Guide to the Federal Reserve's Main Street and Other Lending Programs in Response to COVID-19 Pandemic

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Skadden

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Update: The Federal Reserve has made changes and provided additional guidance on some of these programs after publication of this guide. For example, the Federal Reserve released revised term sheets and guidance with respect to the Main Street lending program on April 30, 2020. Please see our "Updated Guide to the Main Street Lending Program as of May 7, 2020."

Background

The Coronavirus Aid, Relief, and Economic Security Act (CARES Act) became law on March 27, 2020. The economic stimulus package in the CARES Act includes federal funding for business stimulus across three broad categories.

First, the CARES Act provides approximately $350 billion to support small businesses through programs administered by the Small Business Administration (SBA), including the Paycheck Protection Program (PPP). To be eligible for a PPP loan, a business must generally have no more than 500 employees. Some banks began accepting applications for PPP loans on April 3, 2020. Rollout of the PPP has been uneven across banks, SBA systems have struggled to handle the initial volume of loans, and the government continues to refine its guidance under the PPP. See Skadden's April 6, 2020, client alert, "COVID-19 Pandemic Small Business Lending Under the CARES Act's Paycheck Protection Program."

Second, the CARES Act authorizes the U.S. Department of the Treasury (Treasury) to provide more than $45 billion of support in the form of grants and loans to (i) passenger air carriers and certain related businesses, (ii) cargo air carriers and (iii) businesses critical to maintaining national security. Treasury has released guidelines and application forms for these industry-specific programs.

Third, the CARES Act authorizes Treasury to invest more than $450 billion in lending programs to be established by the Federal Reserve. This guide summarizes these Federal Reserve programs. The first three Federal Reserve programs summarized in the table below (Main Street New Loan Facility, Main Street Expanded Loan Facility and Primary Market Corporate Credit Facility) each involve the extension of credit by Federal Reserve vehicles with proceeds to be received directly by individual businesses. The remaining seven programs are more focused on providing liquidity to various areas of the financial markets, including corporate bonds, asset-backed securities, commercial paper, money market mutual funds, and state and municipal obligations.

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Reliance on Federal Reserve Emergency Lending Authority

The total dollars available under these Federal Reserve programs will be much greater than the $450 billion authorized for Treasury investment under the CARES Act because these programs will also draw on the Federal Reserve's practically unlimited financial capacity as the U.S. central bank. The Federal Reserve lending into these programs will leverage the total dollars available into the trillions. The Federal Reserve has long-standing authority under Section 13(3) of the Federal Reserve Act to implement broad-based lending programs in "unusual and exigent circumstances."[1] However, the Federal Reserve's emergency lending authority under Section 13(3) is subject to certain conditions that affect the design and eligibility of its programs. These conditions, including the three key concepts described below, apply to all of the programs summarized in this guide.

Treasury Investment in Programs Mitigates Credit Risk to Federal Reserve

Section 13(3) limits the Federal Reserve's ability to take credit risk in connection with emergency lending programs. A key purpose of Treasury's investment in certain of these programs is to mitigate credit risk to the Federal Reserve in order to satisfy these legal conditions. Treasury's equity investments in those programs protect the credit extended by the Federal Reserve by absorbing first losses.

Participants Must Not Be Insolvent

The Federal Reserve is not permitted to use its emergency lending authority to lend to parties who are "insolvent." Federal Reserve regulations generally define the term "insolvent" to mean that a party is in bankruptcy or a similar insolvency proceeding or is generally not paying undisputed debts as they come due during the 90 days preceding its participation in the Federal Reserve program. Applicants to participate in these programs will likely be required to provide a certification (and perhaps a financial statement to evidence) that they are not insolvent.

Unable To Secure Adequate Credit Accommodations From Other Banking Institutions

When implementing an emergency lending program, Section 13(3) requires the Federal Reserve to obtain evidence that participants are "unable to secure adequate credit accommodations from other banking institutions." Federal Reserve regulations provide flexibility in how the Federal Reserve can meet this requirement. For example, the Federal Reserve may rely on evidence of economic or market conditions generally or on a simple certification from the participant. The materials released to date do not suggest that the Federal Reserve is going to require each prospective participant in a program to provide individualized evidence of its own efforts or inability to "secure adequate credit accommodations from other banking institutions."

