

# SBA Guidance: M&A Transactions and PPP Borrowers

OCTOBER 7, 2020



# Key Takeaways

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- The SBA has issued a long-awaited [Procedural Notice](#) (**Notice**) providing guidance on the procedures for changes of ownership of an entity (**Borrower**) that has received Paycheck Protection Program (**PPP**) funds.
- The Notice clears up confusion around when SBA consent is required for M&A transactions involving Borrowers that want to sell their business (**Seller**) to another entity (**Buyer**). It clarifies that in certain circumstances, set out in flow charts later in this memorandum, only the PPP Lender (**Lender**) would need to consent to the transaction.
  - The two most important requirements to avoid SBA prior approval are that the forgiveness application must be submitted to the Lender before closing the transaction and an escrow arrangement must be implemented.
    - To satisfy the escrow requirement, the parties must establish an interest-bearing escrow account controlled by the Lender with funds equal to the outstanding balance of the PPP loan. After the forgiveness process is completed, including any appeal of the SBA's decision, the escrow funds must be disbursed first to repay any remaining PPP loan balance plus interest.
  - When these conditions are met, the SBA must be given notice of the transaction, but does **not need to provide approval before closing**.

# Borrower and Lender Obligations Continue

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- Regardless of any change of ownership, the Borrower or its successor will remain responsible for:
  - The performance of all obligations under the PPP loan;
  - The certifications made in connection with the application for the PPP loan, including the **certification of economic necessity**;
  - Compliance with all applicable PPP requirements; and
  - Obtaining, preparing, and retaining all required PPP forms and supporting documents, and submitting those documents to the Lender or SBA, as required.
    - PPP rules require Borrowers or their successors to retain relevant documents for **6 years**.
- The SBA has reserved all of its rights and remedies available under the law in the event of fraud, false statements, and/or unauthorized uses of PPP loan proceeds, which can include requiring the loan to be repaid, even if it was forgiven, and criminal penalties.
- In all cases, the Lender is required to continue submitting the monthly 1502 reports until the PPP loan is fully satisfied.
- If a PPP loan associated with a change of ownership was pledged by the Lender to secure a loan under the Federal Reserve's Paycheck Protection Program Liquidity Facility (**PPPLF**), the Lender must comply with any notification requirements of the PPPLF.

