COVID-19: ANALYSIS OF FEDERAL RESERVE "MAIN STREET" LIQUIDITY PROGRAM

Date: 10 April 2020

U.S. Restructuring and Insolvency Alert

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On April 9, 2020, the Federal Reserve Bank announced preliminary details of two new loan facilities of up to $600 billion dollars, offered as part of the Coronavirus Aid, Relief, and Economic Security Act, or “CARES Act.” Together, the “Main Street” facilities are intended to support mid-sized borrowers with up to 10,000 employees or $2.5 billion in 2019 revenues.

Although the titles are similar, the main difference between the programs is that the Main Street New Loan Facility (the “MSNLF”) is for new loans of up to the lesser of $25m or a total of 4X 2019 EBITDA to borrowers who do not already have loans from the lender bank, while Main Street Expanded Loan Facility (“MSELF”) is intended to allow borrowers to upsize existing credit facilities by up to $150m, 30% of the borrower's aggregate bank debt or a total of 6X 2019 EBITDA. Our finance and policy teams have prepared a combined term sheet summarizing the key aspects of each Main Street facility and have also prepared a redline comparison of the two Main Street term sheets released by the Federal Reserve.

While we await further guidance and details from the Federal Reserve on the key details, a few points are worth noting in addition to the linked summary term sheet:

- First and foremost and at the risk of stating the obvious, these loans are not forgivable, unlike the CARES Act's Paycheck Protection Program (“PPP”) loans to small businesses and other eligible recipients.
- A key question will be whether borrowers, especially under MSELF, can use the current EBITDA measure from their existing credit facility to calculate the 6X limit (which is also the Federal Reserve's historic leveraged lending “red line”). Most debt covenants are currently based on “adjusted” EBITDA, which has long been the subject of much debate with respect to the prior leveraged loan guidance. In light of the present uncertainty, the Federal Reserve may be more reluctant to allow generous addbacks, especially because the starting point is already 2019 EBITDA. Because the COVID-19 impacts began for most U.S. businesses in February or early March, most prospective borrowers will have 2019 EBITDA which is almost surely higher than their trailing-twelve-month (“TTM”) EBITDA as of the end of March 2020. In many cases, 2019 EBITDA will be significantly higher than the TTM measure.
- The CARES Act imposed limits on executive comp, stock buybacks, and dividends for the Federal Reserve direct-lending and “mid-sized” facilities, but did not require that such limits apply to the Main Street facility. Many had hoped that the Federal Reserve would use the Main Street facility precisely to avoid those limits, but instead, the Federal Reserve has incorporated them to both MSNLF and MSELF.

We likely will need further guidance from the Federal Reserve as to whether and, if so, how, these limits apply to pass-through and other non-corporate entities and their owners.

- Both MSNLF and MSELF are available only to support loans made by federally insured depositary institutions and savings & loans (and their holding companies). This leaves private non-bank lenders out in the cold somewhat, but they also will not be constrained by the red-line or 4X leverage limit, and are not required to impose the executive compensation and equity limits. Thus, non-bank lenders will likely remain attractive borrowing options for many middle market companies and private equity sponsors, especially if business development companies (BDCs), private credit funds, and other non-bank lenders are able to take advantage of the additional Federal Reserve liquidity facilities for their own balance sheets and liquidity. This may become especially relevant in light of the SEC action earlier this week, which provided borrowing flexibility for BDCs. See our alert on the SEC action here.

The PPP term sheets, Q&A guidance, and regulations were updated several times after they were first issued, and we expect the same will happen with the Main Street facilities. Our team will monitor for future guidance from the Federal Reserve Board. Please contact any member of our team if we can be of assistance.

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