer: Under the CARES Act, any single business entity that is assigned a NAICS code beginning with 72 (including hotels and restaurants) and that employs not more than 500 employees per physical location is eligible to receive a PPP loan.").

58. Maneet Ahuja & Antoine Gara, *Crony Capitalism: Why the Best-Connected Businesses Got Much of The SBA Coronavirus Cash*, FORBES (Apr. 20, 2020, 4:53 PM), https://www.forbes.com/sites/maneetahuja/2020/04/20/crony-capitalism-why-the-best-connected-businesses-got-much-of-the-sba-coronavirus-cash [https://perma.cc/ZHN4-E4GB].

iii. Other Program Terms Are Revised, Predominantly in Favor of Lenders

The April 2 Rule made other significant alterations to the statutorily specified contours of PPP. First, the maximum interest rate on PPP loans was reduced from four percent to one percent.[59] Second, the maturity date on the loans was reduced from ten years to two years.[60] Third, a requirement was added that at least 75 percent of proceeds be used towards payroll expenses.[61] And fourth, the loan forgiveness mechanics were specified.[62]

The cap on interest rates made the loans less attractive for creditors. But the loan forgiveness mechanics buried in the first rulemaking help compensate creditors for the low interest rates. As referenced above, a key feature of PPP loans is that they are conditionally forgivable. If a loan meets conditions to forgiveness, the government repays the lender (i.e., the loan becomes a grant). For a loan to be forgiven, the borrower must put the proceeds towards certain uses, must maintain prior levels of employment and compensation, and must then submit documentation substantiating it met these two conditions.[63] Pursuant to the CARES Act, the proceeds of loans were expected to be used up by the end of June, and most loans were expected to be eligible for forgiveness within eight to ten weeks of their funding.[64] A simpler implementation of the program would require the lender to first obtain evidence that the buyer qualified for forgiveness on the basis of how the proceeds were actually used and only then request compensation from the SBA. This process would reasonably take another couple of weeks after the borrower provided documentation at the end of June and only require SBA personnel to review any loan once to assess whether it should be forgiven. Instead, the April 2 Rule authorizes lenders to make reimbursement requests based on "expected" amounts that would be forgiven with respect to a lender's

59. April 2 Rule, 85 Fed. Reg. at 20,813. See discussion of statutory extension of minimum maturity to five years at *infra* note 100.

60. April 2 Rule, 85 Fed. Reg. at 20,813.

61. *Id.* at 20,814.

62. *Id.* at 20,816.

63. Although forgiveness was initially generally conditioned on maintenance of workforce and payroll at levels at least 75% of a pre-COVID-19 benchmark, there are exceptions.

64. Alexander Bartik, Marianne Bertrand, Zoë B. Cullen, Edward L. Glaeser, Michael Luca & Christopher Stanton, *The Impact of Covid-19 on Small Business Outcomes and Expectations*, 30 PROC. NAT'L ACAD. SCI. U.S. 17656, 17663 (2020) (Nat'l Bureau of Econ. Research, Working Paper No. 26989, 2020) ("Consequently, a significant portion of the [PPP] 'loans' can be seen as a grant rather than traditional debt.").

portfolio of loans. The SBA is required to provide reimbursement in response to requests within fifteen days.[65]

Forgiveness payments ahead of loan maturity combined with other program features to potentially significantly reduce lenders' effective outlays of funding without reducing income from the loans. Loan proceeds frequently remain with the lender (e.g., in a deposit account), thereby netting down actual funding.[66] Furthermore, in addition to SBA purchases of loans in connection with expected forgiveness, private secondary markets provided opportunities to liquidate loans early.[67] In retrospect, however, the generous forgiveness rules did not have an effect favoring lenders because forgiveness applications had yet to be processed as of November 2020.[68]

iv. Use of Decentralized Private Lenders to Distribute Funds Creates Feeding Frenzy

As discussed above, the April 2 Rule reshaped the statutory terms of the PPP into a more lender-friendly regime. Key administrative changes included the release of lenders from liability related to ineligible borrowers and potentially generous forgiveness terms. A separate design element induced a feeding frenzy among participating lenders when funding began on April 3.

The program was established on a "first-come, first-served" basis.[69] As will be revisited below, this approach was taken instead of batching applications that came in over a period of time, and then allocating funds proportionately across them. As a result, lenders and borrowers that anticipated program funds running out faced an incentive to apply for funds as soon as the program opened on April 3. Another design element compounded the race among borrowers.

65. April 2 Rule, 85 Fed. Reg. at 20,816.

66. Ann Saphir and Howard Schneider, *U.S. Small Firms Leave $150 Billion in Coronavirus Stimulus Untapped*, YAHOO NEWS (May 26, 2020) https://www.yahoo.com/now/u-small-firms-leave-150-101725444.html [https://perma.cc/KP9N-2K92] ("Many of Bank of the West's PPP borrowers haven't touched their PPP loan deposits . . . partly because they are confused about the terms.").

67. There was potential to sell PPP loans via private secondary markets. More generally, the Fed provided additional liquidity for business loans (albeit generally for larger borrowers). *See* Lev Menand, *Fed to the Rescue: Unprecedented Scope, Stretched Authority*, CLS BLUE SKY BLOG (Apr. 27, 2020), https://clsbluesky.law.columbia.edu/2020/04/27/fed-to-the-rescue-unprecedented-scope-stretched-authority/ [https://perma.cc/VVM3-PD8L].

68. *See* John Reosti, *Banks, Borrowers Bristle at SBA Questionnaire on Large PPP Loans*, AM. BANKER (Nov. 30, 2020, 2:38 PM), https://www.americanbanker.com/news/banks-borrowers-bristle-at-sba-questionnaire-on-large-ppp-loans.

69. April 2 Rule, 85 Fed. Reg. at 20,813.

Rather than permitting borrowers to apply for a few weeks or a month of funding at a time, the SBA required borrowers to request their full allotment at once.[70] These features accelerated the draining of program funds.

The design of fund disbursement may have been reasonable given an interest in injecting funding quickly. But the design also disadvantages a number of sympathetic borrowers. The April 2 Rule stacked the deck against eligible borrowers that learned of the program later than others as well as eligible borrowers without the organizational infrastructure to expeditiously apply for funding.[71] The design also disadvantaged borrowers without preexisting relationships with participating lenders, who as a result had significantly more onboarding to do.[72] These three groups represented some of the most intensely affected by the economic instability, uncertainty and suspension following the implementation of public health measures. These groups of borrowers may also have disproportionately included female and minority owned-businesses, leading to the program unintentionally exacerbating socio-economic divides.

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70. *Id.*

71. For example, small borrowers that do not systematically track expenses or have a dedicated finance or legal function, whether internally or through independent contractor support.

72. The April 2 Rule sensibly allowed institutions to exempt "existing customers [from] reverification under applicable [Bank Secrecy Act] requirements, unless otherwise indicated in the institution's risk-based approach to BSA compliance." *Id.* at 20,815. Haoyang Liu and Desi Volker proposed a number of factors that may have led banks to lend to existing clients: "banks are quicker to accept loan applications from existing customers, since they already have much of the relevant information and screening is faster. . . [m]ore generally, it has been widely documented that banks prioritize businesses with existing lending relationships for cost savings reasons and to avoid fraudulent applications." Haoyang Liu & Desi Volker, *Where Have the Paycheck Protection Loans Gone So Far?*, N.Y. FED. RESERVE: LIBERTY ST. ECON. (May 6, 2020), https://libertystreeteconomics.newyorkfed.org/2020/05/where-have-the-paycheck-protection-loans-gone-so-far.html [https://perma.cc/G3XD-JDSS]. The authors also observe that "[a]rguably, lenders' preference for their own depository base could be an important factor in explaining the observed PPP loan approval data." *Id. See also* Yuka Hayashi, Ruth Simon & Peter Rudegeair, *PPP Small-Business Loans Left Behind Many of America's Neediest Firms*, WALL ST. J. (June 17, 2020, 11:27 AM), https://www.wsj.com/articles/ppp-small-business-loans-left-behind-many-of-americas-neediest-firms-11592407677 ("Many small-business owners have few ties to banks beyond checking accounts. A survey released in April by the Federal Reserve[ ] . . . found that only 44% of small businesses with at least one employee had obtained a bank loan in the past five years.").

v. To Participate, Borrower Must Represent to Vague and Capacious Standard

Finally, the April 2 Rule specifies the certifications borrowers must make in order to receive PPP funds. In relevant part, these require attestation that "[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the applicant."[73]

Some background is important to construing this vaguely framed requirement. Under the SBA-guaranteed lending program onto which the PPP was grafted, a borrower seeking an SBA guarantee on a loan must demonstrate "that the desired credit is unavailable to the applicant on reasonable terms and conditions from non-Federal sources without SBA assistance."[74] This requirement helps limit participation in the SBA's Section 7(a) loan guarantee program to borrowers that require governmental support in order to receive a loan. The CARES Act expressly exempts PPP loans from this so called "credit elsewhere test."[75] The April 2 Rule acknowledges this suspension of the usual requirement of showing that financing is unavailable except with an SBA guarantee.[76] The "credit elsewhere test" is designed for an array of small businesses that generally receive debt as opposed to equity financing, and by its terms only requires assessment of credit availability. Much of the outrage following the expiration of the first round of PPP funds focused on businesses with potential access to equity financing such as larger, profitable corporations or VC-backed startups. The ambiguous language governing eligibility for PPP funds as well as the suspension of the "credit elsewhere test" will be returned to below as the fracas over larger or more sophisticated businesses participating in the program is examined.

B. Companies with Venture Capital and Private Equity Investors Seek PPP Funds

The first rulemaking offering guidance to lenders and borrowers left a significant question open. Many businesses would only qualify if they employed fewer than 500 people. But given that investors in a business may also be investors in other businesses, when should the

73. April 2 Rule, 85 Fed. Reg. at 20,814.

74. 13 C.F.R. § 120.101 (2020).

75. CARES Act § 1102(a)(2) ("During the covered period, the requirement that a small business concern is unable to obtain credit elsewhere, as defined in section 3(h), shall not apply to a covered loan.").

76. April 2 Rule, 85 Fed. Reg. at 20,816 ("When evaluating an applicant's eligibility lenders will not be required to apply the 'credit available elsewhere' test . . . .").

workforces of the jointly owned businesses be combined for purposes of applying the 500 person threshold?

This is a version of a familiar question, encountered in myriad legal contexts. Where legal thresholds are based on business activity, when should activities between two distinct legal entities be aggregated for purposes of applying the thresholds? Oftentimes (e.g., in banking law or securities law) legal analysis requires defining which entities are "affiliated" or commonly "controlled."[77] Generally, businesses that are operated over multiple entities that are wholly (or majority) owned by a parent are aggregated. And generally, having a person hold small stakes in two distinct businesses (such as an investor purchasing a few shares of IBM and Walmart) does not lead to those two businesses being considered in aggregate when applying law. But of course, there are many shades in between, and that is where design and lawyering takes place and answers differ based on context.

Complex rules written under the Small Business Act govern the question of affiliate aggregation with respect to qualification for pre-CARES Act SBA guarantees of loans. But as explained above, that prior regime is meant for a different class of businesses and responds to policy goals distinct from the extraordinary waves of unemployment claims that began in March. Differences in context and regulatory purpose between the preexisting SBA regime, on the one hand, and the PPP, on the other hand, allowed lawyers to develop arguments for relaxing affiliation rules with respect to PPP funding.

