

PAYCHECK PROTECTION PROGRAM – WE’VE TALKED ABOUT FAQ 31... NOW WHAT?

Posted on May 4, 2020 by Michelle F. Schwerin



Tags: [CARES Act](#), [COVID - Business](#), [Michelle Schwerin](#)



This article was published on May 4th and is current as of that date. On May 5, 2020, the Treasury and SBA issued FAQ 43, which extends the repayment date to May 14 for borrowers wishing to fall within the “safe harbor” and that the SBA intends to issue additional guidance concerning certification prior to May 14, 2020.

[Paycheck Protection Program – Treasury FAQ #31: Am I Really Supposed To Give My Money Back?](#)

In response to last week's blog post, we've received many questions (thank you!) about ramifications for ineligible companies that take out PPP loans and fail to return loan proceeds by May 7. This is a huge question. And, unfortunately, we do not have a single, certain answer. But, there are a plethora of “options” available to the federal government to respond to companies (and to individuals who signed the PPP Loan applications). I will outline them below.

Background

So, let's start at the beginning of the issue: The Government is auditing PPP loans. Companies with such loans in excess of \$2 million will, per FAQ 31, be audited (note, this is not an IRS audit, it is an

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audit by the Small Business Administration of the borrower in connection with its application and use of its PPP loan proceeds). Companies with PPP loans under \$2 million may be audited. These audits will include a review of borrowers' certifications.

The CARES Act contemplated borrowers certifying that:

"the uncertainty of current economic conditions makes necessary the loan request to support the ongoing operations of the eligible recipient."

Accordingly, the SBA issued the PPP Loan application requiring borrowers to certify, among other things, that:

"Current economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant."

All PPP borrowers, including those currently in the process of applying for a loan, signed this certification. Both the CARES Act language and the loan application language focus on "current economic uncertainty". (The Treasury issued informal guidance with similar language.) Most attorneys, accountants, and lenders advised potential borrowers that they should consider whether COVID-19 and the pandemic's impact on the market generated risk to their business. And, for most, it clearly did... and still does.

But then, on April 23, 2020, the SBA and Treasury issued FAQ 31, clarifying this standard. According to the SBA and Treasury, with respect to this certification:

"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."

The guidance in this FAQ effectively adds an additional qualification to meet the standard set forth in the certification. Now, it is not enough to face economic uncertainty, the SBA believes. Rather, the borrower must also consider its (1) current business activity; (2) ability to access other sources of liquidity sufficient to support operations; and (3) ability to access liquidity in a way that is not "significantly detrimental".

Treasury Secretary Steven Mnuchin believes: "The rules were very clear... The certification was very clear in saying that if people had other sources of liquidity, they could not take this loan." To the best of my research, the White House briefing on April 21, followed-up with FAQ 31, is the first time that the SBA or Treasury articulated this standard to the public. The language does not exist in the CARES Act. Interestingly, neither the term "liquidity" nor "detriment" appears on the face of the PPP Loan application. (The terms "access" and "funds" are contained within the application, but in sections unrelated to the certification of the business' need for the loan.)

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Nonetheless, all borrowers are now in the unenviable position of evaluating their exposure with respect their participation in the PPP Loan program. Depending on the borrower's particular facts and circumstances, its Loan application, and its use of the PPP funds, potential exposure might include criminal liability, civil liability, forfeiture of loan forgivability, and immediate default of the loan.

Criminal Exposure

With Great Funding Comes Great Responsibility: Oversight and Enforcement Provisions within the CARES Act In an interview with CNBC, Treasury Secretary Steven Mnuchin stated: "I fault the borrowers... It's the borrowers who have criminal liability if they made this certification and it's not true." In addition to the SBA/Treasury's authority, two of the three entities established to oversee the use of CARES Act funds also have the authority to refer violators to the Department of Justice for prosecution.

