

April 10, 2020

## **Congress Must Act Now to Remove Barriers Based on Arrest or Conviction History for Small Business Owners Seeking COVID-19 Federal Relief**

We oppose the restrictions based on arrest or conviction placed by the Small Business Administration (SBA) on the two small business programs authorized and funded by the CARES Act (see Appendix). With one in three Americans having some sort of record, and people with records experiencing an unemployment rate five times higher than the average rate, these restrictions will have a significant and detrimental impact on individuals, families, and communities across the United States. The restrictions will have a particularly harsh effect on minority business owners and employees who are disproportionately affected by the criminal legal system as a result of institutional discrimination. Specifically, these restrictions are:

- **Unnecessary and confusing:**

- There are no statutes requiring SBA to categorically disqualify individuals from its loan programs based on an arrest or conviction record; the authority to perform a background check does not translate into authority to exclude.
- SBA's proposed interim rule and policy guidance for the Paycheck Protection Program (PPP) and Economic Injury Disaster Loans (EIDL) programs **are far more exclusionary than its own existing regulations on record restrictions for small business loans**, which only exclude those with active cases.
- The new restrictions constitute **unnecessary overreach that interferes with the ability of small businesses to operate** and pay their employees.
- The PPP interim rule and policy guidance, including its application form, are confusing and likely to have a chilling effect that will discourage many eligible applicants. The EIDL guidance and application form are similarly confusing and are likely to have the same effect.

- **Inconsistent with Congress' intent:**

- The intention of the emergency relief programs authorized by the CARES Act is to sustain small businesses that are trying to save the economy by keeping people employed. **Eligibility requirements should be relaxed in these circumstances, not heightened as SBA proposes.**
- SBA's proposed new restrictions on eligibility for its loan programs, which already operate to exclude many people with a record, contravene the intent of the CARES Act, and are inconsistent with SBA's more general mandate of encouraging entrepreneurship and expanding access to employment.
- **A significant number of people with arrest or conviction history have established their own small businesses**, since it is frequently difficult for them to secure employment with others. Moreover, these businesses also tend to be more willing to hire employees with a record. Driving them out of business will result in a severe impact on employment of a population that already is disadvantaged in the workplace.

- A large percentage of small businesses are owned by single owners or a limited number of co-owners, so that any disqualification affecting 20%+ equity owners will have a significant impact on small business owners generally.
  - A policy that excludes from loan eligibility small businesses that are owned in whole or in part by people with arrest or conviction history is not only inconsistent with the CARES Act and the mandate of SBA's own authorizing statutes, it also **frustrates federal and state efforts to encourage the reintegration of individuals involved in the criminal legal system.**
- **Overbroad and unfair:**
    - The PPP's categorical bar based on certain arrest or conviction records means that there is **no opportunity for an individual determination** that considers factors such as rehabilitation, the circumstances of the conviction/disposition, or whether the nature of the underlying crime might adversely affect the ability to properly utilize the loan.
    - The EIDL program restrictions go even further by **asking about any involvement with the criminal legal system at any time**, and potentially exclude most applicants with any arrest or conviction record from the EIDL (the SBA has not provided guidance on this).
    - The PPP and EIDL restrictions extend to individuals that the criminal legal system has specifically determined should not be convicted of a crime, including those that participate in diversionary programs or obtain deferred adjudications – the very kinds of dispositions that are supposed to help protect people involved in the criminal legal system from harsh economic collateral consequences.
    - **The SBA's requirement that people disclose sealed and expunged records circumvents protections in state law** for these cleared records and is contrary to the intent and purpose of those laws.
  - **Racially discriminatory:**
    - The SBA's restrictions will have a **disparate impact on minority business owners and employees**, who are disproportionately affected by the criminal legal system as a result of institutional discrimination.
    - People with a record are already subject to a myriad of disadvantages in seeking to reintegrate into society, notably in bank lending policies but also in housing, employment, licensing, education, voting, and other areas.

**Congress must act now to:**

- Direct the SBA to eliminate new record restrictions introduced by the PPP interim rule and application form, and to clarify the eligibility policy for EIDL applicants.
- Direct the SBA to relax the record restrictions that are applied to Section 7(a) and 7(b) loans under existing rules and policies.
- Direct the SBA to ensure that the application forms for SBA financial assistance accurately reflect the eligibility requirements.

