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A practical cross-border insight into lending and secured finance

"Yankee Loans" – Structuring Considerations; "Lost in Translation" – Comparative Review and Recent Trends

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Introduction

2014 saw a year of record issuance for so-called "Yankee Loans", i.e. US dollar denominated term loans syndicated in the US Term Loan B market to institutional investors and provided to European and Asian borrower groups, based on New York law credit documentation. Yankee Loan issuance volume in 2014 increased to €37.6 billion, up from €30.8 billion in 2013, with at least 20 major deals completing during the year and it is noteworthy that approximately one third of all leveraged loan financings raised by European borrowers in 2014 were placed in the US market. Asian borrowers also continue to look to selectively tap the US market, with at least 9 deals done since the second half of 2012.

Historically, European and Asian borrower groups sourced most of their financing needs through local European and Asian leveraged finance markets and would only seek to raise financing in the US leveraged finance market to match US dollar denominated financing against US dollar revenue streams or in certain more limited circumstances where there was insufficient liquidity in local markets to finance larger transactions.

From around 2010 onwards through the first half of 2013, the depth and liquidity of the institutional investor base in the US Term Loan B market proved to be an attractive alternative source of financing for some European and Asian borrower groups and was a key source of financing liquidity during that period in light of conditions affecting local markets. More recently from the second half of 2013 onwards through the end of 2014, as markets have continued to recover, European and Asian borrower groups have looked to tap US markets on a more opportunistic basis in a search for better pricing and terms (after factoring in currency hedging costs) in leveraged finance transactions, whether new acquisition financings, recapitalisations or repricings.

Market views on the outlook for Yankee Loans in 2015 and beyond are varied but factors that will determine issuance volume in 2015 and beyond will include supply/demand metrics in both the US and European leveraged loan markets, whether US pricing rebounds to become more attractive again, relative to pricing terms available from lenders in Europe and Asia, and whether the institutional investor base in Europe continues to increase in depth and liquidity.

When looking at "Yankee Loan" deals, it is important to remember that there are a number of key structuring issues (driven primarily by location of the borrower(s) and guarantors), that need to be considered carefully, which may not apply in domestic US or in local European or Asian transactions.

It is also important to remember that (1) a number of features that would be considered typical for deals in the US leveraged loan market may not be appropriate to include in a "Yankee Loan" deal, because of the different outcomes in an insolvency or restructuring context depending on location of the borrower group, and (2) there are a number of features that would be considered typical for deals in the European or Asian leveraged loan markets that are not customary, or are treated in different ways, in New York law governed "Yankee Loan" deals.

This article considers, firstly, some of the key structuring considerations for Yankee Loans. Secondly, it looks at how some differences get "lost in translation", by comparing certain key provisions that differ between the US and European and Asian leveraged finance markets and exploring the differences that need to be taken into account for Yankee Loans, focusing on covenants and call protection, conditionality and transaction diligence.

Structuring Considerations

(Re)structuring is key

The primary focus of senior secured lenders in any leveraged finance transaction is the ability to recover their investment in a default or restructuring scenario. The optimal capital structure minimises enforcement risk by ensuring the senior secured lenders have the ability to control the restructuring process, which is achieved differently in the US and in Europe and Asia.

Due to this difference in expectation around how a restructuring is expected to take place, the US and European and Asian leveraged finance markets start from very different places when it comes to structuring leveraged finance transactions.

In the US, a typical restructuring in a leveraged finance transaction is usually accomplished through a Chapter 11 case under the US Bankruptcy code, where the position of senior secured lenders as secured creditors is protected by well-established rights and processes. Chapter 11 allows senior secured lenders to cram down "out of the money" junior secured or unsecured creditors and release their debt claims, guarantee claims and security pursuant to a Bankruptcy-court approved plan of reorganisation.

A Chapter 11 restructuring is a uniform, typically group-wide, court-led process where the aim is to obtain the greatest return by delivering the restructured business out of bankruptcy as a going concern. Bankruptcy petitions filed under Chapter 11 invoke an automatic stay prohibiting any creditor (importantly this includes trade creditors) from taking enforcement action which in terms of its practical effect has global application, because any person violating the automatic stay may be held in contempt of court by the applicable US Bankruptcy Court. The automatic stay protects the reorganisation process by preventing any creditor from taking enforcement action that could lead to a diminution in the value of the business. It is important to note that a Chapter 11 case binds all creditors of the given debtor (or group of debtors). Senior secured lenders retain control through this process as a result of their status as senior secured creditors holding senior secured claims on all (or substantially all) of the assets of a US borrower group.

