PANORAMIC

LOANS & SECURED FINANCING 2025

Contributing Editors

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LEXOLOGY

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Panoramic guide (formerly Getting the Deal Through) enabling side-by-side comparison of local insights into general issues (bank loans versus debt securities; common forms of bank loan facility; bridge facilities; role of agents, trustees and lenders; governing laws); regulation (capital, liquidity and disclosure requirements; use of loan proceeds; cross-border lending; interest rate and currency restrictions); security interests and guarantees; the impact of fraudulent conveyance and similar doctrines on the structure of bank loan financings; intercreditor matters; loan terms and structures; and recent trends.

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Loans & Secured Financing: Global Overview

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Not since the global financial crisis and the collapse of Lehman Brothers in 2008 has the world faced such prolonged economic challenges and uncertainties. In the wake of the covid-19 pandemic, the global leveraged finance markets have also been significantly impacted by recent geopolitical tensions in Europe and the Middle East, a looming US presidential election, combined with surging inflation and interest rate pressures across the globe. Over the last 18 months these headwinds have subjected the global debt capital markets to materially higher borrowing costs, volatile M&A activity, a marked decrease year-over-year in syndicated lending and high-yield offerings, and increased regulatory pressures. However, this backdrop has also revealed the resilience and adaptability of loan market participants.

Unlike 2008, where a shuttered bank market amplified a global recession, private credit funds and other alternative providers of capital stepped into the void left by the retreat of traditional broadly syndicated bank loan financings and the effective closure of the high-yield bond markets. Such private capital gave borrowers and private equity sponsors crucial access to debt financing for refinancings, capital expenditures and liquidity needs – in addition to facilitating relatively modest acquisition and other bolt-on activity. This was a global trend, as borrowers and private equity sponsors in the United States, Europe and Asia increasingly shifted their financing structures, and financing sources, towards private capital. To the benefit of borrowers, there has been a resulting stream of new entrants into the European and US private credit markets, adding to an already competitive landscape. Outside of Europe and the United States, markets that were traditionally bank-dominated (such as Australia, Singapore and the United Arab Emirates) are now also bearing witness to the emergence of private capital providers in the lending landscape.

The rise of private credit has invited increased regulatory scrutiny, both in and outside the United States. US regulatory agencies sought to expand their authority to regulate non-bank financial institutions, including by imposing more detailed reporting requirements on non-bank lending activities. International organisations also followed suit. For instance, the Global Financial Stability Report, published in April 2024 by the International Monetary Fund, called for, inter alia, enhanced regulatory scrutiny over private credit.

The co-existence and interplay of a multiplicity of private and public debt financing sources has benefitted sponsors, which increasingly took advantage of the varied finance options open to them. In the leveraged acquisition space, sponsors will run competitive debt

processes across several types of products and lenders. For instance, to raise buyout financing, a sponsor may multi-track a private credit loan option (with its inherent flexibilities allowing for higher leverage and features such as paid-in-kind interest and committed undrawn facilities to finance future acquisitions) against a syndicated bank loan option (which might offer better pricing and more flexible terms). Starting in late 2023, broadly syndicated financings (both loan and high yield) noticeably picked up in the United States, prompted, in part, by a refocusing on repricing transactions. This trend is expected to continue and possibly spill over from the United States to the rest of the globe, potentially resulting in a re-balancing of deal activity between the broadly syndicated and private credit markets. Stronger sponsors and borrowers will likely continue to enjoy an increasingly diverse range of financing options and providers.

The evolution of the loan market does not stop at the intersection of private capital and bank financing. Other worldwide themes currently influencing lending practices (and appear poised to continue to do so for years to come) include the integration of environmental, social and governance (ESG) considerations into the financing process. The impact of ESG in US financings remains modest, given a complex and evolving political and regulatory climate, and may be limited to know-your-customer and other diligence matters. However, in Europe, the impact is more profound. In European financings, borrowers often receive pricing incentives from lenders by demonstrating achievement of certain agreed ESG-minded benchmarks and goals, and so this will continue to influence financing structures, as well as the types of acquisitions and activities that such borrowers pursue.

While digitisation and technologies such as blockchain have not had the fundamental impact on the loan market than some commentators anticipated, it remains to be seen whether artificial intelligence (AI) might prove transformational. For example, sponsors and borrowers may be able to leverage AI technology to audit certain features of their financing arrangements, track deals across vast data sets, and one day even use such information to negotiate market terms and spot developing trends. Whether or not AI is the next frontier in commercial lending, market participants will watch as this next chapter unfolds in the global leveraged finance market and ushers in novel investment opportunities and ever-evolving deal dynamics.

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United Kingdom

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GENERAL FRAMEWORK

Jurisdictional pros and cons

What are the primary advantages and disadvantages in your jurisdiction of incurring indebtedness in the form of bank loans versus debt securities?

The primary advantage of a commercial loan, whether it is provided by a bank or a non-bank financial institution such as a private credit fund, is its relative flexibility and ease of execution. Under English law, commercial loan parties are generally free to negotiate the terms of a loan agreement as they see fit. The ordinary principles of English contract law will apply to questions of the parties' rights and obligations under the agreement, as well as in relation to the form of documentation, mechanics and day-to-day administration of the loan (for instance, amendments and waivers).

While the provision of certain retail and consumer loans in the United Kingdom are regulated activities, a commercial loan agreement involving a corporate lender and corporate borrower generally falls outside such regulations. English law loan agreements play a significant role in the European acquisition finance market. For example, syndicated bank loans are frequently used by private equity sponsors for the financing of large corporate buyouts, while loans by private credit funds and bilateral bank loans are often used for the financing of mid-market leveraged buyouts.

By contrast, the issuance of debt securities to the public or professional investors in the United Kingdom is subject to various rules and regulations, which generally require detailed disclosures and periodic reporting. Subject to certain exceptions, an approved prospectus will generally be required. Even where the securities are intended to be offered solely to certain qualified professional investors, a prospectus will still likely be required if the securities are intended to be traded on a regulated market. Due to the regulatory framework and disclosure requirements, issuances of debt securities may involve more time, cost and documentation. However, for certain issuers, debt securities can prove a useful source of longer-term financing at competitive pricing.

Law stated - 25 April 2024

Market snapshot

How do borrowers approach the different options of debt products and sources available to them, including debt securities? With respect to bank loans, how is the debt market split between direct lenders and private credit funds on the one hand, and banks and institutional investors on the other?

The question of whether a borrower should incur indebtedness in the form of a loan provided by a bank (or a credit fund), or through the issuance of debt securities in the UK market is generally determined by the financial status and specific objectives of the borrower, rather than being a straight choice between instruments. For example, large investment-grade corporations that wish to access a wide pool of capital at attractive pricing and enhance their visibility in the market are better suited towards the issuance of debt securities in the corporate bond market. Likewise, sovereign issuers, public sector entities

and financial institutions that wish to diversify their funding sources may also find debt securities issuances more appropriate for their needs. Other common issuers include those with a specific project financing need, such as a real estate or infrastructure project. In these cases, subject to market appetite, certain issuers might find that a longer-term project bond issuance will be more congruent with the revenue generation schedule of the project being financed.

Alternatively, other corporate borrowers and private equity sponsors will typically find a bank or private credit loan more appropriate for an acquisition financing or for raising funds for capital expenditure or working capital purposes. This is especially the case where a borrower has a pre-existing strong relationship with one or more lenders.

While the loan market in the United Kingdom and Europe has historically been dominated by banks, the role and significance of direct lenders and private credit funds has grown significantly since the 2008 global financial crisis. This evolution has been particularly notable in the acquisition finance market. Whether a borrower is able to access the syndicated lending market, bilateral bank market or private credit market (or a combination of them) will depend on a multitude of factors. At a simplistic level, financing for large corporate acquisitions requiring a debt quantum above a certain threshold (usually €350 million) tends to be the domain of the syndicated loan market. For financings below this threshold or where the borrower requires higher leverage, private debt providers are a potential financing source. Also, for smaller deals with lower leverage levels, bilateral or club bank lending can also be an option depending on the sectors and industries involved. However, the choice of financing source is much more involved and will depend on many factors including market conditions, the leverage a borrower requires, the extent and priority of security the borrower is able to provide, and the purpose of the financing.

Law stated - 25 April 2024

Forms

What are the most common forms of loan facilities? Discuss any other types of facilities commonly made available to the debtor in addition to, or as part of, the loan facilities.

Most corporate loan financings will typically provide for one or more tranches of committed term debt alongside a committed revolving facility. Term debt is often used to finance the particular transaction in question (say, an acquisition or dividend recapitalisation), whereas the revolving facility is designed to provide liquidity to the borrower so that it can finance its working capital and general corporate requirements.

In UK and European financings, term debt does not typically amortise and is provided on a bullet repayment basis whether it is provided by a bank or a private credit fund. Once a term loan has been repaid, it usually cannot be reborrowed. In contrast, a revolving facility can be drawn, re-paid and re-drawn by the borrower. Revolving facilities are typically only provided by banks and are often structured so that they can be drawn by way of cash or by way of ancillary facilities, which would provide for drawings in the form of letters of credit, bank guarantees and various other instruments the borrower might need for its day-to-day banking and operating purposes.

Lenders might also permit the borrower to raise additional term and revolving debt from new third-party lenders, subject to various conditions such as compliance with a maximum leverage ratio condition and there being no event of default subsisting at the relevant time the new debt is being raised.

In private credit loans, lenders may also offer the borrower a committed undrawn facility to help fund future acquisitions and capital expenditure, provided again that certain conditions are satisfied such as compliance with a leverage ratio, that there is no event of default subsisting and the utilisation occurring within a certain time frame.

Law stated - 25 April 2024

Investors

Describe the types of investors that typically participate in loan financings and the types of investors that participate in various other types of debt products.

The investment banks that agree to arrange and underwrite syndicated term loans in the UK and European market operate on a originate-to-distribute model. This means their primary focus is to sell down or syndicate the loan in portions as quickly as possible to other lenders, rather than holding the entire loan and remaining the lender of record. During the syndication process, the arranging banks will concentrate on selling down the loan to other investment banks, mutual funds, pension funds, collateralised loan obligation funds and hedge funds. Syndication to private credit funds is also becoming increasingly common. There is a substantial and active liquid secondary market for syndicated loans where loan participations can be traded.

In contrast, private credit funds do not syndicate the loans they originate. Rather, their aim is to hold the loan until maturity, in similar fashion to traditional relationship lending. As private credit funds originally raise the funds they on-lend from third-party investors, investing in and holding loans until maturity helps to maximise the returns they can generate for these investors. While private credit loan documentation generally permits loans to be assigned and sold down to other lenders, unlike the syndicated bank market, there is no active secondary market for such trading.

In the case of a bilateral or club bank lending, the lending bank's balance sheet will typically be used to make the loan. Regulatory capital requirements and internal sector exposure limits will therefore impact the availability of such loans and the types of borrowers that are able to access this market.

Revolving facilities, whether they are attached to a private credit term loan or a syndicated term loan, will usually be provided by a bank capable of providing clearing facilities and ancillaries (such as the issuance of letters of credit, bank guarantees, corporate overdrafts, and similar retail products).

Law stated - 25 April 2024

Investors

How are the terms of a loan facility affected by the type of investors participating in such facility?

Due to the difference in investor base, a term loan provided by a private credit fund has some significant differences to a term loan provided as part of a syndicated bank loan. For example, given that a private credit fund generally wishes for its loan to be outstanding until maturity and earning a return for its investors, such loans might attract significant early prepayment premiums (known as call protection), unlike a syndicated bank loan.

For the same reason, a private credit loan will often accommodate the borrower paying a portion of its accrued interest in kind by capitalising it into the loan principal (known as a PIK option), albeit subject to a pricing premium and compliance with certain other conditions. In syndicated loans, accrued interest is invariably required to be paid in cash.

Private credit funds are also generally more willing to accommodate committed undrawn facilities, which provide the borrower with additional flexibility to finance future acquisitions and capital expenditure. In the case of syndicated loans, given that they are premised on drawn amounts being sold down to other lenders, it is less common to see committed undrawn tranches being offered to borrowers. However, the market has evolved in recent times with some syndicated financings now providing for delayed draw term loans, which operate in a similar fashion.

Importantly, as syndicated loans are typically used to finance larger deals and given there has been significant convergence in recent years with US high-yield terms in the large-cap finance market, syndicated loan terms are usually less restrictive than their private credit equivalents. For example, a syndicated term loan will typically not include a financial covenant for the benefit of the term lenders (known as a covenant-lite loan), whereas a private credit loan will usually include at least a leverage maintenance covenant for the benefit of the term lenders.

Law stated - 25 April 2024

Bridge facilities

Are loan facilities used as 'bridges' to permanent debt security financings? How do the structure and terms of bridge facilities deviate from those of a typical loan facility?

Yes, loan facilities can and are often used to bridge permanent debt security financings. Bridge structures are used to ensure funds certainty for leveraged acquisition financing purposes and help overcome the intrinsic uncertainty of accessing the debt capital markets. Bridge loans are often used in European financings that have a US high-yield component.

Bridge loan facilities are similar to standard term loan facilities, but tend to have a shorter maturity, must be prepaid from the proceeds of the debt securities and may have tighter undertakings and covenants in relation to debt incurrence, distributions and otherwise limited permitted leakage.

Law stated - 25 April 2024

Role of agents and trustees

What role do agents or trustees play in administering loan facilities with multiple investors?

