



Legal Perspectives on 2025 Loan Market Trends

MODERATOR

Elizabeth Yazgi, Esq., *Assistant General Counsel, LSTA*

PANELISTS

Jennifer Daly, *Partner, Corporate Department and Chair of Private Credit and Special Situations, Paul Hastings LLP*

Michelle Kilkenney, P.C., *Partner, Debt Finance, Kirkland & Ellis LLP*

Danelle Le Cren, *Partner and Head of U.S. Banking Group, Linklaters LLP*

Sherri Snelson, *Partner, Debt Finance, White & Case LLP*

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Jennifer Daly

*Partner, Chair of Private Credit and Special Situations, Corporate Department
Paul Hastings LLP (New York)*



Michelle Kilkenney

*Partner, Debt Finance
Kirkland & Ellis LLP (Chicago)*



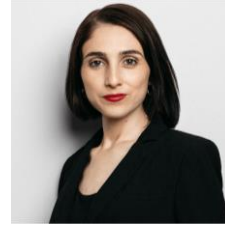
Danelle Le Cren

*Partner and Head of U.S. Banking Group
Linklaters LLP (New York)*



Sherri Snelson

*Partner, Debt Finance
White & Case LLP (New York)*



Elizabeth Yazgi

*Assistant General Counsel
LSTA, Inc. (New York)*

Presentation Overview

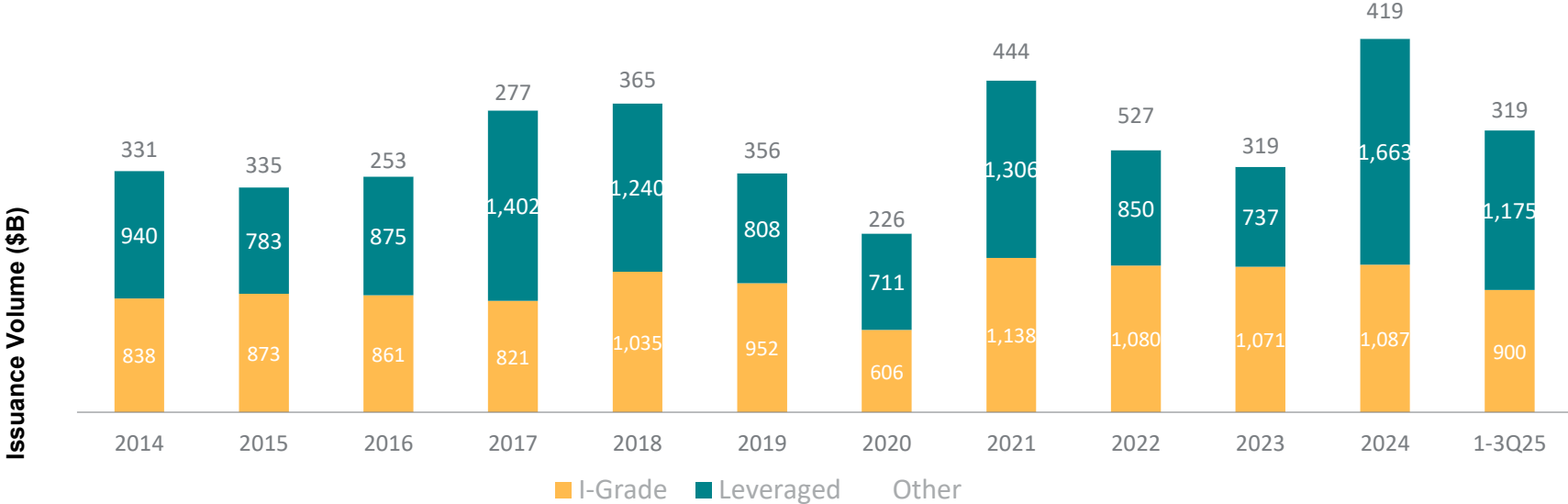
- Loan Market Performance
- Comparing the Broadly Syndicated and Private Corporate Credit Markets
- Primary Market Trends and Terms
 - Covenants
 - Liability Management Transactions
 - Fund Finance and NAV Facilities
- Regulatory and Cross-Border Issues



