

READY FOR LAUNCH (REDUX)?

AN UPDATED ANALYSIS OF THE FEDERAL RESERVE'S
RAPIDLY CHANGING MAIN STREET LENDING FACILITIES

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JENNER & BLOCK

Note from the Editors

Since this alert was published, the end date for the Main Street lending program has been extended to December 31, 2020.

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EXECUTIVE SUMMARY

On June 8, 2020—shortly after announcing the program was set to launch—the Board of Governors of the Federal Reserve (Federal Reserve) announced material changes to some of the key terms for the “Main Street” lending program.¹ As of June 15, 2020, months after it was first announced, the program is finally operational.

As described in our [prior alert](#), the Main Street lending program will provide up to \$600 billion in loans to small- and medium-sized businesses in order to ease the economic dislocation caused by the COVID-19 pandemic. Federal Reserve Chair Jerome H. Powell has underscored in several recent remarks that one key goal of the program is to ensure companies can continue to support the country’s workforce.

Since the initial roll out of the program, the Federal Reserve has continued to announce changes, new details, and clarifying FAQs, that provide important guidance to potential participants. These include significant changes made to the program on May 27, 2020, and then again on June 8, 2020, on the eve of the program’s launch. Understanding the changes and clarifications to the program since its launch will be crucial for companies considering submitting an application for funds.

When it comes to *who* will be able to participate in the program, changes since the program’s initial announcement have cut in different directions:

- On the one hand, the Federal Reserve has made multiple attempts to expand the pool of borrowers who may participate in the program by (1) sweeping in larger businesses (*e.g.*, increasing the caps up to 15,000 employees *or* up to \$5 billion in revenue); (2) reaching smaller companies by lowering the minimum loan amount for new loans, first from \$1 million to \$500,000, and then again to \$250,000; and (3) capturing more indebted companies by both shifting to an “adjusted” earnings before interest, taxes, depreciation and amortization (EBITDA) standard to determine loan size and establishing a new lending facility that companies can use to refinance existing debt.
- On the other hand, the guidance confirms a conservative underwriting approach that may limit participation. For example, recent guidance reiterates that participating borrowers should generally be in good financial health, should be evaluated as of the time they submit their loan application, and explicitly leaves it to lenders to evaluate borrowers’ creditworthiness and financial condition against their own underwriting standards. The explicit nature of this guidance may be intended to ward off the types of lawsuits brought by rejected borrowers in the Paycheck Protection Program (PPP), who alleged that banks that imposed their own standards on top of program requirements violated program rules. But such provisions have also prompted questions from lawmakers and others about whether the program’s rules will serve to undermine the “Main Street” moniker, and about whether even more changes will be needed if businesses that are traditionally considered to reside on “Main Street” cannot participate.

Further complicating matters is the guidance stating that borrowers must also certify that they are “unable to secure adequate credit accommodations from other banking institutions,” even as they are subject to the financial health and bank underwriting requirements noted above. This vaguely worded “financial need” requirement harkens back to the imprecise need certification that led to weeks

¹This alert revises a client alert we issued before those last-minute changes were announced, to account for the Federal Reserve’s latest changes.

of uncertainty and controversy in the rollout of the PPP, and may become an area of focus in the weeks to come. In an attempt to clarify the standard, the FAQs state that this certification does “not mean that no credit from other sources is available to the borrower,” but only 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.” Although the FAQs state that no documentation of that inadequacy is required, the ambiguity around this issue means that borrowers will likely be well served to preserve any documentation that supports their making of this certification.

Further, besides these various changes to the eligibility rules surrounding the program, one of the key changes since the Federal Reserve initially announced the program was the addition of the “Priority” Loan Facility, which, with the most recent changes, all but supplants the previously announced “New” Loan Facility, and sits alongside a significantly enhanced “Expanded” Loan Facility. The Priority Loan Facility raises the lending cap for many potential borrowers by providing a higher leverage ratio, and, unlike the other two facilities, it permits borrowers to refinance existing debt from other lenders with proceeds from the loan. Under the Federal Reserve’s previous guidance, participating lenders retained a 15% stake in the loan, instead of the 5% stake required for loans under the other two facilities. On June 8, 2020, however, the Federal Reserve announced that the Priority Loan Facility would also require lenders to retain only a 5% stake in the loans, in order to further incentivize lender participation in the program.

All three facilities involve the same interest rates, no prepayment penalties, and a year of deferred interest payments. The terms of the loans offered by all three facilities have also been extended from four years to five, and they all now offer the same principal repayment structure, providing for two years of deferred principal payments, 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. All entail agreement to the various CARES Act restrictions, such as limitations on executive compensation, stock buybacks, and dividends for one year past the life of the loan. But there are key differences that borrowers must understand before submitting their applications. The terms of the loans for each facility are described in detail below, and are set forth in the Appendix. Some highlights include the following:

1. The Expanded Loan Facility allows companies to access loan amounts up to \$300 million to expand their existing indebtedness, with lower fees than the other programs. It cannot be used to refinance existing debt, and with a \$10 million minimum, the program will likely make sense for larger borrowers looking for additional debt at favorable terms.
2. The Priority Loan Facility allows for refinancing, enables certain borrowers to potentially access loans in a broad range of \$250,000 to \$50 million, and offers a higher leverage ratio than the New Loan Facility. This will be attractive to companies that are not in a position to expand their existing lines of credit, or who are seeking to refinance their debt on more favorable terms.
3. With the most recent changes, the New Loan Facility appears to have a much smaller universe of intended borrowers. It offers similar terms as the Priority Loan Facility, only with more restrictive leverage ratios, a ban on using the funds to refinance, and a lower cap (\$35 million). The primary remaining advantage is that, unlike the other two facilities, it allows companies that have previously incurred secured debt in order to finance their operations or to acquire a business to be able to obtain an unsecured loan from the facility.