While criminal prosecution seems extreme (especially given that the standard for certification seems to be a moving target), we will likely see at least a few criminal prosecutions. The government has already clearly indicated it will aggressively investigate and prosecute "wrongdoers". Moreover, the issue of certification is already in the public eye, with demands to dole out consequences for violators.

The facts of the situation, along with the prosecutor's goals, will dictate the specific criminal charges, but we might expect:

- False Statements, Generally (18 U.S. Code §1001)
- False Statements, Loan and Credit Applications (18 U.S. Code §1014)
- False Statements to the SBA (15 U.S. Code §645)
- Bank Fraud (18 U.S. Code §1344)
- Wire Fraud (18 U.S. Code §1343)
- Mail Fraud (18 U.S. Code §1341)
- False Claims (18 U.S. Code §287)
- Conspiracy (18 U.S. Code §371)

Civil Consequences

False Claims Act

A borrower's application for forgiveness constitutes a "claim" under the False Claims Act ("FCA") for civil liabilities purposes. (31 U.S. Code §3729) Consequently, a borrower might be liable under the FCA for knowingly submitting a material, false claim to the government, causing the submission of such claim, or making or using a false record or statement in connection with a claim. In addition, a borrower might be liable under the FCA for avoiding an obligation to repay money to the federal government.

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The term “knowingly” includes actually knowing, acting in deliberate ignorance, or acting in reckless disregard. Liability can attach under the FCA if the borrower recklessly disregards the PPP rules. It does not require that the borrower have a specific intent to defraud the government. A violator is subject to treble damages (likely three times the PPP loan amount), civil penalties, and prevailing plaintiffs' expenses and attorneys' fees.

Either the Department of Justice or a private party in a whistleblower (also known as “qui tam”) case (in which an individual sues on the government's behalf and receives a portion of the recovery) can initiate an FCA claim against a borrower. Borrowers would be wise to consider the potential for exposure not only from government investigative agencies and the SBA, but also from those close to them. The FCA will almost certainly be widely used by the government – and by individual whistleblowers – as PPP Loan funds are subject to scrutiny and violators are identified.

Loan Default

The SBA promulgated a standard promissory note, which borrowers executed upon the closing of PPP Loans. Under the terms of this note, an event of default occurs if the borrower: “akes, or anyone acting on their behalf makes, a materially false or misleading representation to Lender or SBA”.

If the SBA determines that the borrower falsely certified as to its need, that would almost certainly constitute a “materially false or misleading” statement and trigger a default, allowing the lender to demand immediate payment of the entire loan balance.

Impact on Forgivability

While we are still waiting on additional guidance concerning forgivability (yes, still waiting), it is almost certain that the SBA's determination that a borrower falsely certified as to its need would disqualify that borrower from loan forgiveness.

Conclusion

Paycheck Protection Program Loans Frequently Asked Questions If a borrower determines that it does not meet the standards of the certification, the borrower may repay the loan proceeds before May 7, 2020. That borrower will fall within a “limited safe harbor” and “will be deemed by SBA to have made the required certification in good faith”.

Ultimately, after a borrower engages in a bit of “navel gazing”, I believe those that legitimately sought the loan out for the purposes set forth in the CARES Act will be able, in good faith, to satisfy the heightened standard set forth in this new guidance.

To prepare for a certain (or potential) audit and enhanced scrutiny, PPP Loan participants should memorialize their analysis and maintain a file of documentation that supports their certification. A robust file should include, but is not limited to:

- Records of the company's operations pre-COVID-19, including employee count, operations,

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revenues, expenses, access to funds, budgeting and other financial performance markers;

- Memoranda analyzing (a) current and foreseeable financial uncertainties and the company's need for funds to support ongoing operations, (b) available alternative sources of funds and the consequences to the business of accessing those funds, and (c) current and future sources of revenue;
- Detailed accounting of the expenses paid from PPP loan funds and the business purposes for incurring those expenses;
- Records of the company's current employee count and compensation;
- Periodic reports of operations and financial performance during this period; and
- Budget projections.

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