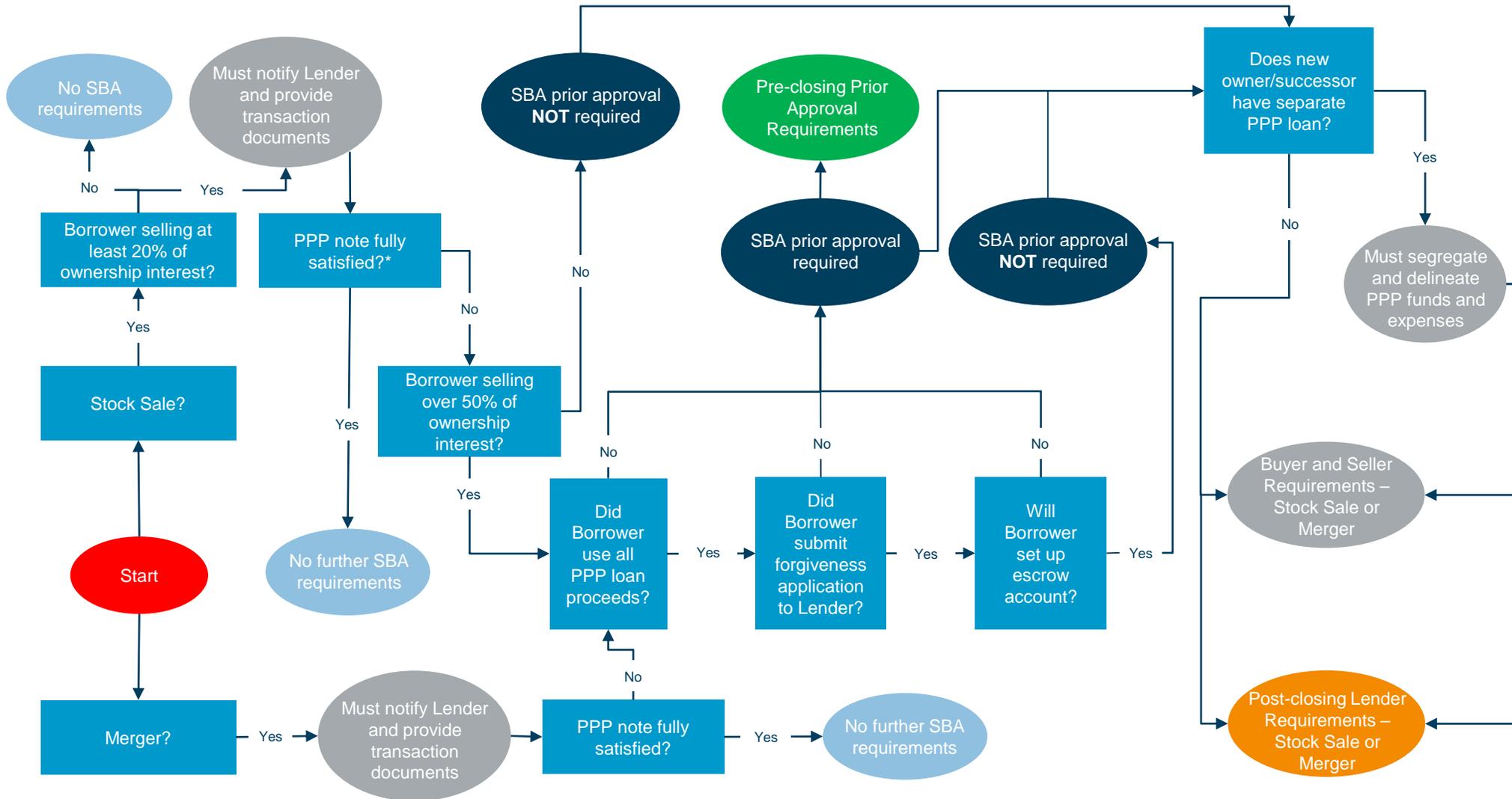
# Key to Flowcharts

- The flowcharts outline the requirements for Buyers, Sellers and Lenders contemplating the following change of ownership transactions:
  - Sale or other transfer of **at least 20%** of a Borrower's common stock or other ownership interest (**Stock Sale**);
    - All sales or transfers since the date of approval of the PPP loan are aggregated.
    - For public companies, only sales or transfers that result in one person owning at least 20% of the ownership interest of the Borrower must be aggregated.
  - Merger of a Borrower with or into another entity (**Merger**); and
  - Sale or other transfer of **at least 50%** of a Borrower's assets (measured at fair market value) (**Asset Sale**).
    - All sales or transfers since the date of approval of the PPP loan are aggregated.
- There are two flowcharts: one for stock sales and mergers; and one for asset sales. Each flowchart uses the following shapes:



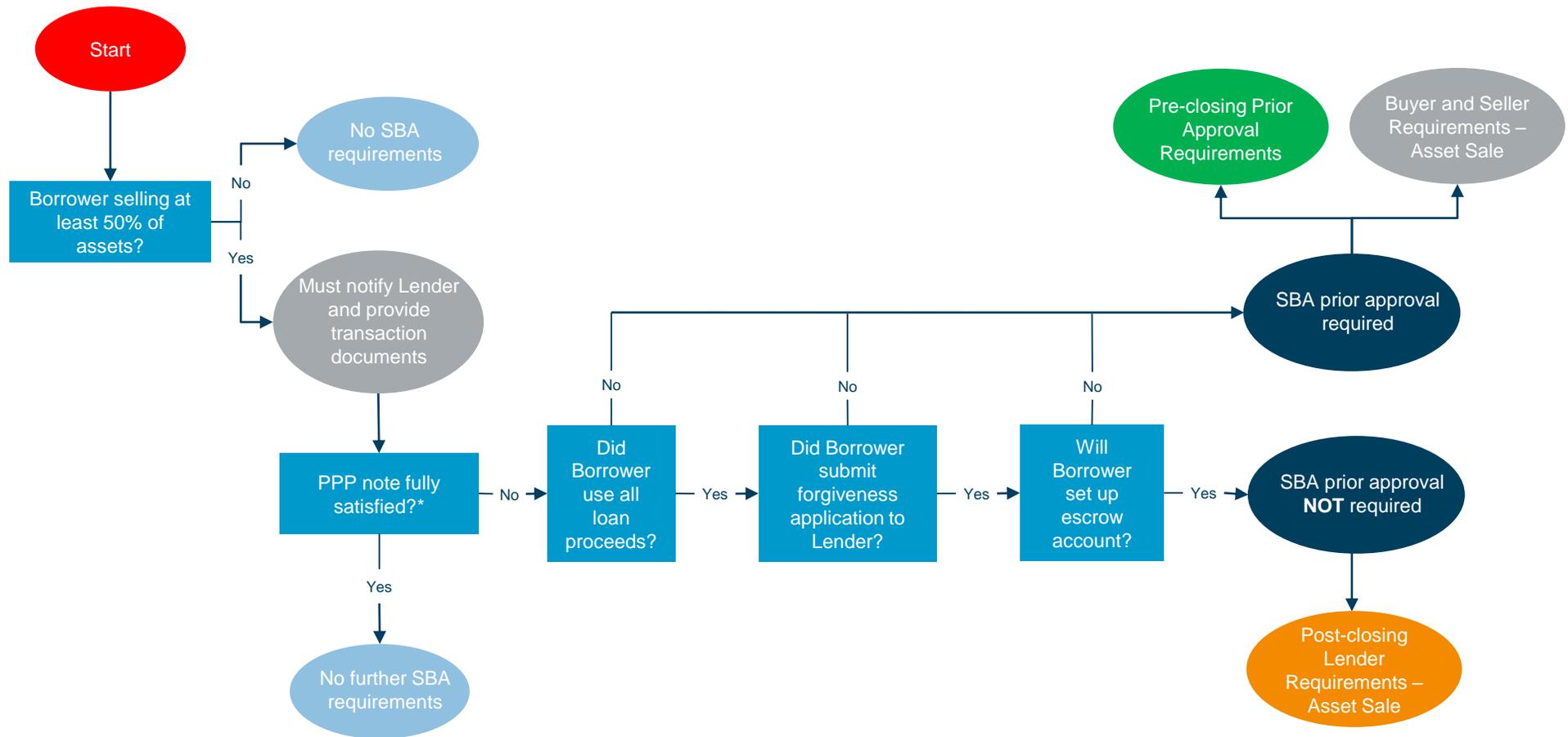
- The flowcharts are followed by summaries of the key Buyer and Seller Requirements and Lender Requirements referenced in the flowcharts.

