

## COVID-19 – The Main Street Lending Program: Looking Back and Looking Ahead

January 11, 2021

The Main Street Lending Program (“MSLP” or the “Program”) is a financial assistance program established by the Federal Reserve System to support small and medium-sized businesses affected by the COVID-19 pandemic. Please consult [our previous Client Alerts](#) for MSLP terms.

### LOOKING BACK

#### **Expiration of Program**

The Federal Reserve extended the expiration date to January 8, 2021 in order to allow more time to process and fund loans submitted on or before the December 14, 2020 submission deadline. As of the date of this Client Alert, the Program has expired.

#### **Windels Marx MSLP Loan Closings**

From the time that the MSLP was first announced, our firm closely followed the Federal Reserve’s MSLP announcements and guidelines and rapidly developed expertise on the Program. We quickly began advising our banking and borrower clients through client alerts, formal presentations and Q&A sessions based on specific fact patterns. After tailoring loan documents for the Program and working our way through the Federal Reserve’s portal system and approval process, we were thrilled to be responsible for one of the first loan closings under the Program.

Following the Federal Reserve’s late November announcement of the loan submission deadline for the MSLP, borrowers and lenders alike rushed to meet the December 14 deadline. During the last week of November and the first week of December, Windels Marx was inundated with an influx of commitment letters for loans under the MSLP. Despite the unusually short time frame and pressure, our financing team closed six loan transactions for lenders and borrowers during that period.<sup>1</sup> Together with loans closed earlier in the year, Windels Marx handled a cumulative total of ten MSLP loan transactions that closed and funded during the MSLP’s brief tenure.<sup>2</sup>

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<sup>1</sup> During this period, our financing team also worked on six other loan transactions for lenders in which the borrowers changed their minds and withdrew prior to funding or closing.

<sup>2</sup> For New Jersey lender clients, our team included our partner Frank Quinn (who led on the loan structuring and loan closing matters), our partner Jonathan Gray (who managed program compliance and approval matters), and our associates Alan Stauber, Jeet Gulati and Brandon Ross. For New Jersey borrower clients, our team included our partner Jonathan Gray, our counsel Mark Larner and our special counsel Frank Biancola. For New York lender clients, our team included our partner Michael Clain, our counsel Lynn Weinig, our special counsel James Pastore, and our associates Mitch Markowitz and Andrew Stoecker. These teams were also supported by our paralegals, secretaries and administrative staff.

## **Review of Program Performance**

From its earliest iterations, the MSLP was subject to widespread criticism from the lending community and struggling businesses. Although the Federal Reserve repeatedly revised the MSLP's terms in the hopes of making it more attractive and responsive to the needs of prospective borrowers and lenders, these efforts were only met with limited success, and lender registration for the MSLP was underwhelming.

As of December 30, 2020, the MSLP held approximately \$16.5 billion in loan participations on its balance sheet, the majority of which appear to have been purchased in December 2020 as borrowers and lenders rushed to meet the final MSLP submission deadline.<sup>3</sup> This represents less than 3% of the \$600 billion in eligible loans authorized under the MSLP. Such limited utilization of the MSLP, together with the continued discontent expressed by its critics, led to the MSLP being largely characterized as a failure in the media.

## **Key Issues With the Program**

Some of the terms of the MSLP which limited its appeal to lenders and borrowers included the following:

- Concerns About Losing Money. Unlike the Paycheck Protection Program, the MSLP had no loan forgiveness features. To the contrary, the MSLP was designed by the Federal Reserve and the Treasury with the intent that the MSLP funds would generally be recouped for taxpayers. This desire to maximize taxpayer recovery appears to have been the driving force behind many of the MSLP restrictions set forth below.
- Borrower Restrictions on Dividends, Compensation, etc. The MSLP's restrictions on paying dividends, repurchasing equity and paying compensation over specified thresholds were significant concerns for many borrowers.
- Refinancing Limitation. The Program prohibited lenders from using loans they originated to refinance their own debt. The funds could only be used to refinance debt of other lenders.
- Collateral Dilution. The MSLP "priority facility" loans required a parity basis intercreditor arrangement with any existing secured debt, thus diluting the existing lender's collateral position. For borrowers with existing debt held by the participating lender, such collateral dilution provided a strong disincentive to originate such a loan. For borrowers with existing debt held by third parties, the borrower's inability to compel third parties to accept such collateral dilution made the requirement impractical.
- Collateral Coverage Ratio. The "priority facility" loans included complex collateral coverage ratio rules. When applicable, the requirements seemed excessive.
- Cash Collateral Limitations. The Program restricted lenders' ability to use cash collateral deposits, compensating balances, cash reserve accounts or cash escrow accounts.

