

To Our Clients and Friends

Memorandum

May 14, 2020

Further PPP Update—Including Extension to May 18 of Safe Harbor Deadline for Return of Loans

The most recent developments relating to the Small Business Administration's Payroll Protection Program (PPP) loans to small businesses under the CARES Act (including the guidance issued May 13, 2020) are as follows:

- **Deadline for a return of loans to obtain safe harbor protection has been extended to May 18, 2020.** Following the negative publicity that accompanied receipt of PPP loans by large public companies and other companies with access to alternative sources of capital, the federal government announced that, even if these companies were eligible for the loans under the terms of the program, their receipt of the loans was inconsistent with the intent of the program and criminal penalties could apply if a company did not make in good faith the certification, which was required as part of the application process, that the loan was "necessary to support ongoing operations." The government revised the PPP regulations to provide that it would not take action against any company for having provided a false certification of necessity *if* the loan was returned by May 7, 2020. That deadline was later extended to May 14, 2020; and now has been extended to May 18, 2020.
- **61 public companies (out of a total of about 409) have returned their PPP loans.** Based on public filings (reviewed by FactSquared), as of the morning of May 14, 2020, approximately 409 PPP loans (totaling \$1.3 billion) had been made to public companies; and 61 of these (totaling \$411 million) had been returned. Note that public companies may generally be required to disclose that they obtained a PPP loan; thus, the negative publicity that followed issuance of the PPP loans, as well as the government's comments in response, have been focused on public companies that received PPP loans.
- **The government will conduct an "audit" of loans over \$2 million to determine whether the borrower made the certification of necessity for the loan in good faith.** The May 13 guidance clarifies that the audit will take place when the company requests forgiveness of the loan; and that the audit will consist of a review of whether the company had "an adequate basis" for making the certification as to necessity for the loan request.
- **No enforcement action will be taken against a company for having provided a false certification if the loan is repaid after the audit.** The May 13 guidance states that, "if the SBA, in the course of the review," determines that the company "lacked an adequate basis" for making the certification, the SBA "will seek repayment" of the loan and "will inform the lender that the borrower is not eligible for loan forgiveness." However, "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.”

- **Loans under \$2 million have “safe harbor” protection with respect to good faith certification of necessity for the loan.** The May 13 guidance states that borrowers of loans under \$2 million “will be deemed to have made the required certification concerning the necessity of the loan request in good faith.” According to the guidance, this “safe harbor” will provide more economic certainty to PPP borrowers with more limited resources and will permit the government to focus its resources on reviewing larger loans (“where the compliance effort may yield higher returns”).
- **The \$2 million threshold applies to the original principal amount of the loans.** The May 13 guidance clarifies that the threshold of \$2 million refers to the original principal amount of the loan; and that the \$2 million threshold will be determined based on loans made to the borrower *and* its “affiliates” (as defined under the PPP program’s affiliation rules).
- **Inconsistencies and questions.** The May 13 guidance appears to contain certain inconsistencies or omissions, which leave open the following questions:
 - ***Will all loans over \$2 million be audited?*** The SBA’s PPP guidance is inconsistent in sometimes stating that all loans in excess of \$2 million “will be audited” and sometimes stating that loans in excess of \$2 million “will be subject to audit.” Thus, it is unclear whether all of these loans *will* be audited, or just *may* be audited. The prudent course for borrowers with loans over \$2 million would be to assume that their loans will be audited.
 - ***Will any loans under \$2 million be audited?*** The guidance is inconsistent in stating that all borrowers of loans under \$2 million will *be deemed* to have provided the certification in good faith, but elsewhere stating that the SBA will “review all loans in excess of \$2 million, *in addition to other loans as appropriate*” (emphasis added). Thus, it is unclear whether or not there is true safe harbor protection for loans under \$2 million that ensures that they will not be subject to audit. The prudent course for borrowers with loans under \$2 million would be to assume that, while it is unlikely these loans would be audited, the government may audit any such loan if it determines it is appropriate to do so.
 - ***Will \$2 million loans be audited?*** The guidelines refer to loans *over* \$2 million and loans *under* \$2 million, but no guidance is provided with respect to loans of exactly \$2 million. Thus, it is unclear whether these loans will be treated like those over \$2 million (which are subject to audit) or under \$2 million (which have safe harbor protection from audit).
 - ***Is it possible that other enforcement authorities could bring charges against a PPP borrower, without a referral from the SBA?*** The guidance and rules do not answer this question. The risk, if any, seems remote, at least absent egregious or fraudulent conduct.
- **Other developments.**
 - ***Guidance on forgiveness of loans is expected soon.*** It is expected that, possibly as early as today, the application form and guidance for the forgiveness of PPP loans will be issued. It is expected that this guidance may provide some additional flexibility with respect to the requirements for forgiveness--*i.e.*, the requirements that the borrower has retained its workforce at pre-pandemic levels, has used at least 75% of the loan to cover payroll costs, and has not