Given the broad discretion granted to participating lenders, borrowers will need to work closely with their lenders when assessing which program both best fits their needs and is acceptable to the

lender. Thus, interested businesses should reach out to lenders promptly about participation in the program.²

This client alert builds on our [prior alert](#) and provides a summary of the key features of the Main Street program, highlighting changes since its initial announcement and how those changes may affect the businesses that are considering seeking relief through this program. We encourage you to follow up with any questions or concerns. Jenner & Block offers a wide array of resources and lawyers with experience necessary to help our clients navigate the implications of these important new programs, led by our COVID-19 Response Team. The firm is well positioned to help our clients manage the challenging issues related to the current crisis, from applications for funds, to managing workforce concerns, to the Congressional oversight and government investigations that may accompany any such financial assistance.

This team includes lawyers who played key, leading roles in the country's response to the last economic crisis and who have been recognized nationally for their insight in this one. It includes government veterans whose senior positions meant that they were intimately involved in the design of many of the government's most recent bailout and stimulus programs, oversaw the loan application and distribution processes that were a key part of them, and ran and responded to the investigations that followed. It also includes transactional lawyers who are already engaged with clients seeking to avail themselves of aspects of the government programs described in this and our prior alerts.

Additional materials prepared by the COVID-19 Response Team are available on Jenner & Block's [COVID-19 Resource Center](#). For more information on the CARES Act, please reach out to CARESAct@jenner.com or your primary Jenner & Block contact.

² On May 27, 2020, the Federal Reserve Bank of Boston released instructions for lender- and borrower-required documentation for the Main Street program, the required certifications and covenants for borrowers and lenders, the participation agreement, servicing agreement, and co-lender agreement terms and conditions, as well as other forms and instructions. As applications are submitted through financial institutions, prospective borrowers should contact their lenders about participation.

I. STRUCTURE OF THE MAIN STREET PROGRAM

The \$600 billion Main Street program is divided into three lending facilities: the [Main Street Expanded Loan Facility](#) (Expanded Loan Facility); the [Main Street Priority Loan Facility](#) (Priority Loan Facility); and the [Main Street Loan Facility](#) (New Loan Facility).

As described in our [prior alert](#), none of these facilities will involve direct lending by the Federal Reserve to eligible businesses. Instead, the Federal Reserve will encourage banks to make loans to eligible borrowers by purchasing a stake in those loans. To do so, the Federal Reserve will lend to a special purpose vehicle (SPV) seeded by a \$75 billion equity investment from the Treasury and administered by the Federal Reserve Bank of Boston. The SPV, in turn, will use up to \$600 billion in funds provided by the Federal Reserve to purchase loans from participating banks. Banks themselves will make the loans to eligible borrowers, and will then sell most of the loan to the SPV, retaining a percentage of each loan, giving them some “skin in the game.”³

For each facility, the SPV will purchase 95% of each loan, with the bank retaining 5%.⁴

II. TERMS OF THE LOANS

Many of the terms for loans issued or expanded under the Main Street program have changed significantly since the program’s initial announcement in response to extensive public comments, including setting the terms for the newly created Priority loans and the revamped loan terms announced first on May 27, 2020, and then again on June 8, 2020.⁵

All Main Street loans will be five-year adjustable rate loans, with payments on interest deferred for one year and payments on principal deferred for two years. Borrowers will be allowed to prepay without penalty.

Other features include the following.

Interest Rate

Main Street program loans will use the one- or three-month London Inter-Bank Offered Rate (LIBOR), and then add 3 percentage points. As of June 15, 2020, the one- and three-month LIBOR stand at approximately 0.19% and 0.32%, respectively.⁶

³ Lenders must retain their share of the loan until the loan matures or the SPV sells all of its participation.

⁴ On April 30, 2020, when the Priority Loan Facility was first announced, the Federal Reserve stated that the SPV would purchase 85% of each Priority loan, and the lenders would be required to retain 15%. On June 8, 2020, the Federal Reserve announced that it would purchase 95% shares for all three facilities, in order to further incentivize lender participation in the program.

⁵ In order to account for its late changes, the Federal Reserve has stated in its FAQs that if any loans were originated or upsized in reliance on the terms and guidance provided in the April 30, 2020 term sheets, the Main Street SPV will purchase participations in those loans during the first 14 days of the operation of the relevant Main Street facility, provided the loans and documentation meet those requirements, and the loans were funded prior to June 10, 2020. Importantly, however, lenders and borrowers may refinance or amend any such loans to include the terms of the programs as revised on June 8, 2020.

⁶ These figures are revised from the original announcement, in which the Federal Reserve said it would use the Secured Overnight Financing Rate (SOFR), and announced a range of 2.5 to 4 additional percentage points. The Federal Reserve changed the reference point for the adjustable interest rate in response to public comments

Minimum and Maximum Amounts.

The Federal Reserve has set minimum and maximum lending amounts that differ in several ways from its initial guidance, as noted below.

