

USA

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1 Overview

1.1 What are the main trends/significant developments in the lending markets in the United States?

The corporate lending markets in the United States are broad and deep. Market trends are often associated with certain segments of the lending markets, and market segmentation in the United States is based on a number of factors. These factors include: the size of the borrower (from so-called “large-cap” borrowers, to those in the “middle-market” to “small-cap”); the credit profile of the borrower (from investment-grade to below investment-grade or “leveraged”); the type of lender (banks, versus non-bank lenders, such as hedge funds, finance companies and insurance companies); the number of holders of the debt (from syndicated loans, to “club” and bilateral facilities); whether the loan is secured, and the relative positions of the lenders *vis-à-vis* one another (from senior unsecured, to senior secured, mezzanine and second-lien loans); the basis on which the loan is made and repayment is (hopefully) assured (from a company’s general credit rating, to cash flow loans, to asset-based loans); and the purpose of the loans (from acquisition finance, asset finance, to general working capital loans, to the development of specific projects). While there are trends within each of these market segments, there are also some broad trends which impact multiple segments. For example:

Low Interest Rates and the Search for Returns. The Federal Reserve announced in September 2012 that it would keep interest rates low through the end of 2015. This is an effort to boost economic growth and employment, which have been slack since the financial crisis, by making it cheaper for companies to borrow. This effort has helped to push yields on investment grade bank loans and bonds to near record lows. As a result, investors have sought higher returns, increasing demand for leveraged loans and high-yield bonds. This increase in demand has coincided with generally depressed levels of M&A activity, a driver for the supply of these assets. This imbalance of demand and supply has generally resulted in a spike in refinancings and repricings at lower rates and dividend recapitalisations. It has also resulted generally in higher leverage levels, lower yields and weaker covenants and structures for lenders and investors (helpful, of course, for borrowers negotiating these transactions).

Certain Trends in Loan Documentation: “Convergence”, Covenant-Lite, etc. The same investors often invest in syndicated leveraged loans and high-yield bonds. While pricing on leveraged loans is generally lower than high-yield bonds, leveraged loans typically have floating rates compared to a bond’s fixed-rate (thus protecting against interest rates moving higher). Leveraged loans

typically have more restrictive covenants than high-yield bonds and are generally secured, so recoveries on leveraged loans in the case of default are considered better. Investors judge the relative values of each of these instruments on a company-by-company basis. With each of these asset classes “competing” with the other, many loans are taking on more and more bond-like characteristics, thus blurring the traditional distinctions. Some aspects of this so-called “convergence” of loans and bonds, as well as certain other documentation trends, are further described below.

The Return of Covenant-Lite. There has recently been an increase of what are commonly known as “covenant-lite” loans, which were popular before the financial crisis. In covenant-lite loans, the borrower generally pays a higher interest rate in exchange for less restrictive covenants and no financial maintenance covenants (similar to high-yield bonds). While financial maintenance covenants test the borrower on a periodic basis, covenant-lite loan agreements typically only include “incurrence” covenants (which test the borrower upon a specific activity). Covenant-lite loans are viewed as creating a risk of greater loss after default. With a covenant-lite loan, the first default is often a payment default, occurring long after a financial covenant default would have occurred. By that time, the borrower’s financial condition is likely to have deteriorated substantially. As of the writing of this chapter, covenant-lite loans are available only to strong borrowers and sponsors in the large corporate market and the upper-end of the middle-market. In addition, in deals that do provide financial covenants, it is becoming more common to set the covenant levels at more significant cushions to the borrower’s business model, making financial covenants less meaningful as an early-warning tool for lenders.

Equity Cures, Builder Baskets and Incremental Facilities. “Equity cures” have regained traction since the financial crisis and can now be seen in many large corporate and middle-market deals. An equity cure allows a borrower’s shareholders to make an additional equity investment in the borrower to cure breaches of its financial covenants. The specifics of an equity cure (the number of times it can be exercised, specific impact on financial covenants, etc.) are subject to negotiation. Loan agreements are also giving borrowers more flexibility around so-called “builder baskets” which provide the borrower with more alternatives for using its excess cash flow. Typically, borrowers are permitted to use builder baskets for capital expenditures, permitted investments and acquisitions, and in larger deals and for stronger sponsors, for equity distributions and repayment of subordinated debt. Non-committed incremental facilities have become standard in most middle-market transactions, and incremental facilities in large corporate loans offer borrowers more flexibility, permitting in many cases an uncapped amount of additional debt, so long as certain *pro forma* leverage ratios are

satisfied. Incremental facilities commonly contain most favoured nation (MFN) provisions, which permit the interest rate margin on the original loans to increase to maintain a certain level of closeness to the incremental loan (typically not more than a 50 bps differential). Some sponsor deals successfully eliminate or “sunset” MFN provisions after a specified period of time.

Prepayment Premiums. Consistent with bank loan and bond “convergence”, in the leveraged market “soft call” prepayment premiums have become increasingly common. Soft call payment premiums are payable when the borrower refinances or reprices an existing financing on better terms (better pricing). This feature benefits institutional investors who seek a relatively long stream of interest payments. “Hard call” premiums, which are premiums payable on any voluntary prepayments, are more often seen in middle-market deals than in large corporate deals.