Loan Market Performance



U.S. Syndicated Lending Market

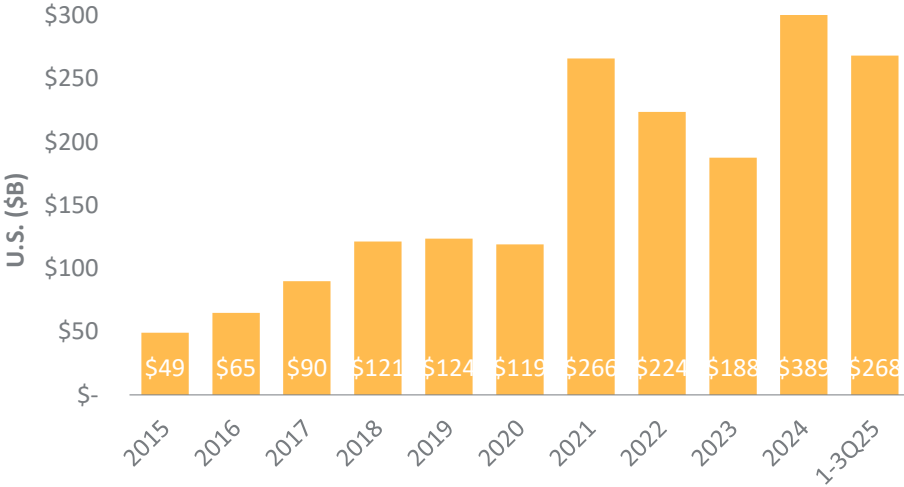


Source: LSEG LPC

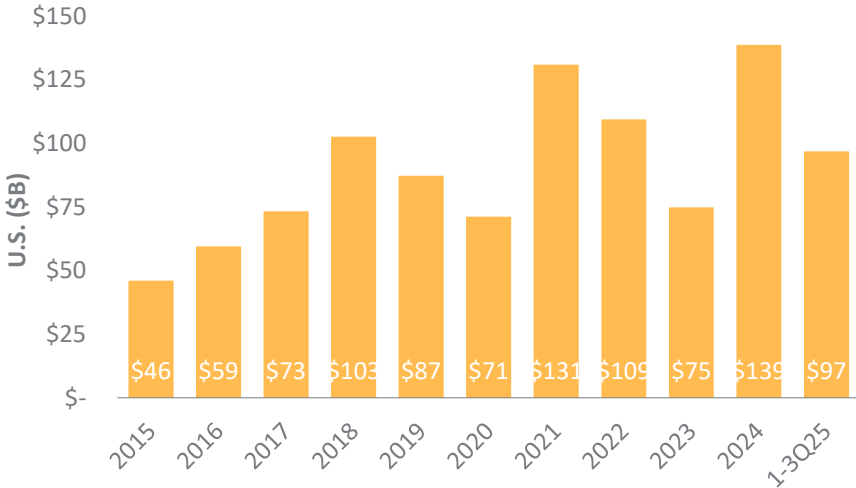
Direct Lending Volume

U.S. sponsored leveraged loans

Sponsored Overall Loan Volume

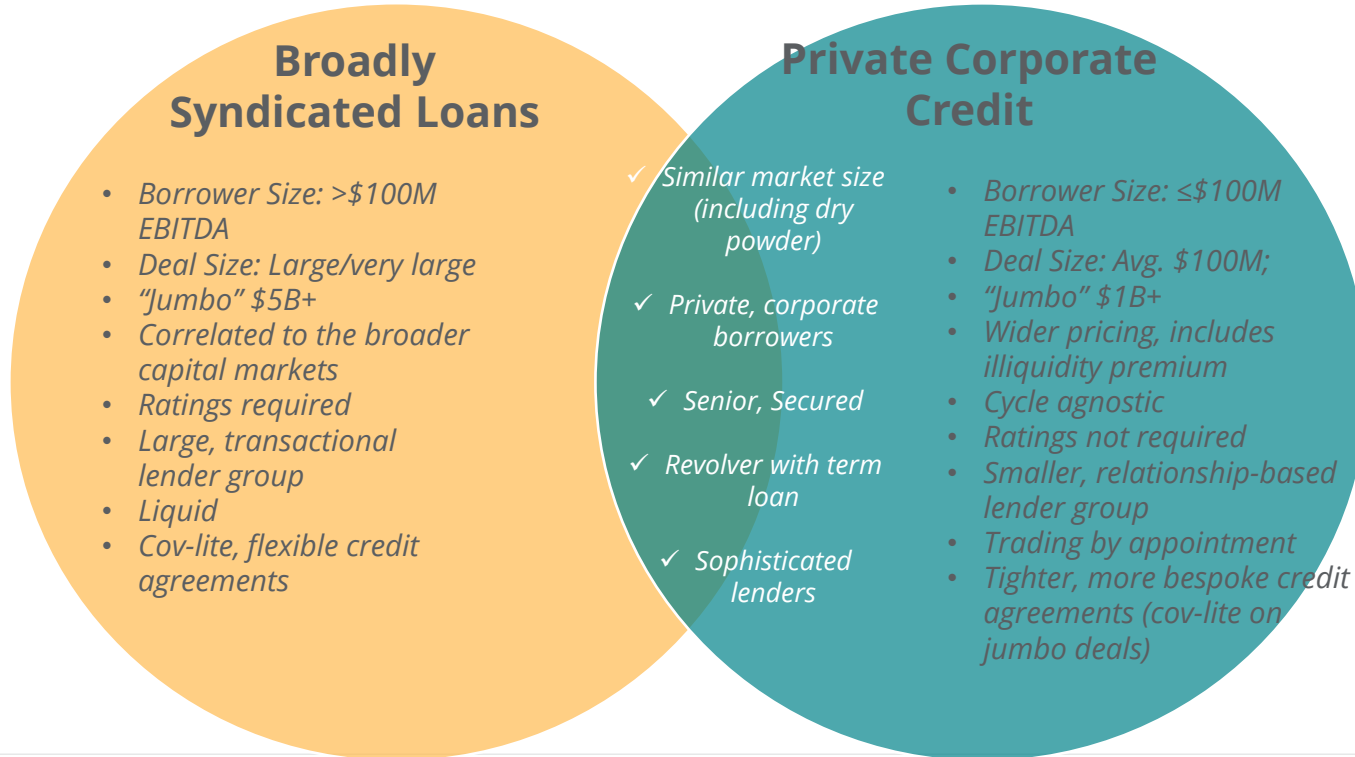


Sponsored Middle-Market Loan Volume



Source: LSEG LPC

Comparing BSL and PCC



General Covenant Trends



General Covenant Trends

- **Portability**
- **Payment-in-kind (“PIK”) Interest**
- **Delayed Draw Term Loans (“DDTLs”)**
- **Dividend Recapitalizations (“Recaps”)**

Portability

- *Describes the ability of a sponsor to proceed with a sale of its equity interest in a borrower without triggering an EoD/mandatory prepay under the “change of control” provision, and allowing existing debt to remain in place despite the sale to a third party.*
- **Typically subject to the following conditions:**
 - *sale transaction must occur within delineated time periods;*
 - *sale can only be to a limited list of incoming sponsors;*
 - *ratings;*
 - *KYC;*
 - *borrower must satisfy a pro forma leverage test and minimum equity condition;*
 - *payment of a fee; and*
 - *limits on exercise of portability option over the life of the agreement.*

Key Advantages

- **Buyer:**
 - *Avoids need to obtain new debt financing.*
 - *Facilitates execution and lends efficiency to sale transactions.*
 - *Minimizes transaction costs.*
