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Federal Reserve Main Street Lending Program: Updates, Timing and Certain Considerations

Article By:

Joseph Price

Joseph J. Ronca

Daniel B. Bosworth

The Federal Reserve Main Street Lending Program ("Program"), aimed at supporting small and mid-sized businesses, is expected to launch soon. Recently, the Federal Reserve Bank of Boston published lengthy and detailed updated FAQs, lender and borrower certifications, terms and conditions, certain form ancillary agreements and other documents relevant to applying for and closing loans under the Program ("Main Street Loans"). Further, on June 8, 2020, the Federal Reserve updated certain terms of the credit facilities to, depending on the facility, lower the minimum loan amount, raise the maximum loan limit, adjust the principal repayment schedule to begin after two years and extend the term to five years.

The Program, as updated, continues to include three credit facility options: (i) the Main Street New Loan Facility ("New Facility"), for new term loans made by eligible lenders, (ii) the Main Street Priority Loan Facility ("Priority Facility"), for new term loans made by eligible lenders under different terms than the New Facility and (iii) the Main Street Expanded Loan Facility ("Expanded Facility"), for upsizing existing loans made by eligible lenders. Although terms, conditions, eligibility criteria and related processes for borrowing under the Program are in many cases similar across the three credit facilities, there are key differences described in the Program documentation.

The homepage for the Main Street Lending Program, which will continue to be updated, contains links to all relevant lender and borrower documentation, FAQs, related resources and a link to subscribe for alerts to Program updates. An extensive list of documents for the Program is provided at the Main Street Lending Program Forms and Agreements page.

Set forth below are current links to relevant documentation for borrowers, although the Main Street Lending Program Forms and Agreements page contains the exhaustive set of documents.

- Main Street Lending Program Forms and Agreements
- Main Street Lending Program FAQs

- New Facility – Term Sheet (updated as of June 8, 2020)
- Priority Facility – Term Sheet (updated as of June 8, 2020)
- Expanded Facility – Term Sheet (updated as of June 8, 2020)
- New Facility – Borrower Certifications and Covenants
- Priority Facility – Borrower Certifications and Covenants
- Expanded Facility – Borrower Certifications and Covenants
- Participation Agreement Transaction Specific Terms
- Participation Agreement Standard Terms and Conditions
- Co-Lender Agreement Transaction Specific Terms
- Co-Lender Agreement Standard Terms and Conditions

The terms, rules, guidance and documentation for the Program are extensive and their relevance will vary depending on the circumstances of particular borrowers. Companies should carefully review all relevant documentation applicable to the credit facility in which they intend to participate. A non-exhaustive set of considerations for prospective borrowers is discussed below.

Timing and Process

To participate in the Program, eligible borrowers will apply for and obtain loans directly from an eligible lender. The lender will in turn sell a 95% participation in the loan to the Federal Reserve special purpose vehicle ("Main Street SPV") established for the Program. Once the Program launches, the Federal Reserve will first register participating lenders, and then the Main Street SPV will begin purchasing participations.[1] During what we expect to be an iterative process, borrowers will work with eligible lenders to complete and submit necessary certifications, undergo an underwriting process (and any related diligence for bank customers) and negotiate and finalize loan documentation. Lenders will then, at their option, either fund the loan and thereafter submit documentation to the Main Street SPV for approval and purchase of the participation; or submit finalized documentation to the Main Street SPV first, obtain a written commitment from the Main Street SPV to purchase the participation, and then fund the loan.

In addition to the eligibility criteria published by the Federal Reserve, eligible lenders are required to apply their own underwriting standards in evaluating the financial condition and creditworthiness of a potential borrower. Lenders may require additional application information and documentation to be submitted beyond what is stated in the Federal Reserve materials. Further, lenders will use their own loan documentation for Main Street Loans, which should be substantially similar, including with respect to required covenants, to the loan documentation such lenders use in their ordinary course lending to similarly situated borrowers, adjusted only as appropriate to reflect requirements of the Program. Such documentation must reflect the terms set forth in Appendix A to the Main Street Lending Program FAQs.

As a result of the foregoing, the timeline and checklist to close a Main Street Loan will vary depending on the parties. If necessary, negotiating amendments or intercreditor agreements with existing lenders will also impact timing. We continue to believe that leveraging existing relationships with eligible lenders will streamline the process, however, the Program may be viewed by some lenders as an opportunity to create relationships with companies that they did not have before. This perspective should be encouraging for companies that lack pre-existing relationships with eligible bank lenders but believe they can benefit from the Program. As noted in the Program FAQs, interested borrowers should contact eligible lenders for more information on whether the eligible lender plans to participate in the Program and to request more information on the application process.

