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Published by
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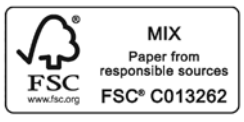

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Country Question and Answer Chapters:

A Comparison of Key Provisions in U.S. and European Leveraged Loan Agreements

Sarah Ward

Mark Darley

Skadden, Arps, Slate, Meagher & Flom LLP

While there are many broad similarities in the approach taken in European and U.S. leveraged loan transactions, there are also still a number of significant differences in commercial terms and general market practice. The importance of having a general understanding of these differences has been highlighted in recent years as an increasing number of European borrowers have turned to the highly liquid U.S. syndicated leveraged loan market as an attractive alternative source of funding. The pace at which this trend will continue is still unclear, especially given the mounting U.S. regulatory scrutiny of leveraged loan transactions and the prospect of increasing benchmark interest rates, but it seems likely that it is here to stay for at least some time.

This chapter will focus only on certain key differences between practice in the United States and Europe that may be encountered in a typical leveraged loan transaction. References throughout this article to "U.S. loan agreements" and "European loan agreements" should be taken to mean New York-law governed and English-law governed leveraged loan agreements, respectively.

This chapter is intended as an overview and a primer for practitioners. It is divided into four parts: Part A will focus on differences in documentation and facility types, Part B will focus on various provisions, including covenants and undertakings, Part C will consider differences in syndicate management and Part D will focus on recent legal and regulatory developments in the European and U.S. markets.

Part A – Documentation and Facility Types

Form Documentation

In both the European and U.S. leveraged loan markets, the standard forms used as a starting point for negotiation and documentation greatly influence the final terms. In Europe, both lenders and borrowers, through conduct adopted over a number of years, have typically become accustomed to and comfortable with using an "industry standard form" as a starting point for documentation. However, in the United States, such practice has not emerged and the form on which the loan documentation will be based (as well as who "holds the pen" for drafting the documentation) – which may greatly influence the final outcome – will be the subject of negotiation at an early stage.

Market practice in Europe has evolved through the influence of the Loan Market Association (or the "LMA") and the widespread membership it attracts from those involved in the financial sector: the LMA is comprised of more than 500 member organisations, including commercial and investment banks, institutional investors, law firms, service providers and rating agencies. While the LMA originated with the objective of standardising secondary loan trading documentation, it now plays an essential role in the primary loan market by producing, updating and giving guidance on key provisions in their recommended forms of English law documents for, amongst other things, investment grade loan transactions, leveraged acquisition finance transactions, real estate finance transactions and most recently, the growing European private placement market.

Market practice in Europe invariably anticipates that parties will adopt the LMA recommended form documents as a starting point for syndicated loans: the practice of individual law firms or banks using their own form of loan document has largely disappeared. The widespread use of the LMA standard forms has resulted in good familiarity by the European investor market which, in turn, has added to the efficiency of review and comprehension not just by those negotiating the documents but also by those who may be considering participating in the loan. The LMA recommended forms are only a starting point, however, and whilst typically, the "back-end" LMA recommended language for boilerplate and other non-contentious provisions of the loan agreement will be only lightly negotiated (if at all), the provisions that have more commercial effect on the parties (such as mandatory prepayments, business undertakings, representations and warranties, conditions to drawdown, etc.) remain as bespoke to the specific transaction as ever.

Similar to the LMA in Europe, the Loan Syndications and Trading Association (the "LSTA") in the United States (an organisation of banks, funds, law firms and other financial institutions) was formed to develop standard procedures and practices in the trading market for corporate loans. One of the main practical differences from the LMA, however, is that although the LSTA has developed recommended standard documentation for loan agreements, those forms are rarely used as a starting draft for negotiation. Instead, U.S. documentation practice has historically been based on the form of the lead bank or agent although many banks' forms incorporate LSTA recommended language. Increasingly in the United States and in Europe, however, strong sponsors succeed in negotiating from an agreed borrower-friendly sponsor precedent drafted by borrower's counsel.

Facility Types

The basic facility types in both U.S. and European loan agreements are very similar. Each may typically provide for one or more term loans (ranking equally but with different maturity dates,

amortisation profiles (if amortising) and interest rates) and a *pari passu* ranking revolving credit facility. Of course, depending on the nature of the borrower's business, there could be other specific, standalone facilities, such as facilities for acquisitions, working capital and letters of credit.

In the United States, as in Europe, revolving and term loan facilities typically share the same security package (or liens in U.S. loan market parlance) and priority. However, in the United States, some revolving loan facilities may be structured as "first-out-revolvers" to make such loans more attractive to potential investors. First-out-revolvers are secured by the same liens granted to all *pari passu* creditors but provide for payment priority to the first-out-revolvers in respect of collateral proceeds. This feature is not so common in European loans except for standalone "super senior" revolving credit facilities used in conjunction with a high-yield bond issuance.

