



FOLEY
HOAG LLP

Paycheck Protection Program Loans

*Avoiding Liability and
Implementing Compliance Best
Practices*

May 4, 2020

■ **Eligibility.** Company must:

- Be a “small business” under SBA guidelines.
- Certify in good faith that current economic uncertainty makes the loan request necessary to support the ongoing operations of the Company.

■ **Small Business Definition.**

- “Small business” is defined by SBA size standards (<https://www.sba.gov/document/support--table-size-standards>)
- Size varies by industry (determined by NAISC Code) and is based on average annual receipts or average number of employees.
- Alternate test of \$15 million tangible net worth and \$5 million two-year average net income.
- PPP Loan special designation for companies with less than 500 US employees, in the restaurant or accommodation industry or with SBIC investments.
- The size determination must also include businesses of affiliates.

■ Treasury FAQ #31 published on April 23, 2020

Question: Do businesses owned by large companies with adequate sources of liquidity to support the business's ongoing operations qualify for a PPP loan?

Answer: 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.

For example, it is unlikely that a public company with substantial market value and access to capital markets will be able to make the required certification in good faith, and such a company should be prepared to demonstrate to SBA, upon request, the basis for its certification.

Note: FAQ #37 published on April 28, 2020 notes that this “other sources of capital” consideration applies to private companies as well

■ Ability to Access Other Sources of Capital

- CARES Act suspended the ordinary requirement that borrowers must be unable to obtain credit elsewhere.
- New standard regarding ability to access other sources of capital added through FAQ guidance and not official regulations.
- FAQ guidance also provides that any borrower that applied for a PPP loan prior to the issuance of the guidance and repays the loan in full by May 7, 2020 will be deemed by SBA to have made the required certification in good faith.

■ Response to public perception and press regarding use of program

- On April 28, U.S. Treasury Secretary Steven T. Mnuchin and Small Business Administrator Jovita Carranza issued a statement that the SBA has decided, in consultation with the Department of the Treasury, that it will review all loans in excess of \$2 million, in addition to other loans as appropriate, following the lender's submission of the borrower's loan forgiveness application.
- U.S. Sen. Marco Rubio said on April 29 that the names of businesses that received federally guaranteed stimulus loans eventually will be made public.

Board Approval Process – Review of Financial Condition

- **Revenue.** Has the Company's revenue and its pipeline and prospects been directly and materially impacted by the current economic situation?
- **Layoffs.** Is / was the Company considering a layoff or across the board salary reductions because of the effects of the Coronavirus?
- **Hiring Plans.** Is / was the Company hiring at this time? Did it institute a hiring freeze?
- **Financial Needs; Model.**
 - Does the Company have runway that will enable it to weather the difficulties?
 - Does the Company's post-Covid-19 financial model support the need for the PPP loan when compared to the pre-Covid-19 financial model?
 - Does the Company's financial model indicate that it will have trouble making payroll in the next couple of months without the PPP Loan?
- **Alternative Capital.** Has the Company explored alternative sources of capital from both existing and potential new investors?
- **Use of Proceeds.** Will the proceeds from the loan enable the Company to retain employees, pay rent and/or remain in business?

Board Approval Process: Review of Loan Specifics

- **Amount.** Has the Company correctly determined the amount of the PPP Loan?
- **Use of Proceeds.** Does the Company have plans to use PPP Loan proceeds as required in the law, e.g., at least 75% to be used for payroll costs.
- **Documents and Records.**
 - Is the Board relying on reasonable projections prepared by management in making its determinations?
 - Has the Board considered the reasonable advice of counsel?
 - Did management present a detailed narrative analysis that supports the necessity of the company applying for the PPP loan?
- **Policies and Controls.**
 - Has management detailed the controls that will be put in place to ensure any loan is used only for permitted purposes?
 - Will the company's analysis and decision process be able to withstand scrutiny if the SBA's inspector general, the FBI or any other government agency looks into the application? What about an investigation by the press?
 - Does the Company have adequate document retention policies in place? Will the record support its determination if any such party investigates the Company's PPP loan application?
- **PR.** As the PPP Loan is publicly available, did the Company consider the PR effect of the company accepting a loan?

Current Oversight



Office of the Special
Inspector General for
Pandemic Response



Congressional
Oversight
Committee



Pandemic Response
Accountability Committee



Office of the Attorney General
Washington, D. C. 20530

March 16, 2020

MEMORANDUM FOR ALL UNITED STATES ATTORNEYS

FROM:

THE ATTORNEY GENERAL



SUBJECT:

COVID-19 – Department of Justice Priorities

“Every U.S. Attorney's Office is thus hereby directed to prioritize the detection, investigation, and prosecution of all criminal conduct related to the current pandemic.”

- Traditional enforcement tools
 - False Claims Act
 - Mail and wire fraud
 - False statements

What to Expect in Investigations and Audits

- Criminal investigations and prosecutions will get headlines.
 - But they will be rare and reserved for clearly fraudulent actions.



