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Client Alert

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Implications of the Main Street Lending Program on Existing Debt

Overview

On April 30, 2020, the Federal Reserve announced certain updates to its Main Street Lending Program. Through the Main Street Lending Program, the Federal Reserve will purchase up to $600 billion in participations in “Eligible Loans” made to “Eligible Borrowers” from “Eligible Lenders.” The updates to the Main Street Lending Program are reflected in revised term sheets for each of the Main Street Facilities and in a FAQ that answers supplemental questions (the FAQ can be found here). A detailed summary of the full terms of the Main Street Lending Program can be found here.

The Main Street Lending Program comprises three distinct facilities authorized under Section 13(3) of the Federal Reserve Act: the Main Street New Loan Facility (the **New Facility**), the Main Street Priority Loan Facility (the **Priority Facility**) and the Main Street Expanded Loan Facility (the **Expanded Facility**, and together with the New Facility and the Priority Facility, the **Main Street Facilities**). The New Facility and the Priority Facility facilitate the availability of new loans to Eligible Borrowers with the Priority Facility providing larger maximum loan sizes than the New Facility along with different repayment terms. The Expanded Facility facilitates increases to Eligible Borrowers’ existing credit facilities through the addition of term loan tranches to those facilities.

This summary focuses on considerations for potential borrowers under the Main Street Lending Program with respect to their existing debt facilities, including restrictions the Main Street Facilities place on preexisting debt and provisions in current loan agreements that may be impacted by a Main Street Facility.

Restrictions and Considerations Relating to Existing Debt

Main Street Lending Program borrowers should consider restrictions the Main Street Facilities place on their existing debt facilities and the other implications of entering into a Main Street Facility.

1. **Limited Prepayment of Outstanding Debt.** Main Street Facilities prohibit the prepayment of other debt while an Eligible Loan is outstanding. This restriction does not limit (i) making debt payments that are mandatory and due, (ii) repaying a line of credit in the normal course, (iii) taking on and paying debt obligations required in the normal course of business (including inventory and equipment financing), provided that such debt is secured by newly acquired property and (iv) refinancing maturing debt.

2. **Potential Option to Refinance Existing Debt at Origination.** The Priority Facility allows Eligible Borrowers to refinance existing debt owed to a non-Eligible Lender at the time the Eligible Loan is originated. There is currently no explicit restriction on using funds from an Eligible Loan to refinance, but parties interested in doing so should carefully review any further guidance released by the Federal Reserve.

3. **Need to Amend Existing Debt Documents.** Under the Expanded Facility, Eligible Borrowers can add a new tranche of term loan debt to their existing facility with an Eligible Lender. Because this addition requires amendments to existing debt documents, Eligible Borrowers should consider amendment procedures and required consents.

4. **Eligible Lenders; Exclusion of Nontraditional Lenders.** Eligible Borrowers may consider seeking an Eligible Loan from their existing lender. "Eligible Lenders" under the Main Street Facilities include the following: a US federally insured depository institution, a US branch or agency of a foreign bank, a US bank holding company, a US savings and loan holding company, a US intermediate holding company of a foreign banking organization or a US subsidiary of any of the foregoing. Nontraditional lenders do not qualify as Eligible Lenders, but Borrowers may still participate in the Main Street Facilities, including the Expanded Facility, if nontraditional lenders are part of their existing syndicate (for purposes of the Eligible Loan that is being upsized through the Expanded Facility).

Credit Agreement Provisions to Consider in Connection with the Main Street Facilities

Entering into an Eligible Loan should be done after a careful review of existing debt agreements. Loan agreement provisions commonly impacted by borrowing under a Main Street Facility include those described below.

- **Mandatory Prepayments.** The proceeds of an Eligible Loan may be picked up in the mandatory prepayment provisions of a loan agreement—for example, some loan agreements require the proceeds from the incurrence of additional debt be used to pay down the existing debt.