In the wrangle over SBA affiliate aggregation rules, private equity (PE) and venture capital (VC) portfolio companies clamored for relief.[78] Private equity and venture capital funds represent two important types of investors providing private capital, generally in the form of equity, to businesses.[79] While VC and PE funds' portfolio company characteristics tend to differ along important dimensions (e.g., VC portfolio companies are less likely to have a consistent history of significant cash flow generation, more likely to be younger and smaller, and less likely to have significant debt), these two classes of investors are likelier to hold stakes in relatively small companies with significant potential for growth or profit. Culturally, although the reputation

77. *See, e.g.*, 12 U.S.C. § 1841(a) (defining control in a banking law context); 17 C.F.R. § 230.405 (2020). (defining control in a securities law context).

78. *See* Sraders, *supra* note <CITE _Ref40214948“> ("[S]everal lobbying groups largely failed to amend affiliate rules for round two of the PPP.").

79. In the private equity context, the equity injections from PE funds are frequently significantly complemented with debt so that the capital structure is leveraged.

of the VC sector has been somewhat tarnished,[80] VC firms continue to enjoy greater social approbation than PE firms.

Days of intense outreach preceded the finalization of affiliate rules on Friday, April 3, 2020. As Dan Primack put it in the daily Pro Rata newsletter, House Speaker Nancy Pelosi and House Minority Leader Kevin McCarthy "who rarely agree on anything except for the grandeur of California, both [expressed they] want the so-called 'affiliation rules' waived."[81] Writing to Treasury Secretary Steven Mnuchin and head of the SBA, Jovita Carranza, Speaker Pelosi and Congressman Ro Khanna pleaded for VC-backed companies using familiar caricatures:

> Startups are the engine of America's innovation economy and our districts in California's Bay Area and Silicon Valley are home to thousands of these companies. Other high-tech hubs around the country with a strong startup ecosystem will also be in need of PPP financing to preserve jobs and survive. From clean technology to sustainable agriculture to biotechnology, startups create high-paying jobs and make important contributions to America's economy.[82]

On Friday, April 3, SBA published guidance on the application of preexisting affiliation rules.[83] The guidance did not significantly change the preexisting regime.[84] As a result, many portfolio companies were disqualified due to crossing the employee threshold when their employees were aggregated with jointly owned portfolio companies' employees.

There was at least one consequence of the April 3 guidance, however. The SBA separately confirmed that "affiliation based on ownership" rules[85] would apply to portfolio companies without

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80. Controversies within the startup community such as Theranos and WeWork have (re)ignited a scholarly examination of the sector. *See generally* Elizabeth Pollman, *Startup Governance*, 168 U. Pa. L. Rev. 155, 155 (2019); Anat Alon-Beck, *Unicorn Stock Options - A Golden Goose or Trojan Horse?*, 2019 Colum. Bus. L. Rev. 107 (2019); Seth C. Oranburg, *Encouraging Entrepreneurship and Innovation Through Regulatory Democratization*, 57 San Diego L. Rev. 757 (2020).

81. Dan Primack, *Bipartisan Push Could Save Private-Equity Owned Small Businesses,* Axios (Apr. 2, 2020), https://www.axios.com/private-equity-stimulus-cash-pelosi-mccarthy-38fef7fa-f6ac-43ca-9a7f-662b9cd66f27.html.

82. Press Release, Nancy Pelosi, Speaker of the House, Pelosi, Khanna Urge Sec. Mnuchin and SBA Admin. Carranza to Support Startups (Mar. 31, 2020), https://www.speaker.gov/newsroom/33120-0 [https://perma.cc/G9SP-2UW6].

83. Affiliates Rule, 85 Fed. Reg. at 20,817.

84. *See id.*; Small Business Size Regulations, 13 C.F.R. § 121.301 (2020) (providing pre-existing standards for aggregating affiliates for purposes of determining loan eligibility under Section 7(a) of the Small Business Act).

85. 13 C.F.R. § 121.301(f)(1).

modification.[86] These rules include a lax definition of control, holding that two entities are commonly controlled and thus subject to aggregation if a person "owns or has the power to control more than 50 percent of the concern's voting equity."[87] In addition, the "SBA will deem a minority shareholder to be in control, if that [person] has the ability, under the concern's charter, by-laws, or shareholder's agreement, to prevent a quorum or otherwise block action by the board of directors or shareholders."[88] This led to some portfolio companies hastily negotiating with fund investors to relinquish veto rights.

C. Failed Attempts to Reach Self Employed Business Owners

On April 14, 2020, the SBA completed a third interim final rule further revising how PPP funds were to be deployed.[89] This rule governs how individual applicants are to be treated, which is a difficult issue given that the preexisting SBA regime contemplates that self-employed individuals do *not* qualify for subsidized loans. While most borrowers could apply for loans starting on April 3, individuals were initially scheduled to wait an additional week, until April 10, to participate in the program. The week's delay was to provide the SBA with additional time to define, inter alia, how compensation-based qualifications would be measured in cases where the same individual was effectively the sole owner and employee of the business.[90] The April 10 timeline, however, was moved back and the SBA published guidance on making loans to individuals on April 14. On April 16, PPP funds ran out. This means that over 25 million[91] self-employed individuals (including sole proprietors and independent contractors)

86. Affiliates Rule, 85 Fed. Reg. at 20,818.

87. 13 C.F.R. § 121.301(f)(1).

88. *Id.*

89. Business Loan Program Temporary Changes; Paycheck Protection Program–Additional Eligibility Criteria and Requirements for Certain Pledges of Loans, 85 Fed. Reg. 21,747 (June 20, 2020).

90. *See also* Steven L. Schwarcz, *Intrinsic Imbalance: The Impact of Income Disparity on Financial Regulation*, 78 LAW & CONTEMP. PROBS. 97 (2015). Subsequent rulemaking acknowledged the rushed context of lawmaking behind the CARES Act and implementing regulations in making clarifications and corrections to the initial rules. *See* Business Loan Program Temporary Changes; Paycheck Protection Program–Nondiscrimination and Additional Eligibility Criteria, 85 Fed. Reg. 27,287, 27,288 (May 8, 2020) ("[T]he purpose of the CARES Act . . . was to afford swift stopgap relief to Americans who might otherwise lose their jobs or businesses because of the economic hardships wrought by the response to the COVID–19 public health emergency.").

91. Christopher Rugaber, *Gig Workers and Self-Employed Keep Waiting for Jobless Aid*, U.S. NEWS (Apr. 23, 2020, 5:20 PM), https://www.usnews.com/news/business/articles/2020-04-23/another-surge-in-us-unemployment-applications-is-likely.

had only two days to queue for the almost exhausted pool of PPP funds.

This failing to distribute funds to the self-employed is understandable given the design of the program. I do not believe SBA officials were consciously picking winners and losers in this regard, let alone expressing animus towards gig-economy employees or other self-employed individuals. Rather, the necessarily rushed[92] design and implementation of the program created challenges in reaching this class of borrowers and the results may be viewed as forced errors.

V.
Barrage of Criticism Comes as First Run of Funding is Depleted

The PPP launched on April 3. Less than two weeks later, on April 16, the program ran out of funds. On April 24, the 45th President would sign an Act authorizing an additional $310 billion in PPP loans. Much Sturm und Drang thundered in the interim due to substantial unmet demand for PPP loans and uncertainty as to whether additional funds were forthcoming. Reports that PPP funds were inequitably distributed raised howls of protest and prompted some borrowers to return funds they qualified for.[93]

The inadequacy of initial PPP funding was predictable and partly due to the capacious standard under which borrowers qualified for program funds.

Although some economic necessity is required to access PPP funds, the governing standard is exceptionally broad.[94] In relevant

92. *See* Sraders, *supra* note <CITE _Ref40214948“> (“The rollout of the SBA’s Paycheck Protection Program was chaotic, and problems were exacerbated by an intense time crunch that tasked lenders and government with distributing $349 billion to small businesses in a matter of weeks.”). The New York Times criticized the lag in providing funding to self-employed applicants as racially discriminatory without grappling with the design and implementation challenges the program faced. Stacy Cowley, *Minority Entrepreneurs Struggled to Get Small-Business Relief Loans*, N.Y. Times (Apr. 4, 2021) (“The program also largely locked out sole proprietors and independent contractors—two of the most popular structures for minority-owned businesses.”).

93. Rolfe Winkler & Yuliya Chernova, *Silicon Valley Debate: Should Venture-Backed Firms Take Stimulus Money?*, Wall St. J. (Apr. 21, 2020, 8:00 AM), https://www.wsj.com/articles/startup-world-wrestles-with-taking-small-business-loans-11587470400.

94. Senator Ron Johnson (R-WI) explained that the PPP’s primary objective, as stated by its sponsors, was to “provide financial support to employees by keeping them connected to their employers, regardless of whether there was work for them to perform.” Ron Johnson, *How to Fix the Paycheck Protection Program*, Wall St. J. (May 31, 2020, 3:44 PM), https://www.wsj.com/articles/how-to-fix-the-paycheck-pro-

part, borrowers must certify that "[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the applicant."[95] The standard is not that available funds are insufficient to meet short-term payroll or other expenses. The nexus between financial position at the time of the borrowing and impacts of the "economic uncertainty" on "ongoing operations" is substantially looser. The standard merely requires that "economic uncertainty" (as opposed to, for example, experienced or imminent losses of revenues or growth in costs) makes the loan necessary for supporting ongoing operations. This implies that strategic as opposed to tactical or reactive responses suffice. Contemplated facility closures, cuts in workforce, reduction of compensation or other operational restructurings in light of anticipated reductions in demand or other factors—if considered in good faith—would be the types of impacts on "ongoing operations" that would qualify a borrower for the program.[96] Moreover, the language uses the term "support" instead of a term that implies a greater level of dependency. The standard, for example, does not require that current economic uncertainty make the loan request necessary to "continue" ongoing operations. Finally, the standard does not specify to what extent "ongoing operations" would have to be impacted absent PPP support. There is no de minimis or materiality qualifier on the extent of impact. It is not a stretch of legal argumentation to certify that the standard is met if, for example, one out of one hundred employees would be laid off in the near term in order to husband funds for economic uncertainty.[97]

A. The PPP Sought to Avert Unemployment and Promote Stability in a Wide Swath of the Economy and Initially Received Inadequate Funding to Accomplish Those Goals

The immense pool of potential PPP fund recipients explains the powerful extra-legal pressures that came to shape policy in mid-April. Small business is a significant component of the U.S. economy. Prior

tection-program-11590954296 (also explaining that "the application didn't require an effective demonstration of need").

95. April 2 Rule, 85 Fed. Reg. at 20,814.

96. *See* Bartik et al., *supra* note 64, at 10–11 (observing differences in expectations as to when crisis will abate).