Unrestricted Subsidiaries. The “unrestricted subsidiary” concept is consistent with features seen in bond indentures, and borrowers in large corporate and middle-market deals have made some headway in negotiating for these provisions. These provisions typically exclude specified subsidiaries from coverage in the representations, covenants and events of default, thus allowing a borrower to use an unrestricted subsidiary to incur indebtedness and liens or make investments without being subject to loan agreement restrictions. In effect, the lender loses the ability to monitor or restrict the unrestricted subsidiaries. The trade-off is that all financial attributes of the unrestricted subsidiaries are excluded from the loan agreement provisions (including any benefit the borrower may have otherwise realised from cash flow generated by such subsidiaries for purposes of loan agreement financial ratios).

Commitment Papers. With respect to commitment papers for equity sponsors in acquisition financings, so-called “SunGard” provisions continue to be standard (SunGard provisions help equity sponsors who rely on financings to fund an acquisition to compete with strategic buyers who do not need such financing, by aligning the conditionality of lending commitments closely to conditions in the acquisition agreement). In terms of commitment papers generally, “market flex” provisions (used to ensure a successful syndication and allow underwriters to sell down exposure) have had less impact on deals in this borrower-friendly market, with deals often being over-subscribed.

The Regulatory Environment: Pushing the Needle in the Opposite Direction? While the Federal Reserve has kept interest rates low in an effort to boost economic activity, other federal regulators with a mandate to protect the US economy from excessive risk-taking associated with the financial crises have, at least in the opinion of some commentators, pushed the needle in the opposite direction by increasing the cost of making loans. For example, the “Guidance on Leveraged Lending” proposed by federal regulators would apply to all financial institutions supervised by agencies that are substantively engaged in leveraged lending activities. The guidance outlines high level principles to assist institutions in establishing safe and sound leveraged finance activities, and will likely significantly increase lending costs. “Risk retention rules” and the “Volker Rule” could seriously impact CLO managers and banks that structure, warehouse and make markets in CLOs. In an effort to fill the government tax coffers, the Foreign Account Tax Compliance Act (“FATCA”), which partially goes into effect on January 1, 2013, is a major revamp of the US withholding tax system, imposing a new 30% withholding on certain payments from foreign lenders that fail to enter into an agreement with the IRS to identify and report specified information with respect to US account holders and investors. This sweeping law could have a significant impact on loan payments and receipts.

The Courts: The TOUSA Decision. In the US, few court cases have spread such a broad concern among lenders in recent years as the TOUSA decision. TOUSA obtained loans from lenders supported by upstream secured guaranties and used the proceeds of the loans to repay existing indebtedness and to settle related litigation (see questions 2.1 and 2.2 below). In a much criticised 2009 decision, the Bankruptcy Court not only avoided the guaranties and liens provided by the subsidiaries to the new lenders, but also ordered that the re-financed lenders repay to the TOUSA estate over \$400 million received in settlement of their litigation with TOUSA. On appeal in 2011, the District Court overturned much of the Bankruptcy Court’s ruling (to the relief of lending markets). Then, in an unanticipated move, in May 2012 the Eleventh Circuit reversed the District Court decision in significant part. The decision upends what had been previously considered to be established notions of market practice when dealing with fraudulent transfer issues, and appears to put increased responsibility on lenders lending into or refinancing distressed companies (including on the part of lenders being re-financed) especially if credit support is being provided by subsidiaries of a borrower.

European Borrowers and US Lenders. With the ongoing turmoil in the Eurozone and the impact on European banks, there has been an increase in the number of European borrowers seeking financing from US lenders. As a result, lenders in the US have become increasingly familiar with European documentation and structure norms. For example, in contrast to the SunGard language in commitment papers relied on in US deals, European acquisition financings typically use a “certain funds” model that requires fully negotiated loan documents at the time an acquisition agreement is entered into (compared to the US model of requiring only a commitment letter at this stage). Collateral packages also may differ: European mezzanine lenders expect to be secured, whereas US mezzanine lenders are typically unsecured. But this security often comes with a cost, as European mezzanine lenders often are *structurally* subordinated to senior lenders. In US deals, mezzanine lenders are often only *contractually* subordinated. Documentation and deal structures also take into account the difference in secured transaction laws and bankruptcy laws in the US and Europe. European-based deals rely more on underlying intercreditor agreements and out-of-court restructurings since there is no pan-European insolvency regime.

Innovations in the Loan Markets: The Unitranche Facility. Given the depth and breadth in the loan markets in the US, many loan market innovations originate or are further developed here (consider, for example, the development of a sophisticated secondary trading market, certain mezzanine and second-lien structures, the securitisation of loans and CLOs). One innovation that has become increasingly popular is the so-called “unitranche” facility. Unitranche loans combine what would otherwise be separate first/second-lien or senior/mezzanine facilities into a single debt instrument, where all the debt is subject to the same terms, and with a blended interest rate. Lenders in unitranche facilities often enter into a so-called “agreement among lenders” which legislates payment priorities among lenders in a manner that may not be visible to the borrower. One advantage of unitranche loans for a borrower is speed and certainty of closing (important in a competitive acquisition process), since negotiation of an intercreditor agreement is not a condition to funding. Another advantage for the borrower is the simplicity of decision-making during the life of the loan since there is no “class voting” from the perspective of the borrower (though the “agreement among lenders” may impact voting issues in ways not visible to the borrower). The use of these facilities has so far been generally restricted to the

middle-market, and lenders of unitranche loans are typically finance companies and hedge funds (and not banks).

