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Prepare for the Main Street Lending Program!

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It’s Rolling Out Soon

Businesses impacted by the COVID-19 pandemic have been eagerly anticipating this important loan program, which according the Federal Reserve Bank of Boston, is now scheduled to launch within “days,” not “weeks.”

Since May 27, 2020, when the Federal Reserve Bank of Boston released details, instructions, and updated FAQs on its Main Street Lending Program, businesses have been eagerly anticipating the launch of this important, yet complex loan program. According to the Fed’s June 3rd webinar, the launch of the Main Street Lending Program is imminent and updates regarding the official launch of the program will be made available on the Fed’s website.

This alert discusses key details from the webinar, as well as the different types of loan facilities, their eligibility requirements, terms, restrictions, and more.

The MSL Program is designed for small and medium size businesses that were in sound financial condition prior to the COVID-19 pandemic. Borrower eligibility is addressed in greater detail below, however some key points are: (i) borrowers under PPP loans are not prohibited, (ii) each “affiliated group” shall have a single aggregate lending limit and may participate in only one type of available Main Street facility. SBA affiliation rules will apply to Main Street loans, however a number of businesses such as the real estate industry and portfolio companies held by private equity and venture capital-owned firms that were ineligible for PPP loans should be able to participate in the MSL Program (provided they satisfy other eligibility requirements), (iii) U.S. subsidiaries of foreign firms may participate provided the loan proceeds are used at the subsidiary level and not to benefit the foreign parent, and (iv) nonprofits are ineligible to participate at this time, as the Fed considers how best to incorporate them into the program.

Snapshot

The MSL Program includes three types of term loan facilities (no revolving facilities are currently available):

- MSNLF (New Loans) – refers to loans originated on or after April 24, 2020, not junior to borrower's other unsecured debt.

- MSPLF (Priority Loans) – refers to loans originated on or after April 24, 2020, senior to or pari passu with, in terms of priority and security, the borrower's other loans, other than mortgage debt.

- MSELF (Upsized Tranches) refers to increases in the amount of existing term loan or revolving credit facilities on or before April 24, 2020, with a remaining maturity of at least 18 months.

Unlike the popular PPP program, loans will ***not*** be eligible for loan forgiveness.

Many of the terms of each loan are the same; however there are key differences. The table below summarizes the terms of each loan. These terms are the same as originally released on April 30, 2020, and more detailed summaries follow the table.

Main Street Program Loan Options	**New Loans**	**Priority Loans**	**Upsized Tranches**
Term	4 years	4 years	4 years
Minimum Loan Size	$500,000	$500,000	$10,000,000
Maximum Loan Size	The lesser of $25M or an amount that, when added to outstanding and undrawn available debt, does not exceed 4.0x adjusted 2019 EBITDA	The lesser of $25M or an amount that, when added to outstanding and undrawn available debt, does not exceed 6.0x adjusted 2019 EBITDA	The lesser of $200M, 35% of existing outstanding and undrawn available debt, or an amount that, when added to outstanding and undrawn available debt, does not exceed 6.0x adjusted 2019 EBITDA.
Lender Retention	5%	15%	5%
Fed Participation	95%	85%	95%
Payment (year one deferred for all)	Years 2-4:33.33% , 33%, 33%	Years 2-4:15%, 15%, 70%	Years 2-4:15%, 15%, 70%
Rate	LIBOR +3%	LIBOR +3%	LIBOR +3%
Prepayment allowed	Yes, without penalty		
Loan Fees	Origination and transaction fees will apply		

New Loans

New Loans will range from a minimum principal amount of $500,000 up to a maximum principal amount that is the lesser of (i) $25 million or (ii) an amount that, when added to the borrower's existing outstanding and undrawn available debt, is less than or equal to ***four*** times the borrower's 2019 adjusted EBITDA. The term of New Loans will be four years, with principal amortization of one-third at the end of the second, third, and fourth year. New Loans may not be, at the time of origination and during the term of the loan, junior in priority in bankruptcy to the borrower's other unsecured loans. The FAQ contains more detailed guidance on this requirement.

