
PPP Loan Eligibility and Good Faith Certification How Can Companies Prepare and Respond?



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DISCLAIMER

THIS DOCUMENT IS A HIGH-LEVEL SUMMARY AND DISCUSSION OF PARTS OF THE PAYCHECK PROTECTION PROGRAM OF THE CARES ACT, THE PAYCHECK PROTECTION FLEXIBILITY ACT AND RELATED REGULATIONS AND GUIDANCE OF BOTH.

LOAN FORGIVENESS APPLICATIONS WILL BE MADE TO YOUR LENDER WHO HAS AUTHORITY TO ADMINISTER THE PPP. IT WILL BE IMPORTANT TO COORDINATE LOAN FORGIVENESS CALCULATIONS WITH YOUR LENDER.

SBA AND TREASURY CONTINUE TO ISSUE REGULATIONS AND GUIDANCE RELATED TO THE PAYCHECK PROTECTION PROGRAM.

THIS DOCUMENT SHOULD NOT BE USED AS A BASIS TO MAKE ANY DECISIONS OR TAKE ANY ACTIONS RELATED TO A PPP LOAN, GOOD FAITH CERTIFICATIONS OR LOAN FORGIVENESS. BORROWERS SHOULD CONSULT THEIR BANK AND THEIR OWN ADVISORS BEFORE MAKING ANY DECISIONS OR TAKING ANY ACTIONS RELATED TO THESE MATTERS.

Discussion Agenda

1. Overview of PPP Eligibility and Good Faith Certification Guidance
2. Preparing & Documenting Good Faith Certification of Eligibility for a PPP Loan
3. SBA Loan Review Process
4. Q & A

Guidance Overview

Cares Act – March 27, 2020

(G)(i) CERTIFICATION – An eligible recipient applying for a covered loan shall make a good faith certification -

- (I) “That the uncertainty of current economic conditions makes necessary the loan request to support the ongoing operations of the eligible recipient.
- (II) Acknowledging that the funds will be used to retain workers and maintain payroll or make mortgage payments, lease payments and utility payments

PPP Interim Final Rule – April 2, 2020

On the Paycheck Protection Program application, an authorized representative of the applicant must certify in good faith to all of the below.

- i. The applicant was **in operation on February 15, 2020** and had employees for whom it paid salaries and payroll taxes or paid independent contractors, as reported on a Form 1099-MISC.
- ii. **Current economic uncertainty** makes this loan request **necessary** to support the ongoing operations of the applicant.
- iii. The funds will be **used to retain workers and maintain payroll** or make **mortgage interest payments, lease payments, and utility payments;**
I understand that if the funds are knowingly used for unauthorized purposes, the federal government may hold me legally liable such as for charges of fraud.

FAQ #17 - April 6, 2020

Question:

I filed or approved a loan application based on the version of the PPP Interim Final Rule published on April 2, 2020. **Do I need to take any action based on the updated guidance in these FAQs?**

Answer:

No. Borrowers and lenders may rely on the laws, rules, and guidance available at the time of the relevant application. However, borrowers whose previously submitted loan applications have not yet been processed may revise their applications based on clarifications reflected in these FAQs.

FAQ #31 - April 23, 2020 (1 of 2)

Question:

Do businesses owned by large companies with adequate sources of liquidity to support the business' ongoing operations qualify for a PPP loan?

Answer:

- In addition to reviewing applicable affiliation rules to determine eligibility, **all borrowers must assess their economic need for a PPP loan** under the standard established by the CARES Act and the PPP regulations at the time of the loan application.
- Although the CARES Act suspends the ordinary requirement that borrowers must be unable to obtain credit elsewhere (as defined in section 3(h) of the Small Business Act), borrowers still must certify in good faith that their PPP loan request is necessary. Specifically, **before submitting a PPP application, all borrowers should review carefully the required certification** that **“current economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant.”**

FAQ #31 - April 23, 2020 (2 of 2)

- 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**. For example, it is unlikely that a public company with substantial market value and access to capital markets will be able to make the required certification in good faith, and such a company should be prepared to demonstrate to SBA, upon request, the basis for its certification.
- Lenders may rely on a borrower's certification regarding the necessity of the loan request. Any borrower that applied for a PPP loan prior to the issuance of this guidance and repays the loan in full by May 7, 2020 will be deemed by SBA to have made the required certification in good faith.