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<sup>3</sup> See the Federal Reserve Statistical Release at <https://www.federalreserve.gov/releases/h41/20201231/>.

- Underwriting. The MSLP had vague and sometimes contradictory requirements that, on the one hand, the lender should generally use customary underwriting and, on the other hand, the lender could disregard customary underwriting to the extent that the borrower's weaknesses stemmed from the pandemic and were expected to be temporary. Whether the weakness was temporary and the borrower would survive the pandemic and recover was inherently uncertain, which made underwriting decisions more difficult.
- Lender's 5% Retention. The Program's requirement that the lender retain a 5% loan participation was a disincentive to originating MSLP loans to high risk borrowers.
- Legal Costs. The complexity of the Program increased the legal costs of MSLP loan transactions, and in many cases the additional expense made small loans impractical.

## LOOKING AHEAD

### **Renewal of the Program Seems Unlikely**

As noted in our [Prior Client Alert](#), U.S. Treasury Secretary Steven T. Mnuchin advised the Federal Reserve that the MSLP should not be extended past its scheduled expiration date and requested that the unused funds be returned to the Treasury. And the Federal Reserve appears to concur, only having extended the expiration date to January 8, 2021.

Given the foregoing, and in light of the limited utilization of the Program, it seems unlikely that the MSLP will be further extended or renewed following its expiration. However, it is possible that other credit programs will be enacted in 2021 to support struggling small and medium-sized businesses. If any such new credit program is announced, we intend to once again rapidly develop industry leading capability and make ourselves available as a key resource for our lending and borrower clients.

### **Ongoing Obligations Under Participation Agreement and Servicing Agreement.**

Once the Program's special purpose vehicle ("*SPV*") purchases its 95% participation from the lender, the Participation Agreement and the Servicing Agreement set forth the duties of the originating lender as servicer of the MSLP loan, and allow the originating lender to administer and enforce the MSLP loan. Such duties include customary administrative agent responsibilities over the participation interest and delivery of specified quarterly and annual borrower financial data.

Payments. The lender is required to pay over to the SPV its 95% share of any payments made on the MSLP loan within two (2) business days of receipt.

Notices. If the lender receives any notice, information or document from the borrower, the lender is required to use commercially reasonable efforts to forward the same to the SPV as soon as practicable, but not later than three (3) business days, after receipt.

Authority and Core Rights Acts. Unless and until the SPV decides to "elevate" its participation interest to an actual assignment, the originating lender retains the authority to administer the MSLP loan and exercise voting rights under the loan documents, except where such actions (or inactions)

would constitute a “Core Rights Act”. Core Rights Acts include:

- any extension, increase or reinstatement of any commitment relating to such loans;
- any reduction in the principal, the rate of interest or any fees or other amounts payable with respect to such loans;
- any delay or postponement of any scheduled payment, or any reduction in the amount of or waiver of such payment;
- any change of the pro rata sharing provisions;
- any release of all or substantially all of the collateral or substantially all of the value of the guarantees;
- the waiver of any condition precedent to closing, effectiveness or funding;
- any waiver of or consent to departure from the certifications of the borrower under the CARES Act or the Federal Reserve Act;
- any waiver of or consent to departure from the borrower’s financial reporting requirements;
- any express subordination of the loans or the collateral securing them;
- any amendment that imposes restrictions on the SPV’s ability to assign, participate or pledge its interest in the loans;
- any action that would have a disproportionately adverse effect on the participated loans;
- any amendment that would affect, or any waiver of, the provision that makes the acceleration of any other debt owed by the borrower to the lender or any of its affiliates a default (a “Seller Debt Cross-Acceleration”);
- the acceleration, or failure to accelerate, the loans following a Seller Debt Cross-Acceleration;
- the exercise, or failure to exercise, remedies with respect to shared collateral following a Seller Debt Cross-Acceleration; and
- any change to any lender voting approval level.

Prior to undertaking any act which falls within the above list of Core Rights Acts, the lender must complete and submit an “Eligible Lender Request for Loan Modification or Waiver Form” to notify the SPV and then act in accordance with the SPV’s instructions. If the lender is uncertain as to whether an action constitutes a Core Rights Act, it can complete and submit the form and have the SPV evaluate the request.

If you have any questions as to any of the above, or as to your ongoing obligations under the MSLP, please do not hesitate to contact your Windels Marx relationship lawyer or a member of our [Financial Transactions Practice Group](#).

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