Cash Flow Considerations in the Time of COVID-19

LAZEAR CAPITAL PARTNERS
AGENDA

1. Lazear Capital Overview
   Cash is King

2. Short-term Solvency
   Source of Capital

3. Existing Bank
   Sources of Capital

4. SBA Loan Programs
   Sources of Capital

5. Support Investors
   Sources of Capital

6. Tax breaks & Incentives
About Us

**MICHAEL MOROSKY | PARTNER**
**LAZEAR CAPITAL PARTNERS**

Mike Morosky is a Partner with Lazear Capital Securities and has been with the firm since 2003. He leads the training, development and management of the firm’s Directors as they execute their client duties and works with the technical committee of the firm to develop and implement novel ideas and expertise that can be used for the benefits of the firm’s clients. Mike has led numerous ESOP transactions, Sell-Side M&A engagements and workout situations. He has served as CEO or Chief Restructuring Officer for numerous distressed companies in order to help them understand their options and then guide them to their best outcome. Mike previously worked at PricewaterhouseCoopers in the Corporate Finance Group specializing in distressed client situations. He is a graduate of the University of Pennsylvania concentrating on Economics, Accounting, and Religious Studies.

**NED GERHOLD | DIRECTOR**
**LAZEAR CAPITAL PARTNERS**

Ned is a Director at Lazear Capital Partners, charged with responsibilities related to ESOP formations, Mergers & Acquisitions, and Capital Solutions. He has spent his career working in industries ranging from retail, wholesale, transportation, and e-commerce; and worked in operations, purchasing, merchandise management, budget & planning and finance in companies ranging in size from three-person start-ups to more than 50k multi-nationals.

Prior to joining Lazear Capital, he served as Director of Finance and Planning for a large international retailer. He graduated with a BA from Capital University and an MBA from Thunderbird, The American Graduate School of International Management with a focus in both International Finance and Japanese.
Creating Value through Strategic Thinking

ESOP Advisory - Management Buyouts

Sell Side Engagements - Capital Raising - Recapitalizations

Turnaround Advisory - Merchant Banking

**OUR EXPERIENCE**
Founded in 1999 and headquartered in Columbus, OH

**OUR FOCUS**
Mid-market companies with sales ranging from $50M - $500M

**OUR ORGANIZATION**
Diverse range of experts on staff (Attorneys, CPAs, CEOs, CFA, ABV, Commercial Bankers, & MBAs)
**Successful Transactions**

<table>
<thead>
<tr>
<th>Company</th>
<th>ESOP Type</th>
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<tbody>
<tr>
<td>Arborwell</td>
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<tr>
<td>Bandit Industries, Inc.</td>
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<tr>
<td>Romanoff Group</td>
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<td>Lwi Woburn</td>
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<tr>
<td>CHAPEL</td>
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<td>BEACON Electrical Contractors</td>
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<td>Capital City Electric</td>
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<td>KBR</td>
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<td>ASI</td>
<td>100%</td>
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<tr>
<td>SL Salons</td>
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<tr>
<td>Decker Construction Co.</td>
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<td>Atlas Industrial Contractors</td>
<td>M&amp;A</td>
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<tr>
<td>UTI</td>
<td>100%</td>
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<tr>
<td>Chemcote</td>
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<tr>
<td>Hercules Industries</td>
<td>100%</td>
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<td>BEST</td>
<td>100%</td>
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<td>Lyon Video</td>
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<td>Marshberry</td>
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<td>CCI</td>
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<td>R&amp;B Mechanical</td>
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<td>Flyers Online</td>
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<td>Zink</td>
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<td>Polaris Automation</td>
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<td>FST Logistics</td>
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<tr>
<td>DAK Enterprises</td>
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</table>
Cash is King | Understanding your solvency

Financial solvency is the ability of a business to meet its payment obligations as they come due in the ordinary course.