By contrast, in Europe and Asia, it is more usual for a restructuring in a leveraged finance transaction to be accomplished through an out-of-court process[i]; this is typically achieved through enforcement of share pledge security to effect a transfer of equity interests of the top holding company of the borrower group and a sale of the business as a going concern, although in some situations restructurings can be achieved through a consensual out-of-court restructuring process without enforcing transaction security.

The reason for this is that placing a company into local insolvency proceedings in many European and Asian jurisdictions is often seen as the option of last resort. Placing a company into insolvency proceedings in many European or Asian jurisdictions is often viewed very negatively (vendors and customers typically view it as a precursor to the corporate collapse of the business) and often there is no Chapter 11 equivalent restructuring process available in the applicable European or Asian jurisdiction(s), meaning that entering into local insolvency proceedings will usually be value-destructive (in particular because of the lack of an automatic stay that binds trade creditors and, in some cases, because of a lack of clear procedures for cramming down junior creditors).

In order for senior secured lenders to retain control of a restructuring process in Europe or Asia, they traditionally rely on contractual tools contained in an intercreditor agreement. These tools include standstills applicable to junior creditors that are party to the intercreditor agreement that limit or prohibit junior creditors from enforcing their own security interests or forcing borrower groups into local insolvency proceedings, thereby allowing senior secured lenders to control the reorganisation of the borrower group's obligations, and release provisions applicable upon a "distressed" disposal of the borrower group, i.e. upon a trigger event such as enforcement of security after the occurrence of a continuing Event of Default or following an acceleration event.

These provisions are designed to enable a borrower group to be sold as a going concern and, in connection with this, for the guarantee and security claims (and in some cases, the primary debt claims) of junior creditors against the borrower group entities that are sold to be released once the proceeds from such sale have been applied pursuant to the waterfall provisions of the intercreditor agreement. This practice has developed because, unlike the US Chapter 11 framework, there is no equivalent single insolvency regime that may be implemented across European or Asian jurisdictions. While the EC Regulation on Insolvency Proceedings provides a set of laws that promote the orderly administration of a European debtor with assets and operations in multiple EU jurisdictions, such laws do not include a concept of a "group" insolvency filing (and there is no equivalent law in Asia) and most European and Asian insolvency regimes (with limited exceptions) do not provide for an automatic stay on enforcement applicable to all creditors.

The important distinction to note is that while a Chapter 11 proceeding binds all of a borrower group's creditors, the provisions of the intercreditor agreement will only be binding on the creditors that are a party to it. Typically these would be the primary creditors to the group (such as the providers of senior secured credit facilities, mezzanine or second lien facilities lenders and in some instances high yield bondholders), but would not include trade and other non-finance creditors, nor would it include (unless execution of an intercreditor agreement is required as a condition to such debt being permitted) third party creditors of permitted debt (e.g., incremental equivalent debt or ratio debt).

Historically, deals syndicated in the US leveraged loan market were those where the business or assets of the borrower's group were mainly in the US, albeit that some of the group may have been located in Europe, Asia or elsewhere, and these deals traditionally adopted the US approach to structuring: the loan documentation was typically New York law governed and assumed any restructuring would be effected in the US through Chapter 11 proceedings. Similarly, deals syndicated in the European or Asian leveraged loan market were historically those where the business or assets of the group were mainly in Europe or Asia, respectively, and these deals traditionally adopted a European/Asian approach to structuring: the loan documentation was typically English law governed, based on the LMA or APLMA form of senior facilities agreement, and provided contractual tools for an out-of-court restructuring in an intercreditor agreement (typically based on an LMA form).

US Term Loan B institutional investors are most familiar with, and typically expect, New York law and US market-style documentation. Therefore, most Yankee Loans are done using New York law documentation, which includes provisions in contemplation of a US Bankruptcy in the event of a reorganisation (including, for example, an automatic acceleration of loans and cancellation of commitments upon a US Bankruptcy filing due to the automatic stay applicable upon a US Bankruptcy filing). However, while a European or Asian borrower group may be able to elect to reorganise itself pursuant to a US Bankruptcy proceeding (which would require only a minimum nexus with the US), most European and Asian borrower group restructurings have traditionally occurred outside of an insolvency process, as described above.