As the COVID-19 crisis continues to devastate communities across this country, federal relief must be made equitably accessible to all who need it.

Sincerely,

American Civil Liberties Union  
Chicago Lawyers' Committee for Civil Rights  
Collateral Consequences Resource Center  
Community Legal Services of Philadelphia  
Drug Policy Alliance  
FreedomWorks  
Georgia Justice Project  
Interfaith Action for Human Rights  
Justice & Accountability Center of Louisiana  
Justice Action Network  
Leadership Conference on Civil and Human Rights  
National Association of Criminal Defense Lawyers  
National Employment Law Project  
Out For Justice  
Public Interest Law Center  
Reproductive Justice Inside  
Safer Foundation  
Washington Lawyers' Committee for Civil Rights and Urban Affairs  
Women Against Registry

## APPENDIX: PROGRAM REQUIREMENTS (Prepared by CCRC)

### Paycheck Protection Program (PPP)

- The [CARES Act](#) authorizes the PPP, which provides small business loans under the SBA’s 7(a) loan program, with provisions for expanded eligibility, allowable uses, and forgiveness.<sup>1</sup>
- **Barriers based on arrest or conviction for 7(a) loans in general:**
  - **By statute:** The SBA “may verify the applicant’s criminal background, or lack thereof,” prior to approval, including through an FBI background check.<sup>2</sup>
  - **By regulation:** “Businesses with an Associate who is incarcerated, on probation, on parole, or has been indicted for a felony or a crime of moral turpitude” are ineligible.<sup>3</sup>
  - **By policy statement:** SBA interprets its regulation to also make ineligible an Associate under deferred prosecution, conditional discharge, order of protection, or a sex offender registry, or currently facing any charges in any jurisdiction.<sup>4</sup> SBA also states that various principals of a business “must be of good character,” which is determined through a character evaluation, requiring disclosure of any: 1) current charges; 2) arrests in the past 6 months; and 3) time the person has been convicted, pled guilty or no contest, or been placed on pretrial diversion or any form of parole or probation—other than for a minor vehicle violation. Expunged and sealed records must be disclosed, with no exceptions. A person will generally be approved if they provide documentation that they have satisfied all sentencing conditions (presumably including payment of costs and restitution) and do not have a felony conviction, misdemeanor conviction for a crime against a minor, recent misdemeanor conviction, or recent charges. Otherwise, they are subject to a fingerprint-based FBI background check and an opaque individual determination by the SBA.<sup>5</sup>
- **Barriers based on arrest or conviction specific to PPP loans:**
  - **By statute:** The CARES Act does not specifically authorize much less require barriers based on arrest or conviction for PPP loans. To be consistent with its purposes, the CARES Act should at the least be read to say that no new barriers based on arrest or conviction should be applied to PPP assistance.<sup>6</sup>
  - **By regulation:** [SBA Interim Final Rule](#) (Apr. 2): “You are ineligible for a PPP loan if...iii. An owner of 20 percent or more of the equity of the applicant is incarcerated, on probation, on parole; presently subject to an indictment, criminal information, arraignment, or other means by which formal criminal charges are brought in any jurisdiction; or has been convicted of a felony within the last five years.”
  - **By application form:** [Borrower Application](#) (Apr. 3): asks two questions; a “yes” to either is disqualifying: 1) “Is the Applicant (if an individual) or any individual owning 20% or more of the equity of the Applicant subject to an indictment, criminal information, arraignment, or other means by which formal criminal charges are brought in any jurisdiction, or presently incarcerated, or on probation or parole?” 2) “Within the last 5 years, for any felony, has the Applicant (if an individual) or any owner of the Applicant 1) been convicted; 2) pleaded guilty; 3) pleaded nolo contendere; 4) been placed on pretrial diversion; or 5) been placed on any form of parole or probation (including probation before judgment)?” (*Note: this is far broader than the Interim Final Rule: the second question includes “any owner” and covers dispositions other than conviction.*)

