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Distressed Financing: Avoiding Pitfalls in Planning and Execution

Agency Resignation and Transfer, Rebalancing of Facilities, and Internal and Regulatory Compliance Considerations

THURSDAY, JUNE 16, 2022

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

Today's faculty features:

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June 16, 2022

Distressed Financing: Avoiding Pitfalls in Planning and Execution

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Agenda

1 Why Distressed Credits are Particularly Subject to Pitfalls

2 Agency Resignations

3 Loan Mechanics Issues

4 Regulatory Considerations

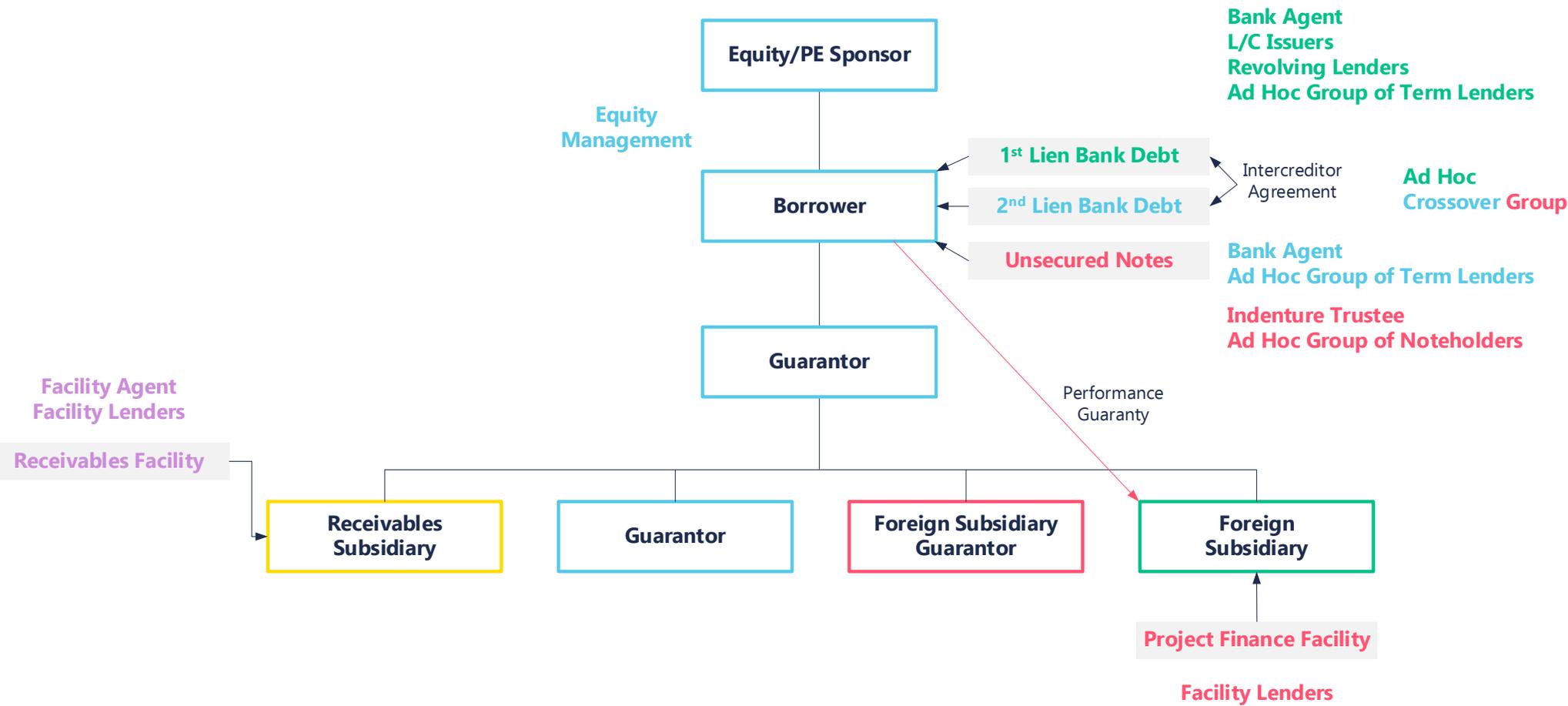
5 Structuring Deals

6 Strategies for Addressing Pitfalls

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Why Distressed Credits are Particularly Subject to Pitfalls

Complexity of the structure and the number of stakeholders involved



Mechanics and deal terms often negotiated without all interested parties present

Why?

