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Main Street Lending Program: Issues, Questions and Proposed Changes

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On April 9, 2020, as part of the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), the Treasury and the Federal Reserve Board (Federal Reserve) unveiled the **Main Street Lending Program (MSLP)**, aimed to provide emergency liquidity to small and mid-sized businesses experiencing losses caused by the COVID-19 pandemic. The program is comprised of two credit facilities: the **Main Street New Loan Facility (MSNLF)**, which allows lenders to originate new loans to eligible borrowers, and the **Main Street Expanded Loan Facility (MSELF)**, which allows lenders to increase the size of existing loans to eligible borrowers.

While the MSLP is a welcome development for businesses across the United States during these uncertain times, there remain several major issues with the program that could prevent the program from helping the greatest number of businesses. A large number of market participants, including lenders, law firms, and trade associations, submitted comments to the Federal Reserve during the public comment period that ended on April 16. Among them were the Loan Syndications and Trading Association (LSTA) and the U.S. Chamber of Commerce (Chamber of Commerce), which provided detailed comments on the MSNLF and MSELF term sheets released by the Federal Reserve.

1. Lack of Flexibility to Negotiate Tailored Loan Terms

The biggest criticism of the MSLP, and the overarching theme of the LSTA and Chamber of Commerce comments, is that the program does not afford parties enough latitude to negotiate loan terms that are tailored to the needs of individual borrowers and the interests of lenders. For example, both the MSNLF and MSELF prescribe a particular interest rate (SOFR plus 250 to 450 basis points), minimum loan size ($1 million), and an EBITDA-based leverage test. By allowing parties to agree to different terms, the general appeal and availability of the program would greatly expand.

For instance, according to the LSTA, the 400 basis point cap on the interest rate spread may be too low to incentivize lenders to make loans to certain high-leverage borrowers. Perhaps even more problematic, requiring the use of SOFR as the benchmark rate may prove difficult for many lenders, as it is still a new index that banks have yet to implement in their credit facilities to any significant degree. Instead, many lenders (particularly smaller financial institutions) would prefer to use Prime,

LIBOR, or other common indexes, which may be accompanied by fallback language that allows for SOFR as a replacement rate. Imposing SOFR on loans under the MSELF would be especially challenging, as it would prove difficult to add a SOFR-based tranche to an existing facility that is based on another reference rate. Because of this, the LSTA has suggested that the Federal Reserve allow a MSELF loan to reference the same benchmark as the existing loan, which would simplify the documentation process and eliminate the need for overly complicated drafting and spread adjustments.

Similarly, the minimum loan size of $1 million is too large and may exclude certain small businesses that are looking for smaller amounts of liquidity, as particularly noted by the Chamber of Commerce. Also, the current MSNLF and MSELF term sheets impose a maximum loan size (and a separate but related attestation) that is dependent on the borrower's debt-to-EBITDA ratio, which would disqualify many companies from borrowing under the program. The LSTA commented that lenders should be permitted to define EBITDA in a way that conforms with the existing debt arrangements with a given borrower, as well as the borrower's industry in general. And for those borrowers that typically do not have a positive EBITDA, such as nonprofits or startups, lenders should be able to use alternative creditworthiness measures typical of the borrower's industry.

2. Exclusion of Private Lenders

Another major drawback of the MSLP is that it is currently limited to "U.S. insured depository institutions, U.S. bank holding companies, and U.S. saving and loan holding companies." This requirement shuts out a significant portion of middle-market companies that often borrow from foreign banks and non-bank lenders like private debt funds. The consensus among observers is that this definition of "eligible lenders" is unnecessarily restrictive. The LSTA highlighted the "urgent need to provide liquidity" to companies affected by the COVID-19 crisis in its argument that a broader range of lenders should be permitted under the program. At a minimum, the LSTA argued, non-U.S. and non-bank lenders should be allowed to lend alongside current eligible lenders of existing loans under the MSELF. The Federal Reserve could go even further by allowing non-eligible lenders to combine with eligible lenders in a syndicate under either the MSNLF or the MSELF.

3. Constraints of Existing Credit Agreements

Yet another source of both criticism and confusion is how loans under the MSLP will fit within existing debt structures. Most borrowers are parties to existing credit agreements that contain negative covenants prohibiting the incurrence of new secured debt (or in some cases, even unsecured debt), such that incurring indebtedness under the MSLP would require a consent or an amendment to the existing credit facility. Additionally, the MSLP currently requires borrowers to refrain from repaying other loan balances of "equal or lower priority," except for mandatory principal payments. It is unclear whether this prohibits the repayment of a loan at maturity or repayment of draws under revolving credit facilities, but it would be reasonable to allow these kinds of payments. On top of these potential roadblocks, issues of collateral also arise under the MSELF. While new loans under the MSNLF are unsecured, loans under the MSELF will be secured by any collateral that secures the existing loan (whether pledged under the original terms of the existing loan or at the time of upsizing) on a pro rata basis, potentially preventing borrowers from participating in the MSELF due to existing debt constraints.

The LSTA noted that where a company's existing credit agreements do not allow new secured indebtedness, a possible solution is to allow an upsized tranche under the MSELF to be unsecured even if the existing loan is secured, as long as the lender in that scenario is willing to make the loan

on an unsecured basis. The LSTA also urges that in any case where a borrower is restricted from taking on new debt, lenders should be permitted to lend to a direct or indirect holding company of the borrower so as not to violate such restrictions.

Changes Needed to the Main Street Lending Program

We have highlighted just a few of the concerns with the MSLP in its current form, in addition to the many other problems, clarifications, and questions raised by the LSTA and other entities. Market participants should be on the lookout for revisions to the program in the coming days and weeks that will hopefully address these concerns. Cooperation and coordination between lenders, borrowers, and the Federal Reserve and the Treasury is essential in order to provide much-needed liquidity to small and mid-sized businesses in the swiftest and most efficient manner.

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