Eligibility Criteria Regarding U.S. Presence

Certain of these Federal Reserve programs, as indicated in the table below, require that their participants meet the following basic criteria related to U.S. presence: (i) be a business created or organized in the United States or under the laws of the United States; (ii) have "significant operations" in the United States; and (iii) have a majority of its employees based in the United States. Nothing in the CARES Act or the Federal Reserve guidance to date suggests that a party who otherwise meets these U.S. presence criteria would be disqualified from participating solely because it has a non-U.S. parent company.

The Main Street Programs and Their Additional Conditions

The Federal Reserve either announced or foreshadowed most of these programs several weeks ago. However, those initial announcements were generally high-level and with few details. On April 9, 2020, the Federal Reserve released additional guidance on many of the programs. Of particular interest to many businesses, the Federal Reserve for the first time outlined the basic eligibility, terms and mechanics of its Main Street programs intended to provide credit to medium-sized businesses.

There are two Main Street programs: the Main Street New Loan Facility and the Main Street Expanded Loan Facility. Both are intended to provide credit to U.S. businesses with either no more than 10,000 employees or no more than $2.5 billion in 2019 revenues. Both Main Street programs rely on banks to originate and service low-interest term loans that meet the criteria outlined in our table below. The originating bank may then sell a 95% participation in the qualifying loans to a special purpose vehicle backed by funding from the Federal Reserve and Treasury. The Federal Reserve has announced that the two Main Street programs will together purchase up to $600 billion of qualifying loans.

The principal substantive difference between the two Main Street programs is the maximum available loan size. Although the maximum loan size for a particular borrower may be lower, the outright maximum loan size under the Main Street New Loan Facility is $25 million; whereas, the outright maximum loan size under the Main Street Expanded Loan Facility is $150 million. In order to qualify for the larger loan size under the Main Street Expanded Loan Facility, the credit under the program must take the form of

[1] *See* 12 U.S.C. § 343(3); 12 C.F.R. § 201.4(d).

an "upsized tranche" attached to a pre-existing term loan from a U.S. bank and originated with the borrower prior to April 8, 2020. Importantly, the pre-existing term loan need not itself meet any specific criteria, and the Federal Reserve appears to contemplate that the terms of the "upsized tranche" may differ materially from the terms governing the pre-existing piece of the term loan. We believe the policy rationale for a larger maximum loan size in the context of an "upsized tranche" to an existing bank loan is that the Federal Reserve derives some comfort that its credit risk is mitigated by a federally regulated bank having already underwritten and decided to extend its own credit to the borrower.

The Main Street programs will each use funds provided by Treasury under the CARES Act and involve direct loans. For this reason, borrowers in either Main Street program must adhere to the following additional conditions related to stock buybacks, capital distributions and compensation. These conditions do <u>not</u> apply to participants in the other Federal Reserve programs summarized in the table below.

Prohibition on Certain Buybacks and Capital Distributions

Until 12 months after the date the loan is no longer outstanding, a Main Street borrower may not (i) repurchase equity securities of itself or its parent that were listed on a national exchange while the loan was outstanding, except as otherwise required pursuant to a contract in effect on March 27, 2020, or (ii) pay dividends or make other capital distributions on common stock.

Limits on Compensation

Until one year after the date the loan is no longer outstanding, a Main Street borrower must comply with the following compensation limitations.

An officer or employee of the borrower whose total compensation exceeded $425,000 in calendar year 2019 may not receive (i) total compensation from the borrower during any 12-consecutive-month period exceeding the total compensation that individual received in calendar year 2019 or (ii) severance pay or other benefits upon termination of employment exceeding twice the total compensation that individual received in calendar year 2019. This limitation does not apply to employees whose compensation is determined through an existing collective bargaining agreement entered into prior to March 1, 2020.