- **In the interest of Time**
 - Acute liquidity issues
 - Competition amongst stakeholders to lead restructuring deal terms
- **Strategic Reasons** (i.e., In-the-Dark Transactions)
- **NDA language**

“Recipient further agrees, on behalf of itself and its Representatives, that Recipient shall only be permitted to discuss Information with...”

Stakeholders that may not be involved with early (or any) negotiations

- **Administrative Agent**

- Meaningful time is needed for Agent and its operations team to review documentation agreed to by other parties to process out of the ordinary transactions
- Delay in beginning certain internal approval processes
- Delay in looping in other applicable departments (ex. letter of credit team)
- Complexity may require bespoke processes

- **Counsel**

- Term sheet might not reflect most efficient, cost-effective way of achieving the desired outcome
- Term sheet may present impossible to implement terms or time-intensive solutions

- **Minority lenders**



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Agency Resignations

Why Are Agency Resignations Common in Distressed Transactions

- **Actual or Perceived Conflicts of Interest**

- Single institution acts as agent under more than one credit agreement (i.e. 1L/2L)
- Parties can have different rights/goals in same Collateral

- **Trading Out**

- Agent more likely to sell out of its position

- **Lenders may prefer an “Agent for Hire”**

- No economic interest
- Acts on instructions from requisite lenders
- Lower agency fees

- **Financial and Reputational Liability**

- Lenders more willing to be aggressive to improve returns
 - Liability management transactions
 - Challenges from excluded minority lenders

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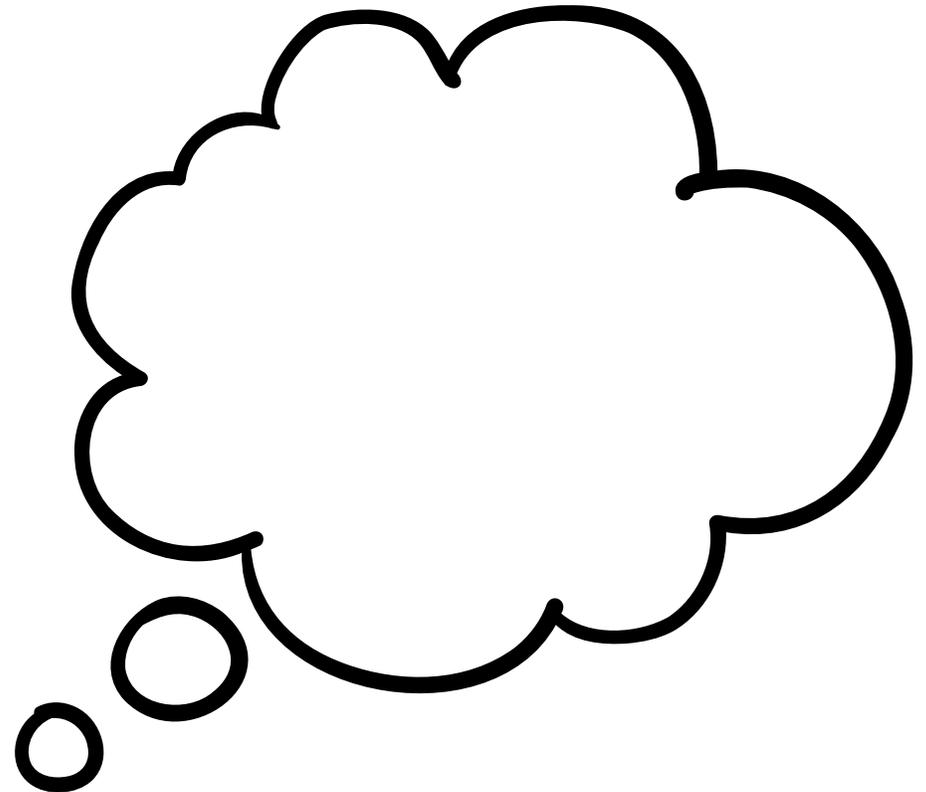
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Replacement Agent logistics

- Will the company or lenders lead the successor agent selection process?
- On what time frame?
- What will the consent process look like?
- Treatment of pending trades?
- Are there any foreign obligors that require signing formalities or registration?
- Is there any collateral outside the US that needs to be released and retaken?



Replacement Agent Requirements

- **Deliverables:**

- Form of register
- Tax forms and administrative questionnaires
 - Will new ones need to be obtained?
- Who will deliver the set of existing loan documents?

