

Debt Financing The Tech Group Capital Markets & Securities

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Heightened Scrutiny for Public Companies and Portfolio Companies of Funds for PPP Loans and No PPP Loans for Funds Themselves

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Certain provisions of the coronavirus/COVID-19 economic stimulus legislation are subject to the issuance of government regulations and other government action; thus, certain details regarding the legislation may be clarified or added.

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Due to increased political pressure, the pendulum has now clearly swung in favor of heightened scrutiny and enforcement in respect of PPP loans taken by public companies and portfolio companies of funds. On April 24, 2020, the Small Business Administration (SBA) issued its fourth **Interim Final Rule** (the Fourth Interim Final Rule) on the Paycheck Protection Program (PPP) created by the CARES Act. Specifically, the Fourth Interim Final Rule provides guidance with respect to promissory notes, authorizations, affiliation, and eligibility. The Fourth Interim Final Rule explicitly states that hedge funds and private equity firms are not eligible for a PPP loan. The Fourth Interim Final Rule and the latest revisions (April 23) to the U.S. Department of Treasury **FAQ sheet** (the PPP FAQ) have increased scrutiny for public companies and for fund portfolio companies that have applied or are applying for PPP loans. The guidance is not, however, limited to public or larger companies. This new guidance makes it more difficult for these companies, as borrowers, to qualify under the certifications required on the **PPP loan application**. While the SBA did not explicitly state that these companies must not

have access to other funds, this clearly has become a significant factor. There is also a new amnesty provision which provides that if a loan was applied for prior to April, 23, 2020, and such loan is repaid by May 7, 2020, the applicant will be deemed to have certified that it needed such loan in good faith.

At the outset, we would like to once again flag that on April 23, 2020, the U.S. Department of the Treasury updated the PPP FAQ to add Question 31, which asks whether businesses owned by large companies with adequate sources of liquidity to support the business's ongoing operations qualify for a PPP loan. In the answer, Treasury explains that:

"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."

We want to focus attention on the use of "ALL borrowers" (as opposed to solely public companies or larger companies).

Question 31 also notes 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 in good faith, and such a company should be prepared to demonstrate to the SBA, upon request, the basis for its certification.¹ The Fourth Interim Final Rule provides further restrictions regarding eligible businesses.

A. Clarification Regarding Eligible Businesses

i. Is a hedge fund² or private equity firm eligible for a PPP loan?

a. No. Hedge funds and private equity firms are primarily engaged in investment or speculation, and such businesses are therefore ineligible to receive a PPP loan. The Administrator, in consultation with the Secretary, does not believe that Congress intended for these types of businesses, which are generally ineligible for section 7(a) loans under existing SBA regulations, to obtain PPP financing.

ii. Do the SBA affiliation rules prohibit a portfolio company of a private equity fund from being eligible for a PPP loan?

a. Borrowers must apply the affiliation rules that appear in **13 CFR 121.301(f)**, as set forth in the Second PPP Interim Final Rule (**85 FR 20817**). The affiliation rules apply to private equity-owned businesses in the same manner as any other business subject to outside ownership or control. However, in addition to applying any applicable affiliation rules, all borrowers should carefully review the required certification on the Paycheck Protection Program Borrower Application Form (**SBA Form 2483**) stating that "[c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant."

At this point, businesses that have received any loan funds should review their current business activity and ability to access other sources of liquidity to determine whether they have made the required certifications "in good faith" given the updated FAQ. For businesses that plan to apply for additional funding pursuant to the PPP, the same considerations must be made before applying and accepting any funds. Loan recipients and applicants should consider (1) reconvening their boards for a meeting prior to May 7, 2020, to determine whether the board feels comfortable with the new clarifications

(or alterations) to the way Treasury is reading the certification of need and (2) appropriate documentation that supports how the borrower meets that standard. We note that Treasury's new guidance calls for a full repayment of the loans on or before May 7 for borrowers who do not satisfy these standards. We recommend discussing with counsel if you have questions.

B. Other Highlights from the Fourth Interim Final Rule

i. Lenders may use their own promissory note or an SBA form of a promissory note.³

ii. A business that is otherwise eligible for a PPP Loan is not rendered ineligible due to its receipt of legal gaming revenues, and **13 CFR 120.110(g)** is inapplicable to PPP loans. Businesses that received illegal gaming revenue remain categorically ineligible.

iii. For purposes of the PPP, a business's participation in an employee stock ownership plan (ESOP) (as defined in **15 U.S.C. § 632(q)(6)**) does not result in an affiliation between the business and the ESOP.

iv. If the applicant or the owner of the applicant is the debtor in a bankruptcy proceeding, either at the time it submits the application or at any time before the loan is disbursed, the applicant is ineligible to receive a PPP loan. If the applicant or the owner of the applicant becomes the debtor in a bankruptcy proceeding after submitting a PPP application but before the loan is disbursed, it is the applicant's obligation to notify its lender and request cancellation of the application.

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¹ For clarity, any borrower that applied for a PPP loan prior to the issuance of the updated PPP FAQ sheet (April 23, 2020) and that repays the loan in full by May 7, 2020, will be deemed by the SBA to have made the required certification in good faith.

² Presumably, they mean Investment Managers.

³ See U.S. Department of Treasury, Paycheck Protection Program Loans, Frequently Asked Questions (FAQs) Number 19, <https://home.treasury.gov/system/files/136/Paycheck-Protection-Program-Frequently-Asked-Questions.pdf> (last visited April 24, 2020).

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