“I want to be very clear it’s the borrowers who have criminal liability if they made this certification and it’s not true,” Mnuchin said Tuesday on CNBC. “We will make sure that what was the intent for taxpayers is fulfilled here.”

- Government audits/inquiries may be numerous.
 - But should not dissuade businesses from borrowing to meet needs.

April 28, 2020 at 8:18 p.m. EDT

Treasury Secretary Steven Mnuchin said all loans of more than \$2 million in a government relief program for small businesses will be audited to ensure they were justified after large public companies and big chains sparked outrage by taking funds.

False Claims Act Overview

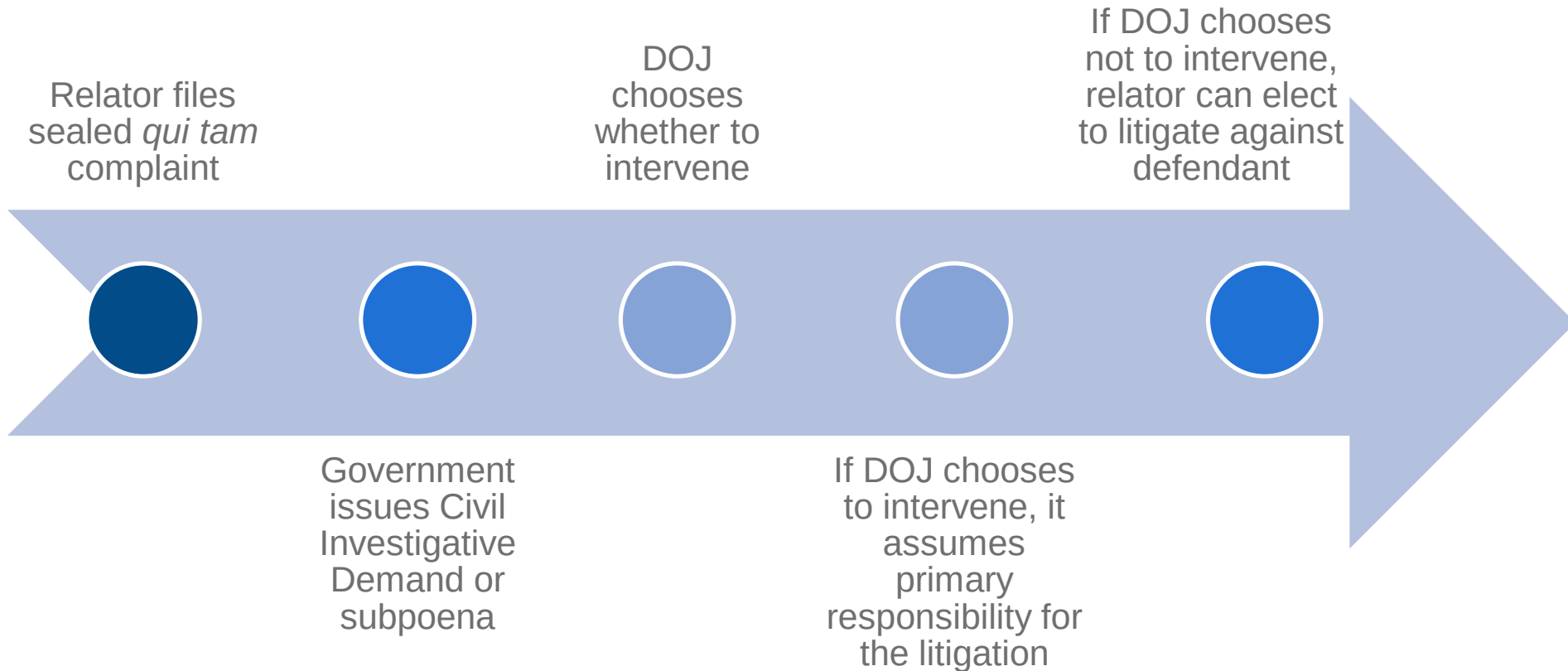
- Primary civil enforcement tool for false representations made to the government
- Primary theory of liability =
Knowingly submitting, or causing another to submit, a false claim to the government
- \$3.0 billion in total recoveries in 2019
 - 636 new cases brought by whistleblowers
 - Loan fraud is a common theory of liability
- Corporate and individual liability
- Significant damages and penalties

Elements of Claim

1. false statement
2. made knowingly
3. material to government's decision to pay a claim
4. caused the government to pay out money or forfeit money owed

- Claims can be brought by government or whistleblower
 - Whistleblower/relator bar gearing up for COVID-related cases
- Whistleblower is typically a company employee with inside information
- Claims often arise when an employee resigns or is terminated and takes evidence to support a potential False Claims Act case
- Qui Tam complaint must be filed under seal to permit the government time to investigate
- A successful relator is entitled to a share of the damages award (up to 30 percent), attorneys' fees, costs and expenses
- False Claims Act contains stringent anti-retaliation provisions

Steps to an FCA Investigation



- Primary theories = falsely certifying compliance with terms and conditions of loan

CERTIFICATIONS

The authorized representative of the Applicant must certify in good faith to all of the below by **initialing** next to each one:

_____ The Applicant was in operation on February 15, 2020 and had employees for whom it paid salaries and payroll taxes or paid independent contractors, as reported on Form(s) 1099-MISC.

