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Paycheck Protection Program: Meeting the Good Faith Need Standard

Bonnie J Roe

On April 24, 2020, the Paycheck Protection Program and Healthcare Enhancement Act was signed into law, providing an additional $310 billion in funding for the Paycheck Protection Program, which commenced under the original CARES Act. The new law reserves $30 billion in funding to be provided through lenders with less than $10 billion in assets and certain other lending institutions serving borrowers who lack relationships with money center banks.

In conjunction with the additional funding, the Small Business Administration and the Treasury Department have responded to widely publicized concerns that the first round of Paycheck Protection loans had gone to borrowers that had other financial resources. The program requires each borrower to certify that the "current economic uncertainty makes this loan necessary to support the ongoing operations of the Applicant." But how necessary must the loan be? In guidance published on its website on April 23, 2020, the Treasury Department emphasized that borrowers must make the 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." A borrower that applied for a loan prior to the issuance of this guidance and repaid the loan in full by May 7, 2020 would automatically be deemed to have complied with the good faith standard.

Organizations applying for a Paycheck Protection Program loan should retain documentation of how they determined that they were eligible for the loan, in order to demonstrate their compliance with the good faith certification requirement.

As an example of a business that would not be able to meet the standard, the Treasury Department noted that it was unlikely that "a public company with substantial market value and access to capital markets" would be able to make the certification. On April 27, 2020, *The Wall Street Journal* reported that, based on a review of public filings, over 200 public companies had obtained Paycheck Protection Program loans in the initial round. Many of these companies appear to be micro-cap companies, and they may not have had access to other sources of capital. According to *The Wall Street Journal*, the median market capitalization of the companies was approximately $36 million and the median loan was $2.4 million. Some larger companies have announced plans to return funds advanced to them under the program, in response to criticism of the participation in the program.

In reviewing their eligibility for a Paycheck Protection Program loan, companies may also need to consider whether funding might be available from a significant shareholder. In Interim Final Rules published on the SBA website on April 23, 2020, the SBA noted that many companies owned by private equity firms were not eligible for the program because of SBA rules regarding affiliated companies. In addition to the affiliation rules, the SBA noted that entities owned by private equity firms would also need to determine whether the loan was genuinely necessary.

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