In light of this, to ensure senior secured lenders' ability to drive the restructuring process in deals that involve European or Asian borrower groups, and protect their recoveries against competing creditors, a Yankee Loan done under New York law documentation should include the contractual "restructuring tools" typically found in a European/Asian-style intercreditor agreement, most notably a release or transfer of claims upon a "distressed" disposal, and consideration should be given as to whether to include a standstill on enforcement actions applicable to junior creditors (which in many ways can be seen as a parallel to the automatic stay under the US Bankruptcy Code) to protect against a European or Asian borrower group's junior creditors accelerating their debt and forcing the borrower group into local insolvency proceedings. If that were to occur, the likelihood of an effective restructuring of the business would be reduced as, not only would the senior secured lenders lose the ability to effectively control enforcement of their security (for example, arranging a pre-packaged sale of the business), but also, the equity holders would lose the ability to negotiate exclusively with the senior secured lenders for a period of time.

Location of borrower and guarantors

Legal/structuring considerations

In US leveraged loan transactions, the most common US state of organisation of the borrower is Delaware, but the borrower could be organised in any state in the US without giving rise to material concerns to senior secured lenders. In Europe or Asia, however, there are a number of considerations which are of material importance to senior secured lenders when evaluating in which European or Asian jurisdiction a borrower should be organised. First, many European and Asian jurisdictions have regulatory licensing requirements for lenders to borrowers organised in that jurisdiction. Second, withholding tax may be payable in respect of payments made by borrowers organised in many European or Asian jurisdictions to lenders located outside of the same jurisdiction (in particular, many "offshore" U.S. Term Loan B investors are unable to lend directly to a borrowers located in certain jurisdictions without triggering withholding tax or interest deductibility issues). Finally, some European and Asian jurisdictions may impose limits on the number of creditors of a particular nature a borrower organised in that jurisdiction may have.

Similarly, the value of collateral and guarantees from borrower group members located in the US in leveraged loan transactions is generally not a source of material concern for senior secured lenders. The UCC provides for a relatively simple and inexpensive means of taking security over substantially all of the non-real property assets of a US entity and, save for well understood fraudulent conveyance risks, upstream, cross stream and downstream guarantees from US entities do not give rise to material concerns for senior secured lenders.

However, the value of upstream and cross stream guarantees given by companies in many European and Asian jurisdictions is frequently limited as a matter of law (and in some cases, may be prohibited altogether). This can often mean that lenders do not get the benefit of a guarantee for either the full amount of their debt or the full value of the assets of the relevant guarantor. There are also very few European and Asian jurisdictions in which fully perfected security interests can be taken over substantially all of a company's non-real property assets with the ease or relative lack of expense afforded by the UCC. In many jurisdictions it is not practically possible to take security over certain types of assets, especially in favour of a syndicate of lenders which may change from time to time (if not from day to day).

As a result, in structuring a Yankee Loan, significant consideration should be given to the jurisdiction of the borrower and guarantors within the borrower group to assess the quality and value of credit support and security that will be available.

In addition, to ensure that a European or Asian borrower group restructuring may be accomplished through the use of the relevant intercreditor provisions, consideration should be given to determine an appropriate "enforcement point" in the group structure where a share pledge could be enforced efficiently in order to effect a sale of the whole group or business. The ease with which such share pledge may be enforced (given the governing law of the share pledge and the jurisdiction of the relevant entity whose shares are to be sold) should also be considered to ensure that the distressed disposal provisions in a European/Asian intercreditor agreement may be fully taken advantage of if needed.

Investor considerations

Many institutional investors in the US leveraged loan market (CLOs in particular) have investment criteria which govern what type of loans that they may participate in. These criteria usually include the jurisdiction of the borrower of the relevant loans, with larger availability or "baskets" for US borrower loans, and smaller "baskets" for non-US borrower loans. As a result, many recent Yankee Loans have included US co-borrowers in an effort to ensure that a maximum number of US Term Loan B institutional investors could participate in the financing. The addition of a US co-borrower in any financing structure merits careful consideration of many of the issues noted above if the other co-borrower is European or Asian. For example, the non US co-borrower may not legally be able to be fully liable for its US co-borrower's obligations due to cross-guarantee or upstream guarantee limitations. In addition, a US co-borrower may raise a number of tax structuring considerations, including a potential impact on the deductibility of interest, which should be carefully considered.