FAQ #37 - April 28, 2020

Question:

Do businesses **owned by private companies** with adequate sources of liquidity to support the business's ongoing operations qualify for a PPP loan?

Answer:

See response to FAQ #31.

FAQ #39 - April 29, 2020

Question: Will SBA review individual PPP loan files?

Answer:

Yes. In FAQ #31, SBA reminded all borrowers of an important certification required to obtain a PPP loan. To further ensure PPP loans are limited to eligible borrowers in need, the SBA has decided, in consultation with the Department of the Treasury, **that it will review all loans in excess of \$2 million**, in addition to other loans as appropriate, following the lender's submission of the borrower's loan forgiveness application. Additional guidance implementing this procedure will be forthcoming.

FAQ #46 - April 29, 2020 (1 of 2)

Question:

How will SBA review borrowers' required good-faith certification concerning the **necessity of their loan request?**

Answer:

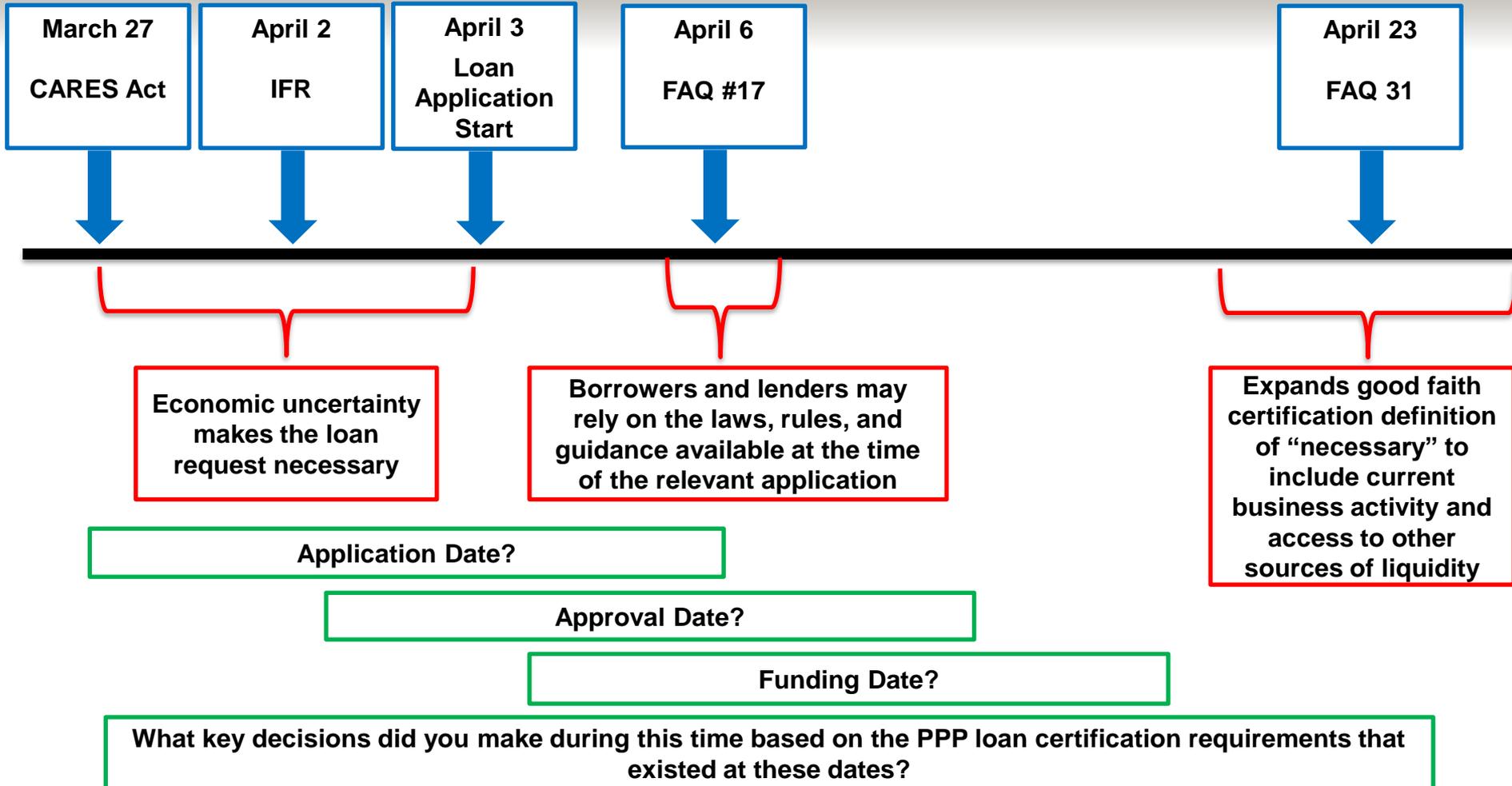
- When submitting a PPP application, all borrowers must certify in good faith that “current economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant.” SBA, in consultation with the Department of the Treasury, has determined that the following **safe harbor will apply to SBA’s review of PPP loans with respect to this issue:**
- **Any borrower that, together with its affiliates, received PPP loans with an original principal amount of less than \$2 million will be deemed to have made the required certification concerning the necessity of the loan request in good faith.** SBA has determined that this safe harbor is appropriate because borrowers with loans below this threshold are generally less likely to have had access to adequate sources of liquidity in the current economic environment than borrowers that obtained larger loans. This safe harbor will also promote economic certainty as PPP borrowers with more limited resources endeavor to retain and rehire employees. In addition, given the large volume of PPP loans, this approach will enable SBA to conserve its finite audit resources and focus its reviews on larger loans, where the compliance effort may yield