Eligibility

The Borrower Certifications and Covenants Instruction and Guidance (there is a separate version for each of the three credit facilities) describes in detail the certifications a borrower must make and, in certain cases, the level of diligence and analysis that should be undertaken by the borrower in support of such certifications. In some instances, the document also contains rules or guidance on Program requirements in addition to those found in the term sheets and FAQs. As this documentation provides a thorough and systematic guide for borrowers to analyze and document their eligibility, it should be reviewed and followed in detail when considering and preparing to apply for the Program.

Size Test and Affiliates; Ineligible Businesses; Foreign Parent Companies

When determining size eligibility (less than 15,000 employees or less than $5 billion in 2019 revenue), borrowers must aggregate the employees or revenue of its affiliates. The broad affiliates rules of the SBA set forth in 13 CFR 121.301(f) (1/1/2019 ed.) (which were applied to the size tests for the Paycheck Protection Program) are used in determining affiliates. Generally, if an entity has control (whether by majority ownership or minority control rights) then that entity will be deemed affiliated.[2] Borrowers that are backed by majority or minority investors should work closely with their equity owners to determine affiliation and create back-up documentation counting employees or revenue of such affiliates to demonstrate size eligibility.

A borrower must certify that, after reasonable, good faith diligence, it has no reason to believe it is an ineligible business. An ineligible business means a business of any of the types listed in **13 CFR 120.110(b)-(j), (m)-(s)**, as modified and clarified by SBA regulations for purposes of the Paycheck Protection Program on or before April 24, 2020, including 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 may further modify the application of these restrictions to the Program. As noted in the Borrower Certifications and Covenants Instruction and Guidance, if representatives of the borrower have reason to believe that the borrower may be an ineligible business under the categories listed in the regulation, borrowers are expected to conduct further inquiry into the SBA's interpretations of such categories, including in the interim final rules, and to reference the FAQs.

An eligible borrower may be a subsidiary of a foreign company, provided that the borrower itself is created or organized in the United States or under the laws of the United States, and the borrower on a consolidated basis has significant operations in and a majority of its employees based in the United States. An eligible borrower that is a subsidiary of a foreign company must use the proceeds of a Main Street Loan only for the benefit of the eligible borrower, its consolidated U.S. subsidiaries and other affiliates of the eligible borrower that are U.S. businesses. The proceeds of the Main Street Loan may not be used for the benefit of an eligible borrower's foreign parents, affiliates or subsidiaries.

Other Federal Reserve Programs and Affiliates

An affiliated group of companies can participate in only one Program facility (i.e., if a company borrows under the New Facility, its affiliates can only borrow under the New Facility and are prohibited from borrowing under the Expanded Facility and Priority Facility), and cannot participate in both a Program facility and the Primary Market Corporate Credit Facility.[3] Further, if more than one affiliate participates in the Program and thus borrows under the same type of facility, the maximum loan amount applicable to such facility will apply across all affiliates in the aggregate, taking into account the aggregate leverage levels of the affiliated entities. The SBA affiliate rules also apply in making this determination. As part of its application, a borrower must certify that, to its knowledge after reasonable diligence, none of its affiliates has accessed any Program facility or the Primary Market Corporate Credit Facility as of the date of such certification and the borrower has informed the lender if, after reasonable diligence, it has determined that any of its affiliates has previously received, or has a pending application to receive, funds in connection with any Program, as well as the value of such funding. Portfolio companies of VC or PE funds or that are part of a complex corporate structure must coordinate with their owners or parent entities as a result of this rule to determine the nature and extent of participation of any of its affiliates in the Program or the Primary Market Corporate Credit Facility.

With respect to applying the loan size limitations to an affiliated group, E.10 of the FAQ explains that eligible borrowers are subject to the following rules:

An affiliated group's total participation in a single Program facility cannot exceed the maximum loan size that the entire affiliated group is eligible to receive on a consolidated basis. Thus, a borrower's maximum loan size would be limited by its own leverage level, the leverage level of the affiliated group on a consolidated basis and the size of any loan extended to other affiliates in the group. For example, in the case of the New Facility, the borrower's maximum loan size would be the lesser of:

1. $35 million (less any amount extended to an affiliate of the borrower under the New Facility);

2. an amount that, when added to the borrower's existing outstanding and undrawn available debt, does not exceed four times the borrower's adjusted 2019 EBITDA; or

3. an amount that, when added to the borrower's affiliated group's existing outstanding and undrawn available debt, does not exceed four times the entire affiliated group's adjusted 2019 EBITDA.