- **Sponsors:** *May delay exits in muted M&A market, adopt portable capital structures and plan for future sales.*
- **Target:** *Allows existing capital structures to remain intact, making target a more attractive investment even when current M&A activity is slow.*
- **Lenders:** *Enhances goodwill with existing sponsors, provides certainty of deal closure and opportunities to deploy capital.*
 - *However, limits visibility/control over borrower and may limit exit opportunities.*

Payment-in-kind (“PIK”) Interest

- *Allows all or a portion of accrued interest to be capitalized (added to outstanding principal on each IPD) and paid upon maturity, instead of being paid in cash.*
 - *Rare in BSL but increasingly common in private credit transactions*
- **Borrower vs Lender Perspectives?**
- **Key Issues:**
 - *Premium*
 - *PIK Period*
 - *Call protection*
 - *MFN protection*
- **Variations:** *True PIK, Contingent PIK, PIK Toggle, Synthetic PIK and DDTLs etc.*

Dividend Recapitalizations (“Recaps”)

- *A transaction whereby existing debt is refinanced while borrower simultaneously raises new debt to fund a dividend to equity holders; allows a sponsor to achieve partial liquidity earlier than other exit strategies (i.e., an IPO or a sale).*
- *Start of 2025 saw strong dividend recap issuance*
- *Factors:*
 - *Difficult PE exit environment; and*
 - *increasing pool of dividend payers (falling interest expense, EBITDA growth and strong debt markets).*
- *Structuring considerations/risks (?)*



