COVID-19: The New Stimulus Package

SBA Programs, Title IV Programs, Federal Reserve Programs, and Other Stimulus Programs

Lee Ann Anderson | andersonle@gtlaw.com | 202.331.3128
Carl Fornaris | fornarisc@gtlaw.com | 305.579.0626
Barbara A. Jones | jonesb@gtlaw.com | 310.586.7773
Robert Mangas | mangasr@gtlaw.com | 202.530.8507
Shomari Wade | wades@gtlaw.com | 202.530.8515
Jennifer Zucker | zuckerjs@gtlaw.com | 202.331.3114

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Presenters – GT’s COVID-19 Economic Stimulus Team

• Barbara A. Jones (Moderator), Shareholder, Los Angeles
• Lee Ann Anderson, Shareholder, Washington, D.C.
• Carl Fornaris, Shareholder, Miami
• Robert Mangas, Shareholder, Washington D.C.
• Shomari Wade, Of Counsel, Washington, D.C.
• Jennifer Zucker, Shareholder, Washington, D.C.
Topics to be discussed

I. Legislative Background

II. Overview of Title I of CARES Act

III. Overview of Title IV of CARES Act
   a. Relief for Specific Industries
   b. Relief for Medium Size Businesses
   c. Relief Under Recent Treasury and Fed Proposals
   d. Relief for Certain Borrowers

IV. Legislative and Regulatory Outlook
Major Congressional Actions

• Coronavirus Preparedness and Response Supplemental Appropriations Act (Pub.L. 116-123) (March 6)
  • SBA 7(b) economic injury disaster loans funding and declaration
    • 3/16: SBA begins issuing state requested declarations

• Families First Coronavirus Response Act (Pub.L. 116-127) (March 18)

• Coronavirus Aid, Relief, and Economic Security (CARES) Act (Pub.L. 116-136) (March 27)
  • SBA 7(a) expanded to include Paycheck Protection Program ($349 Bil.)
  • Treasury’s Exchange Stabilization Fund authorized to support Federal Reserve’s lending facilities to eligible businesses, states, and municipalities ($454 Bil.)
    • 3/23: Fed announces 3 new facilities to support businesses, considering others
Title I, Title IV, and Other Federal Stimulus Programs

- Eligible Businesses/Recipients
  - Small Business/SBA Support
  - Financial Regulatory Guidance on Borrowers
  - Capital and Liquidity Relief
  - Discount Window Access & Reserve Requirement
  - Additional Temporary USD Swap Lines
  - Commercial Paper Funding Facility
  - Primary Dealer Credit Facility
  - Term Asset-Backed Securities Lending Facility
  - Money Market Mutual Fund Liquidity Facility
  - Secondary Market Corporate Credit Facility
  - State, Territory, Tribal, and Municipal Relief
  - Medium Sized Business and Main Street Support
  - Specific Industry Support

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Title I CARES Act Credit Programs
Small Business Interruption Loans

- **Small or Other Business Interruption Loans**
  - Paycheck Protection Program (PPP) under CARES Act and SBA 7 (A)
    - Eligible Businesses and Entities
    - SBA Affiliation Rules
    - Borrowing Amounts
    - Loan Forgiveness
    - Additional Details
  - Economic Injury Disaster Loan (EIDL) under SBA 7(B) lending program
Small Business Interruption Loans

• **Eligible Businesses and Entities**
  - Sole proprietorship or independent contractor and eligible self-employed individuals
  - Small business or other concern that has 500 or fewer employees; or the applicable size standard in number of employees as provided by SBA, if higher
  - Affiliation waived for three types of business:
    - businesses with fewer than 500 employees at one location in the accommodation and food service industry
    - businesses that operate franchises
    - businesses that receive assistance from Small Business Investment Corporation
Small Business Interruption Loans

- **Affiliation Rules**
  - Become important when SBA is deciding whether a business’s affiliations preclude them from being considered “small”
  - Exists when one business controls or has the power to control another through ownership, management, or other relationships or interactions between the parties
  - Not waived for nonprofits and portfolio companies of private equity-backed and venture capital-backed businesses
  - Highly specific fact-based inquiry
Small Business Interruption Loans

• **Affiliation through Control**
  • Deemed to be in control of all entities in which you own more than 50% of the concern’s voting stock
  • Minority shareholder deemed to be in control by SBA if they have the right to appoint board members with veto rights