Facility	Minimum	Maximum
New Loan Facility	<p>The minimum is \$250,000.</p> <p>This was reduced from \$1 million set forth in the initial April 30, 2020 guidance, and from \$500,000 set forth in the May 27, 2020 guidance.</p>	<p>The maximum is the lesser of (i) \$35 million (formerly \$25 million) or (ii) an amount that, when added to the borrower's existing outstanding and undrawn available debt,⁷ does not exceed four times the borrower's adjusted 2019 earnings before interest, taxes, depreciation and amortization (EBITDA). For example, if a borrower's outstanding and undrawn available debt is \$30 million and its 2019 adjusted EBITDA was \$10 million, the maximum loan size would be \$10 million [(4 x \$10 million) - \$30 million]. The use of <i>adjusted</i> 2019 EBITDA will allow more indebted firms to qualify for loans and at higher amounts, as discussed in more detail below this chart.</p>
Priority Loan Facility	<p>The minimum is \$250,000.</p> <p>This facility did not exist in the initial April 30, 2020 guidance. The minimum was reduced from \$500,000 set forth in the May 27, 2020 guidance.</p>	<p>The maximum is the lesser of (i) \$50 million (formerly \$25 million) or (ii) no more than <i>six times</i> the borrower's adjusted 2019 EBITDA when added to the borrower's existing outstanding and undrawn available debt. For example, the maximum loan size for the borrower in the above example would be \$30 million [(6 x \$10 million) - \$30 million].⁸</p>

claiming that the use of the SOFR would lead to implementation challenges and that using the more commonly-used benchmark of LIBOR would be more efficient, even though it is scheduled to be phased out by the end of next year. The Federal Reserve has encouraged lenders and borrowers to account for the possibility that LIBOR becomes unavailable during loan terms by including fallback contract language to be used should that happen.

⁷ The Federal Reserve has clarified the description of debt provided in the original term sheets, which was "existing outstanding and committed but undrawn debt." The Main Street FAQs clarify that "existing outstanding and undrawn available debt" constitutes all amounts borrowed 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. It does not include undrawn commitments (i) that serve as a backup line of commercial paper issuance, (ii) used to finance receivables, (iii) that cannot be drawn without additional collateral, or (iv) that are no longer available due to a change in circumstance.

⁸ For companies seeking *secured* loans from the Priority or Expanded Loan Facilities, additional limits may apply depending on the borrower's other secured loans or debt instruments and the value of the collateral securing the loan.

Facility	Minimum	Maximum
Expanded Loan Facility	<p>The minimum is \$10 million.</p> <p>This was increased from \$1 million set forth in the initial April 30, 2020 guidance.</p>	<p>The maximum loan size for the expanded portion increased to the lesser of (i) \$300 million (up from \$150 million (April 30) and then \$200 million (May 27)) or (ii) an amount that, when added to the borrower's existing outstanding and undrawn available debt, does not exceed six times the borrower's adjusted 2019 EBITDA. For example, if a borrower's outstanding and committed debt is \$200 million and its adjusted 2019 EBITDA was \$50 million, the maximum loan size is \$100 million [(6 x \$50 million) - \$200 million].</p>

Changes to the programs' loan amounts have altered the pool of eligible borrowers in several ways.

First, by lowering the minimum loan amount for the New Loan Facility and Priority Loan Facility to \$250,000 (instead of \$500,000 or \$1 million), smaller businesses that are less able to take on larger amounts of debt may now participate. By contrast, increasing the minimum loan for the Expanded Loan Facility from \$1 million to \$10 million will limit participation in that facility to larger entities. Moreover, the Federal Reserve's June 8 changes eliminated the maximum loan calculation of 35% of the borrower's total outstanding debt, which—by leaving the other adjusted EBITDA-based maximum calculation in place—will allow more heavily indebted companies to participate in the program.

Second, the Federal Reserve's adoption of *adjusted* 2019 EBITDA when determining the Main Street loan caps will expand the maximum loans for certain companies and open the Main Street program to borrowers who previously could not participate. EBITDA is generally calculated by starting with a company's net profit or loss, and then factoring in its interest, tax, and depreciation and amortization expenses to arrive at an earnings number. *Adjusted* EBITDA, by contrast, excludes certain expenses that would normally be deducted, resulting in higher earnings. For example, in 2019, a company may have calculated its EBITDA at \$1 million, which reflected an earnings reduction of \$400,000 for litigation expenses and \$100,000 in losses from foreign exchange fluctuations. That company's adjusted EBITDA would eliminate those deductions, increasing its earnings to \$1.5 million. In this example, assuming that the company had \$2 million in debt, its borrowing maximum under the Priority facility using its unadjusted EBITDA would be \$4 million ((6 x \$1 million) - \$2 million), whereas that maximum would increase under adjusted EBITDA to \$7 million ((6 x \$1.5 million) - \$2 million).⁹

Third, the Federal Reserve has clarified that borrowers' maximum loan sizes are considered on a consolidated basis with their affiliated companies, and that borrowers may only apply to the same Main Street facility as their affiliates. Thus, although each affiliated company will submit its own application, and its maximum loan is determined as set forth above, the overall amount borrowed by an affiliated group is subject to an overall cap. That means that if a portfolio company's affiliates have already received loans from the Priority Loan Facility, that company may only apply to the Priority Loan Facility, and the maximum loan it could receive might be reduced by the amount received by its affiliates. For example, if such a company's affiliates had already received a total of \$45 million, the

⁹ Responding to suggestions that allowing these adjustments to EBITDA could permit "excessive risk-taking," the FAQs emphasize that the EBITDA adjustments "must be of the type the Eligible Lender has previously (and recently) required for the Eligible Borrower or similarly situated borrowers" and note that the lender should document its rationale for the adjustments.

most it could apply for would be \$5 million. The overall EBITDA leverage caps also apply on a consolidated basis to an entire group of affiliated companies, where a borrower from that group has previously received (or is simultaneously applying for) a Main Street loan.