### Economic Injury Disaster Loans (EIDL)

- EIDL loans are authorized under the SBA’s existing 7(b) disaster loan program. The Coronavirus Preparedness and Response Supplemental Appropriations Act (Phase 1) appropriated additional funds and deemed coronavirus a disaster.<sup>7</sup> Pursuant to the CARES Act, SBA is also [allowing](#) business owners in all states, D.C., and territories to apply for an EIDL advance of up to \$10,000, which “will be made available within days of a successful application, and this loan advance will not have to be repaid.”<sup>8</sup>
- **Barriers based on arrest or conviction for EIDL:**
  - **By statute:** Individuals convicted during the past year of a felony during and in connection with a riot or civil disorder or other declared disaster are ineligible.<sup>9</sup>
  - **By regulation:** “Businesses with an Associate who is incarcerated, on probation, on parole, or has been indicted for a felony or a crime of moral turpitude” are ineligible.<sup>10</sup>
  - **By policy statement:** The SBA policy statement on EIDL loans provides: “It is not in the public interest...to extend financial assistance to persons who are not of good character. If any adverse information develops concerning the character or background of a disaster loan applicant or principal owner [on forms], SBA must make a determination as to the applicant’s character before a loan can be approved.”<sup>11</sup> Thus, the SBA will not approve a loan “if the applicant or principal owner is presently on parole or probation following conviction of a serious criminal offense. However, [it] will consider approving an application submitted by partnerships, corporations, and LLEs, where the apparent bar to eligibility was committed independently of any official act for the business and the individual will divest all direct and indirect interest in the business.”
  - **By application form:** Application forms, including the new [COVID-19 EIDL portal](#), include a three-part question, which requires a “yes” or “no” to the entire question: “a. Are you presently subject to an indictment, criminal information, arraignment, or other means by which formal criminal charges are brought in any jurisdiction? b. Have you been arrested in the past six months for any criminal offense? c. For any criminal offense – other than a minor vehicle violation – have you ever been convicted, plead guilty, plead nolo contendere, been placed on pretrial diversion, or been placed on any form of parole or probation (including probation before judgment)?” Under pre-existing policy, if this question is answered “yes,” the SBA requires the applicant to provide a [Form 912](#) with an explanation of the offense(s), and in some cases a fingerprint sample, before the SBA will make a character determination.<sup>12</sup> The SBA has not provided guidance on whether applicants who answer “yes” to this question can obtain an EIDL advance, or whether they will be subject to the customary character evaluation.

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<sup>1</sup> CARES Act (H.R. 748), div. A, Title I; 15 U.S.C. 636(a).

<sup>2</sup> 15 U.S.C. 636(a)(1)(B).

<sup>3</sup> 13 C.F.R. § 120.110(n). An “Associate” includes officers, directors, owners of 20% or more of the equity, key employees, and other specified entities. *See* 13 C.F.R. § 120.10.

<sup>4</sup> *See* SBA Standard Operating Procedure (SOP) [50 10 5\(K\)](#)(B)(2)(III)(A)(13) (eff. April 1, 2019).

<sup>5</sup> The good character requirement applies to every proprietor, general partner, officer, director, managing member of an LLC, owner of 20% or more of the equity, trustor, or person who runs day-to-day operations.” *See id.*

<sup>6</sup> *See* CARES Act (H.R. 748), sec. 1102.

<sup>7</sup> Coronavirus Preparedness and Response Supplemental Appropriations Act (H.R. 6074), tit. 2.

<sup>8</sup> CARES Act (H.R. 748), sec. 1110; <https://www.sba.gov/funding-programs/loans/coronavirus-relief-options/economic-injury-disaster-loan-emergency-advance>.

<sup>9</sup> *See* P. L. 90 448, 1106(e), HUD Act of 1968, and 13 CFR §123.101(a).

<sup>10</sup> 13 C.F.R. § 120.110(n). An “Associate” includes officers, directors, owners of 20% or more of the equity, key employees, and other specified entities. *See* 13 C.F.R. § 120.10.

<sup>11</sup> SBA [SOP 50 30 9](#)(3.6) (effective May 31, 2018) at p. 32.

<sup>12</sup> *Id.*