

# Passenger Airlines and US Treasury Department Reach Agreement on CARES Act Payroll Support Program

April 17, 2020

## KEY POINTS

The US Treasury Department and several US passenger airlines have agreed on basic terms of payroll support to be provided under the CARES Act. This advisory will:

- Summarize the general terms for passenger airlines receiving more than \$100 million in aid under the Payroll Support Program.
- Outline the details of the Treasury Department's agreement with many of these larger carriers.
- Preview the remaining actions to be taken under the CARES Act Payroll Support Program.

On April 14, the US Treasury Department announced that it reached an agreement in principle with 10 US passenger airlines<sup>1</sup> on the basic terms of their participation in the Payroll Support Program under Title IV, Subtitle B of the CARES Act.<sup>2</sup> Reports indicate that other airlines that applied for relief, such as ExpressJet Airlines, Mesa Airlines, Republic Airways and Spirit Airlines, have not yet reached an agreement. The sum of aid to each passenger airline will equal approximately 76 percent of the amount of the salaries, wages and benefits paid by an airline to its full-time, part-time, temporary and leased employees during 2Q and 3Q of 2019. As part of the agreement in principle, a direct grant will account for 70 percent of an airline's total support payment, and the remaining 30 percent will be made in the form of a loan.<sup>3</sup> Loans will be issued on a senior unsecured basis payable over a 10-year term. The loans will accrue interest at a rate of 1 percent above LIBOR for the first five years and 2 percent above LIBOR for the next five years.<sup>4</sup> Loans may be prepaid at any time prior to maturity at par value.<sup>5</sup>

<sup>1</sup> The group is comprised of Alaska Airlines, Allegiant Air, American Airlines, Delta Air Lines, Frontier Airlines, Hawaiian Airlines, JetBlue Airways, SkyWest Airlines, Southwest Airlines, and United Airlines.

<sup>2</sup> Coronavirus Aid, Relief and Economic Security Act (Public Law 116-136).

<sup>3</sup> The loans made under the Payroll Support Program are made separately from the \$29 billion in loans and loan guarantees to be made under Title IV, Subtitle A of the CARES Act.

<sup>4</sup> Daren Fonda, *Airlines Are Finally Getting a Government Bailout. Here's Why Their Stocks Are Falling*, Barron's, Apr. 15, 2020, <https://www.barrons.com/articles/airlines-stocks-government-bailout-grants-loans-cares-act-covid-19-passenger-traffic-51586967006>.

<sup>5</sup> See, e.g., American Airlines Group Inc., Current Report (Form 8-K), at 2-3 (April 14, 2020); Press Release, Southwest Airlines Co., Southwest Airlines Reaches Agreement In Principle On The Payroll Support Program Under The CARES Act (April 14, 2020) (available at: <https://www.swamedia.com/releases/release-1cddf1aa880580a9784fc127733b92cf-southwest-airlines-reaches-agreement-in-principle-on-the-payroll-support-program-under-the-cares-act>).

Much to the dismay of many industry representatives and congressional leaders, many of the larger passenger air carriers must issue to the federal government stock warrants (or other equity instruments) to compensate the US taxpayer and smaller airlines may not be so required.<sup>6</sup> The amount of compensation is valued at 10 percent of the loan portion of the payroll support payments based on closing stock prices on April 9, with the government reportedly receiving ownership stakes in the airlines ranging from 0.5 percent up to 3.3 percent. To the extent the equity instruments provided by an airline are stock warrants, such instruments will expire five years after issuance and will contain anti-dilution provisions. No equity instrument will convey voting rights to the Treasury Department (in accordance with the CARES Act provisions) and the equity interests are to be freely assignable, with registration rights.<sup>7</sup> It has not been determined how the US taxpayer will be compensated for payroll support payments to privately held passenger airlines.

Alaska Airlines, American Airlines, Delta Air Lines, JetBlue Airways, Southwest Airlines and United Airlines have confirmed the details of their basic agreements with the Treasury Department, which are outlined below. To date, none of Allegiant Air, Frontier Airlines, Hawaiian Airlines, SkyWest Airlines or Spirit Airlines have confirmed the details of their agreements.

- Alaska Airlines (together with its affiliate, Horizon Air) will receive \$992 million in total payroll assistance; \$725 million will make up the grant portion and \$267 million will be funded as a loan. The Treasury Department will acquire the right to purchase 847,000 non-voting shares of Alaska Air Group at \$31.61 per share.<sup>8</sup>
- American Airlines (together with affiliates Envoy Air, Piedmont Airlines and PSA Airlines) will receive \$5.8 billion in total payroll support; \$4.1 billion will be paid as a grant and \$1.7 billion will be funded as a loan. The Treasury Department will acquire warrants to purchase approximately 13.7 million shares of common stock of American Airlines Group – the parent company of American Airlines and its aforementioned affiliates – at \$12.51 per share.<sup>9</sup>
- Delta Air Lines will receive \$5.4 billion in total payroll assistance, with a grant of \$3.8 billion and \$1.6 billion making up the loan portion. The Treasury Department will acquire warrants to acquire approximately 1 percent of the company at a price of \$24.39 per share.<sup>10</sup>
- JetBlue Airways will receive \$935.8 million in the aggregate, with \$685.1 million being paid as a grant and \$250.7 million being made as a loan. Analysts estimate that the Treasury Department will acquire warrants to purchase roughly 2.6 million shares of common stock of JetBlue Airways at \$9.50 per share.<sup>11</sup>
- Southwest Airlines will receive \$3.2 billion in total aid, with \$2.3 billion coming as a grant and nearly \$1 billion through a loan. The Treasury Department will acquire warrants to purchase 2.6 million shares in the airline at \$36.47 per share.<sup>12</sup>

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<sup>6</sup> The Treasury Department announced on April 10, 2020 that it would not require passenger airlines receiving up to \$100 million in payroll assistance to issue equity instruments as compensation. See Press Release, U.S. Treasury Department, Treasury Announces Payroll Support to Aid Employees of Small Passenger Air Carriers (April 10, 2020) (available at: <https://home.treasury.gov/news/press-releases/sm973>).

