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CLIENT ALERT

New York Fed Releases Frequently Asked Questions on the Primary Market and Secondary Market Corporate Credit Facilities

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On April 17, 2020, the Federal Reserve Bank of New York (NY Fed) released a set of Frequently Asked Questions (FAQs) to address inquiries about the Primary Market and Secondary Market Corporate Credit Facilities (PMCCF and SMCCF). The FAQs include further details about the two program facilities, which were created on March 23, 2020 by the Board of Governors of the Federal Reserve System (Federal Reserve) under its emergency lending authority under Section 13(3) of the Federal Reserve Act and are funded in part by investments from the Department of Treasury (Treasury) pursuant to the Coronavirus Aid, Relief, and Economic Security Act (CARES Act).

Overview of the Programs Facilities (PMCCF and SMCCF)

The PMCCF was established to provide credit support to large employers in the form of bond and syndicated loan issuances. This facility provides companies access to credit by (i) purchasing qualifying bonds as the sole investor in a bond issuance, or (ii) purchasing portions of syndicated loans or bonds at issuance. This emergency support is intended to assist large employers to better maintain business operations and capacity during the period of dislocations related to the Covid-19 pandemic.

The SMCCF was established to support market liquidity for corporate debt by purchasing (i) corporate bonds of Eligible Issuers (as described below), (ii) shares of U.S.-listed exchange traded funds (ETFs) whose investment objective is to provide broad exposure to the market for U.S. investment-grade corporate bonds, and (iii) shares of U.S.-listed ETFs whose primary investment objective is exposure to U.S. high-yield corporate bonds.

Eligible Issuers and Rating

To qualify as Eligible Issuer under either the PMCCF or the SMCCF, the issuer must be created in or organized under the laws of the United States with material operations in, and a majority of its employees based in, the United States.

In addition, an Eligible Issuer must have been rated at least BBB-/Baa3 as of March 22, 2020, by at least one major nationally recognized statistical rating organization (NRSRO). If rated by multiple major NRSROs, two or more ratings must be at least BBB-/Baa3. If the rating of the Eligible Issuer is subsequently downgraded, the rating must be rated at least BB-/Ba3 as of the date on which the PMCCF or SMCCF makes a purchase. If rated by multiple major NRSROs, such an Eligible Issuer must be rated at least BB-/Ba3 by two or more NRSROs at the time the PMCCF or SMCCF makes a purchase. Ratings are subject to review by the Federal Reserve in every case. Currently, the Federal Reserve considers ratings from three NRSROS: S&P Global Ratings, Moody's Investor Services Inc., and Fitch Ratings, Inc. Other NRSROS may be considered later.

There are other conditions that an Eligible Issuer must satisfy, namely (i) it may not be an insured depository institution or depository institution holding company, as such terms are defined in the Dodd-Frank Act, (ii) it must not have received specific support under the CARES Act or any subsequent federal legislation, and (iii) it must satisfy the conflicts of interest requirements under Section 4019 of the CARES Act. Section 4019 of the Cares Act prohibits any entity that is directly or indirectly owned by the President, Vice President, senior executive branch officials or Members of Congress, or certain of their immediate family members, from receiving any relief funds.

Eligible Issuers will be required to certify compliance with eligibility criteria. Details about such requirements and processes will be provided in the near future.

Eligible Assets

The PMCCF may purchase (i) eligible corporate bonds of Eligible Issuers, with a maturity of 4 years or less, as the sole investor in a bond issuance, or (ii) a portion of syndicated loans or bonds of Eligible Issuers at issuance, with a maturity of 4 years or less. No more than 25 percent of any syndicated loan or bond issuance may be purchased by the PMCCF. The PMCCF's initial focus will be on purchasing bonds at issuance. The PMCCF may refinance existing bonds and issue new bonds. Outstanding debt may be refinanced up to three months ahead of the maturity debt of such outstanding debt. The aggregate amount of outstanding bonds and loans may not exceed 130 percent of the Eligible Issuer's maximum outstanding bonds and loans on any day between March 22, 2019, and March 22, 2020. Eligible Assets in the PMCCF must be rated at least investment grade as of March 22, 2020, and at least BB-/Ba3 at the time of purchase. Investment grade senior secured bonds issued by a non-investment grade issuer are not Eligible Assts.

