



**The FRB's Main Street Credit Programs and the Renewed SBA Programs webinar begins at 1:00 PM Central Time.**

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## **The FRB's Main Street Credit Programs and the Renewed SBA Programs**

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THE FRB'S MAIN STREET CREDIT PROGRAMS AND THE RENEWED SBA PROGRAMS

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## Agenda

- **Discuss latest updates to SBA Stimulus Programs**
- **Discuss the Federal Reserve Board's two new Main Street Lending Programs**
- **Analyze important terms and conditions of the Main Street Lending Programs**
- **Highlight limitations and concerns of the two programs**
- **Discuss Dorsey's comments made to Treasury**



THE FRB'S MAIN STREET CREDIT PROGRAMS AND THE RENEWED SBA PROGRAMS

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## SBA Stimulus Program Update



Ken Logsdon

## Latest Stimulus Bill

- **\$310 billion total for PPP with \$250 billion unrestricted and a \$60 billion set aside for smaller institutions:**
  - \$30 billion for assets less than \$10 billion;
  - \$30 billion for assets between \$10 billion and \$50 billion.
- **\$50 billion for EIDL loans**
- **\$10 billion for EIDL advance grants**
- **\$2.1 billion for SBA administrative expenses**
- **Agriculture enterprises now eligible for PPP**
- **PPP eligibility NOT expanded for to 501(c)(6)s and 501(c)(7)s**
- **Treasury looking into whether they can expand eligibility**
  - Regulatory authority to expand eligibility uncertain

## Paycheck Protection Program (PPP) Loan Terms Review

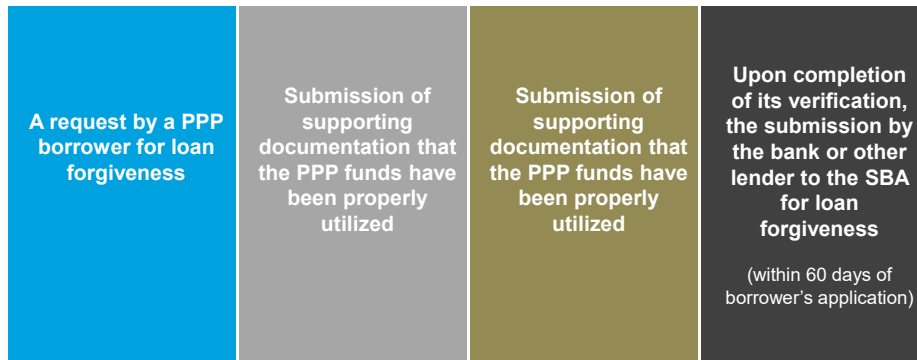
- **A covered loan is non-recourse**
  - unless improper use of proceeds
- **Personal guaranty and collateral requirements waived**
- **100% guaranteed by SBA**
- **A 2-year term from date a PPP borrower applies for loan forgiveness**
  - Seeing many Notes with Maturity being 2 years from funding
- **Interest rate not to exceed 1%**
- **Payment deferral for 6 months**
- **Use of proceeds limited (payroll costs, mortgage interest, rents and utilities)**
- **Eligible for forgiveness**

## PPP Loan Forgiveness

- **Loan principal to be forgiven—certain expenses paid during the 8-week period commencing on the date a covered loan is originated (the “covered period”)**
- **During the covered period, forgivable expenses—**
  - Payroll costs (must be no less than 75% of amount forgiven)
  - Mortgage interest, rent and utility payments (narrow list)
  - “costs incurred and payments made during the covered period”?
- **The SBA will pay amounts forgiven to the lender/holder**
  - Computation of reimbursement subject to the numbers of employees and salary reductions/adjustments, etc.
- **Supporting documentation/certification required**

## Overall Process for Forgiveness

**SBA has indicated that significant supportive documentation will be required to allow a lender to submit the borrower's request for loan forgiveness (additional guidance is likely to come)**



## Documentation

**While the SBA has not yet indicated the amount and adequacy of documentation, the following documentation will be required:**

