

FRB Releases Updated FAQ Regarding The “Main Street Lending Program”

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The “Main Street Lending Program” (*the “Program”*) was established by the Federal Reserve Board (*the “FRB”*) to support lending to small and medium-sized businesses that were in sound financial condition prior to the onset of the COVID-19 pandemic. Under the Program, which was authorized under Title IV the “Coronavirus Aid, Relief, and Economic Security Act” (*the “CARES Act”*) and previously announced on April 9, 2020, the FRB has currently allocated \$600 billion in funds to indirectly facilitate loans to eligible borrowers.

Overview

Initially, the FRB had announced that it would establish two different loan facilities under the Program. However, in later guidance released in late April, the FRB established a third loan facility. As discussed below, all three facilities have the same qualifications for determining eligible lenders (*each an “Eligible Lender”*) and eligible borrowers (*each an “Eligible Borrower”*). The following is a brief description of the three loan facilities currently provided for under the Program:

- **Main Street New Loan Facility** (*a/k/a MSNLF; a “New Loan”*) – This refers to a new loan made by an Eligible Lender to an Eligible Borrower which is structured to meet the requisite New Loan terms, as discussed below. For clarity, a New Loan can be made to either an existing or new customer of an Eligible Lender, as long as it is a new facility. **The total amount of a New Loan can range from \$250k to \$35M** (*subject to a 4x borrower’s 2019 EBITDA cap, as discussed below*).
- **Main Street Priority Loan Facility** (*a/k/a MSPLF; a “Priority Loan”*) – Like the new loan described above, this refers to a new loan made by an Eligible Lender to an Eligible Borrower, but is structured to meet the requisite Priority Loan terms, as discussed below. In general, Priority Loans carry many of the same terms as New Loans; including the fact that **the total amount of a Priority Loan can range from \$250k to \$50M**. However, there are certain variations, which may make them more favorable to Eligible Borrowers (*including a higher loan amount cap of 6x borrower’s 2019 EBITDA, as discussed below*).

- **Main Street Expanded Loan Facility** (a/k/a MSELF; an “**Expanded Loan**”) – This refers to a situation where an Eligible Borrower has an existing loan with an Eligible Lender and the parties agree to roll such loan into (and generally increase the principal amount of such loan pursuant to the terms of) a loan which is structured to meet the requisite Expanded Loan terms, as discussed. **The total amount of an Expanded Loan can range from \$10M to \$300M** (subject to a 6x borrower’s 2019 EBITDA cap and an available funds cap, as discussed below).

For clarity, it should be noted that the FRB is not making loans directly to borrowers. Administratively speaking, essentially the Program will work as follows. Eligible Lenders will underwrite, and fund loans under the Program to, Eligible Borrowers. The FRB (through a newly created “special purpose vehicle” created by the Federal Reserve Bank of Boston) will then buyback between 85%-95% (depending on the loan facility) of such Program loans made by Eligible Lenders.

Comparison of Other Loan Terms

While similar in several respects, each of the Program facilities has its own terms and conditions. For a breakdown of the respective terms of each Program facility, including a comparison matrix of such terms, please see [The “Main Street Lending Program”: What It Is and How It Works](#).

Frequently Asked Questions

With respect to the Program, the FRB has released a detailed, 63 page, set of “[Frequently Asked Questions](#)” (as most recently released on June 8, 2020; the “FAQ”). While inevitably the FAQ does not answer all questions which might arise in connection with the Program, it is well organized, provides breakdowns of questions with respect to each facility, and is relatively easy to follow.

Below are summaries of the questions/answers provided in the FAQ with respect to some of the more commonly asked questions concerning borrowers.

1. What types of businesses are eligible to apply for a Program loan?

Currently, in order for a borrower to be eligible to receive a Program loan, all of the following must be satisfied:

- such borrower must:
 - have been established prior to March 13, 2020;
 - an entity organized for profit as a partnership, a limited liability company, a corporation, an association, a trust, a cooperative, a joint venture with no more than 49% participation by foreign business entities, or a tribal business concern;¹
 - be created or organized in the United States or under the laws of the United States and have a majority of its business operations and employees based in the United States;
 - have been in sound financial condition prior to the onset of the COVID-19 pandemic;
 - either, when calculated together with its “affiliates”;² (a) have less than 15,000 employees; or (b) have had 2019 annual revenues of \$5 Billion, or less; and
 - be able to both make the required certifications and comply with the required covenants
- such borrower must not:

¹ It should be noted that the FAQ specifically provides that other forms of entities may be considered by the FRB for participation in the Program. Moreover, as discussed herein, not-for-profit entities may soon be able to participate in a separate Program facility.