# Stock Sale or Merger



\* The PPP note is fully satisfied if, before closing the sale or transfer, the loan no longer has an outstanding balance, either because the Borrower has repaid the loan in full or the SBA has remitted the forgiven amount to the Lender and the Borrower has paid off any remaining balance, if any.

# Asset Sale



\* The PPP note is fully satisfied if, before closing the sale or transfer, the loan no longer has an outstanding balance, either because the Borrower has repaid the loan in full or the SBA has remitted the forgiven amount to the Lender and the Borrower has paid off any remaining balance, if any.

# Prior Approval Requirements

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## **Pre-closing Prior Approval Requirements:**

- In determining whether to approve a change of ownership, the SBA will consider the following factors (**Prior Approval Factors**):
  - the reason that the Borrower cannot fully satisfy the PPP note or use the escrow funds procedure described in the flowcharts;
  - the details of the requested transaction;
  - a copy of the executed PPP note;
  - any letter of intent and the purchase or sale agreement setting forth the responsibilities of the Borrower, Seller, if different from the Borrower, and Buyer;
  - disclosure of whether the Buyer has an existing PPP loan and, if so, the SBA loan number; and
  - a list of all owners of 20 percent or more of the purchasing entity.
- If deemed appropriate, the SBA may require additional risk mitigation measures as a condition of its approval of the transaction.
- The Lender must submit the approval request, including the Prior Approval Factors, to the appropriate SBA Loan Servicing Center.
- The SBA will make a decision within 60 calendar days of receiving a complete request.

# Buyer and Seller Requirements

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## **Buyer and Seller Requirements – Stock Sale or Merger:**

- The original Borrower (or, in the event of the merger of the Borrower into another entity, the successor to the Borrower) remains subject to all PPP loan obligations, including but not limited to the obligation not to use PPP funds for unauthorized purposes. If the new owners use PPP funds for unauthorized purposes, the SBA will have recourse against the owners for the unauthorized use.

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## **Buyer and Seller Requirements – Asset Sale:**

- Buyer must assume all of Borrower's obligations under the PPP loan, including responsibility for compliance with the PPP loan terms and:
  - The purchase or sale agreement must include appropriate language regarding the assumption of the Borrower's obligations, OR
  - A separate assumption agreement must be submitted to the SBA.

# Lender Requirements

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**Post-closing  
Lender  
Requirements –  
Stock Sale or  
Merger:**

- Lender must notify appropriate SBA Loan Servicing Center of the following, within 5 business days of completion of transaction:
  - identity of the new owner of the common stock or other ownership interest;
  - new owner's ownership percentage;
  - tax identification number(s) for any owner(s) holding 20 percent or more of the equity in the business; and
  - location of, and the amount of funds in, the escrow account under the control of the Lender, if an escrow account is required.

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**Post-closing  
Lender  
Requirements –  
Asset Sale:**

- Lender must notify SBA Loan Servicing Center of location of, and amount of funds in, the escrow account under the control of the Lender within 5 business days of completion of transaction.

# Davis Polk Contacts



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If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

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