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Federal Reserve’s Main Street Lending Program: What Businesses Need to Know to Prepare

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On April 9, 2020, the Federal Reserve, acting under the Coronavirus Aid, Relief, and Economic Security Act (“CARES Act”) and Section 13(3) of the Federal Reserve Act (12 USC §344), announced the creation of a new “Main Street Lending Program.”

The purpose of the Main Street Lending Program is to support lending to small and medium-sized businesses that were in sound financial condition before the onset of the coronavirus (“COVID-19”). The Main Street Lending Program is distinct from the mid-sized business loan program contemplated to be created under Section 4003(c)(3)(D)(i) of the CARES Act, which remains unimplemented.

The Main Street Lending Program will operate 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”). All three facilities use the same eligible lender and eligible borrower criteria, and have many of the same features—including the same maturity, interest rate, deferral of principal and interest for one year, and ability of the borrower to prepay without penalty. The specific features of each type of facility are outlined in the term sheet for each such facility. The combined size of the MSNLF, the MSPLF and the MSELF will be up to $600 billion.

Although the Federal Reserve is currently working to create the infrastructure necessary to operationalize the Main Street Lending Program, term sheets for each facility and Frequently Asked Questions (FAQs) providing more information regarding the program and the facilities are available on the **Federal Reserve’s website.**

The below summary of the Main Street Lending Program and the three facilities is based on the term sheets and FAQs made available on the Federal Reserve’s website on April 30. 2020. The Federal Reserve Board and the Secretary of the Treasury may make adjustments to the program and to the terms of the facilities available under the program. Any changes are to be announced on the Federal Reserve’s website.

General

The **Main Street New Loan Facility** contemplates new loans to eligible borrowers ranging in size from $500,000 to $25 million. The maximum size of a MSNLF loan cannot, when added to the eligible borrower’s existing outstanding and undrawn available debt, exceed **four times** the eligible borrower’s adjusted 2019 earnings before interest, taxes, depreciation and amortization (“EBITDA”). A MSNLF loan may be unsecured or secured. However, a MSNLF loan must not be, at any time, contractually subordinated in terms of priority to any of the eligible borrower’s other loans or debt instruments.

The **Main Street Priority Loan Facility** contemplates new loans to eligible borrowers ranging in size from $500,000 to $25 million. The maximum size of a MSPLF loan cannot, when added to the eligible borrower’s existing outstanding and undrawn available debt, exceed **six times** the eligible borrower’s adjusted 2019 EBITDA. A MSPLF loan may be unsecured or secured. However, at all times the MSPLF loan must be senior to or pari passu with, in terms of priority and security, the eligible borrower's other loans or debt instruments, other than mortgage debt. An eligible borrower may, at the time of origination of the MSPLF loan, refinance existing debt owed by the eligible borrower to a lender that is not the eligible lender.

Under the **Main Street Expanded Loan Facility**, an eligible lender may increase (or "upsize") an eligible borrower's existing term loan or revolving credit facility (e.g., similar to an accordion facility)**[1]**. The upsized tranche is a four-year term loan ranging in size from $10 million to $200 million. The maximum size of a loan made in connection with the MSELF cannot exceed the lesser of (i) $200 million, (ii) 35% of the eligible borrower's existing outstanding and undrawn available debt that is pari passu in priority with the MSELF loan and equivalent in secured status (i.e., secured or unsecured); or (iii) an amount that, when added to the eligible borrower's existing outstanding and undrawn available debt, does not exceed **six times** the eligible borrower's adjusted 2019 EBITDA.

A MSELF loan may be unsecured or secured. However, at all times, the upsized tranche must be senior to or pari passu with, in terms of priority and security, the eligible borrower's other loans or debt instruments, other than mortgage debt. Moreover, a MSELF loan must be secured if the underlying loan is secured. In such case, any collateral securing the underlying loan (at the time of upsizing or on any subsequent date) must secure the MSELF loan on a pro rata basis. Under such an arrangement, if the borrower defaults, the SPV and lender(s) would share equally in any collateral available to support the loan relative to their proportional interests in the loan (including the MSELF loan). Eligible lenders can require eligible borrowers to pledge additional collateral to secure a MSELF loan as a condition of approval.

All loans under the Main Street Lending Program (MSNLF, MSPLF or MSELF) will bear interest at an adjustable rate of LIBOR (1 or 3 month) + 300 basis points. In this regard, the term sheets made available on the Federal Reserve's website on April 30, 2020, modified prior term sheets, which had called for an applicable interest rate of SOFR + 250-400 basis points.

Principal and interest payments for all loans obtained under the Main Street Lending Program (MSNLF, MSPLF, or MSELF) are deferred for one year. Unpaid interest will be capitalized.