Priority Loans

Priority Loans will range from a minimum principal amount of $500,000 up to a maximum principal amount that is the lesser of (i) $25 million or (ii) an amount that, when added to the borrower's existing outstanding and undrawn available debt, is less than or equal to ***six*** times the borrower's adjusted 2019 EBITDA. The term of Priority Loans will be four years, with principal amortization of 15% at the end of the second and third year, and a balloon payment of 70% at the end of the fourth year. At the time of origination and at all times while the loan is outstanding, a Priority Loan must be senior to or *pari passu* with, in terms of priority and security, the borrower's other loans, other than mortgage debt. The borrower may, at the time of origination of a Priority Loan, refinance existing debt owed by the borrower to a lender that is not the eligible lender under the MSL Program. After origination and until the Priority Loan is repaid in full, however, the borrower must refrain from repaying the principal balance of, or paying any interest on, any debt other than the Priority Loan, unless the debt or interest payment is mandatory.

Upsized Tranches

The maximum size for the upsized tranche of any existing loans will range from a minimum principal amount of $10 million up to a maximum principal amount that is the lesser of (i) $200 million, (ii) 35% of the borrower's existing outstanding and undrawn available debt that is *pari passu* in priority with the loan and equivalent in secured status (secured or unsecured) or (iii) an amount that, when added to the borrower's existing outstanding and undrawn available debt, is less than or equal to ***six*** times the borrower's adjusted 2019 EBITDA. To be eligible for "upsizing," the existing term loan or revolving credit facility must have been originated on or before April 24, 2020, and must have a remaining maturity of at least 18 months. The lender may extend the maturity of an existing loan or revolving credit facility at the time of upsizing in order for the underlying instrument to satisfy the 18-month remaining maturity requirement. At the time of upsizing and at all times thereafter, the Upsized Tranche must be senior to or *pari passu* with, in terms of priority and security, the borrower's other loans, other than mortgage debt. The term of the Upsized Tranche will be four years, with principal amortization of 15% at the end of the second and third year, and a balloon payment of 70% at the end of the fourth year.

As noted in the 5/27 Release, the lender of an Upsized Tranche is not required to have been the lender that originally extended the loan underlying the Upsized Tranche and assigned a specified internal risk rating to the underlying loan.

Terms Applicable Across All Three Facilities

- Loans will be subject to an adjustable interest rate of 1- or 3- month LIBOR + 3%. The 5/27 Release prohibits any other interest rate.

- Amortization on Main Street loans will be deferred for one year and no payments of principal or interest is required during this period. Unpaid interest will be capitalized.

- Loans may be prepaid without penalty.

- Loans may be secured or unsecured. An Upsized Tranche must be secured if the underlying loan is secured.

- For New Loans and Priority Loans, the methodology for calculating adjusted 2019 EBITDA must be the same methodology used for adjusting EBITDA when extending credit to the borrower (or similarly situated borrowers). For Upsized Tranches the methodology must be consistent with the underlying loan.

- New Loans and Priority Loans have an origination fee paid to the lender of 1% of the principal amount and Expanded Loans pay an "upsizing" fee of 0.75% of the principal amount. Lenders cannot charge additional fees, except for legitimate services provided.

- Lenders pay the MSL Program a transaction fee of 1% of the principal amount of any New Loan or Priority Loan, and 0.75% of the principal amount of the Upsized Tranche, and may elect to pass this fee on to the borrower.

- Borrowers must 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 (with certain modifications introduced by the Fed, including that an S corporation or other tax pass-through entity may make tax distributions, subject to an annual reconciliation). These restrictions are detailed below.

Borrower Eligibility

Businesses created or organized for profit in the U.S. or under U.S. law prior to March 13, 2020 that were in good financial standing before the COVID-19 crisis are eligible to obtain a Main Street loan if (together with their affiliates) they have either (i) no more than 15,000 employees *or* (ii) 2019 annual revenues of less than $5 billion. In calculating the number of employees, borrowers count their and their applicable affiliates' full-time, part-time, seasonal, and other employees, and exclude volunteers and independent contractors. Borrowers are to use the average of the total persons employed for each pay period over the 12 months prior to the origination of the Main Street loan. Annual revenues can be calculated either using the borrower's and its applicable affiliates' annual "revenues" per 2019 GAAP audited financials or the borrower's and its applicable affiliates' receipts for fiscal year 2019 as reported to the IRS. If the borrower (or its affiliate) does not have audited financial statements or annual receipts for 2019, the borrower should use the most recent audited financial statements or annual receipts available.

