

## **CARES Act Frequently Asked Questions (FAQs) on Affiliate Rules for Small Businesses with PE / VC Sponsors**

The following document provides a high-level overview in the form of FAQs on the implications of the new Paycheck Protection Program under the CARES Act, [FAQs](#) from Treasury released on April 6, and Small Business Administration (SBA) [interim final rule](#) released on April 3 for small businesses that are “controlled” by private equity (PE), venture capital (VC) or other firms. This document is intended to accompany the other documents we provided that summarizes the key provisions of the CARES Act. For any additional questions please speak with your business contacts at Goldman Sachs. For additional resources, visit the [Goldman Sachs US Small Business Resource Center](#). We will update these FAQs as additional guidance is released.

### ***Q1: I know that the CARES Act includes a new Paycheck Protection Program (PPP) that expands the existing SBA loan guarantee program for eligible small businesses. Does my small business qualify to receive a loan under the PPP if I am controlled by another business, such as a PE or VC firm?***

- As a general principle, your business would be deemed to be an affiliate if it is “controlled” by another firm, such as a PE or VC firm. If another firm is deemed to “control” your business, it will be considered to be an affiliate of your business. See the **Annex** for a summary of the affiliation tests to help determine whether “control” exists
- If your business is deemed to be “controlled” by another firm, you must aggregate the number of employees of your business and the controlling firm, along with the employees of any other business that is an affiliate of the controlling firm
- If, after aggregating the employee numbers together, the number exceeds 500 (or such higher size standard the SBA has set for businesses in the relevant industry), your small business likely cannot take out a loan under the PPP unless an exemption applies (see below)
- As an example: your business has 300 employees and you are controlled by a PE or VC firm. That firm also controls another business that has 300 employees. For purposes of the affiliation requirements, both businesses would need to be aggregated together, totaling 600 employees (plus the employees of the PE/VC firm), and would be ineligible to receive a small business loan under the PPP absent an exemption or, if applicable, a higher number of employees set by the SBA for the relevant industry

### ***Q2: Which types of businesses are exempt from the SBA affiliation rules?***

- The following businesses are exempt from the SBA affiliation rules, which means that if your business qualifies as any of the below, you may be able to apply for a loan under the PPP as a small business even if you have more than 500 employees when counted with your affiliate(s), including any controlling PE or VC firm:
  - U.S. businesses in the hospitality and restaurant industries that are assigned a North American Industry Classification System (NAICS) code beginning with 72 are not subject to the affiliation rules. In addition, if you are one of these businesses and have more than 500 employees, you may still qualify as long as you have no more than 500 employees at each business location. This includes hotels, motels, casino hotels, bed-and-breakfast inns, other traveler accommodation, RV parks and campgrounds, rooming and boarding houses, dormitories, workers’ camps, food service contractors, caterers, mobile food services (e.g., food trucks), drinking places, full-service and limited-service restaurants, cafeterias, buffets, and snack and nonalcoholic beverage bars
  - U.S. businesses that are SBA recognized franchises (i.e., they have an assigned franchise identifier code by the SBA). Eligible franchises can be found through the SBA’s [Franchise Directory](#)
  - U.S. businesses that receive financial assistance from an SBIC
  - Faith-based organizations that are affiliated with another organization if the relationship is based on a religious teaching or belief or otherwise constitutes a part of the exercise of religion

### ***Q3: How do I know if my business is “controlled” by a PE or VC firm for purposes of the SBA affiliation rules? What are the general principles of affiliation? (updated on April 7)***

- Generally, affiliation exists when one firm controls or has the power to control the other, or a third party controls or has the power to control both. For purposes of these affiliation rules, it does not matter whether control is exercised so long as the power to control exists
- Control may arise through ownership, management, or other relationships or interactions between the parties. For instance, a PE or VC firm would be deemed to “control” your business if it owns or has the power to control more than 50% of the voting equity of your business
- Control also exists where a minority shareholder has the ability, under the business's charter, by-laws, or shareholder's agreement, to prevent a quorum or otherwise block action by the board of directors or shareholders. The power to veto extraordinary actions outside the ordinary course of business, such as amendments to governing

documents, issuing additional stock or entering into a substantially different line of business, would generally not in itself result in control of a business

- Questions concerning control rights have been the subject of past SBA interpretations and may be the subject of future FAQs, guidance or interpretations
- Minority shareholder rights must be evaluated based on the specific facts and circumstances, and we encourage you to speak with your counsel to conduct this evaluation
- See the **Annex** for additional information from the SBA on the affiliation rules applicable to the PPP

**Q4: The affiliation rule based on ownership states that the SBA will deem a minority shareholder in a business to control the business if the shareholder has the right to prevent a quorum or otherwise block action by the board of directors or shareholders. (updated on April 7)**

***(a) My small business has a number of minority equity investors, and our board of directors includes members who represent those minority investors. None of these minority equity investors have independent or unilateral power to block action by the board of directors or shareholders. In other words, power to block such action is not held by a single investor. Assuming no other relationship triggers the affiliation rules, will these minority equity investors be considered to be affiliates of the business?***

- Ultimately, minority shareholder rights must be evaluated based on the specific facts and circumstances, and we encourage you to speak with your counsel to conduct this evaluation
- If an individual minority investor has the ability unilaterally to block action by the board of directors or shareholders, standing alone, that would constitute control by, and result in affiliation with, the individual minority investor
- On the other hand, having the ability to vote on, but not unilaterally block, actions by the board or shareholders generally should not constitute control (and thus affiliation)

