

Understanding the SBA's New PPP Certification Guidance

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When the SBA's Paycheck Protection Program ("PPP") opened for applications on April 3rd, it was so oversubscribed that it ran through its first \$349 billion appropriation in just two weeks. The PPP has now come under public scrutiny, with news that loans bypassed small mom-and-pop shops in favor of larger businesses that may be more able to weather current economic conditions. The SBA released new guidance on April 23. The new guidance should make loan applicants – and recipients – cautious about taking a PPP loan that their business does not need.

The new guidance, which applies to new loans and also to previously applied-for loans, comes in the form of an addition to the Treasury's Frequently Asked Questions list for the PPP:

Question: Do businesses owned by large companies with adequate sources of liquidity to support the business's ongoing operations qualify for a PPP loan?

Answer: In addition to reviewing applicable affiliation rules to determine eligibility, all 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 (as defined in section 3(h) of the Small Business Act), borrowers still must certify in good faith that their PPP loan request is necessary. 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**

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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.

Lenders may rely on a borrower's certification regarding the necessity of the loan request. **Any 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.**

The required certification was in place before. While the FAQ does not change the legal standard, it makes clear that the Treasury Department and SBA are increasingly focused on ensuring that borrowers have a demonstrated need for PPP funds.

What does the certification that "current economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant" mean in light of this new guidance?

- SBA now requires borrowers to take into account alternative avenues of liquidity, but has not provided standards for determining availability. Businesses that have received PPP loans or that are considering applying should carefully evaluate their currently available cash balances, as well as whether additional financing may be available from their lenders and financial sponsors and on what terms.
- Public companies with the ability to access public markets need to consider carefully whether they can make a need certification, as these types of borrowers are specifically called out in the FAQ. While the FAQ directly addresses public companies, it is not limited to public companies, and all borrowers are required to take into account alternative capital resources.
- This guidance applies retroactively to PPP loan recipients. Borrowers who want to reassess the validity of their certification can return the loan proceeds by May 7, 2020. If they do so, they will satisfy the "good faith" certification requirement.

The new guidance reinforces that borrowers should carefully analyze and be prepared to demonstrate to the SBA the need for a PPP loan. Borrowers should carefully document their process for determining the need for the PPP loan in board minutes and other materials. These should include cash flow projections, balance sheet and other relevant financial statements, and the availability of alternative financing (including terms, timing and other factors with respect any such financing).

While the need certification will depend on the facts and circumstances of each borrower, best would be a record demonstrating that a PPP loan would save the jobs of employees who are soon to be terminated or furloughed, as this would be aligned with the congressional intent of the PPP. Borrowers should be prepared to have their determinations of need scrutinized by the SBA -- both at the time of loan origination and upon application for loan forgiveness.

The SBA and the Treasury Department have indicated that they will continue to provide updated guidance on the PPP.

Please contact one of our Choate attorneys to assist your business in analyzing eligibility for participation in the program.

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