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New SBA FAQs #46 & #47 – Safe Harbor Guidance: The SBA Gets It (Partially) Right for Once

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On May 13, 2020, the SBA finally provided some additional guidance for borrowers under the Paycheck Protection Program (PPP) regarding the so-called necessity certification. Since April 23, 2020 when the SBA issued FAQ #31, PPP loan borrowers have struggled with the SBA's requirement that a borrower certify in "good faith" that their PPP loan request is necessary.

Specifically, the certification states that "[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant." According to the SBA, all borrowers must make this certification in good faith and the only guidance provided is that borrowers should "tak[e] 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."

Since April 23, the SBA has made this applicable to all borrowers, regardless of loan size, and PPP loan borrowers with loans in excess of $2 million will be audited and reviewed to ensure they have complied with the necessity certification.

In light of the SBA changing the rules in midstream, they provided a safe harbor for PPP loan borrowers – namely, if the PPP loan borrower paid the entire PPP loan back on or before May 7, 2020, then the SBA will deem that the necessity certification was made in good faith – and thereby will not require any documentation or proof of such necessity determination. It is the proverbial "get-out-of-jail-for-free" for any PPP loan borrower that was unsure whether it met the necessity certification requirements.

While FAQ #43 extended the safe harbor deadline to May 14, 2020, a number of borrowers who had already received their PPP loans, as well as those still looking to apply for a PPP loan, were confused and concerned that the SBA would change the rules again and determine they did not meet the so-called necessity certification. Without defining "necessity" or "economic uncertainty" for borrowers, the SBA was leaving many out in the cold wondering whether they may (or may not) face criminal liability for obtaining their PPP loan (despite their clear eligibility for the loan).

As the hours inched on and borrowers grew nervous, **the SBA finally issued additional guidance in new FAQ #46 on May 13, 2020 and laid (most) of these concerns to rest.** Specifically, FAQ #46 states the following (with emphasis added):

"46. Question: How will SBA review borrowers' required good-faith certification concerning the necessity of their loan request?

Answer: When submitting a PPP application, all borrowers must certify in good faith that '[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant.' SBA, in consultation with the Department of the Treasury, has determined that the following safe harbor will apply to SBA's review of PPP loans with respect to this issue: ***Any borrower that, together with its affiliates,***

received PPP loans with an 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.

SBA has determined that this safe harbor is appropriate because borrowers with loans below this threshold are ***generally less likely to have had access to adequate sources of liquidity*** in the current economic environment than borrowers that obtained larger loans. This safe harbor will also promote economic certainty as PPP borrowers with more limited resources endeavor to retain and rehire employees. In addition, given the large volume of PPP loans, this approach will enable SBA to conserve its finite audit resources and focus its reviews on larger loans, where the compliance effort may yield higher returns.

Importantly, borrowers with loans greater than $2 million that do not satisfy this safe harbor may still have an adequate basis for making the required good-faith certification, based on their individual circumstances in light of the language of the certification and SBA guidance. SBA has previously stated that all PPP loans in excess of $2 million, ***and other PPP loans as appropriate***, will be subject to review by SBA for compliance with program requirements set forth in the PPP Interim Final Rules and in the Borrower Application Form. If SBA determines in the course of its review that a borrower lacked an adequate basis for the required certification concerning the necessity of the loan request, SBA will seek repayment of the outstanding PPP loan balance and will inform the lender that the borrower is not eligible for loan forgiveness. If the borrower repays the loan after receiving notification from SBA, SBA will not pursue administrative enforcement or referrals to other agencies based on its determination with respect to the certification concerning necessity of the loan request. SBA's determination concerning the certification regarding the necessity of the loan request will not affect SBA's loan guarantee."

Based on this timely FAQ, and as we break this down a bit, the SBA is determining that any PPP loan borrower with a PPP loan of less than $2 million will be deemed to have made the necessity certification in good faith. In other words, **for purposes of the necessity certification in the PPP loan application, borrowers with PPP loans less than $2 million will not have to provide any evidence or proof of necessity.**

This is a very welcome change for many small business owners who were concerned with potential civil or criminal liability for not providing appropriate or sufficient "proof" (at least in the SBA's eyes) of their need for the PPP loan. In recent discussions with small businesses who obtained PPP loans, many wrestled with the decision of returning their PPP loan money and laying off employees instead – primarily because laying off employees is an easier choice than being (potentially) subjected to possible reviews, audits and investigations, or penalized by the SBA's or Treasury's threatened fines, criminal prosecutions, and jail time. Now, they can concentrate on using the PPP loan proceeds for their businesses in the way intended by Congress – keep the business open and maintain or rehire its workforce.

Time to exhale and breathe a little easier – well, at least for some folks.

There is still a question for PPP loan borrowers with loans in excess of $2 million.

The SBA again reiterates in FAQ #46 that such borrowers will be audited and reviewed by the SBA for compliance with the PPP rules and requirements. This includes the necessity certification.