Repayment Schedule

The Federal Reserve has announced repayment details, which are the same for all three facilities. After the first two years of deferred principal, 15% of the principal amortizes at the end of the second and third years, and a balloon payment of 70% is required at maturity at the end of the fourth year. Interest payments are deferred for one year and then capitalized.¹⁰

Fees

Fee schedules for the programs also differ to some extent, although there are certain common features:

Facility	Fees
New Loan Facility	<p>Lenders have the discretion to charge borrowers an origination fee of up to 1% of the principal amount of the loan. Lenders must pay the SPV a transaction fee of 1% of the principal amount of the loan, which the lender may pass on to the borrower at its discretion. Borrowers should therefore expect to pay up to a 2% fee to their lender in order to participate. Lenders are also permitted to charge borrowers de minimis fees for services that are customary and necessary in their underwriting of commercial and industrial loans to similar borrowers.</p> <p>The Federal Reserve will pay lenders an annual fee of 0.25% of the principal amount of the Federal Reserve's stake in the loan in return for the lenders' servicing of the loan.</p>
Priority Loan Facility	Same as for New Loan Facility.
Expanded Loan Facility	<p>Lenders have the discretion to charge borrowers an upsizing fee of up to 0.75% of the principal amount of the upsized tranche of the loan (reduced from 1% in the initial guidance). The new guidance adds a transaction fee of 0.75% of the principal amount of the upsized portion of the loan that lenders must pay to the SPV, which also may be passed on to the borrower. In other words, borrowers may expect to pay up to a 1.5% upsizing fee for participating in this facility. Lenders are also permitted to charge borrowers de minimis fees for services that are customary and necessary in their underwriting of commercial and industrial loans to similar borrowers.</p> <p>As with the other facilities, the Federal Reserve will pay the 0.25% annual servicing fee to lenders.</p>

¹⁰ In order to be eligible for upsizing, the underlying loan must have a remaining maturity of at least 18 months, and have been originated on or before April 24, 2020. However, the lender may extend the maturity of the underlying loan or credit facility at the time of upsizing in order to meet the 18-month remaining maturity requirement.

Risk Sharing

The SPV and the lender will share risk on all loans *pari passu*, meaning they will have equal payment rights. This means that, for example, if a borrower made a \$1 million payment on a loan, the SPV for each facility would receive \$950,000 and the lender would receive \$50,000. Moreover, any collateral securing a loan under the Expanded Loan Facility will secure the loan on a pro rata basis between the SPV and lender.

Subordination

Loans made through any of the three programs cannot be contractually subordinated to unsecured debt (*i.e.*, debt that is not backed by the borrower's assets). In other words, a lender cannot agree to have its claim repaid after general unsecured creditors are repaid.

Security

The fundamental requirements governing whether loans must be secured by the borrower's assets are different under the New Loan Facility, on the one hand, and the Priority Loan Facility and Expanded Loan Facility, on the other hand.

For the New Loan Facility, loans may be provided on either a secured or unsecured basis. If the loan is secured, there are no specific requirements with respect to the value of the security provided. And, unlike the other two programs, a borrower may obtain a New Loan Facility loan without regard to whether it has any existing secured debt. Given the June 8 changes to the program, this distinction may be the principal consideration for a borrower that elects to obtain a loan under the New Loan Facility as opposed to the Priority Loan Facility.

For the Priority Loan Facility and Expanded Loan Facility, whether a loan will be made on a secured or unsecured basis depends on whether the borrower has any preexisting secured debt. If the borrower has no secured debt, then the loans under the Priority Loan Facility and Expanded Loan Facility can be unsecured. But if a borrower has secured debt, then the loans must be secured. Notably, the foregoing requirements exclude existing mortgage debt (*i.e.*, a loan that is secured by real property) and limited recourse equipment financings (including equipment capital or finance leasing and purchase money equipment loans) secured only by the acquired equipment ("equipment secured debt"), such that a borrower that only has mortgage debt or equipment secured debt would be treated as not having any secured debt and could therefore apply for an unsecured loan under these two facilities.

Where a new loan is being made under the Priority Loan Facility to a borrower that has incurred secured debt, and the borrower has other assets that have not been pledged to the existing lenders, the loan can be secured solely by those assets. If the value of those assets is not sufficient to provide the necessary collateral coverage, then the Priority Loan Facility loan will need to be secured by assets that are already pledged to secure an existing loan. In this case, the loan's security interest must be senior to, or equal in priority with, the other lenders' security interests. The sharing of the collateral to satisfy this condition can be accomplished pursuant to an agreement between the lenders that governs their respective rights as to the collateral.

The maximum amount of a secured Priority Loan Facility loan will be based on, in addition to the criteria described above, the value of the collateral securing the loan (a relationship that is commonly referred to as "collateral coverage"). The collateral coverage ratio (*i.e.*, the value of the collateral

(valued pro rata, to the extent such collateral secures other debt) to the amount of the Priority Facility loan) must be either (i) at least 200% (*i.e.*, the value of assets is twice the amount of the loan), or (ii) not less than the aggregate collateral coverage ratio for all of the borrower's other secured debt. Lenders are not required to use the collateral coverage ratio that would permit the borrower to obtain the largest possible loan under the more lenient test.

