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New Federal Reserve Loans to Mid-Size Businesses

By Keith C. Durkin

Today, the Federal Reserve announced to two new lending facilities aimed at assisting mid-sized businesses adversely affected by the COVID-19 crisis. The Main Street New Loan Facility ("Main Street New Loan Facility") is intended to facilitate lending to small and medium-sized businesses beginning today. The Main Street Expanded Loan Facility ("Main Street Expanded Loan Facility") is intended to allow borrowers who obtained loans prior to April 8, 2020 to assist them during the COVID-19 crisis to participate as part of the Main Street Expanded Loan Facility. In other words, the Main Street New Loan Facility will be utilized for loans beginning on April 9, 2020 and thereafter while the Main Street Expanded Loan Facility will be utilized for loans made on or before April 8, 2020.

Main Street New Loan Facility:

The Main Street New Loan Facility will provide new loans to small and medium-sized businesses. The Federal Reserve will make an initial investment of $75 billion in the Main Street New Loan Facility.[1] The combined size of the Main Street New Loan Facility and the other lending facilities created through the Main Street Expanded Loan Facility will not exceed $600 billion. The Main Street New Loan Facility will be established through a special purpose vehicle ("SPV").[2] Eligible lenders will obtain the funds to make these loans directly from the SPV. Eligible lenders include typical banks, bank holding companies, and S&L institutions. Borrowers will have until September 30, 2020 to obtain these loans.

The following is a summary of the term sheet circulated by the Federal Reserve this morning. It is important to note that the term sheet explicitly states the Federal Reserve Board and the Treasury Department may subsequently adjust the terms set forth in the announced term sheet.

Eligible Borrowers. Eligible borrowers must meet the following qualifications:

1. Have no more than 10,000 employees or $2.5 billion in annual revenue.
2. Must be 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.
3. Borrowers participating in this Main Street New Loan Facility cannot participate in the existing Main Street Expanded Loan Facility or the Primary Market Corporate Credit Facility, which are other SPV lending facilities established and funded by the Federal Reserve.

Loan Terms. Each loan will be subject to the following terms:

1. Will be an unsecured term loan with a 4 year maturity.
2. Payments of principal and interest will be deferred for 1 year, but interest will accrue from the loan date.
3. Interest rate will be the Secured Overnight Financing Rate + 2.5% or 4%. The current Secured Overnight Financing Rate is .01%
4. Minimum loan size is $1 million.
5. Maximum loan size is the lesser of: (a) $25 million; or (b) an amount of debt, when added to the borrower's existing outstanding and committed but undrawn debt, does not exceed 4 times the borrowers 2019 earnings before interest, taxes, depreciation, and amortization, i.e., EBITDA.
6. Borrowers can make prepayments without penalty.

Attestations. The following attestations must be made by the lender or borrower, as applicable:

1. The lender must attest the loan proceeds will not be used to repay or refinance pre-existing loans or lines of credit made by the lender to the borrower. The lender must not cancel or reduce any existing lines of credit to the borrower.
2. The borrower: (a) cannot utilize loan proceeds to repay other loan balances; (b) must refrain from repaying debt of equal or lower priority, with the exception of mandatory principal payments, unless the borrower had repaid the loan made pursuant to the Main Street New Loan Facility in full; (c) will not seek to cancel or reduce its outstanding lines of credit with the lender or any other lender; (d) requires financing due to the exigent circumstances of COVID-19 and that it will use the loan proceeds to make reasonable efforts to maintain its payroll and retain its employees during the loan term; (e) meets the EBITDA leverage condition set forth above; (f) must follow compensation, stock repurchase, and capital distribution

1 The term sheet references some of these funds being available for the Main Street Expanded Loan Facility as well. Accordingly, not all $75 billion may be loaned through the Main Street New Loan Facility.

2 The Main Street New Loan Facility and Main Street Expanded Loan Facility will seemingly be administered through the same SPV.

restricts set forth in Section 4003 of the CARES Act;[3] and (g) must certify it can participate in facility without any conflicts of interest. The conflicts of interest generally apply to the President, members of Congress, and their family members.

Main Street Expanded Loan Facility.

The Main Street Expanded Loan Facility provides for an initial $75 billion investment through a special purpose vehicle ("SPV"). The SPV will purchase 95% participations in the upsized tranche of eligible loans from eligible lenders. The original lenders will retain the remaining 5% participation in the upsized tranche of the eligible loans. Risk between the SPV and the lenders will be shared on a pari passu basis, i.e., at the same ratio. The SPV will cease purchasing participations on September 30, 2020.

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1. Have no more than 10,000 employees or $2.5 billion in annual revenue.
2. Must be 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.
3. Borrowers participating in this Main Street Expanded Loan Facility cannot participate in the existing Main Street New Loan Facility or the Primary Market Corporate Credit Facility, which are other SPV lending facilities established and funded by the Federal Reserve

Loan Terms. Each loan will be subject to the following terms:

1. Will be a term loan with a 4 year maturity.
2. Payments of principal and interest will be deferred for 1 year, but interest will accrue from the loan date.
3. Interest rate will be the Secured Overnight Financing Rate + 2.5% or 4%. The current Secured Overnight Financing Rate is .01%
4. Minimum loan size is $1 million.
5. Maximum loan size is the lesser of: (a) $150 million; (b) 30% of the eligible borrower's outstanding and committed but undrawn bank debt; or (c) an amount of debt, when added to the borrower's existing outstanding and committed but undrawn debt, does not exceed 6 times the borrowers 2019 earnings before interest, taxes, depreciation, and amortization, i.e., EBITDA.
6. Borrowers can make prepayments without penalty.

Attestations. The following attestations must be made by the lender or borrower, as applicable:

1. The lender must attest the proceeds of the upsized tranche of the eligible loans will not be used to repay or refinance pre-existing loans or lines of credit made by the lender to the borrower. The lender must not cancel or reduce any existing lines of credit to the borrower.
2. The borrower: (a) cannot utilize the proceeds from the upsized tranche of the eligible loan to repay other loan balances; (b) must refrain from repaying debt of equal or lower priority, with the exception of mandatory principal payments, unless the borrower had repaid the loan made pursuant to the Main Street New Loan Facility in full; (c) will not seek to cancel or reduce its outstanding lines of credit with the lender or any other lender; (d) requires financing due to the exigent circumstances of COVID-19 and that it will use the loan proceeds to make reasonable efforts to maintain its payroll and retain its employees during the loan term; (e) meets the EBITDA leverage condition set forth above; (f) must follow compensation, stock repurchase, and capital distribution restrictions set forth in Section 4003 of the CARES Act;[4] and (g) must certify it can participate in facility without any conflicts of interest. The conflicts of interest generally apply to the President, members of Congress, and their family members.

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3 Section 4003 contains numerous prohibitions. The term sheet issued by the Federal Reserve did not reference all the prohibitions set forth in Section 4003 of the CARES Act. Accordingly, we expect further guidance on the issuance of these loans with respect to the prohibitions not set forth in the Federal Reserve's term sheet circulated this morning. One of the prohibitions set forth in the term sheet discussed stock buybacks, which prohibits, among other things, that the borrower cannot pay dividends or repurchase an equity security that is listed on an national securities exchange of the borrower or any parent, excluding any contractual obligation to do so incurred before the Act. Preliminarily, we believe this would apply to a redemption or buy-back in a closely-held business unless the Shareholders' Agreement or other agreement is signed before the Act. We believe further guidance will be issued to determine whether all the prohibitions set forth in 4003 will be applied to the Main Street New Loan Facility. Preliminarily, we believe this is likely, but will await further guidance.

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