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Syndicated Finance Transactions: Documentation and Trading, Key Provisions, LSTA Forms

WEDNESDAY, NOVEMBER 10, 2021

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

Today's faculty features:

Bridget K. Marsh, Executive Vice President - Deputy General Counsel, **Loan Syndications & Trading Association**, New York

Arleen A. Nand, Shareholder, **Greenberg Traurig, LLP**, Minneapolis

Tess Virmani, Executive Vice President & Associate General Counsel, **Loan Syndications & Trading Association**, New York

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SPEAKERS

Bridget Marsh, Executive Vice President & Deputy General Counsel, LSTA

Arleen Nand, Shareholder, Greenberg Traurig, LLP

Tess Virmani, Associate General Counsel & Senior Vice President, Public Policy, LSTA

Wednesday, November 10, 2021

Session Overview

- **Overview of the LSTA**
- **Transition from LIBOR**
- **Evolution of the US Loan Market**
- **Loan Syndications**
  - Role of the arranger
  - Role of the administrative agent
  - Unique aspects to consider when working with a syndicate
- **2021 LSTA Model Credit Agreement (Investment Grade)**
  - Erroneous Payment Provision
- **2018 Model Credit Agreement Provisions (MCAPs)**
- **Comparison between LSTA and LMA Primary Market Forms**
- **Secondary Loan Market**
  - LSTA Trading Documents

OVERVIEW OF THE LSTA

LSTA Promotes Transparency, Standardisation, and Operational Uniformity

- Primary responsibilities of LSTA Legal Team:
  - Develop legal product for our members
  - Expand and update suite of LSTA documents
    - Lead Primary Market Committee
    - Lead Trade Practices and Forms Committee
  - Respond to member legal and market practice questions
  - Resolve secondary market trading disputes
  - Education

- Some of the LSTA advocacy efforts include engagement with regulators on key issues for the loan market, including submitting comment letters and white papers, and filing amicus briefs.

LSTA Standardises Both Primary and Secondary Documentation and Practices

- **Primary Market**. LSTA has published a Form of Revolving Credit Facility, Model Credit Agreement Provisions (MCAPs), guidelines, and standard agreements for use in the origination and distribution of new deals.

- **Secondary Market**. LSTA offers a comprehensive suite of documents for use in the trading and settlement of all performing and distressed corporate loans.

- **Trade Claims Market**. LSTA has published a form master confidentiality agreement and a sample trade confirm for use in the claims trading market.

LSTA Membership Includes the Sell-Side, Buy-Side, Law Firms, and Vendors

LSTA Memorialises "Market Standard Terms" Used by Loan Market Participants

- LSTA Working Groups and LSTA Committees help to produce new LSTA product.
- Most projects percolate up from our members; occasionally, the LSTA Board may make a decision to tackle an important issue.
- The production of a new document generally takes about one year with numerous turns until the document is released as an Exposure Draft and then published in final form.

GOODBYE, LIBOR

LIBOR Transition: Things to Know

- LIBOR *Origination* ends and *Transition* begins to replacement rates for most non-USD currencies at the end of this year (and, well, now!)

- USD LIBOR *Origination* ends by December 30, 2021, while USD LIBOR *Transition* for most legacy contracts is not required until June 30, 2023

- Several replacement rates are in play in the US syndicated loan market; the US institutional loan market is likely to go to Forward Looking Term SOFR, while CSRs (along with SOFR) are in play in the leveraged pro rata and possibly IG market

- SOFR is different from LIBOR and lenders need to be operationally and economically ready

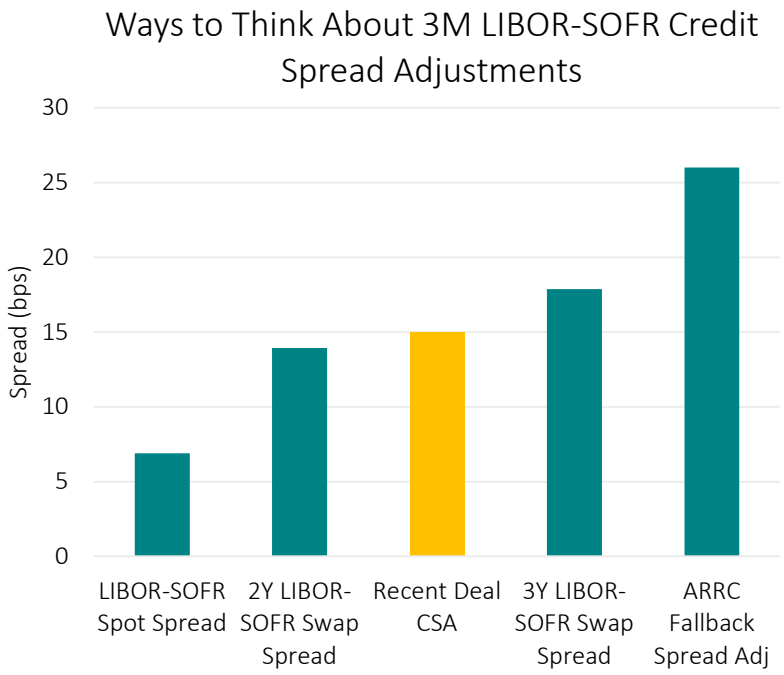
- ***But, we are actually in a much better place than a year ago! Term SOFR is quite useable!***

Likely Replacements for LIBOR: SOFR vs CSRs

- There has been a lively debate on likely replacement rates for LIBOR
- Credit Sensitive Rates – like BSBY, Ameribor or AXI – may gain traction in the more traditional bank loan market
- For the institutional loan market, the most likely replacement is “SOFR” – the Secured Overnight Financing Rate
- SOFR is different than LIBOR
  - It’s a risk free rate and therefore it is generally lower than LIBOR
  - It also has a flatter curve
  - It requires a spread or pricing adjustment
  - It involves changes to systems for the spread adjustment
- Because SOFR is lower than LIBOR – and because interest rates are all unusually low right now – there are some frictions in figuring out how to price new SOFR loans

LIBOR vs SOFR: The "Right?" Spread Adjustment

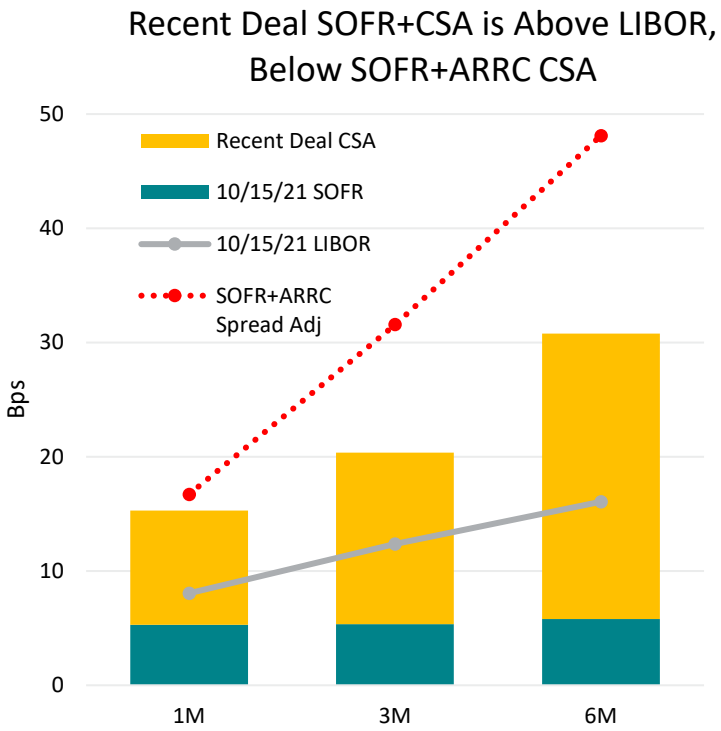
- SOFR is lower and flatter than LIBOR
- Today, SOFR and LIBOR are very similar because interest rates are near zero
- The spot spread adjustment seems low relative to normalized spread differences, while the ARRC fallback spread adjustment may seem high
- Several banks have discussed using the forward LIBOR-SOFR swap basis as the credit spread adjustment ("CSA") on new deals
- Note that it will be less operationally complex if a convention develops as opposed to every bank uses a different spread adjustment (or spread adjustment curve) in every deal



Source: Bloomberg, CME Group, WSJ, ARRC

LIBOR vs SOFR: Splitting the Difference?

- Several recent leveraged loans have offered a "CSA Curve"
  - 10 bps for 1M SOFR
  - 15 bps for 3M SOFR
  - 25 bps for 6M SOFR
- These CSAs appear to "split the difference" between the LIBOR-SOFR spot spread and the ARRC recommended spread adjustment **for fallbacks** (e.g., 11.5 bps for 1M; 26 bps for 3M)
- The resulting rate is higher than LIBOR, but lower than SOFR+ARRC fallback spread adjustments



Source: CME Group, WSJ, LFI

Fallbacks: Old & New

- Legacy Loans
  - What forms of fallbacks did we see – and how frequently?
    - Covenant Review recorded 90% of new issue institutional loans included hardwired fallback language (up from 60% in January – April)
      - 55% of new issue or amended loans in the CS Leveraged Loan Index (Oct. 2020 – August 2021) included hardwired fallback language
    - Practical Law surveyed 181 publicly-filed credit agreements between April 1 and August 30, 2021: 90% incorporated hardwired fallback language and 9% incorporated amendment approach language
  - Will we see a number of direct refinancings into replacement rates to avoid falling back?