On a Q&A call, the Federal Reserve explained that the above aggregation of affiliate leverage levels is triggered by the second Program application from within an affiliated group. Thus, a borrower that, amongst its affiliates, is the sole participant in the Program does not need to aggregate the leverage level of its affiliates for determining the maximum amount of the loan.

Negative EBITDA; Nonprofits

EBITDA is currently the key underwriting metric for the Program and loan size is capped at the lesser of a fixed dollar amount and either 4x or 6x debt to EBITDA ratio depending on the facility. Negative EBITDA companies and nonprofits are therefore currently ineligible for the Program. The Federal

Reserve has noted in the FAQs that it is working to establish soon one or more loan options that are suitable for nonprofit organizations. Also, the Federal Reserve and the Treasury Department will be evaluating the feasibility of adjusting the loan eligibility metrics of the Program for asset-based borrowers. As of the date of this article, no further information has been published.

Unavailability of Credit; Solvency

As part of its application, a borrower must certify that it is unable to secure adequate credit accommodations from other banking institutions. This certification does not require, however, a borrower to show that no other credit is available. Rather, the borrower can make this certification if the amount, price or terms of credit available from other sources are inadequate for the borrower's needs during the current unusual and exigent circumstances. Borrowers are not required to demonstrate that applications for credit had been denied by other lenders or otherwise document that the amount, price or terms of credit available elsewhere are inadequate. The guidance suggests that due weight may be given to both liquidity needs and the difficulty of obtaining credit on typical market terms, in each case as a result of the pandemic.

A borrower must certify that it is not "insolvent" as defined in regulations applicable to Section 13(3) of the Federal Reserve Act. To make this certification a borrower must not be in bankruptcy and must not be generally failing to pay undisputed debt as it becomes due during the 90 days preceding the date of borrowing. Each Borrower Certifications and Covenants Instructions and Guidance clarifies that pandemic-related considerations may enable a borrower to make this certification notwithstanding a pandemic-caused failure to pay certain debts when due. For example, a borrower may not be insolvent for these purposes if it is behind on its debts because of reduced business activity resulting from stay-at-home, shelter-in-place, social distancing or other similar orders or recommendations by federal, state or local government authorities related to the pandemic. Further, a borrower may not be insolvent for these purposes if expected and routine sources of funding were unexpectedly unavailable due to market conditions resulting from the pandemic.[4]

As required by the Program (and not specifically by Section 13(3)), a borrower must separately certify as to forward-looking solvency. It must certify that it has a reasonable basis to believe that it has the ability to meet its financial obligations for at least 90 days after the Main Street Loan's origination date and does not expect to file for bankruptcy during that period.

Remedies for Material Misstatements – Mandatory Prepayment and Indemnification

Borrowers should give due consideration to all certifications made in connection with the Program. For certain certifications, in particular those pertaining to CARES Act eligibility for the Program, CARES Act restrictions on compensation, stock buybacks and dividends (as discussed below) and certifications pertaining to Section 13(3) of the Federal Reserve Act, if the Federal Reserve determines that the borrower made a material misstatement in these certifications, or materially breaches certain related covenants, the Federal Reserve will notify the lender to trigger a mandatory prepayment of the Main Street loan. This mandatory prepayment requirement will be included in the loan documentation. Model language for the prepayment is currently contained in Section II.A. of Appendix B to the FAQ.

The certifications and covenants in the loan documents will also include an indemnification by the borrower of the beneficiaries of such certifications and covenants for losses arising out of a material breach of any of the borrower's certifications or covenants. The indemnification will cover a broader group of certifications and covenants than those subject to the mandatory prepayment discussed above.

Refinancing Existing Credit Facilities

In general, proceeds of Program loans cannot be used to refinance existing debt, and a borrower must refrain from repaying the principal balance of, or paying any interest on, any debt unless mandatory and due, while the Main Street Loan is outstanding and held by the Main Street SPV or a government assignee. There are exceptions to the refinancing and repayment restrictions. Two significant exceptions are highlighted here. First, Priority Facility loans (and only Priority Facility loans) may be used, at the time of origination, to refinance existing debt that is owed to lenders other than the eligible lender that originates the Priority Facility loan. Second, during the term of any outstanding Program loan, a borrower is permitted to refinance debt that is maturing no later than 90 days from the date of such refinancing.