² The Program incorporates the U.S. Small Business Administration’s affiliation test set forth in 13 CFR 121.301(f) for purposes of this affiliation analysis. As such, determining the total number of employees a particular borrower has will be similar to how such determination is made with respect to PPP Loans and would include all full-time, part-time, seasonal, or otherwise employed persons, excluding volunteers and independent contractors. Please note, determining potential “affiliate” relationships, and the resulting number of employees/consolidated revenues, utilizing the foregoing rules requires a highly detailed and fact specific analysis. As such, we highly recommend that potential borrower’s contact a qualified attorney to assist them in making this determination.

- have received other specific support under the CARES Act (*other than an “Economic Injury Disaster Loan” (EIDL) or “Paycheck Protection Program” (PPP) loan*);
- be a “Covered Entity;” meaning that no “Covered Individual”³ owns, controls, or holds 20% or more (*by vote or value*) of any class of equity ownership interest in such borrower; or
- qualify as an Ineligible Business (*as defined below*)

Please note that an Eligible Borrower may only participate in one of the available Program facilities. Further, an eligible borrower that gets a Program loan cannot subsequently apply for/receive economic support from the FRB or otherwise under the CARES Act (*other than EIDL and/or PPP loans*).

2. What types of businesses are ineligible to apply for a Program loan?

The FAQ specifically provides that a borrower whose business qualifies as any of the following (*each, an “Ineligible Business”*)⁴ will not be eligible to apply for/receive a Program loan:

- non-profit businesses (*except for those specifically permitted under the CARES Act*), however for-profit subsidiaries are eligible;
- financial businesses primarily engaged in the business of lending, such as banks, finance companies, and factors (*pawn shops, although engaged in lending, may qualify in some circumstances*);
- passive businesses owned by developers and landlords that do not actively use or occupy the assets acquired or improved with the loan proceeds (except Eligible Passive Companies under [13 CFR 120.111](#));
- life insurance companies;
- businesses located in a foreign country (*although businesses in the U.S. owned by aliens may qualify*);
- pyramid sale distribution plans;
- businesses deriving more than one-third of gross annual revenue from legal gambling activities;
- businesses engaged in any illegal activity;
- private clubs and businesses which limit the number of memberships for reasons other than capacity;
- government-owned entities (*except for businesses owned or controlled by a Native American tribe*);
- businesses principally engaged in teaching, instructing, counseling or indoctrinating religion or religious beliefs, whether in a religious or secular setting;
- loan packagers earning more than one third of their gross annual revenue from packaging SBA loans;
- businesses with an associate who is incarcerated, on probation, on parole, or has been indicted for a felony or a crime of moral turpitude;
- Businesses in which the lender or CDC, or any of its associates, owns an equity interest;
- businesses which:

³ Meaning the President, the Vice President, the head of any Executive Department, any Member of Congress, and certain immediate family members of the foregoing.

⁴ The FAQ requires that the borrower not be an “ineligible business” of a type identified in any of sections (b)-(j) or (m)-(s) of 13 CFR 120.110 (as such rules are modified and clarified by the SBA for purposes of the PPP).

- present live performances of a prurient sexual nature; or
- derive directly or indirectly more than de minimis gross revenue through the sale of products or services, or the presentation of any depictions or displays, of a prurient sexual nature;
- unless waived by SBA for good cause, businesses that have previously defaulted on a federal loan or federally assisted financing, resulting in the federal government or any of its agencies or departments sustaining a loss in any of its programs, and businesses owned or controlled by an applicant or any of its associates which previously owned, operated, or controlled a business which defaulted on a federal loan (*or guaranteed a loan which was defaulted*) and caused the federal government or any of its agencies or departments to sustain a loss in any of its programs. for purposes of this section, a compromise agreement shall also be considered a loss;
- businesses primarily engaged in political or lobbying activities; and/or
- speculative businesses (*including private equity and hedge funds*).

