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Client Alert

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Federal Reserve System Announces Main Street Loan Facilities to Support Small and Medium-Sized Businesses

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Background

On April 9, 2020, the Board of Governors of the Federal Reserve System (the "**Fed**") announced a series of financing programs to provide up to $2.3 trillion in loans to support the U.S. economy.[1] Among those programs authorized under section 13(3) of the Federal Reserve Act are the Main Street Expanded Loan Facility (the "**MS Expanded Facility**") and the Main Street New Loan Facility (the "**MS New Facility**," and together with the MS Expanded Facility, the "**Main Street Facilities**"). The combined size of the Main Street Facilities will be up to $600 billion, nearly double the size of the Small Business Administration's Paycheck Protection Program.[2] The Main Street Facilities are intended to facilitate new and upsized lending to certain small and medium-sized businesses suffering financial harm from fallout of the coronavirus disease 2019 ("**COVID-19**").[3]

How Do the Main Street Facilities Work?

To fund the Main Street Facilities, the United States Department of the Treasury ("**Treasury**") using funds appropriated to the Exchange Stabilization Fund established under section 4027 of the Coronavirus Aid, Relief, and Economic Security Act ("**CARES Act**"), will make a $75 billion equity investment in a single common special purpose vehicle (the "**SPV**"). A Federal Reserve Bank (a "**Reserve Bank**") will then commit to lend to the SPV on a recourse basis. Under the MS Expanded Facility, the SPV will purchase 95 percent direct participation interests in the upsized tranches of certain eligible loans, while under the MS New Facility, the SPV will purchase 95 percent direct participation interests in eligible loans. In each case, an eligible lender will retain the remaining five percent participation interest in, and will service, the underlying loan. The SPV will cease purchasing participations on September 30, 2020, unless the Fed and Treasury extend the Main Street Facilities.

What Lenders are Eligible?

Lenders are eligible to participate in the Main Street Facilities if they are United States insured depository institutions, United States bank holding companies, or United States savings and loan holding companies.

What Borrowers are Eligible?

Borrowers are eligible to participate in the Main Street Facilities if they either (i) employ 10,000 or fewer individuals or (ii) earned $2.5 billion or less in 2019 annual revenues. Borrowers must also be created or organized under the laws of the United States and they must have significant operations and a majority of their employees in the United States. Moreover, a borrower cannot participate in both Main Street Facilities; it must select between the two programs. Notably, however, the Fed Press Release stated that borrowers who are participating in the Small Business Administration's Paycheck Protection Program may also participate in the Main Street Facilities.

What Types of Loans Are Eligible?

Under the Main Street Facilities, loans eligible for participation by the SPV must meet the following criteria:

1. A four-year maturity;
2. An amortization of principal and interest deferred for one year;
3. An adjustable rate of the secured overnight financing rate ("**SOFR**"),[4] plus 2.5–4 percent;
4. A minimum loan size of $1 million; and
5. Prepayment permitted, without penalty.

Additionally, MS Expanded Facility-eligible loans (which are the upsized tranche of existing loans) must meet the following criteria:

- A term loan that originated prior to April 8, 2020,[5] and
- A maximum loan size that is the lesser of:
  - $150 million;
  - 30 percent of the borrower's existing outstanding and committed but undrawn bank debt; or
  - an amount that, when added to the borrower's existing outstanding and committed but undrawn debt, does not exceed six times the borrower's 2019 earnings before interest, taxes, depreciation, and amortization ("**EBITDA**").

By contrast, MS New Facility-eligible loans must meet the following criteria:

- An *unsecured* term loan that originated on or after April 8, 2020, and
- A maximum loan size that is the lesser of:
  - $25 million, or
  - an amount that, when added to the borrower's existing outstanding and committed but undrawn debt, does not exceed four times the borrower's 2019 EBITDA.

What are the Other Conditions on Participation?

Participation in the Main Street Facilities is subject to the following additional criteria (presented in summary):

1. Neither the lender nor the borrower can permit the loan proceeds to be used to pay down or refinance existing lines of credit or other preexisting loans;
2. Neither the lender nor the borrower can permit the borrower to cancel or reduce any existing lines of credit;
3. The borrower must attest that financing is required in response to exigent circumstances triggered by COVID-19;
4. The borrower must attest to use reasonable efforts to maintain payroll and retain employees during the loan term;
5. The borrower must attest that it complies with the applicable EBITDA test, enumerated above;
6. The borrower must attest that it will comply with the compensation, stock repurchase, and capital distribution restrictions that apply to direct loan programs under section 4003(c)(3)(A)(ii) of the CARES Act; and
7. Both the borrower and the lender must certify eligibility to participate in the Main Street Facilities, with reference to the conflicts of interest prohibition in section 4019(b) of the CARES Act.[6]

What Fees are Involved?

For the New Loan Facility, the lender must pay the SPV a one percent facility fee based on the SPV's original participation amount, which may be collected from the borrower.

Under both of the Main Street Facilities, the borrower must pay the lender a one percent upsizing or origination fee based on the total term loan or upsizing tranche amount, as applicable. The SPV will pay the lender an annual 0.25 percent servicing fee based on the SPV's participation amount.

Shumaker's Financial Services Practice Group has extensive experience in representing both financial institutions and commercial borrowers in a variety of transactions and structures, in all areas of commercial lending. Please contact us if you have questions regarding this Client Alert or if we can be of assistance in reviewing loan documentation and advising of potential courses of action.

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[1] Press Release, Board of Governors of the Federal Reserve System, Federal Reserve takes additional actions to provide up to $2.3 trillion in loans to support the economy (Apr. 9, 2020, 8:30 AM), https://www.federalreserve.gov/newsevents/pressreleases/monetary20200409a.htm [hereinafter the Fed Press Release].

[2] Press Release, United States Department of Treasury, With $349 Billion in Emergency Small Business Capital Cleared, Treasury and SBA Begin Unprecedented Public-Private Mobilization Effort to Distribute Funds (Mar. 31, 2020), https://home.treasury.gov/news/press-releases/sm961.

[3] Note, the Fed Press Release contained the following cautionary footnote: "The Board of Governors of the Federal Reserve System ("Board") and Secretary of the Treasury may make adjustments to the terms and conditions described in this term sheet. Any changes will be announced on the Board's website." Thus, this alert and the information contained herein are qualified by that same warning.

[4] Note, that this appears to be an attempt by the Fed to push SOFR as its preferred replacement for LIBOR (the London Inter-Bank Offered Rate) which is the current most-widely used interest index in both domestic and foreign loan markets, and which is anticipated to be phased out at the end of 2021 (See, Shumaker Client Alert of May 14, 2019, What to do about the Libor Time Bomb? ARRC Adopts Recommended Fall-Back Language for Libor Based Credit Facilities, https://www.shumaker.com/latest-thinking/publications/2019/05/client-alert-what-to-do-about-the-libor-time-bomb-arrc-adopts-recommended-fall-back-language-for-libor-based-credit-facilities).

[5] We understand this to mean that the original loan was closed prior to April 8, 2020, and that the increased tranche may be closed on or after April 8, 2020; otherwise, the requirement that the loan bear interest at a SOFR-based rate would severely limit this program's viability.

[6] For additional information on the CARES Act, please refer to Shumaker's COVID-19 crisis center and the client alerts detailing the CARES Act.

For the most up-to-date legal and legislative information related to the coronavirus pandemic, please visit our Shumaker COVID-19 Client Resource Center at shumaker.com. We have also established a 24/7 Legal & Legislative Helpline at 1.800.427.1493 monitored by Shumaker lawyers around the clock.

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