- A formal forgiveness application, yet to be released by the SBA
- Supporting documentation verifying the number of full-time equivalent employees on payroll and pay rates for the referenced periods including payroll tax filings to the IRS, state income, payroll and unemployment insurance filings and payroll registers
- Payroll invoices supporting the payroll costs, employee benefits, and retirement benefits paid if a PEO is involved
- Documentation supporting other covered expenses (mortgage interest, rent, utilities) including canceled checks, payment receipts, account statements, invoices, and/or other documents

## Certification and Lender Reliance

- **A bank or other lender will be required to obtain a certification from an authorized representative of a PPP borrower that—**
  - The documentation presented is true and correct
  - The amount for which forgiveness is requested was used to retain employees, make interest payments on a covered mortgage obligation, make payments on a covered rent obligation or make covered utility payments
- **Can lenders rely on borrower documentation for loan forgiveness?**
  - **Yes.** The lender does not need to conduct any verification if the borrower submits documentation supporting its request for loan forgiveness and attests that it has accurately verified the payments for eligible costs. The Administrator will hold harmless any lender that relies on such borrower documents and attestation from a borrower.
  - The SBA has determined that lender reliance on a borrower's required documents and attestation is necessary and appropriate
    - Does this also cover “clear error”? Likely not...

## Main Street Lending Program Summary



Joseph T. Lynyak III

## FRB Main Street Lending—Background

- In the month of March, the FRB announced the creation of several credit facilities based upon the FRB’s authority under Section 13(3) of the Federal Reserve Act
- Historically most of those facilities were aimed at the traditional goals of the FRB to address economic crises—to provide liquidity to allow banks to lend
- The CARES Act provided \$500 billion to MSBs and larger businesses beyond the small business lending programs to be operated by the Small Business Administration
- In a somewhat curious news release, the FRB announced a credit facility to support lending to MSBs
  - Defined generally as a business with 500 to 10,000 employees
  - While welcomed by the public—no one had any idea what was meant

## FRB Main Street Lending—Background

- On April 9<sup>th</sup>, the FRB announced 2 credit facilities to implement the announced Main Street credit facility—
  - The Main Street New Loan Facility (“MSNLF”)
  - The Main Street Expanded Loan Facility (“MSELF”)
  - Capitalized by Section 4027 of the CARES Act by the Treasury in the amount of \$75 billion
  - Each loan purchase facility to purchase a 95% interest in loans originated by banks through a SPV
  - Aggregate total of \$600 billion
    - Capitalization approximately 12.5% or roughly bank capital
  - All publically available details of each program were described in a two page term sheet . . .

## The Main Street New Loan Facility (“MSNLF”)

- **Effective April 9, 2020**
- **Operated by a Federal Reserve Bank**
- **The SPV will purchase a 95% interest in “eligible loans”**
  - The lender will retain a 5% interest (skin in the game)

## MSNLF—Eligible Lenders

- **An “Eligible Lender” is defined as—**
  - U.S. FDIC-insured depository institutions
  - U.S. bank holding companies, and
  - U.S. savings and loan holding companies
- **Clarification needed about certain financial institutions**
  - FBO intermediate holding companies
  - FDIC-insured foreign bank branches and agencies
  - Affiliates of holding companies



## MSNLF—Eligible Borrowers

- An “Eligible Borrower” is defined as—
  - Businesses with up to 10,000 employees, or
  - Up to \$2.5 billion in 2019 annual revenues
    - It is unclear whether one or the other is a cap
  - Operational requirement—the business must be—
    - Created or organized in the United States, *and*
    - Have significant operations in *and* a majority of its employees based in the United States
  - May not participate in the MSELF or the FRB’s Primary Market Corporate Credit Facility

## MSNLF Eligible Loan Terms

- Must be originated on or after April 8, 2020 with the following loan terms—
  - 4-year maturity
  - Amortization of principal and interest deferred for 1 year
    - Impliedly interest continues to accrue during deferral period
      - Compounding of interest not clear
  - Variable rate of interest based upon SOFR + 250-400 basis points
  - Minimum loan size of \$1 million
  - Maximum loan size that is equal to 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
  - Prepayment permitted without penalty

