WINSTON & STRAWN LLP

CLIENT ALERT

Federal Reserve – Main Street Loan Facilities

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This briefing was originally written on April 10 and was updated on June 9.

On Monday, June 8, 2020, the Federal Reserve released additional information regarding the Main Street Lending Program to small and mid-sized businesses, including updated term sheets and Frequently Asked Questions. Copies of the term sheets can be found here. Updated summaries of the Facilities are set forth below.

Overview

The Facilities, which will be funded up to $600 billion in total, will facilitate lending to businesses by eligible lenders (Eligible Lenders). Under the Facilities, the Federal Reserve Bank of Boston (Reserve Bank) will lend to a single common special purpose vehicle (SPV) on a recourse basis, and the SPV will purchase participations in eligible loans (Eligible Loans). Eligible Lenders must retain 5% of each Eligible Loan. The Department of the Treasury will also make a $75 billion equity investment in the SPV using funds appropriated under the Coronavirus Aid, Relief, and Economic Security Act (CARES Act).

Eligible Lenders

Eligible Lenders are U.S.-insured depository institutions, U.S. branches or agencies of a foreign banks, U.S. bank holding companies, U.S. savings and loan holding companies, U.S. intermediate holding companies of foreign banking organizations, or U.S. subsidiaries of any of the foregoing.

Eligible Borrowers

Eligible borrowers (Eligible Borrowers) are for-profit businesses:

- that are established prior to March 13, 2020;

- that are not considered an Ineligible Business for purposes of the U.S. Small Business Administration's Paycheck Protection Program (PPP) on or before April 24, 2020 (a summary of ineligible businesses for purposes of the PPP can be found here);
- with up to either (i) 15,000 employees or (ii) $5 billion in 2019 annual revenues;
- that are created or organized in or under the laws of the United States and have significant operations in, and a majority of its employees based in, the United States;
- that only participate in one of the Facilities or the Primary Market Corporate Credit Facility; and
- have not received specific support pursuant to the Coronavirus Economic Stabilization Act of 2020.

Observations

- The affiliation rules under the PPP will apply for purposes of calculating a business's employees and annual revenues. A summary of the affiliation rules under the PPP can be found here.
- Certain sponsor-backed portfolio companies may be ineligible due to PPP affiliation rules and the leverage conditions set forth below.
- Borrowers participating in the PPP are eligible for participation in the Facilities.
- 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.

Eligible Loans

The terms of Eligible Loans are as follows:

- In the case of loans under all Facilities:
  - full-recourse and are not forgivable;
  - five-year maturity;
  - principal payments deferred for two years and interest payments deferred for one year (unpaid interest will be capitalized);
  - an adjustable rate of LIBOR (1- or 3-month) + 300 basis points; and
  - no prepayment penalties.
- In the case of loans under the Main Street New Loan Facility (MSNLF):
  - originated after April 24, 2020;
  - secured or unsecured;
  - principal amortization of 15% at the end of the third year, 15% at the end of the fourth year, and a balloon payment of 70% at maturity at the end of the fifth year;
  - minimum loan size of $250,000;
  - maximum loan size that is the lesser of (i) $35 million or (ii) an amount that, when added to the Eligible Borrower's existing outstanding and undrawn available debt, does not exceed 4x the Eligible Borrower's 2019 EBITDA (the "MSNLF EBITDA Leverage Condition"); and
  - is not, at the time of origination or at any time during the term of the Eligible Loan, contractually subordinated in terms of priority to any of the Eligible Borrower's other loans or debt instruments.