- **Collateral Perfection:** in name of new agent can take extended period of time to effectuate

- **Credit Documentation:**

- Amendments to reflect Agent no longer exercising discretion
- Amendments to other agency and indemnification provisions
- Interest calculation considerations

- **Maintenance of platform**

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Loan Mechanics Issues

Rebalancing Facilities

- Additional facilities and vehicles may be created to effectuate a negotiated out-of-court restructuring.
- Considerations for documenting new facilities, particularly with respect to revolving facilities:
 - Review of existing amend and extend provisions.
 - Do the existing documents permit the below between the existing and new facility?
 - Non-pro rata prepayments
 - Non-pro rata borrowings; or
 - Non-pro rata commitment reductions
- Documentation considerations:
 - How will letter of credit exposure be allocated?
 - When will fees and interest on exchanged obligations be paid?



Rebalancing Facilities – Sample Language

Amend and Extend:

Notwithstanding anything to the contrary herein, at any time and from time to time, upon notice to the Administrative Agent (who shall promptly notify the applicable Lenders) specifying in reasonable detail the proposed terms thereof, the Borrower may make one or more loan modification offers to all the Lenders of any Facility that would, if and to the extent accepted by any such Lender, (a) extend the scheduled Maturity Date and any amortization of the Loans and Commitments under such Facility and/or change the Applicable Rate and/or fees payable with respect to the Loans and Commitments under such Facility (in each case solely with respect to the Loans and Commitments of accepting Lenders in respect of which an acceptable is delivered) and (b) treat the Loans and Commitments so modified as a new “Facility” for all purposes under this Agreement; provided that (i) such loan modification offer is made to each Lender under the applicable Facility on the same terms and subject to the same procedures as are applicable to all other Lenders under such Facility (which procedures in any case shall be reasonably satisfactory to Administrative Agent) and (ii) no loan modification shall affect the rights or duties of, or any fees or other amounts payable to, the Administrative Agent, the Swing Line Lender or any L/C Issuer, without its prior written consent.

...and this Agreement and the other Loan Documents shall be amended in a writing (which may be executed and delivered by the Borrower and the Administrative Agent and shall be effective only with respect to the applicable Loans and Commitments of Lenders that shall have accepted the relevant loan modification offer (and only with respect to Loans and Commitments as to which any such Lender has accepted the loan modification offer)) to the extent necessary or appropriate, in the judgment of the Administrative Agent, to reflect the existence of, and to give effect to the terms and conditions of, the applicable loan modification (including the addition of such modified Loans and/or Commitments as a “Facility” hereunder).

Pro-rata borrowing:

To the extent that Revolving Credit Commitments under each of the Extended Revolving Credit Facility and the Non-Extended Revolving Credit Facility are in effect, each Revolving Credit Borrowing under the Dollar Tranche (including any deemed Revolving Credit Borrowings made pursuant to Sections 2.03 and 2.04) shall be allocated pro rata among the Facilities which at such time constitute the Dollar Tranche.

Pro-rata prepayment:

Each prepayment of outstanding Revolving Credit Loans pursuant to this Section 2.05(a) shall be applied to such Revolving Credit Facilities on a pro rata basis.

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Regulatory Considerations

- a. Know-your customer (KYC)
- b. Anti-money laundering (AML)
- c. Environmental, Social and Governance (ESG)
- d. Flood Diligence

Know-Your Customer (KYC)

- New bank account requires depository bank to run KYC check
- Non-existing lender providing rescue financing will need KYC checks
- Unanticipated issues in KYC:
 - Expired identification of director
 - Timing of creation of a new borrowing entity
 - Time to run internal approvals