3. Can multiple affiliated borrowers apply for/receive a Program loan?

If any affiliate of a borrower has participated in the the [“Primary Market Corporate Credit Facility”](#) (*the “PMCCF”*), then such borrower will not be eligible to apply for/receive a Program loan.

Assuming the above does not apply, it is possible for multiple affiliated borrowers to independently apply for/receive a Program loan, provided that:

- all entities must apply for/receive the same type of Program loan;
- the aggregate amount of all Program loans made to the affiliated entities cannot exceed the maximum Program loan amount that the entire affiliated group would be eligible to received on a consolidated basis.

It should be noted that, without further guidance this rule will effectively limit the ability of portfolio companies of private equity/venture capital firms to access Program loans.

4. What is the term of, and interest rate on, a Program loan?

Each Program loan will be for a 5-year term and carry an interest rate equal to the LIBOR rate (*one or three months, as determined by the respective lender*) in effect as of the origination date of the loan + 3%.

It should be also noted that the FRB contemplates the potential phase out of the LIBOR interest rate but has yet to specify the terms with respect to the replacement of such interest rate in the event it is phased out.

5. What is the maximum amount that can be borrowed under a Program loan?

The maximum amount a borrower can borrow under a Program loan will be determined on a borrower-by-borrower basis and will be based on the following 3 factors:

- what type of Program loan they are applying for;
- the aggregate amount of the subject borrower’s “existing outstanding and undrawn available debt” (*as discussed in more detail below*) as of the application date; and
- the subject borrower’s 2019 “adjusted EBITDA” (*as discussed in more detail below*).

More specifically, the maximum amount of a Program loan will be determined based on the following:

New Loan	Priority Loan	Expanded Loan
<p>Maximum loan amount will be the <u>lesser of</u>:</p> <ul style="list-style-type: none"> • <u>\$35 million</u>; or • an amount equal to the result of: <ul style="list-style-type: none"> • <u>4x</u> the subject borrower's 2019 "adjusted EBITDA;" <u>minus</u> • the aggregate amount of the subject borrower's then "existing outstanding and undrawn debt" 	<p>Maximum loan amount will be the <u>lesser of</u>:</p> <ul style="list-style-type: none"> • <u>\$50 million</u>; or • an amount equal to the result of: <ul style="list-style-type: none"> • <u>6x</u> the subject borrower's 2019 "adjusted EBITDA;" <u>minus</u> • the aggregate amount of the subject borrower's then "existing outstanding and undrawn debt" 	<p>Maximum loan amount will be the <u>lesser of</u>:</p> <ul style="list-style-type: none"> • <u>\$200 million</u>; or • an amount equal to the result of: <ul style="list-style-type: none"> • <u>6x</u> the subject borrower's 2019 "adjusted EBITDA;" <u>minus</u> • the aggregate amount of the subject borrower's then "existing outstanding and undrawn debt"

6. How is "adjusted EBITDA" calculated for purposes of determining Program loan caps?

How the "adjusted EBITDA" of a particular borrower is calculated will actually be dependent on the standards of the respective lender underwriting/making the Program loan and whether there is an existing relationship between the respective borrower and lender. More specifically, the FAQ provides that, when calculating the "adjusted EBITDA" of a particular borrower:

- where the borrower is an existing client of the lender, the lender must use the same methodology as it has used in the past when extending credit to such borrower; and
- where the borrower is a new client, the lender must use the same methodology as it used in extending credit to "similarly situated borrowers"⁵ on or before April 24, 2020.

With respect to the above, where a particular lender has more than one methodology for calculating "adjusted EBITDA" (e.g. where a lender has one methodology for use within a credit agreement and one for internal risk management purposes and/or where a lender has different methodologies for different loans made to the same borrower), such lender must select a single method for use with Program loans which should be its most conservative method. In any case, a lender cannot "cherry pick" or selectively apply EBITDA adjustment methodologies.⁶

Notwithstanding the above, solely with respect to Expanded Loans, the "adjusted EBITDA" methodology to be applied by the respective lender must be the same methodology as used by the lender in originating/underwriting the subject loan prior to April 24, 2020.