An officer or employee of the borrower whose total compensation exceeded $3 million in calendar year 2019 may not receive total compensation from the borrower during any 12-consecutive-month period in excess of the sum of $3 million plus 50% of the total compensation over $3 million the individual received in calendar year 2019.

Main Street Programs Not To Be Confused With Assistance to Mid-Sized Businesses in CARES Act

The CARES Act included provisions requiring Treasury to "endeavor" to establish a program for "Assistance for Mid-Sized Businesses." The CARES Act requires that the receipt of assistance under such a program be conditioned on the borrower making a series of certifications. For example, a borrower under such a program would be required to make certifications about retaining 90% of its workforce, restoration of compensation and benefits, outsourcing and offshoring, collective bargaining agreements and union organizing. Importantly, the Main Street programs are not authorized pursuant to these provisions of the CARES Act, and participation in the Main Street programs does <u>not</u> require the borrower to make these certifications. To date, Treasury has not released any information about, or suggested that it is working on, a program pursuant to the Assistance for Mid-Sized Businesses provisions of the CARES Act.

Implementation

The Federal Reserve faces a daunting task of initiating multiple, complex programs in a short period of time — all while its staff face challenging work conditions. In addition, the Main Street programs depend on banks to originate, service and retain a portion of loans to the borrowing companies. As we have seen with the PPP loans for small businesses, the need for banks to understand, become comfortable with and develop systems for an entirely new government-backed lending program introduces additional complexity. Thus, we expect the implementation of these programs will be uneven and iterative.

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What Is the Program?	Who Is Eligible?	How Will It Work?	What Are the Key Economic Terms for Participants?
MSNLF **Main Street New Loan Facility**	Borrower <u>either</u> has no more than 10,000 employees <u>or</u> had no more than $2.5 billion in 2019 revenues Borrower must not be insolvent Borrower must meet basic criteria regarding U.S. presence described in introduction Borrower may not also participate in the MSELF or the PMCCF	Borrower applies for and obtains a qualifying loan from a U.S. FDIC-insured depository institution or its U.S. parent company SPV backed by the Federal Reserve and Treasury will purchase from the lender at par a 95% participation in the qualifying loan Borrower must attest that "it requires financing due to the exigent circumstances presented by [COVID-19] and that, using proceeds of the [program loan], it will make reasonable efforts to maintain its payroll and retain its employees during the term of the [program loan]." Program imposes conditions to ensure that program loan is not used to repay or refinance pre-existing loans or lines of credit and that pre-existing lines of credit are not reduced or canceled Borrower subject to additional restrictions on buybacks, capital distributions and compensation as described in the introduction Program will cease purchasing no later than September 30, 2020, unless extended by the Federal Reserve and Treasury	Unsecured term loan Four-year maturity Prepayment permitted without penalty Adjustable rate of SOFR + 250-400 bps Amortization of principal and interest deferred for one year Origination fee paid by borrower to lender of 100 bps Annual servicing fee paid by SPV to lender of 25 bps of SPV's participation in the loan Facility fee paid by borrower or lender to SPV of 100 bps of SPV's participation in the loan Maximum loan size is <u>lesser</u> of: (i) $25 million; or (ii) an amount that, when added to the borrower's existing (a) outstanding debt and (b) committed but undrawn debt, does not exceed <u>four</u> times the borrower's 2019 EBITDA