higher returns

FAQ #46 – May 13, 2020 (2 of 2)

- Importantly, borrowers with loans greater than \$2 million that do not satisfy this safe harbor may still have an adequate basis for making the required good-faith certification, based on their individual circumstances in light of the language of the certification and SBA guidance.
- SBA has previously stated that all PPP loans in excess of \$2 million, and other PPP loans as appropriate, will be subject to review by SBA for compliance with program requirements set forth in the PPP Interim Final Rules and in the Borrower Application Form.
- If SBA determines in the course of its review that a borrower lacked an adequate basis for the required certification concerning the necessity of the loan request, SBA will seek repayment of the outstanding PPP loan balance and will inform the lender that the borrower is not eligible for loan forgiveness.
- If the borrower repays the loan after receiving notification from SBA, SBA will not pursue administrative enforcement or referrals to other agencies based on its determination with respect to the certification concerning necessity of the loan request. SBA's determination concerning the certification regarding the necessity of the loan request will not affect SBA's loan guarantee.

Guidance Timeline - March 27 to April 23



Preparing & Documenting Good Faith Certification of Eligibility

Documentation Borrower Must Maintain But Not Submit – Other

All records relating to the Borrower's PPP loan, including:

- documentation submitted with its PPP loan application,
- documentation supporting the Borrower's certifications as to the necessity of the loan request and its eligibility for a PPP loan,
- documentation necessary to support the Borrower's loan forgiveness application
- documentation demonstrating the Borrower's material compliance with PPP requirements.

The Borrower must retain all such documentation in its files for six years after the date the loan is forgiven or repaid in full, and permit authorized representatives of SBA, including representatives of its Office of Inspector General, to access such files upon request.