As to payments of principal (including capitalized interest), eligible lenders will provide eligible borrowers with payment information during the loan origination process. Generally:

- Under a MSNLF loan, no principal is paid in the first year. The loan will be amortized over the remaining term of the loan, with one-third of principal due at the end of each of years 2 and 3, and one-third due at maturity at the end of year 4.
- Under a MSPLF loan or a MSELF loan, no principal is paid in the first year. The loan will be amortized over the remaining term of the loan, with 15% of principal due at the end of year 2, 15% of principal due at the end of year 3, and a balloon payment of 70% of principal due at maturity at the end of year 4.

To facilitate the Main Street Lending Program, the Federal Reserve will create a special purpose vehicle ("SPV"). Under the MSNLF facility, the SPV will purchase a 95% participation in a MSNLF loan, and the lender will retain 5% of the loan. Under the MSELF facility, the SPV will purchase a 95% participation in the upsized portion of the loan, and the lender will retain 5% of the upside portion of the loan and ownership of the original amount of the loan. Under the MSPLF facility, the SPV will purchase a 85% participation in a MSPLF loan, and the lender will retain 15% of the loan. The funding for the SPV will come from the Federal Reserve of Boston and a $75 billion equity investment from the Department of the Treasury. The SPV will cease purchasing participations on September 30, 2020, unless the program is extended by the Federal Reserve and the Department of the Treasury.

Eligible Lenders

Eligible lenders are U.S. insured depository institutions (including a bank, savings association or credit union), a U.S. branch or agency of a foreign bank, a U.S. bank holding company, a U.S. savings and loan holding company, a U.S. intermediate holding company of a foreign banking organization, or a U.S. subsidiary of any of the foregoing. There is not current or contemplated eligibility for "non-institutional" lenders.

Eligible Borrowers

Generally, a for-profit U.S. business may be eligible for a loan under the program if it **either** has 15,000 employees or fewer **or** had 2019 revenues of $5 billion or less. To determine eligibility, a business's employees and 2019 revenues are calculated by aggregating the employees and 2019 revenues of the business itself with those of its affiliated entities in accordance with the affiliation test set forth in 13 CFR 121.301(f) (1/1/2019 ed.).

Under section 4003(c)(3)(C) of the CARES Act, an eligible borrower will qualify as a U.S. business so long as it was created or organized in the United States or under the laws of the United States prior to March 13, 2020, and has significant operations in and a majority of its employees based in the United States.

To determine how many employees a business has, it should follow the framework set out in the regulation of the Small Business Administration ("SBA") at 13 CFR 121.106. Consequently, the business should count as employees all full-time, part-time, seasonal, or otherwise employed persons, excluding volunteers and independent contractors. The Federal Reserve has stated that the business should count its own employees and those employed by its affiliates.**[2]** In order to determine the applicable number of employees, the business should use the average of the total number of persons employed by it and its affiliates for each pay period over the 12 months prior to the origination or upsizing of the Main Street loan.

To determine its 2019 annual revenues, a business must aggregate its revenues with the revenues of its affiliates. To calculate its 2019 annual revenues for purposes of determining eligibility a business may **either** (i) use its (and its affiliates') annual "revenue" per its 2019 Generally Accepted Accounting Principles-based (GAAP) audited financial statements **or** (ii) use its (and its affiliates') annual receipts for the fiscal year 2019, as reported to the Internal Revenue Service. For purposes of the program, the term "receipts" has the same meaning used by the SBA in 13 CFR 121.104(a). The Federal Reserve has indicated that if a potential borrower (or its affiliate) does not yet have audited financial statements or annual receipts for 2019, the borrower (or its affiliate) should use its most recent audited financial statements or annual receipts.

It is to be noted that a business will qualify as an eligible borrower only if it is not an "ineligible business." Ineligible businesses include businesses listed in 13 CFR 120.110(b)-(j), (m)-(s), as modified and clarified by SBA regulations for purposes of the Payroll Protection Program on or before April 24, 2020. The Federal Reserve has stated that such modifications and clarifications include the SBA's recent interim final rules available at 85 Fed. Reg. 20811, 85 Fed. Reg. 21747, and 85 Fed. Reg. 23450. The Federal Reserve also has stated that it may further modify the application of these restrictions to Main Street Lending Program.

Program Exclusions

Companies that have obtained loans under the SBA's Payroll Protection Program under the CARES Act are generally eligible to borrow under the Main Street Lending Program. However, an eligible borrower is permitted to access only one of the MSNLF, the MSPLF, the MSELF or the Primary Market Corporate Credit Facility (a separate $750 billion facility that will serve as a funding backstop for companies rated BBB-/Baa3 or greater). However, an eligible borrower may receive more than one loan under a single Main Street Lending Program facility, provided that the sum of MSNLF loans or MSPLF loans received by a single borrower cannot exceed $25 million; and the sum of MSELF loans received by a single borrower cannot exceed $200 million.