Sources of Cash
- Existing cash in bank
- Undrawn bank loans
- Collection of receivables
- Sales of inventory/services for cash
- Cash sales of equipment or property
- Shareholder & investor capital

Uses of Cash
- Payroll & Associated Taxes
- Critical vendors
- Non-Critical vendors
- Utilities & Overhead
- Rent
- Payments on bank loans and mortgages
Cash is King | Understanding your solvency

Communicate with Customers
- Timing of future payments
- Ability to make payments
- Discounts for quicker payments

Business Cost Structure
- Variable costs must be adjusted
- Fixed Costs should be restructured

Negotiate with Vendors
- Defer payments whenever possible
- Critical vs. Non-Critical
- Landlords may defer rent
- Banks may defer loan payments for up to 90 days.
- Health insurers may defer insurance by 90 days
### Cash is King | Sample 13-week cash flow summary

<table>
<thead>
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<tbody>
<tr>
<td>Cash on hand (beginning of month)</td>
<td>55</td>
<td>80</td>
<td>430</td>
<td>605</td>
<td>855</td>
<td>70</td>
<td>20</td>
<td>-</td>
<td>50</td>
<td>70</td>
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<tr>
<td><strong>CASH RECEIPTS</strong></td>
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<tr>
<td>Cash sales</td>
<td>100</td>
<td>200</td>
<td>150</td>
<td>100</td>
<td>200</td>
<td>150</td>
<td>100</td>
<td>200</td>
<td>150</td>
<td>100</td>
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<td>Collections of accounts receivable</td>
<td>1,100</td>
<td>900</td>
<td>850</td>
<td>700</td>
<td>100</td>
<td>450</td>
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<td>500</td>
<td>1,200</td>
<td>500</td>
<td>800</td>
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<td>Bank draws</td>
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<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>130</td>
<td>-</td>
<td>-</td>
<td>180</td>
<td>-</td>
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<tr>
<td><strong>TOTAL CASH RECEIPTS</strong></td>
<td>1,200</td>
<td>1,100</td>
<td>1,000</td>
<td>800</td>
<td>300</td>
<td>600</td>
<td>630</td>
<td>700</td>
<td>1,350</td>
<td>780</td>
<td>1,000</td>
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<tr>
<td><strong>Total cash available</strong></td>
<td>1,255</td>
<td>1,180</td>
<td>1,430</td>
<td>1,405</td>
<td>1,155</td>
<td>670</td>
<td>650</td>
<td>700</td>
<td>1,400</td>
<td>850</td>
<td>1,000</td>
<td>1,500</td>
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<tr>
<td><strong>CASH PAID OUT</strong></td>
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<td>Insurance (other than health)</td>
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<td>200</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>200</td>
<td>-</td>
<td>-</td>
<td>200</td>
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<td>Interest expense</td>
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<td>60</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>55</td>
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<td>Materials and supplies vendors</td>
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<td>500</td>
<td>500</td>
<td>400</td>
<td>400</td>
<td>400</td>
<td>600</td>
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<td>Rent</td>
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<td>-</td>
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<td>-</td>
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<td>Utilities</td>
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<td>75</td>
<td>-</td>
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<td>75</td>
<td>-</td>
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<tr>
<td>Wages (less emp. credits)</td>
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<td>200</td>
<td>-</td>
<td>200</td>
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<tr>
<td>Miscellaneous</td>
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<td>50</td>
<td>50</td>
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<td>550</td>
<td>885</td>
<td>650</td>
<td>650</td>
<td>650</td>
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<td>875</td>
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<td>-</td>
<td>200</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
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<tr>
<td>Capital purchases</td>
<td>-</td>
<td>-</td>
<td>75</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>50</td>
<td>-</td>
<td>-</td>
<td>-</td>
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</tr>
<tr>
<td><strong>TOTAL CASH PAID OUT</strong></td>
<td>1,175</td>
<td>750</td>
<td>825</td>
<td>550</td>
<td>1,085</td>
<td>650</td>
<td>650</td>
<td>650</td>
<td>1,330</td>
<td>850</td>
<td>650</td>
<td>-</td>
</tr>
<tr>
<td>Cash on hand (end of month)</td>
<td>80</td>
<td>430</td>
<td>605</td>
<td>855</td>
<td>70</td>
<td>20</td>
<td>-</td>
<td>50</td>
<td>70</td>
<td>-</td>
<td>350</td>
<td>1,500</td>
</tr>
</tbody>
</table>

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**If cash flow is going to be insufficient:**

- Restructuring existing or obtaining new bank loans (addressed later)
- SBA Disaster and Payroll Protection Loans (addressed later)
- Third party equity or sub debt loans (addressed later)
Source of Capital | Existing Bank

Assess your current banking structure

• Which bank does the company use? Who is the loan officer? How are they handling this situation? Is there a bank that is a better fit?
• Understand each type of loan and the related collateral & security interest?
• What is the company’s current line of credit availability?
• Are there un-encumbered assets that could serve as collateral for a new loan?
• Does the company have any recent appraisals of its assets?
• Are there any personal guarantees in place? What is the collectability of the personal guarantors?