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MSELF **Main Street Expanded Loan Facility**	Borrower <u>either</u> has no more than 10,000 employees <u>or</u> had no more than $2.5 billion in 2019 revenues Borrower has an existing term loan made by a U.S. FDIC-insured depository institution or its U.S. parent company that was originated before April 8, 2020 Borrower must not be insolvent Borrower must meet basic criteria regarding U.S. presence described in introduction Borrower may not also participate in the MSNLF or the PMCCF	Borrower applies for and obtains from the same eligible lender (i.e., a U.S. FDIC-insured depository institution or its U.S. parent company) on its existing term loan an "upsized tranche" that meets the requirements of the program SPV backed by the Federal Reserve and Treasury will purchase from the lender at par a 95% participation in the upsized tranche Borrower must attest that "it requires financing due to the exigent circumstances presented by [COVID-19] and that, using proceeds of the [upsized tranche], it will make reasonable efforts to maintain its payroll and retain its employees during the term of the upsized tranche." Program imposes conditions to ensure that upsized tranche is not used to repay or refinance pre-existing loans or lines of credit and that pre-existing lines of credit are not reduced or canceled Borrower subject to additional restrictions on buybacks, capital distributions and compensation as described in the introduction Program will cease purchasing no later than September 30, 2020, unless extended by the Federal Reserve and Treasury	Existing term loan and upsized tranche may be secured or unsecured Upsized tranche has four-year maturity Upsized tranche may be prepaid without penalty Upsized tranche has adjustable rate of SOFR + 250-400 bps Amortization of principal and interest on upsized tranche deferred for one year Origination fee paid by borrower to lender of 100 bps of the upsized tranche Annual servicing fee paid by SPV to lender of 25 bps of SPV's participation in the upsized tranche Unlike MSNLF, no facility fee Maximum size of upsized tranche is <u>lesser</u> of: (i) $150 million; (ii) 30% of the borrower's existing (a) outstanding <u>bank</u> debt and (b) committed but undrawn <u>bank</u> debt; or (iii) an amount that, when added to the borrower's existing (a) outstanding debt and (b) committed but undrawn debt, does not exceed six times the borrower's 2019 EBITDA

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PMCCF **Primary Market Corporate Credit Facility**	Issuer/borrower must be investment-grade (BBB-/Baa3 or better); if investment-grade on March 22, 2020, but subsequently downgraded, must be BB/Ba3 or better at time of program purchase Issuer/borrower must not be insolvent Issuer/borrower must meet basic criteria regarding U.S. presence described in introduction Issuer/borrower has not received "specific support" pursuant to CARES Act or any subsequent federal legislation Issuer/borrower is not an FDIC-insured depository institution or its parent company Issuer/borrower may not also participate in the MSNLF or the MSELF	SPV backed by the Federal Reserve and Treasury will purchase (i) eligible bonds in new issuance as sole investor and (ii) up to 25% of eligible syndicated loans and bonds as part of a syndicate Program will cease purchasing no later than September 30, 2020, unless extended by the Federal Reserve and Treasury	At time of purchase, maturity of four years or less For bonds that are not syndicated, pricing will be issuer-specific and "informed by market conditions" For loans or bonds that are syndicated, same pricing as received by other syndicate members Facility fee of 100 bps Maximum amount of outstanding bonds or loans of an eligible issuer that borrows from the program may not exceed 130% of its maximum amount of outstanding bonds or loans on any day between March 22, 2019, and March 22, 2020
SMCCF **Secondary Market Corporate Credit Facility**	Issuer/borrower must be investment-grade (BBB-/Baa3 or better); if investment-grade on March 22, 2020, but subsequently downgraded, must be BB/Ba3 or better at time of program purchase Issuer/borrower must not be insolvent Both issuer/borrower <u>and</u> seller into program must meet basic criteria regarding U.S. presence described in introduction Issuer/borrower has not received "specific support" pursuant to CARES Act or any subsequent federal legislation Issuer/borrower is not an FDIC-insured depository institution or its parent company	SPV backed by the Federal Reserve and Treasury will purchase from eligible sellers in the secondary market (i) eligible individual corporate bonds and (ii) U.S.-listed exchange-traded funds with a primary investment objective of exposure to U.S. investment-grade corporate bonds (with a lesser amount invested in ETFs with a primary investment objective of U.S. high-yield corporate bonds) Program will cease purchasing no later than September 30, 2020, unless extended by the Federal Reserve and Treasury	Purchases will be made in secondary market at fair market value Program will avoid purchasing ETFs at prices that materially exceed their estimated net asset value Maximum amount of bonds of an issuer that will be purchased under this program is capped at 10% of the issuer's maximum amount of bonds outstanding on any day from March 22, 2019, through March 22, 2020 Maximum amount of shares of a ETF is limited to 20% of the ETF's outstanding shares as measured at time of purchase