• **Affiliation through Common Management**
  • If officers, directors, managing members, or general partners of a concern control the BOD and/or the management of another business concern
Small Business Interruption Loans

• **Affiliation through Contract or Economic Dependence**
  
  • loan applicant derived more than 85% of its receipts over the previous three fiscal years from a contractual relationship with the other concern, and
  
  • contract restricts the loan applicant from selling the same type of products or services to another purchaser

• **SBA may waive affiliation if it loan applicant’s contract does not provide control to the other party**
Small Business Interruption Loans

• **Borrowing Amounts**
  - Intended to cover 8 weeks of payroll expenses and any additional amounts for making payments towards debt
  - Maximum borrowing amount = $10 million
  - Loan Size determined in one of three ways:
    • In business between February 15, 2019 to June 30, 2019
      • Max loan is equal to 250% of your average monthly payroll costs during that time period
      • If your business employs seasonal workers, you can opt to choose March 1, 2019 as your time period start date.
• **Borrowing Amounts (Continued)**
  
  • Not in business between February 15, 2019 – June 30, 2019
    • Your max loan is equal to 250% of your average monthly payroll costs between January 1, 2020 and February 29, 2020
  
  • EIDL taken between February 15, 2020 and June 30, 2020 can be refinanced into a PPP loan
    • Add the outstanding loan amount to the payroll sum.
Small Business Interruption Loans

• Loan Forgiveness
  • Payroll costs incurred during covered 8 week period
  • Reduced by laid-off employees
  • Reinstated if employees rehired by June 30, 2020
  • Principal plus interest forgiven
  • Will not constitute cancellation of indebtedness income for federal tax purposes
  • Unforgiven portion pursuant to lender terms
Small Business Interruption Loans

• **Additional Details**
  - Unsecured loan
  - No precedence over existing debt
  - Collateral and personal guarantees not required
  - Prepayment penalties waived
  - Unforgiven portion term of 10 years at 4%
  - Application deadline is June 30, 2020
Small Business Interruption Loans

- **Economic Injury Disaster Loan (EIDL)**
  - Up to $2 million, 30 year term at 3.75% (profit) or 2.75% (nonprofit)
  - Grant award of up to $10,000, approved in 3 days
  - If apply for both, EIDL subtracted from the amount forgiven under PPP
  - Cannot be used for same purposes
Update: Paycheck Protection Program

- New guidance issued by SBA on March 31, 2020
- Starting Friday, April 3, 2020, small businesses can apply for PPP loans to cover their payroll and other certain expenses through existing SBA lenders
- Starting April 10, 2020, independent contractors and self-employed individuals can apply for PPP loans to cover their payroll and other certain expenses through existing SBA lenders
- Applicants can apply through any existing SBA lender or through any federally insured depository institution, federally insured credit union, and Farm Credit System institution that is participating
- Other regulated lenders will be available to make these loans as soon as they become SBA-approved and enroll in the PPP
Title IV CARES Act Credit Programs
Title IV of the CARES Act

• Provides $500 billion to Treasury’s Exchange Stabilization Fund to provide loans, loan guarantees, and other investments
  • Direct lending to specific industries
  • $454 billion is available for Federal Reserve loans, loan guarantees, and investments to eligible businesses, states, and municipalities
• An “Eligible Business” is a U.S. business that has not otherwise received adequate economic relief under the CARES Act’s other provisions
Credit Support for Specific Industries

The Secretary of the Treasury is authorized to make loans and loan guarantees to:

- The airline industry
  - Passenger air carriers ($25 billion)
  - Cargo air carriers ($4 billion)
- Businesses critical to national security ($17 billion)

Businesses in these sectors are eligible if:

- Alternative financing is not reasonably available and the assistance is “prudently incurred”
- It is domiciled in the U.S. and has significant operations and a majority of its employees based in the U.S.
Loan Conditions for Specific Industries

- Secured or made at interest rate reflecting risk of loan
- Duration shorter than 5 years
- Employment level may not decrease by more than 10% from March 24 level
- Not eligible for loan forgiveness
- Restrictions on executive compensation
- Restrictions on common stock dividends and stock buybacks
- Real-time public disclosure terms of loans
- The government must receive warrants, equity, or senior debt
- The Secretary of Transportation may require air carriers to maintain some scheduled services
Credit Support for Medium-Sized Businesses