"Lost in translation" – a Comparison of Key Terms

In addition to the well-known (if not always fully understood or appreciated) difference in drafting style between New York leveraged loan credit agreements and European and Asian LMA and APLMA facility agreements, the substantive terms of loan documentation in the US and European and Asian markets have traditionally differed as well, with certain concepts moving across the Atlantic in either direction over time. Since 2010, Yankee Loan deals have been responsible for some increased flexibility for borrowers in a variety of forms moving slowly from the US market to the European market (and to a lesser extent the Asian market), although these terms are now starting to gain more widespread acceptance in European deals due to a number of factors, including "cross-pollination" and continued expansion of the non-bank investor pool in European markets.

US covenant-lite *v.* European covenant-lite & covenant-loose

US covenant-lite

Since 2010, the US leveraged loan market has seen the re-emergence of "covenant-lite" facilities (which accounted for over 57%[ii] market share of US leveraged loan issuance in 2014, compared to 22%[iii] of the market share for European leveraged loan issuance in 2014). In these deals, term loans do not benefit from any financial maintenance covenant. Only the revolving facility benefits from a single financial maintenance covenant, normally a leverage-based ratio (and this only applies on a "springing" basis i.e. at the end of a fiscal quarter, on a rolling LTM-basis, if utilisation exceeds a certain trigger percentage, at the time of writing, typically ranging between 25-35%).

More importantly, the negative covenant package for US "covenant-lite" facilities is either fully or partially incurrence-based in nature, similar to what would commonly be found in a high yield unsecured bond covenant package, reflecting the growing convergence between the US Term Loan B and US high yield bond markets.

Incurrence-based covenants typically provide permissions (for example to incur additional debt) subject to compliance with a specific financial ratio which is tested at the time of the specific event, rather than a financial maintenance covenant which would require continual compliance at all times, which traditionally has been required in secured senior bank loans, testing compliance against a projected business plan or base case financial model.

These US "covenant-lite" negative covenant packages tend to provide a borrower group with much more flexibility than 'traditional' European or Asian leveraged finance negative covenant packages, and therefore Yankee Loans have proved very attractive to European and Asian borrower groups. However, senior secured lenders need to consider these features carefully, because they may have different impacts in a Yankee Loan provided to a European or Asian borrower group compared to a loan made to a US borrower group.

In particular, the following is worth noting:

Debt incurrence (including incremental or accordion baskets and ratio debt baskets)

In US deals (including some Yankee Loans) there is no hard cap on debt incurrence (i.e. an unlimited amount of additional debt can be raised subject to compliance with an incurrence ratio test), which may be equal ranking secured debt incurred pursuant to the credit agreement (as incremental debt) or other incremental "equivalent" debt or "ratio" debt (which may be senior secured debt (either in the form of notes or in some cases in the form of sidecar loans) or junior secured, subordinated or unsecured debt, in each case incurred outside of the credit agreement, subject to a non-guarantor cap).

Debt incurrence flexibility works fine in deals that only involve US borrowers/guarantors because there is generally no material concern about being able to deal with junior secured or unsecured creditors in a restructuring or bankruptcy context.

However, in deals that involve non-US borrowers/guarantors, if comparable debt incurrence flexibility is allowed, issues can arise due to the fact that guarantees provided by non-US entities may be subject to material legal limitations and/or prohibitions and because the collateral provided by non-US entities may be subject to material legal and/or practical limitations resulting in security over much less than "all assets" of the relevant non-US entity, leading to some unexpected results for senior secured lenders in a Yankee Loan deal.

Specifically, the claims of the creditors of such incremental, incremental equivalent or ratio debt, even if junior secured or unsecured, may rank equally, or in some cases even effectively senior, to the guarantee claims of the senior secured lenders who provided the main senior secured credit facilities.

This may be because incremental, incremental equivalent or ratio debt is subject to less stringent guarantee limitations or prohibitions than the guarantee limitations or prohibitions applicable to the senior secured acquisition finance facilities incurred to pay for the acquisition of the applicable European or Asian Borrower group or it may be because the transaction security provided by the applicable European or Asian Borrower group is not fully comprehensive, resulting in a larger pool of unsecured assets, the value of which gets shared equally between senior secured creditors, junior secured creditors and unsecured creditors with equal ranking debt claims.