Agents and trustees play a vital role across the loan market, including in syndicated financings, bilateral and club bank finance, and private credit financings. Professional, third-party agents are invariably appointed to function as the facility or administrative agent, as well as the security agent, which holds and potentially enforces the security package in the case of a secured loan. In the latter case, the security agent will hold the security as trustee for the benefit of the underlying facility lenders.

The duties of an administrative agent include receiving and processing utilisation and drawdown requests, receiving and distributing payments (including repayments of principal and payments of interest and fees), processing loan transfers and assignments, and distributing information to the lender group (including notices, compliance certificates and financial information).

Most facility documentation will make clear that the administrative agent's role is administrative and mechanical only, and that no other duties (fiduciary or otherwise) shall be implied. The loan documentation will also usually provide that the agent will be indemnified by the lenders for any losses it incurs in performing its administrative functions on behalf of the lenders. There will be similar provisions in relation to the security agent (which will usually be included in the intercreditor agreement).

Law stated - 25 April 2024

Role of lenders

Describe the primary roles of, and typical fees charged by, the financial institutions that arrange and syndicate bank loan facilities, as well as lenders that participate in the private credit market.

In the case of syndicated loan facilities, the borrower will usually engage one or more investment banks to serve as the mandated lead arrangers (MLAs). The MLAs will agree to arrange the loan either on a best efforts or underwritten basis. If underwritten, the MLAs will be obliged to provide the requested financing to the borrower even if they are not able to successfully syndicate the loan to other investors. On closing, the borrower will pay the MLAs an arrangement fee, usually structured as a percentage of the total commitments of the committed facilities as of the closing date.

In the case of a private credit loan, as there is no syndication process, the borrower will deal directly with the private credit fund's deal principal in relation to the diligence and underwriting of the requested loan. Once the credit fund agrees to provide the loan, it will determine how the loan should be split and allocated between its various lending funds and vehicles, albeit such allocation will not generally affect the borrower as a practical matter. Similarly to a syndicated loan, the private credit fund will charge an arrangement fee for any term and committed undrawn facilities provided (and commitment fees in relation to such undrawn facilities prior to tier utilisation).

Law stated - 25 April 2024

Governing law

1.8.1. In cross-border transactions or secured transactions involving guarantees or collateral from entities organised in multiple jurisdictions, which jurisdiction's laws govern the loan and intercreditor documentation?

Where the parties have selected English law as the governing law of the loan agreement, the intercreditor agreement will typically also be governed by English law. The guarantee provisions are usually included in the loan agreement itself rather than being separately documented, and therefore will also be governed by English law. English courts will generally respect a contractual choice of law clause.

The governing law of collateral documentation should follow the jurisdiction of where the asset being secured is located. For example, security over an English company should be documented in an English law share security agreement, whereas security over a piece of real estate in Germany should be governed by a German law real estate mortgage.

Law stated - 25 April 2024

REGULATION

Capital and liquidity requirements

Describe how capital and liquidity requirements impact the structure of loan facilities, including the availability of related facilities and the differing impact of such requirements on different types of investors.

The capital, leverage and liquidity requirements associated with the implementation of Basel III has had a significant impact on the banking sector in the United Kingdom, and fundamentally changed the leveraged lending landscape in the United Kingdom and Europe. Most obviously, these stricter prudential standards have directly impacted the ability of bank lenders to underwrite and hold leveraged loans, and loans to certain riskier credits and sectors, by increasing their internal costs for holding such riskier loans on their balance sheets.

In turn, this has facilitated both the growth of private credit lending in the leveraged loan space, as well as entrenching the originate-to-distribute model that is intrinsic to the large-cap syndicated loan market. As these stricter prudential standards do not apply to private credit funds, they have been able to fill the gap left by the retreat of traditional banks and take market share, particularly for leveraged acquisition loans in the mid-market space and other riskier types of lending, such as recurring revenue loans and growth financing.

These capital and liquidity requirements have driven banks to seek new sources of business, including establishing their own direct lending businesses, which seek to compete directly with traditional private credit funds.

Law stated - 25 April 2024

Disclosure requirements

For public company debtors, are there disclosure requirements applicable to loan facilities?

Yes, UK-listed companies are subject to continuing disclosure obligations imposed by the

London Stock Exchange and the Financial Conduct Authority. Such companies must provide periodic financial reports, including comprehensive notes on their financing activities, including the terms of new debt issuances.

Law stated - 25 April 2024

Use of loan proceeds

How is the use of loan proceeds by the debtor regulated? What liability could investors be exposed to if the debtor uses the proceeds contrary to regulations? Can investors mitigate their liability?

Under English law, the parties to a loan agreement are free to negotiate the purpose for which the loan proceeds may be applied. The loan agreement in the case of a leveraged acquisition loan will typically stipulate that the term loan proceeds shall be applied towards paying the consideration for the target company and associated transaction costs, while the revolving facility may be used for working capital or general corporate purposes.

The loan agreement will also invariably stipulate that, as a condition to the utilisation of any loan, the making of the loan (or any lender's participation in the loan) must not be unlawful in any relevant jurisdiction, and that no default is continuing or would result from the proposed loan, which will usually include a breach of applicable sanctions, anti-corruption and anti-money laundering regulations in the jurisdictions of the lender and relevant obligors. Where such a breach occurs after the loan has been drawn, an event of default would occur allowing the lenders to accelerate any outstanding loans, terminate unused commitments, exercise remedies against the borrower, and commence enforcement of the security package.

Law stated - 25 April 2024

Cross-border lending

Are there regulations that limit an investor's ability to extend credit to debtors organised or operating in particular jurisdictions? What liability are investors exposed to if they lend to such debtors? Can the investors mitigate their liability?

Yes, lenders will not extend credit to borrowers incorporated or operating in a sanctioned territory. The specific applicable regulations (and relevant exceptions) will also depend on the jurisdiction of incorporation of the lender itself.

In any case, most commercial loan agreements will be drafted broadly to cover all economic and financial sanctions and measures administered by a wide variety of sanctions authorities in various jurisdictions, including the United Kingdom, the United States, the European Union and the respective governmental institutions that administer such applicable sanctions

law (eg, the US Department of State and the Office of Foreign Assets Control of the US Department of the Treasury).

Law stated - 25 April 2024

Debtors' leverage profile

Are there limitations on an investors' ability to extend credit to debtors based on the debtors' leverage profile?

The Bank of England has written extensively regarding leveraged lending in the UK market and has publicly expressed some concerns about the management of leverage levels in both bank lending and private credit lending contexts. The Prudential Regulation Authority of the Bank of England has issued leveraged lending guidelines in a similar fashion to guidelines previously published by the European Central Bank and the US Federal Reserve. However, these are guidelines only, and emphasise the importance of the relevant institutions themselves having appropriate internal controls and procedures for managing the risks associated with leverage loans, as opposed to mandating specific lending thresholds or limits on leverage.

Law stated - 25 April 2024

Interest rates

Do regulations limit the rate of interest that can be charged on loans?

Under English law, there is no express regulation or usury law that limits the rate of interest that may be charged for commercial loans, and commercial parties are generally free to negotiate the economic terms of their loan arrangement as between themselves, including as regards interest and reasonable default interest for overdue amounts. However, an English court may apply equitable principles to prevent a lender enforcing an unconscionable bargain, or from enforcing a provision that requires payment upon breach of the contract on grounds that it would amount to a penalty, if it was found that such payment did not represent a genuine estimate of loss arising from the breach. Note that usury laws applicable in the jurisdiction of incorporation of the lender or the financier might also be relevant and could apply, notwithstanding that the loan agreement itself might be governed under English law.

Law stated - 25 April 2024

Currency restrictions

What limitations are there on investors funding loans in a currency other than the local currency?

None. There are no foreign exchange or currency controls applicable in the United Kingdom.

Law stated - 25 April 2024

Other regulations

Describe any other regulatory requirements that have an impact on the structuring or the availability of loan facilities.

In the case of loan facilities provided to commercial loan parties incorporated in the United Kingdom, there is no requirement to obtain a banking licence or other regulatory approvals for such activity. However, to the extent the loan is made under an English law facility to a party incorporated or located outside the United Kingdom, there may be regulatory or licensing issues to consider in that jurisdiction.

Certain lending activity is regulated in the United Kingdom, including consumer credit and mortgage lending.

Law stated - 25 April 2024

SECURITY INTERESTS AND GUARANTEES

Collateral and guarantee support

Which entities in the organisational structure typically provide collateral and guarantee support for loan financings? Are there certain types of entity that typically do not provide, or are restricted in their ability to provide, collateral and guarantee support for such financings?

The security and guarantee package is a matter of negotiation for the lender and the borrower, and the parties are free to structure this as they see fit. However, for a conventional English law leveraged acquisition loan, the security and guarantee package will involve the following entities.

- A security agreement executed by the borrower's parent company providing security over all the shares of the borrower, and any intercompany receivables owing to the parent company by the borrower. The governing law of the security agreement will depend on the jurisdiction of incorporation of the borrower. The parent company will also typically be subject to a holding company covenant under which it will not be permitted to trade or incur any other liabilities, to ensure a clean single point of enforcement. The parent company may also provide a guarantee, although often it will provide this security as a non-guarantor third-party security provider only.
- A security agreement granted by the borrower, providing security over any shares it holds in any other loan parties, material bank accounts and material intercompany receivables. To the extent the borrower is located in a jurisdiction where a floating charge or equivalent all assets security is able to be granted (eg, England, Ireland and the United States), the borrower will usually provide such security over all its other assets under such floating charge. To the extent the borrower holds shares in other loan parties incorporated in foreign jurisdictions, a separate share security agreement governed by the laws of that foreign jurisdiction may be required. The borrower will also be a guarantor under the facility agreement to cross-guarantee the obligations of the other obligors.
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The loan agreement will also typically require material subsidiaries to provide security and guarantees of similar scope to that provided by the borrower. What constitutes a material subsidiary is a matter of negotiation but will usually be those entities that represent a certain percentage of profits and (or) assets of the overall group (eg, 5 per cent or 7.5 per cent). Holding companies of such material subsidiaries will also typically be expected to provide share security over the shares of such material subsidiaries along with any intercompany receivables owed to them by the material subsidiary.

Law stated - 25 April 2024

Collateral and guarantee support

What types of obligations typically share with the loan obligations in the collateral and guarantee support? If so, are all such obligations equally and ratably covered by the collateral and guarantee support?

Typically, the term and revolving facilities, including any ancillary facilities established under the revolving facility, together with any permitted secured hedging (where such hedge counterparties have acceded to the intercreditor agreement) will share the security and guarantee package.

However, note that in the case of most private credit deals, the revolving facility (and certain permitted hedging) will rank super senior as regards the proceeds of enforcement of security, so that the lenders providing such facilities will be entitled to enforcement proceeds ahead of the term lenders. This is a common feature of the UK and European private credit market and is designed to attract revolving facility lenders into these deals given that most private credit funds are unable to provide revolving loans and associated clearing facilities.

Law stated - 25 April 2024

Commonly pledged assets

Which categories of assets are commonly pledged to secure loan financings? Describe any categories of asset that are typically not thus pledged, or are restricted from being so.

The security and guarantee package is a matter of negotiation for the lender and the borrower, and the parties are free to structure this as they see fit.

However, the most typical assets secured in a UK or European leveraged acquisition financings are shares, material bank accounts and material intercompany receivables. To the extent it is possible in a jurisdiction for a company to provide a floating charge or other equivalent forms of all-assets security, then that security will also typically be granted in respect of the other assets of the company. Other assets may also be included in the security package depending on the nature and type of the deal. For example, where a loan is made to a group that has significant intellectual property or real estate assets, the lenders may seek to take specific security over the relevant intellectual property or real estate.

Note that the scope of assets and extent of security that may be provided by potential foreign guarantors will depend on and may be limited by local law matters – for example, corporate governance and director duties issues, guarantee limitations, financial assistance laws in respect of upstream guarantees, notarial requirements and potential taxes and stamp duties. For this reason, where an agreement contains an ongoing guarantee and security coverage requirement, parties may negotiate 'agreed security principles' to account for such limitations and to regulate how security and guarantees are to be implemented in respect of foreign incorporated entities.

Law stated - 25 April 2024

Creating and perfecting a security interest

Describe the method of creating and perfecting a security interest on the main categories of assets. What are the consequences of failing to perfect a security interest?

The exact methods of creating and perfecting security depend on the nature of the asset and the type of security provider and are beyond the scope of this overview. However, key points to note are as follows.

Charges

One of the most common types of security is the charge, which creates an encumbrance in favour of the security taker and permits the appropriation of the charged asset in satisfaction of a liability or obligation. It does not transfer a legal or equitable interest in the asset to the security taker. A charge will either be fixed or floating depending on the control exercised by the security taker over the charged asset.

The formalities that must be complied with depend on the asset to be secured. For example, a legal charge over certain assets such land and patents must be in writing. A legal charge can be granted by a security provider by deed executed by that security provider without the security taker having to execute the charge deed.

With limited exceptions, charges created by an English company or limited liability partnership are registrable at Companies House within 21 days of creation. Registration is critical as failure to do so means that the charge is void against a liquidator, administrator or any creditor of the security provider.

Mortgages

To create a mortgage, the legal or beneficial title to the secured asset is transferred to the security holder. The security provider benefits from a right to have title re-transferred to it when the secured obligations are discharged. The security taker does not need to take possession of the mortgage asset. The security provider is prevented from dealing with the mortgaged asset unless the security taker agrees otherwise.

