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PPP Loan Program New FAQs Released: ‘Necessity’ Guidance

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A key aspect of the CARES Act relief package is the now well-known Paycheck Protection Program (PPP) being administered by the Small Business Administration (SBA), which provides for loans of up to $10 million per small business applicant to be used on payroll, benefits, rent and other authorized costs from February 15, 2020, through June 30, 2020. As many are aware, the first $349 billion has already been allocated and we understand Congress is voting today (April 23, 2020) to (hopefully) approve substantial additional funds during the coronavirus pandemic. The PPP loan application requires, among other things, that applicants certify that the current "economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant." While this principles-based certification is consistent with the broad objectives of the PPP, it does not contain any quantitative metrics (such as, a specific percentage drop in expected revenue) or other objective criteria on which boards can rely in making the certification. And, while the PPP itself waived the requirement that applicants first seek alternate sources of credit (i.e., the "credit elsewhere" requirement) before applying for a loan, the PPP was also silent as to how companies should think about alternative sources of capital in making the above certification. In light of the potential civil and criminal penalties for false certifications, this "necessity" certification and the lack of clarity as to precisely what it means, has caused considerable concern among applicants and their boards and investors to date.

On April 23, 2020, the SBA issued additional guidance **in the form of updated FAQs**. These FAQs address, among other things, the "necessity" certification in the PPP loan application (see question 31). The applicable FAQ *does not* introduce quantitative metrics or otherwise set a specific standard for "necessity" but does provide the following additional guidance:

- Applicants must make a reasonable, good faith determination of need
- Applicants will need to assess "their ability to *access other sources of liquidity* sufficient to support their ongoing operations *in a manner that is not significantly detrimental to the business*" [emphasis added]
  - To the extent that applicants did not specifically consider alternate sources of liquidity in connection with their initial application, it is clear from the FAQs that they should
  - If other sources of liquidity are available, then boards will need to consider whether the capital is available on terms or otherwise in a manner that is not significantly detrimental to the business. In making this determination, we expect that boards will consider, among other things, the following as relates to any other source of capital: the likelihood of closing, the timing to closing relative to the applicant's cash needs and potential human resources cutbacks, the repayment terms (if any), the additional preference overhang that might be created, and the dilutive effect upon existing owners
  - Facts and circumstances continue to be paramount, so each applicant will want to carefully consider and reasonably document its determinations
- The FAQ specifically notes "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"
- The FAQ reiterates that companies may need to demonstrate to the SBA the basis for the certification, thus underscoring the need to maintain records supporting the applicant's determination of necessity

Importantly, the FAQ also specifically provides that any borrower that applied for a PPP loan prior to the issuance of this FAQ will be deemed to have made the necessity certification in good faith if the loan is repaid in fully by May 7, 2020. Accordingly, *borrowers considering repaying the loan (because they are questioning whether their "necessity" certification was appropriate or otherwise) should strongly consider doing so prior to May 7, 2020*, as the FAQ introduces a "no fault" return policy for such borrowers.

Notably, this FAQ does not address whether returning the funds will have any impact on the SBA's review of any other certifications (such as the size standard or other eligibility matters), though it seems unlikely the SBA would seek to review loans repaid by May 7, 2020, for other potential eligibility concerns in light of this FAQ.

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