U.S. Term B loans are typically made by U.S. based institutional investors (historically, there has not been much European investor appetite for this type of debt). As many of the U.S. Term B loan investors are also high-yield bond investors and, consequently, familiar and comfortable with high-yield bond terms, many of the U.S. Term B loan terms bear a striking similarity to high-yield bond terms, especially in the relaxed business undertakings, incurrence (rather than maintenance) financial covenants and absence of loan amortisation. The *quid pro quo*, however, is a higher margin and other economic protections (such as "no-call" periods) not commonly seen in Term A loans. Term A loans are syndicated in the United States to traditional banking institutions.

While in Europe, some very strong sponsors and borrowers have been able to negotiate similarly relaxed terms for some time in their European loan agreements, for certain other European sponsors and borrowers, U.S. Term B loans (and/or the U.S. high yield bond market) have provided an increasingly popular alternative means of achieving a similar outcome.

Certainty of Funds

Another key difference between the U.S. and European loan markets relates to the issue of certainty of funds in an acquisition finance context. In the United Kingdom, when financing an acquisition of a UK incorporated public company involving a cash element, the City Code on Takeovers and Mergers requires purchasers to have "certain funds" prior to the public announcement of any bid. The bidder's financial advisor is required to confirm the availability of the funds and, if it does not diligence this appropriately, may be liable to provide the funds itself should the bidder's funding not be forthcoming. Understandably, both the bidder and its financial advisor need to ensure the highest certainty of funding. In practice, this requires the full negotiation and execution of loan documentation and completion of conditions precedent (other than those conditions that are also conditions to the bid itself) at the bid stage of a public company acquisition financing.

The concept of "certain funds" has also permeated the private buyout market in Europe, so that the lenders in a private acquisition finance transaction are, in effect, required to confirm satisfaction of all of their financing conditions at the signing of the loan agreement and disapplying any drawstop events (subject to limited exceptions) until after completion of the acquisition.

In the United States, however, there is no regulatory certain fund requirement as in the United Kingdom. In U.S. acquisition financing, commitment papers, rather than loan documents, are typically executed simultaneously with the purchase agreement. Ordinarily, while such commitment papers are conditioned on the negotiation of definitive loan documentation, they contain "*SunGard*" clauses that limit the representations and warranties made by the borrower and the delivery of certain types of collateral required by the lenders on the closing date of the loan.

Part B – Loan Documentation Provisions

Covenants and Undertakings

Many of the significant differences between U.S. and European loan agreements lie in the treatment and documentation of covenants (as such provisions are termed in U.S. loan agreements) and undertakings (as such provisions are termed in European loan agreements). This Part B explores the differences in some of the more intensively negotiated covenants/undertakings, recognising that the flexibility afforded to borrowers in these provisions depends on the financial strength of the borrower, the influence of a sponsor and market conditions.

Notwithstanding the various differences (outlined below), U.S. and European loan agreements utilise a broadly similar credit "ring fencing" concept, which underpins the construction of their respective covenants/undertakings. In U.S. loan agreements, borrowers and guarantors are known as "loan parties", while their European equivalents are known as "obligors". In each case, loan parties/obligors are generally free to deal between themselves on the basis they are all within the credit group and are bound under the terms of the loan agreement. However, to minimise the risk of credit leakage, loan agreements will invariably restrict dealings between loan parties/obligors and other members of the borrower group that are not loan parties/obligors, as well as third parties generally. In U.S. loan agreements there is usually an ability to designate members of the borrower's group as "unrestricted subsidiaries" so that they are not restricted under the loan agreement. However, the loan agreement will then limit dealings between members of the restricted and unrestricted group and the value attributed to the unrestricted group might not be taken into account in calculating financial covenants.

Restrictions on Indebtedness

U.S. and European loan agreements include an "indebtedness covenant" (in U.S. loan agreements) or a "restriction on financial indebtedness" undertaking (in European loan agreements) which prohibits the borrower (and usually, its restricted subsidiaries) from incurring indebtedness unless explicitly permitted. Typically, "indebtedness" will be broadly defined in the loan agreement to include borrowed money and other obligations such as notes, letters of credit, contingent obligations, guaranties and guaranties of indebtedness.

In U.S. loan agreements, the indebtedness covenant prohibits all indebtedness, then allows for certain customary exceptions (such as the incurrence of intercompany debt, certain acquisition debt, certain types of indebtedness incurred in the ordinary course of business or purchase money debt), as well as a specific list of exceptions tailored to the business of the borrower. The indebtedness covenant will also typically include an exception for a general "basket" of debt, which can take the form of a fixed amount or a formula based on a ratio or a combination, such as the greater of a fixed amount and a ratio formula. Reclassification provisions (allowing the borrower to utilise one type of permitted debt exception and then reclassify the incurred permitted debt under another exception) are also becoming more common in the United States.