1.2 What are some significant lending transactions that have taken place in the USA in recent years?

Given the large number of transactions in the US corporate loan markets, it is difficult to differentiate certain lending transactions as being more significant than others. Any such comparison necessarily excludes transactions for which documentation is not publically available and therefore favours large corporate deals filed with the SEC compared to those in the middle-market, where much loan product innovation takes place. Nevertheless, some transactions that illustrate some of the concepts discussed above include: *Covenant-Lite*: Automatic Data Processing (June 20, 2012); Bristol-Myers Squibb Company (July 30, 2012); and United Technologies Corporation (April 24, 2012); *Unrestricted Subsidiaries*: 99¢ Only Stores (January 13, 2012); and Memorial Resource Development LLC (July 13, 2012); Incremental Facilities: Kinetic Concepts, Inc. (November 4, 2011); and *European Borrowers*: Seagate Technology Public Limited Company (January 18, 2011); Sensata Technologies (May 12, 2011); and LyondellBasell Industries (May 24, 2012).

2 Guarantees

2.1 Can a company guarantee borrowings of one or more other members of its corporate group (see below for questions relating to fraudulent transfer/financial assistance)?

Generally, yes. In the US, guarantees are commonly referred to as one of three types: (a) “downstream” guarantees, whereby a parent company guarantees the debt of a subsidiary; (b) “upstream” guarantees, whereby a subsidiary guarantees the debt of a parent; and (c) “cross-stream” guarantees, whereby a subsidiary guarantees the debt of a “sister company”. Generally, “upstream” and “cross-stream” guarantees may be subject to increased scrutiny given enforceability issues in the context of a bankruptcy, as further described below.

2.2 Are there enforceability or other concerns (such as director liability) if only a disproportionately small (or no) benefit to the guaranteeing/securing company can be shown?

First, as a matter of contract law, some “consideration” (bargained-for contractual benefit to the guarantor) must be received for the guarantee to be enforceable, though this contract law threshold is typically easy to meet.

As a matter of insolvency law, certain types of enforceability issues arise in the context of a bankruptcy. These issues are analogous to, but not the same as, contractual concepts of “consideration”. With downstream guarantees, there is typically little concern, since the parent will indirectly realise the benefit of a loan through the value of its equity ownership of the subsidiary (unless the subsidiary is already, or is rendered, insolvent). However, “upstream” and “cross-stream” guarantees should be subject to increased analysis since the benefit to the guarantor is less evident.

For example, a guarantee or other transaction may be voided by a bankruptcy court in the US if it is found to be a “fraudulent transfer”. Very generally, under the federal Bankruptcy Code, a guarantee may be considered a fraudulent transfer if, at the time the

guarantee is provided, (a) the guarantor is insolvent (or would be rendered insolvent by the guarantee), and (b) the guarantor receives “less than reasonably equivalent value” for the guarantee. (Note that both prongs of the test must occur in order for the guarantee to be voided as a fraudulent transfer; if the guarantor receives “less than reasonably equivalent value” though is nevertheless solvent at the time the guarantee is provided (after giving effect to the guarantee), then the guarantee should not be voided as a fraudulent transfer.) As mentioned above, in a downstream guarantee context, the parent would more likely receive “reasonably equivalent value”, therefore fraudulent transfer is less of a concern for these types of guarantees. In addition to the federal Bankruptcy Code fraudulent transfer test, under state laws there exist similar fraudulent transfer statutes and a federal bankruptcy trustee may also use these tests to void the guarantee in a bankruptcy.

Loan documentation will often provide for solvency representations from borrowers and guarantors in order to address fraudulent transfer concerns. In some high-risk transactions (such as acquisition loans or loans provided so the borrower can make a distribution to shareholders), a third party is required to provide a solvency opinion in order to provide protection from fraudulent transfer attack, though the more common practice today is for lenders to do their own analysis given the expense of such outside opinions. The market practice and documentation norms in connection with subsidiary and affiliate guarantees are in somewhat of a state of flux at this time in light of the recent TOUSA decision (see question 1.1).

Under relevant corporate law, if a guarantee or similar transaction is structured in such a way that it would be tantamount to a distribution of equity by a company while the company is insolvent (or is rendered insolvent), or would impair the company’s capital, the transaction may be improper under the corporate law and could result in director liability. See also question 2.3 below for a general discussion of corporate power issues.

2.3 Is lack of corporate power an issue?

Entity power to enter into a guarantee is generally governed by the corporation (or equivalent) law in the state in which the company is organised, as well as the company’s charter and bylaws (or equivalent documentation).

For corporations, the corporation law of most states provides a broad range of permitted business activities, so few activities are considered to be *ultra vires* or beyond the power of a corporation (note that certain special purpose or regulated entities, such as banks, insurance companies, and utility companies, may be subject to additional statutes which impact corporate power). In a lending context, however, many state corporation statutes limit the power of subsidiaries to guarantee the indebtedness of a corporate parent or a sister company, and a guarantee may be *ultra vires* if not in furtherance of the guarantor’s purposes, requiring analysis of the purpose of the guarantee and the benefit to the guarantor. If the benefit to the guarantor is intangible or not readily apparent, this may provide additional concern. Many corporate power statutes, however, provide safe harbours for certain types of guarantees, irrespective of corporate benefit, including if the guarantor and the borrower are part of the same wholly-owned corporate family, or if the guarantee is approved by a specified shareholder vote, for the guarantor entity. For limited liability companies, state statutes are usually more generous, with a limited liability company generally able to engage in any type of legal activity, including entering into guarantees, unless the charter provides otherwise.

In lending transactions in the US, the analysis that a company has

the corporate or other requisite power to enter into a guarantee is often provided in a legal opinion provided by the guarantor's internal or external counsel (though these opinions will typically assume away the tough factual issues, such as the level of corporate benefit).