97. The United States Census Bureau ran a survey of small businesses between April 26 and May 2, 2020, finding that over 85% of surveyed businesses experienced "large" or "moderate" negative effects due to COVID-19 related circumstances. These results substantiate that almost all small businesses could claim to be affected negatively by the pandemic. Calculations by author based on data available from U.S. CENSUS BUREAU, SMALL BUSINESS PULSE SURVEY, https://portal.census.gov/pulse/data/ (last visited Apr. 26, 2021).

to the health measures responding to COVID-19, U.S. small businesses employed approximately 60 million individuals, or 47.5% of the private workforce in the U.S.[98] These 60 million individuals were employed across over 30 million distinct small businesses throughout the U.S. In addition, there are over 20 million self-employed individuals (including independent contractors and sole proprietors) in the United States.[99] These statistics allow a back-of-the-envelope estimate as to the extent to which $349 billion in initial PPP funds could support the small business and self-employed labor forces for a period of ten weeks.[100] Table 1 calculates how much payroll support the initial round of the PPP provided on the assumption that all small businesses and self-employed individuals participated.

Small business employees + Self-employed individuals	80,000,000
PPP Funds	$349,000,000,000
Funds/employee	$4362.50
Funds/employee-week	$436.25
Funds/employee-hour	$10.91

TABLE 1: CALCULATION OF PAYROLL SUPPORT FROM INITIAL PPP

Considering only small businesses as defined by the SBA prior to the CARES Act and self-employed potential borrowers, program

98. U.S. SMALL BUSINESS ADMINISTRATION, OFFICE OF ADVOCACY, 2018 SMALL BUSINESS PROFILE 1 (2018).

99. Elka Torpey & Brian Roberts, *Small-Business Options: Occupational Outlook for Self-Employed Workers*, U.S. BUREAU OF LAB. STATS. (May 2018), https://www.bls.gov/careeroutlook/2018/article/self-employment.htm; *see also supra* note 91. In addition, there are over 12 million workers in the not-for-profit sector. LESTER M. SALAMON & CHELSEA L. NEWHOUSE, THE 2019 NONPROFIT EMPLOYMENT REPORT (Nonprofit Economic Data Bulletin No. 47, 2019). This estimate also does not account for the work forces of tribal business concerns and veterans organizations, which were also qualifiedly eligible to receive PPP funds.

100. The Flexibility Act extended the length of time available for borrowers to spend their funds from eight weeks to twenty-four weeks. Business Loan Program Temporary Changes; Paycheck Protection Program–Revisions to First Interim Final Rule, 85 Fed. Reg. 36,308, 36,310 (June 16, 2020). In addition, the Flexibility Act lowered the percentage of proceeds that had to be spent on payroll expenses as a condition to loan forgiveness from 75 percent to 60 percent. *Id.* The Flexibility Act also increased the minimum maturity of loans from two years to five years. *Id.* Several of these changes were retroactive to March 27. These retroactive changes from early June do not impact the analysis, however, because important post-Enhancement Act trends became established before then and the contents of the Flexibility Act were a surprise to many (prospective) lenders and borrowers.

funds were expected to be grossly inadequate relative to demand from the outset.[101] The program was to provide funding through the end of June, representing a period of approximately ten weeks from the initiation of the program. For that period, Congress allocated under $4,500 per employee, assuming conservatively that program funds would be used exclusively for payroll. These calculations represent an *over*-estimate of the funds PPP made available to support the U.S. workforce because the calculations do not account for funds being used to pay utilities, interest on preexisting debt, and rent. Also, these estimates do not account for all the expenses businesses face that PPP funds were not authorized for. Further, the estimates do not account for other borrowers that were eligible to participate in the PPP such as not-for-profits and chains within hospitality and restaurant sectors. However, even with these conservative assumptions, the PPP provided less than $11 per hour to small business employees and the self-employed, assuming universal participation, a forty-hour work week and no benefits. Given that Congress authorized PPP funds to cover wages of up to one hundred thousand dollars annually and that non-wage benefits represent a substantial amount of payroll expenses, the subsidy fell far short of covering the costs of retention for many small business employees.[102]

B. COVID-19 and Related Public Health Measures Profoundly Affected Business Planning, Leading a Wide Variety of Employers to Qualify for PPP Funding

A reasonable rebuttal to the calculations in Table 1 emphasizes that not all small businesses or self-employed individuals would qualify for the program.[103] As discussed above, however, the standard under which borrowers qualify for PPP funds is expansive, merely requiring that "[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the applicant."[104] And

101. Senator Marco Rubio, instrumental in designing the program, subsequently regretted not providing more funding to the PPP from the outset. *See* O'Connell et al., *supra* note 6 ("Although the first $349 billion allocated was more than initial drafts of the legislation called for, Rubio said that in retrospect, it's clear the program should have been funded at a higher level to begin with.").

102. Average employee compensation expense for private employers in the U.S. is about $34.72 per hour, with wages making up approximately 70 percent of that amount. *See* News Release, Bureau of Labor Statistics, Employer Costs of Employee Compensation Summary (March 19, 2020). As noted above, the CARES Act (and Treasury regulations) generally authorize each PPP borrower to receive the lesser of ten million dollars or two and a half months of payroll in funding.

103. *See supra* note 100.

104. April 2 Rule, 85 Fed. Reg. at 20,811.

as begun in Part III and continued below, COVID-19 and related private and public health measures severely impacted a wide variety of businesses, suggesting that many would be able to certify they met the standard in good faith.

In a survey conducted at the end of March, Professors Alexander Bartik, Marianne Bertrand, Zoë Cullen, Edward Glaeser, Michael Luca, and Christopher Stanton investigate the impacts related to COVID-19 on small businesses as well as responses to CARES Act support programs.[105] In particular, the working paper from Bartik et al. looks at: (1) financial fragility among small businesses,[106] (2) extent to which small businesses have already temporarily closed and laid off employees,[107] (3) expectations about how long the crisis will last and how this is affecting business decisions, and (4) decisions about whether to seek funding through the CARES Act, and how this will impact layoff and closure decisions. Their results show that business disruptions have been extreme. Their survey also illuminates the sources of business disruption. Among businesses that remained open, the predominant concern was downturn in demand, followed by concerns related to employee health and supply chains.[108] The ranking of concerns was similar for businesses that were temporarily closed or permanently closed, except that stress due to loss of demand was further emphasized.[109] These survey results support that declines in demand powerfully impacted business decisions.

Bartik et al. also show significant differences in cash needs among firms. Of the firms surveyed, approximately one-fourth lacked cash to cover even one month of expenses; and another half of the

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105. *See* Bartik et al., *supra* note 64.

106. Of the surveyed businesses, only 55.5% remained operational (with 41.4% reporting they were temporarily closed due to COVID-19, 1.8% reporting they were permanently closed because of COVID-19 and 1.3% reporting they were temporarily closed for other reasons). *Id.* at 17,661. Bartik et al. also report significant loss in payroll between January 31 and the survey, with the number of full-time employees falling by 32 percent and part time employees by 57 percent. *Id.*

107. Among the study's findings is that businesses with under five employees or over 499 employees were able to retain more payroll than businesses with between five and 100 employees. *Id.* at 17,660. Relative to January 2020 employment, surveyed businesses with under five employees retained two thirds of their employees and businesses with one hundred or more employees retained 72 percent of their employees. In contrast, businesses with between five and nine employees, ten and nineteen employees, and twenty and ninety-nine employees retained 52 percent, 55 percent and 58 percent respectively. This may reflect greater toughness on the part of the very small businesses, which may be more likely to be family-run and involve deep bonding mechanisms. Above the five employee mark, resilience does appear to increase with the size of the labor force.

108. Bartik et al., *supra* note 64, at 17,660.

109. *Id.*

firms had only enough cash to cover between one and two months of expenses.[110] These figures may underestimate liquidity among small firms because the figures do not account for additional inflow of cash from ongoing operations or reductions in expenses due to temporary closures. However, while reasonable people may argue as to the degree of cash shortages, the survey results support that many small businesses faced a severe lack of liquidity to cover pre-COVID-19 payroll levels and other expenses. These shortages help explain the explosive conclusion to the first round of the PPP when program funds ran out before many applicants were able to receive loans.

The findings of Bartik et al. are consistent with those of Professors John Humphries, Christopher Neilson and Gabriel Ulyssea.[111] Humphries et al. used Facebook ads to collect data from over 8,000 small businesses. Their working paper uses the results to investigate three related questions: (1) the extent of layoffs and other COVID-19 related impacts;[112] (2) expectations about the future;[113] and (3) awareness of governmental assistance programs.[114] Their results substantiate that there were widespread concerns about the future economic deterioration among small business owners.[115] And their results provide an alternative explanation for some of the frustrations voiced about the PPP. Humphries et al. observe that awareness of government programs "increases substantially over the period [of the survey], with over 70 percent of businesses reporting that they were aware of pro-

110. *Id.* at 17,662.

111. John Eric Humphries, Christopher Neilson & Gabriel Ulyssea, *The Evolving Impacts of COVID-19 on Small Businesses Since the CARES Act*, COWLES FOUND. RSCH. IN ECON. DISCUSSION PAPER NO. 2230 (2020).

112. The survey finds that by March 30, 59 percent of respondents reported that they had already laid off a substantial portion of their employees. *Id.* at 2. After the initiation of the PPP on April 3, the survey finds an approximately 0.2% weekly increase in the number of survey respondents reporting layoffs. *Id.* at 3. This does not necessarily imply that the PPP failed to reduce layoffs, as post-April 3 growth could have exceeded 0.2% without the PPP. *Id.*

113. The survey finds that "business owners' expectations about the future are in general negative and deteriorated throughout [the] sample period." *Id.* at 3. As of March 28, 30 percent of respondents believed their business would not recover within two years, but this number steadily increased, with almost 50 percent of firms reporting that their business would not recover within two years on April 20. *Id.* at 3.

114. The survey finds that on the "day after the CARES Act was passed, businesses with fewer than 10 full time equivalent . . . employees were much less likely than larger firms to report knowing about any government programs designed to support small businesses when compared to larger firms with 10 to 50 employees." *Id.* at 3.

115. "While layoffs show that many small businesses have already taken action, expectations about the future are also declining over time. . . . Over the three week period, the proportion expecting to ever recover fell by more than 10 percentage points, and the proportion expecting to recover in the next [two] years fell by approximately 15 percentage points." *Id.* at 7.

grams when PPP applications opened, increasing to over 85% on April 16th when the PPP ran out of initial funding."[116] However, the authors note that propagation of information regarding the availability of support was unequal:

> Businesses with 10-50 FTE employees were highly aware of programs . . . . In comparison, businesses with 0 to 4.5 and 5 to 9.5 employees were much less likely to be aware of programs the day after the CARES Act [was] passed. These two groups had very different trends during our sample period. The businesses with 5 to 9.5 employees rapidly become more aware of programs, reaching similar levels of awareness as the larger businesses within one or two days after the PPP opened for applications. In contrast, businesses with fewer than five employees learned about programs much more slowly, with a large gap persisting through when the PPP exhausted initial funding.[117]

These findings cast light on important questions relating both to the rollout of emergency support programs, such as the PPP, and more generally, to the propagation of information concerning law within the business community. As indicated above, smaller businesses are among other things less likely to have a legal function in-house (or consistently available externally). Thus, smaller businesses have less access to information regarding legal changes, less ability to digest that information, and fewer resources (e.g., lawyers and accountants) to enable receipt of government support.

On the whole, however, survey findings support a high degree of program awareness and uptake. A joint report from the SBA and Treasury claims that approximately 80 percent of eligible organizations participated in the program.[118] Using this figure to adjust the qualifying population and reproduce the calculations in Table 1 above, the funding available to each employee, for each employee-week and on an hourly basis to support payroll, respectively, are $5,453, $545, and $13.63. Again, the resulting payroll support falls below minimum wage in a number of states, providing evidence that the initial round was under-funded. Equally importantly, the 80 percent figure supports widespread participation (and presumably eligibility) in the program.

