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Locke Lord QuickStudy: Main Street Lending Program – Federal Reserve Announces Expanded Access for Some Businesses While Affiliation Rules Restrict Access for Others

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On June 8, 2020, the Federal Reserve announced that it is expanding the Main Street Lending Program (the “Program”) to allow more businesses to participate and to provide greater flexibility to borrowers in repaying loans under the Program. A link to the Federal Reserve’s official announcement of these changes, including the updated term sheets for the Program’s three facilities (the “Facilities”) and the Federal Reserve’s updated Frequently Asked Questions with respect to the Program (the “FAQs”) is available [here](#).

Expansion of Program Access for Businesses Based on Program Term Changes

The principal changes announced by the Federal Reserve are to the basic terms regarding loan size, term, amortization, and percentage of the participation interest to be held by the Main Street special purpose vehicle (the “SPV”), including the following:

- a reduction in minimum loan size under both the Main Street New Loan Facility (the “MSNLF”) and the Main Street Priority Loan Facility (the “MSPLF”) from \$500,000 to \$250,000;
- an increase in maximum loan size under the MSNLF from \$25 million to \$35 million;
- an increase in maximum loan size under the MSPLF from \$25 million to \$50 million;
- an increase in maximum loan size for the Main Street Expanded Loan Facility (the “MSELF”) from \$200 million to \$300 million, as well as elimination of the restriction limiting the loan size under the MSELF to 35% of the borrower’s existing pari passu debt;
- an extension of the maturity date for each Facility from four to five years;
- an extension of the period for deferral of principal payments under all Facilities from one to two years; and
- an expansion of the SPV’s participation percentage to 95% for all eligible loans, including loans made under the MSPLF.

Restrictions Based on Application of Affiliation Rules

While the Federal Reserve’s recent term changes will expand Program access for some businesses, the

application of the affiliation rules to the Program may continue to restrict access for others. The Federal Reserve's updated FAQs include new information on the affiliation rules that potential borrowers must consider in determining borrowing eligibility and maximum loan size. The following is a summary of certain of those affiliation provisions and their impact on a borrower's ability (and, in particular, a private equity portfolio company's ability) to access the Program.

General Eligibility Requirements. To be an "Eligible Borrower" under the Program, a Business¹ must meet the Program's maximum size limitations by having not more than (i) 15,000 employees or (ii) \$5 billion in 2019 annual revenues. To determine whether a Business meets those size criteria, the Business must aggregate its employees and revenues with the employees and revenues of its affiliates.

Affiliation Rules. For purposes of determining affiliation, the Program utilizes the affiliation standards set forth in the Small Business Administration ("SBA") regulations at [13 CFR 121.301\(f\)](#) (1/1/2019 ed.). Relevant details of those affiliation standards include the following:

- The SBA regulation provides that "[c]oncerns and entities are affiliates of each other when one controls or has the power to control the other, or a third party or parties controls or has the power to control both. It does not matter whether control is exercised, so long as the power to control exists."
- The SBA regulations provide seven tests for affiliation based on control, including (i) affiliation based on ownership, (ii) affiliation arising under stock options, convertible securities, and agreements to merge, (iii) affiliation based on management, (iv) affiliation based on identity of interest, (v) affiliation based on the newly organized concern rule, (vi) affiliation based on totality of the circumstances and (vii) affiliation based on franchise agreements.

For a summary of all of the SBA's affiliation rules, please see the SBA's guide to its affiliation rules. Potential borrowers should consult their advisors on the application of the SBA's affiliation rules to their specific circumstances. It is important to note that unlike the Paycheck Protection Program, which exempted (i) businesses receiving financial assistance from SBICs, (ii) businesses in the restaurant and hospitality sector, and (iii) certain businesses operating as franchises, from the application of the affiliation rules for purposes of borrower eligibility determinations, the Program does not incorporate any such exemptions.²

Application of Affiliation Rules to Determination of Facility Type and Maximum Loan Size. The affiliation rules also apply in determining which of the three Facilities an Eligible Borrower can access, as well as an Eligible Borrower's maximum loan size. The terms of the Program provide that an Eligible Borrower may participate in only one of the Program's three Facilities and the updated FAQs clarify that this restriction applies not only to a single Eligible Borrower, but also to an Eligible Borrower's affiliates. If an affiliate of an Eligible Borrower has participated, or has a pending application to participate, in one of the Program's Facilities, the Eligible Borrower is limited to participating in the same Facility as its affiliate.

The maximum dollar limitation applicable to a particular Facility will also limit the maximum loan size not only for a particular Eligible Borrower, but also for its affiliates. For example, an Eligible Borrower seeking to borrow under the MSNLF can only do so if none of its affiliates have borrowed, or have pending applications to borrow, under either of the MSPLF or the MSELF. In addition, if any of an Eligible Borrower's affiliates have borrowed (or have pending applications to borrow) under a Facility, the aggregate dollar cap on loans under that Facility will limit the maximum principal amount of loans available to such Eligible Borrower and its affiliates. Finally, if any of an Eligible Borrower's affiliates have borrowed (or have pending applications to borrow) under any Facility, its

maximum loan size will be limited not only by its own leverage level, but also by the leverage level of its affiliated group.

An Eligible Borrower seeking to borrow under one of the Program's Facilities will need to work with its affiliates to determine whether the Program is a viable borrowing option.

Impact of Affiliation Rules on Potential Private Equity Borrowers. While a private equity fund, itself, is barred from being an Eligible Borrower under the Program because a private equity fund is an "Ineligible Business" under the SBA regulations that the FAQs apply to the Program, a portfolio company of a private equity fund may borrow under the Program, provided it meets the eligibility criteria and relevant Facility's maximum loan size criteria, applying the applicable affiliation rules. The application of the affiliation rules will likely result in the aggregation of many portfolio companies with their respective private equity fund sponsors (and the other portfolio companies controlled by the private equity fund) for purposes of determining the portfolio company's size eligibility under the Program, as well as the type and amount of Main Street loan for which the portfolio company may be eligible. As a practical matter, this will likely serve as a significant hurdle to accessing the Program for many private equity portfolio companies.

Given the limitations the affiliation rules may impose on potential borrowers, businesses seeking to access the Program should evaluate the affiliation rules with their advisors to determine the extent to which the application of the affiliation rules will limit their participation in the Program.

Locke Lord team members will continue to publish further guidance on our COVID-19 Resource Center. Please visit our COVID-19 Resource Center often for up-to-date information to help stay informed of the legal issues related to COVID-19.

Your regular Locke Lord contacts and the authors of this article would be happy to help you navigate the CARES Act and associated guidance as they relate to or otherwise affect small and mid-sized businesses and their lenders.

Organizations that plan for their recovery and are rebuilding for the future will be better positioned for a post-pandemic world.

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1. Under E.2 of the FAQs, "Businesses" are defined as "legally formed entities that are 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 percent participation by foreign business entities; or a tribal business concern."
 2. The exemption under 13 CFR 121.103(b)(1) for companies "owned in whole or substantial part by" SBICs does, however, apply to break affiliation between an SBIC and its portfolio company.

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