LSTA 30

30 YEARS OF ADVANCING THE CORPORATE LOAN MARKET

MASTERING COMPLICATED LOAN MARKET INTRICACIES

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Mastering Complicated Loan Market Intricacies

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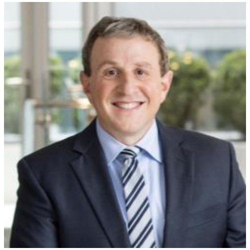

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PRICING 101

Pricing - Funded vs Unfunded

- Buyer pays for funded principal loan balance amount as of Settlement Date multiplied by Purchase Rate
- Buyer receives a credit equal to (100% minus the Purchase Rate) multiplied by any unfunded commitment as of Settlement Date (e.g., an undrawn revolver or delayed draw term loan)

Pricing - Permanent Reductions

Includes reductions to commitment amount and repayments of principal balance

All Permanent Reductions on or after Trade Date are for Buyer's benefit

Buyer receives a credit to the Purchase Price equal to 100% minus the Purchase Rate x the amount of the permanent commitment reduction or principal repayment

Pricing – Non-Recurring Fees

- E.g., fees payable in connection with an amendment, consent or waiver
- Similar to Permanent Reductions, Non-Recurring Fees paid on and after Trade Date are for the benefit of the Buyer
- 100% of any Non-Recurring Fee is for Buyer’s account (applied as a credit to the Purchase Price)

Pricing - Cash Interest & Ordinary Course Fees

- Unlike Permanent Reductions, Interest and Ordinary Course Fees only accrue to the benefit of the Buyer upon the earlier of (i) Settlement Date and (ii) T+7 for Par Trades and T+20 for Distressed Trades
- ***Make your life easy!*** Close on or before T+7 and T+20 (as applicable) and no need for interest calculations
  - Almost all Agents apportion interest between Buyer and Seller based on Settlement Date
  - Only factors to incorporate in pricing would be a Permanent Reduction or Non-Recurring Fee

Pricing - Delayed Compensation

- Kicks in after T+7 (Par Trades) and T+20 (Distressed Trades)
- Provides economic certainty to Buyer and Seller
- Regardless of actual Settlement Date, on or after the Delayed Comp Commencement Date (T+7 or T+20) Buyer gets benefit of all cash interest accruing on the Debt and Seller gets the benefit of interest accruing on the Purchase Price (Cost of Carry)
- BEWARE: on Par trades, make sure you have performed your responsibility as Buyer so you don't miss out on your cash!

Pricing - PIK Interest

Interest that accrues and is then capitalized (or added to the principal balance of the Debt) vs paid out in cash

PIK Interest capitalized prior to Trade Date is included in the funded principal balance of the Purchase Amount

PIK Interest capitalized on or after Trade Date is for the account of Buyer at no additional cost

Sample Revolver Pricing

5MM REVOLVER PURCHASE PRICE CALCULATION @ 70% PRIOR TO T+20

Commitment Amount	$5,000,000
Settlement Date Funded:	$3,000,000
Settlement Date Unfunded:	$2,000,000
Settlement Date Funded	$3,000,000
Purchase Rate:	70%
Funded Purchase Price:	$2,100,000
Credit For Unfunded Commitment	(1-PR) x $2,000,000 = ($600,000)
Purchase Price:	**$1,500,000**

Sample Term Loan Pricing with Delay Comp

$5MM TERM LOAN PURCHASE PRICE CALCULATION @ 70% AFTER T+20 WITH SWOA INTEREST TREATMENT (DISTRESSED)

Interest Rate	7.85%
Avg Cost of Carry Rate:	5.25%
Outstanding Principal Amount:	$5,000,000
Purchase Rate	70%
T+20 Purchase Price:	$3,500,000
Cost of Carry	($3,500,000 x 5.25% x 6/360) = $3,062.50
Credit for Interest	($5,000,000 x 7.85% x 6/360) = ($6,541.67)
Total Purchase Price:	**$3,496,520.83**

Proceeds Pricing; Events of Default & Cash Payoffst

- Proceeds Pricing: Different method for calculating the Purchase Price when Debt has been reorganized or restructured between Trade Date and Settlement Date
- Event of Default → Flip to Flat / Adequate Protection Payments?
- Clawbacks – you've given your Buyer a credit for accrued interest **BUT** the Borrower never pays you
- Cash Full Payoff (and 25% Change Rule for Cost of Carry!)
- LSTA Disgorgement Language vs ClearPar's form of Cash Proceeds Letter

TIME OF TRADE CONSIDERATIONS AND POST-TRADE DATE CORPORATE ACTIONS

Material Terms of Trade

- Traders agree to material terms on phone or by electronic communication (e-mail, Bloomberg, etc.)

