CARES Act Provides $500 Billion to Eligible Businesses, States and Municipalities

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On March 27, 2020 the Coronavirus Aid, Relief and Economic Security Act (CARES Act) was signed into law. Among other programs and types of assistance intended to provide relief to those impacted by the pandemic and to stimulate the economy, the CARES Act provides $500 billion to Treasury’s Exchange Stabilization Fund for states, municipalities and eligible businesses (including those in certain severely distressed industries, as well as mid-sized businesses not eligible to participate in the Paycheck Protection Program).

The funds will be made available as follows:

1. Direct lending by Treasury, through designated financing agents to businesses in severely distressed industries including up to $25 billion for airlines $4 billion for air cargo firms and $17 billion for businesses deemed critical to U.S. national security. By April 6, 2020 Treasury must publish procedures for application and minimum requirements for this aspect of the program.

2. Support of Federal Reserve facilities of $454 billion (plus funding not used as described above) for eligible businesses, states and municipalities. This support may be provided by purchasing obligations or interests directly from
issuers, purchasing obligations or interests in secondary markets, or making loans or other advances (including secured loans). While $454 billion refers to the amount that Treasury may use in support of these facilities, the Federal Reserve is expected to use leverage against the assets and capital of the vehicles established for these facilities to create up to $4 trillion in lending according to the administration. We anticipate Treasury and the Federal Reserve issuing guidance in the coming weeks.

As to all facilities under this program, Treasury has broad discretion in setting general terms and conditions. Interest rates will be determined by Treasury based on the risk and current average yield on outstanding U.S. debt obligations (see below as to the mid-sized businesses facility). Any applicant whose securities are publicly traded must agree not to engage in stock buybacks for the duration of the loan plus one year (except to the extent required under a preexisting contractual obligation), and each applicant (i.e., whether or not public) must agree not to pay dividends on common stock for the duration of the loan plus one year. Assistance will be treated as indebtedness for federal income tax purposes, and Treasury may issue regulations or guidance to carry out this purpose (e.g., providing that the acquisition of warrants, stock options or other equity interests does not result in an ownership change for purposes of IRC 382).

Notably, unlike the Paycheck Protection Program, loans provided under this program are not eligible for forgiveness. Also, each applicant must agree to restrictions that substantially limit executive compensation and severance that last for one year following repayment. This program will be overseen by a Congressional Oversight Commission and a special inspector general who will keep Congress informed through quarterly reports.

Additional terms for direct lending by Treasury to businesses in severely distressed industries:

1. credit is not otherwise reasonably available to the applicant;
2. the loan must be prudently incurred as determined by Treasury;
3. the loan must be secured by sufficient collateral or carry interest at a rate that reflects the risk of the loan and not less than market prior to the pandemic;
4. the loan duration may not exceed five years;
5. until September 30, 2020 the applicant must retain at least 90 percent of its employment level as of March 24, 2020;
6. the applicant must be created or organized in the U.S. and have significant operations in and a majority of its employees based in the U.S.; and
7. the applicant must have incurred or is expected to incur covered losses such that the continued operations of the business are jeopardized, as determined by Treasury.

Additionally, Treasury may not provide assistance unless either (a) the applicant’s securities are publicly traded and Treasury receives a warrant or equity interest in
the applicant or (b) as to any applicant whose securities are not publicly traded, Treasury receives a warrant or equity interest in the applicant or a senior debt instrument issued by the applicant. In any event, Treasury may not exercise voting power with respect to any common shares acquired.

**For mid-sized businesses (with between 500 and 10,000 employees),** including, to the extent practicable, nonprofit organizations, Treasury must endeavor to implement a facility that provides financing to lenders that make direct loans to such businesses as part of its support of Federal Reserve programs and facilities under this legislation. The annualized interest rate may not exceed two percent. For a minimum of six months (Treasury has discretion to extend this period), no principal or interest will be due. Each applicant will be required to certify that:

- the pandemic makes necessary the loan to support the applicant’s ongoing operation;
- loan proceeds will be used to retain at least 90 percent of the applicant’s workforce, at full compensation and benefits, until September 30, 2020;
- the applicant intends to restore no less than 90 percent of its workforce that existed at February 1, 2020 and to restore all compensation and benefits to its workers no later than four months after the end of the pandemic;
- the applicant is domiciled and created or organized in the U.S. with significant operations in and a majority of its employees located in the U.S.;
- the applicant is not a debtor in a bankruptcy proceeding;
- the applicant will not pay dividends on its common stock, or repurchase any publicly-listed equity security, while the loan is outstanding (except to the extent required under a preexisting contractual obligation);
- the applicant will not outsource or offshore jobs for the term of the loan plus two years; and
- the applicant will not abrogate any existing collective bargaining agreements for the term of the loan plus two years and will remain neutral in any union organizing effort for the term of the loan.

The foregoing only supplement Federal Reserve measures. On March 23, 2020 the Federal Reserve announced new measures to support the economy in light of the pandemic, including:

1. support for critical market functioning;
2. establishing new programs providing up to $300 billion in financing to businesses and individuals;
3. establishing two new facilities to support markets issuing credit to large businesses and related secondary markets;
4. establishing a third Term Asset-Backed Securities Loan Facility to support the
flow of credit; and

5. facilitating the flow of credit to municipalities by expanding the existing Money Market Mutual Fund Liquidity Facility and the existing Commercial Paper Funding Facility.

The Federal Reserve also indicated it would be announcing a new Main Street Business Lending Program to support lending to eligible small and mid-sized businesses. For its part, the CARES Act clarifies that the mid-sized businesses facility that it has authorized does not limit the Federal Reserve's discretion in establishing other programs and facilities within the Federal Reserve's authority, including such Main Street Business Lending Program. As of March 29, 2020 the Main Street Business Lending Program has not been formally announced by the Federal Reserve.

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