

Federal Reserve Announces Expansion of Main Street Lending Program

by Erik Detlefsen and Troy M. Keller

On April 30, the Federal Reserve announced an expansion of its Main Street Lending Program. The changes modified the eligibility criteria and increased the scope of the facilities in an effort to augment the flow of credit to small and medium-sized businesses.

Guidance from the Federal Reserve indicates further changes may be coming. In his April 29 press conference, Federal Reserve Chair Powell commented that “it is very likely that [the Federal Reserve] will continue to add different kinds of loan products to the Main Street Facilities to accommodate different types of companies and needs.”

Dorsey will continue to monitor pronouncements from the Federal Reserve and will provide additional updates as appropriate. The following are the main takeaways from the revised Main Street Lending Program:

Eligibility Criteria

- **Expanded Borrower Eligibility.** Borrowers will now be eligible if they either have 15,000 or fewer employees, or \$5 billion or less of revenue in 2019. These criteria represent at 50% increase in the permitted number of employees and a 100% increase in the permitted amount of revenue.
- **New Limitations on Borrower Eligibility.** The revised terms of the Main Street program import several provisions from SBA regulations. No company is eligible for the Main Street program if it is an “Ineligible Business” as determined by SBA regulations. In addition, the number of employees will be determined using the SBA method for calculating employees, including the rules for counting affiliate employees. However, it appears that the relief to the affiliate rules granted in the Paycheck Protection Program will not apply to the Main Street program. The program continues to be limited to businesses created or organized in the United States or under the laws of the United States with significant operations in and a majority of its employees based in the United States.
- **Expanded Lender Eligibility.** Eligible lenders now include U.S. branches or agencies of foreign banks, U.S. intermediate holding companies of foreign banking organizations, or any U.S. subsidiary of any of the foregoing. As under the initial proposal, eligible lenders also include U.S. federally-insured depository institutions

Related People

- Erik Detlefsen
- Troy M. Keller

Related Capabilities

- Banking & Financial Institutions
- Bankruptcy & Financial Restructuring
- Consumer Financial Services

(including banks, savings associations, and credit unions), U.S. bank holding companies and U.S. savings and loan holding companies and their subsidiaries. At this time, nonbank financial institutions are not considered eligible lenders for purposes of the Main Street program. However, the Federal Reserve indicated that it may consider expanding eligibility to encompass nonbank lenders, but offered no details on when or if such changes will be considered.

- Prohibition on Lender Assignment. No lender may assign its Main Street loan until the Federal Reserve's SPV sells its entire participation interest. In addition, the lender for a loan which adds to an existing credit facility or term loan may not assign such underlying credit facility of term loan (subject to certain exceptions).

Loan Terms

- Three Lending Categories. The Main Street program now includes three loan types:
 - Priority Loans (*this facility was added in the revisions*). Minimum size of \$500,000, maximum size \$25 million. Priority Loans cannot exceed 6x adjusted EBITDA. Borrowers are permitted to refinance existing third party debt. The lender must retain 15% of the loan.
 - New Loans. Minimum size of \$500,000 (down from \$1 million), maximum size \$25 million. New Loans cannot exceed 4x adjusted EBITDA. Borrowers are not permitted to refinance any debt. The lender must retain 5% of the loan.
 - Expanded Loans. This loan must be an increase to an existing credit facility (revolving or term loan). Minimum size of \$10,000,000, maximum size the lesser of (i) \$200 million, or (ii) 35% of outstanding and undrawn available debt. Expanded Loans cannot exceed 6x adjusted EBITDA. Borrowers are not permitted to refinance any debt. The lender must retain 5% of the loan.
- Additional Loan Terms.
 - Each loan has a four year maturity, with payments of interest and principal deferred for the first year of the loan.
 - Each loan will use an adjustable interest rate of LIBOR + 3%. The Federal Reserve abandoned its initial proposal to require the use of SOFR.
 - Amortization for Priority and Expanded Loans will be 15% of principal due at the end of year 2, 15% of principal due at the end of year 3, and a balloon payment of 70% of principal due at maturity at the end of year 4. Amortization for New Loans will be one-third of principal due at the end of each of years 2 and 3, and one-third due at maturity at the end of year 4.
 - New and Priority Loans may be secured or unsecured (the initial proposal required New Loans to be unsecured). Expanded Loans must take the collateral position of the underlying facility being expanded.
 - Loans may be prepaid without penalty.
 - The Federal Reserve (through a special purpose vehicle) will purchase from the lender a participation interest in the loan (95% for New and Expanded Loans, 85% for Priority Loans).
- Permitted Use of Adjusted EBITDA. The Federal Reserve clarified that borrowers may use an adjusted EBITDA. The methodology used to calculate adjusted EBITDA must be the methodology the lender has previously used for adjusting EBITDA when extending credit to the borrower or similarly situated borrowers on or before April 24, 2020. For Expanded Loans, it seems relatively straight forward that the definition of adjusted EBITDA in existing agreements would be carried forward to the new Expanded Loans. For New or Priority Loans, it remains to be seen how parties will