The formalities depend on the asset to be mortgaged. By way of example, a legal mortgage over land must be created by deed, one over debts or choses in action must be in writing

and through intellectual property, registered in the relevant register. To the extent that the formalities are not complied with, an equitable mortgage is created.

Equitable mortgages do not involve a transfer of title. The disadvantage of equitable security is that a subsequent legal security interest will take priority over the earlier equitable one if the latter was taken in good faith and without notice.

The perfection requirements for mortgages depend on the nature of the assets. As with charges, mortgages created by an English company or limited liability partnership are typically registrable at Companies House within 21 days of creation. Registration is critical as failure to do so means that the mortgage is void against a liquidator, administrator or any creditor of the security provider. A legal mortgage over land must also be registered at the Land Registry. Failure to do so means that a subsequent mortgage registered at the Land Registry may take priority over the unregistered prior mortgage.

Assignments

Assignments by way of security are a type of mortgage. They involve a transfer of rights by the assignor to the assignee subject to an obligation to reassign those rights back to the assignor upon the discharge of the obligations that have been secured. Assignments are typically used for assets such as debts, intellectual property, receivables, other contractual rights or securities.

An assignment by way of security can be either legal or equitable. An assignment will be legal if it is:

- in writing and executed by the security provider;
- absolute (namely, unconditional and for the whole amount); and
- notified in writing to the person against whom the assignor could enforce those assigned rights.

In the case of a legal assignment, the assignee has the right to sue, in its own name, the relevant third party against whom the assignor has its contractual rights. In the case of an equitable assignment, the assignee would have to join the assignor in the legal action against the third party.

Pledges or liens

As the name implies, to create possessory security under English law such as a pledge or a lien, the security holder must have and retain actual possession of the secured asset. A pledge is the actual or constructive delivery of possession of an asset by way of security. A pledge may confer a power of sale whereas a lien merely entitles the security taker to retain the asset until the relevant debt has been satisfied. Only items of property capable of being delivered can be subject to a pledge or lien. Unlike pledges, liens typically arise by operation of law rather than being granted by a security provider. Pledges and liens are not registrable.

Law stated - 25 April 2024

Future-acquired assets

Can security interests extend to future-acquired assets? Can security interests secure future-incurred obligations?

Yes, security interests can be taken over future assets, depending on the type of security. Both fixed and floating charges can be created over both existing and future assets. On the other hand, it is not possible to take a legal mortgage over property that is not in existence at the time the mortgage is created or is not owned by the mortgagor at the time the mortgage is created. This is because no title can transfer at the time the mortgage is created. However, it is possible to create an equitable mortgage over future property once the property is in existence and owned by the mortgagor. Accordingly, the same principle applies in relation to assignments (which are a type of mortgage) (namely, while it is not possible to enter into a legal assignment in relation to rights under future contracts, it is possible to enter into an equitable assignment in relation to such rights).

Future-incurred obligations can be secured by security interests provided that the security documents expressly include future indebtedness as part of the secured obligations.

Law stated - 25 April 2024

Maintenance

Describe any maintenance requirements to avoid the automatic termination or expiration of security interests.

Generally, validly created and perfected security under English law does not require ongoing maintenance to ensure its validity. However, a fixed charge holder who does not exercise control over the secured asset runs the risk of having his or her security recharacterised as a floating charge. Equally, a pledge-holder giving up possession risks losing his or her security.

Law stated - 25 April 2024

Release

What are typical steps to release security interests on assets? Is such a release automatic under any circumstances?

Once a debt has been repaid, the security provider is entitled to have the secured asset returned free from the security interest. This principle is enshrined in the equity of redemption rule, which provides that upon repayment of the relevant debt in full, there cannot be a fetter on the right of the security provider to redeem the security and recover the asset.

Usually, the mechanism to release the security will be documented in the security agreement. Typically, this entails the entry by the security taker into a deed of release, which confirms the release or termination of the mortgage or charge. In relation to a floating charge, the security taker may also issue a letter of non-crystallisation where required. In connection with the release documentation, the relevant registers (such as Companies House or the Land Registry) are also updated by filing the relevant forms to confirm satisfaction of the security.

Law stated - 25 April 2024

Non-fulfilment of guarantee obligations

What defences does a guarantor have against claims for non-fulfilment of guarantee obligations? Can such defences be waived?

Guarantor protections arise in the context of certain events that can discharge, extinguish or reduce the liability of the guarantor under the guarantee. The key events giving rise to guarantor protections are:

- the granting of time to the principal;
- the release of the principal;
- the release of co-guarantors;
- diminishing the benefit of the security for the guaranteed obligations;
- changes in the identity of the parties; and
- material variations to the underlying contract, which is guaranteed, which could prejudice the guarantor, in each case without the guarantor's consent.

These guarantor protections will provide the guarantor with a defence to a claim under the guarantee. At worst, the guarantor could argue that the guarantee has been released in full due to the variation of the underlying transaction. As a result, the lender could find itself without the benefit of a guarantee. From the lender's perspective, it is important that the guarantor is not permitted to raise a defence to a claim under the guarantee while amounts are still owing under the facility. Guarantor protections can be varied, amended or deferred by agreement between the parties. It is standard practice to include an express provision in guarantees whereby the guarantor agrees to vary its protections by waiving all defences that arise from the guarantor protections noted above.

Notwithstanding the terms of their guarantee, lenders should take care when making any changes to the underlying transaction. As a matter of best practice, for all but the most minor amendments, lenders should require a new guarantee or at least the guarantor's express prior written consent to the relevant events (which could otherwise prejudice the guarantor) together with an express written confirmation from the guarantor that the guarantee remains in full force and effect notwithstanding the occurrence of the relevant event.

Law stated - 25 April 2024

Parallel debt requirements

Describe any parallel debt or similar requirements applicable in a secured loan financing where an agent acts for multiple investors.

Under English law, trust structures are used for holding security in secured syndicated facilities. The security agent (sometimes also known as the security trustee) acts as a trustee and holds the transaction security on trust for the secured parties. The security agent is, therefore, authorised by the beneficiaries in the trust to perform its rights and duties and

to exercise direct or incidental rights, powers and discretions given to it under the terms of the security trust provisions in the facility documentation or security documents. The trust structure avoids the need for security to be:

- granted separately to each of the creditors, which can be expensive and time-consuming; and
- re-taken or re-registered (and hardening periods reset) should a secured party change as a result of a loan transfer.

Law stated - 25 April 2024

Enforcement

What are the most common methods of enforcing security interests? What are typical limitations on enforcement?

The method of enforcing security depends on the type of security interest held and the enforcement rights set out in the security document. The most common enforcement methods include a receivership appointment, exercising the power of sale, taking possession and an administration appointment.

Receivership appointment

A receiver is an individual (typically a licensed insolvency officeholder) appointed by the charge holder to take custody of the charged assets, manage those assets and receive the income from them. Usually, a receiver will also have the power to sell the assets and to apply the proceeds of sale in satisfaction of the secured debt. A receiver appointed under the implied terms of the Law of Property Act 1925 is deemed to be the agent of the security provider, which provides a degree of liability protection for the appointing security taker. A receiver is appointed in relation to the charged assets only, he or she does not take control of the security provider itself and a receivership appointment does not result in the imposition of a moratorium.

Exercising the power of sale

A security taker may be able to exercise a power of sale in relation to the secured assets arising at law or under the security document to pay off the secured liabilities using the enforcement proceeds. Under the Law of Property Act 1925, a mortgagee has the right to sell the property, free from the mortgagor's interest. A lender may not exercise this statutory power of sale unless:

- the mortgage sum has become payable, notice requiring payment has been served on the mortgagor, and payment has not been made three months after service:
- interest under the mortgage is due and unpaid for two months; or
- there has been a breach of a term of the mortgage (other than payment of the mortgage sum).

However, the security document will typically also provide for a contractual power of sale. When enforcing such a contractual power, the security taker must act in good faith, take reasonable steps to obtain a proper price for the asset, obtain the best price reasonably obtainable, act with reasonable care and skill and act fairly towards the security provider.

Taking possession

Under the Law of Property Act 1925, a legal mortgagee has a right to possession of the mortgaged property. As is the case with the power of sale, this right is usually also contained in the security document. A security taker becomes a mortgagee in possession either by taking physical possession of the property if it is possible to do so peaceably or by obtaining a court order. However, this enforcement method is less common because in becoming a mortgagee in possession, the lender assumes responsibility as owner, such as liability for environmental damage.

Administration appointment

A secured party may also apply to appoint an administrator over the security provider (in or out of court depending on the nature of the security). Administration is an insolvency process and allows the reorganisation of a company's affairs or the realisation of its assets for the benefit of creditors. The administrator takes over the control of the company's affairs from its directors. When a company enters administration, it becomes subject to a statutory moratorium that prevents creditors from enforcing their claims against the company. The principal objective of an administration is to rescue the company (as distinct from the business carried on by the company) so that it can continue trading as a going concern. If the rescue of the company is impossible, the administrator must aim to achieve a better result for the company's creditors as a whole than would be likely if the company were put into liquidation.

If the administrator cannot achieve a better result for creditors as a whole, the purpose of the administration is to realise the company's property to make a distribution to the company's secured or preferential creditors.

Law stated - 25 April 2024

Fraudulent conveyance and similar doctrines

Describe the impact of fraudulent conveyance, financial assistance, thin capitalisation, corporate benefit and similar doctrines on the structure of loan financings.

Transactions entered into by a company (such as granting security) prior to its insolvency may be challenged by the administrator or liquidator if the company was insolvent at the time they were made, or if the transactions caused the company to become insolvent. Such reviewable transactions include misfeasance transactions, transactions at an undervalue, preferences, extortionate credit transactions, avoidance of floating charges and transactions defrauding creditors. The challenge typically involves a court application by the insolvency

officeholder. To mitigate against the risk of challenge, it is important to assess the commercial rationale for entering into the transaction, if it was entered into at arm's length, the company's solvency and to document the same.

Corporate benefit rules are relevant in the context of group companies granting guarantees or security for the benefit of the borrower. Directors have a duty to promote the success of the company for the benefit of its members and therefore not to take on obligations without receiving some equivalent commercial benefit. If a company enters into a transaction where there is no commercial benefit, that transaction can be set aside at the instance of the shareholders of the company. Any third party such as a lender may be unable to enforce the transaction and (or) hold the proceeds derived from the transaction as a constructive trustee. This risk can be mitigated by the shareholders passing a resolution approving the entry into the transaction and the directors carefully evaluating and documenting why the entry into the transaction would benefit the company.

A public company may not give financial assistance for the purpose of the acquisition of its shares or those of a parent company, and a private company may not give financial assistance for the purpose of the acquisition of shares of a public parent company. The prohibition does not apply where the company's principal purpose in giving the assistance is not to give it for the purpose of any acquisition, or the giving of the assistance for that purpose is only an incidental part of some larger purpose of the company, and the assistance is given in good faith in the interests of the company. For a private company to provide financial assistance, the directors will need to be satisfied that the proposed transaction is in the best interest of the company, and that the proposed transaction does not constitute an unlawful distribution or other illegal reduction of the company's capital.

Law stated - 25 April 2024

INTERCREDITOR MATTERS

Payment and lien subordination arrangements

What types of payment or lien subordination arrangements are common where the debtor has obligations owing to more than one class of creditors?

Where a borrower has obligations owing to more than one class of creditor, it will be for the parties to agree and negotiate the precise terms of the intercreditor arrangements that will apply as between the competing creditors. The extent of any payment subordination and the order of priority of security as between the creditors will depend on the nature and commercial agreement between the parties, as well as established market practice and custom for certain types of financing arrangements.

For example, the common structure for a private credit loan deal is for the term loan lenders and the revolving facility lenders to rank pari passu in terms of payments and security. However, the intercreditor agreement will usually provide that the revolving facility lenders and certain hedge counterparties will have a super senior claim on the proceeds of any enforcement of the security package (so that they will be, in effect, paid out first from enforcement proceeds). By contrast, an English law-syndicated leveraged loan will not usually elevate the revolving facility to super senior status.

English courts will generally enforce the terms of an English law intercreditor agreement (including on insolvency of the debtor), as regards the contractually agreed order of priority, standstill provisions, and any agreed payment subordination.

Law stated - 25 April 2024

Creditor groups

What creditor groups are typically included as parties to intercreditor agreements? Are all creditor groups treated the same under the intercreditor agreement?

In most cases, the lenders will ideally ensure that all material financial creditors are made party to the intercreditor agreement. Providers of all senior and junior debt will be party to the intercreditor agreement.

Creditors of any shareholder loans provided to the borrowing group will also be expected to become party to the intercreditor agreement as subordinated creditors. Group company creditors that provide intercompany loans will also be party to the intercreditor agreement and subordinate their claims under those loans in favour of the senior creditors. Parties may negotiate certain minimum debt quantum thresholds for the purposes of such accessions. Where debt is incurred above the borrowing group, creditors of such holdco debt will not typically be required to accede to the intercreditor agreement.

Law stated - 25 April 2024

Rights of junior creditors

Are junior creditors typically stayed from enforcing remedies until senior creditors have been repaid? What enforcement rights do junior creditors have prior to the repayment of senior debt?