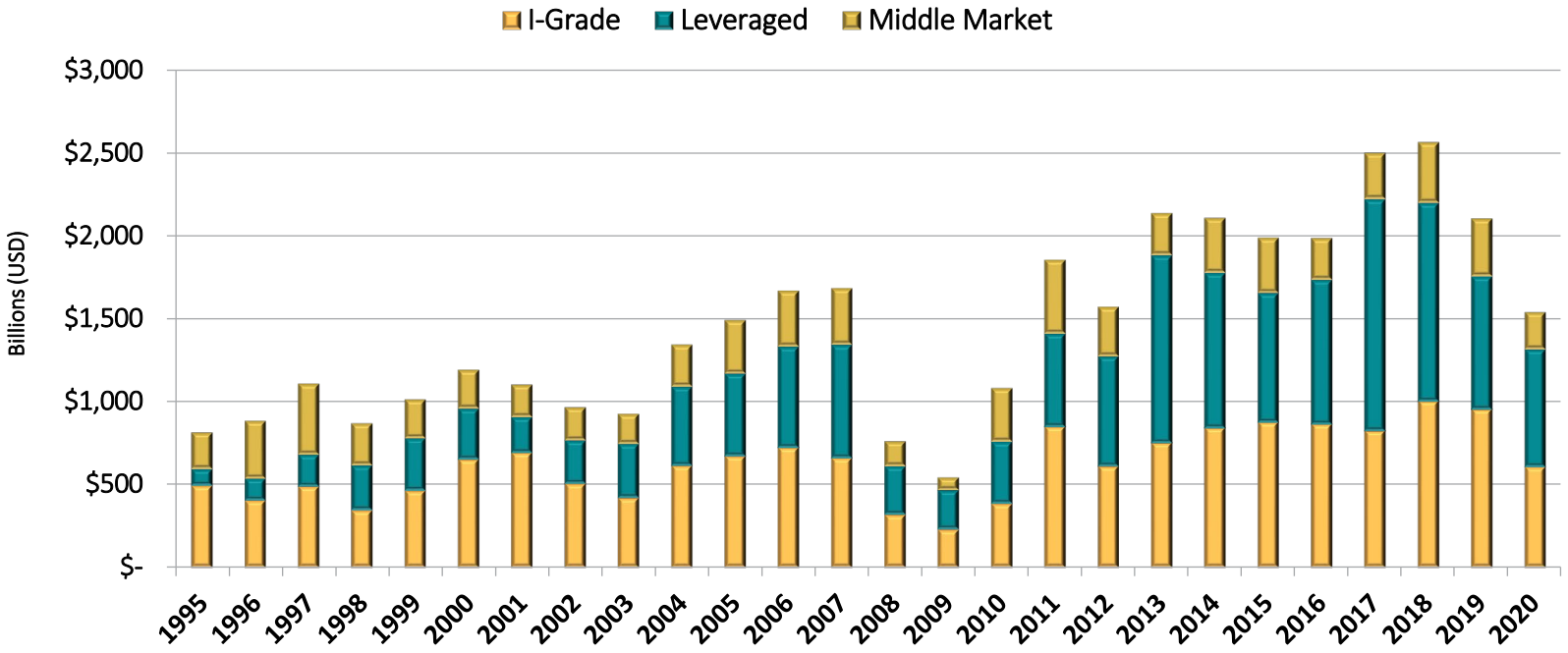
- New Loans
  - What sort of fallback language is emerging in new SOFR loans?

EVOLUTION OF THE U.S. LOAN MARKET

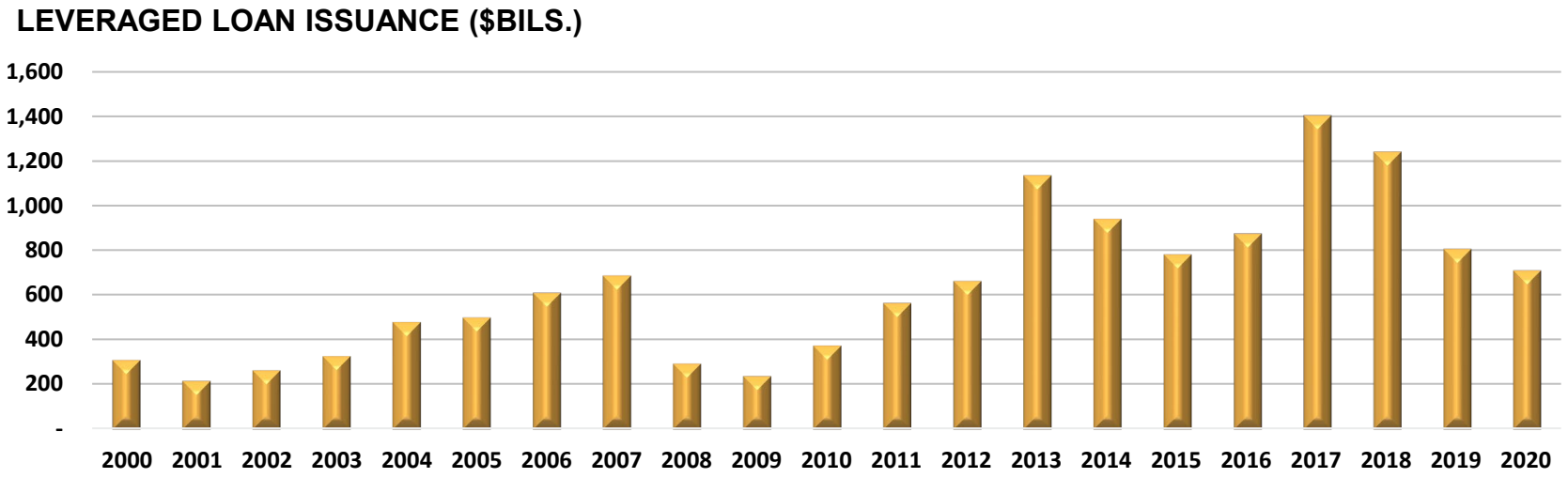
Art of Corporate Loan Syndications, Trading and Investing Has Changed Dramatically in 30 Years

- In the past, banks made loans to their corporate borrowers and kept those loans on their books.
- Over time, investors were drawn to loans because of their attractive features. Unlike bonds, loans are senior secured debt obligations.
- Today, loans are held by banks, but they are also sold to other banks, mutual funds, insurance companies, pension funds, hedge funds, etc.
- Consequently, the US loan market has experienced remarkable growth.

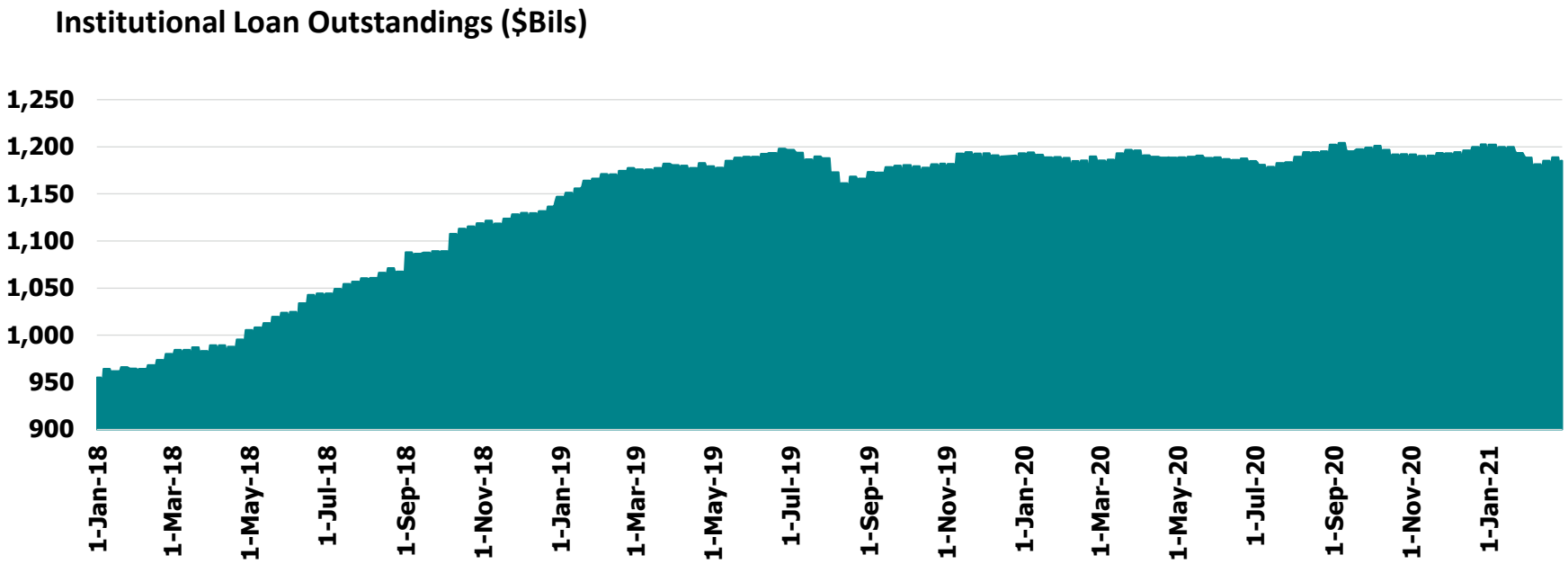
US Corporate Lending Decreased During the Pandemic



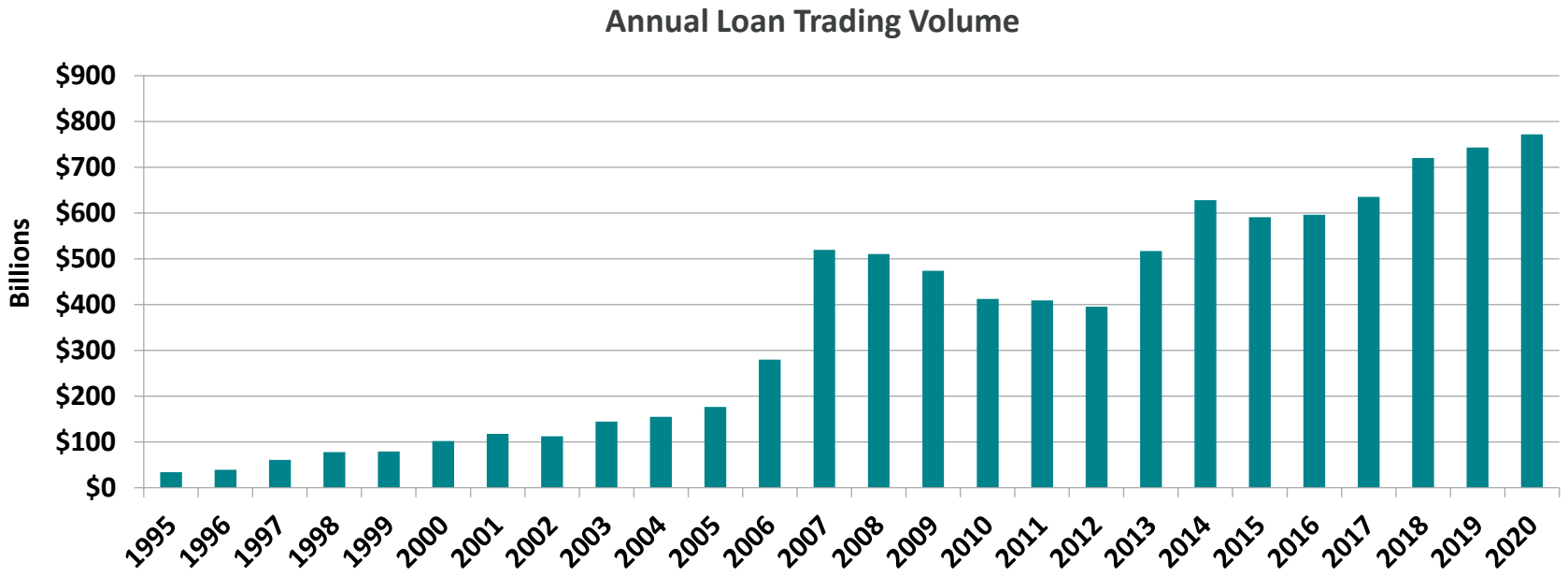
2020 U.S. LEVERAGED LOAN ISSUANCE DECLINED…AGAIN!