The credit agreements of large cap and middle market U.S. borrowers also typically provide for an incremental facility allowing the borrower to incur additional debt (on top of any commitments the credit agreement originally provided for) under the credit agreement, or in the case of certain large cap U.S. borrowers, allowing the borrower to incur additional *pari passu* or subordinated secured or unsecured incremental debt outside credit agreement under a separate facility (known as "sidecar facility" provisions). Traditionally the incremental facilities were limited to a fixed dollar amount, referred to as "free and clear" tranches, but the recent trend is to permit borrowers to incur an unlimited amount so long as a *pro forma* leverage ratio is met. Most incremental facilities have a most favoured nations clause that provides that, if the margin of the incremental facility is higher than the margin of the original loan, the original loan's margin will be increased to within a specific number of basis points (usually 50 bps) of the incremental facility's margin.

The restriction on financial indebtedness undertaking typically found in European loan agreements is broadly similar to its U.S. covenant counterpart and usually follows the same construct of a general prohibition on all indebtedness, followed by certain "permitted debt" exceptions (both customary ordinary course type exceptions as well as specifically tailored exceptions requested by the borrower). Historically, ratio debt exceptions and reclassification provisions were not commonly seen in European leveraged loan agreements. However, recent European deal activity has revealed a movement towards U.S. style permissions, such as "permitted debt" exceptions based on a leverage ratio test combined with a general permitted basket, as well as incremental facilities along the lines of those permitted in U.S. loan transactions.

Restrictions on Granting Security/Liens

U.S. loan agreements will also invariably restrict the ability of the borrower (and usually, its subsidiaries) to incur liens. A typical U.S. loan agreement will define "lien" broadly to include any charge, pledge, claim, mortgage, hypothecation or otherwise any arrangement to provide a priority or preference on a claim to the borrower's property. This lien covenant prohibits the incurrence of all liens but provides for certain typical exceptions, such as liens securing permitted refinancing indebtedness, purchase money liens, statutory liens and other liens that arise in the ordinary course of business, as well as a general basket based on a fixed dollar amount to secure a specified amount of permitted indebtedness. In some large cap deals, both in the U.S. and in Europe, borrowers are able to secure permitted indebtedness based on a total leverage ratio or senior secured leverage ratio.

In the European context, the restriction on liens is known as a "negative pledge". Rather than the "lien" concept, European loan agreements will generally prohibit a borrower (and obligors under the loan agreement) from providing "security", where security is broadly defined to include mortgages, charges and pledges, but may also include other preferential arrangements. As with U.S. loan agreements, the prohibition on providing security is subject to a list of customary and specifically negotiated "permitted security" exceptions. Importantly, most European loan agreements will specifically prohibit "quasi-security" in the negative pledge in circumstances where the arrangement or transaction is entered into primarily to raise financial indebtedness or to finance the acquisition of an asset. "Quasi-security" includes transactions such as sale and leaseback, retention of title and certain set-off arrangements. Borrowers are also typically able to negotiate a "general basket" to permit the securing of a certain fixed amount of general indebtedness. Of course, borrowers may be able to negotiate specific "permitted security" exceptions depending on their creditworthiness and specific business requirements.

Restriction on Investments

A restriction on the borrower's ability to make investments is commonly found in U.S. loan agreements. "Investments" include loans, advances, equity purchases and other asset acquisitions. Historically, investments by loan parties in non-loan parties have been capped at modest amounts. In some recent large cap deals, loan parties have been permitted to invest uncapped amounts in any of their subsidiaries, including foreign subsidiaries who are not guarantors under the loan documents. Other generally permitted investments include short term securities or other low-risk liquid investments, loans to employees and subsidiaries, and investment in other assets which may be useful to the borrower's business. In addition to the specific list of exceptions, U.S. loan agreements also include a general basket, sometimes in a fixed amount, but increasingly based a flexible "builder basket" growth concept.

The "builder basket" concept, typically defined as a "Cumulative Credit" or an "Available Amount", represents an amount the borrower can utilise for investments, restricted payments (as discussed below), debt prepayments or other purposes. Traditionally, the builder basket begins with a fixed-dollar amount and "builds" as retained excess cash flow (or in some agreements, consolidated net income) accumulates. Some loan agreements may require a borrower to meet a *pro forma* financial test to use the builder basket. If the loan agreement also contains a financial maintenance covenant (such as a leverage test), the borrower may also be required to satisfy a tighter leverage ratio to utilise the builder basket for an investment or restricted payment. Some sponsors have also negotiated loan documents that allow the borrower to switch between different builder basket formulations for added flexibility. In another example of convergence with high-yield bond indentures, recently builder baskets that use 50% of consolidated net income (including the proceeds of equity issuances and equity contributions) rather than retained excess cash flow and an interest coverage ratio rather than a leverage ratio have become more common. This approach gives borrowers more flexibility because a basket using consolidated net income is usually larger and an interest coverage ratio is usually easier to comply with than a leverage ratio.