Typically, junior creditors (as well as super senior revolving lenders) are stayed from enforcing remedies until the senior creditors have been repaid. Again, it will be for the parties to agree and negotiate the precise terms of the intercreditor arrangements that will apply as between the competing creditors, although there are established market practices for certain types of financing arrangements. Where the commercial agreement requires the junior creditor to be stayed from enforcing remedies, this will typically be accompanied by both payment subordination and junior ranking in relation to any shared security with the senior lenders.

Law stated - 25 April 2024

Rights of junior creditors

What rights do junior creditors have during a bankruptcy or insolvency proceeding involving the debtor?

This depends on the terms of the intercreditor agreement. Generally, the security agent is authorised to:

- take any enforcement action as instructed by the relevant majorities;
- demand, sue, prove and give receipt for any or all of that debtor's liabilities;
- collect and receive all distributions on, or on account of, any or all of that debtor's liabilities; and
- file claims, commence proceedings and do all other things the security agent considers reasonably necessary to recover that debtor's liabilities.

It is therefore the security agent that will be interacting with the insolvency officeholder on behalf of the syndicate to the extent necessary. The conduct of the security agent will be determined by the instructions given to him or her by the requisite majority in the syndicate, meaning that the senior lenders typically control such conduct.

Whether or not the security agent submits a creditor claim as secured party on behalf of the lenders in a company's administration will therefore depend on the circumstances. Secured creditors typically rely on their security and do not submit a proof of debt in insolvency other than for the unsecured balance of their debt. When a company enters administration, it becomes subject to a statutory moratorium that prevents creditors enforcing their claims against the company, including enforcing (with limited exceptions) security. This means that it is up to the administrator to distribute proceeds in accordance with the statutory order or priority with fixed-charge holders ranking first in the waterfall, and floating-charge holders ranking after expenses of the administration, preferential debts and the prescribed part. Any realisations received by the security agent from the insolvency officeholders are subsequently distributed in accordance with the waterfall set out in the intercreditor agreement.

Law stated - 25 April 2024

Pari passu creditors

How do the terms of the intercreditor arrangement change if creditor groups will be secured on a pari passu basis?

Where the creditors all rank pari passu, the intercreditor agreement will typically provide that the majority creditors (namely, usually defined as the creditor or creditors that represent over 50 per cent to 66 2/3 per cent of the aggregate total commitments) may control enforcement action. Otherwise, in true pari passu deals, the various creditors will not otherwise be prevented from receiving payments, accelerating their debt and filing claims.

Law stated - 25 April 2024

LOAN DOCUMENT TERMS

Standard forms and documentation

What forms or standardised terms are commonly used to prepare the loan documentation?

The Loan Market Association (LMA), which was established in 1996 initially for the purpose of facilitating the development of the European secondary market for leveraged loans, makes available to its members and market participants a suite of standard documentation for use across a variety of financing transactions. Currently, the LMA has published recommended forms for, among other things, leveraged finance financings, investment grade financings, real estate financings, emerging market financings and export finance transactions. In addition to loan agreements, the LMA also publishes recommended forms of intercreditor documentation, foreign law facility documentation and market guidelines on a variety of topics (eg, environmental, social and governance matters and London Inter-Bank Offered Rate (LIBOR) cessation). The LMA is extremely influential in the European loan market, and its recommended forms are extensively used as a starting point (or the base framework) for English law financings, particularly for bilateral, investment grade and non-sponsored financings.

In the case of sponsor-backed financings, legal counsel to the sponsor will usually be responsible for preparing the initial draft of the facility documents, typically based on the sponsor's own adapted version of the LMA recommended form of leveraged finance facility agreement. This sponsor precedent will still feature the drafting style, architecture and boilerplate terms of the LMA recommended form, although the commercial provisions will be heavily tailored (namely, the certain fund's terms, financial definitions, undertakings, representations and financial covenants). To the extent the sponsor and the lender already have agreed form documentation from prior transactions (or deal precedent), that existing documentation is commonly used as the starting point for subsequent deal documentation. Notwithstanding that the initial draft documentation is prepared by the sponsor's counsel, the counsel to the lenders will ordinarily issue the English law enforceability opinion in relation to the English law finance documents.

Note that on larger syndicated English law Term Loan B (TLB) financings, it is now common for the facility documents to include a schedule of New York law governed high yield style incurrence covenants, supplementing an otherwise familiar LMA-style document.

Law stated - 25 April 2024

Pricing and interest rate structures

What are the customary pricing or interest rate structures for loans? Do the pricing or interest rate structures change if the loan is denominated in a currency other than the domestic currency?

As a general principle, parties to a loan agreement are free to negotiate the economic terms of the loan, including the applicable interest rate (be it fixed or floating), any call protection that may apply in the case of early prepayment, and any fees that may apply with respect to the lender arranging the financing and (or) allocating committed capital for the purpose of making available the facility.

Floating rate structures are invariably used for both bank and private credit leveraged finance transactions, where the applicable rate will constitute the aggregate of a floating base rate element and a fixed or ratcheted margin element. Where the margin is ratcheted, this will

usually be by reference to the leverage ratio at the time the margin needs to be determined, where a higher (or lower) leverage ratio will correspond with a higher (or lower) applicable margin.

For sterling loans, since the phasing out of LIBOR, the Sterling Overnight Index Average (SONIA) is usually used as the applicable base rate. Unlike LIBOR, which was a forward-looking rate, SONIA is a backward-looking, daily risk-free rate. For this reason, most facility agreements will include now relatively standard provisions and mechanics published by the LMA for purposes of compounding SONIA to determine the applicable base rate for the relevant interest period. A forward-looking version of SONIA (Term SONIA) is also available and published for a variety of interest periods. However, uptake of Term SONIA in the market (unlike Term SOFR in the United States) has been relatively limited.

Where an English law loan is used for currencies other than sterling, the appropriate base rate for the relevant currencies should be used – for example, Secured Overnight Financing Rate (SOFR) or Term SOFR for US dollar loans and Euro Interbank Offered Rate for loans denominated in euros. For smaller bilateral commercial and retail loans in sterling, it is not uncommon for the Bank of England Base Rate to be used as the base rate.

Law stated - 25 April 2024

Pricing and interest rate structures

Does loan documentation in your jurisdiction incorporate any mechanisms to replace an established, floating benchmark rate in case such benchmark rate becomes, or is expected to become, unavailable?

Yes, in the case of leveraged finance transactions, facility agreements will invariably include interest fall-back provisions in the event of the unavailability of the base rate. The LMA 'recommended form' leveraged facility agreement includes standard fall-back provisions. For example, where the applicable risk-free rate (such as SONIA) is not available, the relevant central bank rate (namely, the Bank of England's Bank Rate) may apply, and failing that, the lender's own determined cost of funding its participation in the relevant loan.

Law stated - 25 April 2024

Other yield determinants

What other loan yield determinants are commonly used?

European syndicated TLB loans are often issued with original issue discounts. Revolving facility lenders and private credit funds will typically receive an upfront fee (or arrangement fee), which is usually deducted from the proceeds of the initial utilisation of the loan, mimicking in effect the original issue discount. The floor for sterling loans using SONIA as the base rate will commonly be set at zero.

Law stated - 25 April 2024

Yield protection provisions

Describe any yield protection provisions typically included in the loan documentation.

Most English law leveraged loan agreements will include provisions to allow the lender to claim for 'increased costs' it may incur as a result of any change in any law or regulation (or compliance with such laws or regulations) following the date of the loan agreement. In most cases, this provision will exclude matters relating to Basel III, the 2013 EU regulation on prudential requirements for credit institutions and investment firms and the 2013 EU directive on prudential supervision.

In contrast to syndicated bank loans, private credit loans will invariably include some element of call protection to protect against the economic impact of early prepayment, given that their intention is to hold the loan to maturity and maximise the return on capital for their own investors. The amount of prepayment premium and length of time the call protection will apply is a matter of negotiation between the parties.

Withholding tax gross-up provisions are also invariably included, which provide that payments to the lender are to be made free and clear of any taxes or withholding, subject to certain relatively standard carve-outs. This is particularly important where a jurisdiction imposes withholding tax, such as the United Kingdom, which imposes a 20 per cent withholding tax on UK-source interest (eg, interest payments by an English entity to a foreign lender) unless certain exceptions apply. The purpose of the tax gross-up provisions is to require the borrower to pay any additional amounts required to ensure the net amount received by the lender is equal to what would have been paid had the relevant tax not been deducted.

Law stated - 25 April 2024

Accordion provisions and side-car financings

Do loan agreements typically allow additional debt that is secured on a pari passu basis with the senior secured loans?

Yes. These provisions – known as incremental facility, accordion or additional facility provisions – are commonly included in both syndicated loans and private credit loans. The key point of negotiation between the parties will focus on the amount of additional indebtedness that is permitted to be incurred under this provision. In most cases, the maximum amount of additional indebtedness will be determined by reference to compliance with a leverage ratio, allowing the borrower to raise and incur debt under such additional facility provided that it does not exceed that agreed leverage limit.

The other key point of negotiation is whether the additional facility must be incurred as a new tranche under the existing facility documentation, or if it can be incurred under a separate facility agreement, known as a side-car facility. Provisions that allow the incurrence of incremental debt by way of side-car facilities are most commonly found in large, syndicated financings. Private credit funds lending in mid-market transactions typically insist that any incremental debt must be incurred inside the existing credit agreement to ensure equal documentary footing between the existing and any new incremental lender.

Law stated - 25 April 2024

Financial maintenance covenants

What types of financial maintenance covenants are commonly included in loan documentation, and how are such covenants calculated?

Whether or not a financing will include a financial maintenance covenant will largely depend on the nature of the financing, its purpose and the market at the time. For example, loans provided to investment-grade borrowers will not include any financial covenants. In contrast, loans to sub-investment-grade leveraged borrowers might include a leverage covenant, depending on the size of the deal and the market. Other types of financings, such as real estate financings or margin lending will warrant other specific types of financial covenants.

Historically, bank lenders under European leveraged loans traditionally had the benefit of a suite of maintenance financial covenants, namely three ratio-based covenants (a leverage ratio, interest cover ratio and a cashflow cover ratio) as well as a limit on capital expenditure by the borrower. As with other matters, the parties were free to negotiate the inclusion of other financial covenants, which sometimes included net worth, gearing and loan to value, depending on the nature of the deal and underlying assets being financed.

Nowadays, mid-market leveraged loans provided by private credit funds will be documented on a covenant-loose basis, meaning that it will typically only contain one maintenance financial covenant (a leverage ratio). A separate leverage ratio for the benefit of the revolving facility lender will also be usually included, albeit set with a certain amount of additional headroom to the term loan covenant. The covenant will be set by refence to the information contained in the sponsor's financial model, including as regards whether the ratio will step down over time, which would require the borrower to de-leverage over time to ensure compliance. In other cases, sponsors may be able to negotiate a flat covenant.

In contrast, the syndicated TLB market typically offers no financial covenant for the benefit of term lenders, and only a springing leverage ratio for the benefit of the revolving lenders. The springing nature of the covenant means that it will only have effect if the relevant trigger condition is met, usually being that the drawings under the revolving credit facility have exceeded a certain threshold amount. These types of covenant-lite structures are now the dominant structure in the syndicated TLB market and are also not uncommon in the case of larger private credit deals.

Law stated - 25 April 2024

Other negative covenants

Describe any other negative covenants restricting the operation of the debtor's business commonly included in the loan documentation.

The parties will be free to negotiate the negative covenants or undertakings that they wish in the case of an English law loan agreement. The nature, type, scope and extent of these undertakings will also depend on the specific type of financing, the creditworthiness of the borrower and market conditions at the time.

For example, a financing provided to an investment-grade public company will contain very few negative undertakings designed to restrict the business of the borrower. In contrast, a leveraged loan to a sub-investment grade borrower for purposes of financing the acquisition

will include numerous negative undertakings restricting a wide variety of corporate actions, including:

- incurrence of additional indebtedness;
- granting security;
- asset sales and disposals;
- the making of distributions;
- providing loans and guarantees to third parties;
- making acquisitions; and
- conducting reorganisations of its corporate group.

Typically, under an English law loan agreement, the negative undertakings will be drafted so that such corporate actions are prohibited generally. However, in the case of each such negative undertaking, certain permitted actions are then specifically carved out from this general prohibition.

Law stated - 25 April 2024

Mandatory prepayment

What types of events typically trigger mandatory prepayment requirements? May the debtor reinvest asset sale or casualty event proceeds in its business in lieu of prepaying the loans? Describe other common exceptions to the mandatory prepayment requirements.

In most English law leveraged loan agreements, a mandatory prepayment will be triggered upon a change of control of the borrower, or where there has been a sale of all or substantially all of the assets of the borrower's group. In most cases, the documentation will provide for either an automatic and immediate prepayment event in relation to the entire facility or extend each lender under the facility with a put right, allowing them to elect to be repaid on an individual basis.

Leveraged loan agreements will typically also require the borrower to prepay outstanding loans (on a pro-rata basis) from various other sources, including proceeds received from disposals of assets, claims against diligence providers in connection with the acquisition, listing (to the extent such listing has not resulted in a change of control requiring full prepayment), as well as from certain insurance claims. The extent to which a prepayment is required and any exclusions from the prepayment obligation are always a matter of negotiation – however, the borrower will not be required to make a prepayment to the extent the proceeds are reinvested in the business.

