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Treasury and Federal Reserve Board Announce Details of $600 Billion Main Street Lending Program

April 9, 2020

As has been widely anticipated, the Treasury and the Federal Reserve Board released the details of their previously announced Main Street Lending Program to promote liquidity in the lending market for small to medium sized businesses. The Treasury will use $75 billion of the $454 billion in funds allocated by Congress under section 4000(b)(4) of the Coronavirus Economic Stabilization Act of 2020 (CESA) – a sub-part of the broader $2 trillion relief package contemplated by the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) – and will leverage the Federal Reserve's emergency lending powers under Section 13(3) of the Federal Reserve Act to allow US banks, depository institutions and savings and loan companies to make available up to $600 billion for the purchase of loans issued by lenders to small and medium sized businesses. While it is expected that the Treasury and Federal Reserve Board, as well as participating banks, will provide additional guidance in the coming weeks, this alert analyzes and summarizes the term sheets published by the Federal Reserve Board on April 9, 2020, and examine the practical implications on potential borrowers seeking to participate in this program.

The Federal Reserve's Main Street Lending Program

The Main Street Lending Program consists of a combination of two separate facilities:

- **Main Street New Loan Facility**. Provides for the purchase by the Federal Reserve from eligible lenders of new unsecured term loans made to eligible borrowers originated on or after April 8, 2020.
- **Main Street Expanded Loan Facility**. Provides for the purchase by the Federal Reserve from eligible lenders of upsized tranches of existing loans originated before April 8, 2020. These will be secured solely to the extent the existing loans are secured and, in such instances, upsized loans will be secured on a pari passu basis.

In order to implement this program, the Federal Reserve will lend funds on a recourse basis to a single special purchase vehicle (SPV) that will be capitalized by $75 billion of equity capital from the Treasury. The SPV will use the proceeds of the Treasury equity capital and loans made from the Federal Reserve to purchase up to $600 billion of eligible loans. The loans made by the Federal Reserve to the SPV will be secured by the portfolio of present and future eligible loans held by the SPV. Notably however, and in contrast to the Federal Reserve's liquidity program for the purchase of loans under the Paycheck Protection Program (PPP), the Federal Reserve will only purchase 95% of the aggregate principal amount of loans made by eligible lenders, requiring eligible lenders to retain 5% of the risk of the loan on their own balance sheet.

Eligible borrowers

Eligible borrowers under the program are businesses with up to 10,000 employees or up to $2.5 billion in 2019 annual revenues. Each eligible borrower must be a business that is created or organized in the United States or under the laws of the United States with significant operations in and a majority of its employees based in the United States. There are two key takeaways for businesses based on the latest Federal Reserve and Treasury announcements:

- **Solvency.** The Federal Reserve press release notes that the Main Street Lending Program is available for businesses that were in good financial standing before the crisis, and lenders will be expected to use customary underwriting standard to ensure that these loans are prudently incurred and are not provided to insolvent entities or a debtor in a bankruptcy proceeding.
- **PPP.** The Main Street Loan Program is available to businesses *in addition* to loans received under Paycheck Protection Program for small businesses.
- **Employee size.** All businesses up to 10,000 employees are eligible, including businesses with 500 or fewer employees. Importantly, the Main Street Lending Program may be an option for private equity or venture capital-backed businesses that may have otherwise had difficulty qualifying for the PPP program given the SBA's "affiliation" rules as to employee head count.

Eligible lenders and eligible loans

As discussed above, the Federal Reserve will not be making direct loans to businesses under this program. Similar to the PPP program, businesses will need to seek loans from banks that qualify as eligible lenders under the program, which are US-insured depository institutions, US bank holding companies, and US savings and loan holding companies. At this point in time, notably absent from the list of eligible lenders are non-bank lenders. Commercial lenders will be responsible for underwriting, documenting and funding loans under the Main Street Lending Program, and prospective borrowers may seek to leverage existing banking, lending and financing relationships to seek such loans. The participating lenders must retain 5% of the eligible loans and are subject to Federal Reserve oversight to ensure prudent lending practices.

Eligible loans under the program must meet the following criteria:		
	Main Street New Loan Facility	**Main Street Expanded Loan Facility (solely with respect to the upsized tranche)**
Origination	Originated on or after April 8, 2020	Originated before April 8, 2020
Security	Unsecured	If original loan is secured, extension is secured on a pari passu basis with original loan. If original loan is unsecured, extension is unsecured.
Maturity	4 years	4 years
Amortization	Amortization of principal and interest deferred for one year	Amortization of principal and interest deferred for one year

Eligible loans under the program must meet the following criteria:		
	Main Street New Loan Facility	**Main Street Expanded Loan Facility (solely with respect to the upsized tranche)**
Interest rate	Adjustable rate of SOFR + 250–400 basis points	Adjustable rate of SOFR + 250–400 basis points
Minimum loan size	$1 million	$1 million
Maximum loan size	The lesser of (i) $25 million or (ii) an amount that, when added to the eligible borrower's existing outstanding and committed, but undrawn debt, does not exceed *four times* the eligible borrower's 2019 EBITDA	The least of (i) $150 million, (ii) 30% of the eligible borrower's existing outstanding and committed, but undrawn bank debt, or (iii) an amount that, when added to the eligible borrower's existing outstanding and committed, but undrawn debt, does not exceed *six times* the eligible borrower's 2019 EBITDA
Prepayment	Prepayment permitted without penalty	Prepayment permitted without penalty

Important for borrowers to note is that the leverage eligibility requirements set forth above for eligible loans look at the borrower's 2019 earnings before interest, taxes, depreciation and amortization (EBITDA), prior to any impact of the coronavirus pandemic. The terms described by the Federal Reserve do not address whether a borrower's EBITDA will be determined on a basis consistent with existing credit facilities or whether the borrower would receive the benefit of non-GAAP add-backs to EBITDA in certifying as to the maximum loan amount requirement for eligible loans.