• Eligible Businesses (including non-profits) with 500 to 10,000 employees
• The CARES Act grants authority to the Secretary of the Treasury to use $454 billion to support Federal Reserve facilities, including a facility to enable direct lending by banks and other lenders to medium sized businesses
  • Favorable payment terms
    • 2% interest rate
    • Payment automatically deferred for the first 6 months
  • Restrictions on management
    • No outsourcing or offshoring of jobs
    • Retention of at least 90% of workforce at full compensation and benefits
    • Intent to restore all employees as of February 1, 2020 within 4 months after the end of the public health emergency
    • May not end existing collective bargaining agreements
    • Neutrality in union organizing efforts
    • Executive compensation limits
    • Prohibitions on stock buybacks and common stock dividends
Credit Support for State, Municipal, and Tribal Governments

• The CARES Act authorizes the Secretary of the Treasury to implement a program or facility to provide liquidity to the financial system that supports lending to States and municipalities

• The term “State” includes Indian Tribes, the District of Columbia, and U.S. Territories and Possessions
Main Street Lending Program

- The CARES Act does not limit the discretion of the Federal Reserve to establish a “Main Street Lending Program” or other similar program or facility that supports lending to small- and mid-sized businesses on terms consistent with the authority given to the Federal Reserve by Section 13(3) of the Federal Reserve Act.
Title IV Accountability Provisions

• CARES Act establishes a Congressional Oversight Commission and Pandemic Response Accountability Committee

• CARES Act establishes within Treasury an Office of the Special Inspector General for Pandemic Recovery. The Special Inspector General is tasked with conducting audits and investigations of loans and loan guarantees made by Treasury under Title IV

• CARES Act requires Treasury to publish on its website a plain language description about each loan and loan guarantee within 72 hours of the transaction, including the date of application, date of application approval, and identity of the recipient-borrower
Title IV: Facilitation of Bank Lending

- Policy goal of encouraging banks to work with borrowers by easing reporting requirements that could otherwise negatively impact regulatory classifications and loan loss allowances
- Relief from Financial Accounting Standards on Current Expected Credit Loss
- Troubled Debt Restructurings for borrowers affected by COVID-19, suspension of generally accepted accounting principles for reporting loan modifications
- Capital ratio requirement for community banks reduced from 9% to 8%
- Federal Deposit Insurance Corporation authorized to further guarantee obligations of depositary institutions
- Office of Comptroller authorized to exempt transactions from lending limits
- Foreclosure moratorium on federally backed mortgage loans and consumer right to request forbearance
Federal Reserve and Treasury Programs to Facilitate Liquidity for the U.S. Capital Markets
# Federal Reserve Facilities

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Primary Market Corporate Facility

- The PMCCF Facility will purchase eligible corporate bonds directly from eligible issuers and will make eligible loans to eligible issuers.

- Eligible corporate bonds and loans must meet each of the following criteria at the time of bond purchase or loan origination by the Facility:
  - Issued by an eligible issuer
  - Issuer is rated at least BBB-/Baa3 by a major NRSRO and, if rated by multiple major NRSROs, rated at least BBB-/Baa3 by two or more NRSROs, in each case subject to review by the Federal Reserve; and
  - Have a maturity of 4 years or less

- The maximum amount of outstanding bonds or loans of an eligible issuer that borrows from the Facility may not exceed the applicable percentage of the issuer’s maximum outstanding bonds and loans on any day between March 22, 2019 and March 22, 2020:
  - 140% for eligible assets/eligible issuers with a AAA/Aaa rating from a major NRSRO;
  - 130% for eligible assets/eligible issuers with a AA/Aa rating from a major NRSRO;
  - 120% for eligible assets/eligible issuers with an A/A rating from a major NRSRO; or
  - 110% for eligible assets/eligible issuers with a BBB/Baa rating from a major NRSRO

- Bonds and loans under the PMCCF Facility are callable by the eligible issuer at any time at par

- At the borrower’s election, all or a portion of the interest due and payable on each interest payment date may be payable in kind for 6 months, extendable at the discretion of the Board of Governors of the Federal Reserve System. A borrower that makes a PIK election may not pay dividends or make stock buybacks during the period it is not paying interest

- The PMCCF Facility will cease purchasing eligible corporate bonds or extending loans on September 30, 2020, unless the Facility is extended by the Board of Governors of the Federal Reserve System
Secondary Market Corporate Facility

- A Special Purpose Vehicle (SPV) established by the Federal Reserve bank of New York will purchase eligible individual corporate bonds as well as eligible corporate bond portfolios in the form of exchange traded funds (ETFs) in the secondary market.