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TALF **Term ABS Loan Facility**	Borrower must (i) own eligible collateral and (ii) maintain an account relationships with a primary dealer Borrower must not be insolvent Borrower and collateral issuers must meet the basic criteria regarding U.S. presence described in introduction	SPV backed by the Federal Reserve and Treasury will make nonrecourse loans to eligible borrowers that are secured by eligible collateral Eligible collateral is USD-denominated cash ABS that: (i) have a credit rating in the highest long-term (or in the case of nonmortgage-backed ABS, the highest short-term) investment-grade rating category from at least two eligible nationally recognized statistical rating organizations (NRSROs) and no rating below the highest investment grade rating category from an eligible NRSRO; and (ii) all or substantially all of the underlying credit exposure: - (a) was originated by a company (that meets the basic criteria regarding U.S. presence described in the introduction); - (b) was issued on or after March 23, 2020 (except for commercial mortgage-backed securities, which must have been issued prior to March 23, 2020); and - (c) is limited to ABS backed by auto loans and leases, student loans, credit card receivables (consumer or corporate), equipment loans and leases, floorplan loans, insurance premium finance loans, certain small business loans that are guaranteed by the SBA, leveraged loans or commercial mortgages Program will not make new credit extensions after September 30, 2020, unless extended by the Federal Reserve and Treasury	Three-year loan terms Fully secured by eligible collateral Administrative fee assessed by SPV of 10 bps of the loan amount on the settlement date for collateral Interest rates will be: - CLOs: 150 bps over 30-day average SOFR; - SBA 7(a) loans: 75 bps over the top of the federal funds target range; - SBA 504 loans: 75 bps over the three-year fed funds overnight index swap (OIS) rate; - Other eligible ABS with underlying credit exposure that do not have a government guarantee: 125 bps over two-year OIS for securities with a weighted average life of less than two years or 125 bps over three-year OIS for securities with a weighted average of two years or greater; and - Other eligible ABS: Will be set forth in detailed terms and conditions that are to be provided at a later date Pledged eligible collateral will be valued and assigned a haircut according to a schedule that is consistent with the original TALF program. With respect to the newly added leveraged loans category (for static CLOs), the base haircut for pools with an average life of five years or less is 20% of par, increasing by one percentage point of par for each additional year

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CPFF **Commercial Paper Funding Facility**	Participant must be U.S. issuer of commercial paper (including municipal issuers and U.S. issuers with a foreign parent company) that (i) is an entity organized under the laws of the United States, or a political subdivision or territory thereof, or a U.S. branch of a foreign bank; (ii) meets certain ratings requirements; and (iii) has issued asset-backed commercial paper to institutions other than the sponsoring institution for any consecutive period of three months or longer between March 16, 2019, and March 16, 2020 Participant must not be insolvent	Program will support issuance of term commercial paper by supporting purchases of eligible commercial paper Primary dealers will purchase from eligible issuers three-month USD-denominated commercial paper, which an SPV backed by the Federal Reserve and Treasury will then purchase from primary dealers Amount of commercial paper of a particular issuer that may be purchased under this program depends in part on the issuer's rating Program will cease purchasing commercial paper on March 17, 2021, unless extended by the Federal Reserve and Treasury, but the Federal Reserve will continue to fund the SPV after such date until the SPV's underlying assets mature	Pricing for commercial paper that is rated A1/P1/F1 will be based on the then-current three-month OIS plus 110 bps (or in the case of downgraded issuers who still qualify, 200 bps) Facility fee paid by issuer to SPV of 10 bps of the maximum amount of the issuer's commercial paper the SPV may own
MMFL **Money Market Mutual Fund Liquidity Facility**	Borrower must be a (i) U.S. depository institution, (ii) U.S. bank holding company (parent company incorporated in the United States or U.S. broker-dealer subsidiary), or (iii) U.S. branch or agency of a foreign bank that purchases eligible collateral from eligible money market mutual funds Borrower must not be insolvent	Program will support the market for assets that underlie money market mutual funds Federal Reserve will extend nonrecourse credit to eligible banking organizations that are secured by assets purchased by the banking organization from eligible money market mutual funds Eligible collateral includes U.S. treasuries, asset-backed commercial paper that has certain short-term ratings, certain municipal variable demand notes, certain bank certificates of deposit, etc., that were purchased from eligible money market funds Eligible money market fund must be a fund that identifies itself as a Prime, Single State or Other Tax-Exempt money market fund on Securities and Exchange Commission Form N-MFP Program will not make new credit extensions after September 30, 2020, unless extended by the Federal Reserve and Treasury	Rate of loan will depend on the collateral securing the loan (*i.e.*, range from primary credit rate in effect at applicable Federal Reserve Bank to 100 bps over such primary credit rate) No special fees associate with the program