2.4 Are any governmental or other consents or filings, or other formalities (such as shareholder approval), required?

In addition to having "corporate power" (or equivalent power for other types of entities) to enter into a guarantee, the guarantee must be properly authorised, which generally means that the procedural rules of the corporation, as set forth in its charter or by-laws, must be followed and that the stockholders or the governing board take the proper measures to authorise the transaction. These procedures are customary and also typically covered in a legal opinion provided by the guarantor's counsel.

One situation that requires special attention in a guarantee context is when a guarantor is providing an upstream or cross-stream guarantee, and the guarantor has minority shareholders. In this context, often the consent of the minority shareholders would be required in order for the guarantee to be provided in order to address fiduciary duty concerns.

Generally, no governmental consents, filings or other formalities are required in connection with guarantees (though, as noted above, certain special purpose companies and regulated entities may be subject to additional requirements).

2.5 Are net worth, solvency or similar limitations imposed on the amount of a guarantee?

Yes, please see question 2.2.

2.6 Are there any exchange control or similar obstacles to enforcement of a guarantee?

Generally, no. Though there are a few other issues worth mentioning that do not relate to "enforcement" *per se*. For example, there may be withholding tax issues if the payment is to a foreign lender (please see question 6.1).

Also, there may be US tax consequences for a US borrower resulting from the involvement of any foreign subsidiary guaranteeing the debt of a US borrower. Under US tax rules, such a guarantee could be construed to be a "deemed dividend" from the foreign subsidiary to the US parent and subject to US tax. This tax also may apply if collateral at the foreign subsidiary is used to secure the loan to the US parent. The US parent may also be subject to tax consequences if it pledges more than 66% of the stock of a first-tier foreign subsidiary. These types of tax issues are important to consider when structuring a transaction with credit support from foreign subsidiaries of US companies. There are many ways to address these types of issues, including having the loans made directly to the foreign subsidiary.

3 Collateral Security

3.1 What types of collateral are available to secure lending obligations?

A wide variety of assets (including land, buildings, equipment, inventory, accounts, contract rights, investment property, deposit

accounts, commercial tort claims, etc.) are available for use as security for loan obligations with many of the most common types of collateral described more fully below. Assets used as security are often divided into two broad categories: (a) "personal property" which generally refers to property other than real property (land and buildings); and (b) real property.

The Uniform Commercial Code ("UCC") provides a well-developed and predictable framework for providing security interests in a wide variety of personal property assets. The UCC is a state law statute rather than a federal one, but the UCC has been adopted by all 50 states in the US and the District of Columbia, with only a few non-uniform amendments of significance.

Under the UCC, when a security interest "attaches", it becomes enforceable as a matter of contract by the lender against the borrower. "Attachment" typically occurs when credit is extended to the borrower, the borrower has ownership or other rights in the collateral in which to grant a security interest, and the borrower signs and delivers to the lender a written security agreement describing the collateral.

After attachment, the security interest must be "perfected" by the lender in order for the lender's security interest to have priority over the rights of an unsecured creditor who later uses judicial process to obtain lien on the collateral. Since a federal bankruptcy trustee has the same status as a state law judicial lien creditor under U.S. law, a bankruptcy trustee will be able to set aside the security interest if the security interest is not perfected.

The method of perfecting a security interest under the UCC depends on the type of collateral in question. The most common method of perfecting a security interest is by "filing" a financing statement in the appropriate state filing office. The UCC provides specific rules for where to file a financing statement, with the general rule that the filing takes place in the jurisdiction where the borrower is located. A borrower organised under a state law in the United States as a corporation, limited partnership, limited liability company or statutory trust is considered to be located in the state in which it is organised. The filing contains only brief details including the name of the borrower, the name of the secured party and an indication of the collateral, and the filing fee is generally fairly nominal. Security interests in some collateral may be perfected by "possession" or "control" (including directly-held securities, securities accounts and deposit accounts). A security interest in certain collateral may be perfected by more than one method.

If two or more lenders have perfected security interests in the same collateral, the UCC provides rules for which lender has "priority" over the other security interest. This is usually determined by a "first-in-time" of filing or perfection rule, but there is a special rule for acquisition finance ("purchase-money") priority and special priority rules also apply to certain collateral (e.g., promissory notes, investment securities and deposit accounts) if a security interest is perfected by possession or "control".

In addition, security interests in certain types of personal property collateral may to some extent be governed by federal statutes and pre-empt the UCC rules. For example, the perfection of a security interest in an aircraft is governed by the Federal Aviation Act and the perfection of a security interest in a ship above a certain tonnage is governed by the federal Ship Mortgage Act.

The requirements for taking a security interest in real property (referred to as a "mortgage" or "deed of trust" in the US) are determined by the laws of the state where the real property is located. Typically the office in which to file the mortgage or deed of trust is in the county of the state where the land is located. These statutes are fairly similar from state to state, but less consistent than the rules for personal property. As a result, mortgage documents

from state to state appear quite different, while security agreements with respect to personal property (governed by the more consistent UCC of each state) are more uniform. Lenders often obtain a title insurance policy in order to confirm the perfection and priority of their security interest in real property.

A security interest in fixtures (personal property that permanently “affixes” to land) is generally perfected by filing in the place where the real property records are filed. A security interest in fixtures may be perfected under the UCC or under the local real estate law.

3.2 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

In general, a single security agreement can cover all UCC personal property which is taken for security as a loan, no matter where the personal property is located.

With respect to real property, generally a separate mortgage or deed of trust document is used for each state where real property is located, given that the mortgage document is typically governed by the laws of that particular state.