7. How is the amount of "existing outstanding and undrawn debt" calculated for purposes of determining Program loan caps?

Per the FAQ, the amount of a particular borrower's "existing outstanding and undrawn available debt" will be an aggregate amount equal to:

- the aggregate amount of all loans then made to such borrower and outstanding "under any loan facility, including unsecured or secured loans from any bank, non-bank financial institution, or private lender, as well as any publicly issued bonds or private placement facilities;"

⁵ As stated in the FAQ, "similarly situated borrowers" are "borrowers in similar industries with comparable risk and size characteristics."
⁶ It should be noted that the FAQ specifically provides that lenders should document the rationale behind its selection of a particular adjusted EBITDA methodology.

plus (without duplication):

- the aggregate amount of all undrawn commitments then available to the subject borrower under any loan facility, except for (and excluding the amount of) any undrawn commitment which:
 - serves as a backup line for commercial paper issuance;
 - is used to finance receivables (including seasonal financing of inventory);
 - that cannot be drawn without additional collateral; and/or
 - that is no longer available due to any change in circumstances (including as a result of any decrease in the underlying borrowing base/collateral value).

For clarity, the total amount of “existing outstanding and undrawn available debt” with respect to a particular borrower will be calculated as of the date of the Program loan application. As such, it appears that any changes with respect to any of the foregoing after the date of the Program loan application would not be taken into account.

8. Are Program loans forgivable?

No, unlike PPP loans, Program loans are full-recourse loans and are not forgivable.

9. Are borrowers required to have/grant collateral for Program loans?

Whether or not a particular Program loan needs to be secured by collateral is a bit unclear at the moment. The FAQ provides that Program loans may be secured or unsecured but does not provide any specifics as to how that decision will be made. That being said, the FAQ appears to imply that the decision as to whether a particular Program loan will need to be secured (and what respective collateral will be required to secure the same) will be made by the respective lender making the loan based on their own risk/underwriting standards.

What is clear from the FAQ, however, is that:

- a Priority Loan or an Expanded Loan may only be unsecured if the respective borrower does not, as of the date of the loan origination, have any secured debt other than “Mortgage Debt;”⁷ and
- solely with respect to an Expanded Loan, any/all collateral that secured the prior loan that is being expanded must also secure the Expanded Loan, on a pari passu basis.

10. Do borrowers need to certify to/evidence economic need for Program loans?

Initial versions of the Program loan term sheets contemplated that borrowers would need to certify/evidence an economic need for the requested loan funds due to an adverse economic affect the COVID-19 pandemic. The FRB has since softened this requirement and now requires only that a borrower certify that it is unable to secure “adequate credit accommodations” from financial institutions or other sources “because 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.” Further, the FAQ makes it clear that Eligible Borrowers will not be required to demonstrate that any application for credit has been denied or that the amount, price, or terms of any other credit available elsewhere is inadequate.

11. What other certifications/covenants do borrowers need to make for Program loans?

In addition to the above certification, in connection with each Program loan, the respective borrower will need to make the following certifications/covenants:

- the borrower must covenant and agree:
 - to refrain from repaying the principal balance of, or paying any interest on, any debt until its Program loan is repaid in full (*other than such payments which become "mandatory and due" (as discussed above) per the terms of such credit facility*);⁸
 - that it will not seek to cancel or reduce any of its committed lines of credit with the Program loan lender or any other lender; and
- the borrower must also covenant and agree that it will follow all of the applicable restrictions set forth in Section 4003(c)(3)(A)(ii) of the CARES Act, which provides that, for the period from the funding of such borrower's Program loan through the date that is one year from the repayment of such loan in full, such borrower:
 - will not repurchase any of its (or any parent entity's) equity securities which are listed on a national exchange at any time while the Program loan was outstanding (*except to the extent such purchase was made pursuant to an agreement that was in effect prior to March 27, 2020*);
 - will not pay dividends or make other capital distributions to its equity holders (*other than tax distributions to the extent the borrower is an S corporation or other tax pass-through entity*); and
 - fully comply with the employee compensation restrictions of Section 4004 of the Cares Act (*as discussed below*); and
- The borrower must certify that it is not a "Covered Entity" and is otherwise eligible to receive a Program loan in light of the conflict of interest prohibits in Section 4019(b) of the CARES Act.

