FEDERAL RESERVE MODIFIES MAIN STREET LENDING PROGRAM TO ATTRACT MORE BUSINESSES

Alert | 06.16.2020
By Charles Kabugo-Musoke, Bart Norman and Peter Bosman

On June 8, 2020, the Board of Governors of the Federal Reserve System (Federal Reserve) issued a **Press Release** (the FRB Press Release) announcing an expansion of its Main Street Lending Program (Program) to help more small- and medium-sized businesses that are not eligible for emergency loans due to negative economic impacts of the COVID-19 pandemic under the Paycheck Protection Program (PPP) established by the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), or that require additional financial assistance. This Alert provides an overview of the Program as revised by the FRB Press Release and the accompanying documentation.

Background

The expanded Program will make up to $600 billion of loans available to small- and medium-sized U.S. businesses. Loans under the Program will still be made by U.S. banks and other U.S. financial institutions. Eligible lenders will make loans under the Program through three facilities: the Main Street New Loan Facility (MSNLF), the Main Street Priority Loan Facility (MSPLF), and the Main Street Expanded Loan Facility (MSELF). The MSNLF and the MSPLF will cover new loans, while the MSELF will cover expansions to existing loans. The Program does not include a forgiveness or grant component similar to other federal loan programs included in the Coronavirus Aid, Relief, and Economic Security Act (CARES Act).

Under the Program, the Federal Reserve will lend funds to a special purpose vehicle (Main Street SPV) established by the Federal Reserve Bank of Boston. An eligible lender may extend a new or upsized loan to an eligible borrower and sell a 95% participation in such new or upsized loan to the Main Street SPV at par value. The eligible lender must retain 5% of the new or upsized loan until (i) it matures or (ii) the Main Street SPV (or a governmental assignee thereof) sells all of its 95% participation, whichever comes first.

Eligible Borrowers

The Program is available to businesses established prior to March 13, 2020, with 15,000 employees or fewer or that had 2019 revenues of $5 billion or less. The businesses must be organized in the United States and have material operations and a majority of employees based in the United States, and they may not be "Ineligible Businesses[1]" as defined under the Small Business Administration's regulations (as modified by regulations implementing the PPP). Program lenders are expected to conduct an assessment of each potential borrower's financial condition at the application stage. Borrowers are not disqualified from the Program by virtue of having received previously received PPP loans.

Loan Terms

MSNLF

Loans under the MSNLF will be term loans made after April 24, 2020, and they may be secured or unsecured. MSNLF loans will carry a five-year maturity, subject to deferral of principal payments for two years, and deferral of interest payments for one year (unpaid interest will be capitalized). Interest will be variable, based on adjustable rate of LIBOR (1 or 3 month) + 300 basis points. The minimum MSNLF loan size will be $250,000, and the maximum will be the lesser of (i) $35 million or (ii) the amount that would result in the borrower having outstanding debt, including the undrawn portion of any committed lines, of not more than four times its 2019 adjusted EBITDA. The borrower will pay its lender a fee of up to 100 basis points on the principal of the loan, and the Main Street SPV will pay the lender an additional annual servicing fee of 25 basis points. However, the lender will be required to pay to the Main Street SPV a facility fee of 100 basis points on the principal of the MSNLF loan at the time of origination, which may be passed on to the borrower.

MSNLF loans may not be contractually subordinated to any of borrowers' other debt, but borrowers are not prohibited from incurring secured debt, regardless of whether their MSNLF loans are secured or unsecured.

A full version of the Federal Reserve's term sheet for MSNLF can be found **here**.

MSPLF

Loans under the MSPLF will offer terms that largely mirror the MSNLF loan terms, except the maximum MSPLF loan size will be the lesser of (i) $50 million or (ii) the amount that would result in the borrower having outstanding debt, including the undrawn portion of any committed lines, of not more than six times its 2019 adjusted EBITDA.

MSPLF loans must remain senior to or *pari passu* with the borrower's other loans or debt instruments, other than mortgage debt. Accordingly, a MSPLF loan must be secured if, at the time of origination, the borrower has any other secured loans or debt instruments (other than mortgage debt), and must meet a minimum collateral coverage ratio. So long as the minimum collateral coverage ratio is maintained, other debt may be secured by collateral on which the MSPLF lender does not hold a lien. A MSPLF loan may be unsecured only if the borrower does not have any secured debt (other than mortgage debt), and an unsecured MSPLF loan must not be contractually subordinated in terms of priority to any of the borrower's other loans or debt instruments.

A full version of the Federal Reserve's term sheet for MSPLF can be found **here**.