In addition, in order for a loan to be deemed an eligible loan under either of the Main Street Lending Facilities, the following attestations will be required in order to syndicate the loan to the applicable Federal Reserve entity:

Attestation by lenders

- Must attest that proceeds of the eligible loan will not be used to repay or refinance pre-existing "loans or lines of credit" made by the lender to the borrower, including with respect to extension loans, the pre-existing portion of the loan.
- Must not cancel or reduce any existing lines of credit available to borrower.

Attestation by borrowers

- Must commit to refrain from using the proceeds of the eligible loans to repay other loan balances.

- Must commit to refrain from repaying other debt of equal or lower priority, with the exception of mandatory principal payments, unless the borrower has first repaid the eligible loan in full.
- Must attest that it will not seek to cancel or reduce any of its outstanding lines of credit.
- Must attest that it requires financing due to the exigent circumstances presented by the coronavirus pandemic, and that, using the proceeds of the loan or upsized tranche of the loan, as applicable, it will make reasonable efforts to maintain its payroll and retain its employees during the term of such loan.
- Must attest that it meets the EBITDA leverage condition described above that is a required feature of eligible loans.
- Must attest that it will follow the executive compensation limitations, stock repurchase restrictions, and capital distribution restrictions that apply to direct loan programs under section 4003(c)(3)(A)(ii) of the CARES Act.

Joint attestation by borrowers and lenders

- Each of the borrower and the lender is required to certify that the borrower is eligible to participate in the facility, including with respect to conflict of interest prohibitions regarding the interests of certain political officials and their respective families in the business as set forth under Section 4016 of the CARES Act.

Fees

- **Loan participation fee:** Solely with respect to a *new loan* made (and not an upsized loan), the lender will be required to pay to the Federal Reserve a 100 basis point fee on the principal amount of the loan purchased via participation (e.g., 95% of the par value of the loan). This fee is permitted to be passed through to the borrower.
- **Loan origination fee:** The borrower shall pay an origination fee of 100 basis points of the principal amount of the new or upsized loans.
- **Loan servicing fee:** The Federal Reserve will pay a per annum fee of 25 basis points of the principal amount of the new or upsized loan that it has purchased via participation as consideration for the lender administering the loan.

Implications for Main Street Lending Program participants

- **Participation in other programs.** Borrowers that have obtained financial assistance under the PPP remain eligible for new loans and loan extensions under the Main Street Lending Program, but issuers of bonds or syndicated loans under the Primary Market Corporate Credit Facility will not be eligible to borrow under the Main Street Lending Program. Participation in the two Main Street programs are mutually exclusive, as extensions of new loans made to borrowers under the Main Street New Loan Facility will not be considered eligible loans under the Main Street Expanded Loan Facility, and new loans will not be available to borrowers under the Main Street New Loan Facility if the borrower's loans were upsized under the Main Street Expanded Loan Facility.
- **Amendments to existing debt.** Borrowers will need to carefully examine existing debt agreements to determine whether any amendments may be needed to permit incurrence of new or upsized loans and implement the required interest payment blockage terms applicable to outstanding loans prior to the repayment in full of the Main Street loans. In particular, prospective borrowers should focus on restrictions on the incurrence of debt and any restriction on negative pledges because borrowers of Main Street loans will be prohibited from repaying debt of equal or lower priority until the Main Street loan is repaid in full. Each pre-existing lender to the borrower would need to agree to such payment subordination, making an amendment to any widely syndicated loan facility to permit the incurrence of new or upsized loans challenging.
- **Upsized loans.** As the ability to incur any new debt under this program will likely require discussion with existing creditors, and lenders will not be required to pay a participation fee to sell upsize loans to the Federal Reserve, there may be a preference for borrowers with existing debt facilities to request upsized loans in the form of incremental loans from their existing lenders. This implied preference for upsize loans may serve to prioritize further lending under existing debt facilities because documentation of incremental loans will likely not require extensive amendments to the borrower's outstanding third-party debt. Furthermore, a

lesson learned from the PPP program is that given the outsized demand from businesses for the Treasury's loan programs, most banks may only provide financing to existing clients given administrative burdens and overwhelming demand from many prospective borrowers.

- **SOFR.** The Federal Reserve has required that both new and upsize loans bear interest at SOFR plus an applicable margin, rather than using the LIBOR reference rate. Particularly in the context of upsize loans in the form of incremental debt, this will prove administratively difficult given that the vast majority of existing variable rate loan facilities look to LIBOR as the reference rate.
- **Additional rulemaking.** The terms of the Main Street Lending Program are subject to further rulemaking and guidance from the Treasury and the Federal Reserve. This alert is a summary based on the term sheets published by the Federal Reserve and the scope of the program will come into focus as applications and standard operating procedures are implemented, similar to the rollout of the PPP.
- **Financial protection.** In contrast to the requirements that borrowers of the loans set aside for air carriers provide financial protection in the form of warrants or senior debt instrument to the Treasury, the Main Street Lending Program does not require issue of any such securities as a condition to funding.

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