Additionally, for reasons detailed in the structuring considerations section above, in the event of a restructuring accomplished by means of a distressed disposal and release of claims, providers of incremental, incremental equivalent or ratio debt may not be subject to the contractual standstills or release provisions provided under a European or Asian intercreditor agreement.

"Grower" baskets

It is now common to include "grower" baskets in US deals (including Yankee Loans) set by reference to the greater of a fixed amount and either a percentage of Consolidated Total Assets (more common) or a percentage of Consolidated EBITDA (now becoming much more common in both US and European deals). These have tended to be more generous in US deals and are of particular relevance for intercompany transaction baskets – typically in US deals, unlimited intercompany transactions (investments and asset transfers) are permitted between borrowers/guarantors but depending on location of certain borrowers/guarantors (where either guarantee or security coverage may be weak) this may give rise to credit support value leakage concerns in Yankee Loan deals for European or Asian borrower groups. Historically, a "grower" did not apply to the "fixed" or "free and clear" components for Incremental debt baskets or Available Amount baskets but that is now starting to creep into deals on both sides of the Atlantic.

"Available Amount" (or "Builder") basket for investments and acquisitions, restricted payments and restricted junior debt repayments

This basket builds with Consolidated Net Income (typically 50% CNI minus 100% losses) or a percentage of Retained Excess Cash Flow, plus certain equity contributions and returns on investments made using the Available Amount basket – this basket may be applied subject to certain Event of Default blocker conditions and subject to *pro forma* compliance with a leverage-based incurrence ratio condition (although leverage-based incurrence ratio condition protection may be limited, or even excluded, in some deals). At the time of writing, US deals have tended to set the incurrence ratio condition more loosely than comparable European deals (while the extent of any Event of Default blocker conditions has varied).

Additional unlimited baskets for permitted investments and acquisitions, restricted payments and restricted junior debt repayments

These baskets allow for application of unlimited amounts subject to (in some cases) an Event of Default blocker condition and *pro forma* compliance with an incurrence ratio condition (at the time of writing the range varies from at least 0.5x inside to at least 2.0x inside closing date total net leverage, depending on the intended application/usage) rather than a fixed cap amount. These have become fairly common in US top-tier sponsor deals (including Yankee Loan deals) but have yet to be seen with any frequency in European covenant-lite or covenant-loose deals or Asian syndicated deals.

Investments and acquisitions

It is now typical not to include a fixed cap in US deals (including Yankee Loan deals) but still typical to include a non-guarantor cap (or in some deals a Guarantor Coverage test requirement, more similar to European deals, or a combination of the two concepts). In Yankee Loan deals with little or no US credit support, and weak guarantee/security credit support packages in non-US locations, this normally is the subject of far more detailed negotiation between lenders and borrowers, with tighter baskets and sometimes fixed caps in place of incurrence ratio conditions.

To enable borrower groups to undertake additional acquisitions on a "Sungard" or "certain funds" conditionality basis, while keeping in place existing capital structure, the market is now seeing:

- Limited Conditionality Acquisitions (i.e. acquisitions that are not conditioned on obtaining financing) – satisfaction of conditions to acquisitions and other events occurring now tested at time of acquisition (including *pro forma* debt incurrence) – what happens in relation to further *pro forma* incurrence testing with respect to other transactions in the time between the Limited Conditionality Acquisition test (if tested at signing) and the consummation of that acquisition is subject of negotiation.
- Limit on requirements with respect to Event of Default blocker conditions or bring down of representation conditions.

We expect that this US flexibility will increasingly be introduced into European and Asian deals.

Asset Disposals

In US deals (including Yankee Loan deals), this is now commonly an unlimited basket, subject to no Event of Default blocker condition (although even this protection is excluded in some deals), and provided that 75% of consideration is cash (or designated non-cash consideration), sale is for fair market value and net sale proceeds are applied and/or reinvested in accordance with mandatory prepayment asset sale sweep provisions. By contrast, it is still more common in European and Asian deals to include some form of fixed cap, although European and Asian deals do tend to include more extensive basket carve-outs for certain identified assets (such as the sale of "non-core" assets following the acquisition of new businesses).

