

# Do I Really “NEED” a Paycheck Protection Program (PPP) Loan and, if I Already Got One, Should I Give it Back?

by Anthony J. Zeoli

A FREEBORN & PETERS LLP CLIENT ALERT



The “Paycheck Protection Program” (PPP) was established as part of Title I of the CARES Act (*entitled the “Keeping Workers Paid and Employed Act”*). The most recent “Frequently Asked Questions” ([FAQ](#)) released by the U.S. Small Business Administration (SBA) (*in cooperation with the U.S. Department of Treasury*) in connection with the PPP contains a section cautioning would be and existing borrowers that they must certify, or in the case of those that have already received a PPP loan have certified, **that their respective PPP loan is actually “necessary” given their respective economic situation and that such borrower may be required to provide evidence supporting such determination if required by the SBA.** In addition to the warning, the subject response also includes a safe harbor for those who have received PPP loan funds and, upon reconsideration on of their “needs,” return the loan funds by May 14, 2020.

The subject guidance at issue comes as a result of the response provided to [FAQ](#) question #31<sup>1</sup> which provides in pertinent part, as follows (*emphasis added*):

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 manner that is not significantly detrimental to the business... **and such a company should be prepared to demonstrate to SBA, upon request, the basis for its certification.**

The above certification language is not new. It comes directly from the CARES Act and is reproduced in both the PPP loan

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1. For clarity, it should be noted that question #31 in the FAQ is directed specifically toward “large companies” (including public companies). However, the same requirements were specifically made applicable to all borrowers (including individual borrowers and borrowers owned by privately versus publically), by reference, as provided in questions #37 and #39 of the FAQ.

application and the actual PPP loan documents. **What is new is the additional guidance that borrowers should be taking into account “other sources of liquidity.”** Prior to this FAQ there was no guidance specifically requiring a borrower to take such other sources into account.

The release of this FAQ section, coupled with the recent unfavorable media coverage related to certain recipients of PPP loans, has created significant concern among both those applying for and those that already received PPP loans. **So what should those who are currently applying for, or who have already received, PPP loans do in response to this new guidance?** Should prospective applicants amend/terminate their existing applications? Should those who received PPP loan funds give the money back? Unfortunately, at this time there is no bright-line test for easily answering these questions. Each borrower is different and whether or not a PPP loan is “necessary” with respect to such borrower requires a detailed facts-and-circumstances analysis taking into account the totality of the circumstances present at the time such borrower submitted their application. Moreover, there still remains ambiguity as to what “ongoing operations” actually means and what factors such be used in the requisite analysis. **What we can say is that each prospective, and existing, PPP loan borrower should be taking the time (before May 14th) to carefully review the claimed necessity of their respective PPP loan with qualified counsel and, to the extent ultimately determined to not be needed, returning such PPP loan proceeds by May 14th.** The foregoing exercise is absolutely critical given the recent public outcry concerning PPP loans going to certain public companies and other borrowers who may not (*at least on the surface*) “need” the funds. Not to mention the noticeable response of the SBA to enforce the “need” requirement in light of such concerns and its stated intention to automatically audit certain PPP loan borrowers.

At the end of the day, if a PPP loan is questioned the borrower will need to demonstrate that they had a “good faith” basis for determining that the loan was “necessary” to support their “ongoing operations.” Borrowers should also be aware that **the required certification as to the necessity of a PPP loan is made and evaluated as of, and taking into account the facts and circumstances of such borrower which exist at, the time it submits its PPP loan application.** A borrower’s particular economic facts and circumstances may change drastically from the time they made the actual certification to the time it is reviewed by the SBA and the borrower will not want to be in a position later where it cannot definitively support their initial reasoning. **Given that, each borrower should take the time now to thoroughly, and in reasonable detail, internally document their respective analysis as to whether**

**their PPP loan is necessary.** There is currently no definitive guidance as to what the SBA will require in the way of supporting documentation, so each borrower should prepare and maintain such records as they determine are adequate to reasonably support their analysis of their respective economic circumstances as of the date of the PPP loan application and their “need” for the PPP loan.

The exact consequences a particular borrower may face for misrepresenting their “need” for a PPP loan are still a bit unclear. At a minimum they will most likely be required to immediately repay the loan, in full. In addition to repayment, the borrower may also find themselves subject to additional criminal/civil penalties which can be extremely harsh. Moreover, where applicable, such criminal/civil liabilities can extend to one or more of the officers/equity holders of an entity borrower. Outside the SBA penalties, a borrower may also face adverse reputational repercussions as a result of being found to have taken a PPP loan that wasn’t needed.

**Without taking away from the severity of the above penalties and consequences, before a borrower erupts into full panic mode they should remember that the standard at issue is only whether they made the certification in “good faith.”** —In particular whether they, in “good faith” and taking into account what they knew or expected as of the time of their PPP loan application, believed they needed the PPP loan to “support their ongoing operations.” **In light of that and given both the very real risk of subsequent audits and the severity of the potential liabilities and other repercussions, the best a borrower can do right now to protect themselves is to document the reasoning and support behind their respective determination of “need” in the event they later become the subject of an SBA audit.**

It should also be noted that, pursuant to the FAQ, the SBA has stated definitively that it will be reviewing all PPP loans of \$2 million or more as/when the respective borrower applies for forgiveness. Now, this is not to say that those with PPP loans of less than \$2 million are off the hook (*as the SBA maintains the ability to audit them as well, in their discretion*), just that those with \$2 million or more will automatically be subject to review and should be prepared to defend their positions.

**We will continue to follow this and the other CARES Act programs and offer updates as further developments arise. If you have any questions, please contact Anthony Zeoli ([azeoli@freeborn.com](mailto:azeoli@freeborn.com)) or another member of the Freeborn & Peters LLP CARES Act team.**

## ABOUT THE AUTHOR



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Anthony Zeoli is a Partner in the Corporate Practice Group and the Leader of the Emerging Industries Team. He concentrates his practice in the areas of banking and commercial finance, securities, real estate, and general corporate law. Anthony's commercial finance practice includes the representation of borrowers and lenders in: secured and unsecured lending transactions; corporate reorganizations and restructuring; syndicated commercial financing transactions; and loan workouts.

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