Law stated - 25 April 2024

Debtor's indemnification and expense reimbursement

Describe generally the debtor's indemnification and expense reimbursement obligations, referencing any common exceptions to these obligations.

In most English law leveraged loan agreements, the borrower will indemnify the lenders for any cost, loss or liability incurred by them in connection with the occurrence of any event of default, failure to pay any amounts due, funding the requested loans or where a loan has not been prepaid in accordance with a notice of prepayment. The borrower will also separately indemnify the administrative agent and the security agent in relation to their costs, losses and liabilities incurred with their duties. For example, the agent will be indemnified for acting on any notice or request made by the borrower, or where it has instructed lawyers or other advisers to the extent empowered to do so under the loan agreement. The security agent will be similarly indemnified, including in relation to its exercise of powers to enforce the transaction security. Gross negligence, wilful misconduct and fraud are common exceptions to the indemnity obligations.

Law stated - 25 April 2024

UPDATE AND TRENDS

Key developments
Are there any current developments or emerging trends that should be noted?

The loan market is continuously evolving and the interaction between the various sources of financing has served to accelerate this evolution in recent years. In the leveraged finance market, sponsors have been taking increasing advantage of the varied finance options open to them. For certain deals, this has allowed sponsors to run competitive debt processes across several types of products and lenders, for instance, dual tracking a private credit loan option (with its flexibilities on leverage, PIK interest and committed facilities) against a syndicated bank loan option (which might have more attractive pricing). To date, such competitive dual tracking has served to benefit sponsors both in terms of documentary flexibilities and pricing. Also, a relative stream of new entrants into the UK and European private credit market are also changing the competitive landscape, again much to the benefit of sponsors.

The evolution of restructuring technologies available under English law is equally notable. The restructuring plan in particular is emerging as a viable rescue tool to avoid insolvency and as a credible alternative to overseas restructuring procedures such as US Chapter 11 bankruptcy. The restructuring plan's ability to cram down non-consenting creditor classes means that there is now increased flexibility to modify capital structures in a manner that was not available under the scheme of arrangement. Each new case is introducing new and innovative features to the process meaning that England will remain a key destination for domestic as well as international debtors to restructure their indebtedness going forward.

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GENERAL FRAMEWORK

Jurisdictional pros and cons

What are the primary advantages and disadvantages in your jurisdiction of incurring indebtedness in the form of bank loans versus debt securities?

Setting aside fact- and market-specific considerations that might make credit facilities or debt securities more or less desirable to an issuer seeking to incur debt, credit facilities and the (issuance thereof) are not subject to federal and state securities regulations. Debt securities are subject to, among other laws, the US Securities Act of 1933 and the rules and regulations promulgated thereunder and blue-sky laws, which regulate the issuance and sale of securities at the state level. As a result, issuing debt securities requires significant time and effort analysing pertinent securities laws considerations, even where an exemption from such regulations applies, and working through required disclosure and timelines. By contrast, loans under credit facilities are more like creatures of contract. Credit facilities are not considered securities and, as such, are not subject to similar regulations and standards.

Law stated - 2 May 2024

Market snapshot

How do borrowers approach the different options of debt products and sources available to them, including debt securities? With respect to bank loans, how is the debt market split between direct lenders and private credit funds on the one hand, and banks and institutional investors on the other?

The type of debt a borrower chooses to incur depends on a variety of factors, from market conditions to the particular purposes for which the debt will be used, and even the business relationships that such borrower has with potential financing sources.

Historically, less creditworthy borrowers often turned to direct lenders because traditional debt capital markets were unavailable to them. Stronger, more creditworthy borrowers enjoyed broader financing options, including the ability to incur debt under both broadly syndicated loans and high yield notes. As a result, direct lender deals were typically concentrated in the middle market and below, with broadly syndicated deals dominating the upper middle to large-cap markets. These lines have become blurred, however, with direct lenders participating in increasingly larger value transactions traditionally provided by syndicated market players. A key contributing factor to that change has been the shifting composition of the debt capital markets investor base. Traditionally, most debt capital markets participants were institutional investors, such as pension funds and insurance companies. In recent years, however, direct lenders, alternative lenders, asset managers have shown tremendous appetite for loan deals.

In terms of syndicated loans, senior secured credit facilities typically include a term loan (sometimes multiple tranches of term loans) and a revolving credit facility. Such term loan and revolving credit facilities are typically documented under the same document and rank pari passu vis-à-vis one another at the top of a borrower's capital structure. In some

instances, the revolving credit facility has super priority and thus ranks senior in right of payment to the term loan.

Direct lender deals often take the form of a senior secured stretch senior or unitranche facility (with a term loan and revolver, such revolver often provided by a regulated bank). Super senior revolving facilities are more common in the direct lending world than in the syndicated market, and some deals even include super senior term loan tranches.

Delayed draw term loan facilities are also commonly included in both broadly syndicated and direct-lender deals, and generally have the same terms as the main unitranche facility, except in respect of the applicable availability period, optional currencies and permitted use of proceeds.

Finally, debt securities in the form of high yield notes are typically either senior secured notes (ranking pari passu in right of payment and security with senior secured term or revolving loan facilities) or senior unsecured notes, issued at a structurally subordinated level, and supported by subordinated guarantees.

Traditionally, direct lender deals were typically clubbed (consisting of a small number of lenders, instead of a broad, potentially ever-shifting syndicate). The limited number of counterparties in such clubbed, direct deals was an attractive feature to borrowers, although clubs have been expanding beyond a handful of players, particularly in larger (US$1 billion plus) unitranche facilities.

Pricing is a key distinguishing factor between syndicated loan deals, direct lender deals and high yield issuances. Broadly, syndicated debt is usually cheaper (namely, has lower pricing margins and upfront fees) than direct lender debt, the pricing of which reflects the riskier nature of the investors' investment and larger leverage multiples of borrowers. That said, such general statement does not apply to pro rata or term loan A deals, where pricing and fees tend to be lower as a means to offset higher amortisation payments. Direct lender deals may also feature the ability to PIK toggle, subject to negotiated conditions such as limits on the number of permitted uses thereof and minimum interest cash pay requirements. For the most part, both syndicated and direct lender deals include floating pricing mechanics. By contrast, high yield notes usually have fixed pricing. Original issue discount is typically lower in initial high yield note issuances as compared to syndicated and direct lender debt. Though less common, PIK notes also exist, sometimes as part of the capital structure of companies in highly regulated industries.

Law stated - 2 May 2024

Forms

What are the most common forms of loan facilities? Discuss any other types of facilities commonly made available to the debtor in addition to, or as part of, the loan facilities.

Term loan and revolving credit facilities are the predominant types of loan facilities in the United States.

Term loan facilities involve a single borrowing of a loan that remains outstanding for a period of time during which it accrues interest and is gradually repaid, via amortisation, typically on a quarterly basis, followed by a large, bullet payment at maturity. Amounts borrowed

and repaid under a term loan facility cannot be reborrowed. Depending on the size of the amortisation and bullet payments, term loans are classified as either term A loans (which have substantial amortisation payments) or term B loans (which have smaller amortisation payments, usually 1 per cent per year, and a bullet payment at maturity). Although term B loans are popular (among other reasons, because they typically come with higher pricing), term A loans have seen a resurgence over the past few years in light of interest rate hikes and a slowdown in the broadly syndicated loan market.

Delayed-draw term loans (DDTLs) are another popular type of term loan – DDTLs involve the establishment of commitments in respect of a term loan facility that may be drawn upon at a later time. Initial term loans are typically used to finance a particular purpose, such as in connection with acquisition or leveraged buyout, and related costs and expenses. Historically, DDTLs were limited to use for acquisitions under letter of intent or otherwise in an issuer's pipeline, but today, may be used for a broader list of enumerated purposes, including the financing of any permitted acquisition or similar permitted investment.

Revolving credit facilities are loan commitments able to be drawn from time to time; importantly, amounts borrowed under a revolving credit facility can be repaid and reborrowed. A helpful, although imperfect, way to conceptualise revolving credit facilities is to think of them as credit cards – there is a set maximum amount (like a credit limit) that may be borrowed and so long as that maximum amount is not exceeded, a debtor is generally free to borrow, repay and reborrow as needed for so long as the credit card is outstanding. No amortisation applies to revolving credit loans, which are due, to the extent outstanding, when the revolving credit facility matures. Revolving credit facilities may be used for a broader set of purposes than term loan facilities, including working capital and general corporate purposes. Many revolving credit facilities include sub-facilities (eg, subsets of the aggregate revolving loan commitment) that may, but are not required to be, used for same-day borrowings and letters of credit. Finally, there are two main types of revolving credit facilities – cash flow revolving credit facilities, under which the revolving loan commitment is based on (and secured by) the loan parties' cash flow and is fixed at the maximum commitment amount; and asset-based revolving credit facilities (ABLs), under which the amount available to be borrowed is the lesser of, at a high level:

Law stated - 2 May 2024

Investors

Describe the types of investors that typically participate in loan financings and the types of investors that participate in various other types of debt products.

The universe of investors in loan financings is broad. We must distinguish between primary issuance and syndication and secondary issuances and trading. The most meaningful difference in today's debt capital markets is between traditional banks and lenders and alternative or direct lenders, notably in primary issuance. Traditional lenders include large investment and commercial banks and similar financial institutions. Traditional syndicated loans were historically distributed to institutional investors such as pension funds and insurance companies, but that universe has expanded to include collateralised loan obligations, asset managers, and other alternative lenders. By contrast, direct lenders historically were non-regulated credit funds and asset managers. These lenders invested

usually using their own balance sheet funds versus syndicating loans to de-risk. The scope of alternative and direct lenders has evolved, and now includes the lending arms of private equity firms and hedge funds, in addition to direct lending by pension funds and insurance companies (who have moved beyond simply participating in syndicated deals). Traditional lenders historically dominated the syndicated loan markets, especially from the upper-middle market upwards. Direct lenders were traditionally confined to the lower market to the middle of the middle market. However, this dichotomy has shifted in recent years, with more direct lenders providing financing for large, upmarket deals. Market volatility generally may benefit direct lenders, as borrowers tend to turn to them when traditional lenders' ability to provide capital becomes limited or conditioned.

Law stated - 2 May 2024

Investors

How are the terms of a loan facility affected by the type of investors participating in such facility?

The investors acting as lenders under a loan facility can have a dramatic effect on its terms. Traditional lenders are larger institutions with less tolerance for risk, resulting in the syndication of a large portion (if not all) of their initial commitments under a loan facility. The market appetite for such de-risking and participation leads to riskier and more borrower-friendly terms – think bond-style credit agreements, especially in larger sponsored deals (other than investment-grade deals), with more permissive covenants and permissions (including the ability to designate and redesignate unrestricted subsidiaries, broader exclusions of assets from collateral, looser financial reporting requirements, less stringent mandatory prepayment and call protection provisions and broader EBITDA (earnings before interest, taxes,

depreciation, amortisation, addbacks and adjustments) formulations). By contrast, direct lenders typically do not syndicate, and tend to hold a larger portion of their commitments throughout the life of a facility. As a result, direct lenders maintain a strategic focus on tighter documentation terms, often aimed at safeguarding the value of collateral and ensuring collateral remains an asset of a loan party, or, restricted subsidiary, group of entities. The heightened focus on lender protective anti-liability management provisions in loan agreements (such as J Crew provisions limiting the ownership and transfers of material IP and other material assets, Chewy provisions restricting the ability to release certain guarantors and Envision provisions limiting the ability to make transfers of value to unrestricted subsidiaries (or, in some cases, non-loan parties) to a specifically earmarked negative covenant basket) was driven in part by direct lenders (although it has made its way into the syndicated, larger-cap arena).

Law stated - 2 May 2024

Bridge facilities

Are loan facilities used as 'bridges' to permanent debt security financings? How do the structure and terms of bridge facilities deviate from those of a typical loan facility?

Bridge facilities may be used, particularly in the context of acquisition financings. Bridge financings take the form of short-term loans, usually 364 days, if a bidder is unable to obtain permanent financing arrangements (usually high yield notes) prior to the closing of a specified transaction. Bridge facilities bear many similarities to regular-way term loans, subject to certain differences including, most crucially, in respect of term – bridge facilities are outstanding for a shorter period or time, after which they either become due or harden into more permanent, longer-term financing arrangements.

Law stated - 2 May 2024

Role of agents and trustees

What role do agents or trustees play in administering loan facilities with multiple investors?

Agents and trustees play a key role in administering financing arrangements with multiple investors. Loan facilities with more than one lender typically involve the designation of an administrative agent (and, if secured, a collateral agent). Typically, the lender leading the syndication efforts and (or) holding the largest commitments at closing acts as agent, although third-party agents for hire are often employed in direct lender deals or in deals where the lead lender is not willing to serve in an agency function. Administrative agents help administer loan facilities throughout their term, coordinating borrowing requests and processing assignments, distributing proceeds of prepayments, receiving notices and financial reporting packages, etc. Trustees play a similar function in respect of high yield bonds. Collateral agents accept the grant of security and collateral on behalf of all lenders, as secured parties and hold possessory collateral (including certificated equity interests). Collateral agents are authorised and entitled to exercise remedies in a downturn scenario. Agents are typically paid an annual administration fee and are entitled to reimbursement by the lenders for losses suffered in the performance of their duties. Notably, financing documentation typically expressly provide that agents and trustees, as applicable, are not fiduciaries of the lenders or other investors, and otherwise, contain exculpatory provisions in favour of the agents.