<sup>7</sup> See, e.g., American Airlines Group Inc., Current Report (Form 8-K), at 2-3 (April 14, 2020).

<sup>8</sup> Notably, Alaska Airlines confirmed that it (together with affiliate Horizon) intends to apply for a \$1.128 billion loan from the Treasury Department under Title IV, Subtitle A of the CARES Act. See Alaska Air Group, Inc., Current Report (Form 8-K), at 2 (April 15, 2020); Press Release, Alaska Airlines, Alaska Airlines and Horizon Air announce details of aid expected under the CARES Act (April 14, 2020) (available at: <https://newsroom.alaskaair.com/2020-04-14-Alaska-Airlines-and-Horizon-Air-announce-details-of-aid-expected-under-the-CARES-Act>). It is expected that the Treasury Department will acquire the right to purchase nearly 3.57 million shares in Alaska Air Group under the same terms as the warrants issued under the Payroll Support Program.

<sup>9</sup> According to its latest 8-K filing with the SEC, American Airlines has said that it will apply for a loan from the Treasury Department under Title IV, Subtitle A of the CARES Act. See American Airlines Group Inc., Current Report (Form 8-K), at 2-3 (April 14, 2020). The principal amount of such loan will be approximately \$4.75 billion, made on a senior secured basis with collateral to be determined. In connection with the borrowing, the Treasury Department would acquire additional warrants to purchase around 38 million shares of common stock in American Airlines Group under the same terms as the warrants issued under the Payroll Support Program.

<sup>10</sup> See Delta Air Lines, Inc., Current Report (Form 8-K), at 2 and Exhibit 99.1 (April 15, 2020).

<sup>11</sup> See Press Release, JetBlue Airways Corporation, JetBlue Provides Update Related to the Coronavirus Aid, Relief and Economic Security (CARES) Act (April 14, 2020) (available at: <https://www.businesswire.com/news/home/20200414006053/en/>).

<sup>12</sup> See Press Release, Southwest Airlines Co., Southwest Airlines Reaches Agreement In Principle On The Payroll Support Program Under The CARES Act (April 14, 2020) (available at: <https://www.swamedia.com/releases/release-1cddf1aa880580a9784fc127733b92cf-southwest-airlines-reaches-agreement-in-principle-on-the-payroll-support-program-under-the-cares-act>).

- United Airlines will receive a total of \$5 billion in total aid. Roughly \$3.5 billion will be a direct grant and \$1.5 billion will be made as a loan. The Treasury Department will acquire a warrant to purchase approximately 4.6 million shares of common stock of the airline's parent company – United Airlines Holdings – at \$31.50 per share.<sup>13</sup>

In accordance with the CARES Act, all aid recipients must use the payroll support payments exclusively to cover the cost of payroll and benefits. Each passenger airline must comply with the required terms and conditions of the CARES Act, such as (1) refraining from imposing involuntary furloughs on US-based employees or reducing employee pay or benefits through September 30; (2) maintaining certain limitations on executive compensation through March 24, 2022; (3) suspending the payment of dividends or other distributions and cease stock buybacks through September 30, 2021; and (4) continuation of service as is reasonable and practicable under Department of Transportation regulations.

With airlines experiencing year-to-year declines in passenger traffic around 95 percent, the completion of this “term sheet” phase of the Payroll Support Program is a significant development in delivering the much needed aid promised by the CARES Act. The immediate next steps will be the execution of definitive agreements between these air carriers and the Treasury Department and processing the hundreds of requests for smaller amounts payroll support.<sup>14</sup>

However, the Payroll Support Program will still require urgent attention. After addressing the needs of passenger air carriers, the Treasury Department must then determine how to allocate the \$4 billion in payroll support for cargo air carriers and \$3 billion in payroll support for certain contractors of passenger airlines. The Treasury Department will soon provide further guidance regarding those cargo air carriers and passenger airline contractors.

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<sup>13</sup> See Press Release, United Airlines, Inc., United Airlines Expects to Receive \$5.0 Billion Through Payroll Support Program Under CARES Act (April 15, 2020) (available at: <https://hub.united.com/2020-04-15-united-airlines-expects-to-receive-5-0-billion-through-payroll-support-program-under-cares-act-2645727457.html>).

<sup>14</sup> In its April 10, 2020 press release, the Treasury Department said that it will process these requests promptly upon approval of the applications.

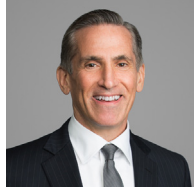
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## CONTACTS

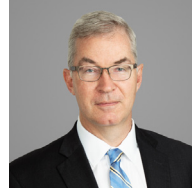
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