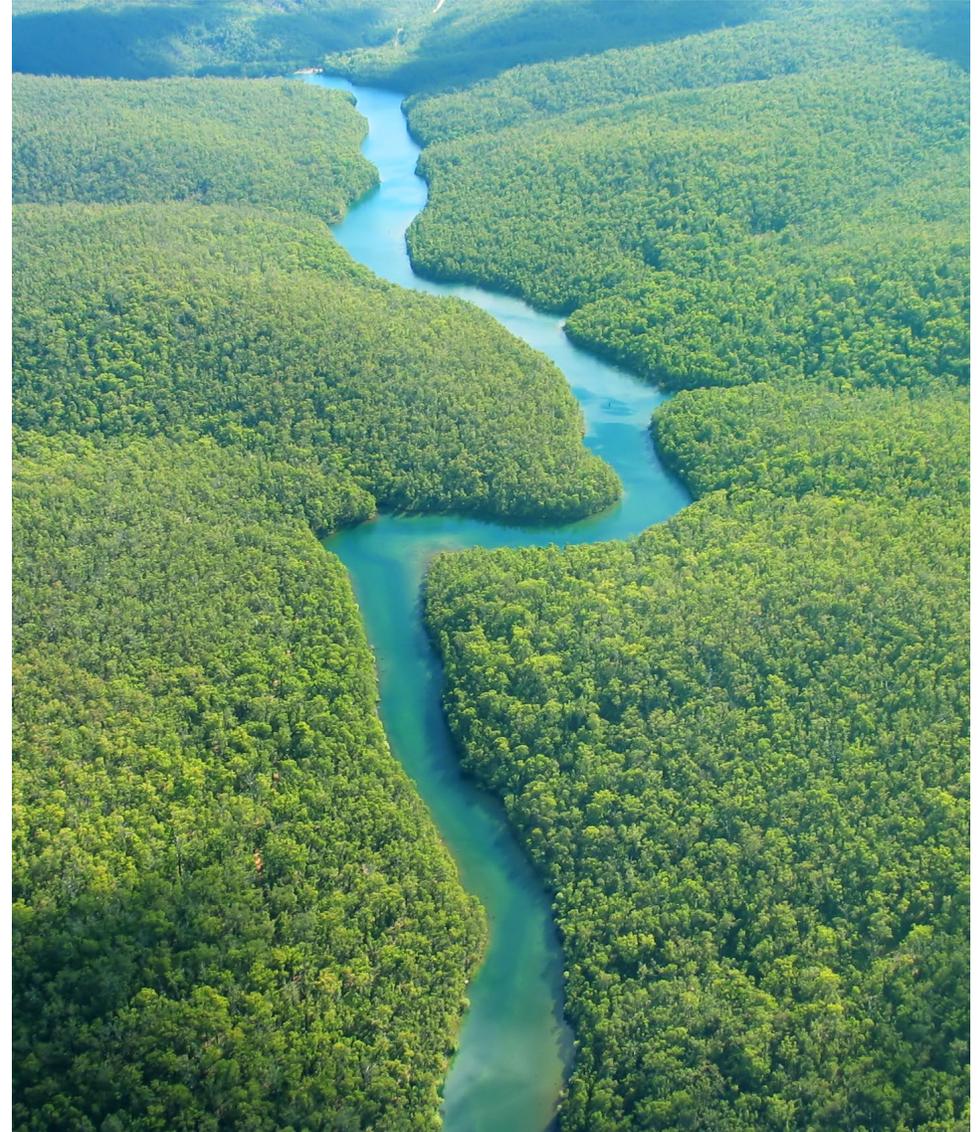
Transaction Structure Could Trip Anti-Money Laundering Laws (AML)

- **Cashless transactions**
 - For example, OID not processed through an arranger at origination
- May require **manual review** to override existing systems



Environmental, Social and Governance (ESG)

- Credits for industries with clear ESG implications
- Certain restructuring terms will trigger ESG issues.
 - Maturity extensions
 - New money
- May require approval from top management



Flood Diligence



- Credits secured by real property
 - National Flood Insurance Reform Act of 1994
- Flood diligence can take weeks depending on internal policies
 - Detailed and organized information required
 - Certain property not subject to standard address convention

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Structuring Deals

- a. Letters of Credit
 - Treatment in a refinancing
 - Treatment in a bankruptcy
- b. Halting Trades

Letter of Credit Basics

THE BANK
DATE: X XX, XXX
IRREVOCABLE STANDBY LETTER OF CREDIT NUMBER: XXXXXXXXX
APPLICANT REFERENCE NUMBER: XXXX

PAGE: 1

APPLICANT	BENEFICIARY
BORROWER	THIRD PARTY VENDOR
100 First Street	200 Second Street
New York, NY 10022	New York, NY 10022

ISSUING BANK
THE BANK
ONE BANK WAY
New York, NY 10022

AMOUNT
USD 1,000,000.00
ONE MILLION US DOLLARS|

- **Applicant:** Borrower or any subsidiary are typically permitted as applicant under the Credit Agreement
- **Beneficiary:** Entity benefiting from letter of credit
- **Issuing Bank:** If under a syndicated credit facility, the letter of credit issuer under the Credit Agreement (or an affiliate permitted to issue the letter of credit under the Credit Agreement)
- **Evergreen Expiration Date:** Letter of credit that extends automatically at the end of its indicated term, unless the issuing bank issues a notice of non-extension. Typically, a Credit Agreement will require an annual right to issue a notice of non-extension