decreased salaries by more than 25%. Many companies that received PPP loans reportedly have not been able to meet these requirements given that they have been closed (in accordance with governmental orders or otherwise). Some companies for whom these requirements have been problematic have not used the loans given the uncertainty about their ability to obtain forgiveness—and the guidance that will be issued is likely to affect their decisions whether to return the loans by the May 18 deadline.

- **Increased loan amounts available to partnerships and seasonal employers.** A new interim final rule was issued May 13, 2020, which permits partnerships and seasonal employers to now apply for upward adjustments in the amount of PPP loans they received, to obtain a higher amount, based on the calculation methods set forth in previous guidance that was issued.
- **First PPP-related arrests are reported.** On May 10, 2020, it was reported that a resident of Massachusetts and a resident of Rhode Island have been arrested based on fraudulent applications to obtain PPP loans. The men, who applied for more than \$500,000 in PPP loans, allegedly claimed to have dozens of employees at their restaurant businesses, although the businesses were not in operation on the required date and had no salaried employees. The situations involved included a restaurant that had closed in March 2020 when the town revoked its liquor license; a restaurant that had been closed since 2018; and a company as to which the Rhode Island State Department of Revenue had provided information to the IRS of having no record of employee wages having been paid by the company or its owner in 2020 (and, in interviews conducted by federal agents, the purported employees reported that they had never worked for the business or its owner). Email correspondence between the two men indicated a plan to fabricate payroll records to obtain the loans. The Criminal Division of the Justice Department charged the men with, among other things, conspiracy to make a false statement to influence the SBA to obtain a loan and conspiracy to commit bank fraud. The Justice Department stated that these are the first criminal charges that have been made relating to the PPP program.
- **Other issues.** Please see ([here](#)) our May 7, 2020 update on PPP developments for additional open issues relating to the determination of whether a certification of necessity was provided in good faith. Please see also ([here](#)) our April 28, 2020 memorandum, *Considerations on Returning PPP Loans*.

* * *

Authors:

Gail Weinstein

Michael T. Gershberg

Suzanne deVries Decker

William J. Breslin

Jessica Forbes

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its contents. If you have any questions about the contents of this memorandum, please call your regular Fried Frank contact or an attorney listed below:

Contacts and COVID-19 Task Force Co-Heads:

Gail Weinstein (Co-Head)	+1.212.859.8031	gail.weinstein@friedfrank.com
Michael T. Gershberg	+1.202.639.7085	michael.gershberg@friedfrank.com
Suzanne deVries Decker	+1.212.859.8351	suzanne.decker@friedfrank.com
William J. Breslin	+1.202.639.7051	william.breslin@friedfrank.com
Jessica Forbes	+1.212.859.8558	jessica.forbes@friedfrank.com
Steven M. Witzel (Co-Head)	+1.212.859.8592	steven.witzel@friedfrank.com
Jennifer A. Yashar (Co-Head)	+1.212.859.8410	jennifer.yashar@friedfrank.com
Joshua D. Roth (Co-Head)	+1.212.859.8035	joshua.roth@friedfrank.com