European loan agreements will typically contain stand-alone undertakings restricting the making of loans, acquisitions, joint ventures and other investment activity by the borrower (and other obligors). While the use of builder baskets is still not the norm in European loan agreements, often acquisitions will be permitted if funded from certain sources, such as retained excess cash flow. Exceptions by reference to ratio tests alone are not commonly seen in European loan agreements, although they frequently form one element of the tests that need to be met to allow investments such as permitted acquisitions.

Restricted Payments

U.S. loan agreements will typically restrict borrowers from making payments on equity, including repurchases of equity, payments of dividends and other distributions, as well as payments on subordinated debt. As with the covenants outlined above, there are typical exceptions for restricted payments not materially adverse to the lenders, such as payments on equity solely in shares of stock, or payments of the borrower's share of taxes paid by a parent entity of a consolidated group.

In European loan agreements, such payments are typically restricted under separate specific undertakings relating to dividends and share redemptions or the making of certain types of payments, such as management and advisory fees, or the repayment of certain types

of subordinated debt. As usual, borrowers will be able to negotiate specific carve-outs (usually hard capped amounts) for particular "permitted payments" or "permitted distributions" as required (for example, to permit certain advisory and other payments to the sponsor), in addition to the customary ordinary course exceptions.

In U.S. loan agreements, a borrower may use its "builder basket" or "Available Amount" (increasingly based on consolidated net income rather than retained excess cash flow as discussed above) for restricted payments, investments and prepayments of debt, subject to annual baskets consisting of either a fixed-dollar amount or a certain financial ratio test. In some recent large cap and sponsored middle market deals in the United States, borrowers have been permitted to make restricted payments subject only to being in *pro forma* compliance with a specific leverage ratio, rather than meeting an annual cap or basket test.

European loan agreements typically have not provided this broad flexibility. However, some strong sponsors have been able to negotiate provisions permitting payments or distributions from retained excess cash flow, subject (typically) to satisfying a certain leverage ratio and, illustrating further convergence of terms, some transactions have adopted the U.S. approach outlined above.

Call Protection

In both European and U.S. loan agreements, borrowers are commonly permitted to voluntarily prepay loans in whole or in part at any time. However, some U.S. loan agreements do include call protection for lenders, requiring the borrower pay a premium if loans are repaid within a certain period of time. While "hard call" premiums (where term loan lenders receive the premium in the call period for any prepayment, regardless of the source of funds or other circumstances) are rare, "soft call" premiums (typically 1%) on prepayments made within the first year, or increasingly, the first six months, and funded from a refinancing or re-pricing of loans are common in the U.S. loan market. In some recent large cap deals, though, lenders waived call protection premiums in connection with a refinancing to consummate a material acquisition.

While call protection is relatively rare in the European market for senior debt, soft call protections have been introduced in certain European loans which have been structured to be sold or syndicated in the U.S. market. Call protection provisions are more commonly seen in the second lien tranche of European loans and mezzanine facilities (typically containing a gradual step down in the prepayment premium from 2% in the first year, 1% in the second year, and no call protection thereafter).

Voluntary Prepayments and Debt Buybacks

During the financial crisis, many U.S. borrowers amended existing loan agreements to allow for non-*pro rata* discounted voluntary prepayments of loans that traded below par on the secondary market. Although debt buybacks are much less frequent in the current strong syndicated loan market, the provisions allowing for such prepayments have become standard in U.S. loan agreements.

U.S. loan agreements typically require the borrower to offer to repurchase loans ratably from all lenders, in the form of a reverse "Dutch auction" or similar procedure. Participating lenders are repaid at the price specified in the offer and the buyback is documented as a prepayment or an assignment. Loan buybacks may also take the form of a purchase by a sponsor or an affiliate through non-*pro rata* open market purchases. These purchases are negotiated directly with individual lenders and executed through a form of assignment. Unlike loans repurchased by the borrower and then cancelled, loans assigned to sponsors or affiliates may remain outstanding. Lenders often cap the amount that sponsors and affiliates may hold and also restrict the right of such sponsors or affiliates in voting the loans repurchased.

Similarly, in European loan agreements, "Debt Purchase Transaction" provisions have been included in LMA recommended form documentation since late 2008. The LMA standard forms contain two alternative debt purchase transaction provisions – one that prohibits debt buybacks by a borrower (and its subsidiaries), and a second alternative that permits such debt buybacks, but only in certain specific conditions (for example, no default continuing, the purchase is only in relation to a term loan tranche and the purchase is made for consideration of less than par).

Where the loan agreement permits the borrower to make a debt purchase transaction, to ensure that all members of the lending syndicate have an opportunity to participate in the sale, it must do so either by a "solicitation process" (where the parent of the borrower or a financial institution on its behalf approaches each term loan lender to enable that lender to offer to sell to the borrower an amount of its participation) or an "open order process" (where the parent of the borrower or financial institution on its behalf places an open order to purchase participations in the term loan up to a set aggregate amount at a set price by notifying all lenders at the same time).