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116. *Id.* at 8.
117. *Id.* at 9.
118. Press Release, U.S. Dep't of the Treasury, SBA and Treasury Announce Release of Paycheck Protection Program Loan Data (July 6, 2020) ("'The PPP is providing much-needed relief to millions of American small businesses, supporting more than 51 million jobs and over 80 percent of all small business employees, who are the drivers of economic growth in our country,' said Secretary Steven T. Mnuchin.").

C. The PPP Decentralizes Funding Across Thousands of Lenders Preventing Coordination and Impeding Prioritization of Needier Borrowers

Three features of the PPP combined to cause intense dissatisfaction with the program's first round. These features were the broad eligibility standard, the inadequate amount of funding, and the decentralized system of private lenders used to deliver funds. Because of these design choices, a stampede took place between April 3 and April 16 that left many sympathetic businesses unfunded.

The decentralized system was a key component that prevented need-based distribution. Even if lenders and borrowers were intent on exercising moral discipline in leaving funds for the more-hard pressed, there was inadequate information to practice such forbearance. Assuming a broadly accepted metric that measures need-based merit, how could a borrower apply that metric to rank itself within over 60 million potential program participants? And even assuming a borrower knew its ranking, how would the borrower know whether $349 billion dollars was sufficient to allocate funds to more needy borrowers as well as itself? But there were other design elements, beyond insufficient information available to borrowers, that assured a messy rollout with plenty of inequitable outcomes to fuel frustrations and fill front pages.

The foregoing questions are an incomplete inventory of the reasons the PPP's design destined it to provoke public anger.[119] As discussed above in Part IV.A.i, the terms of the program encouraged lenders to dole out PPP dollars competitively. There was a limited pool of funds expected to be drained at a rapid pace through thousands of lenders. Each lender faced powerful incentives to maximize uptake among its borrowers in order to justify the fixed costs of adapting its operations for participation in the program. A participating lender also had reason to seek scale due to the largely riskless character of the federally guaranteed (and often forgivable) loans as well as the fixed fees and low interest PPP loans paid. As discussed above, dispensations to rely on borrower representations further assured lenders that careful vetting was superfluous. A lender's profits from participation were limited primarily by how much in eligible loans it could subscribe before program funds dissipated. And similarly to the informationally constrained borrowers discussed above, even if a lender was

119. *See* Bartik et al., *supra* note 64 at 17,666 (estimating that small businesses will need approximately $410 billion, whereas the CARES Act only authorized $349 billion).

intent on exercising moral or ethical restraint, it had no practically available means to compare the needs of its applicants with the needs of other lenders' applicants. Moreover, PPP borrowers could (and many did) have preexisting commercial relationships with lenders, so that granting PPP funds satisfied both business interests in maintaining relationships and customer financial health and professional ethics in serving customers.

As a result, neither lenders nor borrowers had enough information to institute a need-based queue for PPP funds. And furthermore, both lenders and borrowers faced incentives to rush for funding.

D. Many of the Criticisms that Followed the Depletion of Funds Either Misunderstood the Program or Neglected its Statutory or Regulatory Terms

After funding ran out, some observers criticized lenders' decisions to prioritize applicants with existing credit relationships. These critics saw the decision as representing less an administrative necessity and more a perverse expression of lenders' interests. Funding preexisting borrowers carries two types of benefits for lenders: first, the borrower would be less likely to default on preexisting debt to the lender due to receipt of PPP funds; and second, the commercial relationship between lender and borrower would be strengthened due to the lender serving as a conduit to inexpensive SBA-backed financing. Senators Cardin, Schumer, and Brown (Democrats from MD, NY and OH, respectively) wrote a letter to the SBA's Inspector General on April 23, 2020 requesting an urgent review of "reports that certain lenders participating in the [PPP] prioritized the applications of their larger and wealthier clients to the detriment of smaller businesses adversely impacted by the coronavirus pandemic."[120] The SBA's Inspector General issued a report on May 8, 2020, which did not conclude that lenders improperly prioritized pre-existing or favored clients. However, the Inspector General's report was a farcical, blundering legal analysis[121] and sidestepped the Senators' concerns.[122] The Senators' concerns can be tested, at least in part, by subsequent scholarship

120. Press Release, U.S. Senate Committee on Small Business & Entrepreneurship, Cardin, Schumer & Brown Call on SBA IG to Investigate Reports that Some PPP Lenders Prioritized Larger, Wealthier Clients Over Hard-Hit Small Businesses in Urgent Need (April 24, 2020), https://www.sbc.senate.gov/public/index.cfm/2020/4/cardin-schumer-brown-call-on-sba-ig-to-investigate-reports-that-some-ppp-lenders-prioritized-larger-wealthier-clients-over-hard-hit-small-businesses-in-urgent-need.

121. Among other things, the Inspector General's report skated over bicameralism requirements, applying the sense of the Senate provision as law without analysis. *See infra*, note 137 and surrounding text; Office of Inspector General, Flash Report Small

comparing funding rates for borrowers with preexisting banking relationships (e.g., on deposit accounts) with those receiving specifically credit services (e.g., outstanding loans or credit facilities) from lenders.[123] If it is found that banks directed PPP funds to financially unstable or more lucrative clients, then these criticisms may be vindicated.

Criticisms, however, did not stop with banks and other lenders. Many businesses were excoriated for drawing on PPP funds while smaller or less sophisticated employers were left out in the cold. A New York Times article typifying the zeitgeist identified a group of 130 hotels operated by Ashford Inc., a publicly traded company, as the largest beneficiary in the first round of PPP.[124] The article identified Monty Bennett as the owner of Ashford and a "Texas conservative [who] has remained unwilling to return his loans even as public anger builds over large companies getting the funds – a fact now drawing scrutiny of a key lawmaker."[125] The article continued, explaining that "Senator Chuck Schumer, the Democratic leader, sent a letter to the Small Business Administration demanding a thorough review of use of the program by Mr. Bennett's companies."[126] In that letter, Senator Schumer wrote that "[i]t is imperative that limited taxpayer dollars go to help legitimate small businesses."[127] The Ashford companies received a whopping $70 million in loans to help fund what was a heavily leveraged business.[128] Notably, these criticisms were not limited to publications and politicians falling into the same political camp as the New York Times.[129] In the same spirit as Senator Schumer, Senator

Business Administration's Implementation of the Paycheck Protection Program Requirements, Report No. 20-14 (May 8, 2020).

122. Primarily, the Inspector General's report compared statutory sections with language in rulemakings and FAQs rather than use data to identify whether lenders unduly favored preexisting clients. Office of Inspector General, *supra* note 121, at 8, 29.

123. As further specification, the inquiry could consider the extent of borrowers' indebtedness and independent resources for repaying those amounts when considering the extent to which lenders used PPP funds as credit support for their loans.

124. Jeanna Smialek & Kenneth P. Vogel, *Hotelier's Push for $126 Million in Small-Business Aid Draws Scrutiny*, N.Y. TIMES (May 1, 2020), https://www.nytimes.com/2020/05/01/business/economy/monty-bennett-small-business-loans-coronavirus.html [https://perma.cc/F9CP-PYLK].

125. *Id.*

126. *Id.*

127. *Id.*

128. Ashford subsequently returned loan amounts and has laid off approximately 13,000 employees since the start of the pandemic. Saphir & Schneider, *supra* note 66.

129. Many articles began with outraged headlines and introductions lambasting businesses for taking funds unjustifiably while subsequently acknowledging that no misbehavior occurred. *See, e.g.*, Ahuja & Gara, *supra* note 58.

Marco Rubio lambasted large businesses while distorting his voting record on the CARES Act.[130]

The Senators' rhetoric provides a case study in modern-day populism. It was predictable that large chains from restaurant and hospitality sectors would participate in the PPP. Indeed, the Senators in question voted for the language that qualified these businesses to participate. However, vociferously castigating relatively larger or more successful organizations served electioneering purposes. In the language of Gersen and Stephenson, the Senators "went out of [their] way to harass, burden, or persecute unpopular groups in order to credibly signal that [they were] not [ ] captured by, and [were] not secretly sympathetic to, those groups."[131] Prior crises taught lawmakers that holding elites "accountable" is a winning strategy for demonstrating independence, and this crisis was no exception notwithstanding that in this case decision-making by elites could not have been to blame for causing the catastrophe.[132]

Lawmakers' statements following the enactment of the CARES Act also crystalize the difficulties politics create for lawyers where favoritism disrupts the rule of law.[133] Senator Schumer did not claim

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130. *See* Sraders, *supra* note 48 (stating Sen. Rubio declared that "aiding multiple subsidiaries of a national brand [like Ruth's Chris] . . . was not the intent of Congress, and that the regulatory guidance [from the Treasury] does not reflect legislative intent and should be corrected"). Subsequently, Sen. Rubio qualified his criticism and defended the program, noting that public companies received only 0.35% of program funding. Zach Budryk, *Overwhelming Majority of Publicly Traded Firms Have Not Returned Small-Business Loans: Review*, HILL (May 24, 2020, 3:14 PM), https://thehill.com/policy/finance/499386-overwhelming-majority-of-publicly-traded-firms-have-not-returned-small. It deserves mention that Sen. Susan Collins reportedly took a more pragmatic approach, engaging privately with administrators concerning problems applicants were having with the program. O'Connell et al., *supra* note 6.

131. *Over-Accountability*, *supra* note 19, at 203.

132. *See* Adam C. Pritchard, *Populist Retribution and International Competition in Financial Services Regulation*, 43 CREIGHTON L. REV. 335, 344–45 (2010) (discussing legislators' populist maneuvers to stimulate and harness anger); Stephen M. Bainbridge, *Dodd-Frank: Quack Federal Corporate Governance Round II*, *supra* note 18, at 1785–86.

133. Letters from Republicans and Democrats in the House encouraging the SBA and Treasury to make funds available for startups were discussed above. Similar after-the-fact letters from lawmakers urged other changes. These ex post requests from lawmakers complicated already-rushed work for SBA and Treasury personnel as well as for the private sector lawyers advising on the CARES Act and their clients. As one example, a bipartisan group of nineteen senators wrote to request that the condition to loan forgiveness requiring at least 75 percent of the proceeds be put towards payroll expenses be relaxed. Sylvan Lane, *Bipartisan Group of Senators Asks Treasury, SBA to Loosen Coronavirus Loan Restrictions*, HILL (May 6, 2020, 1:06 PM), https://thehill.com/policy/finance/496391-bipartisan-group-of-senators-asks-treasury-sba-to-loosen-coronavirus-loan. This request would have the effect of shifting the program from one aiming to contain unemployment to one aimed at supporting business opera-

that the legislation he voted for alongside majorities in both houses of Congress does not authorize the loan to Ashford.[134] Rather, Senator Schumer claimed that as a matter of private decisionmaking, the funding should not have been extended. Ashford[135] and other large businesses such as the Ruth's Chris chain of steakhouses, Shake Shack chain of burger joints, Potbelly chain of sandwich shops, and Kura Sushi bent to the bully pulpit and returned funding.[136] These incidents show that as advisors, lawyers must appreciate not only what the law permits but what managed public opinion will allow. This foresight is difficult when advice is given hastily with less than twenty-four hours between regulations being published and a program initiating.