- What are material terms of trade?
  - Borrower
  - Credit Agreement (e.g. 1st Lien and 2nd Lien)
  - Type or Tranche of Loan (Term or Revolver)
  - Purchase Amount
  - Purchase Rate
  - Interest Convention

Other Terms of Trade (OTOT)

- OTOT are additional material terms that are credit specific or party specific
- Must be agreed at time of trade
  - Allocation of voting rights on and after trade date
  - Big boy release and waiver for MNPI/borrower restricted information
    - Increased participation in ad hoc committees
  - Lock up vs. non-lock up paper
- Additional considerations if closing by participation is a possibility
  - Participants' voting rights
    - Subject to terms of the CA
  - Collateral requirements (RC)

Corporate Actions

- Parties may know of corporate actions at Trade Date or may only become aware post-Trade Date
- New Money Subscription Opportunities
- Maturity Date Extension
- Covenant Relief
- Forbearance
- Participation in Ad Hoc Group / Coop / TSA / RSA

Corporate Actions – Who Controls?

- LSTA Standard Terms provide Seller retains voting rights through settlement
  - Common market practice is to solicit direction from downstream on open trades
- Is the vote divisible?
- Dealer Perspective
  - Dealer' ability to act at buyer's direction is limited
    - Majority voting
    - Upstream actions
  - Inventory must be carefully tracked ("Yes" vs. "No" paper)
- Buyside Perspective
  - Ensure language requires seller to use best efforts to follow buyer's instructions

Corporate Actions – Process and Timing

- Corporate action materials
  - Often provided on expedited time frame
- Discuss terms and timing with counterparties
  - Important deadlines
    - Voting record date
    - Election deadline
    - Funding deadline
  - Set firm timeline for downstream to provide direction
  - Use OTOT or side letter to document seller’s and buyer’s rights and obligations

Corporate Actions – Process and Timing (Cont.)

- Other Considerations for Open Trades
  - Trade Date vs. Settlement Date position
  - Will seller require prefunding?
  - Can downstream subscribe and/or fund directly
  - Consider that proceeds could be distributed to downstream prior to actual settlement
- Dealer Perspective vs. Buy Side Perspective

LIABILITY MANAGEMENT TRANSACTIONS (A/K/A CREDITOR ON CREDITOR VIOLENCE)

Liability Management / Lender-On-Lender Violence

Liability Management Exercise involves a company restructuring its capital structure/debt obligations outside of formal bankruptcy proceedings (Chapter 11 very expensive)

Lender-on-Lender Violence refers to liability management transactions whereby borrower/sponsor and certain lenders exploit “holes” and/or relaxed credit terms to reduce leverage/debt and create liquidity often to disadvantage of excluded lenders

Types of Liability Management Transactions

- **Drop-Down Transactions:** Moving assets into unrestricted/non-guarantor entities (often utilizing existing lax credit terms) followed by new financing secured by those assets; amend credit terms if needed to facilitate by majority vote
- **Uptier Transactions:** Priming transaction whereby new-money provided from subset of lenders. Typical uptier:
    - (A) Majority creditors negotiate with borrower amending financing agreement allowing for new senior debt and priming liens; (B) Once amended, majority creditors fund new senior debt and often exchange existing debt for new issuance and (C) Exchange utilizes borrower buyback exceptions to restrictions on pro rata sharing
- **Ability to Participate →** sometimes limited to AHG
    - Exchange rates may differ (preferential treatment to SteerCo and AHG)

Pricing – Proceeds / LMT

- **When Do You Use Proceeds Pricing?** Restructuring/Conversion occurs with Purchase Amount after Trade Date → occurs often in connection with effectiveness of LMT or Bankruptcy Plan
  - Funded amount measured as of date ***immediately prior to Restructuring Date*** *(**not** Settlement Date)* → purchase rate paid on funded amount of debt immediately prior to conversion (**not** funded amount on settlement date x purchase rate)
  - All cash proceeds from Restructuring Date through Settlement Date for buyer → including principal and interest on new money debt & Ch 11 exit debt
  - ClearPar functionality limited; manual pricing may be required