When an existing secured facility is being upsized pursuant to the Expanded Loan Facility, the new borrowing will be secured by the existing collateral, and the amount of the upsizing will be determined by application of the facility's collateral coverage test.¹¹ The borrower may add additional collateral at the time of upsizing in order to allow it to borrow additional funds under that facility's collateral coverage test.

These requirements may limit the ability of borrowers that have already incurred secured debt to obtain financing under the Priority Loan Facility or the Expanded Loan Facility. As described above, these borrowers cannot use these programs to incur unsecured debt. A potentially significant obstacle is that the borrower may not have sufficient assets to pledge as collateral to support a new loan under the Priority Loan Facility, or to upsize an existing facility under the Expanded Loan Facility. As noted above, new borrowings will need to satisfy the applicable collateral coverage test.

Certain borrowers may not be able to easily upsize an existing unsecured facility under the Expanded Loan Facility. As described above, this program mandates that the upsized facility be secured if the borrower has any secured debt, excluding mortgage debt and equipment secured debt. This requirement is not limited to whether the facility that could be expanded is secured. Accordingly, where a borrower has an unsecured facility and other non-mortgage, non-equipment secured debt that is secured, it would need to arrange for that facility to become secured in order for the facility to be eligible for upsizing under the Expanded Loan Facility.

Other Debt

To further reduce the risk that the lender under the Priority Loan Facility and Expanded Loan Facility will not be repaid in full, and regardless of whether the new loan is secured or unsecured, the loan agreement must include a covenant that restricts the borrower's ability to incur additional secured debt. This covenant, commonly called a "negative pledge," generally prevents the borrower from incurring secured debt, subject to certain exceptions such as mortgage and construction debt, and receivables financings. The covenant's terms must be consistent with those used by a lender in its ordinary course lending to similarly-situated borrowers.¹² The negative pledge does not restrict the borrower's ability to incur additional unsecured debt.

III. BORROWERS

When applying for a Main Street loan through an eligible lender, borrowers must submit a number of required certifications, signed by their principal executive and principal financial officers,¹³

¹¹ If the underlying credit facility includes both a term tranche and a revolving tranche, the upsized tranche only needs to share collateral with the term tranche.

¹² The FAQs provide that, with respect to an upsized tranche under the Expanded Loan Facility where the underlying loan is part of a multi-lender facility, an existing covenant will be sufficient so long as it was negotiated in good faith prior to April 2, 2020.

¹³ If there are no such individuals in the company, then the borrower must have individuals performing similar functions make these certifications. If the borrower's principal executive officer and principal financial officer are

and submit certain documentation supporting those certifications. In short, borrowers must certify that they meet the business eligibility requirements for the program (discussed below in subsection A), that they meet certain financial health and use requirements (subsection B), and that they will comply with certain restrictions, such as limits on executive compensation and stock buybacks (subsection C). In connection with these certifications, borrowers must submit financial statements consistent with how they typically prepare those statements. For example, if a borrower is subject to US GAAP reporting requirements or already prepares its financials in accordance with US GAAP, the borrower must submit U.S. GAAP-compliant financial records. If borrowers typically prepare their financials on a consolidated basis with their subsidiaries, then they must do the same for their certifications. In turn, lenders are entitled to rely on these certifications without additional verification. Borrowers are also required to provide detailed financial data related to their compliance with these requirements to the lenders on a quarterly basis, which will then be forwarded to the Federal Reserve's SPV for review.

A. Eligibility Certification

The criteria for determining borrower eligibility is uniform across the three facilities, and have been expanded in key respects by Federal Reserve guidance.

Size Eligibility

First, eligible borrowers include businesses¹⁴ established prior to March 13, 2020, with up to 15,000 employees or up to \$5 billion in 2019 annual revenues. These figures are an expansion of the initial guidance provided by the Federal Reserve, which had capped eligibility at up to 10,000 employees or up to \$2.5 billion in 2019 annual revenues.

For determining eligibility, potential borrowers will need to count their employees and revenue by including their affiliates. To count employees, potential borrowers should include all full-time, part-time, and seasonal employees, and use the average of the total number of individuals employed by the borrower and its affiliates for each pay period over the 12 months preceding the origination or upsizing of a Main Street loan. To determine whether other entities are affiliates, businesses are expected to use the affiliation rules set forth at 13 C.F.R. § 121.301(f), and used for the PPP, which generally provide that entities are affiliates when one entity controls or has the power to control another, or a third entity has the power to control both.

Business Types

In order to qualify for the Main Street program, borrowers must not be an "ineligible business" as defined by 13 CFR 120.110(b)-(j), (m)-(s), and as modified and clarified by SBA regulations issued in connection with PPP. In other words, businesses that were ineligible under that provision for PPP

the same person, then the second signatory should be the next-in-line officer or an employee who works in a financial or accounting capacity.

¹⁴ The revised Federal Reserve term sheets define a business as "an entity that is 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 as defined [by federal law]." The Federal Reserve has indicated that other forms of organization "may be considered for inclusion" at the Federal Reserve's discretion. Nonprofit organizations are ineligible under the expanded program. However, the Federal Reserve will continue to evaluate the feasibility of adjusting borrower eligibility criteria and loan eligibility metrics of the Main Street program to evaluate the credit risk posed by nonprofit organizations, which is currently not possible based on the EBITDA underwriting metric required by the New Loan Facility, Priority Loan Facility, or Expanded Loan Facility.

funds pursuant to SBA regulations will also be ineligible for the Main Street program. Amongst those excluded are private equity firms and hedge funds, which fall within the definition of “speculative businesses,” and thus ineligible pursuant to SBA guidelines. However, the guidance from the PPP program states that a portfolio company of a private equity fund may still qualify for the program, provided it meets the affiliation rules and other requirements. The Federal Reserve specifically incorporated this guidance for the Main Street program.