MSELF

The Program also provides for borrowers and lenders to agree to upsize an existing term loan or add a term loan to an existing revolving credit facility, so long as the existing term loan or revolving credit facility was made on or before April 24, 2020 and has a remaining maturity of at least 18 months (taking into account any amendments to the maturity after April 24, 2020, including at the time of upsizing). The upsized tranches will have the same terms as described above with respect to the MSPLF, except that the minimum MSELF loan size will be $10 million and the maximum will be the lesser of (i) $300 million or (ii) the amount that would result in the borrower having outstanding debt, including the undrawn portion of any committed lines, of not more than six times EBITDA (based on adjusted 2019 results). In addition, the borrower will pay its lender a fee of 75 basis points on the principal of the upsized tranche of the MSELF loan, the Main Street SPV will pay the lender an additional 25 basis points as a servicing fee. The lender will be required to pay to the Main Street SPV a facility fee of 75 basis points on the principal of the upsized tranche of the MSELF loan, which may be passed on to the borrower.

MSPLF loans must remain senior to or *pari passu*, in terms of priority and security, with the borrower's other loans or debt instruments, other than mortgage debt. If the existing loan were secured by collateral prior to being upsized, that same collateral must secure the upsized tranche on a *pari passu* basis. However, if the underlying credit facility includes both term loan and revolving credit facilities, the upsized tranche of the MSELF loan need only share collateral on a *pari passu* basis with the term loan facility. Otherwise, MSELF loans are subject largely to the same priority and security requirements as loans under the MSPLF.

A full version of the Federal Reserve's term sheet for MSELF loans can be found **here**.

Certifications and Requirements

Each borrower will be expected to make commercially reasonable efforts to maintain its payroll and retain its employees during the time the loan (or upsized tranche of the loan) is outstanding. Furthermore, each borrower under the Program will be required to make certain certifications, including that it will:

- refrain from repaying the principal balance of, or paying any interest on, any debt until the loan (or upsized tranche of the loan) is repaid in full, unless the debt or interest payment is mandatory and due (although, for MSPLF loans, the borrower may, at the time of origination of the loan, refinance existing debt owed by the borrower to other lenders);
- refrain seeking to cancel or reduce any of its outstanding committed lines of credit;
- certify that it has a reasonable basis to believe that, as of the date of origination (or upsizing) of the loan and after giving effect to such loan (or upsizing), it has the ability to meet its financial obligations for at least the next 90 days and does not expect to file for bankruptcy during that time period; and
- Agree to follow compensation, stock repurchase, and capital distribution restrictions that apply to direct loan programs under the CARES Act, except that an S corporation or other tax pass-through entity may make distributions to the extent reasonably required to cover its owners' tax obligations in respect of the entity's earnings. We expect additional guidance from the Federal Reserve on these points, but generally they apply to employee compensation above $425,000 and prohibit dividends and other capital distributions and stock repurchases by publicly traded companies until 12 months after the loans under the Program have been repaid.

Each lender under the Program is separately required to certify that it will:

- avoid requesting that the borrower repay debt extended by such lender, or pay interest on such outstanding obligations, until the Program loan is repaid in full, unless the debt or interest payment is mandatory and due or in the case of default and acceleration;
- avoid canceling or reducing any existing committed lines of credit available to borrower, except in an event of default; and
- certify that the methodology used for calculating the borrower's adjusted 2019 EBITDA for the Program's leverage requirement is the methodology it has previously used for adjusting EBITDA when extending (or originating or amending) credit to the borrower (or similarly situated borrowers) on or before April 24, 2020.

Finally, lenders and borrowers are both required to certify that they are eligible to participate in the Program, including in light of the conflicts of interest prohibition in section 4019(b) of the CARES Act.

Additional Documentation and Resources

The FRB Press Release included, among other things, **Frequently Asked Questions (FAQs)** providing more information regarding eligibility and conditions and information regarding the form lender registration documents, loan participation and servicing agreements, and borrower and lender certifications and covenants, as well as other required form agreements, which can be found on the **Federal Reserve Bank of Boston's Main Street Lending Program Forms and Agreements website**. Although the Federal Reserve will not provide form loan documents for the Program loans, the Federal Reserve has clarified that such loan documents must reflect the terms of the Program and must include the items set out in the loan document checklist contained in **Appendix A of the Main Street FAQs (PDF)**.

As the economic and regulatory climate resulting from COVID-19 evolves, Smith Anderson will continue to provide updates as the Federal Reserve, the U.S. Treasury Department and other governmental entities issue additional guidance. If you have any questions related to this alert, please do not hesitate to contact your regular Smith Anderson lawyer or any other member of our firm. Additionally, please visit and bookmark our firm's **Coronavirus (COVID-19) Business Resource Center**, which is updated continuously with useful materials and resources related to COVID-19. This tool has been made available to ensure that our clients and the broader business community stay informed on key issues that may impact their operations and to navigate the related business and legal issues during these challenging times.

---

[1] "Ineligible Businesses" include certain financial companies, passive investment entities, lobbying entities, gambling concerns, insurance companies, among several others described at 13 C.F.R. Part 120.110 (note that the linked text excludes non-profit businesses, which are generally ineligible for SBA purposes, but are included as eligible businesses through the PPP).

PROFESSIONALS

Peter E. Bosman

Charles R. Kabugo-Musoke

Bart A. Norman

PRACTICE AREAS

Banking & Finance

Corporate & Transactional