Liability Management Exercises



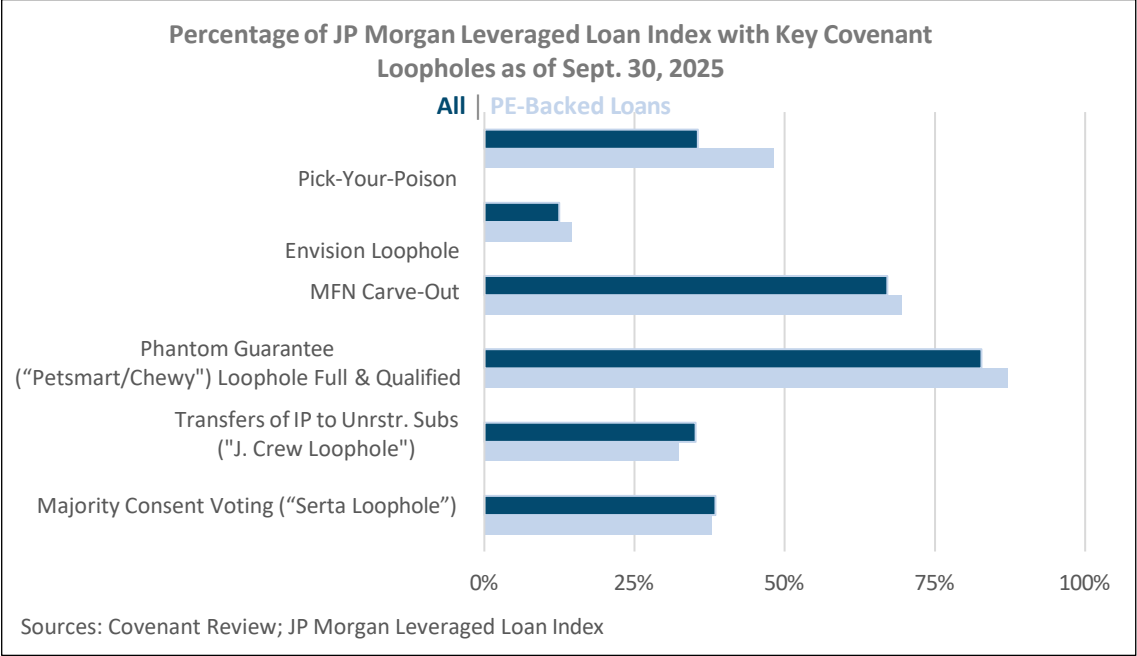
Type of LMT	Related Provisions
<p>“Drop-down” financings, in which a borrower identifies assets that may be readily separated from the rest of the business (e.g., discrete intellectual property or other material assets) and transfers those assets to either an unrestricted subsidiary or a non-guarantor (excluded) restricted subsidiary (“NewCo”). Upon such transfer, the lien on those assets securing the borrower’s obligations to existing creditors is automatically released and such (newly) unencumbered assets are available to secure newly incurred indebtedness of NewCo provided by new creditors.</p>	<p>“J. Crew” prohibits or limits unrestricted subsidiaries from owning specified material assets (typically material intellectual property).</p> <p>“Envision” protection limits the baskets that can be used to transfer assets of the restricted group to an unrestricted subsidiary.</p> <p>“Pluralsight” protection prevents a company from transferring assets to a non-guarantor restricted subsidiary, raising preferred equity from the sponsor and making a dividend of the proceeds back to the company.</p>
<p>“Uptiering” transactions, which refers to the ability to contractually subordinate payment obligations and/or the liens securing credit agreement obligations by obtaining the consent of required lenders. The structural concern presented here is the subordination of minority lenders’ loans (either on a payment or lien basis) in connection with a non-pro rata uptiering transaction which is approved by “Required Lenders”, excluding minority lenders.</p>	<p>“Serta” protection makes subordination of liens or payment obligations to third party indebtedness an affected lender vote, subject to certain exceptions. Generally, key areas lenders should focus on include:</p> <ul style="list-style-type: none"> • subordination provisions; • intercreditor arrangements; • pro rata treatment/payment waterfall; and • open market purchase limitations
<p>“Double Dip” transactions, in which a creditor has the benefit of a guarantee from the loan parties for a primary obligation, and the primary obligor – against which the creditor also has a claim – has its own intercompany claim against the guarantor debtor as well.</p> <p>“Double-Dip” pari plus/layering another iteration is “pari-plus” - where different (and additional) obligors under the loan incur or guarantee the new financing, so that the new lenders have structurally senior claims against the new obligors and continue to share indirect claims against the original obligors.</p>	<p>“At Home” protection prohibits or limits unrestricted subsidiaries’ ability to receive credit support from, or from owning debt or equity of, the restricted group.</p>
<p>“Chewy” transactions, which represent the ability of a borrower to transfer minority equity interests of a loan party to effect its automatic release from an existing guaranty and pledge of collateral, enabling it to incur structurally senior debt.</p>	<p>“Chewy protection” involves the incorporation of key conditions precedent to the release of a non-wholly owned subsidiary as a safeguard against this type of LMT.</p>