3.3 Can collateral security be taken over real property (land), plant, machinery and equipment? Briefly, what is the procedure?

Yes. Please see question 3.1.

3.4 Can collateral security be taken over receivables? Briefly, what is the procedure? Are debtors required to be notified of the security?

Yes. Receivables are considered personal property, and a security interest in the receivables granted under a security agreement would typically be perfected by filing a financing statement in the appropriate filing office. If the receivable is evidenced by a promissory note or bond or by a lease of or loan and security interest in specific goods, the receivable may also be perfected by the lender’s possession or “control”. Debtors on the receivables are not required to be notified of the security interest in order for perfection to occur.

The security agreement can grant a security interest in future receivables. An already filed financing statement will be effective to perfect a security interest in a future receivable when it arises.

3.5 Can collateral security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes. A security interest granted under a security agreement in a deposit account as original collateral must be perfected by control (not by filing). To obtain control of the deposit account, a secured lender typically enters into a control agreement with the borrower and the institution that is the depository bank by which the bank agrees to follow the lender’s instructions as to the disposition of the funds in the deposit account without further consent of the borrower. Many depository banks have forms of control agreements which they will provide as a starting point for negotiations. (However, if the secured lender is also the depository bank or the lender becomes the depository bank’s customer on the deposit account, control is established without the need for a control agreement to perfect the security interest.)

3.6 Can collateral security be taken over shares in companies incorporated in the USA? Are the shares in certificated form? Can such security validly be granted under an English law governed document? Briefly, what is the procedure?

Yes. Companies are typically incorporated under the laws of individual states in the US, and usually not under federal law. Shares may be issued in either certificated or uncertificated form.

A security interest may be created by either a New York law or English law-governed security agreement. If the security agreement is governed by English law, the UCC in New York requires that the transaction bear a reasonable relationship to England for the choice of law clause to be enforceable. (Please also see question 7.1 as to the extent a court in New York will enforce a contract that has a foreign governing law.)

In general, a security interest in such directly-held shares can be perfected either by filing or by control, though perfection by control has priority. The law governing perfection of such security interest in certificated securities depends on whether perfection is achieved by filing (location of debtor) or by control (location of collateral).

If the shares are credited to a securities account at a bank or broker and are therefore indirectly held, a borrower’s interest in the securities account can be perfected either by filing or control. Once again, perfection by control has priority. The law governing perfection of a security interest in a securities account depends on whether perfection is achieved by filing (location of debtor) or by control (location of bank or broker as determined usually by the law governing the securities account relationship).

3.7 Can security be taken over inventory? Briefly, what is the procedure?

Yes. Please see question 3.1. A security interest may be granted under security agreement and may be perfected by the filing of a financing statement in the appropriate UCC filing office. Perfection may also be achieved by possession, though this method is seldom practical from a secured lender’s perspective.

The security agreement can grant a security interest in future inventory. An already filed financing statement will be effective to perfect a security interest in a future inventory when it is created or acquired.

3.8 Can a company grant a security interest in order to secure its obligations (i) as a borrower under a credit facility, and (ii) as a guarantor of the obligations of other borrowers and/or guarantors of obligations under a credit facility (see below for questions relating to the giving of guarantees and financial assistance)?

Yes to both (i) and (ii). Note that with respect to item (ii), a guarantor would be subject to the same fraudulent transfer analysis discussed in question 2.2.

A security agreement may also secure obligations relating to future loans. An already filed financing statement perfecting a security interest securing existing loans will be effective to perfect a security interest in a future loan when the loan is made.

3.9 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets?

With respect to personal property governed by the UCC, and the

filing of financing statements, there are typically no material costs and UCC filing fees are usually minimal.

With respect to real property, there may be significant recording taxes and fees. These taxes and fees will depend on the state and local laws involved. A number of practices are used in loan transactions in an attempt to minimise such costs. For example, in the case of refinancings, lenders may assign mortgages rather than entering into new mortgages; and in the case of mortgage tax recording states, lenders may limit the amount secured by the mortgage, so that the mortgage tax payable is set at a level commensurate with the value of the property as opposed to the overall principal amount of the loans.

3.10 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Please see question 3.9. In terms of a time-frame, UCC personal property security interests may be perfected in a matter of days. Real property security interests typically take longer, though they can usually be completed in a couple of weeks.

3.11 Are any regulatory or similar consents required with respect to the creation of security?

Generally no, except in the case of certain regulated entities where consent of the regulatory authority may be required for the grant or enforcement of the security interest.

Also, please see question 2.6 for a quick summary of tax issues that may arise in connection with foreign subsidiaries providing guarantees or collateral to secure loans to US borrowers.

3.12 If the borrowings to be secured are under a revolving credit facility, are there any special priority or other concerns?

Under the UCC, many traditional concerns under revolvers have been addressed by the “first to file or perfect” rule, though lenders should be aware of certain priority issues. For example, with respect to secured creditors who each have perfected security interests in UCC collateral, as stated previously certain “purchase-money” security interests and security interest in certain collateral perfected by possession or control may obtain over a security interest perfected merely by the filing of a financing statement. In addition, tax liens and some other liens created outside of the UCC may obtain priority over a UCC perfected security interest. Judgment liens may pose a priority problem for future advances, and tax liens may pose a priority problem for some after-acquired property and future advances. Otherwise, under the UCC, the first secured creditor to “file or perfect” has priority.

With respect to real property, the matter is less clear. As a general matter, absent special legislation in the state, future loans may not have same priority as loans advanced when the mortgage or deed of trust is recorded if there is an intervening mortgage, deed of trust or lien recorded before the future loan is made. Accordingly, a close review of state rules and individual state documentary requirements is required in order to ensure priority.