Both LMA alternatives permit debt purchase transactions by the sponsor (and its affiliates), but such purchasers are subject to the disenfranchisement of the sponsor (or its affiliate) in respect the purchased portion of the loan.

Mandatory Prepayments

U.S. borrowers are typically required to prepay loans incurred under their loan agreements using the net proceeds of certain asset sales, incurrences of new *pari passu* debt and issuances of equity. Recently, though, mandatory prepayment provisions relating to asset sales have provided greater flexibility for borrowers by carving out more types of dispositions from the definition of asset sale, expanding the duration and scope of reinvestment rights, increasing the threshold amount under which the borrower need not use the proceeds to prepay and allowing the borrower to use asset sale proceeds to ratably repay *pari passu* debt.

While the mandatory prepayment triggers are broadly similar in European loan agreements, a notable trend in Europe has been the rise of "portability" provisions, which allows a change of control to occur, without the usual mandatory prepayment obligation found in European loan agreements. While portability is not a common feature in European loans, stronger European borrowers and sponsors have been increasingly able to achieve this flexibility subject to certain restrictions (typically, a one-time use limit and a requirement that the buyer be on an approved white list of "acceptable buyers"). In U.S. loan agreements a change of control triggers an event of default rather than a mandatory prepayment. A handful of deals in the United States have included "precapitalised" or "precap" provisions that permit the sale of a borrower to a qualified purchaser without causing a change-of-control event of default but the concept has not taken off and "precap" provisions remain rare.

Financial Covenants

Historically, U.S. and European leveraged loan agreements contained at least two maintenance financial covenants: total leverage; and interest coverage, typically tested at the end of each quarter.

In the United States, "covenant-lite" loan agreements containing no maintenance or on-going financial covenants now comprise more than 60% of outstanding S&P/LSTA loans and have found their way into many middle market deals (although the volume of covenant-lite middle market deals receded substantially in the fourth quarter of 2014 as compared to earlier in the year, reflecting the pullback in the market as a whole from the trend in 2013 and the first half of 2014 toward increasingly scarce financial covenants and climbing leverage ratios). In certain transactions, the loan agreement might be "quasi-covenant-lite" meaning that it contains only one maintenance financial covenant (usually a leverage covenant) which is applicable only to the revolver and only when a certain percentage of revolving loans are outstanding at the testing date (15-25% is fairly typical, but has been as high as 37.5%). Covenant-lite (or quasi-covenant-lite) loan agreements may nonetheless contain financial ratio incurrence tests – such tests are used merely as a condition to incurring debt, making restricted payments or entering into other specified transactions. Unlike maintenance covenants, incurrence based covenants are not tested regularly and a failure to maintain the specified levels would not, in itself, trigger a default under the loan agreement.

European loan agreements traditionally included a full suite of on-going financial maintenance covenants with a quarterly leverage ratio test being the most common. However, deal activity in 2014 revealed that the European market has become more accepting of the covenant-lite and covenant-loose deal structures more typically seen in deals in the U.S. market, especially where it is intended that the loan will be syndicated in the U.S. market in addition to the European market. Whilst structures containing no term loan maintenance covenant and a single springing leverage covenant applicable only to the revolving facility have become more common in the European market, it is fair to say they are still not as prevalent as in the United States.

In the United States, the leverage covenant historically measured consolidated debt of all subsidiaries of the borrower. Today, leverage covenants in U.S. loan agreements frequently apply only to the debt of restricted subsidiaries. Moreover, leverage covenants sometimes only test a portion of consolidated debt – sometimes only senior debt or only secured debt (and in large cap deals of top tier sponsors sometimes only first lien debt). Lenders are understandably concerned about this approach as the covenant may not accurately reflect overall debt service costs. Rather, it may permit the borrower to incur unsecured senior or subordinated debt and still remain in compliance with the leverage covenant. This is not a trend that has yet found its way over to Europe.

In the event a U.S. loan agreement contains a leverage covenant, it invariably uses a "net debt" test by reducing the total indebtedness (or portion of debt tested) by the borrower's unrestricted cash and cash equivalents. Lenders sometimes cap the amount of cash a borrower may net out to discourage both over-levering and hoarding cash. The trends with regard to netting over the past few years illustrate borrowers' rapidly increasing success in pushing for greater flexibility. The LSTA[1] reported that, in the third quarter of 2013, a sample of leveraged credit agreements revealed that nearly half had a fixed capped and the rest had unlimited netting – only a year later, in the third quarter of 2014, credit agreements with a fixed cap had dropped to only a quarter of the sample.

In Europe, the total net debt test is tested on a consolidated group basis, with the total net debt calculation usually including the debt of all subsidiaries (but obviously excluding intra-group debt). Unlike the cap on netted cash and cash equivalents in some U.S. loan agreements, European borrowers net out all cash in calculating compliance with the covenant.