This incident also points to a challenge that lies in the hinterlands between legislative history and public opinion. The Senate inserted an unusual provision in the CARES Act, which has questionable force as law. The provision explains that "[i]t is the sense of the Senate that the [SBA] should issue guidance to lenders and agents to ensure that the processing and disbursement of covered loans prioritizes small business concerns and entities in underserved and rural markets, including veterans and members of the military community, small business concerns owned and controlled by socially and economically disadvantaged individuals . . . , women, and businesses in operation for less than 2 years."[137] The House declined to issue a similar statement or endorse the "sense of the Senate;" however, the House agreed to print

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tions more generally. *Id*. Ultimately, Congress would statutorily retroactively reduce the 75 percent threshold to 60 percent in June. *See* Flexibility Act, *supra* note 41.

134. There were four abstentions on the bill in the Senate. *See* 166 CONG. REC. S2060 (2020) (roll call vote on Passage of H.R. 748 As Amended). The House adopted the Act by a voice vote. David Morgan, *Speak, Then Clean–U.S. House Guidelines for Coronavirus Debate*, REUTERS (Mar. 26, 2020), https://cn.reuters.com/article/us-health-coronavirus-usa-debate-idINKBN21D3JI. *See* Sraders, *supra* note 48.

135. Bill Hethcock, *Dallas-Based Ashford, Braemar Missing Payments on 'Nearly All' Hotel Loans after Returning PPP*, DALL. BUS. J. (May 22, 2020, 10:59 AM), https://www.bizjournals.com/dallas/news/2020/05/22/ashford-braemar-hotels-default.html.

136. *See, e.g.*, Neil Barofsky, *Why the Small-Business Bailout Went to the Big Guys*, BLOOMBERG (Apr. 30, 2020, 6:00 AM), https://www.bloomberg.com/opinion/articles/2020-04-30/why-small-business-bailout-went-to-shake-shack-and-ruth-s-chris ("Americans are rightly outraged after learning that many large companies, including Shake Shack and Ruth's Chris Steakhouse, received millions of dollars from a coronavirus response program that was supposed to go to small businesses. . . . The finger-pointing for the current program has now begun in earnest. Treasury Secretary Steve Mnuchin is blaming the large corporate borrowers for joining the program – for which many appear to have been fully qualified – and even threatening them with prosecution.").

137. CARES Act § 1102(a)(2).

the "sense of the Senate" in the bill presented for the President's signature. What effect does this statement have as a matter of law? It is a curious question, but one that does not directly impact the story because no such rulemaking was completed before the program ran out of funds.

The public opprobrium that chains of hotels, restaurants and other large businesses faced after receiving funds points to another curious question. As a matter of policy aimed at preserving employment,[138] what is the difference between workforce contractions at, for example, ten independently run motels or restaurants, on the one hand, and ten commonly owned motels or restaurants, on the other hand? The question of distinguishing between standalone businesses and locations of larger chains is not trivial. On the one hand, larger businesses have more scale to support overhead such as dedicated legal and finance functions that can ease access to capital, implying that these businesses need the support less than smaller outfits.[139] On the other hand, these businesses were justifiably singled out in the legislation due to widely applicable mandatory closures within these industries, and even where government mandates were absent, consumer decisions to avoid travel, hotel stays and restaurants. Revenue impacts of COVID-19 were felt especially heavily in the food and hospitality industries,[140] which successfully lobbied to have the general 500 employee restriction relaxed to apply on a location by location basis rather than business-wide.[141] Although lawmakers and media excoriated larger companies for exercising their statutory rights to participate in the program (again, leading many to return funds), it is far

138. Business Loan Program Temporary Changes; Paycheck Protection Program–SBA Loan Review Procedures and Related Borrower and Lender Responsibilities, 85 Fed. Reg. 33,010, 33,012 (June 1, 2020) ("[T]he CARES Act's central purpose [is] keeping workers paid and employed.").

139. Ruth Simon & Peter Rudegeair, *Small Businesses Tackle New PPP Puzzle: Forgiveness*, WALL ST. J. (June 14, 2020, 8:00 AM), https://www.wsj.com/articles/small-businesses-tackle-new-ppp-puzzle-forgiveness-11592136025 ("The [loan forgiveness] process is particularly daunting for small companies such as Reddell's Glass & Metal Inc. . . . that received a roughly $45,000 PPP loan . . . 'If you have a 100-person company, most likely you will have a CFO, a controller, people that deal with this,' said Reddell owner Guy England, who writes payroll checks manually each week for his six full-time employees."); *see also* Hayashi et al., *supra* note 72 (reporting that National Small Business Association survey identified that over half of small business respondents don't have employees or manage payroll themselves, which entails difficulty in understanding qualification for PPP loans and eligibility for loan forgiveness).

140. Hayashi et al., *supra* note 72 ("The hotel and food-services industry shed 40% of its jobs, 5.7 million, from January to May, the most of any economic sector.").

141. *See* Sraders, *supra* note 48, and surrounding text.

from clear that as a policy matter PPP funds should not have been available to maintain payroll at these chains.[142]

Large hotel and restaurant chains were not the only fund recipients that acquired tar and feathers. Lawmakers and media lambasted companies that had legal troubles, private schools with substantial endowments,[143] companies that had prior to 2020 offered seven-figure compensation to their executives, and other organizations that did not fit the mold of a salt-of-the-earth, high-integrity outfit irrespective of whether their workforces were in jeopardy.[144] Within days of the PPP exhausting funds, the public narrative began to lump technology startups with these undeserving others. As a typical piece explained:

> Questions about whether the funds were disbursed fairly and whether some applicants deserved them have drawn scrutiny to the aid program. . . . Now, scrutiny of the program has reached technology start-ups . . . . While many of these young companies have been hurt by the pandemic, they are not ailing in the same way that traditional small businesses are. Many mom-and-pop enterprises, which tend to employ hourly workers and operate on razor-thin margins, are shutting down immediately because of economic pain or begging for donations via GoFundMe campaigns. But start-ups, which last year raised more than $130 billion in funding, have sometimes turned to the government loans not for day-to-day survival but simply to buy useful time.[145]

142. Some will say that these chains and other businesses should have followed their moral compass to maintain employee levels without turning to PPP funds. This raises the old stakeholder debate as to whether and when management, directors, or equivalent decision makers should exercise their authority to favor employees or other stakeholders over owners. This debate goes beyond the scope of this Article, and takes different turns depending on how and where an entity is formed as well as its governance documents. However, even if decisionmakers were intent on maintaining employee levels regardless of costs to owners, there is still the question of whether to participate in a government run bail-out program for which the organization is eligible.

143. James Politi & Kiran Stacey, *US Private Schools Told to Return Coronavirus Rescue Loans*, FIN. TIMES (May 1, 2020), https://www.ft.com/content/2e584d52-4c46-4f85-9cc8-6cf3361a1ba1.

144. Jessica Silver-Greenberg, David Enrich, Jesse Drucker & Stacey Cowley, *Large, Troubled Companies Got Bailout Money in Small-Business Loan Program*, N.Y. TIMES (Apr. 26, 2020), https://www.nytimes.com/2020/04/26/business/coronavirus-small-business-loans-large-companies.html.

145. Erin Griffith and David McCabe, *Start-Ups Pursue 'Free Money' with Relief Funds, Prompting Backlash*, N.Y. TIMES (Apr. 27, 2020), https://www.nytimes.com/2020/04/27/technology/startups-sba-loans-backlash.html. *See* Winkler & Chernova, *supra* note 93.

The PPP's design ensured that these questions would not be answered in a satisfactory way.[146] As discussed above, eligibility for PPP funds did not require an applicant to show that they had insufficient liquidity to meet amounts payable in the ordinary course. Congress or the SBA could have imposed such a requirement through a variety of formulations but elected not to.[147] Similarly, Congress and SBA could have created a staged distribution of funds with applicants showing low account balances relative to historical expenditures granted priority. But again, the standard that Congress drafted and that SBA elected not to refine treated strategic operational shifts no differently from operational shifts mandated by imminent lack of funding.

There is ample policy justification for the broad standard that Congress and the SBA adopted and borrowers relied on. If the PPP aims at staunching unemployment and other payroll reductions, then there is reason for the program to be agnostic as to whether the reductions were prompted by strategic decision-making, on the one hand, or more exigent circumstances such as lack of funds to support preexisting levels of compensation, on the other hand. The agnostic viewpoint is reflected in the text of the CARES Act. If the PPP was meant to target "mom-and-pop enterprises" suffering cash shortages then the PPP did not work and, from its outset, was not drafted to work.

There were alternatives available to legislators that could have targeted PPP funds towards smaller, less sophisticated or more cash-strapped businesses. It would have been trivial for Congress to bin distribution of funds, for example, based on the number of employees an organization has. To illustrate, some percentage of PPP funds would have been available for businesses with under ten employees, another percentage for businesses with under twenty-five employees, and so on. This would have assured that larger businesses did not compete with smaller businesses for scarce funds. Alternatively, Congress could have provided for staged distribution with initial loans limited to, for example, $250,000 per borrower. This would have assured slower depletion of funds while allowing smaller businesses to continue operations. But again, Congress chose not to refine the allocation of PPP funding so as to avoid the stampede. Whether these drafting decisions represent a bug or a feature is a question returned to

146. It is also worth asking whether it is relevant to a specific startup applying for PPP funds that startups in aggregate received $130bn in funding.

147. *See* Naomi Jagoda, *Mnuchin: Hardest Hit Businesses Should Be Able to Get Second PPP Payment*, HILL (July 17, 2020, 12:58 PM), https://thehill.com/policy/finance/507830-mnuchin-hardest-hit-businesses-should-be-able-to-get-second-ppp-payment (relating that Treasury Secretary Steven Mnuchin proposed that additional PPP funding should go to "businesses that have significant revenue declines").

below, but because of the obvious nature of the alternatives available to lawmakers, it is doubtful that they were not willfully ignored by at least some of the elected members of Congress.[148]

i. SBA & Treasury Guidance Strongarms Qualified Borrowers, Showing Tension Between Populism and Rule of Law

After PPP funds ran out and the finger-pointing began, members of Congress began work on allocating a new round of funding while SBA prepared additional guidance. On Thursday, April 23, a week after funding ran out, Treasury released new guidance on eligibility for PPP funds. The guidance provides that:

> [A]ll borrowers must assess their economic need for a PPP loan under the standard established by the CARES Act and the PPP regulations at the time of the loan application. Although the CARES Act suspends the ordinary requirement that borrowers must be unable to obtain credit elsewhere . . . borrowers still must certify in good faith that their PPP loan request is necessary. [sic] Specifically, before submitting a PPP application, all borrowers should review carefully the required certification that '[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant.' Borrowers must make this certification in good faith, taking into account their current business activity and their ability to access other sources of liquidity sufficient to support their ongoing operations in a manner that is not significantly detrimental to the business. For example, it is unlikely that a public company with substantial market value and access to capital markets will be able to make the required certification in good faith, and such a company should be prepared to demonstrate to SBA, upon request, the basis for its certification.[149]

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148. *See* Sraders, *supra* note 48 (reporting advice from Ryan Metcalf, the head of U.S. regulatory affairs for Funding Circle, that "if the SBA wanted to cater to the smallest businesses, it would allot separate money for loans $50,000 and under, or for companies with 20 or fewer employees, for example, rather than refueling smaller lenders whose average loan size can be in the hundreds of thousands"). Months after this Article was developed and distributed via SSRN, the terms for obtaining PPP funding were revised under the Biden administration. Dan Primack, *Why Biden Hit Pause on PPP Loans for Businesses with Over 20 Employees*, AXIOS (Feb. 26, 2020), https://www.axios.com/paycheck-protection-program-ppp-biden-congress-96697b57-e725-4de5-bb57-25c0f2656e1a.html. The changes to the PPP adopted some of the alternatives this Article considers above, including binning for smaller businesses and requirements for borrowers to show decreased revenues. *Id.*

149. The guidance was published as a revision to a list of Frequently Asked Questions (FAQs) on the Treasury's website. SMALL BUSINESS ADMINISTRATION, PAYCHECK PROTECTION PROGRAM LOANS FREQUENTLY ASKED QUESTIONS 11 (FAQs) (2020).