It should be noted that the above certifications/covenants only represent the current minimum required certifications/covenants. The actual Program loan application/loan documentation can (*and most likely will*) contain additional substantive certifications/covenants of the respective borrower which are required by the respective lender making the Program loan.

12. What employee compensation restrictions would apply to a borrower that receives a Program loan?

A borrower that receives a Program loan would need to fully comply with the employee compensation restrictions of Section 4004 of the Cares Act. Those rules require that, during the Restricted Period, the maximum compensation paid to such borrower's officers and employees must be limited as follows:

- with respect to each officer and employee of such borrower whose total compensation for the 2019 calendar year (*respectively, their "2019 Compensation"*) was more than \$425k but less than (*or equal to*) \$3M⁹, such person may not receive from such borrower:
 - during any 12-month period during the Restricted Period, total compensation which exceeds their 2019 Compensation; and/or
 - severance pay or other employment termination benefits which exceeds 2x their 2019 Compensation;

⁸ It should be noted that, solely with respect to Priority Loans, the borrower would be permitted, at the time of origination of the Priority Loan, to refinance existing debt owed by the subject borrower to a lender who is not the Priority Loan lender.

⁹ Note that employees who would otherwise fall into this category, but whose compensation is determined through an existing collective bargaining agreement entered into prior to March 1, 2020, would be excluded.

- with respect to each officer and employee of such borrower whose 2019 Compensation was more than \$3,000,000,¹⁰ such person may not receive from such borrower:
 - during any 12-month period during the Restricted Period, total compensation which exceeds the sum of: (a) \$3M; plus (b) 50% of the amount by which their 2019 Compensation exceeds \$3M; and/or
 - severance pay or other employment termination benefits which exceeds 2x their 2019 Compensation.

For purposes of the above, “total compensation” includes salary, bonuses, awards of stock, and other financial benefits provided by the respective borrower to the subject officer/employee.

13. Are not-for-profit organizations eligible to receive Program loans?

Currently not-profit organizations are not eligible to receive Program loans. However, the FRB is said to be considering loan options which are suitable for not-profit organizations. In fact, while not finalized yet, on June 15, 2020 the FRB released “proposed” term sheets for two new Program facilities: a “[Nonprofit Organization New Loan Facility](#)” (a/k/a “NONLF”) and a “[Nonprofit Organization Expanded Loan Facility](#)” (a/k/a “NOELF”).

14. How will Program loans be documented?

Program loan lenders are required to document their Program loans in a manner that is substantially similar to the loan documentation such lender uses in the ordinary course of business with respect to lending to similarly situated borrowers (*with necessary adjustments to reflect applicable Program requirements*). Please note, while the FAQ provides certain model terms/covenants to be included in Program loan documentation, it does not address all of the terms and conditions that will be included in the definitive loan documentation. Accordingly, the actual loan documentation terms and conditions of a particular Program loan, even a Program loan of the same type, may vary significantly from one lender to another.

15. How can Eligible Borrowers apply for a Program loan?

To obtain a Program loan an Eligible Borrower will need to submit an application to a participating lender, together with all supporting documentation and other information such lender may require. Please note, unlike in connection with PPP loans, there is not expected to be a uniform Program loan application (*or other loan documentation*). As such, each participating lender will have the ability (*and is expected*) to develop its own application process, as well as its own underwriting procedures and requirements.

Please note, the rules and guidance surrounding the Program are in flux and are changing rapidly, any related information, guidance or interpretations herein are date/time sensitive and subject to change without notice.

It should also be noted that, as of the date of this Alert, the Program has not yet been made effective so no loan applications can be accepted. The FAQ provides that updates regarding the official launch date of the Program will be made available on the FRB’s [Program page](#).

We will continue to follow this and the other CARES Act programs and offer updates as further developments arise. If you have any questions, please contact Anthony Zeoli (azeoli@freeborn.com), Kenneth Crane (kcrane@freeborn.com) or another member of the Freeborn & Peters LLP CARES Act team.

¹⁰ Note that employees who would otherwise fall into this category but whose compensation is determined through an existing collective bargaining agreement entered into prior to March 1, 2020 would be excluded.

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