

Practice Update

Updated: Reviewing PPP Loan Application Certifications in Light of Additional SBA Guidance

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Since the implementation of the Paycheck Protection Program (PPP) under the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) on April 3, 2020, the U.S. Small Business Administration (SBA) through consultation with the U.S. Department of the Treasury has issued additional guidance on the PPP loan program through the publication of Frequently Asked Questions (FAQs) and a number of Interim Final Rules (collectively, IFRs).

The recent guidance has resulted in applicants – big and small – questioning: Should I have taken a PPP loan? Do I need to pay it back? What rules apply to me? Arriving at these answers will require careful consideration of the specific facts and circumstances applicable to an applicant. We urge each applicant to carefully consider the new guidance, review and document its eligibility for a PPP loan and to be prepared for an audit of a PPP loan by the SBA.

Below is an overview of the challenges that an applicant may face in light of the new guidance with a particular focus on two of the most significant updates: the SBA's guidance on what constitutes a good faith certification to support the need for a PPP

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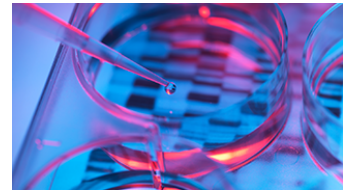
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loan and the SBA's new \$20 million cap applicable to corporate groups. The SBA is providing a "safe harbor" and allowing applicants who may not comply with the certifications in the PPP loan application in light of the new guidance to repay a PPP loan in full by May 14, 2020*, and be deemed to have made a good faith certification at the time of the application for a PPP loan.

I. SBA Review of PPP Loans Greater Than \$2 Million

The SBA has stated that PPP loans in excess of \$2 million in addition to other PPP loans "as appropriate" will be reviewed by the SBA following a lender's submission of a PPP loan forgiveness application by a borrower. The SBA has stated it will provide additional guidance on the PPP loan forgiveness process.

II. Revisiting the Certification

All applicants for a PPP loan must certify that "[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant." The CARES Act waived the requirement that applicants must be unable to obtain credit elsewhere, in other words, the PPP loan is not a loan of last resort. However, the recent guidance makes it clear that the SBA will scrutinize this certification; specifically, reviewing the sources of liquidity accessible to an applicant.

While the loan application certifications have not changed, the FAQs provide limited guidance addressing what may deem to support an applicant's certification that the PPP loan is "necessary to support ongoing operations." The FAQs provide that applicants, when making this certification, must "tak[e] into account their current business activity and ability to access other sources of liquidity sufficient to support their ongoing operations in a manner that is not significantly detrimental to the business."

An applicant that has applied or plans to apply for a PPP loan should carefully assess its specific needs and resources in light of this new guidance. As it is a factually specific analysis, an applicant should take into account the following considerations as well as any other considerations the applicant deems relevant:

- An applicant should carefully assess the financial condition of the business and whether and to what degree its operations are and may continue to be adversely impacted by the current COVID-19 pandemic. There may be significant variations in the pandemic's effects on different industries. For instance, consumer facing businesses (e.g. restaurants, health clubs, retail stores) are likely to suffer much more severe and rapid revenue declines than online businesses.
- An applicant should consider whether it has adequate sources of liquidity to support its ongoing operations. Sources of liquidity could include cash on hand, continuity of revenues and collection of accounts receivables, lines of credit, revolving lines and access to capital markets. The new guidance provides that accessing these sources, however, should not be "significantly detrimental" to the business.
- Consideration should be given to the difficulties, impositions, restrictions, or other injurious impacts accessing liquidity may pose on the business and the company.
- Portfolio companies of private equity firms may be eligible for a PPP loan after considering applicable SBA affiliation rules. The new guidance does not change the SBA affiliations rules. To support the PPP loan certifications and in addition to the items above, eligible portfolio companies should also take into account whether pending subscription agreements or other commitments to fund capital have been honored or are required and any impediments to private equity follow-on investments (e.g. vintage of the private equity fund and portfolio company investment

limitations, etc.). (Note that the new guidance provides that private equity funds and hedge funds are ineligible for PPP loans.)

Please note that for public companies, the new guidance provides that “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.”

The liquidity and capital availability analysis is not limited to large public companies. On April 27, 2020, the SBA further clarified in FAQ #37 that private companies must engage in the same liquidity analysis as large public companies.

The SBA is providing a “safe harbor” by allowing applicants that repay outstanding PPP loans in full by May 14, 2020*, to be deemed by the SBA to have made the required certification in good faith at the time of the PPP loan application and funding. An applicant making false statement to obtain a PPP loan is punishable under various laws by imprisonment and penalties. Misrepresentation or false certifications may also be subject to penalties under the False Claims Act.

III. A New “Cap” for Corporate Groups

On April 30, 2020, the SBA published an IFR restricting amounts that a single corporate group may receive in PPP loans to \$20 million. Although only one applicant may apply and receive one PPP loan up to \$10 million, the SBA is now limiting the aggregate amount of PPP loans applicants may receive if they are found to belong to a single corporate group. An applicant is considered a single corporate group if it is majority owned, directly or indirectly, by a common parent. The IFR makes clear that SBA affiliation rules as it relates to eligibility for a PPP loan (and applicable waivers) are independent from the corporate group analysis. Therefore,

although several applicants within a corporate group may qualify for eligibility of a PPP loan under the SBA affiliation rules (and applicable waivers), applicants deemed to be within a corporate group will be subject to a cap of \$20 million in the aggregate among all such applicants together (not individually).

This new limitation applies immediately to any PPP loan that has not been fully disbursed as of April 30, 2020. For loans that have been partially disbursed, this limitation applies to any additional disbursement that would cause the total PPP loans to a single corporate group to exceed \$20 million.

Applicants within a control group must notify its lender if they have applied for or received PPP loans in excess of the \$20 million cap and withdraw or request cancellation of any pending application or approved but not disbursed funds. Failure to comply will be regarded as an unauthorized use of the loan, subject to full repayment and penalties.

IV. Considerations for Applicants

Below are certain steps that applicants should consider in order to prepare for a PPP loan audit and scrutiny by the SBA:

- Document and memorialize the management and board deliberations, decision making and analysis supporting eligibility, certifications, and the impact of COVID-19 on business operations, including deliberations on sources of liquidity per the newest SBA guidance.
- Carefully review the PPP loan application to ensure accuracy of the statements made on the application. Consult with advisors to review the PPP loan application for accuracy, full disclosures and transparency as this may help demonstrate that at the time the PPP loan application was made, all facts available to the applicant at the time were considered, disclosed, and that there was no intent to mislead the government.

- If PPP loan proceeds are repaid and returned due to the new guidance (or any subsequent guidance), management and board deliberations and the decision to repay and return PPP loan proceeds should also be documented along with communications with the lender and the SBA.
- After receipt of PPP loan proceeds, carefully monitor the use of proceeds to ensure PPP loan proceeds are properly held and disbursed in accordance with the CARES Act.

The SBA and the U.S. Department of the Treasury continue to provide further guidance on the PPP loan program. We encourage applicants to review its pending and prior PPP loan application in light of the latest SBA guidance, and continue to review the PPP loan program with its lenders and advisors.

**On May 5, the SBA extended the safe harbor date from May 7 to May 14. The SBA indicated that the extension is an automatic extension, and it intends to provide additional guidance on how it will review the certification prior to May 14. We will issue an update on the SBA's additional guidance.*

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