The new guidance twisted without breaking criteria for eligibility. Although it did not expressly claim to do so, the guidance invited the reading that it applied retroactively.[150] Having added new criteria that borrowers "should assess" when determining whether they "in good faith" qualified for the funding, the guidance continued that "[a]ny borrower that applied for a PPP loan prior to the issuance of this guidance and repays the loan in full by May 7, 2020 will be deemed by SBA to have made the required certification in good faith."[151] The guidance did not address the equities of retroactive application.[152] Nor did the guidance elaborate on the new requirement that borrowers must be unable "to access other sources of liquidity sufficient to support their ongoing operations in a manner that is not significantly detrimental to the business." Would available but costly capital in the form of debt or equity from preexisting or new investors preclude a company from participating in the PPP? Would the costs of capital only matter if they fell on the business rather than investors? Would that mean dilution through issuance of new equity would be inadequate to qualify for funds while potential changes in the profile of owners and their preferred strategies for the business would serve as a valid basis? The surprising guidance raised far more questions than it answered and reflected the populist attitudes exhibited by lawmakers and media. Although formally lacking the force of law, the guidance created unease among borrowers. As discussed above, numerous companies returned PPP funding around the time of this guidance whether out of concern with enforcement risk or for reasons of public relations.[153]

150. *See* Primack, *supra* note 148 (discussing pressure put on large borrowers due to new guidelines from Treasury).

151. Small Business Administration, *supra* note 149.

152. *Id.* The preamble to the FAQ explained that "[t]he U.S. government will not challenge lender PPP actions that conform to this guidance, and to [rulemakings implementing the PPP] in effect at the time." In a footnote to that statement of enforcement policy, the FAQ stated that in contrast to the rulemakings, "[t]his document does not carry the force and effect of law independent of the statute and regulations on which it is based." *Id*. at 1. In referencing Treasury regulations in effect at the time of the borrowing, the FAQ may have been acknowledging that it could not retroactively change qualification standards. However, the preamble was far removed textually from new guidance and furthermore, the new criteria for assessing the good faith of borrower certifications coupled with a safe harbor from findings of bad faith for borrowers refunding loans, suggested enforcement risk based on retroactively applied standards. This implication compounded by a media frenzy, irrespective of whether any enforcement action would be sustained by a court, could be enough for sensitive borrowers to withdraw from the program. Indeed, after the April 23 guidance, many of the borrowers that were criticized for accepting PPP loans did return their funding.

153. *See* Ken Tysiac, *SBA Extends Safe Harbor for Returning PPP Funds*, J. Acc. (May 6, 2020), https://www.journalofaccountancy.com/news/2020/may/sba-extends-

The populist tone was only solidified in subsequent guidance. On May 6, SBA explained that "any borrower [that] received PPP loans with an original principal amount of less than $2 million dollars will be deemed to have made the required certification concerning the necessity of the loan request [i.e., that current economic uncertainty makes this loan request necessary to support the ongoing operations of the borrower] in good faith."[154] Notably, this safe harbor was not phrased solely in terms of administrative efficiency, in which case the safe harbor would not have deemed the "good faith" requirement to have been met by qualifying loans. Rather, the safe harbor was phrased to express that loans of two million dollars or more were less likely to qualify under the statutory standard (notwithstanding that the statute contemplated loans of up to ten million dollars).[155] It deserves reflection that the SBA went so far as to express a presumption that borrowers receiving more funds were likelier to be engaging in fraud (as opposed to having a larger business with more expenses)![156]

The chorus of hostility from Congress, agencies and the media effectuated a rebalancing of PPP disbursements. Although need-based criteria were not tailored through law, ex post, the vitriol shifted the

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safe-harbor-for-returning-ppp-funds.html. Shortly after threats of enforcement from Treasury, the Department of Justice took action in what is alleged to be a simple case of egregious fraud involving two men that fabricated payroll information in applying for PPP loans. Laura Noonan, *Two Men Charged with Scheme to Defraud US Rescue Loan Fund*, FIN. TIMES (May 5, 2020), https://www.ft.com/content/185eb4fb-8542-4fcb-830d-e129663a800e. The DOJ also initiated a broader investigation into PPP lending practices, issuing subpoenas to large banks involved in the program. Koh Gui Qing & Pete Schroeder, *Exclusive: U.S. Justice Dept. Subpoenas Wall Street Banks for Small Business Loans Info-Sources*, REUTERS (May 15, 2020, 7:10 PM), https://www.reuters.com/article/us-usa-doj-banks/exclusive-u-s-justice-dept-subpoenas-wall-street-banks-for-small-business-loans-info-sources-idUSKBN22R3EZ. *Cf. supra* note 46 and surrounding text.

154. SMALL BUSINESS ADMINISTRATION, *supra* note 149.

155. *See id.* at Question 46 ("SBA has determined that this safe harbor [for loans under $2mm] is appropriate because borrowers with loans below this threshold are generally less likely to have had access to adequate sources of liquidity in the current economic environment than borrowers that obtained larger loans. This safe harbor will also promote economic certainty as PPP borrowers with more limited resources endeavor to retain and rehire employees. In addition, given the large volume of PPP loans, this approach will enable SBA to conserve its finite audit resources and focus its reviews on larger loans, where the compliance effort may yield higher returns.").

156. The potential penalties when SBA believes that a borrower does not qualify for a loan are generally limited to the borrower returning the full amount of the loan to the lender. *Id.* Furthermore, borrowers were invited to proactively return their proceeds on or before May 18, in which case they were eligible for a safe harbor from enforcement. Business Loan Program Temporary Changes; Paycheck Protection Program—Second Extension of Limited Safe Harbor With Respect to Certification Concerning Need for PPP Loan and Lender Reporting, 85 Fed. Reg. 31,357, 31,358 (May 26, 2020).

policy effects of the PPP from generally slowing unemployment to subsidizing business continuity for smaller and more sympathetic concerns. This incident shows extratextual, quasi-democratic forces shaping legal systems. From a perspective that views the initially written PPP as overbroad, this incident also shows how an iterative, bottom-up process can significantly refine law, albeit without reference to procedural legislative or regulatory norms. As discussed above, however, the shifting goalposts also complicate the work of lawyers and undermine predicates to the rule of law.

When the PPP went into effect, lenders and borrowers turned to their in-house and law firm attorneys to assess who may borrow pursuant to the terms of the program. These initial predictions, for which clients paid and on which clients relied, were established on shifting sands due to the lawmaking context. Moreover, lawyers without political savvy were less able to provide apt advice due to evolving discrepancies between governmental positions, on the one hand, and legal authorities, on the other hand. This poses an additional concern with this style of lawmaking, namely, its distributive impact within the legal community and among clients. To the extent lawyers' predictive power is based on publicly available information rather than relationships and similarly exclusive assets, income within the legal industry will be more equitably distributed and clients will have less restricted access to sound legal advice. But if knowing what the law allows requires predicting what a Senator or newspaper may subsequently write, relationships and access to positions of influence become more important. This suggests a counter-intuitive result of populist pressure, in that it may create a more relationship-based legal system (i.e., the kind of non-transparent, elite-dominated legal institutions that populism is a reaction to).

Notwithstanding the chorus of criticism shifting distribution of PPP funds, small businesses insistent on the rule of law and less sensitive to the public relations consequences could theoretically—absent time and other resource constraints—challenge administrative decisions in court. Indeed, while funds from the second round of the PPP remained available in early May, U.S. District Judge Matthew Leitman enjoined the SBA from discriminating against banks, political lobbying firms, strip clubs and certain additional "unsavory" businesses.[157] But it is questionable whether other disfavored businesses that were not already subjects of public opprobrium could practicably

157. Jonathan Stempel, *Strip Clubs, Other 'Disfavored' Businesses Entitled to Emergency Loans in Pandemic: U.S. Judge*, REUTERS (May 11, 2020, 6:11 PM), https://www.reuters.com/article/idUSKBN22N2YG.

challenge SBA decisions, let alone lender-level policies. For example, would a hotel chain sue the federal government to be permitted to participate? As discussed above, popular restaurant chains and other businesses catering to broad classes of consumers and thus sensitive to public opinion returned PPP funds in response to criticism.

Furthermore, extralegal concerns (such as stigma attached to some industries) permit agencies to pick winners and losers. The SBA, after deliberation, allowed gambling businesses to participate.[158] And from the outset, drinking establishments were welcome participants. To what extent should the SBA apply moral or ethical criteria when deciding industry eligibility? Should it be up to agency personnel to determine that financial firms and lobbyists should not participate while bars, liquor stores, and racetracks are welcome?[159]

ii. Did the PPP Deflect Blame from Public Bodies?

There is another view, however, from which to assess the disappointed and angry response to the first round of the PPP. COVID-19 and related health measures promised unprecedented tolls in terms of health and economic wellbeing. As infection spread in March, there was no doubt that millions of Americans would suffer. If one further supposes that people prefer to pin their suffering on other humans rather than attribute it to something more amoral, systemic and mysterious, then the CARES Act can also be analyzed as a tool to shape public perception of culpability for the harms of the crisis.[160] Lacking another scapegoat, many Americans would blame the government as inadequately responding to the crisis. In retrospect, the program's design created several levels of delegation that could be exploited to

158. Business Loan Program Temporary Changes; Paycheck Protection Program—Requirements—Promissory Notes, Authorizations, Affiliation, and Eligibility, 85 Fed. Reg. 23,450, 23,451 (Apr. 28, 2020) (reversing Treasury's prior rulemaking position that limited participation in PPP by legal gaming businesses).

159. Moral suasion also affected lender choices. Responding to a combination of public relations concerns and internal commitments to pro-social missions, lenders voluntarily pledged funds to relief efforts. Caroline Hudson, *Bank of America Pledges $250M for CARES Act Small Business Loan Program*, CHARLOTTE BUS. J. (Mar. 30, 2020, 12:30 PM), https://www.bizjournals.com/charlotte/news/2020/03/30/bank-of-america-pledges-250m-for-cares-act-small.html.