What Should Your Documentation Look Like

- ❑ SBA has yet to issue guidance on what it will require when it reviews a borrower's loan to determine whether the borrower acted in good faith related to eligibility for a PPP loan
- ❑ SBA has said it will review loans for good faith certification when the forgiveness application is submitted to SBA by the bank and has 90 days to do so (although SBA has reserved the right to review any borrower's loan at any time)
- ❑ Based on the # of loans to review, it is unlikely that you will have a face to face interaction to explain your position.
- ❑ Documentation should:
 - be clear and concise as to your conclusions related to compliance with the requirements in the guidance and demonstrate that you acted in good faith based in following the guidance
 - be organized and easy to read
 - cover the things contained in the certification requirements (or new requirements that the SBA provides guidance on)
 - Provide sufficient detail to support your arguments and conclusions

Good Faith Certification Documentation

Necessity of the Loan Request at the Time of the Application

1. BORROWER MUST DEMONSTRATE AND DOCUMENT:

- Borrower acted in good faith
- regarding the necessity of the loan request
- based on economic need for a PPP loan (new in FAQ #31)
- under the standard established by the CARES Act and the PPP regulations
- at the time of the loan application

2. COMPONENTS OF BORROWERS DOCUMENTATION

- Existence of Economic Uncertainty caused by COVID-19
- Affect on Current Business Activity caused by COVID-19
- Access to other sources of liquidity sufficient to support your ongoing operations in a manner that is not significantly detrimental to the business
- Intended use of funds consistent with the goals of PPP to retain workers and maintain payroll or make mortgage payments, lease payments and utility payments

- Economic Uncertainty**
- Current Business Activity**
- Other Sources of Liquidity**
- Use of Funds**

Conditions & Impact Analysis

Document the Conditions & Impact of COVID-19 on Your Business

AT THE TIME OF YOUR PPP LOAN APPLICATION:

- ❑ Document your business conditions
- ❑ Develop an analysis that thoroughly documents the impact of the pandemic on your business
- ❑ This should include:
 - the uncertainties and risks you were faced with
 - state of your business conditions and activities
- ❑ This analysis will be different for every company and will be case specific
- ❑ It should include specific details of the key things going on in the business that illustrate the impact of the pandemic
 - Specific metrics
 - Internal and external data/reports, etc.

Conditions & Impact Analysis - Examples

- Effect of mandated closures on the business and its ability to operate
- Effect on customers, market segments, geographic markets, suppliers, employees
- Customer losses, delays, closings, shutdowns or cancellations
- Requests for price reductions or extended payment terms
- Supply chain disruptions, delays and closures
- People issues, including distancing measures, people not coming to work, etc.
- Layoffs, reductions or other personnel actions
- Sales and booking details and trends
- Project shutdowns/demobilization costs
- Order cancellations/bidding cancellations or deferrals
- Receivables and collection risks and deterioration
- Working capital deterioration
- Production levels and trends
- Cash balances and cash flow trends
- Potential debt covenant breaches/bank pressure/default risks/loss of lines of credit
- Potential risks to bonding relationship and capacity, ability to bid work

Decision Processes

Document Your Decisions & How They Related to Your PPP Loan

- ❑ Document your analysis and the many alternative courses of action you considered to address the potential significant threats and adverse impacts on your business, including why you chose your course of action
- ❑ Document the specific planning and actions you took when considering your PPP loan, such as layoffs, pay reductions, etc. that would have been necessary without the PPP funds
- ❑ Document your planned use of the funds and the decisions you made based on receiving the funds
- ❑ Document your thinking and decision process regarding the availability and use of other sources of liquidity and why you concluded that those sources would have been insufficient or inappropriate to use in lieu of PPP funds to support your business operations and to maintain employment and compensation levels
 - This should include your analysis of the risks and limitations associated with lines of credit and other forms of debt and cash reserves as well as inability of a private company to access capital markets

Decision Processes, continued

- ❑ Demonstrate the seriousness and intensity of your deliberations during this time related to the severity of the situation and the level of uncertainty and risk you faced. Assemble documentation consisting of:
 - Meeting agendas
 - Meeting notes
 - Action steps
 - Board meetings and resolutions, etc.

