31 The Role of the Lawyer: Changing Expectations

By Kathrine Meloni

Introduction

The publication of the LMA's first recommended form of facility agreement for investment grade borrowers might be described as a 'Big Bang' event for banking lawyers. LMA terms now provide the basis for, or at the least, have an influence on, virtually all English law commercial loan documentation and few banking lawyers in the market are able to practise effectively without access to the LMA library. Those able to recall pre-LMA terms are in a shrinking minority.

There is no doubt that LMA resources have contributed materially to the efficiency of the documentation process. A common baseline for the more mechanical provisions of a loan agreement has enabled transactional lawyers to focus on settling the commercial terms of the deal and keeping on top of the continuing stream of emerging developments to be addressed.

As the English law primary documents come of age, this chapter reflects on how market developments and the work of the LMA over the last 25 years have altered the role of the loan finance specialist, and the expectations of their clients.

Familiarity with the LMA library

In the pre-LMA world, letters were signed in triplicate and fax machines remained in use. Email was something of a novelty (to the extent that the first iteration of the LMA's investment grade agreements did not cater for electronic communication). There was an appreciation that the efficiency of the loan documentation process needed to be improved and law firms were getting to grips with document automation software. Nonetheless, each loan agreement had to be reviewed from scratch, often a challenging game of 'spot the difference', as each law firm presented the same mechanics in a slightly different style.

The widespread adoption of LMA terms has meant that the areas of each agreement that must be newly deciphered are significantly fewer. Familiarity with the LMA's documentation suite is therefore essential for those operating in the primary market, as well as an understanding of how the documents are used in practice.

Expert use of LMA terms

The early drafts of the LMA agreements sought to distinguish 'hard' provisions, boilerplate clauses which do not require negotiation, from 'soft provisions', which are expected to be discussed on a case-by-case basis, thereby narrowing the universe of provisions to be negotiated. The payment mechanics, for example, were considered 'hard' provisions. The 'soft' provisions included the representations, undertakings and events of default. However, as the market has become familiar with the various documents in the LMA's collection, their use has become more sophisticated. The framework is broadly accepted, but users appreciate that even LMA terms thought of by many as 'hard' provisions may, on occasion, need to flex.

As a result, the distinction between 'hard' and 'soft' provisions has faded over time, as bargaining power and/or market developments have altered the parties' perspectives. The terms of particular LMA templates in that sense, are being used more flexibly. For example, a number of the covenant restrictions in the investment grade templates are significantly relaxed, or even omitted by stronger borrowers.

The expansion of the LMA's library has enabled those familiar with its broader collection to mix and match provisions from different documents. There are currently 30+ LMA forms of English law facility agreement, plus multiple forms governed by the laws of other European and of various African jurisdictions. These are used as a clause library, from which lawyers are able to build the document that suits their transaction. The investment grade agreements, for example, where used as the basis of facilities extended to borrowers at the lower end of the investment grade spectrum or in the cross-over space, are often supplemented with additional representations and undertakings modelled on those in the LMA's leveraged facility documentation. As a result, the inclusion of a particular provision simply because 'it's in the LMA' (often a source of frustration, in particular for borrower-side lawyers), holds less weight than was the case in the early years.

Guidance on market norms

The parties' flexibility to depart from LMA terms, however, is not absolute. There is a tension between adaptability – the unique selling point of the loan product – and the level of documentary commonality required for a syndication market to function effectively. Lenders and borrowers expect their lawyers to offer guidance on how far LMA-based terms can be flexed, while maintaining a level of consistency sufficient to enable successful syndication on a basis that remains cost-effective for the borrower. This is something that needs to be understood and considered on a borrower-by-borrower basis. Arrangers' request for proposals (RFP) will commonly reference recent comparable deals as indicators of pricing, maturity and other key terms; lawyers have come to apply the same skill set to the detail of the documentation terms.

The meat of any loan agreement is driven by the borrower's actual or implied credit rating, its business sector and the purpose of the loan. The other key determinant of lending terms is, of course, the amount of liquidity in the market. The impact of adverse market conditions can be quite subtle at the top end of the investment grade market, but for most transactions, context and timing is everything. With the growth of the market, it has become possible to group and benchmark the

terms applicable to comparable deals on a clause by clause basis, meaning that in a dynamic way, the loan market has become more precedent driven. Within particular types of deal and, more specifically, particular types of deal for borrowers within the same ratings band, the margins for negotiation remain flexible, but over time, have become more defined. What has been achieved recently by other similar borrower places parameters around most loan negotiations; and clients expect their lawyers to be fully apprised of those market norms.

A certain depth of knowledge as to market norms is thus a pre-requisite for banking lawyers looking for satisfied clients. Law firms must ensure that their junior lawyers quickly develop an awareness of the factors that influence the documentation terms any particular borrower is able to achieve.