## Main Street Extended Loan Facility ("MSELF")

- Effective April 9, 20201
- Similar in many respects to structure of the MSNLF—
  - Capitalized by the Treasury
  - Utilizing an SPV to purchase 95% interest in loans
  - An “Eligible Lender” defined the same as in the MSNLF
  - An “Eligible Borrower” defined the same as in the MSNLF
    - May not participate in the MSNLF or the Primary Market Credit Facility

## MSELF—Loan Terms

- Must be a modification of an existing term loan extended *before* April 8, 2020, *and*
- The new advance—described as the “upsized tranche”—must be originated on or after April 8, 2020 with the following loan terms—
  - 4-year maturity
  - Amortization of principal and interest deferred for 1 year
    - Impliedly interest continue to accrue during deferral period
      - Compounding of interest not clear
  - Variable rate of interest based upon SOFR + 250-400 basis points
  - Minimum loan size of \$1 million
  - Maximum loan size that equal to the lesser of
    - \$150 million, or
    - 30% of the borrowers 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 EBITDA
  - Prepayment permitted without penalty

## Loan Origination and Administration

- **SPV Facility Fee—**
  - A lender must pay the SPV a facility fee of 100 basis points of the principal amount of the loan participation purchased by the SPV
    - The facility fee may be passed-on to the borrower
    - Not required for an MSELF loan (probably a typo)
- **Loan Origination Fee—**
  - A borrower must pay a lender an origination fee of 100 basis points of the principal amount of the loan
- **Servicing Fee—**
  - The SPV will pay a lender 25 basis points per annum of the principal amount of its participation in the loan for loan servicing
- **Facility Termination—**
  - The SPV will cease purchasing participations in loans on September 30, 2020, unless extended

## Attestations

- **The lender must attest that—**
  - The loan proceeds of the loan will not be used to repay or refinance pre-existing loans or lines of credit made by the Eligible Lender to the Eligible Borrower
  - The Lender will not cancel or reduce any existing lines of credit outstanding to the Eligible Borrower
    - Including the pre-existing portions of a MSELF
- **Both lenders and borrowers must certify that the borrowing entity is eligible to participate in the loan program, including the conflicts of interest prohibition in section 4019(b) of the CARES Act.**

## Eligible Lender and Borrower Attestation

- A borrower must attest that it—
  - Will not seek to cancel or reduce any of its outstanding lines of credit with the originating lender (or any other lender)
  - Will “commit” to refrain from using the proceeds of the loan to repay other loan balances
  - Must “commit” to refrain from repaying other debt of equal or lower priority, with the exception of mandatory principal payments, unless the borrower has repaid the Title IV loan in full
  - Requires financing due to the exigent circumstances presented by the coronavirus disease 2019 (“COVID-19”) pandemic
  - Using the proceeds of the loan, it will make reasonable efforts to maintain its payroll and retain its employees during the term of the loan
  - It meets the EBITDA leverage conditions for the program, and
  - It will follow compensation, stock repurchase, and capital distribution restrictions that apply to direct loan programs under section 4003(c)(3)(A)(ii) of the CARES Act

## Main Street Lending Program Concerns



Erik Detlefsen

## Program Concerns—Lender

### Lender Eligibility

- Private Funds Excluded
- U.S. Branches of Foreign Banks
- Syndicated Loans—Participant Bank Eligibility Analysis

### Lender Interests

- Legal risk to banks—required attestation may limit program to known bank customers
- Underwriting will be extensive and time-consuming
- Basic documentation will have to be drafted
- Incorporation of reps and warrants of borrowers
- Who represents the Treasury and the FRB?

## Program Concerns—Borrower

### Borrower Eligibility

- Leverage Requirements—No GAAP Concept and No Add-Backs
- Domestic Companies with Foreign Operations
- Domestic Companies with Foreign Ownership

### Borrower Interests

- These are “real” lending programs, not free money
- Loan terms impose significant restrictions

## Program Concerns—Operational

- **Program Restrictions Impact Existing Loans—Repayment; Lender Consent**
- **Restrictions on Distributions—Taxes; Management Fees**
- **MSELF Documentation—Different Terms (Interest Rate, Amortization, P&I Deferral, Maturity)**
- **SOFR Not Yet Operational**
- **Unique Amortization Structure**
- **Collateral and Intercreditor Issues for MSELF**
- **Voting/Participant Rights for the SPV**