Questions to Consider Regarding A Company's Letter of Credit Needs

- Are there ongoing letter of credit needs that will require outstanding letters of credit to “**ride through**” a restructuring process unaffected?
 - Will other creditors **consent** to such treatment?
- Do the letters of credit provide **backstops** for other letters of credit, bank guarantees or bonding obligations?
 - Consider backstopped letters of credit for **foreign subsidiaries**, which are in theory supposed to be unaffected by a restructuring
- Can outstanding letters of credit be returned **undrawn** and **replaced**?



Undrawn Letters of Credit as Contingent Obligations

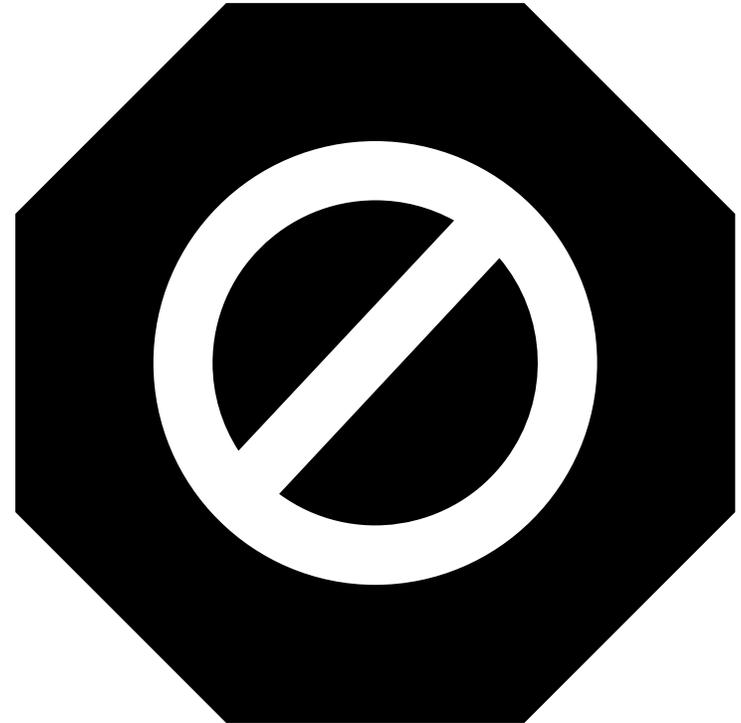
- In a bankruptcy, first lien obligations are often negotiated assuming that all creditors of the same class will receive similar consideration
 - However, a company's reimbursement obligations with respect to undrawn letters of credit are contingent and, therefore, not suited for direct comparison to outstanding principal obligations despite both sets of obligations having equal lien and payment priority.
 - For efficiency and expediency, the company's plan should specifically address treatment for letters of credit within an applicable class
- There are mechanisms in bankruptcy proceedings to reduce claims to a dollar value; however such mechanisms leave openings for objections and litigation (and time delays).

11 U.S.C. Section 502(c): "There shall be estimated for purpose of allowance under this section . . . any contingent or unliquidated claim, the fixing or liquidation of which, as the case may be, would unduly delay the administration of the case"

- May require arbitration, mediation or a full-blown trial

Halting Trades

- Consideration of when trades will be halted and on what timeline
- Unable to determine certain beneficial lenders and their holdings
- Failure to arrange trading halts can have implications for entitlement to participate in DIP lending



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Strategies for Addressing Pitfalls

Helpful Tips

- a. Address Issues early**
- b. Develop a working plan**
 - Include all stakeholders
- c. Communicate with lenders and noteholders**
 - Provide detailed notices to lenders and noteholders
- d. Be mindful of dual capacities**
 - Communication with Agent in minority group
 - Lead time for agency team to execute operationally



Contacts



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Ms. Braunstein is counsel in our Restructuring and Insolvency team. She counsels clients on various financial restructuring matters. Ms. Braunstein's experience includes both in-court and out-of-court representation of agents, banks, funds, borrowers and potential purchasers of distressed debt and assets. Much of her experience entails multi-jurisdictional complexities.



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Thank you