***(b) If a minority shareholder irrevocably gives up those rights, is it still considered to be an affiliate of the business?***

- No. If a minority shareholder in a business irrevocably waives or relinquishes those existing rights (as stated in the question), the minority shareholder would no longer be an affiliate of the business (assuming no other relationship that triggers the affiliation rules)

**Q5: What should I do if it's unclear whether my business would need to aggregate employees with a PE or VC firm?**

- Minority shareholder rights must be evaluated based on the specific facts and circumstances, and we encourage you to speak with your counsel to conduct this evaluation
- The [borrower application](#) will require you to certify that information provided in the application and in supporting documents and forms is true and correct and to acknowledge that making a false statement is punishable by fine and/or imprisonment
- Before submitting an application, it is your responsibility as the borrower to determine which entities (if any) are your affiliates and determine the employee headcount of your business and all affiliates

**Q6: If I can't get a loan under the PPP because of the SBA affiliation rules, am I able to get funding under other provisions of the CARES Act?**

- You may be able to qualify for loans or other support under other programs of the CARES Act, including the Economic Injury Disaster Loan (EIDL program) and / or other programs that have not yet been rolled out by the Federal Reserve. Please refer to our other materials for a description
- We are closely watching for additional details and will provide an update as soon as more information is available

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This document been prepared by Goldman Sachs and its legal counsel and is intended to serve as only a high-level summary of specific provisions of the CARES Act. This summary does not constitute advice and does not cover all aspects of the law, including provisions that may be relevant to, or apply differently to, your business, your employees and/or your shareholders. For any specific questions about the CARES Act and how it may impact your business, we strongly encourage that you contact your legal counsel and your business contacts at Goldman Sachs.

**Annex****AFFILIATION RULES APPLICABLE TO U.S. SMALL BUSINESS ADMINISTRATION PAYCHECK PROTECTION PROGRAM**

Based on the SBA [fact sheet](#) on affiliation released on April 4, the four tests below summarize whether a small business applying for a loan in the Paycheck Protection Program would be deemed to be controlled by another company.

**Four tests for affiliation based on control apply to participants in the Paycheck Protection Program. For purposes of the determining the number of employees of an applicant to the Paycheck Protection Program, the applicant is considered together with its affiliates. Following is a summary of the applicable affiliation tests.**

Concerns and entities are affiliates of each other when one controls or has the power to control the other, or a third party or parties controls or has the power to control both. It does not matter whether control is exercised, so long as the power to control exists. Affiliation under any of the circumstances described below is sufficient to establish affiliation for applicants for the Paycheck Protection Program.

- (1) Affiliation based on ownership.** For determining affiliation based on equity ownership, a concern is an affiliate of an individual, concern, or entity that owns or has the power to control more than 50 percent of the concern's voting equity. If no individual, concern, or entity is found to control, SBA will deem the Board of Directors or President or Chief Executive Officer (CEO) (or other officers, managing members, or partners who control the management of the concern) to be in control of the concern. SBA will deem a minority shareholder to be in control, if that individual or entity 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.
- (2) Affiliation arising under stock options, convertible securities, and agreements to merge.**
  - (a) In determining size, SBA considers stock options, convertible securities, and agreements to merge (including agreements in principle) to have a present effect on the power to control a concern. SBA treats such options, convertible securities, and agreements as though the rights granted have been exercised.
  - (b) Agreements to open or continue negotiations towards the possibility of a merger or a sale of stock at some later date are not considered "agreements in principle" and are thus not given present effect.
  - (c) Options, convertible securities, and agreements that are subject to conditions precedent which are incapable of fulfillment, speculative, conjectural, or unenforceable under state or Federal law, or where the probability of the transaction (or exercise of the rights) occurring is shown to be extremely remote, are not given present effect.
  - (d) An individual, concern or other entity that controls one or more other concerns cannot use options, convertible securities, or agreements to appear to terminate such control before actually doing so. SBA will not give present effect to individuals', concerns', or other entities' ability to divest all or part of their ownership interest in order to avoid a finding of affiliation.
- (3) Affiliation based on management.** Affiliation arises where the CEO or President of the applicant concern (or other officers, managing members, or partners who control the management of the concern) also controls the management of one or more other concerns. Affiliation also arises where a single individual, concern, or entity that controls the Board of Directors or management of one concern also controls the Board of Directors or management of one of more other concerns. Affiliation also arises where a single

individual, concern or entity controls the management of the applicant concern through a management agreement.

**(4) Affiliation based on identity of interest.** Affiliation arises when there is an identity of interest between close relatives, as defined in 13 CFR 120.10, with identical or substantially, identical business or economic interests (such as where the close relatives operate concerns in the same or similar industry in the same geographic area). Where SBA determines that interests should be aggregated, an individual or firm may rebut that determination with evidence showing that the interests deemed to be one are in fact separate.

**Religious Exemption.** The relationship of a faith-based organization to another organization is not considered an affiliation with the other organization if the relationship is based on a religious teaching or belief or otherwise constitutes a part of the exercise of religion.

**Waiver.** The affiliation rules described above are waived for (1) any business concern with not more than 500 employees that, as of the date on which the loan is disbursed, is assigned a North American Industry Classification System code beginning with 72; (2) any business concern operating as a franchise that is assigned a franchise identifier code by the SBA; and (3) any business concern that receives financial assistance from a company licensed under section 301 of the Small Business Investment Act of 1958 (15 U.S.C. 681).