



Southern California

COVID-19 IMPACT SERIES

Lending and SBA Options

**BUSINESS
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Today's Presenters

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Bianca Barredo has been with MidCap Financial for four years focusing on originating and structuring asset-backed financing solutions of \$10 and \$500 million for public and private companies. Bianca has provided financing for middle market companies in the west coast for 15 years. Prior to joining MidCap, she was Senior Vice President at GE Capital, Corporate Finance Group, where she was responsible for sourcing and originating cash flow, ABL, and unitranche transactions. Bianca holds an M.B.A. from UCLA Anderson School of Management and a B.S. from USC Marshall School of Business.

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Managing Director



Chuck Doyle

Founded Business Capital in 2002 and is the Managing Director, heading up the firm's Investment Committee. He has nearly 30 years of experience in the financial industry and holds a Certified Turnaround Professional (CTP) designation. Chuck's primary responsibilities include the development, review and analysis of client strategies, sourcing and structuring hyper growth, distressed & non-distressed transactions that involve the investment of Business Capital resources.

Currently President-elect of the Secured Finance Network NorCal, a member of the Boards of TMA NorCal and SoCal, and the National Board of the Boston-based non-profit, Team Impact.

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Heads a national corporate restructuring practice representing corporate debtors, creditors, committees, equity holders and acquirers in distressed financial situations with the goal of creating and structuring transactions that maximize value for his clients.

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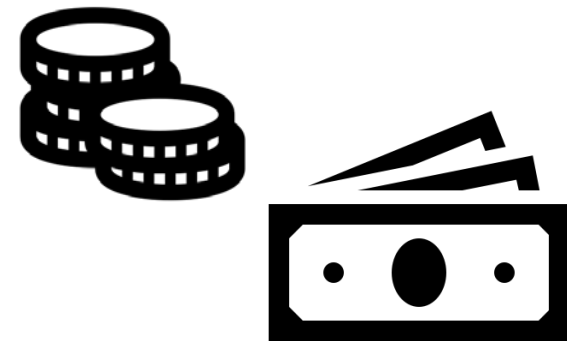
- I. Current Challenges: Lenders**
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I. Current Challenges: Lenders

- The most critical is for businesses to have ample liquidity to weather the next 60-90 days
- Less focus on performance covenants in the short-term with more immediate focus on weekly cash collections and borrowing base availability
- Performance covenant defaults will be with March or April reporting packages so not until end of April and May
- Weekly dialogues with Borrowers most affected and monitoring of:
 - 1) Liquidity
 - 2) Sales
 - 3) Cash collections
 - 4) Cash disbursements to vendors, employees, etc.
 - 5) Inventory balances and mix
 - 6) Quality of receivables: aging, turns, concentrations



Corporate Borrowers Recent Draw Downs

Company	Max Borrowings	Draw Down	Availability Year End	Availability Post Draw Down
Advanced Auto Parts	\$1Bn	\$500MM	\$1Bn	\$500MM
Best Buy	\$1.25Bn	\$1.25Bn	\$1.25Bn	\$0
BJ's	\$250Bn	\$88.9MM	\$88.9MM	\$0
Carnival Corporation	\$3Bn	\$3Bn	\$2.8Bn	\$0
CEC Entertainment	\$114MM	\$105MM	\$105MM	\$0
Dollar Tree	\$1.25bN	\$750MM	\$1.11Bn	\$363MM
Grocery Outlet Holding	\$100MM	\$90MM	\$96.4MM	\$6.4MM
Kirkland's Inc.	\$75MM	\$40MM	\$75MM	\$35MM
McDonald's Corporation	\$1Bn	\$1Bn	N/A	\$0
Regis Corporation	\$295MM	\$183MM	\$213.5MM	N/A
Rent-A-Center	\$300MM	\$183MM	\$213.5MM	N/A
Restaurant Brands Int'l	\$1Bn	\$1Bn	\$998MM	\$0
Shake Shack	\$50MM	\$50MM	\$50MM	\$0
Sysco Corporation	\$2Bn	\$1.6Bn	\$1.15Bn	N/A
US Foods Holding Corp.	\$1.25Bn	\$1Bn	\$552MM	N/A
Vail Resorts	\$500MM	\$400MM	\$231.4MM	\$19MM
WW Grainger, Inc.	\$1.25Bn	\$1Bn	\$750MM	\$250MM
YUM! Brands	\$1Bn	\$950MM	\$998.7MM	\$50MM