Law stated - 2 May 2024

Role of lenders

Describe the primary roles of, and typical fees charged by, the financial institutions that arrange and syndicate bank loan facilities, as well as lenders that participate in the private credit market.

The roles of, and types of fees charged by, the arrangers in larger, syndicated deals and smaller, direct lender deals (including club deals) are largely similar. These include:

- lead arranger or lead left: the lender primarily responsible for arranging and marketing a credit facility or high yield transaction;
- active book runners, arrangers or on the right: other lenders with an active role in arranging the debt transaction in cooperation with the lead left. Such lenders

are often granted titles such as joint lead arrangers, lead arrangers or other titles like syndication agent or documentation agent. In some cases, regardless of title, bookrunners and other agents may play little to no active role in arrangement and syndication;

- syndicate: the full group of lenders agreeing to purchase or that are allocated a portion of the debt on or shortly after closing (as part of primary syndication). The syndicate generally does not take part in leading or structuring the transaction; and
- participating lender: a purchaser of a participating interest in a lender's commitment. The lender remains the record holder of the loan, with the participant owning the rights to the amount purchased.

Arrangers are compensated by an arrangement fee, based on a percentage of the total commitments at either closing or at the time when commitments are provided (if in advance of closing and funding). Arrangement fees, including amount and parties entitled to the same, vary on a deal-to-deal basis and are negotiated between borrowers and lenders.

Law stated - 2 May 2024

Governing law

1.8.1. In cross-border transactions or secured transactions involving guarantees or collateral from entities organised in multiple jurisdictions, which jurisdiction's laws govern the loan and intercreditor documentation?

This depends on whether the jurisdictions in question are in or outside the United States and in some instances, its territories.

In a secured credit facility with a credit agreement governed by US law (eg, New York law), loan parties organised under different US jurisdictions (eg, Delaware, California and Texas), and assets located in different US jurisdictions (in our example, New York, California and Texas), the collateral and guaranty documents will usually be governed by the same law as the principal loan document (here, New York).

The situation is more complex when non-US loan parties exist and (or) when assets constituting collateral are located outside the United States. The analysis is fact-specific and may require consultation with local counsel. Entry into local law-governed security and guarantee agreements governed by local law may be required to ensure the lenders' security interest is effective and enforceable. The nature and scope of non-US guarantees and security is negotiated and often boils down to pragmatic considerations. While certain jurisdictions (such as Canada, most Caribbean countries, and many European countries) make the taking and enforceability of security relatively simple and cost-effective, other jurisdictions may present obstacles (often in the form of regulatory requirements) burdensome or difficult to overcome that lenders and borrowers agree not to spend money and effort pursuing local security.

Law stated - 2 May 2024

REGULATION

Capital and liquidity requirements

Describe how capital and liquidity requirements impact the structure of loan facilities, including the availability of related facilities and the differing impact of such requirements on different types of investors.

Capital and liquidity requirements differ among regulated banks, direct lenders, and institutional investors and may impact the ability, and willingness, of different investors to provide certain loan structures. Regulated banks are typically subject to capital and liquidity rules, related reporting requirements (and testing thereof), and inspections by federal or state regulators. As a result, regulated banks may be more conservative about credit extended and resulting leverage, but more willing, and able, to provide products like revolving lines of credit, swingline facilities, letters of credit and banker's acceptances. Historically, regional and midsize banks were not subject to all federal capital and liquidity requirements. However, following the collapse of Silicon Valley Bank and First Republic Bank in 2023, the Federal Reserve, the Office of the Comptroller of Currency (OCC), and the Federal Deposit Insurance Corporation jointly published a Notice of Proposed Rulemaking, referred to as Basel III Endgame, which would enhance and expand regulatory capital requirements, including making them applicable to regional and midsize banks.

Direct lenders, whether or not structured as private credit funds, are generally not subject to the same capital and liquidity requirements as regulated banks. For private credit lenders, the internal funding features (eg, subscription, capital call, net asset value or similar facilities) and requirements of constitutive documents often impact their ability to provide certain credit facility structures. Direct lenders are also less willing (or able) to provide revolving credit facilities and related products and often partner with banks or other third parties to provide the same. However, as private credit's footprint has expanded, more private credit lenders provide revolving credit facilities, even asset-based loans, and similar offerings. Additionally, direct lenders that are also pension funds or insurance companies or affiliates, there may be certain other legal or regulatory concerns due to the highly regulated nature of these industries.

Traditional institutional investors (as described above) almost exclusively invest in term loans. Due to, among other things, operational requirements and restrictions, and investment theses, institutional investors are typically not set up to fund multiple, unexpected draw requests. Accordingly, such investors often are unable to provide or participate in revolving credit facilities, delayed-draw term loans, letter of credit requests or swingline facilities.

Law stated - 2 May 2024

Disclosure requirements

For public company debtors, are there disclosure requirements applicable to loan facilities?

Public company debtors regulated by the Securities and Exchange Commission or otherwise elect to publicly report are subject to disclosure requirements applicable to loan facilities, such as the filing of a Form 8-K (Entry into a Material Definitive Agreement). This 8-K announces the entering into of the loan agreement or other material document and attaches

a copy of the same. With respect to disclosure, most public company debtors file only final credit agreements (without any schedules or exhibits) and commitment letters for bridge facilities. Virtually all other loan documents remain private, with some terms of publicly filed debt documents redacted (if the redacted terms are subject to disclosure restrictions).

Law stated - 2 May 2024

Use of loan proceeds

How is the use of loan proceeds by the debtor regulated? What liability could investors be exposed to if the debtor uses the proceeds contrary to regulations? Can investors mitigate their liability?

Use of loan proceeds by the debtor is generally subject to several sets of regulations addressing anti-bribery, anti-corruption, anti-money laundering, anti-terrorism, and similar matters. The USA Patriot Act, part of the Bank Secrecy Act, imposes minimum standards on lenders to verify their customers' identities, a process referred to as know-your-customer and intended to combat the foregoing. Compliance is overseen by the Financial Crimes Enforcement Network (FinCEN). FinCEN also requires that lenders comply with related customer due diligence regulations (CDD rules). The CDD rules require lenders to obtain beneficial ownership information for borrowers to determine whether funded proceeds could be sent to a prohibited party or otherwise used in a proscribed manner. Banks may require additional information to the extent required by bank regulators, and direct lenders may require information specific to their disclosure obligations with the Securities and Exchange Commission and (or) governing fund documentation. Additionally, the Office of Foreign Assets Control of the US Department of the Treasury (OFAC) administers federal regulations prohibiting any US person or entity transacting with (including by extending credit), directly or indirectly, any person or country or region subject to economic sanctions.

Law stated - 2 May 2024

Cross-border lending

Are there regulations that limit an investor's ability to extend credit to debtors organised or operating in particular jurisdictions? What liability are investors exposed to if they lend to such debtors? Can the investors mitigate their liability?

OFAC's regulations prohibit investors from engaging in transactions with certain specially designated nationals (SDNs) and blocked persons. SDNs include individuals or entities owned, controlled by, or acting on behalf of, the governments of target countries or jurisdictions, and with certain target countries or jurisdictions subject of comprehensive economic sanctions (OFAC target jurisdictions). As of April 29, 2024, OFAC target jurisdictions include Cuba, Iran, North Korea, Syria, and the Crimea, Donetsk and Luhansk regions of Ukraine. These regulations impose a strict liability regime wherein penalties for violations may be assessed regardless of whether any violation is intentional, direct, or in bad faith (and with greater penalties for any deliberate and egregious violations). Although OFAC has some enforcement discretion, financing sources may face hefty fines and other penalties for any noncompliance. To mitigate liability, investors conduct due diligence of

credit parties' business and operations, as well as their equity and capital structure. Loan documentation will typically include representations and warranties confirming compliance by the credit parties with all applicable anti-money laundering and sanctions laws and regulations as of closing and (or) funding, as applicable, as well as affirmative covenants that require compliance by the credit parties at all times after closing and funding.

Law stated - 2 May 2024

Debtors' leverage profile

Are there limitations on an investors' ability to extend credit to debtors based on the debtors' leverage profile?

In 2013, the OCC introduced Leveraged Lending Guidance (LLG) for regulated banks, which are still applicable today. The LLG capped pro forma leverage for leveraged finance transactions at six times earnings and required that a debtor would be able to pay down at least 50 per cent of its closing date borrowings within five to seven years. Federal banking agencies monitor compliance therewith biannually via the interagency Shared National Credit Program, which reviews compliance for any loans exceeding US$100 million made by three or more lenders.

Law stated - 2 May 2024

Interest rates

Do regulations limit the rate of interest that can be charged on loans?

State usury laws limit the amount of interest charged for certain subject loans. Failure to comply with the usury laws could result in both civil and criminal penalties for the lending institution. Usury laws vary by state, but generally restrict the maximum rate of interest for loans to individuals and businesses, which may vary, or not apply, based on the loan quantum. The usury laws typically do not apply to commercial loans. For example, under New York state law (which is a common governing law choice), the maximum interest rate for entities (25 per cent) only applies to loans less than US$2.5 million.

Law stated - 2 May 2024

Currency restrictions

What limitations are there on investors funding loans in a currency other than the local currency?

Outside of OFAC regulations prohibiting lending to certain proscribed persons or jurisdictions, there are generally no statutory or regulatory restrictions limiting investors' ability to fund in currencies other than US dollars. However, certain state and local (including foreign countries) lending licensing and (or) individual investor's operational requirements may restrict individual investors from funding, or receiving payments in, certain non-local currencies. As a result, most US credit facilities with multi-currency permissions include a

pre-agreed list of available currencies for borrowings and corresponding payments that may only be updated with the consent of all lenders required to fund in any additional currency.

Law stated - 2 May 2024

Other regulations

Describe any other regulatory requirements that have an impact on the structuring or the availability of loan facilities.

QFC Stay Rules

Qualified Financial Contracts (QFC) Stay Rules require globally significant banking institutions party to QFCs, including guarantees of borrower obligations under certain swaps, to preserve certain default rights with respect thereto. Subject institutions may comply by incorporating standard provisions acknowledging these rules and preserving such default rights into any affected loan documentation.

The Investment Company Act of 1940

The Investment Company Act of 1940 (the 1940 Act) prohibits entities that constitute investment companies under the 1940 Act from incurring loans and pledging assets unless such entity registers under the 1940 Act. Making a loan to an investment company without the required registration may render the debt documentation unenforceable.

Anti-tying regulations

Anti-tying regulations restrict US banks providing a loan to a US person from tying the availability or pricing of any loan to having the applicable borrower purchase a non-bank product (eg, investment advisory services) from the bank or its affiliates.

Law stated - 2 May 2024

SECURITY INTERESTS AND GUARANTEES

Collateral and guarantee support

Which entities in the organisational structure typically provide collateral and guarantee support for loan financings? Are there certain types of entity that typically do not provide, or are restricted in their ability to provide, collateral and guarantee support for such financings?

Although fact-specific considerations might necessitate a different structure, the predominant credit group structure in both syndicated and direct lending secured financings consists of one or more US-organised borrowers, whose obligations are supported by:

- its direct parent entity; and

- its direct and indirect US-organised subsidiaries, subject to certain customary and negotiated exceptions.

Borrowers and guarantors are commonly referred to, collectively, as loan parties or credit parties, interchangeably. In the syndicated loan market, loan parties provide collateral over substantially all their assets, including equity interests, subject to customary and negotiated carve-outs. Non-US and certain immaterial subsidiaries are typically excluded from the guarantee obligation and may even be unrestricted subsidiaries (eg, specially-designated subsidiaries beyond the scope of the financing and, as such, not required to comply with the various restrictions imposed by credit documents). Additionally, some perfection steps (such as, for instance, obtaining control agreements over deposit and securities accounts or mortgages over owned real property below an agreed-upon fair market value threshold) are typically not required in broadly syndicated deals, unless otherwise agreed.

Direct lending deals usually have similar guarantor and collateral packages, though it can be said direct lenders have historically insisted on tighter collateral and guarantee requirements. For instance, some direct lenders are more focused on obtaining guarantees from non-US subsidiaries and security interests over non-US assets. Direct lenders may be, as a general matter, more insistent on fulsome perfection actions, such as the establishment of foreign perfection, control agreements and, increasingly less commonly, landlord waivers and other collateral access agreements.

Finally, senior secured notes are generally supported by similar collateral and guarantee packages as syndicated loan deals, though note security may differ if or as the notes are issued at a non-credit party entity or level. Certain secured note deals involving the establishment of an escrow account for a specified purpose might also involve the creation of a security interest over such escrow account, until the applicable escrowed funds are released.

Law stated - 2 May 2024

Collateral and guarantee support

What types of obligations typically share with the loan obligations in the collateral and guarantee support? If so, are all such obligations equally and ratably covered by the collateral and guarantee support?

Collateral and guarantees support all obligations under a credit facility – this includes not only principal and interest, but also applicable fees, interest rate-related breakage costs, and indemnification and reimbursement obligations, including with respect to legal and other expenses. In many cases, secured and guaranteed obligations also cover other services (such as swap, hedging and other cash management obligations) provided by the lenders under a facility. As a general matter, subject to payment priorities established in the deal documentation, all secured and guaranteed obligations receive the same level of collateral and guarantee support.

Law stated - 2 May 2024

Commonly pledged assets

Which categories of assets are commonly pledged to secure loan financings? Describe any categories of asset that are typically not thus pledged, or are restricted from being so.

