

FUND FINANCE FRIDAY

Are Loans Securities?

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We have been following a case that has been winding its way through New York federal courts for some time that players in the syndicated loan market have described as everything from “a potential game changer” to an “existential threat” to the syndicated loan market.

The case in question is *Kirschner v. JPMorgan Chase Bank, N.A.*, which is before the United States Court of Appeals for the Second Circuit. In this case, the Court will consider an appeal of a 2020 decision by the United States District Court for the Southern District of New York which held that the syndicated term loan in question was not a security. Significantly, this ruling indicated that because syndicated term loans are not securities, they are therefore not subject to securities laws and regulations.

The consequence of a determination that syndicated loans are securities would be significant. It would mean, among other things, that the syndicated loan market would have to comply with various state and federal securities laws. This would significantly change the cost of these transactions as well as the means by which syndication and loan trading take place. The Loan Syndications and Trading Association (LSTA) filed an amicus brief in this case in May of this year, which we covered [here](#). The LSTA argued in its brief, among other things, that beyond the increased cost, regulating syndicated loans as securities would fundamentally change other aspects of the syndicated loan market. Specifically, the LSTA pointed to the importance of a borrower’s ability to have veto rights and other control in determining which entities will hold its debt. The LSTA also noted the importance of quick access to funding on flexible terms specific to the borrower in question – something we know is at the heart of so many fund finance transactions – which would be greatly compromised within a securities regulatory regime. The LSTA brief also discusses potential negative impacts on the CLO market.

Those in favor of a change in regulation point to features such as nonbank lender participation in the market, the fact that the test to determine whether a loan is a security may be outdated, and the overall size of the syndicated loan market – at \$1.4 trillion – which could be a risk to the larger global financial system potentially warranting more stringent regulation.

Most experts believe that the Second Circuit will not overturn the decision issued in the lower court, but the issue in question is significant enough that market players should keep an eye on this one. Oral arguments will take place early next year. We will continue to watch as this case develops and update you here.