1) CreditIntel 4/1/2020

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S&P U. S. High Yield Corporate Bond Index

S&P U.S. High Yield Corporate Bond Index (as of April 3)						
	4/3/2020	4/3/2019	Daily change	1 week change	1 month change	YTD change
All						
WA bid price	84.62	98.71	-0.44	-0.68	-1.15	-5.99
OAS (bps)	863	345	15	5	29	54
YTW	9.67%	5.99%	0.13%	-0.68%	0.31%	1.53%
7-day return	-0.16%	0.47%	-1.66%	-4.66%	0.63%	-0.13%
MTD return	-1.66%	0.23%	-0.48%	12.20%	0.78%	-1.36%
YTD return	-14.82%	7.32%	-0.42%	-0.13%	-0.74%	-7.71%
BB						
WA bid price	90.19	101.77	-0.14	-0.48	-0.95	-7.35
OAS (bps)	671	214	5	-6	22	55
YTW	7.21%	4.66%	0.02%	-0.20%	0.18%	1.40%
7-day return	0.95%	0.24%	-1.30%	-3.34%	0.30%	-0.20%
MTD return	-0.76%	0.08%	-0.14%	12.08%	0.97%	-0.89%
YTD return	-11.95%	6.97%	-0.12%	0.83%	-0.43%	-9.06%
B						
WA bid price	86.37	99.11	-0.64	0.89	-1.02	-5.07
OAS (bps)	909	359	23	-2	32	48
YTW	9.82%	6.07%	0.22%	-0.77%	0.34%	1.75%
7-day return	-0.58%	0.59%	-1.88%	-5.88%	0.72%	0.01%
MTD return	-2.18%	0.35%	-0.69%	11.09%	0.86%	-1.08%
YTD return	-15.37%	7.54%	-0.59%	-0.49%	-0.51%	-6.01%
CCC & Lower						
WA bid price	62.70	88.19	-0.98	-4.14	-1.99	-4.54
OAS (bps)	1614	781	46	98	50	82
YTW	20.54%	10.57%	0.44%	-2.43%	0.73%	1.51%
7-day return	-3.90%	0.97%	-2.59%	-7.08%	1.47%	-0.25%
MTD return	-4.20%	0.47%	-1.42%	15.47%	0.04%	-3.52%
YTD return	-24.74%	7.92%	-1.11%	-3.05%	-2.36%	-7.83%
Distressed						
WA bid price	67.71	68.53	-0.32	27.74	0.55	-5.52
OAS (bps)	1495	1611	20	-1098	-16	131
YTW	17.27%	19.23%	0.19%	-26.69%	0.74%	4.85%
7-day return	-3.40%	1.53%	-0.92%	-5.35%	2.58%	-0.87%
MTD return	-1.95%	0.60%	-0.43%	31.71%	-1.37%	-6.51%
YTD return	-41.70%	8.43%	-0.25%	-2.05%	-7.06%	-4.92%

Index Codes: SPUHYB0 (All), SPUHY2B (BB), SPUHY1B (B), SPUHYCW (CCC & Lower), SPUHYDS (Distressed)

Source: S&P Dow Jones Indices

b



- How do you diligence a new opportunity?
 - In-house field examiners for off-site exams
 - Desktop inventory appraisals from known appraisals with good experience in industry or known to the company.
- How do you meet and evaluate a management team?
- How do you underwrite lasting effects of COVID-19? What industries or sectors are COVID-proof?