- ❑ Document the **CHRONOLOGY OF YOUR DECISIONS**
 - in relation to the date of FAQ #31 (4/23/20)
 - specific business decisions you made based on the timing of your PPP loan dates:
 - Application Date
 - Approval Date
 - Funding Date

Access to Other Forms of Liquidity

❑ Private Company Lack of Access to Capital Markets

- Comment on lack of access to capital markets
- Comment how capital is scarce and expensive for private companies
- Comment on time, effort and cost to access new forms of capital in the context of the emergency situation you were in
- Comment on your debt capacity and ability to borrow additional money quickly and easily

❑ Existing Lines of Credit

- Not a permanent source of liquidity/availability
- Have to renew annually – what is your expiration date - will your bank renew?
- Subject to meeting quarterly/annual debt covenants
- Bank can prevent drawdowns with covenant default
- Purpose to bridge working capital needs – not to fund losses. Bank would not expect/allow borrowers to fully expend lines of credit rather than reduce costs
- Comment on how a line draw down would be “significantly detrimental” to the business since the company would have no capital reserve/access to additional liquidity if needed
- Asset-based lines present reduced line capacity due to declining volumes and receivables

Access to Other Forms of Liquidity

❑ Bonding Lines

- Important for bonding company to see capacity on the line of credit as part of bonding program for a contractor
- Lack of line capacity could cause reduction in ability to get bonds and bid work which would be “[significantly detrimental](#)” to the business
- Significantly negative effect on future revenues for a contractor by not having adequate bonding capacity

❑ New Bank Borrowing other than PPP

- Banks not lending – too much uncertainty
- Bank credit tightening rather than loosening
- Banks focused on protecting themselves from credit losses rather than making new loans
- Banks already stretched to capacity to implement government mandated PPP and directed their resources to those activities rather than making new conventional loans
- Banks increasing loan loss reserves

Access to Other Forms of Liquidity

□ Cash Levels

- Consider affect on working capital of cash spent to fund losses
- Consider level of cash relative to levels of overhead (i.e. how many months of overhead/payroll etc. does our cash balance cover?)
- Comment on prudent business practices to maintain levels of cash to support the businesses and jobs in the future and the detrimental effect of spending down the company's cash
- Comment on the risk associated with not maintaining adequate cash and working capital reserves (relative to the size of the business) and the negative affect that could have on the business and jobs over the long term
- Comment on the need to maintain cash reserves to maintain flexibility and the what it does to allow the business to survive in the middle of a pandemic
- Comment on the need to keep reasonable cash levels based on the significant economic uncertainty at that time
- Benchmark your cash and working capital levels against industry standards to determine reasonableness

Financial Analysis & Planning

Document Rigorous Analysis of Decision Processes

- ❑ Document the financial analysis and cash flow planning that you engaged in as part of your decision process to demonstrate the need to apply for the loan and the effect of the pandemic on your financial condition
- ❑ Include various scenarios that you considered in projecting cash flows, cash balances, and other key business metrics
- ❑ Consider other unique risk factors, including:
 - existing debt levels and debt service requirements
 - leverage
 - cash levels
 - and customer, supplier and market concentrations and dependencies
- ❑ Consider unique claims on capital, including:
 - existing purchase commitments
 - capital project commitments
 - shareholder redemption commitments, as well as ESOP redemptions
- ❑ Include the factors and risks that affect your access to lines of credit, including borrowing base limitations, ramifications of potential debt covenant violations and the uncertainty related to expiration and renewal of your line of credit given the current environment. This could include limitations or restrictions on your bonding lines

4. Use of PPP Funds

- ❑ Document your planned use of the PPP funds within your decisions processes in a manner consistent with the purpose of the program.
- ❑ Demonstrate how this was part of your good faith effort in applying for the loan, as well as your planning and execution related to the use of the funds.
- ❑ Emphasis should be on retaining workers and maintain wages.