Most secured loan financings are all-asset deals – obligations are secured by substantially all assets of the loan parties, subject to certain customary exceptions and materiality thresholds. Assets typically included in collateral packages consist of equity interests, accounts receivable, intellectual property, other general intangibles, cash, cash equivalents, deposit accounts, securities accounts, commodities accounts, commercial tort claims, letter of credit rights, goods, documents, equipment, inventory, ownership interests in real property, fixtures and others. Assets excluded from collateral vary from deal to deal, but examples of items typically excluded are real property interests with a fair market value below a materiality threshold, assets the pledging of which is prohibited by law or existing contract, or would lead to adverse tax consequences, and leasehold interests.

Law stated - 2 May 2024

Creating and perfecting a security interest

Describe the method of creating and perfecting a security interest on the main categories of assets. What are the consequences of failing to perfect a security interest?

Article 9 of the Uniform Commercial Code (UCC), a set of guidelines adopted by all 50 states and the District of Columbia, provides the principal legal framework for the creation and perfection of security interests in the United States.

Under the UCC, for a security interest to 'attach' to certain collateral (eg, to be properly created), the security agreement (or other applicable collateral document) must properly describe the relevant collateral grant using the proper terms (as defined in the UCC – such terms include many of the items described further above, such as cash and cash equivalents, deposit accounts, inventory, general intangibles, etc). Creation and attachment is only one of two necessary steps, however. The second, crucial, step is perfection – how a security interest is perfected depends on the asset at hand. The most common way to perfect is the filing of a UCC-1 financing statement with the secretary of state or other applicable filing office of the jurisdiction of organisation of the applicable debtor – a UCC-1 filing suffices to perfect a security interest in most assets. In other cases, perfection is only achieved by a specific type of filing (eg, a copyright security agreement filed with the US copyright office is required to perfect a security interest in copyrights) or by control – control, in turn, means different things depending on the type of asset in question. Control over possessory collateral (such as certificated equity interests) is only attained by physical possession of such collateral in addition to the possession of an appropriate transfer instrument (such as a stock power) endorsed in blank. Control over cash in a deposit account requires the establishment of a three-party deposit account control agreement with the depositary bank holding such account. A security interest over real property can only be perfected through the filing of a mortgage.

An unperfected security interest, while not altogether invalid, puts a secured party in a weakened position relative to a properly perfected, competing security interest. Between

a perfected secured lender and an unperfected secured lender, the perfected secured lender has priority. This is particularly important in a bankruptcy scenario, whereunder an unperfected secured party will be in the same position as an unsecured creditor.

Law stated - 2 May 2024

Future-acquired assets

Can security interests extend to future-acquired assets? Can security interests secure future-incurred obligations?

Yes. Secured deals in the United States typically involve a blanket security interest over all or substantially all current and future assets of a debtor. The UCC permits the granting and perfection of such a security interest, with a few exceptions (including in respect of security interests in commercial tort claims and certain consumer goods).

Law stated - 2 May 2024

Maintenance

Describe any maintenance requirements to avoid the automatic termination or expiration of security interests.

Most UCC-1 financing statements lapse within five years from filing, unless continued. Continuation is achieved by the filing of a UCC-3 continuation statement – a simple, but critical step. Many secured loan and note financings have a tenor longer than five years, which requires secured parties to ensure timely continuations are filed. Other important developments necessitating the filing of a UCC-3 amendment (which modifies an original UCC-1 filing) include changes in debtor's legal name, jurisdiction of organisation or mailing address. Loan documents typically require debtors to notify secured parties of such changes and accordingly, enable secured parties to make requisite filings and take other steps, as needed to preserve notice and perfection.

Law stated - 2 May 2024

Release

What are typical steps to release security interests on assets? Is such a release automatic under any circumstances?

Simply put, a security interest is released by the proper termination of the document or instrument that created it. The most common release scenario is in the context of a payoff (namely, a credit facility is being paid off (usually in the context of an acquisition or other refinancing)). A proper release in the context of a payoff includes a payoff letter or similar document expressly providing that, upon the satisfaction of certain conditions (including, most importantly, the receipt of a specified payoff amount), the credit facility is terminated, and all relevant security interests are also terminated and released. Payoff letters are also typically accompanied by UCC-3 termination statement filings (which terminate existing UCC-1 financing statements), the filing of releases in respect of any previously filed IP

security agreements, terminations of any control agreements, etc. Lenders and borrowers must tailor payoff and release documents to existing credit and security documents and filings, to ensure all requisite release steps are taken (eg, UCC-3 termination statements must be drafted following a thorough review of appropriately-run lien searches in all applicable jurisdictions). In the event further steps are needed to obtain a full release (eg, the unfortunate, but not unheard of, example of stray financing statements or IP filings that were inadvertently not terminated), payoff documents often include further assurances language providing that the parties will take such further steps as necessary to obtain a release.

Law stated - 2 May 2024

Non-fulfilment of guarantee obligations

What defences does a guarantor have against claims for non-fulfilment of guarantee obligations? Can such defences be waived?

Guaranty documents typically include an express waiver of any applicable defences that a guarantor may have against having to fulfil its guarantee obligations. Absent such a waiver, various defences may apply, including a claim the relevant debt has been materially altered, the applicability of statutes of limitations, and a claim that an upstream or sidestream guaranty should be avoided as a fraudulent conveyance because the value received by the guarantor from the credit facility is not reasonably equivalent to the value of the guaranty. It is particularly important to creditors that a guarantee be a guarantee of payment, and not only a guarantee of collection. This will enable such creditor to go after a guarantor for payment of a borrower's unpaid obligations, without having to first exhaust all remedies it may have against the borrower.

Law stated - 2 May 2024

Parallel debt requirements

Describe any parallel debt or similar requirements applicable in a secured loan financing where an agent acts for multiple investors.

No parallel debt or similar provisions are required under US law in respect of US collateral or US guarantors. US-law-governed credit facilities might include parallel debt provisions if non-US loan parties and (or) security interests exist, and such provisions are required or desirable under applicable local law.

Law stated - 2 May 2024

Enforcement

What are the most common methods of enforcing security interests? What are typical limitations on enforcement?

Following an event of default in respect of obligations, most definitive agreements permit creditors to exercise remedies in respect of security interests in collateral – this may take many forms, including declaring all loans and related amounts to be immediately due and

payable, retaining possession of collateral, selling collateral, directly pursuing collection efforts against persons owing money to a debtor, and even exercising voting rights under pledged equity interests (eg, taking the keys) of a debtor. The most potent limitation on enforcement is the filing of a bankruptcy petition in respect of a debtor – for the most part, this prompts the imposition of an automatic stay, which prevents the creditors from directly exercising remedies against such debtor.

Law stated - 2 May 2024

Fraudulent conveyance and similar doctrines

Describe the impact of fraudulent conveyance, financial assistance, thin capitalisation, corporate benefit and similar doctrines on the structure of loan financings.

Fraudulent conveyance is defined by the US bankruptcy code (11 USC section 548(a)(1)(A)-(B)) as the avoidance or reversal of a transfer of a debtor's interest in property, or of any obligation incurred by the debtor, that was made or incurred on or within two years before the date of filing a petition in bankruptcy. A fraudulent conveyance has taken place if, voluntarily or involuntarily:

- the transfer or incurrence was made with the actual intent to hinder, delay or defraud creditors; or
- if a debtor received less than reasonably equivalent value in exchange for the transfer and:
- was insolvent on the date the transfer was made or the obligation was incurred or became insolvent as a result;
- was engaged in business or a transaction (or was about to engage in business or a transaction) for which any property remaining with the debtor was an unreasonably small capital;
- intended to incur, or believed that the debtor would incur, debts that would be beyond the debtor's ability to pay as such debts matured; or
- made such transfer to, or for the benefit of, an insider, or incurred such obligation to or for the benefit of an insider, under an employment contract outside the ordinary course of business.

In addition, each US state has a fraudulent conveyance law and framework applicable in and outside of bankruptcy; most states have adopted the Uniform Fraudulent Transfer Act as the applicable state law. Loan documents tend to address this risk by including specific waivers and representations by debtors (most importantly, a representation as to solvency). Financial assistance, thin capitalisation, and corporate benefit doctrines do not have analogous constructs under US law.

Law stated - 2 May 2024

INTERCREDITOR MATTERS

Payment and lien subordination arrangements

What types of payment or lien subordination arrangements are common where the debtor has obligations owing to more than one class of creditors?

The most common types of such payment or lien subordination arrangements are:

- intercreditor agreements;
- subordination agreements; and
- agreements among lenders (AALs).

Intercreditor agreements set forth lien and payment priority between one or more class of creditors with respect to the related obligations and collateral. Intercreditor agreements are generally considered enforceable in bankruptcy, with each creditor group of creditors being separately classified. Intercreditor agreements may include first lien or second lien (or other multiple lien) arrangements, where the second lien is subordinated in respect of lien priority and as a result, collateral proceeds, to the first lien (and so on for all further subordinated lien creditors) or split collateral arrangements, where one group of creditors (eg, asset-based lenders) has priority with respect to certain collateral (receivables, cash, etc) and another group has priority (in this example, term lenders) with respect to the remaining collateral (like equity interests), with each group having a second lien on the other creditors' priority collateral. Subordination agreements are a specific category of intercreditor agreements wherein one creditor's rights are subordinate to another creditor's with respect to payment and, if one exists, lien priority (eg, senior or mezzanine) and are typically enforceable in insolvency proceedings. AALs are used in unitranche financings where all lenders are part of the same credit facility tranche, sharing in one lien, but have separately negotiated and documented agreements for first out (FO) lenders (typically paid first with respect interest, mandatory prepayments and otherwise) and last out (LO) lenders, as to payment priority, rights, and remedies. AALs may be enforceable in bankruptcy as subordination agreements; however, the lenders risk being classified as a single class without the bankruptcy court enforcing the separate rights of the respective lender groups that were negotiated in the AAL (courts have not ruled definitively on the treatment of AALs in bankruptcy).

Law stated - 2 May 2024

Creditor groups

What creditor groups are typically included as parties to intercreditor agreements? Are all creditor groups treated the same under the intercreditor agreement?

Intercreditor agreements, subordination agreements, and AALs are typically executed by a representative on behalf of each set of creditors (eg, the first lien agent, the revolving agent, etc) or the creditor itself (if such creditor is the sole creditor). Borrowers are typically not party to intercreditor arrangements but may sign an acknowledgment. When unitranche financings first became popular, AALs were separate confidential arrangements and generally not disclosed to the borrower. However, following potential enforceability concerns,

including in bankruptcy, some creditors now actively seek borrower acknowledgement to AALs and (or) set out principal AAL terms (eg, the priority waterfall, waterfall trigger events, etc) in the body of the related credit agreement. Voting rights in intercreditor arrangements are typically negotiated based on the priority of the various creditors with voting is governed by the credit agreement until certain triggering events occur (eg, a payment default, insolvency event or otherwise).

Law stated - 2 May 2024

Rights of junior creditors

Are junior creditors typically stayed from enforcing remedies until senior creditors have been repaid? What enforcement rights do junior creditors have prior to the repayment of senior debt?

When an inter-creditor arrangement exists, junior creditors may be stayed, usually per a specified standstill period, from enforcing remedies until senior creditors have been repaid. The length and nature of the standstill varies based on the negotiated or agreed intercreditor arrangement; market standstills include:

- first lien or second lien, 90 to 180 days standstill for second lien, with most shaking out between 120 to 180 days;
- split collateral, typically none (or may be permanent if one creditor holds a comparatively outsized portion of the commitments);
- unitranche, often five to 45 days for the FO lenders and 90 to 120 days for the LO lenders (subject to a buyout right for the LO lenders, and subject to negotiation depending on the relative sizes of the FO and LO commitments); and
- senior secured or unsecured junior debt, likely a permanent standstill for the subordinated creditor.

At a minimum, junior creditors typically have unsecured creditor rights, and, following the expiration of the senior creditors' standstill, the ability to exercise remedies in accordance with the relevant inter-creditor arrangement. In AALs, the LO lenders generally have a buyout right, whereupon certain triggering events, the LO lenders may purchase the FO commitments and along with that purchase, corresponding additional negotiated enforcement rights (eg, requiring consent of the majority LO lenders and the majority FO lenders prior to any exercise of remedies), particularly if the LO holds the bulk of the commitments.

Law stated - 2 May 2024

Rights of junior creditors

What rights do junior creditors have during a bankruptcy or insolvency proceeding involving the debtor?

Junior creditors typically have limited, negotiated rights during a bankruptcy or insolvency proceeding involving the debtor with respect to:

- providing debtor-in-possession (DIP) financing;
- certain asset sales (363 sales); and
- plan classification.

In first lien or second lien (1L/2L) arrangements, the 2L is generally deemed to have consented to any DIP financing provided by the 1L (subject to a dollar cap and certain conditions), any 363 sales approved by a majority of the 1L, and any plan under which the 1L and 2L are separately classified. For split collateral arrangements, the asset-based lenders and term lenders have consent rights with respect to any DIP financing, 363 sale and (or) plan that gives priority treatment to the other lenders' priority collateral. Unitranche financings and subordination agreements typically mirror 1L/2L arrangements, unless the subordinated creditor is unsecured, in which case, such matters may not be specifically addressed. In unitranche arrangements where the LO holds a larger portion of the commitments, the LO may have certain blocking rights and (or) the FO may expressly need to obtain the consent of the LO to approve any plan or to provide a debtor-in-possession financing. Otherwise, junior creditors may have limited veto power and only be able to object if any plan of reorganisation would adversely and disproportionately disadvantage their recovery.

