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COVID-19 CARES ACT UPDATE
LOAN PROGRAMS AND FACILITIES AVAILABLE TO MID-SIZED BUSINESSES

On March 27, 2020, the President signed the Coronavirus Aid, Relief, and Economic Security ("CARES") Act. Section 4003 of Title IV of the CARES Act allocates $500 billion in financial assistance (including loans, loan guarantees, and investments) to eligible businesses, states, and municipalities. The programs established under Section 4003 of the CARES Act have two components: (i) up to $46 billion in loans and loan guarantees to support a short list of distressed industries/companies considered essential, including air carriers and businesses critical to maintaining national security (the "Industry-Specific Business Lending Program"), and (ii) at least $454 billion (as well as amounts remaining from the Industry-Specific Business Lending Program) in available loans, loan guarantees, and investments through programs or facilities established by the Board of Governors of the Federal Reserve System designed to support lending to eligible businesses, states, and municipalities (the "Federal Reserve Direct Loans").

The CARES Act also clarifies that the Federal Reserve may establish a "Main Street Lending Program" to support lending to small and mid-sized businesses on terms consistent with the Federal Reserve's authority under Section 13(3) of the Federal Reserve Act (the "Main Street Lending Program").

This Update focuses on Federal Reserve Direct Loans under Section 4003(b)(4) of the CARES Act and the Main Street Lending Program.

Federal Reserve Direct Loans

The Federal Reserve Direct Loan program will be established by the Federal Reserve System for the purpose of lending to states, municipalities, and eligible businesses (other than businesses receiving loans or loan guarantees under the Industry-Specific Business Lending Program described above). Funds under this program may be used to (i) purchase obligations or other interests directly from issuers of such obligations or other interests, (ii) purchase obligations or other interests in secondary markets or otherwise, or (iii) make direct secured and unsecured loans to an eligible borrower.

The Federal Reserve Direct Loan program provides an alternative to mid-sized businesses who do not qualify for a Paycheck Protection Program (PPP) loan by providing banks and other lenders with funds to make direct loans to mid-sized profit and non-profit businesses with between 500 and 10,000 employees. Federal Reserve Direct Loan program applicants are not subject to the same size-testing and affiliation rules that are applicable to the SBA's small business lending programs.

Direct loans made to an eligible mid-sized business under the Federal Reserve Direct Loan program will have an annualized interest rate of no greater than 2% and with no principal or interest due for at least six (6) months (or longer, as determined by the Secretary of the Treasury). Specific terms and conditions of the loans will be established by the Secretary of the Treasury and the Federal Reserve. To this end, while the CARES Act does not provide the forgiveness of Federal Reserve Direct Loan obligations (unlike express forgiveness provisions of the

CARES Act applicable to PPP loans), forgiveness is not expressly prohibited and can be considered by the Secretary of the Treasury and the Federal Reserve.

In order for an otherwise eligible mid-sized business to receive a Federal Reserve Direct Loan, it must make a good faith certification that:

- Uncertainty of the economic conditions as of the date of application makes the loan necessary for the support of ongoing operations.
- It will retain 90% of its workforce at full compensation and benefits until September 30, 2020.
- It intends to restore not less than 90% of its workforce with all compensation and benefits that existed as of February 1, 2020 no later than four (4) months after the termination of the public health emergency declared January 31, 2020.
- It is domiciled in the United States with significant operations and employees in the United States.
- It is not a debtor in a bankruptcy proceeding.
- It is organized under the laws of the United States and has significant operations and the majority of its employees based in the United States.
- It will not pay dividends with respect to its common stock or buy back any equity security listed on a national securities exchange, except to the extent required under a pre-existing contractual obligation.
- It will not outsource or offshore jobs during the term of the loan and for two (2) years after repayment.
- It will not abrogate existing collective bargaining agreements during the term of the loan and for two (2) years after repayment.
- It will remain neutral in any union organizing effort for the term of the loan.

Additionally, in order to receive a loan, loan guarantee, or other investment under the Federal Reserve Direct Loan program, an otherwise eligible mid-sized business must agree that:

- For twelve (12) months after the loan is no longer outstanding, the business will not buy back any equity security in the eligible business or a parent company listed on a national securities exchange;
- For twelve (12) months after the loan is no longer outstanding, the business will not pay any dividends or make any capital distributions with respect to common stock of the business; and
- The business will comply with the following compensation limits as applicable;
    - An officer or employee whose total compensation exceeded $425,000 in 2019 may not receive more compensation than that officer or employee received in 2019, and may not receive any severance pay or termination benefits which exceeds twice the maximum total compensation received in 2019.
    - An officer or employee whose total compensation exceeded $3,000,000 in 2019 may not receive more than the sum of $3,000,000 plus 50% of the excess over $3,000,000 of the total compensation received by the officer or employee in 2019.