The Certification

- **Baseline Rule:** forgiveness is dependent on whether you can meet the criteria to which you certified; and it only matters “what you can prove”.
- As applicants, you certified that:
 - “current economic uncertainty makes this loan request necessary to support the ongoing operations of the Applicant”
- Certification must be made of “good faith”
- When making the certification, you were to account for current business activity and the ability to access other sources of liquidity to support ongoing operations in a way that does not significantly harm the company

Purpose and Context Matter on the Certification

- From the SBA's perspective, the condition did not exist if you can't demonstrate it – think not just about what you have to prove, but how you are going to prove it
- “Good faith” means you have to make your best efforts based on the knowledge you have at the time – it does not require you to be 100% right on your analysis
 - Caveat: this is not a license to be cavalier about your approach
- The question was never really if they would review applications, it was always how they will review them – present scuttlebutt suggests it will be entirely electronic
- Fitting into the “safe harbor” does not mean you will escape review; it just means you are get the benefit of a the presumption of good faith

Purpose and Context

- PPP is a government backed loan program, not a government loan program
- The certification process is the methodology for the government to get its hooks into you since the banks actually made the loans
- Think of certification as the same as being sworn in before testifying in court – there is potential punishment if you are less than honest (important: have to be honest, not right)

Purpose and Context

- the certification process was designed to prevent abuse of the program beyond what the lending banks could enforce
- the standard is good faith; think through the process like a lawyer (or use one to help) and gather the proofs to show you arrived at your conclusion that you needed the money based on accurate facts and sound reasoning
- optics matter; don't do or document anything that is going to draw unnecessary attention (New York Times Rule)

A Few Special Notes on Certification

- the normal SBA requirement that you show an inability to obtain credit does not apply; instead have to show it's "necessary" –what qualifies as necessary and who decides?
- Lenders are entitled to rely on the borrower's certification, so only the certifying borrower is on the hook; and the government will not challenge lenders that conform to guidance
- Possible loophole: the actual certification language does not appear in the CARES Act, Interim Final Rules, or the PPP application; and no documents were required to be submitted with many of the applications – how do you enforce a certification that was never really made?

Consequences if Fail to Meet the Standard

- if SBA determines after audit that more than \$2M was borrowed without sufficient basis for the certification, it will not pursue enforcement if the loan is repaid
 - Issue 1: it's not clear whether it's an accelerated repayment or paid over time – more likely accelerated based on prior guidance
 - Issue 2: this does not stop other government agencies from pursuing fines, penalties and charges – and once you are “in the system” you might be exposed to other government reviews

A Word on Enforcement

- There are civil and criminal penalties if the “good faith” provision is deemed to have been violated
- False Claims Act is applicable (treble damages, penalties up to \$21K per claim, and more)
- Depending on the standard applied, you do not have to have an intent to defraud – reckless indifference is enough

Keep In Mind That Trouble Lurks Elsewhere

- The “good faith” certification process is the biggest area in which you can get into trouble, but there are others where you can find it:
 - Miscalculation of maximum amount of the loan
 - Whether you are eligible or not (for example, investment companies are not)
 - Improperly counting number of employees
 - Violation of SBA affiliation rules
 - Improper use of loan proceeds

How They Will Audit the Veracity of the Certification

- The trigger will likely be the application for loan forgiveness, which will result in them asking for a showing that your certification was accurate; have your proofs lined up and ready when you submit for forgiveness
- Pick the right proofs; and avoid “overdoing” your proofs
- Consider that it’s most likely going to be someone looking at the records electronically with no context on your situation – what you show them on paper is the only picture they will have when they make a decision.

Proving Your Case During an Audit

- Context: Understand the set-up is designed to close loopholes on previous big government programs that were gamed – avoid communication that sounds like that is what you are doing (example “free money”)
- Engage legal counsel and an accountant to help review your analysis and to prepare and submit the applications, as it connotes good faith
- Be consistent with other applications for loans or requests for investment; document loan denials

Proving Your Case During an Audit

- Account for the funds in a “separate” way (separate account) and track the details of where they went, what the company spent those funds on, and dates and times (think something similar to a schedule of values)
- Stay away from anything that remotely looks like self-dealing
- Show a written document that demonstrates a formal process was used to manage intake, use, and recording of the funds so that they can see more than one set of eyes on the process; document each step so that it’s transparent and easy to show what was done.
- Formally document that the issue was taken to the Board or equivalent thereof for approval with a vote, minutes, and a formal resolution