With strong sponsor backing, borrowers have increasingly eased the restriction of financial covenants by increasing the amount of add-backs included in the borrower's EBITDA calculation. Both U.S. and European loan documents now include broader and more numerous add-backs including transaction costs and expenses, restructuring charges, payments to sponsors and certain extraordinary events. Recently many borrowers have negotiated add-backs (generally to the extent reasonably identifiable and factually supportable) for projected and as-yet unrealised cost savings and synergies. The Leveraged Lending Guidance and supplementary commentary from federal regulatory agencies (discussed further in Part D), though, suggest that regulators may apply heightened scrutiny to definitions of EBITDA that provide for add-backs without "reasonable support". While lenders have accommodated savings and synergies add-backs, increasingly such add-backs are capped at a fixed amount or certain percentage of EBITDA (15% in the United States, 5-20% in Europe).

Equity Cures of Financial Covenants

For a majority of sponsor deals in the United States, loan agreements that contain a financial maintenance covenants also contain the ability for the sponsor to provide an "equity cure" for non-compliance. The proceeds of such equity infusion are usually limited to the amount necessary to cure the applicable default, and are added as a capital contribution (and deemed added to EBITDA or other applicable financial definition) for this this purpose. Because financial covenants are meant to regularly test the financial strength of a borrower independent of its sponsor, U.S. loan agreements increasingly place restrictions on the frequency (usually no more than two fiscal quarters out of four) and absolute number (usually no more than five times over the term of the credit facility) of equity cures.

In Europe, equity cure rights have been extremely common over the last few years. As in the United States, the key issues for negotiation relate to the treatment of the additional equity, for example, whether it should be applied to increase cash flow or earnings, or otherwise reduce indebtedness (although it is typically restricted to the latter). Similar restrictions apply to equity cure rights in European loan documents as they do in the United States in respect of the frequency and absolute number of times an equity cure right may be utilised – however, in Europe the frequency is typically lower (and usually, an equity cure cannot be used in consecutive periods) and is subject to a lower overall cap (usually, no more than two or three times over the term of the facility). From a documentation perspective, it is also important to note that there is no LMA recommended equity cure language.

Sanctions, Anti-Money-Laundering and Anti-Bribery Provisions

A recent trend in credit agreements involving U.S. borrowers, whether the bank is American or European, is the increasing expansiveness of the representations, warranties and covenants relating to anti-bribery, anti-money laundering and sanctions laws in the U.S. or abroad (the "Anti-Corruption/Sanctions Laws") coupled with lenders' increasing rigidity and resistance to negotiation with regard to these expansive Anti-Corruption/Sanctions Laws provisions. Negotiation of these provisions may focus on whether it is appropriate to limit these provisions by materiality and/or by knowledge. Borrowers often are concerned about their ability to fully comply with broadly drafted provisions without some form of knowledge, scope and/or materiality qualifiers.

Part C – Syndicate Management

Voting Thresholds

In U.S. loan agreements, for matters requiring a vote of syndicate lenders holding loans or commitments, most votes of "required lenders" require only a simple majority of lenders (that is, more than 50% of lenders by commitment size) for all non-unanimous issues. In European loan agreements, most votes require 66.67% or more affirmative vote of lenders by commitment size. In some, but not all, European loan agreements, certain votes that would otherwise require unanimity may instead require only a "super-majority" vote, ranging between 85-90% of lenders by commitment size. Such super majority matters typically relate to releases of transaction security or guarantees, or an increase in the facilities.

"Unanimous" decisions in U.S. loan agreements are limited to fundamental matters and require the consent only of affected lenders (and are not, therefore, truly unanimous), while in European loan agreements (except where they may be designated as a super majority matter), decisions covering extensions to payment dates and reductions in amounts payable (even certain mandatory prepayment circumstances), changes to currencies and commitments, transfer provisions and rights between lenders all require the unanimous consent of lenders (not just those affected by the proposed changes).

Yank-a-Bank

U.S. loan agreements often contain provisions allowing the borrower to remove one or more lenders from the syndicate in certain circumstances. A borrower may, for example remove a lender where such lender refuses to agree to an amendment or waiver requiring the unanimous consent of lenders, if the "required lenders" (typically more than 50% of lenders by commitment) have consented. Other reasons a borrower may exercise "yank-a-bank" provisions are when a lender has a loss of creditworthiness, has defaulted on its obligations to fund a borrowing or has demanded certain increased cost or tax payments. In such circumstances, the borrower may facilitate the sale of the lender's commitment to another lender or other eligible assignee. In most European loan agreements, yank-a-bank provisions are also routinely included (described as such or as "Defaulting Lender" provisions) and are similar in mechanism. However, the threshold vote for "required lenders" is typically defined as at least 66.67% of lenders by commitment.