negotiate adjusted EBITDA to meet the “similarly situated borrower” criteria.

- **Operational Restrictions on Borrowers.** The compensation, stock repurchase, and capital distribution restrictions that apply to direct loan programs under the CARES Act apply to loans under the Main Street program. However, restrictions on dividends and other capital distributions will not apply to distributions made by an S corporation or other tax pass-through entity to the extent reasonably required to cover its owners’ tax obligations in respect of the entity’s earnings. In general, borrowers may not make voluntary or elective payments of principal or interest on existing debt until Main Street loans are paid in full (scheduled interest and principal payments are permitted). For Priority Loans, the borrower may refinance existing debt to a lender other than the lender of the Priority Loan. The prohibition on debt payments would not prevent a borrower from (i) repaying a line of credit in the borrower’s normal course of business for such line of credit; (ii) taking on and paying additional debt obligations required in the normal course of business and on standard terms, including inventory and equipment financing; or (iii) refinancing maturing debt. Borrowers may obtain loans in only one of the three facilities under the Main Street program. Borrowers, however, may separately receive forgivable loans under the Paycheck Protection Plan, but not any other form of assistance under the CARES Act.
- **Covenants by Borrowers.** Borrowers must make commercially reasonable efforts to maintain payroll and retain employees during the term of any Main Street loan. Borrowers that have already laid-off or furloughed workers as a result of the disruptions from COVID-19 are eligible to apply for Main Street loans. Notably, borrowers will not be required to certify that they are unable to obtain alternative sources of financing due to the impact of COVID-19 on their businesses. Borrowers will also be required to certify that they reasonably expect to meet their financial obligations for 90 days and do not expect to file for bankruptcy during that time. In addition, borrowers will be subject to the conflict of interest prohibitions of the CARES Act.

Logistics and Timing

- **Timing.** The Main Street program is not yet operating. Updates regarding the Main Street Program, including the official launch date will be made on the Federal Reserve’s Main Street page.
- **Bank Discretion.** Even though a borrower may satisfy all the conditions outlined in the Main Street program to receive a loan, each lender must conduct an assessment of each borrower’s financial condition. Lenders have full discretion whether to actually extend loans to borrowers. It is anticipated that lenders will apply their own underwriting, informational and documentation requirements.
- **Fees.** Borrowers will be required to pay a separate transaction fee and loan origination fee on Main Street loans. The transaction fee and loan origination fee will each be 100 basis points on the principal amount for New and Priority Loans and 75 basis points for Expanded Loans. In addition, the lender will receive a 25 basis point annual fee for servicing the loans.

The Main Street Lending Program is complex and fluid, but the latest updates suggest the Federal Reserve is committed to making the Main Street Lending Program available to a range of small and mid-sized business. The highlights provided in this update are not an exhaustive review of the Main Street program and its terms. Dorsey has a team of attorneys following the updates and market reaction. We would be pleased to discuss if you have any questions.