Proving Your Case During an Audit

- Do a financial analysis that shows the impact of COVID-19 on revenue as compared to expenses – show your company would be financially in trouble without the help (spreadsheet showing jobs lost, jobs postponed, expected revenue lost, deferred compensation, money saved in layoffs and furloughs, cash flow analysis, etc.)
- Where possible provide project communications showing you were prepared to move forward and the owner or others closed the project down (the reason for the shutdown may not matter as much)
- Keep accurate records of efforts to keep working – examples: any waivers submitted to continue working, COVID-19 safety protocols put in place to show can work safely, letter or emails to customer

Proving Your Case During an Audit

- Keep written records of people moved to remote work by name, date, job description, and length of time
- Make sure time cards and other work records are turned in regularly and accurately show time worked; do an analysis of prior periods and show less hours
- Gather copies of documents to show qualified expenditures (cancelled checks, lease agreements, mortgage documents and loan amortization tables, etc.)
- Have employees certify in writing to the fact that they did not collect unemployment compensation

Proving Your Case During an Audit

- Maintain a copy of the PPP loan application and any other records submitted as part of the loan process
- Customer lists before and after COVID-19 by head count, gross revenue, and percentage of your company's revenue
- Documents showing rates that the market won't yield the same amount for your work (margins, bids documents?) since COVID-19.
- Complete a debt to value ratio for pre-COVID period, at time COVID hit, and appropriate period after COVID hit.

Proving Your Case During an Audit

- Document that your line of credit is or could be maxed out; get written communication from your bonding company or creditors about the issue being “of concern”.
- Show any unfunded deferred compensation agreements or other legal obligations that are required to be paid from operations in the future and cannot be paid
- Evidence of customers requesting longer payment terms or discounts; aged receivables reports showing collections slow
- Documents showing possible negative action by customer because of manpower, supplier, or other issues

SBA Loan Review Process

- The statutory 90-day period to review the PPP loan and forgiveness documentation is a procedural protection to ensure compliance, prevent fraud or misuse of PPP funds, and allow borrowers to get closure on the process
- There will be some challenges because of the large number and diverse types of PPP lenders, many of which were not previously SBA participating lenders and which were approved rapidly in order to enable financial assistance to be provided as rapidly as feasible to millions of small businesses.
- The confusion will be accentuated by the fact that there has been no actual guidance on how they will perform the review and audit process, so be patient and prepared for the situation to change.

SBA Loan Review Process

- There is not set rule on who or when review of a loan will take place
 - While there is a safe harbor provision, it's only a presumption
 - SBA reserved the right to look into any loan at any time
 - Some question of whether a whistleblower issue may arise; so probably a good idea not to broadcast you received PPP money.
 - Borrower must retain PPP documentation in its files for six years after the date the loan is forgiven or repaid in full, and permit authorized representatives of SBA, including representatives of its Office of Inspector General, to access such files upon request

SBA Loan Review Process

- Borrower will have the opportunity to respond to SBA questions if loan documentation submitted to SBA by the lender or otherwise indicates that the borrower was ineligible for a PPP loan or for forgiveness, the SBA will likely ask the lender to contact the borrower in writing to request additional information
- SBA may also request information directly from the borrower though; verify who you are talking to before you give information away (lot of scams going on right now)
- Lender will provide any additional information provided to it by the borrower to SBA; SBA will consider supplemental information provided by the borrower
- Failure to respond to SBA's inquiry – not good

SBA Loan Review Process

- A borrower will be able to appeal the SBA's determination that the borrower is ineligible for a PPP loan or ineligible for forgiveness of the loan amount because some sort of appeal is likely required legally
- SBA intends to issue a separate interim final rule addressing this process; there is no guidance on this issue presently though; and there is not timeline available as to when we will get it.
- Three likely challenges to the process:
 1. The overall set-up violated an already in place standard (for example, a constitutional challenge)
 2. The process as applied is "flawed"
 3. I was treated differently than someone else who had the same circumstances

In Closing

- Keep in mind it's a fluid situation and subject to change
- Each company's situation will be fact specific, so don't assume it's one size fits all – engage with the experts and others who are going through the process.
- Given what's at stake, better to be a little more conservative if you can