INSTITUTIONAL LOANS OUTSTANDING HAVE HOVERED ABOUT $1.2T



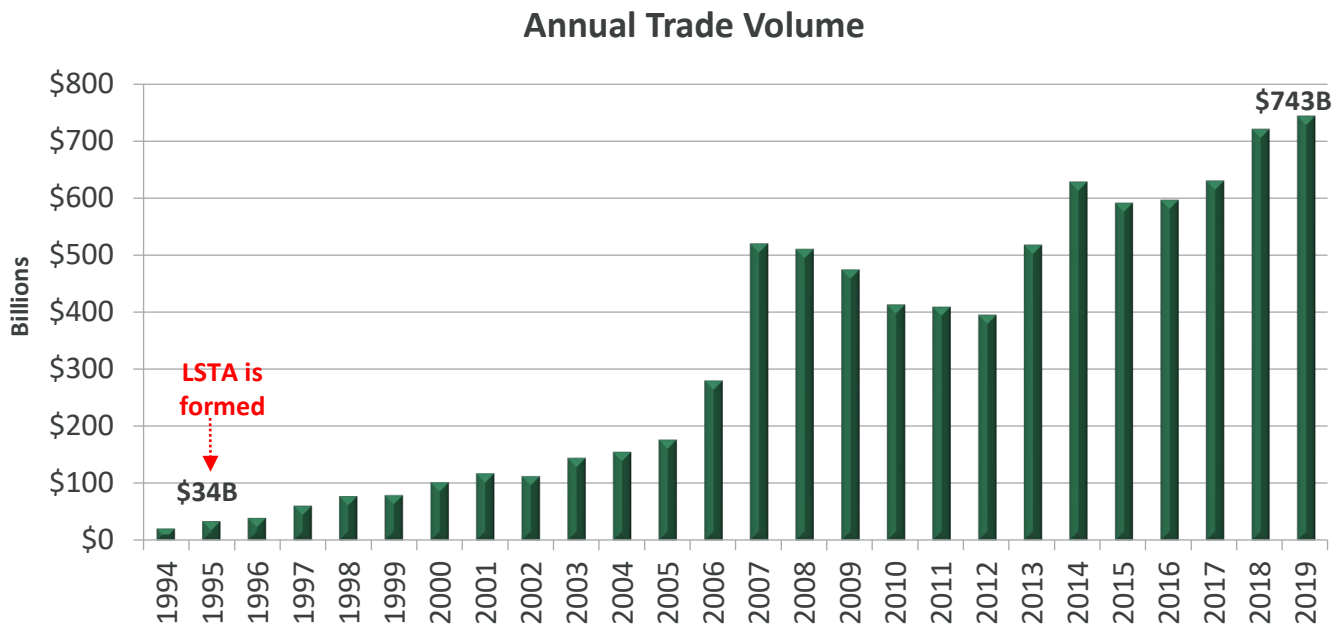
US Secondary Loan Market Has Performed Well in The Past 15 Years – and Last Year Was No Exception!



Term Loan Bs Have Evolved to Suit the Demands of the Institutional Lender Class

- Term Loan As are syndicated in the US to traditional banking institutions that typically require amortization and tighter covenants.
- Arrangers of syndicated loans modified traditional deal structures and, in particular, the features of Term Loan Bs which would be acquired by the non-bank lenders.
  - Size of tranche was increased and the maturity date was extended.
  - Amortization schedule – small / nominal installments made until the final year when a large bullet payment is typically scheduled to be made by the borrower.
- Term Loan Bs can have less or no financial maintenance covenants and permit greater overall covenant flexibility as compared to Term Loan As.
- In return, the lenders were paid a higher interest rate and afforded other economic protections (such as “no-call” periods) not commonly seen in Term Loan As to compensate for less rigorous terms.
- This all contributed to a more aggressive risk-return profile which, in turn, attracted still more liquidity to the loan market.

U.S. Secondary Loan Market Has Grown Significantly



Source: LSTA Trade Data Study

LOAN SYNDICATIONS

Three Segments of Syndicated Loan Market

- In 2020, total corporate lending in the United States was **$1.5 trillion** (representing a $600 billion decrease from 2019), comprised of three subsectors of the syndicated loan market – the **investment grade market**, the **leveraged loan market**, and the **middle market**.
- In the **investment grade market**, total lending exceeded **$605 billion** in 2020 (a decrease from $950 billion in 2019). Most lending in the investment grade market consists of revolving credit facilities to larger companies.
- In the **leveraged loan market**, loans are made to companies with non-investment grade ratings (or with high levels of outstanding debt). These financings represented approximately **$711 billion** of the market in 2020 (a decrease from $807 billion in 2019). These borrowers are usually companies seeking to refinance existing debt, to finance acquisitions or leveraged buy-outs, or to fund projects and other corporate endeavors such as dividend recapitalizations. (Leveraged is typically defined by a bank loan rating by Standard & Poor's of BB+ and below (by Moody's Investor Service, Ba1 and below) or, for non-rated companies, typically with an interest spread of LIBOR + 125 basis points.)
- In the **middle market**, lending consists of loans of up to $500 million that are made to companies with annual revenues of under $500 million. For these borrowers, the loan market is a primary source of funding. In 2020, middle market lending totaled approximately **$225 billion** (a decrease from $343 billion in 2019).

Source of Market Statistics: Thompson Reuters Loan Pricing Corporation / LSTA

Lead Arranger Interfaces With the Borrower, Drives the Deal, and Manages the Syndication Process

- "**Lead arranger**" is the firm that leads the structuring and syndication of a loan, i.e., the lead arranger drives the deal; sets the terms; interfaces with the client and investors; prepares, negotiates, and closes documents; and manages the syndication process.

- The borrower pays the arranger a fee to find investor dollars for it, and this fee increases with the complexity and riskiness of the loan.

A Syndicate Loan Requires an Agent to Administer the Loan Until it Matures

- The administrative agent administers the loan; it is the **agent of the lenders and not the agent of the borrower**. In practice, however, the agent often has the business relationship with the borrower. (The agent's role should not be confused with the arranger's role, although it will typically be the same institution.)

- The agent's role is to interface between the borrower and the lenders and amongst the lenders themselves. The agent executes the "back office functions":
  - Receives financial reports from the borrower and makes them available to the lenders
  - Receives and disburses funds (*e.g.*, payment of principal, interest, and fees) between the borrower and the lenders
  - Takes and delivers notices

Syndicated Loans Raise Unique Interlender Issues Which Must Be Addressed in a Credit Agreement

- When drafting a credit agreement for a syndicated loan, in addition to the deal terms and other key boilerplate provisions such as the pro rata sharing provision, parties should focus on the following provisions which are included in the LSTA's Model Credit Agreement Provisions (MCAPs):
  - Agency
  - Voting
  - Assignment
  - Disqualified Institution Lists
  - Defaulting Lenders

LSTA's Agency Language Makes Clear that the Agent's Duties are Merely Administrative in Nature

- In today's market, the agent may be faced with active institutional lenders who have more varied and perhaps conflicting lender group politics.

- Agent's appointment by the lenders is stated to be irrevocable so that, absent bankruptcy, other lenders cannot challenge the agent's authority by trying to revoke its appointment.

- Agent is not a fiduciary; its responsibilities are ministerial only; and agent is not liable for any action by it (other than for its gross negligence or willful misconduct) and nor is it responsible for monitoring the loans on behalf of the lenders.

Agent May Resign But this is Contingent on Appointment of a Successor Agent

- Agent's right to resign is typically contingent upon a successor agent's having been pointed by required lenders and having accepted the role as agent.

- Certain requirements must be met. LSTA language requires that the successor be a bank in a named city; this is driven largely by operational considerations.

- If a borrower files for bankruptcy and goes into workout mode, the agent may want to resign but find it tricky to find a willing successor. LSTA form language requires the borrower to pay to a successor agent whatever fees were payable to the resigning agent. Although borrowers may want approval rights over the incoming agent, the **LSTA language only requires consultation by the lenders with the borrower in appointing a new agent**.

- An agent may be removed but this is typically limited to when the agent has become a defaulting lender.

LSTA 2021 MODEL CREDIT AGREEMENT (INVESTMENT GRADE)

LSTA First Published the Credit Agreement Provisions Nearly 20 Years Ago

- The LSTA initially published provisions which could impact a loan's liquidity and then tackled boilerplate language:
  - Assignment Agreement (2000)
  - Model Transfer Provisions (2002)
  - Model Credit Agreement Provisions (2004 and 2005) addressed typical boilerplate provisions, including:
    - Yield Protection
    - Rights of Setoff
    - Tax
    - Sharing of Payments by Lenders
    - Indemnity

Documentary Evolution of LSTA Credit Agreement Forms

- More expansive **MCAPs** were published on August 8, 2014, which included select provisions of a New York law governed credit agreement (*e.g.*, tax, yield protection, agency, assignment, defaulting lender, and disqualified institution provisions, etc.) that were suitable primarily for leveraged finance transactions. Updated MCAPS were published on October 16, 2018.

- **Form of Credit Agreement – Revolving Credit Facility** was published on October 19, 2017, for investment grade borrowers, and updated on November 2, 2021.

- **Form of Incremental Facility Amendment to Credit Agreement** was published on August 2, 2018, which contemplated the creation of a new tranche of loans or an increase in an existing tranche.

- **Form of Credit Agreement - Investment Grade Term Loan and Revolver** was published on January 20, 2021.

- **SOFR Concept Credit Agreement – Daily Simple SOFR / Daily Compounded SOFR** was published on May 6, 2021, with concept documents reflecting Term SOFR published on August 25, 2021.

2021 LSTA Model Credit Agreement - Background

- 2021 Form of Revolving Credit Agreement serves as a model for investment grade borrowers (the **"Model Credit Agreement"**).
- It documents an unsecured, single currency revolving credit facility that is committed.
- The form incorporates sublimits for swinglines, letters of credit and competitive loans.
- While large banks and sponsors have, for the most part, developed their own forms of credit agreements, the Model Credit Agreement serves as a reference source for the loan market. Also, European lawyers have found it helpful because they have had Loan Market Association (**"LMA"**) templates available, and this form serves a reference point for cross-border deals.
- *Section number references in following slides reference Word version of Model Credit Agreement*.

2021 LSTA Model Credit Agreement – Revolving Loans

Section 2.01 - **Revolving Commitment**

- In a revolver, the Borrower is allowed to **borrow, repay, and reborrow** Revolving Loans during the availability period, provided that the outstanding amount does not exceed the aggregate Revolving Credit Exposure and all applicable conditions precedent are satisfied. The aggregate outstanding amount of the Revolving Loans can fluctuate during the commitment period.