Call Protection

In nearly all US deals (including Yankee Loan deals), it is now customary to include "soft call" protection for the benefit of institutional investors but this protection only applies on a limited basis in relation to repricing transactions and it has become common to carve-out certain exceptions:

- "soft call" protection will not apply in relation to any refinancing or repricing transaction triggered by a Change of Control transaction (or in many cases now, if triggered by an IPO, "transformative" acquisition or 3rd party investment transaction); and
- "soft call" protection will not apply where "primary purpose" is not to reduce yield.

Following the expansion in depth and liquidity in the European institutional investor base, European deals are now starting to include "soft call" protection.

European covenant-lite and covenant-loose

In order to remain competitive, European (and to a lesser extent Asian) lenders have been forced to agree to more flexible covenant packages for borrower groups to retain business and to avoid such borrower groups choosing to do a Yankee Loan transaction and syndicate their debt financing in the US market.

European covenant-lite deals tend to follow the same approach as US covenant-lite deals with respect to financial maintenance covenants. However, although negative covenants are likely to be less restrictive than in a traditional European leveraged financing, (1) they are unlikely to include full US-style covenant-lite incurred-based flexibility, and (2) whether the loan is considered covenant-lite is driven purely by the lack of any financial maintenance covenant protection.

We do expect, however, that over time there will continue to be more convergence between the US and European markets, because borrower groups will continue to seek to maximise flexibility through adoption of "best in class" on both sides of the Atlantic, and cross-pollination (i.e. the same underwriting banks and sometimes the same investors will already be familiar with concepts from US or European deals) will make it easier to import new terms into the respective leveraged loan markets. It may take a little longer for convergence to occur to the same degree with Asian markets (because of the smaller volume of Yankee Loan deal flow).

By the same token, in reaction to the changes that have been taking place in the European market as a result of the increase in Yankee Loan deals, we are starting to see more European covenant-loose deals being done. Covenant-loose deals typically include less than the "full suite" of three financial maintenance covenants (ignoring capex covenants) in relation to both term loans and revolving facilities. Some deals have included one leverage covenant only while others have also included an interest cover covenant but no cashflow cover covenant.

Conditionality

Documentation Principles vs. Interim Facilities and "Full Docs"

In acquisition financing, the risk that the purchaser in a leveraged buyout will not reach agreement with its lenders prior to the closing of the acquisition (sometimes referred to as "documentation risk") is generally not a material concern (or at least is a well understood and seen to be manageable concern) of sellers in private US transactions. Under New York law, there is a general duty to negotiate the terms of definitive documentation in good faith and US leveraged finance commitment documents also typically provide that the documents from an identified precedent transaction will be used as the basis for documenting the definitive credit documentation, with changes specified in the agreed term sheet, together with other specified parameters. These agreed criteria are generally referred to as "documentation principles" and give additional comfort to sellers in US transactions that the documentation risk is minimal.

In European and Asian deals, documentation risk is generally a much greater concern for sellers. This can be explained in part by the fact that there is no similar duty imposed to negotiate in good faith under English law, the typical governing law for European and Asian leveraged financings (and under English law, an agreement to agree is unenforceable). Therefore, to address seller concerns about documentation risk in European and Asian deals, lenders typically agree with purchasers to enter into fully negotiated definitive credit documentation prior to the submission of bids, or to execute a short-form interim facility agreement under which funding is guaranteed to take place in the event that the lenders and the borrower are unable to agree on definitive credit documentation in time for closing, with the form of the interim facility pre-agreed and attached as an appendix to the commitment documents (or in some more recent cases, actually executed at the time of bid submission).

Over time, it will be interesting to see if European sellers (and their advisors) become more comfortable with addressing documentation risk by relying on documentation principles, and follow the US practice for commitment documentation, given that the governing law of the finance documents, not the jurisdiction of the seller, is the key factor in evaluating documentation risk. However, until this point becomes more settled, consideration will need to be given to the appropriate form of financing documentation and the potential timing and cost implications that may arise as a result.

SunGard vs. Certain Funds

Certainty of funding for leveraged acquisitions is a familiar topic on both sides of the Atlantic and in Asia. It is customary for financing of private companies in Europe and Asia to be provided on a private "certain funds" basis, which limits the conditions to funding or "draw stops" that lenders may benefit from as conditions to the initial funding for an acquisition. Bidders and sellers alike want to ensure that, aside from documentation risk, there are minimal (and manageable) conditions precedent to funding at closing (with varying degrees of focus by the bidder or seller dependent on whether the acquisition agreement provides a "financing out" for the bidder – an ability to terminate the acquisition if the financing is not provided to the bidder).