Eligible borrowers also must have significant operations, and a majority of employees, based in the U.S. The 5/27 Release specifies that in order to determine if an eligible borrower has "significant operations" and a "majority of employees" in the U.S., the business's operations should be evaluated on a consolidated basis together with its subsidiaries, but not its parent companies or "sister" affiliates.

In the 5/27 Release, an eligible borrower may be a U.S. subsidiary of a foreign company that has, on a consolidated basis, significant operations, and a majority of its employees based, in the U.S.

However, a borrower that is a subsidiary of a foreign company must use the proceeds of a Main Street Loan only for the benefit of itself, its consolidated U.S. subsidiaries, and other affiliates of the borrower that are U.S. businesses, and not for the benefit of an eligible borrower's foreign parents, affiliates, or subsidiaries.

The 5/27 Release provides additional details around these restrictions and the application of the SBA affiliation rules.

Borrowers also must not be an Ineligible Business listed in 13 CFR 120.110 (b)-(j), (m)-(s), as modified and clarified on or before April 24, 2020 by Small Business Administration (SBA) regulations for purposes of the Paycheck Protection Program, created under Title I of the CARES Act. Businesses that receive targeted benefits under the CARES Act are also ineligible.

Nonprofit entities continue to be ineligible for Main Street loans. The Fed continues to review the feasibility of adjusting the borrower eligibility criteria and loan eligibility metrics of the MSL Program for nonprofit entities.

Compensation Restrictions

For officers and employees whose total compensation exceeded $425,000 (but was less than $3 million) in 2019 or, if applicable, a subsequent reference period (as described below), borrowers may not, beginning the year of the loan and continuing for the one-year period following the satisfaction of the loan, pay such officer or employee during any 12 consecutive month period more compensation than that officer or employee received in 2019 or the subsequent reference period or pay severance/other benefits upon termination of employment with the borrower that exceed twice the maximum total compensation in 2019 or the subsequent reference period. The 5/27 Release specifies that these restrictions do not apply to any employee whose compensation is determined through an existing collective bargaining agreement entered into prior to March 1, 2020.

For officers and employees whose total compensation exceeded $3 million in 2019 or the subsequent reference period, borrowers may not, beginning the year of any loan and continuing for the one-year period following the satisfaction of the loan, pay such officer or employee during any consecutive 12 month period more than $3 million plus 50% of the amount over $3 million received by the officer in 2019 or the subsequent reference period or, except for an employee whose compensation is determined through an existing collective bargaining agreement entered into prior to March 1, 2020, pay severance pay/other benefits upon termination of employment with the borrower that exceed twice the maximum total compensation in 2019 or the subsequent reference period.

The 5/27 Release adds restrictions applicable to new hires and existing officers or employees who become highly compensated. An officer or employee whose employment started during 2019 or later, the "subsequent reference period" is the 12-month period starting from the end of the month in which the individual began employment, if his or her total compensation exceeds $425,000 during such period. For an officer or employee whose total compensation first exceeds $425,000 during a 12-month period ending after 2019, the "subsequent reference period" is the 12-month period starting from the end of the month in which his or her total compensation first exceeded $425,000.

The 5/27 Release also instructs that "officers or employees" means individuals who perform compensated services for a borrower and either (a) for whom, in connection with those services, the borrower would be responsible for reporting the compensation on Form W-2 and withholding federal income taxes (regardless of whether the compensation is subject to withholding or tax is withheld) or

(b) is a partner in a partnership, member of a limited liability company or similar. Independent contractors and independent directors are *not* considered officers or employees.

“Total compensation” includes salary, bonuses, awards of stock, and other financial benefits provided by the borrower and its affiliates to an officer or employee of the borrower.