3.13 Are there particular documentary or execution requirements (notarisation, execution under power of attorney, counterparts, deeds)?

With respect to UCC collateral, the documentation requirements are

spelled out clearly in the UCC and the requirements generally are straightforward. No notarisation is required. Under prior versions of the UCC, the debtor was required to sign a written security agreement, though as the world moves away from paper and into electronic media, the model UCC, including the UCC as adopted in New York, now requires the debtor to “authenticate a record” that may include an electronic record. Nevertheless, most lenders in corporate loan transactions still generally require a written security agreement. With respect to real property collateral, the documentary and execution requirements tend to be more traditional by looking to a writing, but various law reform efforts are underway to permit electronic mortgages and deeds of trust and electronic recording of mortgages and deeds of trust. The requirements may vary significantly from state to state (for example, real property mortgages often require notarisation under state law, whereas this is generally not the case for UCC collateral).

4 Financial Assistance

4.1 Are there prohibitions or restrictions on the ability of a company to guarantee and/or give security to support borrowings incurred to finance or refinance the direct or indirect acquisition of: (a) shares of the company; (b) shares of any company which directly or indirectly owns shares in the company; or (c) shares in a sister subsidiary?

- (a) Shares of the company
- (b) Shares of any company which directly or indirectly owns shares in the company
- (c) Shares in a sister subsidiary

Generally no. There is no “financial assistance” law *per se* in the United States, but please see the discussion of fraudulent transfer and related principles described in question 2.2.

5 Syndicated Lending/Agency/Trustee/Transfers

5.1 Will the USA recognise the role of an agent or trustee and allow the agent or trustee (rather than each lender acting separately) to enforce the loan documentation and collateral security and to apply the proceeds from the collateral to the claims of all the lenders?

Yes. In loan documentation, the role is typically that of an “agent”, with bond documentation typically using a “trustee”.

5.2 If an agent or trustee is not recognised in the USA, is an alternative mechanism available to achieve the effect referred to above which would allow one party to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Not applicable, please see question 5.1.

5.3 Assume a loan is made to a company organised under the laws of the USA and guaranteed by a guarantor organised under the laws of the USA. If such loan is transferred by Lender A to Lender B, are there any special requirements necessary to make the loan and guarantee enforceable by Lender B?

In a syndicated lending transaction that includes a lender acting in an agency capacity, a guarantor typically would provide a guaranty

to the agent “for the benefit of the lenders under the loan agreement” (or some similar formulation). As such, it should not be necessary for a guarantor to sign the transfer (assignment) documentation in order to be bound, though the contractual language should be carefully reviewed for specific requirements. In the case of a bilateral loan, the contractual terms should also be closely reviewed, though it is advisable to obtain the guarantor’s consent to such assignment in any event.

6 Withholding, Stamp and other Taxes; Notarial and other Costs

6.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

With respect to the payment of interest to foreign lenders (other than a payment made to a US branch of a foreign lender that is engaged in business in the US), the general rule is that a withholding rate of 30% is applied to payments on interest and other amounts (other than principal). The US has in place bilateral treaties with many jurisdictions, which reduce or entirely eliminate this withholding tax for qualifying foreign lenders. A listing of these treaties is available at www.irs.gov. Generally, the proceeds of a claim under a guarantee or the proceeds of enforcing security are similarly taxed. Such withholding taxes may also be reduced by the so-called “Portfolio Interest Exemption,” which is generally not available to banks, but could be available to non-bank lenders such as hedge funds provided the requirements for the exemption are satisfied.

6.2 What tax incentives or other incentives are provided preferentially to foreign lenders?

The US federal government has generally provided few incentives targeted to foreign lenders (as there has not been a policy focus on promoting foreign loans into the United States), though please refer to the bilateral tax treaties and Portfolio Interest Exemption referred to in question 6.1. Note that under FATCA (mentioned in question 1.1), foreign institutions will be required to identify and report directly to the US IRS information about financial accounts held by US taxpayers, and failure to comply with FATCA may result in such foreign institutions being required to file a refund claim pursuant to the applicable bilateral tax treaty to recoup any amounts withheld under FATCA, and could result in the limitation of or denial of benefits under the tax treaty.

6.3 Will any income of a foreign lender become taxable in the USA solely because of a loan to or guarantee and/or grant of security from a company in the USA?

In general, a foreign lender, with no presence or activities in the US, does not become subject to US federal income taxation on its net income solely as a result of loaning to, or receiving a guarantee or grant of security from, a borrower or guarantor in the US. However, income derived specifically from a loan made to a US borrower (i.e., interest income) would be subject to gross-basis US taxation, typically at a rate of 30%, unless a treaty specified a lower rate, or the Portfolio Interest Exemption applied (please see question 6.1). Moreover, if a foreign lender has a presence or activities in the United States (for instance, employees or agents working out of, or a lending office located in, the US), the foreign lender could be viewed as being engaged in a trade or business in the US, and if so

would be subject to net-basis US taxation on any income deemed “effectively connected” with that trade or business.

6.4 What taxes apply to foreign lenders with respect to their loans, mortgages or other security documents, either for the purposes of effectiveness or registration? Will there be any other significant costs which would be incurred by foreign lenders in the grant of such loan/guarantee/security, such as notarial fees, etc.?

With regards to mortgages and other security documents, there are generally no taxes or other costs applicable to foreign lenders that would not also be applicable to lenders in the US (please see question 3.10 for a general summary of such costs).