US Nexus Requirement

Borrowers also must certify that they were created or organized in the United States, or under the laws of the United States, and have “significant operations”¹⁵ in and a majority of their employees based in the United States. A borrower may be a subsidiary of a foreign company, provided that the borrower itself meets these US nexus requirements. However, that borrower must use the proceeds of the Main Street loan only for its own benefit, and the benefit of its consolidated US subsidiaries and other affiliates that are US businesses.

Requirement Concerning Other Programs

Borrowers and their affiliates must not have participated in the Federal Reserve’s Primary Market Corporate Credit Facility, and borrowers and their affiliates may only participate in one of the three Main Street facilities. As noted above, if a borrower’s affiliate has previously participated, or has a pending application to participate in a particular Main Street facility, the borrower can only apply to participate in that Main Street facility.

Borrowers also must not have received specific support pursuant to Subtitle A of Title IV of the CARES Act, which provides loans and loan guarantees for passenger air carriers, cargo air carriers, and businesses critical to maintaining national security. There is no restriction, however, preventing businesses that have participated in the PPP, or whose affiliates have participated in the PPP, from participating in the Main Street program.

B. Use and Financial Health Certifications

Participation in the Main Street program will require potential borrowers to make numerous certifications and meet certain conditions concerning their financial health.

First, a borrower must certify that it has a reasonable basis to believe that, after it has received the proceeds of the Main Street loan, it expects it will be able to pay its undisputed debts that are due as of that date and that will become due during the 90 days thereafter. A borrower must also certify that it does not expect to file for bankruptcy during that period. The FAQs emphasize that lenders should evaluate borrowers’ financial condition by looking at its circumstances “at the time of the potential borrower’s application.”

¹⁵ A borrower has “significant operations” in the United States when, evaluated on a consolidated basis with its subsidiaries but not parent companies or sister affiliates, greater than 50% of the borrower’s: (1) assets are located in the United States; (2) annual net income is generated in the United States; (3) annual net operating revenues are generated in the United States; or (4) annual consolidated operating expenses (excluding interest and other debt-related expenses) are generated in the United States. The Main Street FAQs provide that this is a non-exhaustive list that “reflects the principles” that should be applied by the borrower in evaluating its eligibility under this requirement.

Those financial health certifications—which focus on the time of application—appear to be in tension with other parts of the recently issued FAQs. Specifically, the FAQs recognize that otherwise healthy businesses suffering short-term cash flow issues caused by the impact of the pandemic should not be disqualified from the program. They state that “many Main Street loan applicants may be experiencing temporary cash flow disruptions” and acknowledge “the high degree of uncertainty in predicting COVID-19’s economic impact and effect on individual borrowers.” The Federal Reserve therefore “encourages” lenders to “work with borrowers affected by COVID-19 and may originate or expand loans to such borrowers under the Main Street Program.” That assessment may consider “a borrower’s credit history and financial performance prior to the crisis, as well as its post pandemic business prospects.”

Second, in another financial health requirement, if a borrower had other loans outstanding with the participating lender as of December 31, 2019, such loans must have had an internal risk rating equivalent to a “pass” rating based on the Federal Financial Institutions Examination Council (FIEC)’s supervisory rating system as of that date. This is the FIEC’s highest rating, and is another requirement that appears to be intended to ensure that the borrower was in “sound financial condition prior to the onset of the COVID-19 pandemic.”

Third, a borrower must certify that it will make “commercially reasonable efforts” to maintain payroll and employees during the term of the loan. The Federal Reserve explains in its FAQs that this means that borrowers should “undertake good-faith efforts to maintain payroll and retain employees, in light of its capacities, the economic environment, its available resources, and the business need for labor.” But even this guidance remains vague and broadly worded, underscoring the significant ambiguity in what is expected of companies making this attestation. Underscoring the lack of clarity, the Federal Reserve has stated that borrowers that have already laid off or furloughed workers as a result of COVID-19 are still eligible to apply for Main Street loans.

Fourth, a borrower must certify that it is “unable to secure adequate credit accommodations from other banking institutions.” The FAQs have clarified that this does “not mean that no credit from other sources is available to the borrower.” This instead means “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.” The FAQs indicate that a borrower need not provide documentation of this, nor need it show that an application for credit has been denied. Moreover, the FAQs specifically contemplate that borrowers may have available, undrawn lines of credit, which are factored into the borrower’s calculation of “existing outstanding and undrawn available debt.” Thus, the Federal Reserve appears to tacitly approve of borrowers accessing the Main Street program despite the existence of credit elsewhere.

This vague requirement, that credit available from other sources is “inadequate for the borrower’s needs,” is reminiscent of the similarly opaque language surrounding the PPP’s borrower certification on their need for those loans. High-profile controversy ensued even for those borrowers that otherwise seemed to meet the terms of the program. Given the close political attention the Main Street program is likely to attract, borrowers should likely document their basis for making this certification, even in the absence of a requirement to do so.

Fifth, a borrower must certify that neither the President of the United States, the Vice President, a head of an Executive department, Member of Congress, or the spouse, child, or son- or daughter-in-

law of any of the foregoing holds an interest in the company of 20% or greater, pursuant to section 4019(b) of the CARES Act.¹⁶

C. Restrictions

Main Street loans will have potentially significant strings attached. To receive funding, borrowers will have to agree to the following restrictions.

