King & Spalding

CRISIS PRACTICE

Coronavirus

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Insurers Now Offering PPP Loan Insurance

As additional and conflicting guidance on Paycheck Protection Program (PPP) loans is released by the Small Business Administration (SBA), uncertainty about eligibility and loan forgiveness has persisted. In connection with the PPP application, each company is required to make numerous certifications related to eligibility. For example, companies that obtained loans were required to certify that the company needed the because "[c]urrent economic uncertainty makes [the] loan request necessary to support the ongoing operations of the Applicant." Various government officials then announced that the necessity certification inherently included the concept of available liquidity from owners, shareholders, or stockholders. Neither the SBA, nor the Department of Treasury has published any specific guidance articulating what amount of available liquidity would jeopardize the eligibility certification and it is widely expected that the interpretation may be subject to political pressures.

Eligibility may also be impacted by affiliation with other companies. An applicant is affiliated with another entity if the other entity controls the applicant. The affiliation rules are complex and new to many companies that have not previously participated in SBA's programs. Affiliation may result in a company unknowingly exceeding the applicable employee cap, which would render the company ineligible for the SBA loan.

The CARES Act establishes numerous enforcement mechanisms, including appointment of a Special Inspector General. The SBA will also be charged with enforcing the PPP requirements and will audit loans to ensure that the applicant was eligible. Furthermore, the False Claims Act applies to the PPP loans, which can create additional civil liability (and, in extreme instances, criminal liability) for false certifications.

The SBA has announced that it will audit loans in excess of $2 Million and we expect the SBA to closely scrutinize applications to review whether the applicant was eligible, needed the loan to sustain operations, and did not have adequate sources of liquidity available. The repercussions for submitting false or inaccurate certifications can range from repayment of the loan to litigating allegations of a False Claims Act violation, which can carry treble damages and penalties. These risks could be catastrophic to companies that are struggling in the wake of COVID.

In light of these risks, insurance companies have begun offering PPP policies to address the risk that a business was ineligible to receive a PPP loan at the time it was granted. The terms and coverage of these policies vary, and although coverage may appear to overlap with existing corporate policies, these policies are specifically targeted toward mitigating the risk of the PPP loan. The policy may not cover risks of a reduction in forgiveness, including for salary reductions, misused funds, or layoffs. Instead, the policy is designed to address the risk of false or inaccurate certifications arising from affiliation and necessity. In order to underwrite the policy, insurers will likely conduct the same diligence that many companies undertook when deciding whether to apply for, or keep, the PPP loan.

Companies that seek more certainty may find this coverage helpful given the economic impact of COVID and the rapidly changing program requirements.