WINSTON & STRAWN LLP

CLIENT ALERT

Federal Reserve – May 27 Updates to the Main Street Loan Facilities

JUNE 1, 2020

On Wednesday, May 27, 2020, the Federal Reserve released additional information regarding the Main Street Lending Program to small and mid-sized businesses, including a form loan participation agreement, form borrower and lender certifications and covenants, and updated Frequently Asked Questions (FAQs). A copy of the press release can be found here.

Background

On April 30, 2020, the Federal Reserve released revised term sheets for the previously announced proposed facilities, the Main Street New Loan Facility (MSNLF) and the Main Street Expanded Loan Facility (MSELF). The Federal Reserve also released a term sheet for the proposed Main Street Priority Loan Facility (MSPLF; together with the MSNLF and the MSELF, the "Facilities"). Our summary of the Facilities can be found here.

Key Takeaways

Borrower Eligibility

Significant Operations

FAQ E.8 addresses what it means to have "significant operations in the United States." An Eligible Borrower will be considered to have "significant operations" if, on a consolidated basis together with its subsidiaries, but not its parent companies or sister affiliates, it has greater than 50% of its:

- assets located in the United States;
- annual net income generated in the United States;
- annual net operating revenues generated in the United States; or
- annual consolidated operating expenses (excluding interest expense and any other expenses associated with debt service) generated in the United States.

U.S. Subsidiaries of Foreign Companies

FAQ E.9 clarifies that a U.S. subsidiary of a foreign company may qualify as an Eligible Borrower. However, the proceeds of such an Eligible Loan may only be used for the benefit of the Eligible Borrower, its consolidated U.S. subsidiaries, and other affiliates that are U.S. businesses. The proceeds of such an Eligible Loan may not be used for the benefit of an Eligible Borrower's foreign parents, affiliates, or subsidiaries.

Maximum Loan Size

FAQ E.10 introduces limitations on the participation of affiliated Eligible Borrowers. First, if an affiliate of an Eligible Borrower is participating in one of the Facilities, the Eligible Borrower may only participate in the same Facility as its affiliate. In addition, the maximum loan size for an Eligible Borrower will be limited based on (1) its own leverage, (2) the leverage of its affiliates (on a consolidated basis), and (3) any loan(s) provided to its affiliates. The FAQ provides the following example:

In the case of the MSNLF, the Eligible Borrower's maximum loan size would be the lesser of:

1. $25 million (less any amount extended to an affiliate of the Eligible Borrower under the MSNLF);
2. an amount that, when added to the Eligible Borrower's existing outstanding and undrawn available debt, does not exceed four times the Eligible Borrower's adjusted 2019 EBITDA; or
3. an amount that, when added to the Eligible Borrower's affiliated group's existing outstanding and undrawn available debt, does not exceed four times the affiliated group's adjusted 2019 EBITDA.

Significantly, the affiliation rules under the PPP will apply for purposes of calculating the Eligible Borrower's maximum loan size. A summary of the affiliation rules under the PPP can be found here.

Facility Terms

"Priority Loans" Must Be *Pari Passu* or Senior in Security

FAQ C.6 explains that for a "Priority Loan" to meet the requirement that it be senior or *pari passu*, in terms of priority and security, with the borrower's other debt, except mortgage debt, if the "Priority Loan" is secured, the collateral coverage ratio for that loan at time of origination must be either (i) at least 200 percent or (ii) not less than that ratio for all of the borrower's other non-mortgage secured debt.

In order to comply with this requirement, loan documents must not only ensure that the "Priority Loan" does not become contractually subordinated, but also contain a lien covenant or negative pledge consistent with those used by the lender in the ordinary course of its lending to similar borrowers. The FAQs also provide a form of model lien covenant.

Lenders for "Expanded Loan" Upsized Tranches

FAQ D.4 clarifies that, to be an Eligible Lender on an Upsized Tranche on an "Expanded Loan," a lender need not have originated the underlying loan. However, if it did not do so, it must have purchased its interest in the underlying loan as of December 31, 2019.