- **Several Liability of Each Lender**. Provision notes that, "-each Lender ***severally*** agrees to make Revolving Loans to the Borrower…" (emphasis added).
  - Each Lender undertakes a separate commitment to the Borrower; its commitment may be part of a tranche with other Lenders, but each Lender is individually obligated (*i.e.*, ***severally obligated***) to make loans to the Borrower.
  - No Lender is excused from making its loan if the conditions precedent are satisfied, even if there is a Defaulting Lender. No Lender is obligated to cover a Defaulting Lender's commitment.

2021 LSTA Model Credit Agreement – Revolving Loans

Sections 2.02 and 2.03 - **Borrowing Mechanics**

- **Advance Notice**. The Borrower must give advance notice of any Borrowing to the Administrative Agent, which will then notify the Lenders.
  - Needs to be in writing or request can be made telephonically, with written confirmation afterwards.
  - Signed by a Responsible Officer (*i.e.*, senior officer as specified in definition) or other officer or employee designated by such senior officer solely for purposes of borrowing requests, etc…
  - Notices for LIBO Rate Loans are required to be delivered at least three Business Days prior to the date that the Loan is made. (LIBOR Loans require a longer notice period because they are fixed two London banking days prior to the day the loan is made.)
  - Notices for ABR Loans require one Business Day's notice.
  - If Borrower fails to specify the Type of Loan, it shall be deemed an ABR Loan. If Borrower fails to specify interest period for a LIBOR Loan, it shall be deemed to select a one-month Interest Period.

2021 LSTA Model Credit Agreement – Swingline Loans

Sections 2.04 - **Swingline Features**

- Swingline Loans made by one of the revolving lenders, usually the Administrative Agent, designated as the "swingline lender." The sublimit is within the Revolving Facility.
- Model Credit Agreement provides alternatives for **committed** or **discretionary swingline facility.**
- Provides same-day funding; Swingline Loans can be made on such short notice because they are being advanced by only one lender.
- Gives the Borrower access to loans at lower minimum amounts.
- The Swingline Lender is obligated to make Swingline Loans only within the limit of its revolving credit commitment and will never be required to make revolving credit loans and Swingline Loans in excess of that commitment.
- Swingline loans required to be repaid in a very short time. Model Credit Agreement **suggests five Business Days** in brackets (see Section 2.11(b)). It's a short-term funding mechanism until a revolving credit borrowing from the full syndicate can be made.
- If the Borrower does not repay the Swingline Loans when due (including by reason of an intervening Default / Event of Default), other revolving credit lenders will be unconditionally obligated to purchase participations in the Swingline Loans so that the risk of the Swingline Loans is shared ratably among all revolving credit lenders and not borne disproportionately by the Swingline Lender.

2021 LSTA Model Credit Agreement – Letters of Credit

Sections 2.05 - **Letters of Credit - Structure**

- Subfacility of revolver. Maximum amount of Revolving Loans, Swingline Loans, Letters of Credit (and unreimbursed Letter of Credit drawings) [and Competitive Loans] cannot exceed aggregate revolving commitment.
- L/C is signed by only one party (the issuer), but it has three principal parties: **the issuer (bank**), an **account party (borrower)**, and a **beneficiary**.
- The Issuing Bank (as termed in the Model Credit Agreement) agrees to pay the Beneficiary a specified sum upon delivery to the Issuing Bank of documents set forth in the L/C.
- Result is that the Beneficiary has the credit strength of the Issuing Bank substituted for that of its customer/Borrower, the account party, and it is the Issuing Bank that takes the credit risk of the account party. **The undertaking by the Issuing Bank under an L/C is independent of the contract between the account party/Borrower and the beneficiary**. Only requirement is that the documents presented conform to the conditions stipulated in the L/C; the Issuing Bank is not under an obligation to verify the truth of statements in the documents. As long as the documents appear on their face to comply with the terms of the Letter of Credit, the Issuer is obligated to pay.
- The Issuing Bank can resign from acting in such capacity.
- Most banks have a separate letter of credit department that provides standalone L/C applications for the Borrower/applicant to sign. If there is any conflict between the L/C Application and the Credit Agreement, the Credit Agreement controls.

2021 LSTA Model Credit Agreement – Letters of Credit

Sections 2.05 - **Letters of Credit – Expiry Date; Strict vs. Substantial Compliance**

- L/Cs expire (a) the earlier of one year of issuance or, in the case of "evergreen" letters of credit, within one year of its most recent renewal and (b) five Business Days prior to the Revolving Facility Commitment Termination Date.
- Account Parties / Borrower are unconditionally obligated to reimburse the Issuing Bank upon a drawing under the L/C. Model Credit Agreement **requires reimbursement to be made on the day on which a drawing under the L/C is honored** or the **next Business date if the Disbursement Request is made after noon**.
- Exposure is shared by all of the lenders ratably in accordance with their revolving credit commitments. Each lender acquires a participation in the letter of credit exposure upon issuance of the L/C.
- Obligation to pay for the participation will, subject only to demand by the Issuing Bank, be absolute, regardless of whether any of the conditions for the making of loans under the credit agreement have been satisfied. Bankruptcy of Borrower or reduction or termination of commitments will not excuse lenders from their obligation to pay the Issuing Bank.
- **Strict vs. Substantial Compliance**. As against a beneficiary, Issuing Bank can dishonor any drawing that does not "strictly" comply with the provisions of the L/C. As against Borrower, Issuing Bank can pay against documents that "substantially" comply with the terms of the credit.

2021 LSTA Model Credit Agreement – Letters of Credit

Sections 2.05 - **Letters of Credit – Cash Collateral**

- The Borrower must provide Cash Collateral for its obligation to reimburse the Issuing Bank upon an L/C drawing if the Administrative Agent makes a demand after an Event of Default has occurred and is continuing or immediately if a bankruptcy-related Event of Default has occurred or the loans are accelerated.
- The amount of Cash Collateral typically required to be posted ranges between 102% – 105% of the face amount of the L/C. The amount in excess of the face amount is to cover Letter of Credit commissions, interest charges on any reimbursement obligation, and fees associated with any drawing under the Letters of Credit.
- Deposits held in a Cash Collateral account will normally not bear interest or even be invested except in the discretion of the administrative agent.
- Cash Collateral is intended to be a substitute for payment by the Borrower and not an earning investment; cash, once posted with the agent, is not subject to control by the Borrower.

2021 LSTA Model Credit Agreement – Competitive Loans

Section 2.06 **Competitive Loans**. (pages 34-36) Not very common in the loan market, included in the Model Credit Agreement for reference purposes. Usually offered to high credit quality borrowers by Lenders (other than Defaulting Lenders) and tied to the revolving credit facility.

- Purpose is to allow Lenders opportunity to **provide loans to the Borrower at rates lower than those available under Credit Agreement.**
- Lenders are not committed; **Competitive Bid Facility is discretionary**.
- The Borrower initiates process by requesting a Competitive Bid for loans for specified period and usually at specified interest rates or at specified margins over LIBOR.
- Individual Lenders can lend more than the amount of their own revolving credit commitment, so long as the aggregate of all revolving credit loans and all Competitive Loans does not exceed the aggregate of the revolving credit commitments of all the Lenders.
- The Borrower has the option to accept (or reject) the offers made, although if the Borrower wishes to accept any offers, it must do so in ascending order by agreeing to offers for the lowest rates first.
- If there are multiple Competitive Bids at the lowest rate, Competitive Loan shall be made pro rata in accordance with the amount of each such Competitive Bid.
- If the Administrative Agent elects to submit a bit, it must submit it directly to the Borrower at least one quarter of an hour before the time by which the other Lenders must submit a Competitive Bid.
- Once the Borrower accepts a Competitive Bid, that Lender is bound. The Model Credit Agreement has a proviso that doesn't require the Lender which extended Competitive Loan to accept a voluntary prepayment without its consent (Section 2.09(a)).

2021 LSTA Model Credit Agreement – Prepayment; Commitment Termination; Repayment

Section 2.09 **Optional Prepayments**. (page 38) Since Lenders are not required to accept prepayments under common law, credit agreements must explicitly permit them.

- Under the Model Credit Agreement, the Borrower can prepay a loan in whole or in part without prepayment or penalty, but notice must be provided for a certain number of days in advance depending upon the type of loan (*i.e.*, Swingline Loan, ABR Loan, LIBO Loan).
- **Prepayment notices are generally irrevocable**, but the Model Credit Agreement contains bracketed language stating that if a notice of prepayment is given in connection with a conditional notice of termination under the Model Credit Agreement (Section 2.10), then such notice of prepayment may be revoked if the underlying notice of termination is revoked in accordance with the Model Credit Agreement.
- Prepayments are applied ratably to the Loans.

Section 2.10 **Termination or Reduction of Revolving Commitment**. (pages 38 and 39) Borrower can terminate or reduce the revolving commitment upon advance notice, but it cannot reduce the revolving commitment amount to an amount less that the current revolving commitment exposure of the lenders. Reduction is applied ratably among the lenders.

Section 2.11 **Repayment of Loans**. (page 39) Revolving Loans must be repaid on the Revolving Commitment Termination Date. Swingline Loans must be repaid in 5 Business Days, and Competitive Loans must be repaid on the last day of their respective Interest Periods.

2021 LSTA Model Credit Agreement – Interest; Fees

Section 2.12 **Interest**. - Provides for ABR and LIBOR pricing. Incentive-based / grid pricing contained in definition of "Applicable Rate," which is added to the rates specified in Section 2.12. Default Rate in Model Credit Agreement is 2%.

LIBOR replacement is not addressed in Model Credit Agreement or MCAPs and will likely not be until market coalesces around mechanics of pricing based on SOFR (Secured Overnight Financing Rate). However, the LSTA posted on October 1, 2019, a draft of "Compounded SOFR in Arrears Concept Document."

Section 2.13 - **Fees**.

- **Commitment Fee** charged on daily unused portion of revolving credit commitment using incentive-based / grid pricing. In calculating usage, all outstanding Loans, undrawn Letters of Credit, and outstanding reimbursement obligations for payments under L/C are considered utilizations of the revolving credit commitments.
  - **Outstanding Swingline Loans are not deducted** for purposes of calculating commitment fees because Lenders that have not advanced Swingline Loans nevertheless remain committed to extend credit to the Borrower in the amount of those Loans.
  - LSTA notes that some investment grade facilities charge a **"Facility Fee"** that is payable on the amount of the Commitment (whether drawn or undrawn).
  - **L/C Fees** charged to pay to each Lender a Letter of Credit fee that accrues at an agreed per annum rate on its participation in the undrawn amount of each outstanding L/C.
  - **Fronting Fee** is an additional fee charged by the Issuing Bank because as the issuer of the L/C it bears some risk that other Lenders might not fund their participations in the L/C if the Borrower fails to repay the Issuing Bank.
  - **Administrative Agent Fee** is payable to the Administrative Agent for administrating credit and is specified in a fee letter, which is confidential and not available for review by other Lenders in the syndicate.