As a result, if a borrower keeps the PPP loan funds, the borrower will need to provide documentation and proof of their "need" for the PPP loan. As perhaps an olive branch to these borrowers, the SBA now provides that, if the SBA determines said borrower lacked an adequate basis for the required necessity certification during the SBA's review of the loan, the SBA will seek repayment of the outstanding PPP loan balance before seeking administrative enforcement.

The SBA will also inform the borrower's lender that the borrower is not eligible for any PPP loan forgiveness. However, as an additional safe harbor, if the borrower repays the PPP loan in full after receiving the SBA's notification, then the SBA will not pursue administrative enforcement or any referrals to other agencies based on its determination concerning the necessity certification. In other words, a borrower with a PPP loan in excess of $2 million will still have a chance to avoid criminal liability if the SBA determines that borrower does

not meet the requirements of the necessity certification. The remedy – pay the entire loan (plus interest) back to the lender, with no forgiveness granted as well.

New FAQ #47 - New Safe Harbor Pay-Back Deadline Extended

Finally, in light of the lateness of the FAQ #46 with the May 14 deadline around the corner, the SBA issued FAQ #47 late in the evening of May 13, 2020 that extends the "original" safe harbor pay-back deadline to **May 18, 2020** in order "to give borrowers an opportunity to review and consider FAQ #46."

Thus, any PPP loan borrower (regardless of loan size but presumably those receiving PPP loans in excess of $2 million) may still repay the entire PPP loan (plus interest) to their lender on or before May 18, 2020 in order to be deemed to have made the necessity certification in good faith.

Key Takeaways To Consider

1. **FAQ #46 only applies to the necessity certification required for all PPP loans.** In other words, any borrower (regardless of loan size) may still be subject to civil or criminal liability if they do not follow the PPP loan requirements. However, it is clear that borrowers with PPP loans less than $2 million will not be subject to civil or criminal liability solely due to the necessity certification. Such liability would have to be for some other reason (i.e., false information in their application, improper use of the loan funds, etc.).
2. **While FAQ #46 provides a partial remedy for borrowers with PPP loans in excess of $2 million, the SBA has still not defined or clarified the meaning of "necessary" or "economic uncertainty" or even "significantly detrimental to the business."** These questions still remain and in light of this FAQ, the SBA seems unlikely to provide more clarification (but we have been surprised before). As a result, such borrowers must still build a clear analysis and record of their good faith necessity certification, and thereby must still document their findings and good faith determination within the guidance we have thus far. Each borrower must keep those records and documents in their permanent business files in anticipation of the pending SBA audit that will follow their application for loan forgiveness with their lender. Again, these borrowers must be able to demonstrate why the PPP loan was necessary in their business industry and circumstances... and that such decision was made in "good faith' to meet the necessity certification.
3. **While still not determinative, the FAQ #46 does seem to indicate that the SBA is looking at the notion of "liquidity" for those businesses that need to consider the necessity certification.** In issuing the revised safe harbor, the SBA stated that borrowers below the $2 million threshold "are ***generally less likely to have had access to adequate sources of liquidity*** in the current economic environment than borrowers that obtained larger loans." Based on this rationale and without more guidance, it appears the SBA is considering the notion of "access to liquidity" as a key indicator for the necessity certification. However, the notion of "liquidity" can take many forms and circumstances. For example, should a borrower who has access to a line of credit use that line of credit for payroll purposes, when historically and operationally, it has used the line of credit to purchase materials and supplies to manufacture their products? If they exhaust that line of credit for payroll, then they have little financial room on the line of credit to purchase materials. The result could mean a shutdown of operations and laying off of employees, etc. – all the things the PPP loans are intended to address and remedy. Unfortunately, we may never get true guidance from the SBA as to how much "liquidity" is enough (or too much).
4. **Finally, FAQ #46 appears to state that, for loans in excess of #2 million, the SBA will review and make a determination on the necessity certification after the borrower has applied for loan forgiveness but before the lender provides approval of such loan forgiveness.** Obviously, this may create some timing issues for both borrowers and lenders on the PPP loans and the loan forgiveness approval. Arguably, a borrower could apply for loan forgiveness as soon as the applicable 8-week covered period expires. However, the SBA has stated that decisions by a lender on loan forgiveness must be made in 60 days from the forgiveness request. These time periods may need to be adjusted (and/or more guidance is needed) in order to give the SBA time to review and "audit" such PPP loans. Alternatively, it is possible that the SBA may make a retroactive determination on the PPP loan even

after forgiveness is granted by the lender; however, the accounting and documentation requirements for this would be nightmarish at best. When would the loan be deemed forgiven, especially since it might not ever be forgiven if the SBA gets its way? Ultimately, it seems more likely that the SBA will need to formulate a process and plan for lenders for those loans in excess of $2 million – which may mean that those borrowers may have a long time to wait until it is determined how much (if any) of the PPP loan is forgiven.

But that is for another day... or another FAQ or Interim Final Rule.

For more information, please contact the author: Mark A. Denlinger, or any of our Business & Tax attorneys.

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