Other LMT Drafting Issues

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- *Cooperation Agreements/Anti-Cooperation Agreements*
- *Sacred Rights/Voting Rights*
- *Transferability and DQ Lists*

Key Covenant Loopholes Remain in the BSL Market

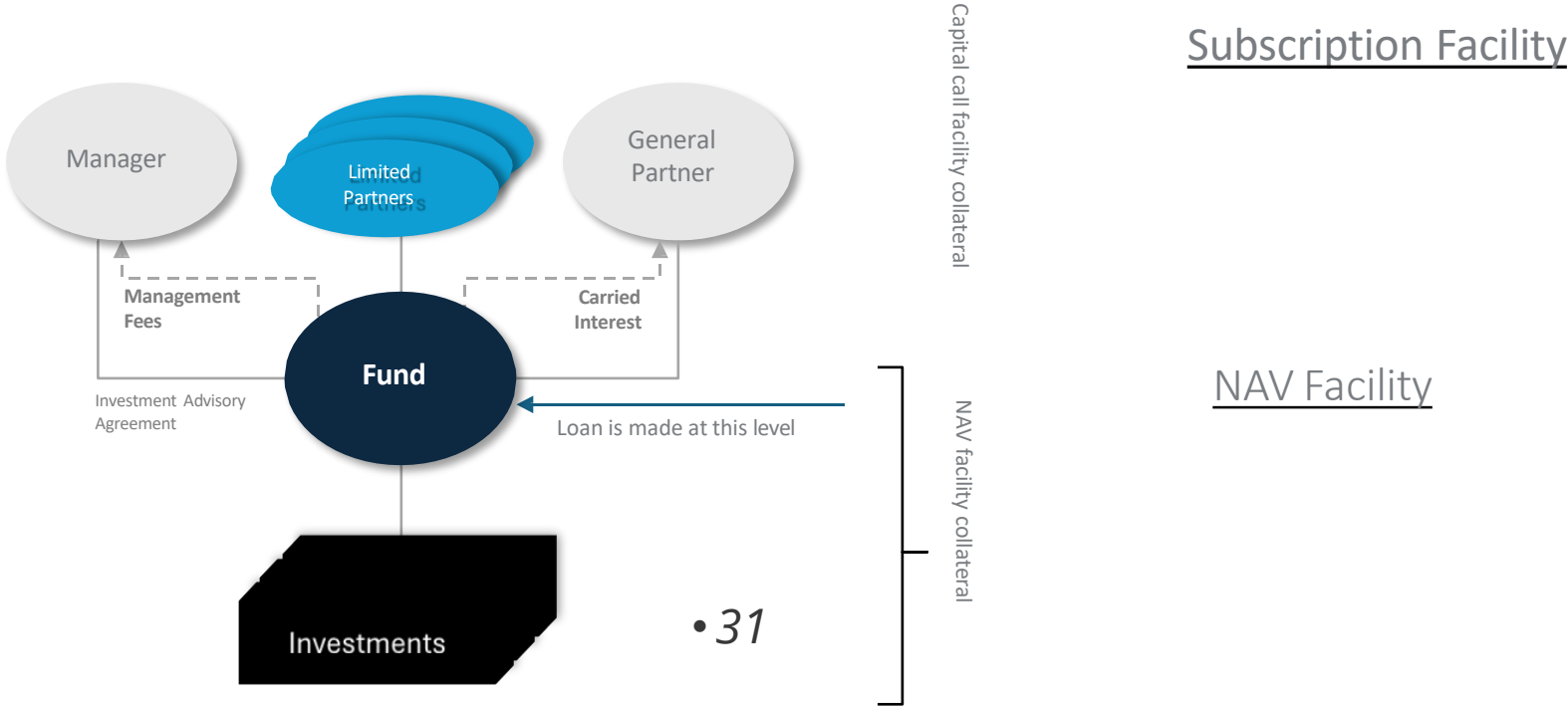




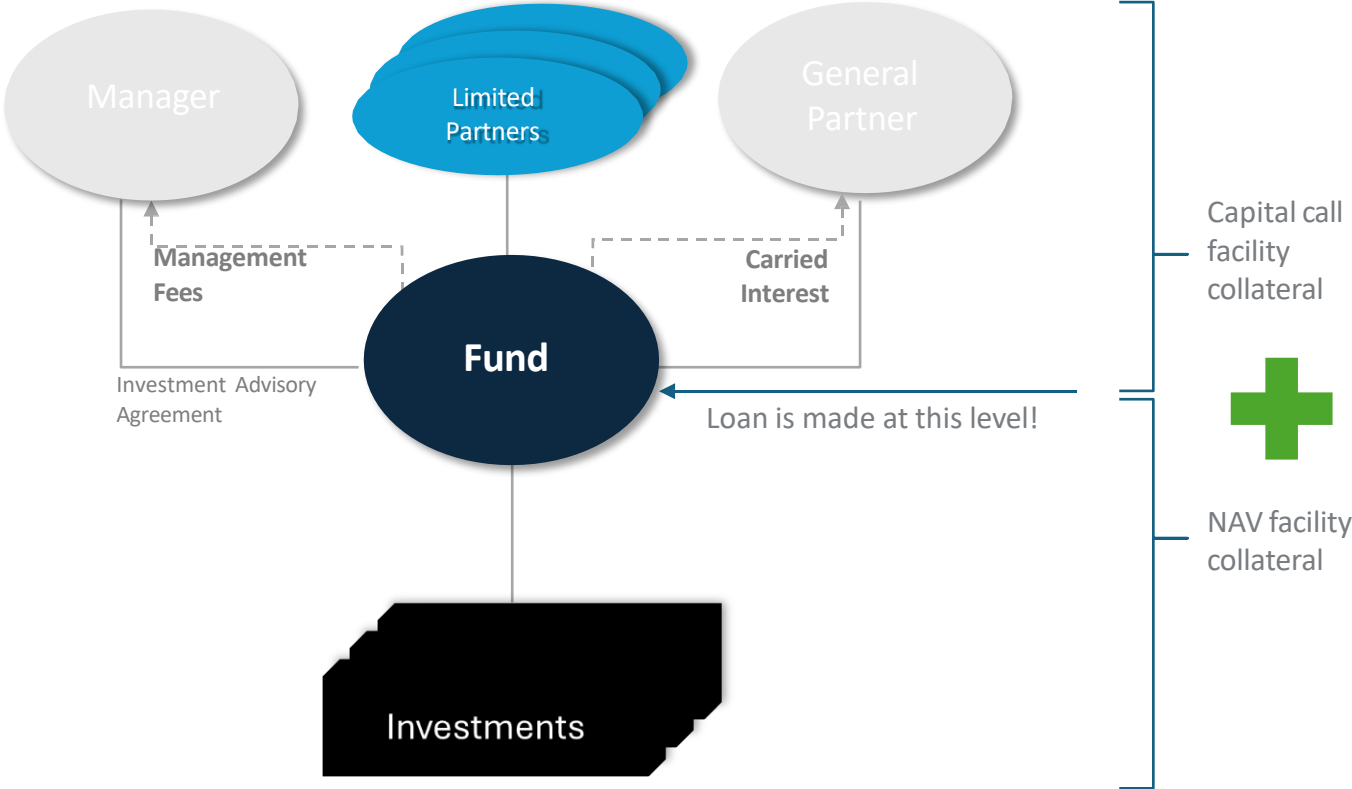
Growth of Fund Finance



Overview of Different Financing Options



Hybrid Facility



Regulatory and Cross-Border Issues

- **Outbound Investments Rule**

- *1/2/25 Treasury rule that prohibits or requires notification of “covered transactions” and “covered foreign persons” involved in high-tech industries (advanced semiconductors, microelectronics, quantum computing, and artificial intelligence) and located in limited jurisdictions (PRC/HK/Macau).*
- *Covers certain loan transactions: (i) those resembling equity investments, (ii) convertible debt (i.e., “contingent equity interests”) and (iii) certain secured loans where foreclosure on the collateral results in possession of pledged equity (subject to limited exceptions).*

- **Basel III Endgame**

- *The Fed has begun developing a new risk-based capital rule aimed at easing the burden on the largest US banks (with more than \$100 billion in assets).*
- *This would significantly alter the regulatory capital regime for US banks.*
- *Net result could be banks having more lending capacity and being increasingly competitive with direct lenders*