- No Buybacks or Dividends. From the time the borrower receives the loan until one year after the loan is fully repaid, a borrower may not purchase its own stock or the stock of its parent company, except to the extent required under a contractual obligation predating the enactment of the CARES Act. A borrower is also prohibited from paying dividends or making other capital distributions with respect to the borrower's common stock. The newly issued guidance clarifies that this restriction does 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 with respect of the entity's earnings.
- Executive Compensation. From the time the borrower receives the loan until one year after the loan is fully repaid, the borrower may not increase total compensation for any officer or employee whose total compensation exceeded \$425,000 in 2019, including salary, bonuses, awards of stock, and "other financial benefits," which the CARES Act does not define. The borrower may pay any officer or employee who earned more than \$3 million in 2019 no more than \$3 million plus 50% of the excess over \$3 million that they earned in 2019.
- Limits on Golden Parachutes. For the same period, for the same set of officers and employees whose 2019 compensation exceeded \$425,000, a borrower may not provide severance pay or other benefits upon termination of employment that exceed twice the maximum total compensation received by the officer or employee in 2019.
- Limits on Refinancing, Cancellation, or Reduction of Debt. As discussed in more detail in Section II above with respect to priority and debt repayment, the New Loan Facility and Expanded Loan Facility place restrictions on refinancing debt, and all Main Street facilities place restrictions on borrowers' payment of other debt.

IV. LENDERS

Only certain financial institutions can participate as lenders—specifically, US federally insured depository institutions, US branches or agencies of foreign banks, US bank holding companies, US savings and loan holding companies, US intermediate holding companies of foreign banking organizations, or any US subsidiary of any of the foregoing. Unlike the PPP, non-bank lenders are not eligible. The Federal Reserve is "considering options to expand the list of Eligible Lenders in the future."

¹⁶ Absent actual knowledge that any covered government official holds an interest in the borrower's company, a borrower may satisfy a reasonable diligence requirement by checking the name of its beneficial owners of a 5% or greater equity interest in the company, and cross-referencing those names against a list of all government officials provided in the Federal Reserve's instructions form for the borrower, and, if unable to confirm whether any beneficial owner is a covered family member of a government official, asking each beneficial owner directly if they are a family member.

As stated above, as part of a borrower's participation in the Main Street program, lenders must collect the required certifications and covenants, but lenders do not need to independently verify the certifications or actively monitor compliance with the covenants. If a lender becomes aware of a borrower's material misstatement or breach of covenant, however, they are expected to notify the Federal Reserve Bank of Boston.

Overall, the Federal Reserve has given lenders a flexibility to apply their own underwriting requirements, even if such requirements are stricter and would potentially deny an otherwise eligible borrower from participating in the program. The FAQs expressly state that even eligible borrowers who otherwise meet all program requirements still "may not be approved for a loan or receive the maximum allowable amount" from their lender. This requirement is not surprising given that lenders will be required to retain 5% of the loan, and will presumably want to minimize their own risk.

Like borrowers, lenders will also be subject to certain restrictions. Specifically, lenders must represent that for each loan they sell to the facility, they will not (1) "cancel or reduce any existing committed lines of credit to the borrower, except in the event of default" or (2) request payment on existing debt with the borrower until the Main Street loan is repaid in full, except for mandatory and due payments or in the case of default and acceleration. As discussed in greater detail in Section II, "mandatory and due" payments generally include payments scheduled by the terms of the debt agreement, as well as mandatory prepayments triggered by the occurrence of an event. Additionally, lenders must also represent that they have no conflicts of interest (as discussed above for borrowers).

V. MAIN STREET START AND END DATES

According to the Federal Reserve Bank of Boston, the program is now up and running. Borrowers should contact their lenders to determine whether they will be participating in the program, and then apply by providing an application, documents certifying their eligibility under the Main Street program, and any other information required by the bank to underwrite the loan. The Main Street program will continue purchasing loans until the earlier of it expending \$600 billion or September 30, 2020, unless it is expanded or extended by the Federal Reserve and Treasury. The Treasury Secretary recently stated that if the Main Street program's funding is exhausted, he "would absolutely give more capital" to the program.¹⁷ On June 10, 2020, Federal Reserve Chairman Jerome Powell stated that the Federal Reserve would keep the Main Street facilities open "as long as we need to," and that the decision to stop making loans would be made together by the Treasury and the Federal Reserve.

VI. OVERSIGHT AND DISCLOSURE

Because the Main Street program draws on funding from the CARES Act, participants should be aware that by taking part in the program, they may be subject to various forms of reporting and oversight set forth in that legislation. For example, the Federal Reserve has confirmed that participants in these programs will be included in its reporting. Specifically, the Federal Reserve FAQs state that the Federal Reserve will "disclose information regarding the [three facilities] during the operation of the

¹⁷ See Craig Torres et al., "Fed Widens Main Street Loan Program to Reach More Businesses," *Bloomberg Law* (Apr. 30, 2020), <https://news.bloomberglaw.com/banking-law/fed-expands-eligibility-for-its-main-street-lending-program>.

facilities, including information regarding names of lenders and borrowers, amounts borrowed and interest rates charged, and overall costs, revenues, and other fees.”