- **Representations and Warranties.** Eligible Borrowers with existing revolving lines of credit should consider whether incurring additional debt will impact their ability to bring down representations and warranties at the time of a future draw. Representations and warranties that may be of particular concern include those relating to contravention of material contracts, defaults, priority of liens and burdensome restrictions.

- **Negative Covenants:**

    - **Burdensome Restrictions.** Many loan agreements prohibit borrowers from entering into new agreements that place "burdensome restrictions" on their ability to make dividends and grant liens on their assets. Main Street Facilities prohibit Eligible Borrowers from repaying the principal balance of, or any interest on, existing debt until the Main Street Loan is repaid in full, unless the debt or interest payment is mandatory and due. The Main Street Facilities also provide that Eligible Borrowers cannot make any distributions or pay any dividends (other than distributions necessary to cover tax payments for S Corps and other tax pass-through entities) in respect of common stock of the Eligible Borrower until one year after the Eligible Loan is no longer outstanding. Depending on how a loan agreement defines burdensome restrictions, that negative covenant may be tripped by one or more of these restrictions in Main Street Facilities.

    - **Liens.** Most loan agreements prohibit placing additional liens on a borrower's property except in limited instances. The Expanded Facility and Priority Facility require loans be senior to or *pari passu* with existing debt, which would require additional liens on the Eligible Borrower's property if the Eligible Borrower's existing debt is secured.

    - **Indebtedness.** Loan agreements commonly restrict the incurrence of additional debt, and entering into a Main Street Loan will violate this restriction unless the loan agreement includes a carve-out for the Main Street Facility.

- **Restricted Payments.** Main Street Facilities prohibit Eligible Borrowers from making distributions or paying dividends (other than distributions necessary to cover tax payments for S Corps and other tax pass-through entities) for one year after the Eligible Loan is no longer outstanding. Although most loan agreements restrict payments of this type from being made while the debt is outstanding, most loan agreements also contain carve-outs from that restriction. Potential Eligible Borrowers need to evaluate the impact of losing that flexibility by entering into the Eligible Loan.

- **Prepayment of Indebtedness.** Certain loan agreements prohibit payment of other indebtedness except scheduled payments of principal and interest. This restriction may prevent Eligible Borrowers from prepaying an Eligible Loan (despite prepayments being permitted under the Main Street Facilities).

- **Financial Covenants.** Incurring additional debt may impact the financial covenants in a loan agreement (for example, leverage ratios and the fixed charge coverage ratio). Eligible Borrowers should consider how the debt will be included in financial covenant calculations.

- **Cross-Default.** Most loan agreements contain a cross-default provision, providing that a default under other material contracts constitutes a default under the loan agreement. An event of default under the Main Street Loan may result in an event of default under an Eligible Borrower's existing loan agreement.

- **Collateral Considerations Relating to the Expanded Facility and Priority Facility.** Under the Expanded Facility and Priority Facility, Eligible Loans must be senior to or *pari passu* with the Eligible Borrower's other loans or debt instruments (other than mortgage debt). Eligible Borrowers should review intercreditor agreements and any collateral provisions in debt documents to determine the relative rights of each separate lender to ensure compliance for purposes of the Eligible Loan and existing loan and debt instruments.

- **Collateral Considerations Relating to the New Facility.** Under the New Facility, Eligible Loans cannot be contractually subordinated in terms of priority to any of the Eligible Borrower's other loans or debt instruments.

Next Steps and Conclusions

There is still substantial uncertainty regarding the Main Street Lending Program, and it is unclear how attractive these loans will be to borrowers considering collateral requirements, restrictive terms, a four-year maturity date and limitations on existing debt. It is possible those with existing lending relationships will look to a private solution for additional debt (even if that solution is more expensive), and those without existing lending relationships may turn to the Main Street Facilities.

The Federal Reserve has not yet announced a launch date for the Main Street Facilities and it is possible that further guidance may be released. Potential borrowers under the Main Street Facilities should carefully review existing loan and debt agreements and begin conversations with existing lenders regarding their entry into an Eligible Loan.

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