2021 LSTA Model Credit Agreement – Taxes; Extension of Commitment; Incremental Facility

Section 2.19 **Taxes**. Generally, whatever taxes Lenders have to pay that are directly attributable to the Loans will—with exceptions, including for net income taxes—be passed on to Borrower. Model Credit Agreement includes tax gross-up, FACTA and other provisions widely adopted by the industry. Foreign Account Tax Compliance Act adopted to detect tax evasion by U.S. persons who hide their U.S. income through the use of offshore accounts and foreign entities. FACTA imposes 30% withholding tax on interest and certain other payments made by U.S. borrowers to foreign financial institutions or non-financial foreign entities.

Section 2.26 **Extension of Commitment Termination Date**. Provision designed for credit agreements in which the Commitments are scheduled to expire within one year and in which the parties desire to specify an extension mechanism consistent with the regulatory capital rules issued by the Board of Governors of the Federal Reserve System (12 CFR Part 217) for commitments that are to have a 20 percent conversion factor (*i.e.*, commitments with an original maturity of one year or less).

- Suggested notice is not earlier than 45 days and no later than 35 days prior to the Commitment Termination Date, although for facilities in excess of $1 billion or that have at least 15 lenders, parties may consider replacing the 45- and 30-day notice periods with 60- and 45-day notice periods.
- Conditions Precedent – no Default / Event of Default; representations and warranties are true and correct as date of extension and after giving effect thereto, as though made on and as of such date (or, if any such representation or warranty is expressly stated to have been made as of a specific date, as of such specific date); and the Borrower shall have paid in full all principal, interest and other amounts owing to a non-extending Lender.

Section 2.27 **Increases in Commitments**. Incremental facility is not committed; the Borrower can request increase to commitment. Same conditions as the extension of the Commitment Termination Date in Section 2.25, but also includes joinder for any new lenders and legal opinions and other documents reasonably requested by the Administrative Agent.

2021 LSTA Model Credit Agreement – Representations and Warranties

Representations and Warranties Generally. Affirmations by the Borrower of facts or conclusions.

- Model Credit Agreement provides that reps and warranties are being given by the Borrower and [Material] Subsidiary. A Material Subsidiary is defined as a Subsidiary with total assets in excess of a certain percentage of consolidated total assets of the Borrower and its Subsidiaries, or some other metric.
- Some reps are covered by an opinion of counsel.
- Section 3.01 **Existence; Qualification and Power**. The organization and existence representation affirms that the Borrower: is organized; exists; has certain powers; and that it is qualified to do business where required. Model Credit Agreement suggest that MAE may qualify certain, limited representations in this section.
- Section 3.02 **Due Authorization; No Contravention**. Confirmation that Credit Agreement and other Loan Documents have been authorized by board or other required action. Non-contravention applies to the Borrower's organizational documents, other material contractual obligations, governmental decrees or applicable law. Model Credit Agreement suggest that MAE may qualify certain, limited representations in this section.
- Section 3.03 **Governmental Authorization; Other Consents**. No approvals from required from Governmental Authorities, defined broadly as federal and state government agencies, courts, foreign governments, central banks and municipalities, are necessary to close financing. Confirmation that Credit Agreement and other Loan Documents have been authorized by board or other required action.
- Section 3.04 **Execution and Delivery; Binding Effect**. Enforceability representation has standard formulation, with typical limitation for bankruptcy and other laws affecting creditors' rights.

2021 LSTA Model Credit Agreement – Representations and Warranties

- Section 3.05 **Financial Statements; No Material Adverse Effect**. The financial statements representation has the Borrower affirm that all listed statements have been prepared in accordance with GAAP, and that they "fairly present" the Borrower's financial condition in "all material respects." Additional representation that no Material Adverse Change has occurred since audited financials were delivered.
- Section 3.06 **Litigation**. Litigation representation has standard formulation. Threatened litigation is qualified by the Borrower's knowledge.
- Section 3.08 **Property**. Model Credit Agreement provides brackets for title rep to apply to the Borrower and [Material] Subsidiaries, with limited MAE qualifiers.
- Section 3.10 **Disclosure**. Completeness of disclosures provided to the Administrative Agent and the Lenders. Applies to confidential information provided by the Borrower to the Administrative Agent and the Lenders.
- Section 3.13 **Environmental Matters**. Rep included, although investment grade public companies may object on the basis that information is already provided in SEC filings. However, the Lenders will likely require detailed disclosure schedules that go beyond SEC filing requirements, particularly if the Borrower is engaged in a manufacturing, refining, chemical processing, etc… or other similar business.
- Section 3.15 **Investment Company Act**. Rep included to ensure that the Lenders are not lending to an unregistered investment company. Consequences for being an unregistered investment company include possible unenforceability of credit agreement, and the Borrower may be subject to potential criminal sanctions.
- Section 3.16 **Sanctions; Anti-Corruption**. List of sanctioned countries continues to evolve, for instance Sudan was deleted by the LSTA on January 10, 2018 to reflect termination of U.S. territorial sanctions against Sudan. Regarding FCPA, the Lenders are not required to guarantee that borrowers will not violate antibribery provisions in future. However, there is reputational risk for lending to a borrower with FCPA violations.
- Section 3.17 **Solvency**. Solvency representation included; option to require only as of Closing Date.
- Section 3.18 **Beneficial Ownership**. Representation that information contained in Beneficial Ownership Certification is true and correct.

2021 LSTA Model Credit Agreement – Conditions

- Article IV – **Conditions**. The conditions precedent in a credit agreement specify what documents the Borrower must deliver to the Administrative Agent, what actions it must take, and what other circumstances must exist in order for credit to be available. Customarily, the conditions are broken out into two types: those to be **satisfied at closing** and those to be **satisfied at each extension of credit**. In the Model Credit Agreement, all Lenders must consent to waive a condition. See Section 9.02(b)(v).

- The Model Credit Agreement contains conditions found in most credit agreements: execution of documents, corporate matters, opinions, the material adverse change (or MAC) condition, payment of fees, KYC, financial statements, etc....

- The Model Credit Agreement offers in brackets as a condition an opinion delivered to the Administrative Agent by agent's counsel. Similar to many cross-border deals where agent's counsel renders an opinion.

- As to the documentary conditions, the Model Credit Agreement includes at the end of Section 4.01 a provision that the Administrative Agent may presume that each Lender is satisfied with the conditions unless it receives notice to the contrary. Although this may appear repetitive of the agency exculpations in Section 8.03, many agent institutions insist upon inclusion of additional language to this effect.

2021 LSTA Model Credit Agreement – Affirmative Covenants

- Article V – **Affirmative Covenants**. Generally cover ministerial matters such as the delivery of periodic reporting information, providing notices, compliance with applicable laws, payment of taxes and other expenses, and similar items.
- As with negative covenants, each affirmative covenant is independent of each other covenant.
- Affirmative covenants apply to Borrower and [Material] Subsidiaries.
- Disclosure covenants enable the Lenders to monitor the Borrower's performance – delivery of financial statements, SEC filings, compliance certificates, notices of material events.
- Affirmative covenants relating to how the Borrower runs its business are another category of covenants in the Model Credit Agreement – preservation of existence (MAE included), maintenance of properties (MAE included), maintenance of insurance, payment of obligations, compliance with laws, sanctions and books and records.
- Inspection Rights – pre-default can be exercised only by the Administrative Agent twice a year; post-default, no limitation on number of inspections. Included in brackets: post-default, the Administrative Agent and the Lenders can give the Borrower opportunity to participate in any discussions with the Borrower's accountants.
- Use of Proceeds – General working capital purposes; Model Credit Agreement does not contemplate an acquisition financing or other specific financing need.

2021 LSTA Model Credit Agreement – Negative Covenants

- Article VI – **Negative Covenants**. Restrictions on the Borrower's activities; generally divided into two categories. An **incurrence test** is a one-time restriction. A **maintenance test** is a continual or periodic restriction.

- Among negative covenants included in the Model Credit Agreement are standard covenants covering debt, lien and fundamental changes, transactions with affiliates, restrictive agreements, change in nature of business. Bracketed negative covenants include ones covering investments, dispositions and restricted payments.

- Placeholders for baskets included in the Model Credit Agreement for certain negative covenants – debt, liens, dispositions, restricted payments and investments.

- Types of baskets (Model Credit Agreement includes placeholders for dollar baskets):
  - Cap of a fixed dollar amount is a **"hard cap"** or **"dollar" basket;**
  - Cap based on a percentage of a variable (*e.g.*, a percentage of total assets, consolidated net income, or other variable) is a **"grower" basket** or **"soft cap;"** and
  - Basket that is sized by a percentage of cumulative consolidated net income or the Borrower's cumulative excess cash flow that is retained by the Borrower is referred to as a **"builder basket"** because it builds in size as the Borrower's cumulative consolidated net income or retained excess cash increases over time.

2021 LSTA Model Credit Agreement – Negative Covenants (Financial Covenants)

Section 6.12 – **Financial Covenants**.

- Financial covenants can be **divided into three categories**: those that test the Borrower's financial position at a **particular date** (such as a net worth or current ratio covenant), those that test its **performance over one or more fiscal periods** (such as a fixed charges or interest coverage covenant), and those that are a **hybrid of the first two** and contain both date-specific and performance elements, such as a debt ratio covenant that tests the ratio of debt at a particular date to earnings for a specified fiscal period ending on that date.
- The Model Credit Agreement includes following financial covenants: Consolidated Leverage Ratio, Consolidated Interest Ratio and Tangible Net Worth.
- **In keeping with LSTA's policy, the Model Credit Agreement leaves economic terms, such as covenant levels, blank and does not make any suggestions.**
- **Covenant-lite transactions** typically replace financial covenants that constitute "maintenance" tests with covenants constituting "incurrence" tests. A maintenance covenant requires the Borrower to maintain a given level of financial performance (with a default occurring if that level is not continually satisfied for any reason, voluntary or involuntary), while an incurrence covenant simply requires the Borrower not to take some action within its control, such as issuing additional debt or paying dividends, unless a given financial ratio meets agreed parameters (with a default occurring only if the Borrower nevertheless takes the voluntary action in breach of the parameters).

2021 LSTA Model Credit Agreement – Events of Defaults

Events of Default – Specified events or circumstances that may (a) decrease likelihood that the Borrower will be able to pay its obligations under the credit agreement and (b) increase Lenders' desire to terminate credit facility. Can serve as basis for the Lenders to stop extending credit to the Borrower and start exercising remedies, such as exercising setoff, foreclosure on collateral or lawsuit to recover the Obligations.