6.5 Are there any adverse consequences to a company that is a borrower (such as under thin capitalisation principles) if some or all of the lenders are organised under the laws of a jurisdiction other than your own? Please disregard withholding tax concerns for purposes of this question.

If a corporation is “thinly capitalised,” and certain other factors are present, the US tax authorities may assert that instruments described as debt actually constitute equity for US tax purposes. The effect of such re-characterisation would be that payments on the instrument would not be deductible to the borrower for US federal income tax purposes (and could be subject to withholding in a manner different than interest payments). Moreover, even if treated as debt, US tax rules may deny a deduction (in whole or in part) for payments of interest by a thinly-capitalised borrower (i.e., a borrower with a debt to equity ratio in excess of 1.5 to 1) to a “related party” that is exempt from US federal income tax on the interest, taking into account any treaty-based reductions in tax rate. If the lenders are organised in a jurisdiction other than that of the borrower, this should not impact the thin capitalisation analysis itself, but, as mentioned above, may impact the withholding rate as well as any relevant “gross-up”.

7 Judicial Enforcement

7.1 Will the courts in the USA recognise a governing law in a contract that is the law of another jurisdiction (a “foreign governing law”)? Will courts in the USA enforce a contract that has a foreign governing law?

Generally, yes, so long as the choice of law bears a “reasonable relation” to the transaction and application of the foreign governing law would not be contrary to the public policy of the forum state.

On a related note, in connection with a choice of *New York* law as a governing law, a New York statute allows for New York law to be chosen by parties to a contract and, with certain exceptions, such choice of law will be given effect by New York courts if the transaction exceeds \$250,000 in value, regardless of whether the choice of New York law bears any reasonable relationship to the transaction. (The choice of New York as a forum is subject to additional requirements under the statute.) California has a similar statute.

7.2 Will the courts in the USA recognise and enforce a judgment given against a company by English courts (a “foreign judgment”) without re-examination of the merits of the case?

In most instances, yes. Despite the strong commercial ties between the United States and the United Kingdom, there is no international

treaty on reciprocal recognition and enforcement of court judgments (attempts to come to terms on a bilateral treaty in 1981 broke down over the negotiation of the final text). Nevertheless, the Uniform Foreign Country Money Judgments Recognition Act has been adopted by most states (including New York) and sets out basic rules of enforceability in connection with the enforcement of judgments between states in the United States, with “foreign-country” judgments treated in a similar manner as the judgment of a sister state. Generally, if a judgment is obtained in accordance with procedures compatible with United States due process principles, it will be recognised under the Uniform Act. There are many examples of English judgments having been enforced in New York courts.

7.3 Assuming a company is in payment default under a loan agreement or a guarantee agreement and has no legal defence to payment, approximately how long would it take for a foreign lender to (a) assuming the answer to question 7.1 is yes, file a suit against the company in a court in the USA, obtain a judgment, and enforce the judgment against the assets of the company, and (b) assuming the answer to question 7.2 is yes, enforce a foreign judgment in a court in USA against the assets of the company?

In New York, a court could rule almost immediately, perhaps within 3 to 6 months or less, with enforcement against assets of the company in New York beginning as soon as the judgment was entered (unless the defendant obtained a stay of enforcement). However, in practice, particularly if an opposing party appears and raises procedural or other issues, matters could take materially longer, up to a year or more.

Enforcement of a foreign judgment is generally pursued in New York by having the foreign judgment “confirmed”, with time frames similar to those mentioned above.

7.4 With respect to enforcing collateral security, are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction or (b) regulatory consents?

In a non-bankruptcy context, the timing and restrictions that apply to enforcement of collateral can vary significantly, depending on the type of collateral and relevant state law that applies. The UCC provides a great deal of flexibility in the rules governing disposition of personal property collateral (see question 3.1). The UCC generally permits either “private” or “public” sale, with the only real limitation on the power to sell that the secured party must “act in good faith” and in a “commercially reasonable manner”. Under the UCC, after the sale, the secured party generally may pursue the debtor for amounts that remain unpaid (the “deficiency”). The requirements with respect to real property collateral will vary significantly from state to state (and note in particular that in California, there may be limitations with respect to the ability of a creditor to collect on a deficiency if the creditor is secured with real property collateral). With respect to regulated entities (including certain energy and communications companies) enforcement may require regulatory approval.

In a bankruptcy context, enforcement would be restricted by the automatic stay (please see question 8.1).

7.5 Do restrictions apply to foreign lenders in the event of (a) filing suit against a company in the USA or (b) foreclosure on collateral security?

For the most part, distinctions will not be made between foreign and

domestic creditors in such proceedings. However, there are certain issues a foreign lender would need to consider in connection with such activities. For example, generally a foreign creditor will need to be authorised to do business in New York before availing itself as a plaintiff of the New York courts. In addition, foreign creditors may be subject to federal or state limitations on or disclosure requirements for the direct or indirect foreign ownership of certain specific types of companies or collateral, including in the energy, communications and natural resources areas.

7.6 Do the bankruptcy, reorganisation or similar laws in the USA provide for any kind of moratorium on enforcement of lender claims? If so, does the moratorium apply to the enforcement of collateral security?

Yes, please see question 8.1.

7.7 Will the courts in the USA recognise and enforce an arbitral award given against the company without re-examination of the merits?

The United States is party to the New York Convention. As set forth in the Convention, the Convention requires courts of contracting states to give effect to private agreements to arbitrate and to recognise and enforce arbitration awards made in other contracting states, subject to certain limitations and/or potential challenges. Note, however, that loan agreements under New York law generally do not include arbitration clauses.