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II. Challenges: Companies

COVID-19 impact to industries is wide-spread and

■ 1st Degree Impact

- Restaurants
- Retail
- O&G
- Auto
- Aerospace

■ 2nd Degree Impact

- Consumer spending
- Sole through retail or grocery channels (if not deemed essential)
- Non-essential healthcare

■ 3rd Degree Impact

- Facility closures
- Unable to pivot to a work from home

Borrowers are doing what they can to boost liquidity:

- Negotiating with lenders
 - Drawing down on revolvers
 - P&I deferrals
 - Re-negotiating liquidity covenants or blocks
- Deferrals & other actions
 - Stretching terms with vendors
 - Rent payment deferrals (under executive order or abatement programs, if available)
 - Selling slow-paying receivables
- Operating measures
 - Employee furloughs and layoffs
 - Salary reduction
 - Reduction or elimination of overtime
 - Reducing or eliminating capital expenditures
- Additional Capital
 - Equity
 - Loan-to-Own



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III. The Legislative Solution: The SBA Loan Program

New SBA Programs

SBA Subsidies: \$17Bn

- Pays existing SBA loan payments for next 6 months or 6 months after deferment
- Effectively a grant that does not need to be repaid
- Relief “should be” automatic with no need to apply or request relief
- Loans in good standing may leave some unsure of what to do

SBA Payroll Protection Program: \$349 Bn

- Up to \$10 million per business
- Eligible business < 500 employees
- “Affiliation Rules” apply for all except hospitality and restaurant business (NAICS ‘72’) and businesses with financial assistance from SBIA

Expanded SBA Programs

SBA Emergency Disaster Loans

- Added up to a \$10,000 “grant” payable within 24 hours
- Expanded eligibility (not for sex, gambling, illegal activity, lobbyists and agriculture)
- Expanded limit to \$2 million through December 31, 2020
- Can get BOTH an EIDL and PPP, but not to cover same expenses

SBA Express Loans

- 36 hour approval
- Increased from \$350,000 to \$1 million
- Increased limit available through December 31, 2020

TERMS

- Up to \$2 million up to \$10,000 advance 'grant' in 24 hours
- 3.75% int. rate (2.75% for non-profits)
- Up to 30 year maturity
- "Working capital" loan – not to replace revenues, lost sales or profits
- Available at increased limits up to December 31, 2020

ELIGIBILITY

- Lenders make underwriting decisions, gov't provides minimum guidelines
 - Can approve based solely on credit score
- Expanded to most businesses <500 employees, sole proprietors, individual Contractors
 - But not for illegal, sex, gambling, lobbyists or agriculture
- Waiver of typical SBA requirements such as less than 1yr. in business, no personal guarantee < \$200K, no need to seek money elsewhere first
 - No waiver of "Affiliation Rules"
- Available in conjunction with a PPP, but NOT for same purpose (payroll)
 - You can use your PPP to repay portion of prior EIDL used for payroll

KEY HIGHLIGHTS

- Approved within 36 hours, available in 90 days
- Increased the limit from \$350,000 to \$1 million
- 50% guarantee by SBA
- Also, Express “Bridge” Loans - \$25,000 cash in 36 hours, typically a bridge to an EIDL

USES

- Working Capital
- Property, Plant & Equipment; Inventory; Raw Materials; Supplies
- Construction and renovation costs
- Acquisitions
- Debt Refinancing



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IV. The Paycheck Protection Program ("PPP")

WAIVER OF MANY SBA LOAN REQUIREMENTS FOR LENDERS

- Lenders **MUST** comply with the applicable lender obligations set forth in the interim final rule (rule is subject to change)
- Lender does not need to comply with section 120.150 “What are SBA’s lending criteria?”
- Lenders may significantly decrease diligence and rely on certifications of the borrower in order to determine eligibility of the borrower and use of loan proceeds
- Lenders may rely on specified documents provided by the borrower to determine qualifying loan amount and eligibility for loan forgiveness
- Lenders will be held harmless for borrowers’ failure to comply with program criteria

You are eligible for a PPP loan if you have 500 or fewer employees whose principal place of residence is in the United States, or are a business that operates in a certain industry and meet the applicable SBA employee-based size standards for that industry, and:

- You are:
 - A small business concern as defined in section 3 of the Small Business Act (15 USC 632), and subject to SBA's affiliation rules under 13 CFR 121.301(f) unless specifically waived in the Act;
 - A tax-exempt nonprofit organization described in section 501(c)(3) of the Internal Revenue Code (IRC), a tax-exempt veterans organization described in section 501(c)(19) of the IRC, Tribal business concern described in section 31(b)(2)(C) of the Small Business Act, or any other business; and
- You were in operation on February 15, 2020 and either had employees for whom you paid salaries and payroll taxes or paid independent contractors, as reported on a Form 1099-MISC, including individuals that operate:
 - under a sole proprietorship; or
 - as an independent contractor; or
 - as an eligible self- employed individual.