Similar concerns exist in the US market, which has developed a comparable, although slightly different approach to "certain funds". In the US market, these provisions are frequently referred to as "SunGard" provisions, named after the deal in which they first appeared. In both cases, the guiding principle is that the conditions to the initial funding should be limited to those which are in the control of the bidder/borrower, but as expected there are some familiar differences which are relevant to consider in the context of a Yankee Loan.

The first key difference is that in the US market, lenders typically benefit from a condition that no material adverse effect with respect to the target group has occurred. However, the test for whether a material adverse effect has occurred must match exactly to that contained in the acquisition agreement. With this construct, the lenders' condition is the same as that of the buyer, however if the buyer did want to waive a breach of this condition the lenders would typically need to consent to this. In European and Asian private "certain funds" deals, the lenders typically have no material adverse effect condition protection, although they usually would benefit from a consent right to any material changes or waivers with respect to the acquisition agreement (the same protection would also be present in deals based on "SunGard" conditionality). Therefore, if a European or Asian buyer wished to waive a material adverse effect condition that it had the benefit of in an acquisition agreement, it is likely that this would be an action that lenders would need to consent to.

The second key difference is that in the US market, lenders typically benefit from a condition that certain key "acquisition agreement representations" and certain key "specified representations", in each case made with respect to the target, must be true and correct (usually in all material respects), although in the case of such "acquisition agreement representations" these must be consistent with the representations made by the target in the acquisition agreement and this condition is only violated if a breach of such "acquisition agreement representations" would give the buyer the ability to walk away from the transaction. By contrast, in the European and Asian markets, no representations with respect to the target group generally need to be true and correct as a condition to the lenders' initial funding. The only representations which may provide a draw stop to the initial funding are typically core representations with respect to the bidder. Similar to the material adverse effect condition, while these appear different on their surface, in most European and Asian transactions if a representation made with respect to the target group in the acquisition agreement was not correct, and as a result the buyer had the ability to walk away from, or not complete, the transaction, waiver of this condition would likely require the consent of the lenders under a European or Asian "certain funds" deal.

Much like the comparison between documentation principles v. full documents (or an interim facility), a comparison between SunGard *v*. European "certain funds" reveals that notwithstanding the slightly different approaches taken to these issues on each side of the Atlantic, the substantive outcomes are similar. Thus far, Yankee Loans have approached these issues on a case by case basis, with a slight majority so far favouring the US approach to these issues.

Diligence – reliance or non-reliance

Lenders in US leveraged finance transactions will be accustomed to performing their own primary diligence with respect to a target group, and their counsel will perform primary legal diligence with respect to the target group. Frequently this may include the review of diligence reports prepared by the bidder's advisors and/or the seller's advisors, which will be provided on a non-reliance basis and primary review of information available in a data room or a data site.

Lenders in European or Asian leveraged finance transactions will also be accustomed to performing their own diligence with respect to a target group with the assistance of their counsel, which will also frequently include the review of diligence reports prepared by advisors to the bidder and/or the seller. However, European and Asian lenders typically benefit from express reliance on these reports, which is also extended to lenders which become party to the financing in syndication.

In the context of a Yankee Loan, while the advisors to the bidder and/or seller may be willing to provide reliance on their reports for lenders, consideration will need to be given as to whether this is needed and/or desired. Lenders' expectations may also diverge in the context of a Yankee Loan which includes a revolving credit facility to be provided by European or Asian banks (likely relationship banks to the borrower or target group) as opposed to the US banks that initially arrange and underwrite the term loan facilities.

Conclusion

Ultimately, Yankee Loans can be seen as simply US Term Loan B tranches provided by institutional investors to European or Asian borrower groups. However, the fundamental differences between how a restructuring of US and European and Asian borrower groups is likely to occur and the "lost in translation" issues that have arisen and will continue to arise in the future caused by a confusion in differing market practices and the use of different terminology in New York law and English law transactions, means that greater care must be taken when structuring a Yankee Loan.

Endnotes

i. While it is possible in certain European and Asian jurisdictions to restructure through court-controlled processes that achieve a result similar to a Chapter 11 Case, this will depend entirely on the jurisdiction of the borrower(s) and material guarantors.

ii. Source: LCD's online Loan Market Primer, February 17, 2015.

iii. Source: S&P Capital IQ LCD Report, December 19, 2014.

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