In addition to this reporting and disclosure, Main Street participants could become the subject of congressional and executive branch oversight and investigation pursuant to the oversight provisions of the CARES Act. The CARES Act sets forth the following mechanisms for oversight and transparency (as detailed further in our prior [client alert](#)):

- The Office of the Special Inspector General for Pandemic Recovery (SIGPR): The CARES Act creates an office of a Special Inspector General responsible for auditing and investigating the loans, loan guarantees, and investments made to businesses by the Treasury Secretary under the Act. SIGPR has law enforcement authority and may subpoena documents related to its oversight of Title IV funds distributed under the Act. The Act does not expressly state that SIGPR’s authority reaches participants in Federal Reserve facilities like the Main Street program. However, under the similarly worded Emergency Economic Stabilization Act of 2008 (EESA), the Special Inspector General for the Troubled Asset Relief Program applied oversight over similar Federal Reserve facilities that were seeded with Treasury equity investments. SIGPR became operational with the confirmation of Brian Miller as the Special Inspector General on June 2, 2020.
- Congressional Oversight Commission: Title IV of the CARES Act also creates a five-member commission responsible for oversight of the loan relief under Title IV, expressly charging the commission with “oversight of the implementation of [Title IV] by the Department of the Treasury and the [Federal Reserve], including efforts of the Department and the [Federal Reserve] to provide economic stability as a result of the . . . COVID-19 pandemic of 2020.” Similar to an oversight panel created under EESA in connection with the 2008 economic crisis, the congressional commission is likely to hold robust hearings and issue commentary on the effectiveness of the Federal Reserve programs created pursuant to the CARES Act and on loan recipients.

As of this date, only four of the five members of the commission have been selected, with the chair of the commission currently vacant.¹⁸ It nonetheless issued its first report on May 18, 2020. The report summarized the Federal Reserve lending facilities announced as of that time, and provided a list of questions about the facilities for the Treasury Department and the Federal Reserve. The questions about the Main Street program asked for the rationales behind many of the terms, including participation rates, the size criteria, the use of adjusted EBITDA and leverage standards, and also asked how the agencies would enforce the requirement to make “commercially reasonable efforts” to maintain payroll.

- Pandemic Response Accountability Committee: Finally, the CARES Act creates a new Pandemic Response Accountability Committee (PRAC) to oversee the entire governmental response to COVID-19, including all funds distributed pursuant to that response. The PRAC consists of at least nine Inspectors General and will have full-time staff devoted to overseeing,

¹⁸ The four appointed members include Senator Pat Toomey (R-Pa.) (appointed by Senator Majority Leader McConnell); Bharat Ramamurti, a former aide to US Sen. Elizabeth Warren (appointed by Senate Minority Leader Schumer); Representative French Hill (R-Ark.) (appointed by House Minority Leader McCarthy); and Representative Donna Shalala (D-Fla.) (appointed by House Majority Leader Pelosi). The chair of the commission, currently vacant, is to be appointed jointly by Senate Majority Leader McConnell and House Majority Leader Pelosi.

auditing, and investigating any fraud, waste, abuse, or mismanagement within the government's response.

On March 30, 2020, then-Acting Inspector General of the Department of Defense Glenn Fine was appointed to serve as the Chair of PRAC. Shortly thereafter, President Trump removed Fine from his role as Acting Inspector General, thus ending his role as Chair of PRAC. Another chair has not yet been appointed since then. On April 27, 2020, Robert A. Westbrooks, the inspector general for the Pension Benefit Guaranty Corporation, was appointed as Executive Director of PRAC. On the same day, PRAC launched a [website](#) that will allow the public to track the various oversight programs and distribution of COVID-19-related funding.

- Other Congressional Oversight: In addition to the regular Senate and House Committees that have oversight of the CARES Act, a House Select Committee on the Coronavirus Crisis was established, which will also oversee the use of the funding for all of Congress's COVID-19-related legislation. Participants in the Main Street Loan facilities may find themselves subject to oversight by this committee given its early actions. For example, in May 2020, the committee sent letters to five companies that had participated in PPP asking them to return the PPP funding, or otherwise produce documents related to their PPP applications.

Appendix: Chart of Key Main Street Loan Features

Main Street Program Loan Options	New Loans	Priority Loans	Expanded Loans
Term	5 years	5 years	5 years
Minimum Loan Size	\$250,000	\$250,000	\$10 million
Maximum Loan Size	Lesser of \$35 million, or an amount that, when added to the borrower's existing outstanding and undrawn available debt, does not exceed 4x the borrower's 2019 EBITDA	Lesser of \$50 million, or an amount that, when added to the borrower's existing outstanding and undrawn available debt, does not exceed 6x the borrower's 2019 EBITDA	Lesser of \$300 million, or an amount that, when added to the borrower's existing outstanding and undrawn available debt, does not exceed 6x the borrower's 2019 EBITDA
Risk Retention	5%	5%	5%
Payment (years one and two deferred for all)	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	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	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
Priority	May be unsecured irrespective of whether borrower has existing secured debt, and cannot be junior in priority to unsecured debt	Senior or <i>pari passu</i> in priority and security with other debt, and may be unsecured only if borrower has no secured debt (excluding mortgages and equipment financings)	Senior or <i>pari passu</i> in priority and security with other debt instruments, and may be unsecured only if borrower has no secured debt (excluding mortgages and equipment financings)
Rate	LIBOR + 3%	LIBOR + 3%	LIBOR + 3%

Adapted from <https://www.federalreserve.gov/newsevents/pressreleases/monetary20200430a.htm>.
Changes/Additions from prior guidance highlighted gray.

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