



Forming a view on the LMA agreement

The Association has produced guidance to help corporate treasurers to form an opinion of the LMA facility agreements. Caroline Bradley is your guide.

With the assistance of and sponsorship from Slaughter and May, the Association has produced a *Guide to the Loan Market Association Facility Agreements* (the 'Guide') for borrowers. The full text of the *Guide* will be freely available on the Association's website from early July.

The *Guide* is in two parts: Part I is an executive summary of the main commercial issues for corporate treasurers, while Part II is a clause-by-clause commentary on the provisions of the Loan Market Association Facility Agreements ('the LMA Agreement'). This article is an extract from Part I: Executive Summary, the aim of which is to help corporate treasurers to form a view on the LMA Agreement. Treasurers' views will vary. They will depend on a variety of factors, including the strength of the company's credit rating, the nature of the transaction in question, the attractions of existing documentation, the relationship with the Arranger in question, and so on.

Essential information

The LMA published their recommended form of facility agreement in October 1999. The project had been undertaken in response to demand from the syndicated loan market for a standard form agreement. Both the British Bankers' Association and The Association of Corporate Treasurers were actively involved in providing comments and input to the LMA. The agreement which emerged is the product of drafting by Clifford Chance and Allen & Overy, with input from a working group which also included representatives of leading banks and major City law firms.

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and secondary markets. However, neither they, nor the BBA, nor the Association seek to mandate its use in any particular case.

The points set out below are designed to help treasurers decide whether the LMA Agreement should be adopted for documentation of their loan facilities. Alternatives, such as existing documentation, should always be considered.

If the LMA Agreement is to be used, independent legal advice will continue to be needed. It is important to appreciate that, although it is sometimes regarded as a 'standard document', it is only a starting point. For example, the document contains no financial covenants; and representations,



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covenants and events of default will always need to be tailored to the circumstances of the individual Borrower and the transaction in question. Thus, although the LMA Agreement is expressly intended to reflect current market practice for a syndicated facility for a Borrower with an investment grade credit rating, it will always need to be negotiated, whatever the status of the borrower. Borrowers should not be deterred from negotiating in their own interests.

Transactions for which the LMA Agreement is suitable

The LMA Agreement is designed for 'plain vanilla' loans to UK corporates. In particular, it assumes the following:

- the Agent is based in London;
- syndication takes place primarily in the London market and the euromarkets;
- the Lenders are all banks or financial institutions;
- a multi-currency revolving facility and/or a term facility with currency switching;
- a group of Obligors, the main Borrower being the holding company, with Subsidiaries as additional Borrowers and/or Guarantors;
- all the Obligors are companies incorporated in England and Wales;
- the main Borrower has an investment grade credit rating;
- no security is provided;
- each Lender participates in each facility proportionately; and
- English law is the governing law.

Where the features of a transaction do not correspond to those listed above, the LMA Agreement may be used as the basis for documentation, but amendment will naturally be required.

Note, however, that there are three versions of the LMA Agreement: a term and revolving facilities agreement, a revolving facility agreement, and a term facility agreement. This *Guide* is tailored for use with the first of these, though it can also be used with either of the others, since they are the same in all but essential mechanics.

Advantages

For many Borrowers, it may be advantageous to use as a basis for negotiation a format which will become familiar in the market. It is hoped that this familiarity will make for greater efficiency in negotiation of the loan document and in the syndication process, leading to lower costs for the Borrower.

On the whole, the LMA Agreement reflects what is current market practice for investment grade Borrowers.

The following features of the LMA Agreement might be regarded as standard for investment grade Borrowers and hence attractive to less powerful Borrowers:

- rollover of loans is permitted when a potential event of default is outstanding;
- many provisions are qualified by materiality: for example, on repetition at utilisation, representations must be true in all material respects;
- similarly, the concept of a Material Adverse Effect is used to soften various provisions, such as the representation as to no litigation;
- provision is made for the Borrower to benefit from tax credits obtained by the Lenders (though in very limited circumstances);
- the Lenders are required to take reasonable steps to mitigate the effect of certain circumstances (such as increased costs) on the Borrower;
- grace periods and threshold amounts are envisaged, for example in the negative pledge and cross default provisions; and

- the Borrower's consent is required for most loan transfers.

Disadvantages

It can be harder to negotiate a draft which is presented by lenders as a market standard than, for example, a draft which is the standard form of a law firm.

The following features of the LMA Agreement are likely to be regarded as rather unattractive by most Borrowers, though many will be found in the first draft of a facility agreement produced by a law firm acting for a bank:

- the indemnities given to the Lenders and the Agent by the Borrower are extensive;
- there is a very broad tax indemnity;
- the representations, covenants and events of default catch not only all the Obligors, but in many cases also their Subsidiaries or even the entire Group;
- the negative pledge and covenant against disposals are very restrictive;
- there is a 'Material Adverse Change' event of default as well as representation;
- the Lenders can accelerate on change of control;
- the set off provision is very broadly drafted;
- the consent of all Lenders is required for a currency to become an Optional Currency;
- the definition of Break Costs does not give the Borrower credit for one day's interest: this is, in effect, a prepayment premium; and
- there are no proper constraints on a Lender's ability to recover ECB reserve asset costs.

To an appreciable extent, 'the devil is in the detail'.

Alternatives

The alternatives to the LMA Agreement are to use:

- existing loan documentation;

- the LMA Agreement, but with the representations, covenants and events of default from the Borrower's existing loan documentation substituted;
- a new draft produced by the Arranger's lawyers; or
- as above, but labelled 'LMA compliant' by the Arranger's lawyers.

The views that Borrowers will take of these alternatives will naturally depend on their varying circumstances: some will feel comfortable with their existing documentation or existing events of default, and some will not. It is not unknown for the Borrower's lawyers to do the drafting, but usually only very powerful credits are able to persuade the Arranger to agree to this. Where a document is described as 'LMA compliant', Borrowers need to find out how far it is compliant; unless the differences are very minor, it will not enjoy any benefit of being an LMA Agreement.

Key points for negotiation

At various points in the LMA Agreement, the parties are given the choice of alternative provisions or expected to insert their own provisions (such as the length of grace periods). Key points to note are listed in the *Guide* but include, for example, the definition of terms such as Material Adverse Effect and the issue of reimbursing the Agent for management time.

In addition, a list is provided of the key clauses for Borrowers relating to costs (other than payments of interest and principal) since these tend to be dotted about throughout the documentation.

Readers are encouraged to view the full text of the *Guide* on the Association's website – www.treasurers.org. Any comments from users would be very gratefully received as this will be a 'living' document, updated regularly to reflect changes in the LMA Agreement. ■

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