160. Jeffrey J. Rachlinski & Cynthia R. Farina, *Cognitive Psychology and Optimal Government Design*, 87 CORNELL L. REV. 549, 608 (2002) ("Observations about human vulnerability to self-fulfilling prophecies warn that a formally endorsed, widely promulgated model of civic behavior which blames bad outcomes on the inevitability of greedy, self-serving action might itself become outcome determinative."). Outside the legal field, political scientists study how members of Congress and other political actors shape rather than reflect public opinion. *See generally* LAWRENCE R. JACOBS & ROBERT Y. SHAPIRO, POLITICIANS DON'T PANDER (2000).

reallocate blame. This is another frame that can be used to understand the misdirected outrage of lawmakers reacting to nothing more than the inexorable working of the program they drafted and voted for.

Addressing unemployment stemming from COVID-19 required tremendous vision, resources, and coordination. Crucially, Congress needed infrastructure through which to send funding to qualifying businesses in exchange for the businesses retaining payroll. The lack of pre-existing infrastructure through which funding could be efficiently targeted to preserve payrolls was a critical constraint. Political polarization, arguable lack of competence in senior governmental posts, and federalist decentralization (whether legal or norms based) further reduced capacities for coordination when the pandemic began to spread across the U.S. in March. As a result of these challenging demands and constraints, the question in designing the CARES Act was how to do more with less? With the Scylla and Charybdis of infection and economic distress, tragedy was inevitable. Through delegating, Congress created a new focal point for frustrations.[161] Rulemaking was delegated to the SBA and Treasury. In turn, lending was delegated to banks and other private actors. And, as discussed above, the decision whether to accept PPP funds was significantly delegated to the borrowers themselves.

As explained above, small businesses, independent contractors, the self-employed, not-for-profits and other eligible program participants represent well over 80 million adults[162] — many of them middle class voters. Through delegating funding and setting up a scramble, the PPP's design assured that there would be private parties to share the blame when funding ran out. The PPP's design established these "intervening causes" that could be blamed for failure.[163] Banks and other lenders could be blamed for favoring their own clients or otherwise discriminating against hard-hit salt-of-the earth small businesses. Coastal startups, large businesses, and other unpopular actors in the economy could be cast as seizing program funds. The headlines were predictable and distracted from the simple fact that initial PPP funds were significantly insufficient. However, in explaining some of the inequitable and unfortunate outcomes of the rollout, critics blamed

161. Rabin, *supra* note 12, at 1220 (discussing importance of media to inciting populist discontent).

162. *See* SBA Office of Advocacy, *supra* note 99 and surrounding text.

163. Rabin, *supra* note 12, at 1250 ("The WPA was highly visible and created the unmistakable impression that government spending was being used to attack the Depression psychology, stimulate demand, and ultimately, it was hoped, achieve economic recovery.").

program participants rather than acknowledging that the program's design predictably led to these outcomes.[164]

If the PPP had been given more resources from the outset, the cacophony of blame could have been avoided. As discussed below, when an additional $310 billion became available through the PPP in its second round, disbursement significantly slowed. In the two weeks following the second round's rollout, approximately $188 billion was used with daily loan approvals slowing to $2 billion per day by the end of the period. This suggests that a larger initial grant would have satisfied applicants and avoided the hullabaloo that ensued when the first round of PPP funds ran out.[165] One explanation for underfunding in the first round is that Congress estimated a smaller amount would be sufficient to support eligible participants.[166] Similarly, Congressional actors may not have been able to come to agreement on a larger amount without taking significantly more time to negotiate. Subject to the pragmatic constraints of crafting consensus and appropriating funds, it would have been reasonable for Congress to err on the side of overfunding the program and have a balance remaining rather than underfund and cause the clamor that ensued.

iii. Most Flaws in the PPP Stem from its Design Rather than its Implementation

While disbursements from the first round of PPP funds met vociferous criticism in the popular press, a review of the program shows its remarkable achievements. Without guidance or documentation until twenty-four hours prior to its initiation, the first round of the PPP

164. Rulemakings implementing the PPP both shape history and make law. In describing the origins of the program, the non-independent agency specifically referred to only a single public official, the President, as managing the response to the crisis: "On March 13, 2020, President Trump declared the ongoing Coronavirus Disease 2019 (COVID–19) pandemic of sufficient severity and magnitude to warrant an emergency declaration for all states, territories, and the District of Columbia. . . . On March 27, 2020, the President signed the . . . CARES Act . . . to provide emergency assistance and health care response for individuals, families, and businesses affected by the coronavirus pandemic." April 2 Rule, 85 Fed. Reg. at 20,811.

165. Take-up of funds in the second round may have been greater if not for the adverse attention directed to PPP participants during April. Thus, an initial appropriation comparable in size to the first two appropriations may not have sufficed.

166. There is reason to doubt, however, that congressional actors should have viewed the initial allocation as sufficient. *See* Bureau of Labor Statistics, *supra* note 102 and surrounding text. *See also* higher estimate of required funds for the PPP from Bartik et al., *supra* note 64.

was able to disburse loans to 1,661,367 different businesses.[167] Almost five thousand distinct lenders participated over those two weeks.[168] These figures represent an exceptional level of uptake across borrowers and lenders, which the design of the program encouraged through effectively paying businesses to maintain payroll and providing lenders with a riskless revenue stream.

The first round of the program successfully enrolled smaller lenders, and indirectly, their customers. Notwithstanding high levels of concentration in the banking industry, the top fifteen banks distributed only about 26 percent of PPP funds in the first round.[169] A number of factors may explain the observed success of smaller banks.[170] Larger lenders focused on building out technology to process PPP applications at scale, thus delaying initiation of lending under the program. Loan officers at smaller lenders may have also felt sharper impetus to promote the program to clients.[171] High-touch lending in the small business sector has been on the decline[172] due to efficiency gains from automating documentation and decisioning as well as suspicion of decisions driven by subjective assessments. Technology and proceduralization have served as scalable substitutes to relational banking. Relative to larger rivals, however, smaller lenders transitioned more slowly to scalable, capital-intensive, technology-driven approaches. The relative persistence of subjective credit assessments based on meaningful interactions may have created stronger ties between smaller lenders and their business customers, leading to greater proactive outreach by smaller lenders. Loan officers at these smaller institu-

167. SMALL BUSINESS ADMINISTRATION, PAYCHECK PROTECTION PROGRAM (PPP) REPORT (APPROVALS THROUGH 12PM EASTERN ON 4/16/2020) 2 (2020) [hereinafter FIRST PPP REPORT].

168. *Id*.

169. *Id*. at 6. Compare this with the assets of the top five U.S. banks, which represent over 45 percent of the industry's assets since 2010. *See* FED. RESERVE BANK ST. LOUIS, 5-BANK ASSET CONCENTRATION FOR UNITED STATES (2019) [https://perma.cc/6HK3-LRL2].

170. Peter Rudegeair, Orla McCaffrey & Liz Hoffman, *Small Businesses Were at a Breaking Point. Small Banks Came to the Rescue*, WALL ST. J. (May 4, 2020, 9:52 AM), https://www.wsj.com/articles/small-businesses-were-at-a-breaking-point-small-banks-came-to-the-rescue-11588590013. Haoyang Liu and Desi Volker found that the presence of community banks is a strong predictor of first round PPP funding within a state, while infection rates and unemployment are not. Liu & Volker, *supra* note 72.

171. O'Connell et al., *supra* note 6 ("Large banks, leery of inadvertently misusing taxpayer money, waited for more clarity from the government before they started lending. Community bankers asked staff members to work overtime, but even the most successful ones say it was nowhere near enough.").

172. Craig Hall, *How the Decline in Community Banks Has Hurt U.S. Entrepreneurship*, BARRON'S (May 18, 2019, 9:00 AM), https://www.barrons.com/articles/how-the-decline-in-community-banks-has-hurt-u-s-entrepreneurship-51558184413.

tions may have been driven both by their connections to their employer and connections to their customers.[173] Smaller lenders may have been nimbler, more hungry or otherwise faster to offer PPP to their clients. In a working paper, Professors João Granja, Christos Makridis, Constantine Yannelis, and Eric Zwick show that relative geographic availability of PPP funds in the first round was inversely related to the footprint of the largest banks in the small business lending sector of the relevant area.[174] These results further suggest that smaller lenders were faster on the uptake.

The SBA released limited information as to how funds from the first round of PPP were distributed in mid-April.[175] Analysis of this data reflects that the number of loans within a state is proportional to the number of small businesses within the state, and the amount of PPP funds disbursed within a state is proportional to the small business payroll within that state.[176] Figures 3 and 4 show these relationships, reflecting that PPP funds were targeted roughly in line with qualification:

173. In other words, loan officers at smaller lenders may have been more motivated to serve their employer as well as more motivated to serve their client.

174. João Granja, Christos Makridis, Constantine Yannelis & Eric Zwick, *Did the Paycheck Protection Program Hit the Target* 10 (Nat'l Bureau of Econ. Rsch., Working Paper No. 27095, 2020). In the second round of funding, however, the larger banks' investment in PPP-specific technology paid off. *See* Elizabeth Dilts Marshall & Michelle Price, *Biggest U.S. Banks Says They Submitted $45.8 Billion in Loans for Emergency Aid Program*, REUTERS (Apr. 30, 2020, 8:30 AM), https://www.reuters.com/article/us-health-coronavirus-jp-morgan-loans/biggest-u-s-banks-says-they-submitted-45-8-billion-in-loans-for-emergency-aid-program-idUSKBN22C270.

175. FIRST PPP REPORT, *supra* note 167.

176. Information on the number of small businesses by state and their annual payroll is drawn from available Insurance Information Institute statistics. *A Firm Foundation: How Insurance Supports the Economy: Small Businesses by State, 2016 (1)*, INS. INFO. INST., https://www.iii.org/publications/a-firm-foundation-how-insurance-supports-the-economy/a-50-state-commitment/businesses-by-state [https://perma.cc/4U2H-RXFG].

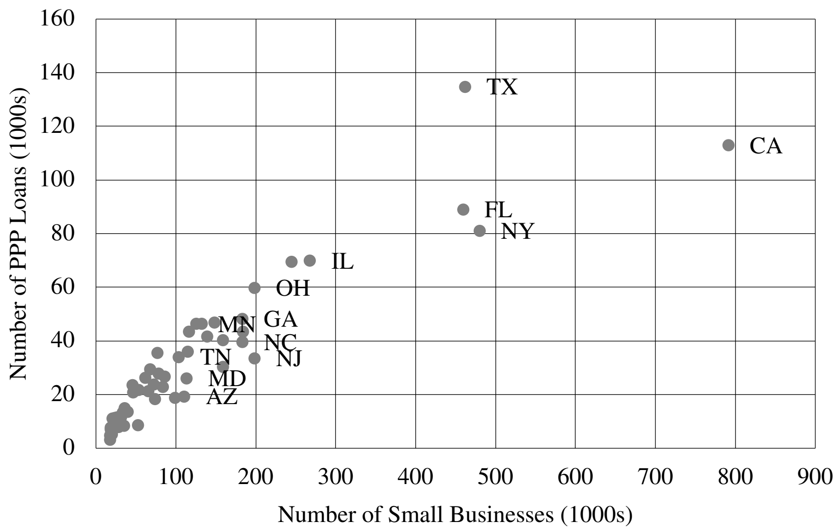

FIGURE 3: NUMBER OF PPP LOANS BASED ON NUMBER OF SMALL BUSINESSES[177]

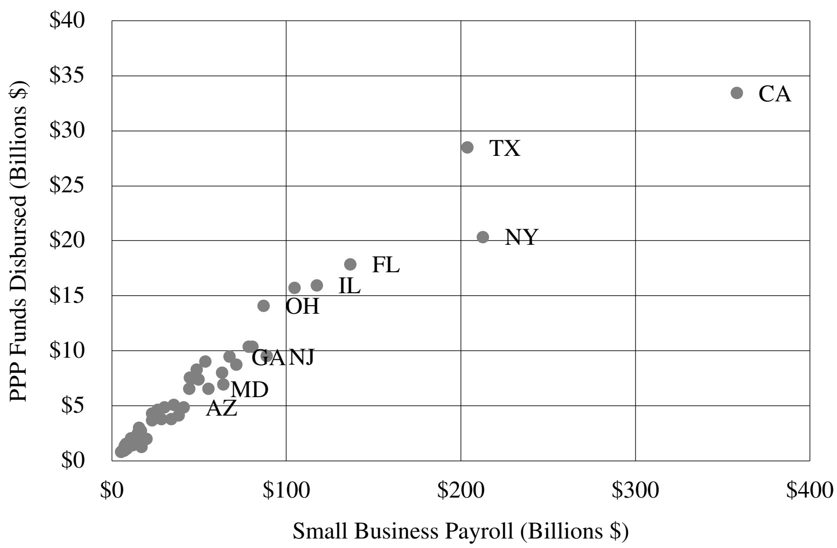

FIGURE 4: AMOUNT OF PPP LOANS DISBURSED BASED ON SMALL BUSINESS PAYROLL[178]

177. Loans graphed thanks to data from FIRST PPP REPORT, *supra* note 167.
178. Claims graphed thanks to data from INS. INFO. INST, *supra* note 176.

