Applications Are Open, Now What? FAQs for Accommodating PPP Loans Under Existing Credit Agreements

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The new $349 billion Payment Protection Program ("PPP") administered by the Small Business Administration under the CARES Act began accepting loan applications on April 3, 2020, with more than $4.3 billion of loans processed on the first day alone. Proceeds of these loans may be used for payroll, utilities, rent and mortgage payments. While many private credit lenders may lend to portfolio companies that are ineligible for participation in the program in light of the current regulations with respect to affiliation, other private credit lenders (particularly those with SBIC vehicles) are receiving an influx of requests from their borrowers for amendments to their loan documents in order to permit them to obtain loans pursuant to the PPP. As requests come in, private credit lenders are being asked to act quickly to support their borrowers' efforts to obtain PPP funds as expeditiously as possible. It is to the benefit of both borrowers and lenders to accommodate these loans given that they are unsecured, very low interest loans that are subject to forgiveness. However, private credit lenders should consider some key questions under their existing credit agreements:

Are my Borrowers permitted to incur these loans under their existing debt basket capacity? – Loan documents typically give borrowers general flexibility to incur additional debt subject to dollar and/or ratio based limits. Do your borrowers have remaining capacity under these baskets to incur loans under the PPP, or will they need lender consent to the incurrence of additional debt? If they do have capacity, then an amendment to the Loan Documents may not be required for them to access these funds. If they do not, lenders will either need to increase general debt capacity (which would survive the forgiveness or repayment of the PPP loans) or provide a dedicated basket for the incurrence of PPP loans. Private credit lenders may consider imposing appropriate guardrails on any such dedicated basket, including, for example, dollar caps, cash interest rate caps, and maturity limitations to protect against future changes to the regulations.

How does the new debt flow through leverage ratios? – The PPP loans will be unsecured, so they will not be included in any first lien leverage ratios or secured leverage ratios. For loan documents that employ total leverage ratios, lenders will need to consider whether the PPP loans will be included for purposes of financial covenant compliance, ratio based incurrence tests and/or pricing ratios. Some private credit lenders may be willing to exclude such debt for purposes of financial covenant compliance during the first six months while payments are deferred pursuant to the terms of the PPP, but may provide for different treatment in later periods if the loans have not been forgiven.

What are the conditions for paying these loans if they are not forgiven? – Unlike mezzanine loans or subordinated loans, the PPP loans will not be subject to payment subordination, which means in the ordinary course borrowers will be permitted to make payments with respect to the PPP Loans (including after the occurrence of an event of default). Private credit lenders will have to consider whether they will require satisfaction of payment conditions (such as pro forma covenant compliance, minimum liquidity, absence of any default or event of default) for PPP loans to be paid at their two year maturity and whether any such payment will reduce other basket capacity for restricted debt payments using any general baskets or available amount.

Is there additional reporting private credit lenders should require? – An attractive feature of PPP loans is that they are subject to being forgiven. Up to 100% of the proceeds of PPP loans used to fund payroll costs may be forgiven and up to 25% of the proceeds of the PPP loans forgiven may be used for eligible non-payroll items. Private credit lenders may wish to require regular updates as to efforts by the borrower to seek forgiveness of the PPP loans so that they can track the borrower's efforts to seek forgiveness.

What else? – Prudent private credit lenders are asking for additional affirmative covenants to ensure their borrowers remain eligible for loan forgiveness under the PPP. These covenants may include information rights (requiring borrowers to share with their private credit lenders any correspondence with their SBA lender) and other covenants to comply with requirements for forgiveness of the PPP loans.

Proskauer has created a dedicated a team of lawyers, across disciplines and offices, to help support our clients as they navigate through issues related to COVID-19 and the CARES Act. Should you have any related questions or need any additional information about these issues, please do not hesitate to reach out to a member of Proskauer's Private Credit Group.

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