- Events of Default related to lesser nonpayment breaches sometimes described as "technical defaults," and can merit less drastic consequences such as late fees, default interest, etc…
- The Model Credit Agreement does not include for a grace period for a breach of a representation or warranty, but does provide for a 30-day grace period for certain technical defaults.
- Dollar baskets included for judgments and ERISA-related Event of Default.
- Section 7.02 **Application of Payments**. Waterfall provides for the fees and expenses of the Administrative Agent to be paid before any other claims, then fees and expenses to the Lenders and the Issuing Bank, payment of unpaid L/C fees and for interest (and breakfunding payments) to be paid before principal, for revolving loans to be paid before cover for any outstanding letters of credit (except that during a Default, the waterfall requires all principal and cover among all tranches of Loans and Letters of Credit to be paid ratably).

2021 LSTA Model Credit Agreement – Miscellaneous

Section 9.02 **Waivers; Amendments**

- **Required Lenders** – set at 50% threshold (in brackets). Basic rule is that the majority or "Required Lenders" must approve any modification, waiver, or supplement to any provision of the credit agreement. Certain modifications need to be approved by lenders ***directly and adversely affected*** (*i.e.*, adverse financial terms, alterations in pro rata provisions and changes to voting provisions).

- **Unanimous Consent** – Waive a condition precedent, permit expiration of L/C to occur after Commitment Termination Date, changes to definition of Required Lender.

ERRONEOUS PAYMENT PROVISION

Judge Furman's Decision in Revlon Surprised Many in the Loan Market

- In August 2020, the agent under a Revlon credit agreement was due to pay approximately $7.8 million in interest to lenders.

- Due to a series of errors, however, the agent wired Revlon's lenders approximately $900 million (an amount coinciding with the aggregate principal and interest then outstanding).

- **Agent realized its error within 24 hours** and **promptly notified the lenders** of the mistake and requested they return the funds. Adhering to market practice, many lenders promptly returned the funds, and agent quickly recouped about $385 million. But about $500 million was not returned

- Agent sought to recover the monies paid by mistake from those "non-returning lenders." The non-returning lenders, in turn, relied upon the common law defense of "**discharge-for-value**".

Erroneous Payment Provision is Agent's Response to the Revlon Decision

- Judge Jesse Furman's decision in *In re Citibank August 11, 2020 Wire Transfers* (a.k.a. "*Revlon*") raised a number of issues for the loan market
- Legal response: LSTA drafted a new erroneous payment provision ("EPP") for credit agreements
- Operations response: LSTA worked with agent banks who created appropriate payment notices to limit the risk of a Revlon type situation

In the LSTA EPP, Lenders Waive the Discharge for Value Defense

Waiver of the Discharge for Value Defense: Most importantly, lenders are required to waive the discharge for value defense. No ones disputes the necessity of that….

Issues still being monitored include:

- **Clawback Cutoff Date:** After an accidental payment has been made, the "clawback cut-off date" is the date after which the agent can no longer seek the return of the mistakenly paid funds. Agents want unlimited time… lenders want a tightframe
- **Determination of Whether a Mistake Has Been Made:** sole discretion or reasonable discretion? LSTA draft provides for both options in brackets to describe the threshold for the agent's determination of whether a mistake has occurred.

"Deemed Assignment of Loans" Clause of the EPP May Be Deleted

Issues still being monitored include:

- **Deemed Assignment of Loans**: If the agent does not recover an erroneous payment from a lender, then that lender shall be deemed to have assigned its loans…. complicated!

- **Payment of Interest on Returned Funds**: Recipient must return the funds with interest. Certain lenders objected to this because the provision was triggered by the agent – not them - making a mistake. But precedent for this in typical credit agreements for the return of funds paid by the agent on the presumption that either the borrower or the lenders were going to fund them an equivalent amount.

2018 MCAPS: BOILERPLATE PROVISIONS

MCAPs: List of Boilerplate Provisions

- Yield Protection
- Right of Setoff
- Cash Collateral
- Sharing of Payment by Lenders
- Administrative Agent's Claw-Back
- Indemnity

Yield Protection

- **Economic Rationale**
  - Lenders expect to receive a certain return usually calculated by reference to an agreed margin over its cost of funds.
  - This pricing model rests upon certain assumptions regarding the regulatory treatment of loan and the lender.
  - If regulatory treatment makes the loan more expensive for lenders or otherwise reduces their rate of return, lenders expect to have the right under the loan agreement to pass on these costs to the borrower to protect this expected return.

- **Delay in Requests:** The Borrower is not required to compensate a Lender for increased costs incurred or reductions suffered more than nine months prior to the date that the Lender has notified the Borrower of the Change in Law giving rise to the increased costs or reduction giving rise to the Lender's claim.

Right of Setoff

- **Setoff versus Recoupment**
  - **Setoff:** Application of a mutual debt owed by a creditor to the debtor against claim held by such creditor against the debtor, to satisfy the claim in the amount of the applied debt — **effectively the netting of the two obligations**. Section 553 of the U.S. Bankruptcy Code addresses setoffs, and, although it does not create any rights, Section 553 generally preserves any setoff rights that were available pre-petition.
  - **Recoupment:** Similar to setoff, but not subject to the same restrictions in a bankruptcy (11 U.S. Code § 553). Recoupment exists under common law and continues without restriction in bankruptcy. Recoupment permits the netting of mutual obligations between a debtor and creditor but only if they arise under a single, integrated transaction. In that sense it is different from setoff, which when permissible in bankruptcy would permit the netting of mutual obligations from different transactions.

Right of Setoff (cont.)

- **MCAP Setoff Provision**
  - **Event of Default:** Setoff right can be exercised upon the occurrence and continuance of an Event of Default.
  - **Defaulting Lenders:** If a Defaulting Lender exercises any right of setoff, all amounts so set off shall be paid over immediately to the Administrative Agent for further application in accordance with the provisions of Section [Defaulting Lenders] and, pending such payment, shall be segregated by such Defaulting Lender from its other funds and deemed held in trust for the benefit of the Administrative Agent, the Issuing Banks, and the Lenders.
  - **Participants:** To the extent permitted by law, each Participant also shall be entitled to the benefits of Section [Right of Setoff] as though it were a Lender; provided that such Participant agrees to be subject to Section [Sharing of Payments by Lenders] as though it were a Lender. See Successors and Assigns and Sharing of Payments MCAPs.

Cash Collateral

- **"Cash Collateralize"** means, to [deposit in a Controlled Account or to] pledge and deposit with or deliver to the Administrative Agent, for the benefit of one or more of the Issuing Banks or Lenders, as collateral for L/C Obligations or obligations of Lenders to fund participations in respect of L/C Obligations, cash or deposit account balances or, if the Administrative Agent and each applicable Issuing Bank shall agree in their sole discretion, other credit support, in each case pursuant to documentation in form and substance satisfactory to the Administrative Agent and each applicable Issuing Bank.

- The Borrower is generally required to Cash Collateralize Fronting Exposure of Non-Defaulting Lenders.

- MCAPs do not indicate the required amount of Cash Collateral, but the Borrower may typically request to specify 100%.

- The Issuing Bank's right to consent to documentation governing Cash Collateralization may be subject to minimum L/C Obligation threshold.

Sharing of Payments by Lenders

- **Greater Payments to Participants**. If a lender exercises its right of setoff or counterclaim or otherwise, receives payment for principal and interest of any of its Loans in excess of its proportionate amount, such lender shall (a) notify the Administrative Agent, and (b) purchase (for cash at face value) participations in the Loans and such other obligations of the other Lenders, or make such other adjustments as shall be equitable, so that the benefit of all such payments shall be shared by the Lenders ratably in accordance with the aggregate amount of principal of and accrued interest on their respective Loans and other amounts owing them, subject to certain exclusions.

Administrative Agent's Clawback

- In the MCAPs, Administrative Agents consent to provide funding before they have access to lenders advances. As a protective measure, they have the ability to claw back advanced amounts.

- The debt instrument should be reviewed to determine whether the Administrative Agents has the obligation or right to make such advances. If so, if the Administrative Agent has such right then a clawback clause would usually be included.

- **Practice Note**: If a debt instrument provides that the Administrative Agent will only advance when it has same day available funds from the parties, then the clawback clause may not be required. The clawback will generally expend both to funding by Lenders and payments by the Borrower. The determination as to whether the Administrative Agent will make advances on behalf of either prior to receipt of same day funds is a business matter to be negotiated, and generally will be dependent upon the credit quality of the parties involved.

Indemnity

- Indemnification by the Borrower. The Borrower shall indemnify the Administrative Agent (and any sub-agent thereof), each Lender and each Issuing Bank, and each Related Party of any of the foregoing Persons (each such Person being called an "Indemnitee") against, and hold each Indemnitee harmless from, **any and all losses, claims, damages, liabilities and related expenses** (including the fees, charges and disbursements of any counsel for any Indemnitee)[, and shall indemnify and hold harmless each Indemnitee from all fees and time charges and disbursements for attorneys who may be employees of any Indemnitee], incurred by any Indemnitee or asserted against any Indemnitee by any Person (including the Borrower [or any other Loan Party]) other than such Indemnitee and its Related Parties **arising out of, in connection with, or as a result of**:
  - the execution or delivery of this Agreement, any other Loan Document or any agreement or instrument contemplated hereby or thereby, the performance by the parties hereto of their respective obligations hereunder or thereunder or the consummation of the transactions contemplated hereby or thereby;
  - any Loan or Letter of Credit or the use or proposed use o the proceeds therefrom (including any refusal by any Issuing Bank to honor a demand for payment under a Letter of Credit if the documents presented in connection with such demand do not strictly comply with the terms of such Letter of Credit), any actual or alleged presence or Release of Hazardous Materials on or from any actual;

Indemnity (cont.)

- alleged presence or Release of Hazardous Materials on or from any property owned or operated by the Borrower or any of its Subsidiaries, or any Environmental Liability related in any way to the Borrower or any of its Subsidiaries; or

- any actual or prospective claim, litigation, investigation or proceeding relating to any of the foregoing, whether based on contract, tort or any other theory, whether brought by a third party or by the Borrower [or any other Loan Party], and regardless of whether any Indemnitee is a party thereto; provided that such indemnity shall not, as to any Indemnitee, be available to the extent that such losses, claims, damages, liabilities or related expenses (x) are determined by a court of competent jurisdiction by final and nonappealable judgment to have resulted from the gross negligence or willful misconduct of such Indemnitee or (y) result from a claim brought by the Borrower or any other Loan Party against an Indemnitee for breach in bad faith of such Indemnitee's obligations hereunder or under any other Loan Document, if the Borrower or such Loan Party has obtained a final and nonappealable judgment in its favor on such claim as determined by a court of competent jurisdiction. This Section [ ](b) shall not apply with respect to Taxes other than any Taxes that represent losses, claims, damages, etc. arising from any non-Tax claim.