Snooze-You-Lose

In addition to provisions governing the required votes of lenders, most European loan agreements will also contain "snooze-you-lose" provisions, which favour the borrower when lenders fail to respond to a request for an amendment, consent or waiver. Where a lender does not respond within a specific time frame, such lender's vote or applicable percentage is discounted from the total when calculating whether the requisite vote percentage have approved the requested modification. Similar provisions are rare in U.S. loan agreements.

Transfers and Assignments

In European loan agreements, lenders may assign their rights or otherwise transfer by novation their rights and obligations under the loan agreement to another lender. Typically, lenders will seek to rely on the transfer mechanism, utilising the standard forms of transfer certificates which are typically scheduled to the loan agreement. However, in some cases, an assignment may be necessary to avoid issues in some European jurisdictions which would be caused by a novation under the transfer mechanic (particularly in the context of a secured deal utilising an English-law security trust, which may not be recognised in some European jurisdictions).

Generally, most sub-investment grade European deals will provide that lenders are free to assign or transfer their commitments to other existing lenders (or an affiliate of such a lender) without consulting the borrower, or free to assign or transfer their commitments to a pre-approved list of lenders (a white list), or not to a predetermined list of lenders (a blacklist). For stronger borrowers in both Europe and the United States, the lenders must usually obtain the consent of the borrower prior to any transfer or assignment to a lender that is not an existing lender (or affiliate).

In the United States, the LSTA has recommended "deemed consent" of a borrower where a borrower does not object to proposed assignments within five business days. Similar to stronger European borrowers and sponsors who are able to negotiate a "blacklist", stronger borrowers in the United States, or borrowers with strong sponsors, often negotiate a "DQ List" of excluded (disqualified) assignees. Recently in the United States, large cap borrowers have pushed for expansive DQ lists and the ability to update the list post-closing (a development not seen in European loan agreements). In both the European and US contexts, the DQ List or blacklist helps the borrower avoid assignments to lenders with difficult reputations.

In the U.S. market, exclusion of competitors and their affiliates is also negotiated in the DQ List. In European loan agreements, the LMA recommended form assignment and transfer language provides that existing lenders may assign or transfer their participations to other banks or financial institutions, or to trusts, funds or other entities that are "regularly engaged in or established for the purpose of making, purchasing or investing in loans, securities or other financial assets". This language has the practical effect of limiting the potential range of investors in the loan, including competitors of the borrower.

Part D – New Regulatory and Legal Developments in the Loan Market

Leveraged Lending Guidance

U.S. federal bank regulators indicated during the third quarter of 2014 that they would more carefully scrutinise leveraged lending issuances following their determination that a third of leveraged loans they reviewed did not comply with the Leveraged Lending Guidance (the "Guidance") issued in March 2013 by the Federal Reserve, the OCC and the FDIC. The Guidance provides, among other things, that a leverage level in excess of 6x total debt over EBITDA will raise regulatory concern for most industries and may result in the loan being criticised. In addition, the Guidance provides that a borrower should be able to amortise its senior secured debt or repay half its total debt with five to seven years of base cash flows.

Supplementary regulatory commentary provides that failure to adhere to these requirements is not a bright line bar to an issuance if there are other mitigating factors. The lack of a bright line rule may permit some loan issuances that do not achieve complete compliance, but it also introduces significant uncertainty into the process of underwriting a loan issuance for sponsors, borrowers and lenders alike. Increased concern from banks regarding regulatory approval likely contributed to the pull back in the second half of 2014 from the ballooning volume of leveraged lending issuances

and the increasingly sponsor/borrower-friendly documentation that characterised leveraged lending in 2013 and the first half of 2014. The Guidance and the heightened regulatory attention may result in more borrowers electing to obtain financing in the high-yield market instead of the leveraged lending market or electing to use non-regulated institutions rather than traditional banks as agents and lenders.

Restrictive Auditor Selection Clauses in Europe

Both U.S. and European loan agreements traditionally contain provisions restricting the accountancy firm that may be engaged by the borrower for the purposes of examining and auditing its financial statements to a "big four" firm (that is, E&Y, KPMG, PwC or Deloitte). However, the European Parliament and the Council of the European Union have recently passed an audit market reform package that, amongst other things, seeks to prohibit such restrictive auditor choice clauses in any contract, including loan agreements. The legislative package consists of a regulation and a directive, which European Union Member States are required to incorporate the provisions into their respective national law by 2016. The prohibition on "big four" auditor clauses will apply to both existing and future loan agreements and will come into effect in June 2017. Significantly, the regulation also requires borrowers that are public-interest entities (for example, listed companies and insurance entities) to inform authorities of any attempt by any third party, such as a lender, to impose such a contractual clause or to otherwise "improperly influence" the decision of the general meeting of shareholders or members on the selection of a statutory auditor or an audit firm. Restrictive auditor clauses are still permitted in the United States. The Public Company Accounting Oversight Board, implemented by the Sarbanes-Oxley Act of 2002, considered a mandatory auditor rotation requirement to promote independence but abandoned the proposal upon pressure from legislators.