## Program Concerns

- **Treasury and FRB staff are not commercial lenders**
- **Treasury announced guidelines will not be issued for a week or more**
- **Registration by lenders and application logistics still to be determined**

## Questions and Comments Directed to Treasury

- **The Extended Main Street Facility**—The language describing the Extended Main Street Facility uses the term “tranche,” and the context indicates that it is intended to be used to modify an existing credit extension
  - The credit had to be originated before April 8, 2020, and the upsized tranche extended on or after April 8, 2020
  - This structure significantly detracts from usefulness
  - Allow stand-alone loans and lines of credit (recommended)
- **Use of EBITDA**—The EBITDA ratio-based limitation on loan amounts is a restrictive and overly simplistic approach to assessing both need and credit-worthiness of potential borrowers
  - Allow a more holistic analysis
  - Not a formal accounting principle

## Questions and Comments Directed to Treasury

- **Operating Restrictions**—Given that loans under the two Main Street Programs carry meaningful operating restrictions, many companies are put in a difficult position
  - The two Main Street Programs should provide more flexibility for companies to apply and qualify for a loan now, but be able to draw down on it at a later date if needed, and only upon drawing on the facility would they then become subject to the operating restrictions
- **CARES Act Compliance**—Statements made by FRB representatives imply that the Main Street Programs announced earlier this week appear to be Treasury's and the Federal Reserve's implementation of the program described in 4003(c)(3)(D) “Assistance for Mid-Size Businesses” of the Cares Act.
  - The two Main Street Program vary from the CARES Act in significant ways
    - The 2% rate cap
    - Availability to non-profits
- **Documentation**—Will a bank be permitted to use its current commercial loan documentation for either of the two Main Street Programs?
  - Will the FRB provide authority similar to that provided for the SBA's PPP for a bank to originate the two Main Street Programs, or will the FRB or an agent of the FRB have to first sign-off?
  - Because by its terms (except for the aviation and national security loans authorized under Title IV of the Cares Act, taking equity or warrants is discretionary, what entity will have the authority to negotiate those and similar loan contract terms and conditions?

## Questions and Comments Directed to Treasury

- **Bank Attestation**—The attestation/certification requirements imposed on a bank for either of the two Main Street Programs creates possible unreasonable legal risk for banks
  - May deter a bank from either making a loan or may result in extensive due diligence
- **Waivers**—Will a bank making loan under either of the two Main Street Programs be authorized to waive requirements under the two programs?
  - For example, are the EBITDA limits waiveable?

## Questions and Comments Directed to Treasury

- **Registration by Banks with the SPV**—When will guidance be issued (and loan contract terms and conditions) for banks to register to sell participations in loans originated under the two programs to the SPV?
  - Will it be permissible to syndicate loans originated under the two Main Street Programs?
  - Will securitization be permitted in a manner whereby the SPV would issue a guaranty rather than purchasing a tranche?
- **Loan Terms**—For either of the two Main Street Programs:
  - Will the rate of interest be capped at 2% per annum?
  - During the deferral period, is it correct that interest will continue to be accrued; may it be compounded?
  - Are lenders permitted to impose other fees and charges not prohibited by the terms of the two Main Street Programs?
- **FBOs**—For foreign banking organizations (“FBOs”), is it necessary that a foreign bank either have a FDIC-insured branch or agency or an intermediary holding company in order to be an eligible lender under the two Main Street Programs?



## Questions and Comments Directed to Treasury

- **Foreign-Owned Businesses**—applicant companies are required to list their owners, including tax ID and address
  - However, the SBA system, Etrans, does not accept non-US TINs or addresses
  - Foreign companies employ over 7 million Americans; this inequitably limits access to the PPP to an important market segment
- **SBA Participation by Banks**—Will banks/lenders have an option to alert prudential bank regulators as to how they are attempting to meet the requirements of the PPP and related SBA requirements (including doing nothing)?
  - Further, will lenders be required to perform standard ongoing reporting as is the case with other SBA 7(a) programs?



## Need Credit?

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## Questions

If you have questions, you are welcome to follow-up directly with the presenters or call on your trusted Dorsey contact.



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