How much can I borrow?

The following methodology, is one of the methodologies contained in the Act:

- 1** Aggregate payroll costs (defined in next slide) from the last twelve months for employees whose principal place of residence is the United States.
- 2** Subtract any compensation paid to an employee in excess of an annual salary of \$100,000 and/or any amounts paid to an independent contractor or sole proprietor in excess of \$100,000 per year.
- 3** Calculate average monthly payroll costs (divide the amount from Step 2 by 12).
- 4** Multiply the average monthly payroll costs from Step 3 by 2.5.
- 5** Add the outstanding amount of an Economic Injury Disaster Loan (EIDL) made between January 31, 2020 and April 3, 2020, less the amount of any “advance” under an EIDL COVID-19 loan (because it does not have to be repaid).

Payroll costs consist of compensation to employees (*whose principal place of residence is the United States*) in the form of:

- Salary, wages, commissions, or similar compensation;
- Cash tips or the equivalent (based on employer records of past tips or, in the absence of such records, a reasonable, good-faith employer estimate of such tips);
- Payment for vacation, parental, family, medical, or sick leave; allowance for separation or dismissal;
- Payment for the provision of employee benefits consisting of group health care coverage, including insurance premiums, and retirement;
- Payment of state and local taxes assessed on compensation of employees; and for an independent contractor or sole proprietor—wage, commissions, income, or net earnings from self-employment or similar compensation.

Is there anything that is expressly excluded from the definition of payroll costs?

The Act expressly excludes the following:

- Any compensation of an employee whose principal place of residence is outside of the United States;
- The compensation of an individual employee in excess of an annual salary of \$100,000, prorated as necessary;
- Federal employment taxes imposed or withheld between February 15, 2020 and June 30, 2020, including the employee's and employer's share of FICA (Federal Insurance Contributions Act) and Railroad Retirement Act taxes, and income taxes required to be withheld from employees; and
- Qualified sick and family leave wages for which a credit is allowed under sections 7001 and 7003 of the Families First Coronavirus Response Act (Public Law 116–127).



Do independent contractors count as employees for purposes of PPP loan calculations?

No, independent contractors have the ability to apply for a PPP loan on their own so they do not count for purposes of a borrower's PPP loan calculation.

What is the interest rate on a PPP loan?

The interest rate will be 100 basis points or one percent. Note that the Act provides for a maximum of 4%, BUT the Rules are determinative.

What will be the maturity date on a PPP loan?

The maturity is two years. While the Act provides that a loan will have a maximum maturity of up to ten years from the date the borrower applies for loan forgiveness, the Administrator determined that a two-year loan term is sufficient.

Can I apply for more than one PPP loan?

No eligible borrower may receive more than one PPP loan. While the Act does not expressly provide that each eligible borrower may only receive one PPP loan, the Administrator has determined that a one loan per borrower limitation is necessary.

Can my PPP loan be forgiven in whole or in part?

The actual amount of loan forgiveness will depend, in part, on the total amount of payroll costs, payments of interest on mortgage obligations incurred before February 15, 2020, rent payments on leases dated before February 15, 2020, and utility payments under service agreements dated before February 15, 2020, over the eight-week period following the origination date of the loan. However, *not more than 25 percent of the loan forgiveness amount may be attributable to non-payroll costs.*

What happens if PPP loan funds are misused?

If you use PPP funds for unauthorized purposes, SBA will direct you to repay those amounts. If you knowingly use the funds for unauthorized purposes, you will be subject to additional liability such as charges for fraud. If one of your shareholders, members, or partners uses PPP funds for unauthorized purposes, SBA will have recourse against the shareholder, member, or partner for the unauthorized use.