- In the case of loans under the Main Street Priority Loan Facility (MSPLF):
  - originated after April 24, 2020;
  - secured or unsecured;
  - principal amortization of 15% at the end of the third year, 15% at the end of the fourth year, and a balloon payment of 70% at maturity at the end of the fifth year;
  - minimum loan size of $250,000;
  - maximum loan size that is the lesser of (i) $50 million or (ii) an amount that, when added to the Eligible Borrower's existing outstanding and undrawn available debt, does not exceed 6x the Eligible Borrower's 2019 EBITDA (the "MSPLF EBITDA Leverage Condition"); and
  - at the time of origination and at all times the Eligible Loan is outstanding, the Eligible Loan is 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.
- In the case of loans under the Main Street Expanded Loan Facility (MSELF):
  - originated on or before April 24, 2020 and that has a remaining maturity of at least 18 months (taking into account any adjustments made to the maturity of the loan after April 24, 2020, including at the time of upsizing);
  - secured or unsecured term loan or revolving credit facility made by an Eligible Lender (provided that any collateral securing the Eligible Loan must secure the upsized tranche on a pro rata basis);
  - principal amortization of 15% at the end of the third year, 15% at the end of the fourth year, and a balloon payment of 70% at maturity at the end of the fifth year;
  - minimum loan size of $10 million;
  - maximum loan size that is the lesser of (i) $300 million or (ii) an amount that, when added to the Eligible Borrower's existing outstanding and undrawn available debt, does not exceed 6x the Eligible Borrower's 2019 EBITDA (the "MSELF EBITDA Leverage Condition"); and
  - at the time of upsizing and at all times the upsized tranche is outstanding, the upsized tranche is 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.

Observations

- 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 Federal Reserve provides the following example:

  In the case of the MSNLF, the Eligible Borrower's maximum loan size would be the lesser of:
  - $35 million (less any amount extended to an affiliate of the Eligible Borrower under the MSNLF);
  - 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
  - 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.
- If an Eligible Borrower is the only business in its affiliated group that seeks funding under a Facility, the affiliation rules under the PPP will not apply for purposes of calculating the Eligible Borrower's maximum loan size. However, if an affiliate of an Eligible Borrower is seeking funding under a Facility, the entire affiliated group's debt and EBITDA are relevant for calculating the Eligible Borrower's maximum loan size.
- The Term Sheets reference an Eligible Borrower's adjusted EBITDA, which must be one of the following:

- With respect to the MSNLF and the MSPLF, a methodology that the Eligible Lender previously used for adjusting EBITDA when extending credit to the Eligible Borrower or a similarly situated borrower on or before April 24, 2020; or
- With respect to the MSELF, the methodology used for adjusting EBITDA when originating the underlying Eligible Loan.

Required Certifications and Covenants

In addition to certifications under applicable law, the following certifications and covenants will be required with respect to each Eligible Loan or the upsized tranche of each Eligible Loan:

- By Eligible Borrowers:
  - It must commit that the proceeds of the Eligible Loan or the upsized tranche of the Eligible Loan will not be used to (i) repay the principal balance of or (ii) repay any interest on, any debt until the Eligible Loan is repaid in full, unless the debt or interest payment is mandatory and due. However, for the MSPLF, the Eligible Borrower may, at the time of origination of the Eligible Loan, refinance existing debt owed by the Eligible Borrower to a lender that is not the Eligible Lender.
  - It must commit that it will not seek to cancel or reduce any of its committed lines of credit with the Eligible Lender or any other lender.
  - It must 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.
  - It must 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.
    - Those restrictions, until 12 months after the loan is no longer outstanding, (i) prohibit increases in compensation for employees who received total compensation of more than $425,000 in 2019 and (ii) require reduction in total compensation of employees whose 2019 total compensation exceeded $3,000,000.
    - They also prohibit, until 12 months after the loan is no longer outstanding, repurchase of stock by borrowers that are publicly traded companies.
    - They also prohibit, until 12 months after the loan is no longer outstanding, the payment of dividends or other capital distributions on common stock.
  - It must certify that it is eligible to participate in the applicable Facility, including in light of the conflicts of interest prohibition in Section 4019(b) of the CARES Act (the "Conflicts of Interest Prohibition").
  - It must demonstrate that it is "unable to secure adequate credit accommodations from other banking institutions." 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 that 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. It need not demonstrate that applications for credit have been denied or otherwise document inadequacy of amounts, prices, or terms of credit available elsewhere.
- By Eligible Lenders:
  - It must commit that it will not request that the Eligible Borrower repay debt extended by the Eligible Lender to the Eligible Borrower, or pay interest on such outstanding obligations, until the Eligible Loan is repaid in full, unless the debt or interest payment is mandatory and due, or in the case of default and acceleration.