Equity-Based Transaction Limitations

Borrowers (or subsidiaries) with listed securities cannot engage in stock buybacks, unless required under pre-existing contracts in effect as of March 27, 2020. Borrowers may not pay dividends or make other capital distributions with respect to the common stock equivalents of the borrower, until one year after the date the Main Street loan is no longer outstanding, subject to the tax-distribution exception for pass-through entities.

The 5/27 Release also instructs that dividends and other capital distributions means any payment made with respect to the borrower’s common stock equivalents, including discretionary dividend payments, and would include mandatory or preferential payments of dividends or other distributions in respect of preferred stock unless both the equity interest and the obligation to pay dividends or distributions existed as of March 27, 2020. Dividends and other capital distributions do not include repurchases or redemptions. The 5/27 Release provides that tax distributions are subject to an annual reconciliation.

Certifications and Covenants

The 5/27 Release details the certifications and covenants required from borrowers, which includes indemnification by the borrower of the beneficiaries of such certifications and covenants in respect of losses arising out of a material breach of any certifications or covenants.

As announced in the FAQs on April 30, 2020, a borrower should undertake good-faith efforts to maintain payroll and retain employees, in light of its capacities, the economic environment, its available resources, and the business need for labor. Borrowers that have already laid off or furloughed workers as a result of the disruptions from COVID-19 remain eligible to apply for Main Street loans.

Main Street Lenders

Eligible lenders under the MSL Program are U.S. insured depository institutions, U.S. bank holding companies, and U.S. savings and loan holding companies. The 5/27 Release provides that multiple affiliated entities may register as eligible lenders under the MSL Program.

The MSL Program pays lenders an annual loan servicing fee of 0.25% of the principal amount of the participation.

Lenders are expected to conduct an assessment of each potential borrower’s financial condition at the time of the potential borrower’s application and should satisfy themselves with respect to a borrower’s ability to repay Main Street loans, taking into account a borrower’s credit history and financial performance prior to the COVID-19 crisis, as well as its post-pandemic business prospects.

Under the MSL Program, lenders will have two options for funding loans:

- Funded Loan: A lender may extend Main Street loan to an eligible borrower and fund such loan. Thereafter, a lender that has registered with the MSL Program can seek to sell a participation in such loan to the MSL Program.

- Condition of Funding: A lender may also extend a Main Street loan to an eligible borrower, but make the funding of the loan contingent on a binding participation commitment from the MSL Program. The 5/27 Release includes proposed language for use in loan documentation for lenders who choose this option.

Disclosure and Reports

The Fed will disclose information regarding the Main Street loans during the operation of MSL Program, including information regarding names of lenders and borrowers, amounts borrowed and interest rates charged, and overall costs, revenues, and other fees. Under section 11(s) of the Federal Reserve Act, the Fed also will disclose information concerning the MSL Program one year after the effective date of the termination of the authorization of the MSL Program. This disclosure will include names and identifying details of each participant in the MSL Program, the amount borrowed, the interest rate or discount paid, and information concerning the types and amounts of collateral pledged or assets transferred in connection with participation in the MSL Program.

Documentation

The 5/27 Release included the form agreements and other documents for lenders and borrowers to use in connection with Main Street Loan participation, but the Fed will not provide form loan documents for eligible lenders to use when making eligible loans to eligible borrowers—and eligible lenders are advised that they should provide these documents. Such documentation should be substantially similar, including with respect to required covenants, to the loan documentation that the lender uses in its ordinary course lending to similarly situated borrowers, adjusted only as appropriate to reflect the terms and requirements of the MSL Program. The FAQs also contain appendices setting forth a checklist of terms and covenants that must be reflected in the loan documentation in order for the MSL Program to purchase a participation in the loan, certain model covenants that lenders can elect to reference when drafting their documentation certain borrower certifications, cross-acceleration provisions, and financial reporting and covenants.

The Board of Governors of the Federal Reserve System and the Secretary of the Treasury reserve the right to make adjustments to the terms and conditions of the MSL Program and will announce any changes on the Fed’s website.

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