AGENCY

LSTA Agency Language Makes Clear that the Agent's Duties are Merely Administrative in Nature

- The agent does not act in a fiduciary capacity and:
  - Shall not have any duty to take any discretionary action.
  - Shall not have any duty to disclose any borrower related information.
  - Shall not be liable for any action taken or not taken by it with the consent or at request of lenders **in the absence of its own gross negligence or willful misconduct**.
  - Shall not have any duty to ascertain any statement made in connection with the agreement, the contents of any certification, performance of any terms, covenants, conditions, etc.

Agent Has No Duty to Monitor or Enforce Compliance with a DQ List

"The Administrative Agent shall not be responsible or have any liability for, or have any duty to ascertain, inquire into, monitor or enforce, compliance with the provisions hereof relating to Disqualified Institutions. Without limiting the generality of the foregoing, the ***Administrative Agent shall not (x) be obligated to ascertain, monitor or inquire as to whether any Lender or Participant or prospective Lender or Participant is a Disqualified Institution*** *or (y) have any liability with respect to or arising out of any assignment or participation of Loans, or disclosure of confidential information, to any Disqualified Institution."*

ASSIGNMENTS

The LSTA Published Model Transfer Provisions Nearly 20 Years Ago and Periodically Updates Them

- **Minimum Amounts**: MCAPs provide that the minimum amount of a revolver assignment is **$5 million** and a term loan assignment is **$1 million**, or no minimum amount if it's the entire remaining amount of the assigning lender's commitment/loans.

- **Borrower's Deemed Consent**: MCAPs state that no consent is required for any assignment except borrower's consent is required (unless default has occurred and is continuing); provided that the **borrower shall be deemed to have consented** to an assignment **unless it shall object by written notice to agent within 5 business days after receiving notice**.

Loans Cannot be Assigned to Natural Persons

- In 2014, the LSTA clarified the prohibition on assignments to people. Now MCAPs expressly state that **loans can't be assigned to a natural Person or to a holding company**, **investment vehicle or trust for, or owned and operated for the primary benefit of, a natural person**. Thus, someone interested in acquiring a loan cannot circumvent this provision by setting up a LLC or other entity to then acquire that loan.

- **Register of Lenders**: The **entries** in the register shall be **conclusive absent manifest error**. The register shall be available for inspection by the borrower and any lender at any reasonable time and from time to time upon reasonable prior notice.

- **LSTA Best Practices**: LSTA has promulgated best practices regarding the sharing of lender lists. If a request for an amendment is pending, a lender seeking to consult with other syndicate members in connection therewith may request from the agent a **lender list with the names of the other lenders in the syndicate and their exposures**.

Lenders May Sell Participations Without Borrower or Agent Consent

Any Lender may at any time, without the consent of, or notice to, the Borrower or the Administrative Agent, sell participations to any Person (other than a natural Person…)…; provided that (i) such Lender's obligations under this Agreement shall remain unchanged, (ii) such Lender shall remain solely responsible to the other parties hereto for the performance of such obligations, and (iii) the Borrower, the Administrative Agent, the Issuing Banks and Lenders shall continue to deal solely and directly with such Lender in connection with such Lender's rights and obligations under this Agreement.

Limitations on Free Transferability are Undesirable Because They Impede Liquidity

- Borrower will generally lose its right to consent to assignments upon the occurrence of certain specified Defaults or Events of Default (but a DQ list survives).

- Consent rights are often qualified by a requirement that the consent not be unreasonably withheld or delayed. Whether the Borrower wrongly withholds its consent must be analyzed on the basis of objective factors. Borrowers and Lenders have an interest in loans being treated as commercial debt relationships (not securities); consent rights may be a factor in making such a determination.

Participant May Vote on the Sacred Rights But This Will Depend on the Terms of the Participation Agreement

- Participation agreement shall provide that the lender/grantor shall retain the right to enforce the credit agreement and to approve any amendment, but the participation agreement may provide that such lender will not, without the participant's consent, agree to any amendment with respect to the sacred rights, i.e., those terms requiring unanimous lender consent.

- What if the lender/grantor of the participation has sold its position to many different participants? What if the lender/grantor is permitted, under the terms of the participation agreement, to count the interests of its affiliates when determining the majority participants?

DISQUALIFIED INSTITUTIONS

LSTA MCAPs Include a Disqualified Institution Structure

- **Health Warning!** LSTA DQ Structure should be viewed as a "package deal".
- **DQ List:** The DQ List includes the names of the institutions which the borrower does not want to own its loans and be in the syndicate.
- LSTA MCAPs define "**Disqualified Institution**" as follows:

  "Disqualified Institution" means, on any date, (a) any Person designated by the Borrower as a "Disqualified Institution" by written notice delivered to the Administrative Agent on or prior to the date hereof and (b) any other Person that is a Competitor of the Borrower or any of its Subsidiaries, which Person has been designated by the Borrower as a "Disqualified Institution" by written notice to [the Administrative Agent and the Lenders (including by posting such notice to the Platform) not less than [_] Business Day[s] prior to such date]; provided that "Disqualified Institutions" shall exclude any Person that the Borrower has designated as no longer being a "Disqualified Institution" by written notice delivered to the Administrative Agent from time to time.

DQ List May Be Updated With Names of Borrower's Competitors

- **Updating**: DQ List is created on or before the date of the credit agreement, and the names of the Borrower's competitors may also be added after the Closing Date. The LSTA form does not provide a definition of "Competitor;" instead, a drafting note suggests that the term be defined with specificity in reference to the particular borrower and its business.

- **Transparency:** LSTA DQ Structure assumes that the DQ list will be posted to the public side of a platform so that lenders may easily access and review it before they trade (the agent should also give the DQ List to a lender upon request).

- **No Pop-ups:** Assignees should not need to finalise AA.

DQ List Applies to Both Assignments and Participations

- **The DQ List applies to assignments** and **participations.**

- **But the DQ List has no retroactive effect.** Thus, trades entered into with a party that is added to DQ list post-trade date (ie, a competitor of the borrower) may be settled.

  "For the avoidance of doubt, with respect to any assignee that becomes a Disqualified Institution after the applicable Trade Date (including as a result of the delivery of a notice pursuant to, and/or the expiration of the notice period referred to in, the definition of "Disqualified Institution"), (x) such assignee shall not retroactively be disqualified from becoming a Lender and (y) the execution by the Borrower of an Assignment and Assumption with respect to such assignee will not by itself result in such assignee no longer being considered a Disqualified Institution. ***Any assignment in violation of this clause (h)(i) shall not be void****, but the other provisions of this clause (h) shall apply."*

Borrower May "Yank" a Disqualified Institution and Prepay Their Loans

- **Borrower's remedies**: If an assignment or participation is made to a Disqualified Institution, borrower may "yank" the DI or require the DI to assign its loans to an Eligible Assignee. The LSTA form leaves it to the parties to decide whether the borrower should prepay or purchase the term loans at par, the price paid by the DI, or market price.

  "If any assignment or participation is made to any Disqualified Institution without the Borrower's prior written consent… or if any Person becomes a Disqualified Institution after the applicable Trade Date, the Borrower may… terminate any Revolving Credit Commitment of such Disqualified Institution and repay all obligations of the Borrower owing to such Disqualified Institution in connection with such Revolving Credit Commitment, (B) in the case of outstanding Term Loans held by Disqualified Institutions, purchase or prepay such Term Loan by paying the ***[lowest] [lesser] of (x) the principal amount thereof [and][,] (y) the amount that such Disqualified Institution paid to acquire such Term Loans [and (z) the [market price] of such Term Loans]****, in each case plus accrued interest, accrued fees and all other amounts (other than principal amounts) payable to it hereunder and/or (C) require such Disqualified Institution to assign, without recourse… all of its interest, rights and obligations under this Agreement to one or more Eligible Assignees…."*

LSTA's DQ Structure is Finely Balanced – A Package Deal

- LSTA's DQ Structure works when each element of the paradigm is present.
- If the DQ List is to apply not only to assignments but also to participations, then it must be posted so lenders may easily review it.
- If the agent has no responsibility for monitoring the list, then parties must be able freely and regularly to access it and share it with prospective assignees.
- If the list is capable of being updated for competitors post-closing, then there must be a notice period before the updated DQ List takes effect.
- **Parties are urged to remember that the elements of the LSTA's DQ Structure are carefully intertwined; changing one aspect without regard for the whole can impact its effectiveness.**

Disqualified Institutions are Walled Off from Borrower Information and Lender Actions

- The LSTA DQ Structure provides that all Disqualified Institutions are **prohibited** from **receiving confidential borrower information**, engaging in **fundamental lender actions and** taking part in **creditor decisions** in connection with insolvency scenarios. (See clause (h)(iii) in the "Successors and Assigns" section of the MCAPs).

- MCAPs "Confidentiality Provision" also expressly provides that the **DQ List may be disclosed to any assignee or participant, or prospective assignee or participant**. This is important because the assignee confirms in the Assignment Agreement that it meets all the requirements to be an assignee under the Successors and Assign provision of the CA and thus is also confirming that it is not a Disqualified Institution.

MCAPs Confidentiality Provisions Include Carveouts Which Help the Loan Market Function

- As noted above, the **DQ List may be disclosed to any assignee or participant or any prospective assignee or participant.**

- In addition, the agent and lenders may disclose the existence of the credit agreement and information about it to **market data collectors** and similar service providers to the lending industry.

- With respect to borrower confidential information, Lenders must keep that information confidential except that it may be disclosed to, amongst others, affiliates, regulators, as required by law, and subject to a confidentiality agreement with substantially the same terms as the confidentiality provision to any assignee/participant and **any prospective assignee/participant**; any actual or prospective party to a swap; any rating agency; and the CUSIP Service Bureau.

LSTA AND LMA FORMS – POINTS OF CONVERGENCE AND DIVERGENCE

Intercreditor Arrangements: Unitranche (Lsta's Agreement Among Leaders)

- **Typical Syndicated Financing Structure** - All lenders in a facility share the same collateral package, the same ability to enforce liens and the same priority in relation to payments and the proceeds from the enforcement of security.
- **First Lien / Second Lien Structure** - Alternative structure in which the "first lien" and "second lien" loans are secured by the same collateral, with the liens of second lien lenders subordinated to those of first lien lenders. Usually documented as two separate loans via separate loan documents and agents, with lender rights and priorities established in an intercreditor agreement.
- **Unitranche** – Hybrid structure. Developed to affect a "first lien/second lien" structure through a consolidated credit facility that has a single loan with two tranches (a first out tranche and a last out tranche). Features **one**: set of loan documents; agent; "blended" interest rate; and set of lenders. More prevalent in middle market deals.
- **Agreement Among Lenders ("AAL")**- Key document in unitranche financing. Governs the rights and obligations of the first out and last out lenders as well as the allocation of payments.
- **LSTA Form of AAL –** Published on March 1, 2019.
- Initially, there were questions about the enforceability of unitranche structures because the AAL was not signed by the borrower. However, *In re RadioShack Corp.* provided some guidance because it implicitly recognized the court's ability to interpret and enforce an AAL. (A first-out lender was entitled to enforce the provisions of the AAL prohibiting the last-out lender from objecting to the sale of the debtor. *In re RadioShack Corp.*, Case No. 15-10197, Docket No. 1744 (Bankr. D. Del. Apr. 9, 2015).)

