CADWALADER

FUND FINANCE FRIDAY

“Nothing to see here...move along” or “Something’s happened...let’s stop and look”

May 3, 2019 | Issue No. 27

A common area of focus in LMA-based fund finance (and other) facilities in Europe is on the trigger point for acceleration of a facility and/or enforcement of security following the occurrence of an event of default. The borrower will generally want an opportunity to “cure” or “remedy” events that would be events of default when they occur, and will equally not want to be subject to acceleration or enforcement action if an event that is an event of default no longer applies. The lenders, at the same time, will want to ensure that these rights are not abused and, in particular, that the borrower cannot just repeatedly commit then “cure” events that are events of default, particularly where these are significant—at least not without the lenders expressly choosing to waive that event of default.

The problem is that, in the LMA documentation on which most funds finance and many other European facilities are based, the question of when and how to deal with events of default is addressed in two different places and the two provisions are not consistent with each other.

First, it is dealt with in the “definitions” clause, in which an event of default is deemed to be “continuing” if it has not been remedied or waived (the reference to “waiver” here being treated by the LMA as a point to be negotiated). Second, it is dealt with in the events of default clause itself where certain events of default (for example, most covenant breaches) are said to constitute events of default if they are capable of remedy and are not remedied within a defined cure period (usually somewhere between 10 and 20 business days).

So the question is, how do you reconcile one with the other (and how do borrowers and lenders with their somewhat different concerns reach a common position on this)? In summary, the definitions clause (the first clause referenced above) is more where the borrower wants to be (particularly if it can remove the reference to “waiver”), and the second clause is more where the lenders want to be (because it defines exactly which events of default can be cured and the time period during which that can happen, and applies only to events of default that can be remedied in the first place). Lenders will also want to retain the reference to waivers in the first clause, so that they can make a specific decision on whether an event of default has been remedied under that clause.

What resolution is reached often depends on the negotiating stance of the parties and the underlying background of the parties. A common (but not universal) “market” position is for

lenders and borrowers to agree that an event of default can be remedied at any time if it is a “minor” event of default but that a “major” event of default would require a specific waiver from the lenders (so the lenders have the option to make the decision).

It remains to be seen whether the LMA form itself will ever be changed to bring the two clauses more in line with each other, but until and unless that happens, the way in which they work together to reflect the underlying borrower and lender concerns will and should continue to be an area of particular focus for the parties in their negotiations.