

Investment Management Alert

Akin Gump

STRAUSS HAUER & FELD LLP

New SBA Rule Bars Investment Managers from PPP Loans

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On Friday, April 24, 2020, the Small Business Administration (SBA) published an **Interim Final Rule** (IFR) governing the Paycheck Protection Program (PPP) of the Coronavirus Aid, Relief and Economic Security Act (CARES Act). In Section 2 of the IFR, entitled “Clarification Regarding Eligible Businesses,” the SBA expressly foreclosed the ability of hedge funds and private equity firms to obtain PPP loans:

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, . . . , to obtain PPP financing.

See IFR Part III, 2(a)(emphasis added). Under SBA regulations and Standard Operating Procedures for the SBA 7(a) loan program existing prior to the CARES Act, undefined “investment companies” and “[s]peculative businesses (such as oil wildcatting)” were ineligible to receive loans. 13 CFR 120.110(f); SBA Standard Operating Procedure (SOP) 50 10 5(k) at page 104. Furthermore, under limited circumstances the SBA SOP provided that “a business engaged in providing the services as a financial advisor on a fee basis” may be eligible for SBA loans provided that the loans were not used to invest in their own portfolio investments. This SOP could have been interpreted to allow entities with a primary business as a hedge fund or private equity firm themselves to be eligible for PPP loans. This argument appears to be foreclosed by the IFR for entities that primarily operate as private equity or hedge fund firms.

Importantly, the IFR’s prohibition on eligibility does not extend to the portfolio companies of private equity firms, which are still permitted to seek such loans “in the same manner as any other business subject to outside ownership or control.” The IFR shines a bright light, however, on a PPP applicant’s certification in the existing PPP loan documents: “[A]ll borrowers should carefully review the required certification . . . that [c]urrent economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant.” See IFR Part II, 2(b)(emphasis added). The IFR does not, however, repeat language from an FAQ released a day earlier which stated that borrowers should “tak[e] into account their current business activity and their

Contact Information

If you have any questions about this Alert, please contact:

Prakash H. Mehta

Partner

pmehta@akingump.com

Add to address book

New York

+1 212.872.7430

Kelli L. Moll

Partner

kmoll@akingump.com

New York

+1 212.872.8041

Richard J. Rabin

Partner

rrabin@akingump.com

New York

+1 212.872.1086

Angela B. Styles

Partner

astyles@akingump.com

Washington, D.C.

+1 202.887.4050

Rebekah M. Jones

Counsel

rjones@akingump.com

Washington, D.C.

+1 202.887.4489

ability to access other sources of liquidity sufficient to support their ongoing operations in a manner that is not significantly detrimental to the business.” See <https://home.treasury.gov/system/files/136/Paycheck-Protection-Program-Frequently-Asked-Questions.pdf>, at FAQ 31.

The IFR does provide a “Safe Harbor” for companies that previously received PPP loans, but that may have concerns about their ability to prove “necessity”: “Any borrower that applied for a PPP loan prior to the issuance of this regulation and repays the loan in full by May 7, 2020 will be deemed by SBA to have made the required certification in good faith.” See IFR Part II, 5. Thus, to the extent firms have received PPP loans, or have PPP loan applications pending, prudence suggests conferring with counsel regarding whether the Treasury Department’s recent guidance alters their strategy.

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