Commentators have criticized the geographic distribution of the first round of PPP funding.[179] Indeed, midwestern states, such as Oklahoma and Nebraska, received proportionately more PPP funding per small business than coastal states, such as California, New York, and New Jersey.[180] But other criticisms of the PPP's distribution are misdirected. The program has been criticized for not distributing more funds to areas where COVID-19 infection or mortality rates were higher.[181] But Congress did not intend for the program to target areas with greater infection or mortality, or at the very least, the text of the CARES Act and relevant SBA regulations do not provide for such targeting.[182] Similarly, PPP disbursements have been criticized for not tracking state level unemployment data.[183] But the goal of PPP was not to provide relief to areas hit hard by payroll cuts. Rather, the goal of the program was to encourage businesses to *retain* payroll levels.[184]

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179. Philip Elliott & Chris Wilson, *'This Is a Shot in the Arm for Us:' How Small Midwest Businesses Are Outpacing Coastal States for Government-Backed Loans*, TIME (Apr. 17, 2020, 5:59 PM), https://time.com/5823430/midwest-small-businesses-federal-loans/; Dion Rabouin, *PPP Failed to Get Money to Industries and Areas Most in Need*, AXIOS (May 27, 2020), https://www.axios.com/ppp-small-businesses-distribution-e161a0d9-8dde-492e-b29b-3f715f9350f9.html.

180. Elliott & Wilson, *supra* note 179.

181. Liu & Volcker, *supra* note 72 (finding a "negative relationship between COVID-19 cases per capita and the share of small firms getting PPP funding", which the authors explain "suggest[s] that credit is misallocated."); *see* Granja et al., *supra* note 174, at 14 (similarly misdirecting criticism at PPP for not targeting areas with greater COVID-19 infection rates or death rates).

182. Nor have critics offered means to create dynamically updating laws that target aid based on how COVID-19 evolves from the end of March to the program's conclusion.

183. Liu & Volcker, *supra* note 72 (finding that based on "unemployment claims per capita in the four weeks starting March 15" there is no "statistically significant[relationship between] economic hardship due to COVID-19 and the chance of getting a PPP loan").

184. Joao Granja, Christos Makridis, Constantine Yannelis, and Eric Zwick provide an early assessment of the PPP program. Granja et al., *supra* note 174. Their work identifies an important factor for explaining the geographic distribution of PPP funds, specifically, lenders' ratio of participation in the PPP to their other small business lending. Geographies where deposits are predominantly with banks that outperformed PPP lending relative to typical small business lending, somewhat tautologically, received more PPP funds (both by amount and number of loans). In studying which banks' first round PPP lending under-performed their usual small-business lending, Granja et al. discover a powerful explanation. The top percentile of banks by total assets, which represent an enormous share of lending and deposits in the ordinary course, drastically under-perform when it comes to distributing PPP funds. *Id.* at 10. This suggests that regions where the behemoth banks (e.g., JPMorgan, Bank of America, Wells Fargo, Citibank, US Bank, Truist Bank, Capital One) were dominant would be underfunded. *See id.* at 30. These top tier banks dominated small business lending in some of the hardest hit areas, so that their internal operational lags or hesitations to implement PPP lending in the first round plausibly explains the geo-

Among other things, loan disbursement was initially conditional on at least 75 percent of the proceeds going to cover payroll, and loan forgiveness—a powerful incentive—was conditional on employee salaries being largely maintained and significant layoffs being avoided. The goal of the PPP was to reduce unemployment ex ante rather than address it ex post. Thus criticism that PPP funds were not disbursed in a manner correlated with unemployment claims fails to appreciate the design of the program.[185] Equally importantly, the language of the statute and regulations did not call for greater disbursements in areas with greater unemployment claim filings. While potentially attractive in the abstract, this was not the criteria for loan disbursements. The primary criteria for evaluating the success of the PPP should be whether areas that received disproportionate funding also had relatively higher payroll retention rates. In other words, were program participants more likely to retain their employees (and compensate them roughly in line with pre-COVID levels) than comparable organizations that did not participate in the PPP? A secondary consideration would be whether disproportionate receipt of PPP funds coincided with disproportionate survival of small businesses. In other words, were program participants more likely to survive without bankruptcy or other interruption than a control group? Positive results to the preceding two questions would speak well of the PPP.

VI.
Conclusion

On April 24, 2020, the 45th President signed the Paycheck Protection Program and Health Care Enhancement Act (the "Enhancement Act") into law.[186] Among other things, the Enhancement Act authorized an additional $310 billion in loans under the PPP. With this significant infusion, the program resumed on April 27.[187]

graphic disparities. *Id.* at 14 ("[O]ur bank-level results point to an important loan supply channel distorting the distribution of PPP loans."); *see also id.* at 14–15 (identifying that PPP funds were not distributed geographically in proportion to rough proxy for shelter-in-place restrictions).

185. Liu & Volcker, *supra* note 72 (acknowledging that "PPP loans could be viewed as a substitute for unemployment claims, since firms applying for PPP loans, and expecting relief, may refrain from reducing payroll or at least delay it"). Granja et al. similarly misdirect criticism at the PPP for under-distributing funds to areas that experienced greater unemployment or pre-PPP business closure. Granja et al., *supra* note 174, at 13.

186. Paycheck Protection Program and Health Care Enhancement Act Pub. L. 116–139, 134 Stat. 620.

187. Danielle Kurtzleben, *Why the Small Business Rescue Program Has Slowed Way Down*, NPR (May 28, 2020, 5:00 AM), https://www.npr.org/2020/05/28/863387203/

Performance of the PPP in its second round helps frame assessment of the first. While the initial $349 billion in PPP funds ran out in under two weeks, the additional $310 billion in PPP funds authorized on April 24 remained substantially available in early summer 2020.[188] Starting in mid-May, as prior borrowers returned funds and few new borrowers submitted applications, net borrowings under the program turned negative.[189] This suggests that higher initial funding levels would have avoided many sophisticated or large businesses being flogged for taking funds while smaller and less sophisticated businesses suffered cash shortages.

When releasing data on the PPP in early July, Treasury Secretary Steven T. Mnuchin heralded the program as "providing much-needed relief to millions of American small businesses [and] supporting more than 51 million jobs." As discussed above, "supporting" is an ambiguous word and there is at present insufficient data to judge whether the PPP efficiently achieved its goals. In a leading work on these questions, Professors Raj Chetty, John Friedman, Nathaniel Hendren, and Michael Stepner explore the impact of PPP funding on payroll retention.[190] Their analysis uses a difference-in-difference design to compare payroll losses between businesses eligible for PPP funds, on the one hand, and businesses ineligible for PPP funds, on the other hand. Chetty et al. find that pre- and post-April 3 (i.e., when PPP funding began), PPP eligible businesses reduced payroll at comparable rates to larger, ineligible businesses. This analysis supports that to the extent PPP tempered unemployment, it did so modestly.[191] It is likely that

why-the-small-business-rescue-program-has-slowed-way-down ("There was a mad dash for the first, $349 billion round of PPP money, which was gone in 13 days. This second round, of $310 billion, is going much more slowly, and still has more than $140 billion left one month later.").

188. *See An Update on the Paycheck Protection Program*, COMM. FOR A RESPONSIBLE FED. BUDGET (May 28, 2020), https://www.crfb.org/blogs/update-paycheck-protection-program ("From the data, it appears that most companies who wanted a PPP loan may have applied in the first round."); O'Connell et al., *supra* note 6 ("Once beset by a flood of complaints, balky computer systems, changed rules and frantic calls to the Treasury Department, the federal government's small-business Paycheck Protection Program is suddenly looking like a measured success.").

189. Saphir & Schneider, *supra* note 66.

190. Raj Chetty, John N. Friedman, Nathaniel Hendren & Michael Stepner, *How Did Covid-19 and Stabilization Policies Affect Spending and Employment? A New Real-Time Economic Tracker Based on Private Sector Data* 4–5 (Nat'l Bureau of Econ. Rsch., Working Paper No. 27431, 2020) ("Employment rates at firms with fewer than 500 employees (which were eligible for PPP assistance) increased by only 2 percentage points after the PPP was enacted relative to larger firms that were ineligible for PPP.").

191. The paper's views that the PPP largely funded infra-marginal firms where (substantial) layoffs or other payroll reductions would not have occurred in the absence of

further analyses will revisit this question while also commenting on whether the PPP contributed to maintaining payroll in the long term.[192] However, understanding whether PPP dollars translated efficiently into reductions in unemployment or maintenance of businesses that would have otherwise shuttered is not enough. A more difficult question for policymakers will be what could be done as an alternative to satisfy the goals of the PPP. At present, hindsight does not provide substantially better alternatives. And that may be the greatest endorsement the program receives and the lesson to be drawn from this traumatic experience. Effective economic support in times of crisis requires a "smart" funding mechanism that does not only provide funds to businesses and other organizations, but can do it quickly, at scale, and on the basis of complex economic conditions, such as loss of revenue or profit at the recipient and the structure of expenditures the recipient faces. Technology and greater in-housing of financial functions at government agencies such as the Federal Reserve can achieve these goals, but would do so likely at the expense of financial privacy. In preparing for the next crisis, this investment and tradeoff is worth considering.

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conditional PPP funding are consistent with the views above that the eligibility standard was written in a capacious manner.

192. Hayashi et al., *supra* note 72 ("The PPP was most helpful to enterprises able to continue operations or quickly reopen. It largely failed those that either closed during prolonged lockdowns, drew too few customers to afford more than a skeleton staff, or were overwhelmed by high overhead costs, such as rent."). This criticism of the PPP as not helping enterprises anticipating a prolonged lockdown misunderstands the PPP. Funds would be available to retain employees temporarily even if PPP funds were expected to be insufficient to bridge the period until COVID-19 related concerns abated.