

PPP UPDATE: SBA PROVIDES GUIDANCE ON APPLICATION OF NECESSITY CERTIFICATION

Hodgson Russ Banking & Finance Alert
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On May 13, 2020, the Small Business Administration (“SBA”) issued additional guidance on the interpretation of the certification necessary to obtain a loan under the Paycheck Protection Program (“PPP”), in the form of FAQ 46.

Certification. PPP applicants and borrowers are by now quite familiar with the certification required to obtain a PPP loan: “Current economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant.” Initially the SBA provided no guidance on the meaning of this certification; in light of the severe economic impact of the pandemic and associated shut downs, and the broad language of the certification, many borrowers understandably believed they could make this certification in good faith.

Uncertainty Based on FAQ 31. In response to media and political pressure, SBA issued FAQ 31 on April 23 (which we discussed here), indicating that it was unlikely that public companies with substantial market value and access to capital markets would be able to make the necessity certification in good faith. Late in FAQ 37, SBA confirmed that a similar analysis would apply to private companies with adequate sources of liquidity to support the business’ ongoing operations.

In FAQ 31, SBA instructed borrowers to consider current business activity and ability to access other sources of liquidity sufficient to support their ongoing operations in a manner not significantly detrimental to the business. Finally, FAQ 31 created a safe harbor for borrowers who had already received loans under the program – anyone who returned funds by May 7 (later extended to May 14) would be deemed to have made the certification in good faith.

Several days after FAQ 31 was published, the Secretary of the Treasury also announced that all borrowers that received PPP loans in excess of \$2 million would be subject to an automatic review of the necessity certification in connection with any application for loan forgiveness.

FAQ 46. Today’s guidance provides some potential comfort to borrowers struggling with the substantial uncertainty created by FAQ 31 and the automatic review requirement, in two key ways:

1. **Possible Safe Harbor for Loans less than \$2 million.** The guidance provides that any borrower that, together with its affiliates, received PPP loans with an

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original principal amount of less than \$2 million will be deemed to have made the required certification concerning the necessity of the loan request in good faith.

- **Key Issue:** Given that over 95% of PPP loans have a loan size of less than \$2 million, this safe harbor should provide some comfort to the vast majority of PPP borrowers.

2. **Consequence of an Inaccurate Certification.** For loans of \$2 million or more, if SBA determines in its mandatory review that the borrower did not have an adequate basis for the necessity certification, SBA states that it will seek repayment of the outstanding PPP loan balance and the loan will not be eligible for forgiveness.

If the borrower repays the loan after receiving notice from SBA, SBA states that it will not pursue administrative enforcement or referrals to other agencies based on its determination with respect to the necessity certification.

- **Key Issue:** It is unclear whether the repayment would need to be made immediately upon SBA's determination, or whether the borrower could repay the loan over the term stated in the PPP loan documents.

- **Key Issue:** Many borrowers have expressed concern about civil and criminal penalties related to the PPP program. This guidance indicates that, absent actual fraud or misrepresentation, SBA will likely not seek penalties for inaccurate necessity certifications, which should limit a borrower's exposure to repayment of principal and interest on the PPP loan.

- **Key Issue:** For all borrowers, but particularly those with loans in excess of \$2 million, we recommend carefully documenting in writing the basis of the borrower's good faith determination that the loan was necessary as of the application date, and updating that determination again in advance of the May 14 repayment date.

PPP guidance continues to evolve daily. If you are considering applying for a PPP loan, or have received a loan, and would like to better understand SBA guidance on the necessity certification or any other facet of the program, please contact Chris Fattey (716.848.1757) or Valerie Stevens (646.218.7614).

Please check our Coronavirus Resource Center and our CARES Act page to access information related to both of these rapidly evolving topics.

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