How can PPP loans be used?

The proceeds of a PPP loan must be used for:

- insurance payroll costs (as defined in the Act and in 2.f.);
- costs related to the continuation of group health care benefits during periods of paid sick, medical, or family leave, and premiums;
- mortgage interest payments (but not mortgage prepayments or principal payments);
- rent payments;
- utility payments;
- interest payments on any other debt obligations that were incurred before February 15, 2020; and/or
- refinancing an SBA EIDL loan made between January 31, 2020 and April 3, 2020.

However, at least 75 percent of the PPP loan proceeds shall be used for payroll costs to be forgiven.

What do lenders have to do in terms of loan underwriting?

Each lender shall:

- Confirm (i) receipt of borrower certifications; (ii) information demonstrating employees and prior payroll; and (iii) dollar amount of average monthly payroll costs
- Follow applicable Bank Secrecy Act (BSA/AML) requirements:
- PPP loans for existing customers will not require re- verification under applicable BSA requirements, unless otherwise indicated by the institution's risk-based approach to BSA compliance.
- For new or existing customers who are eligible borrowers under the PPP, establish an anti-money laundering (AML) compliance
- Also understand the nature and purpose of their PPP customer relationships to develop customer risk profiles.

Each lender's underwriting obligation under the PPP is limited to the items above and reviewing the "Paycheck Protection Application Form."

Can lenders rely on borrower documentation for loan forgiveness?

Yes. The lender does not need to conduct any verification . . . The Administrator will hold harmless any lender that relies on such borrower documents and attestation from a borrower.

What fees will lenders be paid?

SBA will pay lenders fees for processing PPP loans in the following amounts:

- Five (5) percent for loans of not more than \$350,000;
- Three (3) percent for loans of more than \$350,000 and less than \$2,000,000; and
- One (1) percent for loans of at least \$2,000,000.

Can SBA purchase some or all of the loan in advance?

Yes. A lender may request that the SBA purchase the expected forgiveness amount of a PPP loan or pool of PPP loans at the end of week seven of the covered period

.....

The Administrator will purchase the expected forgiveness amount of the PPP loan(s) within 15 days of the date on which the Administrator receives a complete report that demonstrates that the expected forgiveness amount is reasonable.

Note that the 7 week waiting period was added by the Rules (at the 11th hour).



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V. PPP Implementation Issues

- **Compressed Rule Making Process –**
 - Rules govern and modify the legislation
 - Banks are penalized for non-compliance
 - Banks asked to put out an enormous sum - \$325 billion
 - Typical rule-making and comment process 90-180 days
 - Compressed to 5 days for rule-making, 0 days for comments and questions
- **Changes to the Legislation, 12 hours before going “live”**
 - 4% interest changed to 1%
 - 10 year changed to 2 year
 - 15 day sell back changed to 7 weeks
 - AML guidelines apply
- **Looking Forward To The Backlash**
 - Banks will be blamed – government will point the fingers
 - There will not be enough money to go around
 - Banks have final decision-making/underwriting authority
 - Banks will profit handsomely



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VI. SBA PROGRAMS: EPILOGUE

Distributions to Date:

EIDL – unknown

Express Loans – unknown

Subsidies – unknown

PPP - \$38 billion on 130,000 new loans as of 4/6 at 5pm ET

- Large % of processed applications are from small banks
- Represents avg. loan/grant of \$290,000
- Indicates only smallest businesses being approved (approx. 14-25 employees)
- Majority of filed applications have not been processed
- Largest SBA lender in the Country is not participating
- Predictions ?? Money runs out, disappointed expectations, backlash ?

Are SBA Programs “The Answer”?

- What will be the corresponding cost of bailout for big business
- How does PPP help businesses that cannot operate over the next 8 weeks
- What % of 30 million small businesses can benefit? (approx. 10%)
- Band-aids do not cure trauma

Predictions / Ideas For Office Betting Pools

- Money runs out (how many days)
- Funding For Next Round
- Market reaction to disappointed expectations
 - When and how steep a drop?
- Backlash to Banks

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