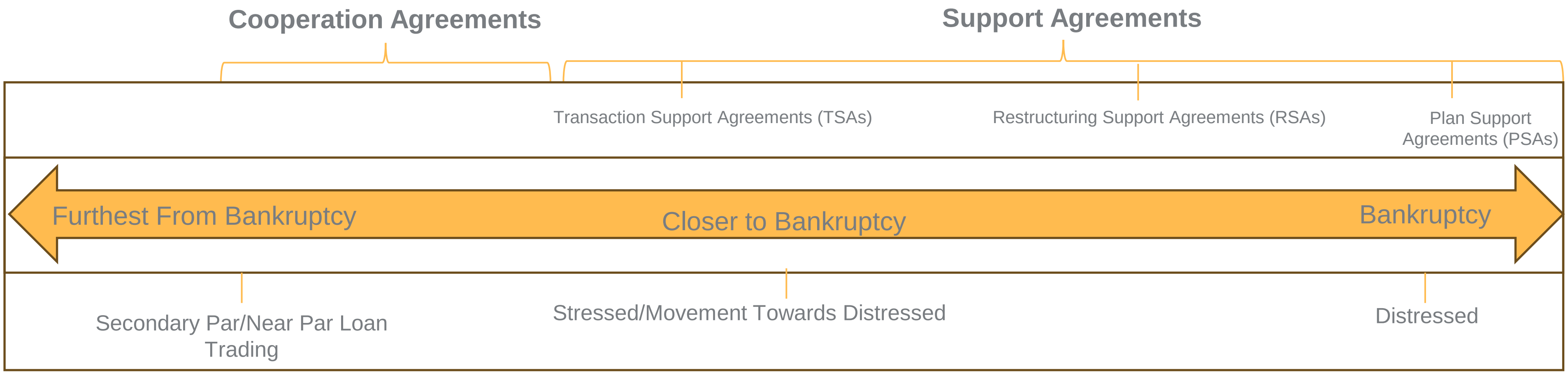
Cooperation Agreements

- Cooperation Agreements often a foundational step upon which a liability management transaction devised and positions subset of lenders to negotiate directly with the company, often to detriment of other lenders.
- At its core, a cooperation agreement is an agreement among an ad hoc group of lenders whereby such lenders unite with goal of obtaining a favorable transaction with a stressed/distressed company involving such company's indebtedness.

Cooperation Agreements vs. TSA & RSA

- **Under a Cooperation Agreement** an entity agrees it will not enter a transaction away from the group and will only enter into an agreement with the group. However, an entity part of a coop **<u>not required</u>** to participate in an "Approved Transaction".
  - Debtor/Company **NOT** part of the Cooperation Agreement.
- Cooperation Agreements are often predecessor step to out-of-court **Transaction Support Agreement (TSA)** or in-court **Restructuring Support Agreement (RSA)**
  - **Under a TSA or RSA, a term sheet** (e.g., approved transaction) has been developed with the Company, and **by signing onto a TSA or RSA a supporting party commits to support and participate on the terms set forth in TSA or RSA**.
- Under a Coop Agreement no term sheet has been developed or agreed upon with the Company relating to some type of restructuring of the company's indebtedness.

Cooperation Agreements vs. Transaction/Restructuring Support Agreements



- Coop = no borrower and no term sheet
- TSA = borrower, term sheet and out of court restructuring
- RSA= borrower, term sheet and generally just before in court restructuring/bankruptcy filing
- PSA = borrower, term sheet and generally after in court restructuring/bankruptcy filing

Reason for Recent Boom in Cooperation Agreements

- In *Serta*, participating lenders had blended recovery rate of around 80% v. non-participating lenders recovery rate of only 1.5% .
- In *Revlon*, participating lenders recovered 52.5% on exchanged second-out loans, while non-participating lenders holding non-exchanged loans recovered 20%.
- In *Envision*, blender recovery rate was roughly 85% for participating lenders, while non-participating fourth-out lenders recovered essentially 0%.
- **Core Protection Point → *be part of Coop group to minimize risk of being left behind*** as an excluded lender.

Additional Transfer Restrictions

- TSAs, RSAs & Coops each restrict transfer of underlying debt held by signatories
    - ***Who monitors compliance with Transfer Provisions?***
- Transfer Restrictions generally prevent signatory party from transferring any TSA, RSA or Coop debt unless:
    - Transferee existing party and timely notice of transfer provided to advisors; or
    - Transferee executes joinder and delivers joinder to advisors; or
    - Transferee is "Qualified Marketmaker"
        - Typically, QM's required to transfer debt to a transferee that meets criteria described in 1 or 2 above within a set time
- **Transfers not done in compliance are generally deemed void** and each signatory party has right to enforce such provision, and injunctive rights typically expressly provided.

Additional Transfer Restrictions (continued)

- Coops, TSAs and RSAs more complex for QM's and loan market participants → must track inventory and make liquid markets
- Some Coops, TSAs and RSAs require parties to track whether traded loans are deemed "initial/early bird" or "subsequent/regular"
  - Economics can be materially different (careful review of agreements required)
- **Careful OTOT needs to be crafted** → dealer v buyside perspective?
  - New Money Opportunity?
- QM's will often need to have different inventory tracking for coop paper and non-coop
- Note LSTA Market Advisory re to Coop Agreements