The SMCCF may purchase (i) corporate bonds that are issued by an Eligible Issuer; (ii) have a remaining maturity of 5 years or less; and (iii) are sold to the SMCCF by an Eligible Seller. In addition, the SMCCF may purchase shares of U.S.-listed ETFs whose investment objective is to provide broad exposure to the market for U.S. corporate bonds. The preponderance of ETF holdings will be of ETFs whose primary investment objective is exposure to U.S. investment-grade corporate bonds, and the remainder will be in ETFs whose primary investment objective is exposure to U.S. high-yield corporate bonds.

Size of the Program Facilities

The combined size of the PMCCF and the SMCCF will be up to $750 billion. The PMCCF and SMCCFs are special purpose vehicles (SPVs) funded by the Federal Reserve on a recourse basis (i.e., secured by all assets of the SPVs), which will purchase the bonds, ETFs and loans. The Treasury will make a $75 billion equity investment in the SPVs to support both the PMCCF ($50 billion) and the SMCCF ($25 billion).

The PMCCF will leverage Treasury's equity at (i) 10 to 1 when acquiring corporate bonds or syndicated loans from Eligible Issuers that are investment grade at the time of purchase, and (ii) 7 to 1 when acquiring corporate bonds or syndicated loans from Eligible Issuers that are rated below investment grade at the time of purchase.

The SMCCF will leverage Treasury's equity at (i) 10 to 1 when acquiring corporate bonds of issuers that are investment grade at the time of purchase and when acquiring ETFs whose primary investment objective is exposure to U.S. investment-grade corporate bonds, and (ii) 7 to 1 when acquiring corporate bonds of issuers that are rated below investment grade at the time of purchase and in a range between 3 to 1 and 7 to 1, depending on risk, when acquiring any other type of eligible asset.

Restrictions On LIBOR-Based Floating Bonds Purchases by PMCCF

LIBOR-based floating-rate debt will not be eligible for purchase in an offering where the PMCCF is the sole participant. When participating in a syndicated issuance, PMCCF purchases will be restricted to fixed-rate debt. Where the PMCCF is participating in a syndication of floating-rate debt, it will require any debt priced off LIBOR to include adequate fallback language. No such restrictions pertain to purchases by the SMCCF. It intends to purchase a range of bonds, including LIBOR-based floating-rate debt.

Pricing

For bonds that the PMCCF purchases as sole investor, pricing will be issuer-specific, informed by market conditions, plus a 100 bps facility fee. For eligible syndicated loans and bonds purchased at issuance, the PMCCF will receive the same price as other syndicate members, plus a 100 bps facility fee paid by the borrower on the PMCCF's share of the issuance. For example, in a syndicated bond issuance of $1 billion in which the PMCCF purchases 25 percent ($250 million), the issuer must pay a facility fee of $2.5 million at closing.

Facility Fees

A facility fee will be applied to each issuance to, or borrowing from, the PMCCF.

Investment Managers Supporting the PMCCF and SMCCF

The following investment manager is acting, on an initial basis, at the sole direction of the NY Fed on behalf of the PMCCF and SMCCF: **Block Rock Financial Markets Advisory**.

Termination Date of the Two Program Facilities

The SPVs will operate through September 30, 2020, unless extended by the Federal Reserve Board and the Treasury. Thereafter, the NY Fed will continue to fund the two program facilities until their holdings either mature or are sold.

Publicity of the Program Facilities

Information about the lending under the PMCCF and SMCCF will be publicly disclosed by the NY Fed during the operation of the facilities. It is anticipated that the NY Fed will launch both of these programs in the near future. If you think that your company meets the eligibility requirements and this type of financing and you are interested in receiving further information about program details and the launch date, you can sign up to receive email alerts directly from the Federal Reserve here for the PMCCF and here for the SMCCF.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

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