Distributions and Compensation Limitations

The compensation limitations and distribution and stock buyback restrictions (with respect to publicly traded securities), which remain in effect during the life of the loan and one year thereafter, required by the CARES Act remain mostly unchanged by the latest guidance, which maintains the tax distribution exception. With respect to the limits on distributions, the Borrower Certifications and Covenants Instructions and Guidance clarifies that preferred stock or any other equity interest in a borrower that provides for mandatory or preferential payment of dividends or other distributions are subject to the distribution restrictions *unless* both the equity interest and the obligation to pay dividends or distributions existed as of March 27, 2020. This exception should enable borrowers to honor pre-existing mandatory distributions in their equity documents and should be carefully reviewed with eligible lenders so that loan documents permit necessary distributions.

Ongoing Reporting

Depending on the credit facility, borrowers will be required to provide substantial ongoing financial and other reporting on a quarterly and annual basis. The required reporting may exceed the scope of reporting a borrower typically expects under a credit facility. Appendix C of the FAQ "Required Financial Reporting" lists the timing and nature of financial reporting that will be required to be incorporated into the loan documentation for each Program loan. Borrowers should carefully review these requirements to ensure reporting systems are in place to timely comply with the anticipated reporting obligations.

Collateral Coverage

A new test added in the latest guidance, solely for loans under the Priority Facility, is the Collateral Coverage Ratio. If a Priority Facility loan is secured, then the Collateral Coverage Ratio for the loan at the time of origination must be either (i) at least 200% or (ii) not less than the aggregate Collateral Coverage Ratio for all of the borrower's other secured loans or debt instruments (other than mortgage debt). "Collateral Coverage Ratio" means (i) the aggregate value of any relevant collateral security, including the pro rata value of any shared collateral, divided by (ii) the outstanding aggregate principal amount of the relevant debt.

For any secured Program loans, the borrower must certify that it has provided the eligible lender with (i) good faith valuations of any collateral security for the Program loan at the time of origination of the loan, (ii) good faith valuations of any collateral security for each of the borrower's other loans or debt instruments (other than mortgage debt) at the time of origination of the Program loan, (iii) good faith calculation of the outstanding aggregate principal amount of each of the borrower's other loans or debt instruments (other than mortgage debt) at the time of loan origination, and (iv) confirmation as to whether any collateral security for the Program loan is shared collateral. Borrowers should prepare to provide these valuations and amounts in connection with their certifications to facilitate an efficient application process.

Revised Term Sheets

The Federal Reserve published revised term sheets on June 8, 2020. Depending on the facility, the changes to the terms include lowering the minimum loan amount, raising the maximum loan limit, adjusting the principal repayment schedule to begin after two years and extending the term to five years. The changes for each credit facility are shown below.

	New Loans	Priority Loans	Expand
Term	5 years (*previously 4 years*)	5 years (*previously 4 years*)	5 years (*previou*
Amortization	Amortization payments deferred two years (*previously deferred one year*) Year 3: 15% Year 4: 15% Year 5: 70% (*previously 33.33% per year amortization payments)*	Amortization payments deferred two years (*previously deferred one year*) Year 3: 15% Year 4: 15% Year 5: 70% (*previously 15%, 15%, 70% repayment due in years 2, 3, and 4, respectively*)	Amortiz two yea (*previou* Year 3: Year 4: Year 5: (*previou* *repaym* *and 4, r*
Minimum Loan Size	$250,000 (*previously $500,000*)	$250,000 (*previously $500,000*)	$10,000
Maximum Loan Size	Lesser of (i) $35 million (*previously $25 million*) or (ii) 4 times adjusted 2019 EBITDA	Lesser of (i) $50 million (*previously $25 million*) or (ii) 6 times adjusted 2019 EBITDA	Lesser c million a 2019 EB (*previou* *35% of c* *was stru*
Federal Reserve SPV Participation[5]	SPV will purchase 95% participation and Eligible Lenders will retain 5%. The Eligible Lender must retain 5% of the New Loan until it matures or the SPV sells all of its participation, whichever comes	SPV will purchase 95% participation and Eligible Lenders will retain 5%. The Eligible Lender must retain 5% of the Priority Loan until it matures or the SPV sells all of its participation, whichever	SPV wil participa tranche retain 5% must ret tranche SPV sel

first.	comes first. (*Previously risk retention by the eligible lender was 15%*)	whichev

Endnotes

1 During Q&A sessions, the Federal Reserve has indicated verbally that at this time it does not expect to publish a list of participating lenders.

2 See FAQ E.12, which discusses affiliation in some detail.

3 The Primary Market Corporate Credit Facility is another Federal Reserve program intended for investment grade issuers and borrowers.

4 *See* Main Street New Loan Facility Borrower Certifications and Covenants Instructions and Guidance, Section 3.B.

5 With respect to each facility, the sale of a participation in the eligible loan to the SPV will be structured as a “true sale” and must be completed expeditiously after the origination or upsizing of the eligible loan.

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