Eligible Lender's Required Attestations and Certification

An eligible lender must:

- Attest that proceeds of an eligible loan will not be used to repay or refinance preexisting loans or lines of credit made by the eligible lender to the eligible borrower (including, in the case of MSELF loans, the pre-existing portion of the eligible loan).
- Attest that it will not cancel or reduce any existing lines of credit outstanding to the eligible borrower.
- Certify that the methodology used for calculating the eligible borrower's adjusted 2019 EBITDA (i) in the case of MSNLF and MSPLF loans, is the methodology that it previously used for adjusting EBITDA when extending credit to the eligible borrower or similarly situated borrowers on or before April 24, 2020 and (ii) in the case of MSELF loans, is the methodology it previously used for adjusting EBITDA when originating or amending the eligible loan on or before April 24, 2020.
- Certify that it is eligible to participate in the Main Street Lending Program, including in light of the conflicts of interest prohibition in section 4019(b) of the CARES Act.

While most of the certifications and covenants are the same, there are two variations. The eligible lender certification relating to EBITDA is different in the MSELF than it is in the MSNLF and MSPLF, owing to fact that the MSELF necessarily includes an existing loan from the eligible lender. In addition, the MSPLF includes a modification to the eligible borrower covenant regarding debt repayment to allow an eligible borrower to refinance existing debt owed to a lender that is not the eligible lender at the time the MSPLF Loan is originated.

Eligible Borrower's Required Attestations and Certification

An eligible borrower must:

- Commit to refrain from repaying the principal balance of, or paying any interest on, any debt until the eligible loan (or the upsized tranche of a MSELF loan) is repaid in full, unless the debt or interest payment is mandatory and due. (However, under a MSPLF loan, the eligible borrower may, at the time of the origination of such loan, refinance existing debt owed by the eligible borrower to a lender that is not the eligible lender.)

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- Commit that it will not seek to cancel or reduce any of its outstanding lines of credit with the eligible lender or any other lender. (However, under a MSPLF loan, the eligible borrower may, at the time of the origination of such loan, refinance existing debt owed by the eligible borrower to a lender that is not the eligible lender.)
- Certify that it has a reasonable basis to believe that, as of the date of origination of the eligible loan and after giving effect to such loan, 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.
- Commit that it will follow compensation, stock repurchase, and capital distribution restrictions that apply to direct loan programs under section 4003(c)(3)(A)(ii) of the CARES Act, except that an S corporation or other tax pass-through entity that is an eligible borrower may make distributions to the extent reasonably required to cover its owners' tax obligations in respect of the entity's earnings.**[3]**
- Certify that it is eligible to participate in the Main Street Lending Program, including in light of the conflicts of interest prohibition in section 4019(b) of the CARES Act.

In addition to the foregoing, an eligible borrower must use commercially reasonable efforts to maintain its payroll and retain its employees during the time that the eligible loan is outstanding.

Please contact the authors or your Miller Canfield attorney for more information.

The information is based on facts and guidance available at the time of publication, and may be subject to change.

[1] An "accordion facility" is a feature of some loan agreements that allows the borrower to add a new term loan or tranche, or increase the revolving credit loan commitments under an existing revolving credit, term loan, or delayed draw loan facility up to a specified amount under certain terms and conditions. The advantage of this feature is that the increase in the loan amount is pre-approved by the lenders so that the borrower does not have to obtain the lenders' consent if it increases the loan facility at a later date.

[2] It is to be noted that 13 CFR 121.106 does NOT include a U.S. residency limitation. So it appears that in determining the number of employees a business has, employees are to be counted regardless of where they are resident.

[3] Under the restrictions applicable to the Federal Reserve's direct lending facilities under Title IV of the CARES Act, the **borrower may not do any of the following during the period commencing when the loan agreement or loan guarantee agreement is executed and ending 12 months after the loan or loan guarantee is no longer outstanding**:

- Purchase its own or parent company's equity securities that are listed on a national securities exchange (absent a pre-existing contractual obligation);
- Pay dividends on common stock or make other **capital** distributions;
- To any employee whose 2019 compensation **exceeded $425,000**, pay
  - more than $425,000 during any 12 consecutive months; or
  - an amount in severance that is twice the total compensation the employee received in 2019.

- To any employee whose 2019 compensation **exceeded $3 million**, pay more than the sum of (i) $3 million plus (ii) 50% of the excess over $3 million of the total compensation which the employee received in 2019.

The Federal Reserve has stated that the restrictions on restrictions on dividends and other capital distributions will not apply to distributions made by an S corporation or other tax pass-through entity to the extent reasonably required to cover its owners’ tax obligations in respect of the entity’s earnings.