- The SMCCF may purchase corporate bonds that meet each of the following criteria at the time of purchase:
  - Issued by an eligible issuer
  - Rated at least BBB-/Baa3 by a major NRSRO and, if rated by multiple major NRSROs, rated at least BBB-/Baa3 by two or more NRSROs, in each case subject to review by the Federal Reserve
  - Have a remaining maturity of 5 years or less

- The SMCCF may also purchase U.S.-listed ETFs whose investment objective is to provide broad exposure to the market for U.S. investment grade corporate bonds.

- The maximum amount of bonds that the SMCCF will purchase from any eligible issuer will be capped at 10% of the issuer’s maximum bonds outstanding on any day between March 22, 2019 and March 22, 2020.

- The facility will not purchase more than 20% of the assets of any particular ETF as of March 22, 2020.

- The SMCCF will purchase eligible corporate bonds at fair market value in the secondary market. The Facility will avoid purchasing shares of eligible ETFs when they trade at prices that materially exceed the estimated net asset value of the underlying portfolio.

- The SMCCF will cease purchasing eligible corporate bonds and eligible ETFs no later than September 30, 2020, unless the Facility is extended by the Federal Reserve.
The loans under TALF will have a term of 3 years; will be nonrecourse to the borrower; and will be fully secured by eligible ABS.

Eligible collateral under TALF includes U.S. dollar denominated cash (that is, not synthetic) ABS that have a credit rating in the highest long-term or the highest short-term investment-grade rating category from at least two eligible NRSROs and do not have a credit rating below the highest investment-grade rating category from an eligible NRSRO. All or substantially all the credit exposures underlying eligible ABS must have been originated by a U.S. company. Eligible ABS must be issued on or after March 23, 2020. Eligible collateral must be ABS where the underlying credit exposures are one of the following:

- Auto loans and leases;
- Student loans;
- Credit card receivables (both consumer and corporate);
- Equipment loans;
- Floorplan loans;
- Insurance premium finance loans;
- Certain small business loans that are guaranteed by the Small Business Administration; or
- Eligible servicing advance receivables.

Eligible borrowers under the TALF include all U.S. companies that own eligible collateral and maintain an account relationship with a primary dealer.

The pledged eligible collateral will be valued and assigned a haircut according to a schedule based on its sector, the weighted average life, and historical volatility of the ABS.

Loans made under the TALF will be pre-payable in whole or in part at the option of the borrower.

No new credit extensions will be made after September 30, 2020, unless the TALF is extended.
An SPV formed for purposes of creating the CPFF will purchase from eligible issuers 3-month U.S. dollar-denominated commercial paper through the New York Fed’s primary dealers.

Eligible issuers are U.S. issuers of commercial paper, including municipal issuers and U.S. issuers with a foreign parent company.

Except as provided in the next sentence, the SPV will only purchase U.S. dollar-denominated commercial paper (including asset-backed commercial paper (ABCP) that is rated at least A1/P1/F1 by a major nationally recognized statistical rating organization (NRSRO) or, if rated by multiple major NRSROs, is rated at least A1/P1/F1 by two or more major NRSROs, in each case subject to review by the Federal Reserve. An issuer that, on March 17, 2020, was (1) rated at least A1/P1/F1 by a major NRSRO or, if rated by multiple major NRSROs, was rated at least A1/P1/F1 by two or more major NRSROs; and (2) is subsequently downgraded, will be able to make a one-time sale of commercial paper to the SPV so long as the issuer is rated at least A2/P2/F2 by a major NRSRO or, if rated by multiple major NRSROs, is rated at least A2/P2/F2 by two or more major NRSROs, in each case subject to review by the Federal Reserve.

The SPV will not purchase asset-backed commercial paper (ABCP) from issuers that were inactive prior to the creation of the CPFF. An issuer will be deemed inactive if it did not issue ABCP to institutions other than the sponsoring institution for any consecutive period of 3-months or longer between March 16, 2019 and March 16, 2020.