Status of relationship

• Payment default vs. Covenant defaults
• Has the loan been placed into the bank’s “workout” group?

Restructuring vs Refinancing

• Restructuring existing loans to make payment terms line up with anticipated cash flow.
• If necessary, Company may need to exit to a new lender. The new lender may often be more expensive or have more onerous terms.
• Financial advisors assist with restructuring or refinancing of existing loans.

Rule #1
Be transparent with your bank!
Source of Capital | Small Business Administration

Government assistance to businesses during the COVID-19 outbreak

The federal government is instituting lending programs to help businesses impacted by the current economic impacts.

Payroll Protection Program (PPP)
• Currently provides business <500 employees to access $350B of funds from the SBA
• Funds are designed to incentivize companies to retain as many employees on payroll as possible
• Loans are designed to be partially or completely forgiven if the company meets certain payroll requirements
• Congress is seeking an additional $250B of funds for the program

Emergency Economic Injury Disaster Loans (E-EIDL)
• Currently provides business <500 employees with emergency access $50 billion of funds from the SBA for short term cash flow needs
• Can quickly provide $10K of finds, and total loans per business are limited to $2M. Loans are not forgivable
• Money is dispensed by the SBA and current reports suggest the borrowers are having difficulty accessing funds

Main Street Lending Program (MSLP)
• This program is still in development- designed for companies with 500-10k employees, it may soon also be available to smaller businesses
• Borrowers will have to certify specific economic needs to qualify for loans (principal and interest to be deferred for one-year)
• Companies seeking MSLP loans will have to make reasonable efforts to maintain payroll and retain employees
• Borrowing will likely come with further restrictions on compensation, stock repurchase, dividend, offshoring, and collective bargaining matters

Anticipated Future Programs (Phase 4)
• Anticipated by end of April or mid-May, the next phase has yet to be determined - but options being presented consist of:
  o A $1-2T infrastructure program; or
  o A $1T extension of the current Phase 3. (SBA lending and direct payments to citizens)
When companies have maximized their senior debt borrowing capacity need additional capital to pursue growth opportunities (acquisitions, large capital programs, etc.), for shareholder activity (distributions, shareholder buyout, etc.), or in times of market dislocation - to fund general corporate purposes, they are typically left with two options: raise Equity or Mezzanine

Junior Debt or “Mezzanine” financing is a class of capital that sits between (less risky) senior debt and (higher risk) equity that has both debt and equity features

- Mezzanine can be viewed as either expensive (higher coupon) debt or cheap (less dilutive) equity
- It will carry higher interest rate than the senior debt that companies would obtain through their banks (reflecting greater risk than senior debt), but is substantially less expensive than equity in terms of overall cost of capital
Why your Senior lender likes Mezzanine Debt

- The bank is no longer injecting new funds into the business
- Mezzanine is usually unsecured and subordinated to a company’s senior debt.
- In the event a company is facing liquidity constraints, the senior lender can pause (or “block”) current interest payments on mezzanine debt

“Business Development Companies” have filled the void left by the retreat of commercial

- In 1990, there were more than 12,000 commercial banks in the US, while today there are fewer than 5,000
- While banks remain a significant player in corporate lending, middle market credit has been rationalized in favor of larger and more liquid syndicated loans

Traditional closely-held businesses (including Founder and ESOP owned entities) comprise nearly 90% of what is traditionally defined as the “middle market”. Accessing these borrowers is more challenging for private debt lenders given lack of relationships and the bespoke nature of each credit

