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Main Street Was a Lifesaver—For Some

By Dennis Monroe

There have been so many interesting developments in restaurant lending over the last nine months. The PPP loan program has obviously gotten the most press, but, of real assistance, the Economic Injury Disaster Loans (EIDL) program has now been extended. In addition to the new round of PPP, the new CARES Act makes the traditional SBA 7a and 504 loans more available by increasing the bank's guaranteed portion to 90% and waiving borrower and lender fees. In addition, the SBA will cover for a period of time, certain payments of principal and interest (P&I) on 7(a), 504 and Microloan Programs.

One program that deserves some review is the Main Street Loan program (MSL), that expired at the end of 2020, which we hoped would be extended. The MSL encompassed three different programs. The first was the New Loan Facility, which is based on four times the previous year's EBITDA. This was not utilized to the extent that was anticipated. The second type of loan was the Expanded Loan Facility which wrapped around existing debt. This facility was based on six times 2019 EBITDA, less existing debt; and while this is pretty complicated, it was utilized to a large extent by large operators, particularly multi-unit franchisees. Finally, the third program was the Priority Loans Facility, which again is based on six times 2019 EBITDA.

What was unique about the MSL is that it was administered not by the SBA, but by the Federal Reserve of Boston. In speaking with bankers, I found they were reluctant to get involved in the MSL because: (1) they were worn out from issuing PPP loans; (2) the guidelines by the Federal Reserve of Boston provided that underwriting was to be at a level comparable to the standard, conservative underwriting by the originating bank; and (3) there was a lack of clarity on the rules governing the MSL. Loan proceeds were advanced 95% by the Federal Reserve of Boston, and 5% by the bank, with both parties as co-lenders.

Brad Cashman, a partner with Monroe Moxness Berg, was one of the leading attorneys representing various MSL borrowers, in many cases large multi-unit franchisees. Cashman made it clear the big drawback to the MSL loans was while the cash advances were favorable (because 6x EBITDA is an advance rate much higher than most banks would offer), there was a restriction in that the borrower couldn't make any distributions to shareholders (other than tax distributions) or, in some cases, increase the owner's salaries.

The entire MSL idea was to stabilize the borrower, providing working capital so they could make it through the Covid period. These funds were not meant for growth or expansion.

As to the Expanded Loan Facility, this facility was used for businesses with existing debt. One important point is that existing lenders are not paid off and are required to agree to change the priority of their lien position and share pro rata, the lien on the collateral with the new loan.

Some of the MSL transactions involved refinancing. In a case we know, an owner had two restaurant concepts: One concept was doing well and one was struggling. The owner refinanced the struggling side of the business through the MSL Priority Facility. The existing lenders reduced their exposure substantially. The owner was able to wall off risk and the new lender was comfortable taking on the concept that was not performing quite as well, based on the favorable risk retention and economics of the MSL to lenders.

The lenders that took an active role in originating MSL loans were not usually the traditional, restaurant, foodservice industry lenders we deal with on a regular basis. In fact City National Bank, one of Florida's largest community banks, was the most aggressive

From a bank standpoint, Cashman felt the MSL program turned out to be fairly lucrative in that a bank only had to advance 5% of the loan, while 95% came from the Federal Reserve, with a separate 1% fee going to each. Normally the funds, particularly the Expanded Loan Facility advances, did not have to pay off existing debt. The borrower ended up with cash balances for working capital deposited with the originating bank. The bank, in many cases, had significant deposits which it would hold, and then were administered according to the liquidity requirements provided in the loan. The loan terms were tight since the advance rates were favorable, and there was not much negotiating. The rules that the Federal Reserve of Boston put out had to be adhered to.

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While MSL loans were slow getting going, these loans did help a number of our clients and restaurant owners. And, they turned out to be a valuable tool, particularly for larger operators who had a reasonable level of profitability in 2019. These loans were also important to the casual-dining owners, which have been severely hurt by Covid-related closures.

In our view, MSL turned out to be a lifesaver. With that being said, we are now thankful for the new HR133 and all the provisions that are provided for in that bill. The provisions applicable to the discussion of this article are called SBA Lending Enhancements. As I mentioned, the bill increases the SBA guaranty on normal 7(a) loan to 90%. Also, there is a continued waiver of principal and interest payments on existing loans, particularly the EIDL loans.

We have had many programs to deal with and more to come. So far, the book is still open as to the full extent of the success of these programs, but we do know the banks are trying.

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