



Thomas Balmat

Partner
303.295.8357
Denver
tjbalmat@hollandhart.com

Warning... You Might Not Be Eligible for a PPP Loan

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On April 23, 2020, the SBA by way of FAQ #31, provided meaningful direction concerning the PPP loan certification as to “necessity.” The SBA clarified that PPP “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**” (emphasis added). FAQ #31 goes on to state that “it is unlikely that a public company with substantial market value and access to capital markets will be able to make the required certification [as to necessity] in good faith.” Businesses have until May 7, 2020 to return the loan proceeds without penalty.

Not mentioned is how private companies or family run businesses should assess their access to capital and resulting eligibility for PPP loans. So, how should private businesses respond to FAQ #31?

First, a business should confirm that the loan proceeds can and will be used for the allowable uses. There is general agreement that protection of jobs is a key principle of the PPP loan program. Directing the proceeds towards payroll costs as a way to maintain employee headcount and salaries/wages should be the driving force for obtaining the loan.

Second, a business should determine whether it has alternative sources of funding. FAQ #31 makes clear that public companies with access to capital markets probably don't qualify for a PPP loan. For private companies, the “alternative funding” analysis is less clear and requires assessing the following:

1. the current financial stability of the business including cash on hand, revenue projections, and the potential for payroll shortfall over the next several months;
2. the timing to obtain alternative funding compared to immediate cash needs and the potential in the interim for employee and/or salary cutbacks;
3. the repayment terms or dilutive effect of alternative sources of funding and how this might affect the business going forward; and
4. whether the industry sector or the geographic location of the business is likely to rebound sooner or much later than others.

The above information should be collected and readily available should the business need to support its application decision.

Third, the business should assess its sensitivity to public

scrutiny. Is the client base of the business largely consumers, private companies, or government contracts? How would a government audit impact the business going forward? Secretary Mnuchin announced that the SBA will conduct audits of all loans over \$2 million before loan forgiveness is confirmed. Random audits of smaller loan amounts should also be expected.

Finally, the business should determine whether to return the PPP loan proceeds by May 7. The SBA has created an amnesty period whereby any business that repays the loan in full by May 7, 2020, will be deemed to have made its “necessity” certification in good faith. Since PPP loans are being administered by individual lenders, the bank or credit union responsible for the loan should have a process in place for returning the proceeds.

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