Significant Growth in BDC Market

Source: Capital IQ
Source of Capital | Taxes

**Employer Retention Credit** | Enacted by The Coronavirus Aid, Relief, and Economic Security Act ("CARES")
Effective March 13, 2020 – December 31, 2020

- Eligible employers receive fifty percent credit for qualified wages up to $10,000 per eligible employee retained (i.e. $5,000 credit).
- Credit is applied against Social Security taxes
- Excess retention credit can be provided as an advanced refund or applied against other employment taxes
- **NOTE:** Employer is not eligible for retention credit if debt is forgiven under a Payroll Protection program loan of the CARES Act

### Eligible Employer Qualifications:

1) Operations Suspended (full or partial) as result of government order, or
2) Over 50% reduction in quarterly receipts measured year over year
   - Employer remains eligible until gross receipts are 80% or more of preceding year comparable quarter

### Qualified Wages

- **100 or Fewer Employees**
  - Qualified Wages = Up to $10,000 for each Employee
- **More than 100 Employees**
  - Qualified Wages = Up to $10,000 for each Employee unable to provide services due to COVID-19
Sick Leave Credit and Payroll Tax Deferral

Emergency Sick Leave and Emergency Paid FMLA Credit: Enacted by The Families First Coronavirus Response Act ("FFCRA")
Effective April 1, 2020 through December 31, 2020

• The FFCRA requires each private employer with fewer than 500 employees to provide special paid emergency family and medical leave and paid sick leave due to certain COVID-19-related circumstances to all full-time and part-time employees who have been employed with a covered employer for 30 calendar days or more

• There is a refundable Social Security tax credit for covered employers equal to the qualified wages paid for family medical leave or qualified sick leave under FFCRA. The credits and refunds for applicable family leave and sick leave can be advanced to covered employers.

Emergency Paid Sick Leave
- Employees eligible April 1st
- Up to 80 Hours (Basically, first 10 days)
- Six Triggers on required pay and credit
- Full or 2/3rd pay depending on Trigger
  - Full pay capped at $511 daily and $5,110 in aggregate, or
  - 2/3rd pay capped at $200 and $2,000 in aggregate

Emergency Paid FMLA
- Employees eligible April 1st
- Employees eligible with 30 calendar days on payroll
- Up to 12 weeks
  - First two weeks may be unpaid
  - One Trigger
  - 2/3rd pay capped at $200 and $10,000 in aggregate
Net Operating Loss
- The CARES Act grants taxpayers a five-year carryback period and indefinite carryforward period for Net Operating Losses ("NOL") arising in tax years beginning after December 31, 2017 and before January 1, 2021
  - This can create rate benefits for carrybacks to 2013 – 2017 tax years due to tax rate arbitrage (35% vs 21% corporate income tax rate)
- Capital loss carryover periods have not changed with the enactment of the CARES Act (three-year carryback and five-year carry forward periods)

Interest Expense Disallowance
- Adjusted Tax Income ("ATI") limit is increased from 30% to 50% for tax years beginning in 2019 and 2020
- A company can elect to use ATI from last tax year beginning in 2019 for their ATI in the 2020 tax year (likely allowing a higher deduction for companies with reduced 2020 earnings)

Delays in General Tax Filings and Payments
- The filing date of specific federal income tax returns and the due date of specific federal income tax payments due on April 15, 2020 has been postponed until July 15, 2020
  - There is no limit on the amount of income tax payments that can be deferred until July 15, 2020 (this includes amounts owed on April 15th for the 2019 tax return, or 2020 estimates)

Delay Employer Payroll Taxes
- CARES Act allows employers and self-employed individuals to defer payment of the employer share (6.2%) of the Social Security tax they otherwise are responsible for paying in 2020, effective for payments due after the date of enactment.
  - Deferral period begins March 27, 2020 and ends before January 1, 2021
  - Fifty percent (50%) of the deferred payroll taxes are due on December 31, 2021, and the remaining amounts are due on December 31, 2022.
  - NOTE: Payroll deferral program is not available if debt is forgiven under a Payroll Protection program loan
Lazear Capital Partners has multi-disciplinary capabilities and dedicates a full team of senior professionals with industry expertise to its engagements to offer objective, unbiased advice regarding the range of strategic and capital structure alternatives that may be available.

For more information about our services and firm, please contact:

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