Fees

The April 30, 2020 Term Sheets expressly permitted a lender to charge a borrower a loan origination fee and a lender to pass through to a borrower a transaction fee payable by the lender to the SPV purchasing the participation in the loan. FAQ G.12 clarifies that, although the April 30, 2020 Term Sheets did not expressly prohibit the charging of additional fees by a lender, a lender is not permitted to charge any additional fees, except *de minimis* fees for services that are customary and necessary in the lender's underwriting of loans to similar borrowers, such as appraisal and legal fees.

Certifications and Covenants (Inability to Secure Adequate Credit)

FAQ H.9 introduces a requirement that a borrower demonstrate that it is “unable to secure adequate credit accommodations from other banking institutions,” which was not a borrower requirement in the April 30, 2020 Term Sheets. The Federal Reserve explains that this does not mean that no credit from other sources is available to the borrower. Rather, the cause of the unavailability may be the amount, price, or that terms of credit available from other sources are inadequate for the borrower’s needs during the current unusual and exigent circumstances. The borrower need not demonstrate that applications for credit have been denied or otherwise document inadequacy of amounts, prices, or terms of credit available elsewhere.

Loan Participation

Elevation

The form Participation Agreement and FAQ J.4 provide that the SPV may transfer and/or elevate its participation interest in an Eligible Loan without the consent of the Eligible Lender under certain conditions, including:

- the Eligible Borrower or other obligor fails to make any payment when due, subject to any applicable grace period;
- the Eligible Borrower or Eligible Lender becomes subject to bankruptcy or other insolvency proceedings; or
- if required by any statute or court; or
- automatically if the Eligible Lender would take, or refrain from taking, an action that would result in impermissible forgiveness of principal of the portion of the Eligible Loan owned by the SPV.

FAQ J.5 clarifies that while the SPV has the right to Elevate its participation interest following a payment default, the Federal Reserve does not expect the SPV to exercise that right as a matter of course. The Federal Reserve instead expects each Eligible Lender to follow market-standard processes, using the same standard of care that the Eligible Lender exercises in connection with loans held for its own account.

SPV Voting Rights

The Participation Agreements provide that with respect to certain “Core Rights Acts,” an Eligible Lender may only act, or refrain from acting, in accordance with prior instructions of the SPV. A “Core Rights Act” is defined to include, among other things:

- extension or increase of commitments;
- reduction in principal, interest, fees, or other amounts;
- delay or postponement of any payment;
- release of all or substantially all of any collateral;
- certain waivers, modifications, or amendments;
- the exercise of certain remedies; and
- any action that would have a disproportionate adverse effect on the SPV’s participation interest.

FAQ J.6 clarifies that, in exercising its voting rights, the SPV “will make commercially reasonable decisions to protect taxpayers from losses on Main Street loans and will not be influenced by non-economic factors.”

Indemnification

The Participation Agreement provides for a broad indemnification of the Buyer by the Eligible Lender for any losses incurred as a result of, or arising out of, a breach of any of the Eligible Lender’s representations, warranties, covenants, or agreements in the Participation Agreement.

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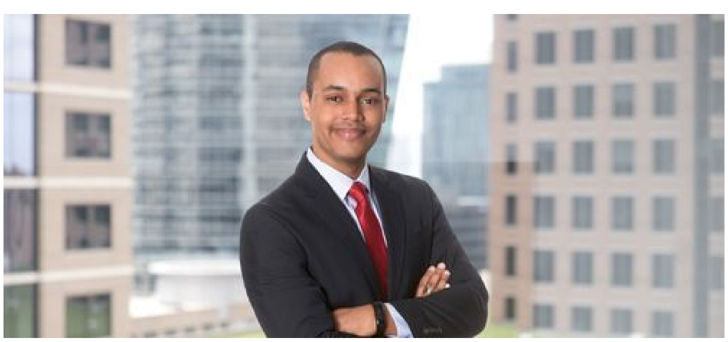

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