The maximum amount of a single issuer’s commercial paper the SPV may own at any time will be the greatest amount of U.S. dollar-denominated commercial paper the issuer had outstanding on any day between March 16, 2019 and March 16, 2020.

For commercial paper rated A1/P1/F1, pricing will be based on the then-current 3-month overnight index swap (OIS) rate plus 110 basis points.

For commercial paper rated A2/P2/F2, pricing will be based on the then-current 3-month OIS rate plus 200 basis points.

At the time of its registration to use the CPFF, each issuer must pay a facility fee equal to 10 basis points of the maximum amount of its commercial paper the SPV may own.

The SPV will cease purchasing commercial paper on March 17, 2021, unless the Board extends the facility.
Money Market Mutual Fund Liquidity Facility

- The Federal Reserve Bank of Boston will lend to eligible borrowers, taking as collateral certain types of assets purchased by the borrower from MMMFs.
- Eligible borrowers are all U.S. depository institutions, U.S. bank holding companies (parent companies incorporated in the United States or their U.S. broker-dealer subsidiaries), or U.S. branches and agencies of foreign banks.
- The applicable MMMFs must identify as a Prime, Single State, or Other Tax-Exempt money market fund under item A.10 of Securities and Exchange Commission Form N-MFP.
- Borrowings under the MMFL will mature at the lesser of 12 months and the maturity date of the pledged collateral.
- Loans under the MMLF will be in a principal amount equal to the value of the collateral pledged to secure the advance.
- Loans made under the MMLF are made without recourse to the Borrower.
- Federal Reserve, the OCC, and the FDIC issued an interim final rule to allow banking organizations to neutralize the effects of purchasing assets through the program on risk-based and leveraged capital ratios.
Additional Federal Financial Agency Actions

• Federal Open Market Committee purchases of Treasury securities and agency mortgage-backed securities
• Discount window usage for loans to depository institutions
• Authorization of U.S. banking organizations to access their Dodd-Frank mandated capital and liquidity buffers for adverse situations
1. Meeting the Financial Needs of Affected Borrowers
   • On March 9, 2020, the Federal Reserve, FDIC, OCC, NCUA, and state bank regulators issued a statement “encouraging” financial institutions to meet the financial services needs of their customers and members in areas affected by COVID-19

2. Community Reinvestment Act Favorable Consideration
   • On March 19, 2020, the Federal Reserve, FDIC, and OCC issued a joint statement on Community Reinvestment Act (CRA) consideration for activities in response to COVID-19, stating that for CRA purposes, the agencies will favorably consider retail banking and lending activities that meet the needs of affected low- and moderate-income individuals, small businesses, and small farms, consistent with safe and sound banking practices and applicable laws, including consumer protection laws
3. **Short-Term Loan Modifications**

On March 23, 2020, the Financial Agencies issued an Interagency Statement on Loan Modifications and Reporting for Financial Institutions Working with Customers Affected by the Coronavirus. The Guidance does two key things:

- Short-term loan modifications (for loans of all types) granted to borrowers that have become financially distressed as a result of economic conditions created by COVID-19 will not result in a loan being classified a troubled debt restructuring (TDR). According to U.S. GAAP, a restructuring of a loan or other credit constitutes a TDR if the lender/creditor, for economic or legal reasons related to the debtor’s financial difficulties, grants a concession to the debtor that it would not otherwise consider.

  - The Financial Agencies have confirmed with staff of the Financial Accounting Standards Board that short-term (e.g., 6 months or less) loan modifications made on a good faith basis in response to COVID-19 for borrowers who were current prior to any relief, are not TDRs.

  - Modification actions can include payment deferrals, fee waivers, extensions of repayment terms, or other delays in payment that are insignificant.

- Bank regulators will not criticize bankers for granting short-term loan modification relief, if the action taken is done in good faith. This represents a departure from past practice (Great Recession).
Legislative and Regulatory Outlook and Update
Future Congressional and Regulatory Actions

• Congress is likely to consider at least one more Coronavirus-related bill
  • Senate has announced no more votes prior to April 20
  • House schedule uncertain, but also unlikely to return before April 20

• Fourth bill will reportedly focus on economic growth
  • Infrastructure funding
  • Other job creation initiatives
  • Any technical changes required to the first three bills

• Stay Tuned!
Questions?

For more information,

Visit: GT COVID-19 Economic Stimulus

Email: prepared@gtlaw.com