8 Bankruptcy Proceedings

8.1 How does a bankruptcy proceeding in respect of a company affect the ability of a lender to enforce its rights as a secured party over the collateral security?

In the US, a bankruptcy proceeding may be initiated by either the company (debtor) itself or by its creditors. Once the proceeding is commenced, the relevant statutes in the United States (the “Bankruptcy Code”) provide that an “automatic stay” immediately occurs. This automatic stay is effectively a court order that prevents creditors from taking any actions against the debtor or its property, including enforcement actions against collateral. A creditor that violates the automatic stay could face severe penalties, including actual damages caused to the debtor and other creditors, as well as having its enforcement action declared void (punitive damages are typically limited to individual, rather than corporate debtors).

There are, however, a number of protections for a secured creditor who has properly perfected its liens and such liens are not subject to avoidance. First and foremost, upon a liquidation of a debtor, a secured creditor is paid its claim (up to the value of its collateral) prior to the payment of general unsecured creditors or, alternatively, it may receive its collateral back in satisfaction of its secured claim. Also, in the case of a reorganisation of a debtor, cash collateral cannot be used by the debtor without specific authorisation from the bankruptcy court or consent of the secured party, and in other circumstances the Bankruptcy Code mandates that a secured party’s interest in its collateral be “adequately protected”.

8.2 Are there any preference periods, clawback rights or other preferential creditors’ rights (e.g., tax debts, employees’ claims) with respect to the security?

In short, yes. A lender’s security interest could be voided as a

“preferential transfer” if it is provided to the lender within 90 days before a bankruptcy filing (or one year if the lender is an “insider,” or related party of the debtor) and as a result of the transfer the lender receives more than it would have otherwise received in the liquidation of the debtor. There are a number of exceptions to this rule, including where there has been a substantially contemporaneous exchange for new value. Please also see the discussion of “fraudulent transfers” in question 2.2.

There are certain claims that may have priority even over a properly perfected security interest, including tax liens, mechanics lines, and certain costs associated with the bankruptcy itself.

8.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

There are a number of entities that are either excluded from the Bankruptcy Code or for which special provisions of the Bankruptcy Code or other special legislation apply, including banks, insurance companies, commodity brokers, stockbrokers and government entities and municipalities. Municipalities and government-owned entities (but not states themselves) are eligible for relief under Chapter 9 of the Bankruptcy Code.

8.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of a company in an enforcement?

Yes. The UCC allows for so-called “self-help” remedies without first commencing a court proceeding. Note that the relevant provisions of a security agreement and governing law should be considered before exercising these types of remedies. These remedies typically can only be used so long as no “breach of the peace” would occur. Subject to the above, the market generally accepts these types of remedies for collateral, such as bank accounts and certificated securities.

9 Jurisdiction and Waiver of Immunity

9.1 Is a party's submission to a foreign jurisdiction legally binding and enforceable under the laws of the USA?

Generally, yes.

9.2 Is a party's waiver of sovereign immunity legally binding and enforceable under the laws of the USA?

Yes. The Foreign Sovereign Immunities Act (“FSIA”) codifies the law of sovereign immunity in the US. The FSIA allows for such immunity to be waived, and generally upholds waivers, with some limitations (for example, non-commercial property of a sovereign cannot be attached). Certain organisations also receive immunity under authority separate from the FSIA: the International Organizations Immunity Act covers immunity for certain institutions like the IMF, the OECD and the African Union. One issue in connection with the enforcement of such waivers is whether a borrower actually had the immunity to waive when it provided a waiver. Such scenarios arise in the context of the nationalisation of a company. In such a case, a company may not have had any

immunity to waive (since it was not previously owned by the state) when it entered into the loan, so any waiver provided prior to being taken over by a state may be considered void. For this reason, New York law-governed loan agreements often include a representation that a loan represents a “commercial act”, which excludes the transaction from protection under relevant immunity statutes, whether or not such immunity was in fact effectively waived.

10 Other Matters

10.1 Are there any eligibility requirements in the USA for lenders to a company (for instance, that the lender must be a bank) or for the agent or security agent? Do lenders to a company in the USA need to be licensed or authorised in the USA or in their jurisdiction of incorporation?

In the US, a lender is not required to be a bank (indeed, many lenders are non-banks). A lender should be aware of any relevant state lending licensing laws which may require a lender to be licensed. These licensing laws are much more stringent in the consumer lending area than in the commercial or corporate lending area, though in any event are typically easier to obtain than a “banking licence”. In some cases, one needs to be “in the business of making loans” in order for the licensing statute to be given effect (for example, the New York lender licensing law indicates those lenders who engage in “isolated, incidental or occasional transactions” are not “in the business of making loans” and therefore not covered for purposes of the statute). Non-compliance with a licence statute could have a material impact on the lender, from not being able to access a state’s court system to having a loan be determined to be unenforceable. Whether an agent on a lending transaction would also need to be licensed will depend on the wording of each state’s particular statute.

Note there are often contractual restrictions in New York law-governed loan documentation that require a lender be a certain type of organisation that is in the business of making loans. The rationale for this is many-fold, from securities law concerns to the preference of the borrower to only deal with sophisticated financial institutions should the loan be sold.

10.2 Are there any other material considerations which should be taken into account by lenders when participating in financings in the USA?

The material considerations to be considered in connection with a financing in the US will vary depending on the type of financing and the parties involved, and a discussion with counsel is encouraged before entering into any financing in the US. However, the above questions address many of the main material issues that arise.

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