Crisis management

The financial markets have become more complex and over the last decade have thrown up a series of often unanticipated issues. Lawyers who were in practice during the Financial Crisis have experience of managing and executing the swift and thorough analysis of new scenarios as they arise, with an appreciation of their wider market impact. The effect on the loan market of defaulting and insolvent lenders and administrative parties for example, soaked up many hours of legal analysis in the autumn of 2008, but was not a topic that had previously been considered extensively.

During 2020, the effects of the Covid-19 pandemic and national lockdowns forced most borrowers to analyse and take steps to address drawstops and weak spots in lending documentation. Financial covenant provisions, cessation of business events of default, MAC provisions and provisions relating to reporting and audit were among the lending terms that were adjusted as a result of amendments and waivers sought by borrowers during the Covid period.

Many law firms, formally or otherwise, have developed a crisis management framework, to be brought into play to assess the legal and practical implications of significant market events as they arise. Consistent documentation terms facilitate greatly the ability of market participants to assess the impact of crisis events. In that respect, the advance of the LMA has contributed to the resilience of the loan market in EMEA.

Regulatory expertise

Managing the implications of the array of adverse events affecting the financial sector remains an ongoing challenge for all loan market participants. The ability to anticipate, keep up with and relay succinctly the relevant details of new legislative or regulatory pronouncements as they are available has become a factor which distinguishes banking lawyers in a competitive market, and must be clearly demonstrable (alongside the documentation and market expertise already mentioned and the further abilities highlighted below).

Sanctions and anti-corruption laws are one example of an area of regulatory expertise that has come to the fore over the last decade. Increasingly aggressive enforcement action and the

severity of the penalties imposed by regulators has led most lenders, as a matter of policy, to seek additional and specific contractual assurances from borrowers regarding the group's compliance with sanctions and anti-corruption laws to which both the borrower group and the lenders are subject. Negotiating these provisions is impossible without knowledge of the underlying legislative regimes as applicable to both sides.

There are many other regulatory initiatives with moving parts of direct relevance to the loan market, which require similar background study. The most significant example, is the transition from Libor to risk-free rates, arguably the most complex issue, operationally and in terms of documentation, the loan market has had to address in recent memory. The move from a Libor screen rate, calculated consistently across currencies, to multiple and in most cases, manually calculated rates, has been challenging for all market participants.

The LMA has provided the market with a commensurately large amount of helpful guidance on many of these issues, but the stream of new developments has required many banking lawyers to sharpen their expertise. In general, the areas of which a broad awareness is essential have not changed, but, the necessary level of familiarity, as well as the sheer volume of material, has increased.

Innovation, innovation, innovation

The choice of debt financing products on offer continues to proliferate, as does the range of providers. New terms and new products have had to be designed both to meet the needs of these providers and in some cases, to stimulate the market for the relevant product.

This has influenced the LMA's agenda. The LMA first amended the investment grade agreements to acknowledge the potential involvement of non-bank lenders such as hedge funds and CLOs in lending syndicates back in 2001 (by amending the transfer provisions to permit participations to be sold to 'trusts, funds or other entities regularly engaged in or established for the purpose of making, purchasing or investing in loans, securities or financial assets'). Many of the templates it has produced since, most notably the leveraged financing agreements, have been designed with the needs of participants, other than banks, in mind. A few years ago, the LMA developed a suite of documentation for the then-nascent UK private placement market.

The greater choice of products on offer (or possibly the prominence of alternative sources of finance) means that effective banking lawyers need to be fully conversant with products other than loans. The disintermediation of the loan market has been debated since 2008, but the reality is that borrowers requiring debt in sufficient size use the term loan and the bond markets as alternatives, and will choose the product that best suits their needs and provides the most attractive terms at the relevant time. Sub-investment grade corporates access the high-yield bond market alongside private equity backed LBO targets, which the remainder of their capital structure must accommodate. In the UK, a significant proportion of the FTSE 350 uses the private placement market in some form, and the covenants applicable to a private placement are typically drafted to be consistent with the covenant package applicable to the issuer's loans. The global marketplace means that the borrower's debt options may include looking overseas (or looking at

products, the terms of which borrow from overseas); 'yankee loans' are a well-trodden path for European issuers when market conditions permit, and the influence of New York law high-yield bond and loan terms on the European leveraged debt market is now well-established.

As a result, it is essential that lawyers advising on syndicated loan transactions have an awareness of the borrower group's present and future debt requirements. Lending terms must be negotiated with an eye to how the loan will sit alongside any other debt currently outstanding, or which is likely to be raised in the future.

What is expected of today's banking lawyers?

The consistent framework for loan documentation provided by the LMA has enabled loan finance specialists to focus on those areas where they can add most value. For both this reason, and as a result of the market developments, the skill set required to operate effectively in the primary loan markets has broadened.

Alongside detailed regulatory expertise and the ability to work with a continuously evolving range of debt financing products, keeping up with the credit markets is essential. Clients have increasingly come to rely on their lawyers to advise on what represents a 'good deal' relative to other facilities (and other debt products) in the market, as well as on legal and regulatory issues. As the credit markets continue to evolve and the market for legal advice becomes ever more competitive, an ability to meet and exceed client expectations in this regard, is fundamental.