Law stated - 2 May 2024

Pari passu creditors

How do the terms of the intercreditor arrangement change if creditor groups will be secured on a pari passu basis?

In unitranche financings, debt under the credit facility is separated into an FO tranche and an LO tranche, usually governed by an AAL. After certain triggering events have occurred, payments and proceeds of collateral are applied to the FO tranche prior to application to the LO tranche in a waterfall-dictating order of payment application. The AAL governs the rights and obligations of the FO lenders in relation to the LO lenders. There is no market standard or reference for AALs, as they are subject to negotiation and contract, and credit facility structure and relative tranche sizes may also impact the rights of the FO and LO tranches. In pari passu intercreditors, typically the first (in time) pari tranches governs (namely, controls exercise of remedies and enforcement) for the benefit of both pari tranches subject to both pari tranches sharing in the liens and collateral on an equal basis.

Law stated - 2 May 2024

LOAN DOCUMENT TERMS

Standard forms and documentation

What forms or standardised terms are commonly used to prepare the loan documentation?

There is no standard form of loan documentation, although most generally follow a similar structure, including separate sections documenting the commitments and borrowing procedures, representations and warranties, conditions precedent to closing

and subsequent credit extensions, affirmative covenants, negative covenants, events of default, amendments and waivers, assignments and participations, voting, and agency terms. Initial drafts of loan documents are usually based on agreed-upon precedents or a lender or sponsor's form (depending on the deal dynamics and the parties' relative negotiating power). The Loan Syndications and Trading Association (LSTA) also offers model forms, provisions and drafting suggestions for a wide array of financing documents (such as credit agreements, intercreditor documentation and ancillary loan documents). Though not definitive or dispositive, LSTA forms are helpful drafting references and are particularly influential in shaping important documentary provisions, such as interest rate sections (including benchmark replacement terms), regulatory provisions and assignment mechanics.

Law stated - 2 May 2024

Pricing and interest rate structures

What are the customary pricing or interest rate structures for loans? Do the pricing or interest rate structures change if the loan is denominated in a currency other than the domestic currency?

Floating rate structures are generally more common, though some facilities have fixed interest rates. Floating rate pricing is based on a benchmark interest rate (typically Term SOFR or Base Rate), sometimes subject to a credit spread adjustment and minimum threshold (or interest rate floor) plus an applicable margin (a spread over the benchmark interest rate that the lender charges). The applicable margin levels vary, depending on a debtor's credit profile, a facility's position in the capital structure (eg, senior or first lien facilities typically have lower applicable margin levels than subordinated facilities), etc. In better credits, and subject to negotiation, the applicable margin may decrease as the borrower's leverage decreases.

Credit facilities that permit borrowings in currencies other than US dollars typically bear interest at a different benchmark rate (eg, the benchmark rate for loans denominated in Pounds Sterling is typically SONIA, the benchmark rate for loans denominated in euros is EURIBOR, etc), plus an applicable margin.

Law stated - 2 May 2024

Pricing and interest rate structures

Does loan documentation in your jurisdiction incorporate any mechanisms to replace an established, floating benchmark rate in case such benchmark rate becomes, or is expected to become, unavailable?

Yes. Prior to Term SOFR, LIBOR was the predominant benchmark option, alongside the base rate, available to borrowers in the United States. Due to the gradual cessation of LIBOR, credit agreements were amended to both:

- designate a successor rate to LIBOR; and
-

establish a replacement framework if another benchmark became unavailable in the future.

Most credit agreements have adopted a benchmark replacement approach modelled after the relevant LSTA form language – with some providing for a future amendment to establish a successor rate and others hardwiring a prioritised waterfall of successor rates (eg, Daily Simple SOFR is often pre-selected as the designated successor if Term SOFR is discontinued).

Law stated - 2 May 2024

Other yield determinants

What other loan yield determinants are commonly used?

Loans are often established with upfront or new issuance fees that may take the form of original issue discount. Other fees might include the previously-mentioned arrangement fees, ticking fees in situations where a commitment period is particularly long, and, after a facility has been established, commitment fees based on unused portions of a revolving credit or delayed-draw term loans facility. The size of such fees differs on a deal-to-deal basis, depending on factors such as the size and creditworthiness of a debtor, the size and relative priority of a credit facility, and overall market conditions.

Additionally, as previously mentioned, benchmark rates are subject to floors, which typically range between zero and one per cent, and are sometimes lower in connection with revolving credit loans as opposed to term loans. Additionally, a credit spread adjustment might also apply (eg, in the case of Term SOFR loans, 10 basis points (bps) across the board or 10 bps, 15 bps or 25 bps depending on the applicable interest period).

Law stated - 2 May 2024

Yield protection provisions

Describe any yield protection provisions typically included in the loan documentation.

Separately from prepayment premium provisions, which may be highly negotiated, most credit agreements include customary cost and yield protection provisions. These are typically based on the applicable lenders' institutional requirements and forms, or the applicable precedent, and are not highly negotiated. Tax withholding and gross-up provisions are included, and may be negotiated.

Law stated - 2 May 2024

Accordion provisions and side-car financings

Do loan agreements typically allow additional debt that is secured on a pari passu basis with the senior secured loans?

Upmarket loan agreements typically allow additional pari passu secured debt as part of incremental facilities, and, depending on the deal structure and credit profile, also as sidecar facilities. Incremental facilities allow the borrower to add new debt tranches or increase existing commitments (the increase of existing commitments feature colloquially referred to as the accordion) subject to negotiated conditions, and, often without the consent of existing lenders (other than any existing lender providing any portion of the incremental financing). Smaller deals and deals up to the middle market may not include additional pari passu debt incurrence, or may so include up to only a small, capped amount. In some credit facilities, the borrower may be able to incur such pari secured debt as a separate facility or sidecar, usually subject to a first-lien leverage governor among other conditions. Both incremental facilities and sidecar financings may be incurred up to a capped amount and thereafter, in better credits, in an unlimited amount subject to a first liken leverage test, with incurrence subject to limitations on guarantors and collateral, default blockers, maturity limitations, and lender pricing and terms protections, which may vary based on the size of the credit facility and strength and size of the involved parties.

Law stated - 2 May 2024

Financial maintenance covenants

What types of financial maintenance covenants are commonly included in loan documentation, and how are such covenants calculated?

Financial maintenance covenants commonly included in loan documentation are leverage covenants (most prevalent), fixed charge covenants and liquidity covenants, and, less commonly, minimum earnings before interest, taxes, depreciation, amortisation, addbacks and adjustments (EBITDA) covenants and (or) maximum capital expenditure covenants. Covenant types vary based on the structure of credit facilities, with EBITDA-based leverage covenants being most common in cash-flow EBITDA-based deals, parallel covenants based on recurring revenue included in recurring revenue-based credit facilities and fixed charge coverage ratios appearing most frequently in asset-based credit facilities. Testing levels are usually set based on a cushion of 35 per cent to 50 per cent to the provided model for the transactions. The scope of included debt in leverage calculations varied based on market segment and is generally broader in middle market deals including debt for borrowed money, debt represented by notes or other instruments, capital leases and purchase money debt with large-cap deals potentially excluding capital leases and (or) earnouts. Cash netting is often permitted when calculating leverage, and may be capped in middle-market deals, particularly for corporate borrowers and borrowers backed by smaller private equity sponsors. Most credit facilities include an equity cure construct whereby financial covenant defaults (in some cases solely with respect to leverage-based covenants) may be cured by a capital contribution from the debtor's shareholders and (or), in larger deals, by subordinated debt owing to the Borrower's shareholders or parent entities. In middle-market deals, the equity cure may be required to prepay the outstanding term loans.

Most cash-flow credit facilities, particularly outside of the lower middle market, include springing financial covenants where testing of the financial covenant is only required subject to the occurrence of a triggering event (typically, drawing down the revolver in excess of an agreed level (often 35 per cent to 40 per cent of the revolving commitments)). In such covenant-lite structures, often only the revolving lenders have the benefit of the financial

covenant (namely, only they can call a default). Equity cures are generally permitted for springing financial covenants with the cure proceeds applied to either increase EBITDA or pay down the revolver below the testing threshold.

Law stated - 2 May 2024

Other negative covenants

Describe any other negative covenants restricting the operation of the debtor's business commonly included in the loan documentation.

Negative covenants are generally intended to protect the lenders' investment without unduly limiting the borrower's business objectives and conduct. Such negative covenants limit the borrower's ability to enter into material transactions outside the ordinary course of business, or other transactions that could be detrimental to the credit. These covenants will, subject to highly negotiated exceptions, set forth actions that the borrower is not allowed to take (or permit its subsidiaries, the other loan parties, or a subset of its restricted subsidiaries to take), and may also similarly restrict the borrower's parent company. Common negative covenants include limitations on indebtedness, liens, restricted payments (dividends or other upward distributions), restricted debt payments (with respect to junior or unsecured debt), investments, asset sales and dispositions, and mergers and acquisitions.

Law stated - 2 May 2024

Mandatory prepayment

What types of events typically trigger mandatory prepayment requirements? May the debtor reinvest asset sale or casualty event proceeds in its business in lieu of prepaying the loans? Describe other common exceptions to the mandatory prepayment requirements.

Mandatory prepayments are most often required in connection with asset sales, casualty or condemnation events (upon receipt of related insurance proceeds), incurrence of prohibited debt, and generation of any excess cash flow (ECF); the amount of generated cash remaining after the payment of essential operating expenses, capital expenses and certain dividends), and, less often, equity issuances and extraordinary receipts (large sum payments received outside the ordinary course). Revolving credit facilities, particularly asset-based credit facilities, may additionally require prepayments in connection with any over-advances of credit beyond the permitted maximum amount of the revolving commitments. Most credit facilities permit reinvestment of proceeds received in connection with asset sales and casualty events within an agreed time frame (in better credits, often 12 to 18 months, with an additional six to 12 months to reinvest thereafter for any such proceeds committed to be reinvested within the initial reinvestment period). Retained ECF may be used to increase transactional capacity under the negative covenants (via a builder basket construct, referred to as the available amount or cumulative credit). Otherwise, there are typically de minimis exclusionary thresholds for asset sale, casualty event and ECF mandatory prepayments (often set at a dollar amount equivalent to 10 per cent to 15 per cent of EBITDA), negotiated dollar-for-dollar deductions to the ECF prepayment for certain cash expenditures made

during the relevant measurement period, and exclusions for certain proceeds that would require repatriation and subject the loan parties to adverse tax consequences.

Law stated - 2 May 2024

Debtor's indemnification and expense reimbursement

Describe generally the debtor's indemnification and expense reimbursement obligations, referencing any common exceptions to these obligations.

Debtors typically indemnify the agent and lenders, together with certain of their related parties and affiliates, with respect to liabilities arising out of the loan documentation and related transactions. Expense reimbursement is often negotiated and may be limited to cover a single counsel for the agent and lenders, together with any required local or specialist counsels (and potentially an additional counsel in the case of any conflicts). Common exceptions include any events arising out of the agent's or lender's gross negligence, bad faith, or wilful misconduct, frequently only to the extent such attribution has been determined in a final judgment by a court of competent jurisdiction. Such indemnification and expense reimbursement obligations are typically expressly enumerated as part of the debtors' obligations under the credit facilities and are secured to the same extent as the loans and other obligations thereunder (although paid near to last in the waterfall).

Law stated - 2 May 2024

UPDATE AND TRENDS

Key developments

Are there any current developments or emerging trends that should be noted?

Pricing

Over the past several months, reference rates have held steady in the United States. In March 2023, the Federal Reserve announced that it expects to cut rates three times before year-end. Accordingly, rates appear likely to decline in the near term, reducing all-in-yields, which may continue to increasing repricings and dividend recapitalisations.

Return of broadly syndicated market

The year 2023 saw private credit largely dominate the US loan markets with depressed levels of activity in the broadly syndicated loan market and minimal high yield issuances. Beginning in late 2023, spurred in part by a return of repricings, activity in the broadly syndicated markets, both loans and high yield, picked up markedly. Going forward, investors predict greater balance of deal activity as across the broadly syndicated and private credit markets, with stronger sponsors and borrowers potentially having their pick of financing structures and providers.

Increased scrutiny of private credit

With the private credit market expanding its footprint and prominence, there has been an increased focus on non-bank activities in lending, particularly from federal agencies such as the Securities and Exchange Commission (SEC) and Financial Stability Oversight Counsel (FSOC). Last year, the SEC enacted the Private Fund Adviser Rules, which includes five sets of regulations and prohibitions intended to increase reporting and supervision of private fund advisers (many of which are, or oversee, private credit funds and institutional investors). That same year the FSOC announced its intent to monitor private credit more closely for vulnerabilities and potential risks to the broader financial system. The FSOC proposed requiring greater detail on reporting of loans to non-bank financial institutions and finalised guidance that provides the FSOC with greater flexibility to designate nonbanks as 'systematically important' financial institutions that would be subject to the Federal Reserve's supervision. Higher scrutiny of private credit has not been limited to the United States. In April 2024, the International Monetary Fund published its Global Financial Stability Report, which, inter alia, called for enhanced regulatory scrutiny of private credit.

Law stated - 2 May 2024