The Federal Reserve and the Department of Treasury have yet to establish any specific programs or facilities pursuant to Title IV. The CARES Act imposes no specific deadline on the Federal Reserve or the Secretary of the Treasury by which they must establish or publish procedures relating to an application process or minimum requirements. The Department of Treasury and the Federal Reserve are expected to provide additional information and guidance about Federal Reserve Direct Loans under Section 4003(b)(4), including the application process and requirements, in the near future.

Main Street Lending Programs

On April 9, 2020, the Federal Reserve issued term sheets announcing a Main Street Lending Program which will allow eligible banks to originate new Main Street loans and expand upon existing loans (new tranche). While we await formal details, the following is a brief summary of the terms:

- These Main Street loans can be obtained in addition to PPP loans.
- Eligible borrowers can have up to 10,000 employees or up to $2.5 billion in 2019 annual revenue.
- "Most" of the borrower's employees have to be based in the United States.
- The loans are for four (4) years with principal and interest deferred for one (1) year.
- Interest rates are between 2.5% and 4%.
- The minimum loan size is $1 million.
- The maximum loan amount for a <u>new</u> loan is the lesser of $25 million or the amount that when added to the borrower's existing and committed but undrawn debt does not exceed four (4) times borrower's 2019 earnings before interest, taxes, depreciation, and amortization.
- The maximum loan amount for an <u>upsized tranche of an existing loan</u> is the lesser of (i) $150 million, (ii) 30% of the borrower's existing outstanding and committed but undrawn bank debt, or (iii) an amount that when added to the borrower's existing outstanding and committed but undrawn debt does not exceed six (6) times the borrower's EBITDA.
- There is no prepayment penalty.
- The borrower cannot use it to repay or refinance pre-existing loans or lines of credit.
- Distinct from the PPP, the borrower certification relating to employee retention merely states that the borrower will use "reasonable efforts" to maintain payroll and retain its employees during the term of the loan.

In addition to certifications required by applicable statutes and regulations, the following attestations will be required with respect to each Main Street loan:

- For new loans, the eligible lender must attest that the proceeds of the loan will not be used to repay or refinance pre-existing loans or lines of credit made by the eligible lender to the borrower. For loans expanding existing loans, the eligible lender must attest that the proceeds of the upsized tranche of the loan will not be used to repay or refinance pre-existing loans or lines of credit made by the eligible lender to the borrower, including the pre-existing portion of the loan.
- The borrower must commit to refrain from using the proceeds of the loan to repay other loan balances. The borrower must commit to refrain from repaying other debt of equal or lower priority, with the exception of mandatory principal payments, unless the borrower has first repaid the loan in full.
- The eligible lender must attest that it will not cancel or reduce any existing lines of credit outstanding to the borrower. The borrower must attest that it will not seek to cancel or reduce any of its outstanding lines of credit with the eligible lender or any other lender.
- The borrower must attest that it requires financing due to the exigent circumstances presented by the COVID-19 pandemic, and that, using the proceeds of the loan, it will make reasonable efforts to maintain its payroll and retain its employees during the term of the loan.
- The borrower must attest that it meets the EBITDA leverage condition as described above.
- The borrower must attest that it will follow compensation, stock repurchase, and capital distribution restrictions that apply to the Federal Reserve Direct Loan programs under Section 4003(c)(3)(A)(ii) of the CARES Act.
- Eligible lenders and borrowers will each be required to certify that the entity is eligible to participate in the Facility, including in light of the conflicts of interest prohibition in section 4019(b) of the CARES Act.

Borrowers will be required to pay a loan origination fee to the eligible lender in the amount of 100 basis points of the principal amount of the loan and may also be required to reimburse the eligible lender for the facility fee it owes to the Federal Reserve (100 basis points of the principal amount of the loan participation purchased by the Federal Reserve through a special purpose vehicle).

The Federal Reserve and the Department of the Treasury will likely make adjustments to the terms and conditions of the Main Street Lending Program. Further, the reactions of eligible lenders to the details of the program remains uncertain. As a result, material aspects of the Main Street Lending Program may change.

The Jaffe COVID-19 Task Force will continue to monitor developments related to these programs and is available to answer any questions you may have about them. Because we anticipate ongoing developments and guidance, we highly encourage you to seek the advice of legal counsel before applying for a loan under any of these programs.

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