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PDCF **Primary Dealer Credit Facility**	Borrower must be a primary dealer of the Federal Reserve Bank of New York that has eligible collateral Borrower must not be insolvent	Program will help primary dealers support smooth market functioning by providing primary dealers with short-term loans Federal Reserve will offer overnight and term funding to primary dealers with eligible collateral with recourse to the primary dealer itself Eligible collateral includes collateral eligible for pledge in open market operations, investment grade corporate debt securities, international agency securities, commercial paper, municipal securities, etc. Program will continue to lend to primary dealers until at least September 20, 2020, or longer if conditions warrant	Up to 90-day term Loans will be made at a rate equal to the primary credit rate in effect at the Federal Reserve Bank of New York offered to depository institutions via the Discount Window
PPPLF **Paycheck Protection Program Liquidity Facility**	Borrower must be a depository institution that originates PPP loans Borrower must not be insolvent Federal Reserve indicated it was working to expand eligibility to other lenders that originate PPP loans "in the near future"	Program will promote the PPP SPV backed by the Federal Reserve and Treasury will make nonrecourse loans to eligible borrowers that are secured by PPP loans guaranteed by the SBA Program will not make new credit extensions after September 30, 2020, unless extended by the Federal Reserve and Treasury	Extensions of credit under the program will be made at rate of 35 bps Principal amount of extension of credit will equal principal amount of underlying PPP loan No fees associated with the program Maturity date of an extension of credit under the program will equal the maturity date of the underlying PPP loan, but it will be accelerated (i) if the PPP loan goes into default and the borrower sells the loan to SBA to realize the SBA guarantee, or (ii) to the extent of any loan forgiveness reimbursement received by the borrower from the SBA

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MLF **Municipal Liquidity Facility**	Issuer must be a (i) U.S. state or the District of Columbia, (ii) U.S. city with a population exceeding 1 million residents or (iii) U.S. county with a population exceeding 2 million residents Issuer must not be insolvent	Program will support lending to eligible U.S. states, cities and counties SPV backed by the Federal Reserve and Treasury will purchase eligible notes from issuers Eligible notes are tax anticipation notes, tax and revenue anticipation notes, bond anticipation notes and other similar short-term notes issued by issuer Relevant legal opinions and disclosures will be required as determined by the Federal Reserve prior to purchase Issuer may use the proceeds to help manage the cash flow impact of income tax deferrals resulting from an extension of an income tax filing deadline; potential reductions of tax and other revenues or increases in expenses related to or resulting from the COVID-19 pandemic; and requirements for the payment of principal and interest on obligations of relevant state, city or county. (Issuer may also use the proceeds to purchase similar notes issued by, or otherwise to assist, political subdivisions and instrumentalities of the relevant state, city or county for the aforementioned purposes) Program will cease purchasing eligible notes on September 30, 2020, unless extended by the Federal Reserve and Treasury	Eligible notes must mature no later than 24 months from date of issuance Pricing will be based on the eligible issuer's rating at the time of purchase with details to be provided later Origination fee paid by issuer to SPV of 10 bps of the principal amount of the issuer's notes purchased by the SPV