    - It must commit that it will not cancel or reduce any existing committed lines of credit to the Eligible Borrower, except in an event of default.
    - It must certify that the methodology used for calculating the MSNLF EBITDA Leverage Condition, the MSPLF EBITDA Leverage Condition, and the MSELF EBITDA Leverage Condition, as applicable, is the methodology it has previously used for adjusting EBITDA when extending credit to the Eligible Borrower or similarly situated borrowers on or before April 24, 2020.
    - It must certify that it is eligible to participate in the applicable Facility, including in light of the Conflicts of Interest Prohibition.

Observations

- With respect to the MSELF, if the Eligible Loan is a multi-lender facility, the Eligible Lender must be one of the lenders in the facility. Other members of the facility are not required to be Eligible Lenders. The Eligible Lender may not share its 5% retention with other members of a multi-lender facility.

Retention of Employees

Each Eligible Borrower that participates in a Facility must make commercially reasonable efforts to maintain its payroll and retain its employees during the time the Eligible Loan is outstanding. Borrowers that have already laid off or furloughed workers as a result of COVID-19 are eligible to apply to a Facility.

Loan Classifications and Assessment of Financial Conditions:

- In the case of loans under MSNLF and MSPLF:
    - If the Eligible Borrower had other loans outstanding with the Eligible Lender as of December 31, 2019, such loans must have had an internal risk rating equivalent to a “pass” in the Federal Financial Institutions Examination Council’s supervisory rating system on that date.
- In the case of loans under MSELF:
    - The Eligible Loan must have had an internal risk rating equivalent to a “pass” in the Federal Financial Institutions Examination Council’s supervisory rating system as of December 31, 2019.
- In the case of loans under all Facilities:
    - Eligible Lenders are expected to conduct an assessment of each potential borrower’s financial condition at the time of the potential borrower’s application.

Fees Under MSNLF and MSPLF

- Transaction Fee:
    - Eligible Lenders must pay the SPV a transaction fee of 100 basis points of the principal amount of the Eligible Loan at the time of origination. Eligible Lenders may require their Eligible Borrowers to pay this fee.
- Loan Origination and Servicing Fee
    - An Eligible Borrower will pay an Eligible Lender an origination fee up to 100 basis points of the principal amount of the Eligible Loan.
    - The SPV will pay an Eligible Lender 25 basis points of the principal amount of its participation in the Eligible Loan per year for loan servicing.

Fees Under MSELF

- Transaction Fee:
  - Eligible Lenders must pay the SPV a transaction fee of 75 basis points of the principal amount of the upsized tranche of the Eligible Loan at the time of upsizing. Eligible Lenders may require their Eligible Borrowers to pay this fee.
- Upsizing and Servicing Fees:
  - An Eligible Borrower will pay an Eligible Lender an origination fee up to 75 basis points of the principal amount of the upsized tranche of the Eligible Loan at the time of upsizing.
  - The SPV will pay an Eligible Lender 25 basis points of the principal amount of its participation in the upsized tranche of the Eligible Loan per year for loan servicing.

Observations

- An Eligible 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. An Eligible Lender may also charge customary consent fees if such fees are necessary to amend existing loan documentation in the context of upsizing a loan in connection with the MSELF.

Termination of the Facilities

- The SPV will cease purchasing participations in Eligible Loans under each Facility on September 30, 2020, unless the Board of Governors of the Federal Reserve System (Board) and the Treasury Department extend either Facility.
- Notwithstanding the above, the Reserve Bank will continue to fund the SPV after such date until the SPV's underlying assets mature or are sold.

The Board and the Secretary of the Treasury may make adjustments to the terms and conditions set forth above, and any changes will be announced by the Board.

Practical Suggestion

While a launch date for the Facilities has not yet been announced, potential borrowers are encouraged to contact their relationship managers at their banks now to get in the queue and be ahead of the curve.

View all of Winston & Strawn's COVID-19 perspectives here. Contact a member of our COVID-19 Legal Task Force here.

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