Intercreditor Arrangements: LMA's Super Senior/ Senior Intercreditor Agreement

- Increasingly, European private debt funds have been lending directly to private equity sponsors and others borrowers using a "unitranche" term loan that consolidates senior and mezzanine tranches into a single instrument with a blended margin. However, the European form of unitranche differs from the approach taken in the US, which documents the transaction with an AAL that the borrower does not sign.
- In Europe, intercreditor provisions are typically contained in a single intercreditor agreement that is signed by the borrower and all lenders. The most common structure adopted in these deals is one where one of more funds participate in the term loan on a pari passu basis, and a bank provides "super senior" working capital facilities.
- On 17 May 2018, the LMA published the Intercreditor Agreement for Leveraged Acquisition Finance Transactions (Super Senior / Senior) (the "**Super Senior/Senior ICA**"). The approach reflected in the LMA's Super Senior / Senior ICA is that all of the debt ranks *pari passu* as to payments but, upon enforcement, the working capital liabilities are elevated to the top of the waterfall to a "super senior" position and, as such, are repaid from recoveries ahead of the term loan debt.
- **Single Class of Creditors in EU Restructuring Context —** It is worth noting that where the American-style unitranche structure is adopted in Europe (*i.e.*, an AAL not signed by the borrower), there do exist some questions about enforceability. In particular, there are questions about whether the first out and last out creditors can form a single class of creditors for the purposes of an English law scheme of arrangement under **Part 26 of the Companies Act 2006**, or if junior lenders can form a separate class to capitalize upon hold-out value. Recent case law has suggested that for junior creditors to form a separate class in a restructuring, they must demonstrate that their distinct economic rights are also accompanied by separate legal rights enforceable against the borrower. Since borrowers do not typically sign AALs, it is unlikely that junior creditors would be able to form a separate class of creditors. *Re Apcoa Parking Holdings GmbH & Ors* [2014] EWHC 1867 (Ch.).

Modified European Term Loan Bs

- As mentioned previously, Term Loan As are syndicated in the US to traditional banking institutions that typically require the amortization and tighter covenants.

- Term Loan Bs are usually held by non-bank lenders who are generally comfortable with no financial maintenance covenants and permit greater overall covenant flexibility. Term Loan Bs have a higher margin and other economic protections (such as "no-call" periods) not commonly seen in Term Loan As to compensate for less rigorous terms.

- Demand by European sponsors and borrowers to achieve greater flexibility has led to the English law "European TLB" market.

- The European TLB market is now a funding option for borrowers in larger leveraged transactions (£250m of debt or greater). However, European TLBs are generally less flexible than their US counterparts. European TLB instruments typically contain guarantor coverage tests, higher lender consent thresholds, more robust events of default and mandatory prepayment provisions and generally have smaller permitted baskets when compared to their US counterparts.

LMA and LSTA Forms – Covenants and Undertakings

Examples in which US and European loan markets document covenants (per U.S. loan agreements) / undertakings (per European loan agreements) differently, include:

1. **Unrestricted Subsidiaries**. To minimize the risk of credit leakage, loan agreements restrict dealings between obligors and other members of the borrower group that are not obligors, as well as third parties. In U.S. loan agreements, there is usually an ability to designate members of the borrower's group as "unrestricted subsidiaries" so that they are not restricted under the loan agreement. However, the loan agreement will then limit dealings between members of the restricted and unrestricted group and the value attributed to the unrestricted group might not be taken into account in calculating financial covenants.

2. **Reclassification of Permitted Debt and Liens**. Reclassification provisions (allowing the borrower to utilize one type of permitted debt exception and then reclassify the incurred permitted debt under another exception) are graining traction in the US. Additionally, reclassification is being applied to lien covenants, allowing borrowers to reclassify transactions that were permitted under a fixed basket as permitted under an unlimited leveraged-based basket after the borrower's financial performance improves.

LMA and LSTA Forms – Covenants and Undertakings (cont.)

3. **Lien Covenant vs. Negative Pledge**. Both sets of forms broadly define liens to include any security interest, charge, pledge, claim, mortgage, hypothecation or other arrangement to provide a priority or preference on a claim to the borrower's property.

   - Lien covenants in U.S. loan documents prohibit the incurrence of all liens, but provides for **exceptions**, such as liens securing permitted refinancing indebtedness, purchase money liens, statutory liens and other liens that arise in the ordinary course of business, as well as a general basket based on a fixed dollar amount or a percentage of consolidated total assets to secure a specified amount of permitted indebtedness.

   - The European equivalent, known as a **"negative pledge,"** covers the same elements as the U.S. restriction on liens, but typically goes further and restricts "quasi-security" where the arrangement or transaction is entered into primarily to raise financial indebtedness or to finance the acquisition of an asset. **"Quasi-security"** includes transactions such as sale and leaseback, retention of title and certain set-off arrangements.

LMA and LSTA Forms – Covenants and Undertakings (cont.)

4. **Investment Covenant & Builder Baskets**. Both sets of forms restrict a borrower's ability to make investments, which cover loans, advances, equity purchases and other asset acquisitions.

   - In addition to the specific list of exceptions, U.S. loan agreements also include a general basket, sometimes in a fixed amount or based upon a flexible **"builder basket"** aggregation concept. The builder basket represents an amount that the borrower can utilize for investments, restricted payments, debt prepayments or other purposes. Traditionally, the builder basket begins with a fixed-dollar amount and "builds" as retained excess cash flow or consolidated net income accumulates.

   - European loan agreements will typically contain stand-alone undertakings restricting the making of loans, acquisitions, joint ventures and other investment activity by the borrower (and other obligors) and commonly restricted such activity by way of fixed cap baskets and other additional conditions. While builder baskets are not as prevalent in European loan agreements, acquisitions will be permitted if funded from certain sources, such as retained excess cash flow.

LMA and LSTA Forms – Covenants and Undertakings (cont.)

5. **Restricted Payments**. Both sets of forms restrict a borrower from making payments on equity, including repurchases of equity, payments of dividends and other distributions, as well as payments on subordinated debt. There are typical exceptions for restricted payments not materially adverse to the lenders, such as payments on equity solely in shares of stock, or payments of the borrower's share of taxes paid by a parent entity of a consolidated group.

   - In European loan agreements, such payments are typically restricted under separate specific undertakings relating to dividends and share redemptions or the making of certain types of payments to non-obligor shareholders, such as management and advisory fees, or the repayment of certain types of subordinated debt. Borrowers can negotiate specific carve-outs (usually hard capped amounts) for particular "permitted payments" or "permitted distributions" as required (for example, to permit certain advisory and other payments to the sponsor), in addition to the customary ordinary course exceptions.

   - In U.S. loan agreements, a borrower may use its builder basket for restricted payments, investments and prepayments of debt, subject to annual baskets based on either a fixed-dollar amount or compliance with a certain financial ratio test.

LMA and LSTA Forms Comparison – LMA Guarantee Provision

- **LSTA Model Credit Agreement** does not include a guarantee. In most investment grade, U.S. transactions, the borrower is a public reporting company and is usually the only borrower.

- LMA As is the case in Europe, however, it is not unusual to see guarantees of investment grade loans if the borrower's capital markets debt is guaranteed.

SECONDARY MARKET DOCUMENTS

LSTA Has Published a Suite of Documents for the Trading and Settling of Loan Trades

- LSTA has published documents for use in the secondary loan market, including:
  - Par and Distressed Confirms that can be used to evidence a loan trade
  - Assignment Agreement
  - Purchase and Sale Agreement
  - Proceeds Letter Agreements
  - Par and Distressed Participation Agreements. The LSTA forms of participation are afforded sale accounting treatment.

Traders Determine Whether to Trade on Par or Distressed Documents

- Generally, **loans made to US borrowers will trade on LSTA documents**.

- Before the financial crisis, loans trading at a price above 90 were generally regarded as "performing loans" and traded on a par confirm. After the financial crisis, that was no longer the general rule, and market participants considered many factors – not just price – when choosing to trade a loan on par or distressed documents.

- Whether to trade on par or distressed is a business decision to be made by the parties at the time of trade.

- The **type of Confirm determines the method of settlement**. If a trade is entered on a Par Confirm and the market shifts to distressed before the par trade settles, the parties still settle only on an Assignment Agreement.

Oral Loan Trades are Binding When Parties Agree to the Material Terms

- **Statute of Frauds Exemption**. Since 2002, loan trades have been eligible to qualify for the exemption from the statute of frauds.

- **QFC Exemption.** In order for an oral agreement to be eligible for the "qualified financial contract" exemption, there must exist either (i) sufficient evidence to indicate that a contract was made or (ii) a prior or subsequent writing between the parties by which they agree to be bound.

- LSTA Confirms include an agreement by parties not to assert the Statue of Frauds as a defense to enforcement of oral trades and to require the parties to prepare and maintain an internal record reflecting the terms of each trade.

- "**A trade is a trade**". Provided the parties have traded on LSTA documents previously and agree the borrower's name, and the name, type, and amount of debt, and the price, their oral trade will be binding at the time of the trade.

Trades Must Settle as Assignments or Participations or Cash Settle

- Each of the **LSTA Par Confirm** and **Distressed Confirm** is divided into two parts: (i) the "face" of the confirm which includes all the trade specific information and any special riders, and (ii) the second part is comprised of the standard terms and conditions.

- **Form of Purchase.** If parties cannot settle their trade as an assignment, then the trade is still binding and they must settle as a participation. If that, too, is not possible, they must "cash settle", an arrangement which must give the parties the economic equivalent of the agreed-upon trade.

- "**Assignment Only**". If parties agree to this at the time of trade, then they must settle as an assignment or cash settle.

Loan Market Trades on Syndicate Information Which May Constitute Material Non-Public Information

- Parties may trade as a **principal** or an **agent**. A party acting as principal is directly liable for completion of trade.
- **Riskless Principal** concept is available provided it is discussed at time of trade. Trade is subject to successful purchase from/sale to a third party.
- LSTA Confirms include **Big Boy Reps.**
- Loan Market trades on **Syndicate Information**.
- **Voting**. LSTA Confirms provide that, while a trade is open, a seller need not solicit the buyer's vote with respect to any amendment or waiver. However, the market practice is for sellers to consult with their downstream buyers.

THANK YOU

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