Changes in LIBOR Administration

In response to the LIBOR-rigging scandal that was exposed in 2012, extensive LIBOR reforms were adopted, including discontinuation of certain rates and the addition of confidentiality restrictions on each bank's LIBOR submission. One documentation issue the reforms have raised is determining LIBOR for interest periods that have been discontinued. Some U.S. credit agreements have taken the approach of approximating LIBOR for an interest period for which it is not available by interpolating on a linear basis the rates for the next longest and next shortest interest period for which LIBOR is available. Others have taken the approach of using an alternative benchmark in the event that a particular LIBOR rate is unavailable. Some use a hybrid of the two approaches – if the requisite LIBOR rate is unavailable, then an alternative benchmark is to be used and, if that is not available, an interpolated rate is to be used. The LMA's suggested provision uses linear interpolation. Banks have also questioned whether the new confidentiality rules could affect reference banks or restrict the provision of internal rates. The opinion of the LMA is that this is not an issue, but some banks remain concerned about liability for quoting their internal rates or acting as a reference bank.

Conclusion

As highlighted in this article, it is important for practitioners and loan market participants to be aware of the key differences in the commercial terms and market practice in European and U.S. leveraged loan transactions. While there are many broad similarities between the jurisdictions, borrowers and lenders that enter into either market for the first time may be surprised by the differences, some of which may appear very subtle but which are of significance. As more and more European-based borrowers attempt to access the U.S. syndicated loan market by entering into U.S. loan agreements (whether to obtain more favourable pricing or better loan terms generally), the importance of having a general understanding of the differences is now even more critical.

For further information in relation to any aspect of this chapter, please contact Sarah Ward in New York by email at sarah.ward@skadden.com or by telephone at +1 212 735 2126, or Mark Darley in London by email at mark.darley@skadden.com or by telephone at +44 20 7519 7160.

Endnote

1. *Credit: Just the Stats (Well, Maybe a Little Commentary),* Loan Syndications and Trading Association Week in Review, Nov. 7, 2014, available at http://www.lsta.org/news-and-resources/lsta-newsletter (accessed Feb. 26, 2015).

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Sarah Ward
Skadden, Arps, Slate, Meagher & Flom LLP
4 Times Square
New York, NY 10036
USA

Tel: *+1 212 735 2126*
Fax: *+1 917 777 2126*
Email: *sarah.ward@skadden.com*
URL: *www.skadden.com*

Sarah Ward serves as co-chair of Skadden's Legal Opinion Oversight Committee. She served as co-head of Skadden's Banking Group from 2009 to 2014 and is a former member of Skadden's Policy Committee, the firm's governing body. Ms. Ward focuses primarily on the representation of borrowers and lenders in acquisitions and other leveraged financings, as well as corporate restructurings and workouts. She has extensive experience representing financial institutions such as Barclays, Citigroup and Goldman Sachs, and companies such as Travelport, CIT and Exide.

Ms. Ward is recognised as a leading attorney in *Chambers Global: The World's Leading Lawyers for Business* and *Chambers USA: America's Leading Lawyers for Business*, and has been singled out for her extensive experience in leverage financing work. She also has been included in *IFLR1000* (2013 and 2014), *Legal 500 U.S.* (2013) and *The International Who's Who of Banking Lawyers* (2014). Ms. Ward has authored numerous articles related to her practice, and has lectured extensively on banking-related topics.

Mark Darley
Skadden, Arps, Slate, Meagher & Flom LLP
40 Bank Street, Canary Wharf
London, E14 5DS
United Kingdom

Tel: *+44 20 7519 7160*
Fax: *+44 20 7072 7160*
Email: *mark.darley@skadden.com*
URL: *www.skadden.com*

Mark Darley has led Skadden's European law banking practice since joining the firm in April 2002 and was appointed global co-head of Skadden's Banking Group in 2009. Throughout his career, Mr. Darley has focused particularly on leveraged finance, restructuring and project finance transactions. His practice embraces advising both lenders and borrowers, including international financial institutions, private equity houses, hedge and other funds, and investment grade corporates. His clients have included Citibank, RBS, SG, SEB, Credit Suisse, UCB SA, Joh. A. Benckiser, Ares Life Sciences, Pfizer Inc., News Corporation, Vue Cinemas, Doughty Hanson and Oaktree, among others.

Mr. Darley has been selected for inclusion in *Chambers Global: The World's Leading Lawyers for Business*, *Chambers UK* and *Who's Who Legal – Banking*, and named "Leveraged Finance Lawyer of the Year in England 2014" by *Global Law Experts*.

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GLG
Global Legal Group

59 Tanner Street, London SE1 3PL, United Kingdom
Tel: +44 20 7367 0720 / Fax: +44 20 7407 5255
Email: sales@glgroup.co.uk

www.iclg.co.uk