



## The Paycheck Protection Program: Preparing for the Loan Forgiveness Audit

Prepared by Auspex Capital

### Paycheck Protection Program Background:

The federal government's Paycheck Protection Program ('PPP') has made \$660 billion in potentially forgivable loans available to small businesses struggling to survive the economic disruption caused by the COVID-19 pandemic. Although the program was crafted with unusual bi-partisan support and was initially very well received by both the business community and the general public, in recent weeks the program has been tainted by the revelation that a significant number of large loans were made to high profile companies like Ruth's Chris, Shake Shack and the Los Angeles Lakers that do not fit the public perception of a needy small business. In the wake of the intense negative publicity, Secretary of the Treasury Steven T. Mnuchin announced that prior to approving forgiveness for any PPP loan of \$2.0 million or more, the Small Business Administration ("SBA") will conduct an audit of the borrower to confirm that the need certification provided by the borrower was true and accurate.

Although there has been very little guidance from the SBA about the scope and depth of the audits, it is imperative that any PPP borrower that got a loan of \$2.0 million or more be fully prepared for what will likely be a detailed and comprehensive audit. While the audit will likely not take place for several months, the time to prepare for it is now when the facts and circumstances that drove the decision to take the PPP loan are still fresh and clear. We recommend that each entity that received a PPP loan of \$2.0 million or more prepare a detailed and thoughtful memorandum which clearly and persuasively makes the case for taking the loan. The outline on the following page will help you organize your presentation.

## The Outline:

### A. Critical Dates:

1. Application Date(s)
2. Funding Date(s)
3. May 7, 2020 (Final Date to Return Funds with no questions asked)

### B. Original Certification Standard:

Borrower to certify that: *"Current economic uncertainty makes this loan request necessary to support the ongoing operations of the applicant."*

### C. Revised Certification Standard:

Added to the original certification standard was the following: *"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."*

### D. Suggested Documentation Necessary to Support the Required Certification:

#### I. Financial Performance Issues:

1. Daily sales trends at each Critical Date
2. Daily transaction count trends at each Critical Date
3. Cash on hand at each Critical Date
4. Total working capital at each Critical Date
5. Projected cash burn rate at each Critical Date
6. Overall brand sales and transaction count trends at each Critical Date

#### II. Senior Lender Issues:

7. Document lender's ability to declare a loan in default as a result of a Material Adverse Change
8. Calculate pro forma financial covenants at each Critical Date to assess the risk of breaches that would allow the lender to terminate future funding obligations and potentially accelerate loan repayment
9. Document the temporary nature of lender relief packages that, while they provided some temporary relief, rapid repayment requirements impact near term solvency/viability.
10. Revolving line of credit annual out of debt requirements.
11. Identify any near-term balloon loan maturities.



#### III. Other Business Issues:

12. Identify any supply chain disruption issues, potential protein shortages and commodity cost volatility that are, or are likely to, impact the business.
13. Document the temporary nature of franchisor, landlord or vendor relief packages. While the programs may have provided some temporary relief, rapid repayment requirements impact near-term solvency/viability.
14. Status of dining rooms open/closed at each Critical Date
15. Local City/County/State Ordinances regarding shelter in place at each Critical Date
16. Change to hours of operation due to local government ordinances
17. Document day / date of stimulus checks
18. Document any ongoing remodel /construction projects
19. Document any remodel / construction / purchases that were put on hold
20. Document any emergency capital expenditures
21. Document any staffing issues and incentives / bonuses offered to retain / attract employees
22. Document any restaurant closures as a result of any employees testing positive for COVID-19
23. Document any layoffs, furloughed employees
24. Document employees brought back to work as a result of PPP funding