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

_____ The funds will be used to retain workers and maintain payroll or make mortgage interest payments, lease payments, and utility payments, as specified under the Paycheck Protection Program Rule; I understand that if the funds are knowingly used for unauthorized purposes, the federal government may hold me legally liable, such as for charges of fraud.

_____ The Applicant will provide to the Lender documentation verifying the number of full-time equivalent employees on the Applicant's payroll as well as the dollar amounts of payroll costs, covered mortgage interest payments, covered rent payments, and covered utilities for the eight-week period following this loan.

_____ I understand that loan forgiveness will be provided for the sum of documented payroll costs, covered mortgage interest payments, covered rent payments, and covered utilities, and not more than 25% of the forgiven amount may be for non-payroll costs.

_____ During the period beginning on February 15, 2020 and ending on December 31, 2020, the Applicant has not and will not receive another loan under the Paycheck Protection Program.

_____ I further certify that the information provided in this application and the information provided in all supporting documents and forms is true and accurate in all material respects. I understand that knowingly making a false statement to obtain a guaranteed loan from SBA is punishable under the law, including under 18 USC 1001 and 3571 by imprisonment of not more than five years and/or a fine of up to \$250,000; under 15 USC 645 by imprisonment of not more than two years and/or a fine of not more than \$5,000; and, if submitted to a federally insured institution, under 18 USC 1014 by imprisonment of not more than thirty years and/or a fine of not more than \$1,000,000.

_____ I acknowledge that the lender will confirm the eligible loan amount using required documents submitted. I understand, acknowledge and agree that the Lender can share any tax information that I have provided with SBA's authorized representatives, including authorized representatives of the SBA Office of Inspector General, for the purpose of compliance with SBA Loan Program Requirements and all SBA reviews.

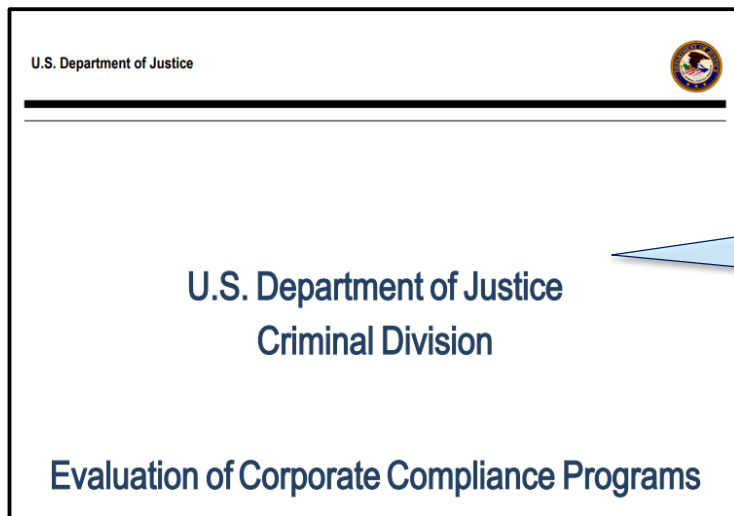
Compliance Program: Why?

- Systemic and programmatic approach is important because:
 - (Obvious) Best way to ensure compliance
 - Perhaps less obvious:
 - Existence of adequate processes and procedures could insulate you from scrutiny in the first instance
 - Investors and acquirers already taking notice of the law's requirements – future due diligence WILL cover this
 - Prevents footfaults and missteps that give an appearance of non-compliance (even if you are in fact compliant)



Compliance Program: What?

- What should a compliance program for this law seek to accomplish?
 - Veracity of representations and certifications
 - Ongoing adherence to terms and conditions
- What does that look like?
 - Existing guidance from DOJ is still good authority



Is the compliance program
1. Well designed?
2. Implemented effectively?
3. Working in practice?

Compliance Program: How?

- How is this different from existing compliance programs?
 - It doesn't have to be!
 - Examples for supplementation to existing program:
 - Create new policies regarding the use of the funds
 - Designate a point person for this compliance responsibility
 - Train relevant personnel on purpose and acceptable use for funds
 - Engage your internal and/or external accounting function to ensure appropriate use
 - Use or tweak existing documentation procedures to monitor compliance
 - Existing program is lacking or out of date? Might be time to revisit.
 - In particular, look carefully at your monitoring/reporting tools once further guidance comes out





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