**Syndication**

This element introduces syndicated lending: the nature of a syndicated loan; why a loan might be syndicated; the process of syndication; and the parties involved.

N.B. clause references throughout this element are to the LMA Agreement.

**What is a syndicated loan?**

A **bilateral loan** is a loan made available by a single lender.

A **syndicated loan** is a loan made by two or more lenders (together called the **syndicate**) on the same terms and governed by a single loan agreement.

For example: A borrower, XYZ plc, needs a substantial sum of money which a single lender is not able or does not wish to provide. Assuming that XYZ plc wants to borrow this money by way of a loan, rather than in the capital markets, it could borrow the funds from either:

1) a group of lenders using a series of separate bilateral loans (each loan negotiated separately with the individual lender and on different terms); or

2) a group of lenders under one overall agreement (a ‘**syndicated facility**’).

Syndicated facilities are a popular source of funding with facilities ranging from relatively small amounts (e.g. £20 million) with relatively few lenders, to huge ‘jumbo’ facilities involving over 200 lenders.

Bilateral and syndicated loans work on the same basic principles, but with syndication comes additional parties and associated provisions and liabilities.

**Syndicated Loan Structure (pre-signing)**

[Diagram showing a box marked “Single loan agreement signed”. Above this are 4 boxes marked Lender A, Lender B, Lender C and Lender D. An arrow from each box points towards a single box marked “Arranger” (this section is labelled “the Syndicate”). There is an arrow from “Arranger” to a box marked “XYZ Plc (Borrower)”].

**Why syndicate?**

When a lender lends money, it makes a profit made up of fees paid by the borrower and the margin (the difference between its cost of lending and the interest paid by the borrower to it).

So why would a lender that has been approached by a borrower want to form a lending syndicate and be forced to share its profit?

This is due to a number of limitations which impact upon a lender’s lending, including the size of the loan, internal risk policy and large exposure regulations.

**Large loans**

Syndication allows large amounts to be lent to a single entity with large financing needs. Often it would not be feasible for one lender to make available such sums.

Therefore, a borrower will appoint a lender to put together or ‘arrange’ a syndicate of lenders and each member of the syndicate will commit to contributing towards the total facility on signing of the loan agreement.

**Internal risk policy**

Even if it had the cash to do so, one lender would have a considerable credit risk if it were to lend large sums to any one borrower or concentrate its lending in specific sectors or countries.

This is something which the lender’s internal credit committee will look at when the proposed loan is first put forward (see Element 1 of this Topic).

**Large exposure regulations**

Irrespective of a lender’s internal risk policy, it may be prohibited by large exposure regulations (for example, those stemming from the Capital Requirements Directive) from taking so much risk with a single borrower.

Lenders gain fees and prestige from participating in high profile syndicated loans and this could lead to follow on business with the borrower. So even for lenders with small participations in a syndicate, it is a good way of entering the market and being introduced to the borrower.

From a borrower’s point of view, the more lenders, the bigger the potential amount to be borrowed but also the more unwieldy the syndicate becomes to manage. This is somewhat mitigated by the syndicate appointing an ‘agent’. As mentioned below, one of the Agent’s roles is to act as a conduit between the borrower and the syndicate lenders.

**Post-signing syndication**

N.B. the borrower may need funds for a specific project and by a specific time (e.g. to fund a property acquisition). It may not be feasible to form a syndicate prior to the signing of the loan agreement in time for completion. A solution is to enter into a loan agreement with either the Arranger or, more likely, a small group of syndicate lenders so that the borrower has its funds on time. The initial lender(s), **post signing** of the loan agreement, will then syndicate the loan by **transferring** ‘portions’ of it to other lenders, thereby reducing their overall exposure to the borrower.

This is called **post signing syndication**.

We will consider different methods of transferring a loan in Workshop 7.

**Parties to a syndicated loan and their roles**

**Arranger**

The starting point of syndication will be for the borrower to appoint a lender to put a syndicate together. This is known as ‘arranging’ the syndicated loan and the name generally given to the lender taking on this role is that of ‘**Arranger**’.

The Arranger (also known as the ‘lead arranger’ or ‘mandated lead arranger’) is appointed (i.e. ‘mandated’) by the borrower to arrange the raising of the required amount of debt, by organising a syndicate of lenders which is able to provide those funds. Such an appointment or mandate will be confirmed and documented by the**mandate letter** (see element 3). The borrower will usually expect the Arranger to provide a substantial proportion of the total facility.

The Arranger will charge an **arrangement fee** for its role as arranger of the loan This is usually documented in a fee letter so that the exact amount is confidential as between the borrower and the Arranger.

The Arranger will **advise** as to the most appropriate loan structure, key terms and the cost taking into account the borrower’s creditworthiness, the purpose of the loan and prevailing market conditions. The Arranger will advise the borrower generally (if it is not familiar with the syndicated loan market) on how the syndication procedure will move forward.

The Arranger will prepare an **information memorandum** from information provided by the borrower. This is the document used by the Arranger to market the loan to potential syndicate lenders. It will contain, amongst other things, a description of the borrower’s business and financial details.

The role of the Arranger ceases on the signing of the loan agreement (clause 33.4). However, the loan agreement should still contain some clauses which are designed to protect the Arranger, e.g., providing for the ability to enter into other future business with the borrower (see clauses 33.5 & 33.6).

The Arranger will appoint solicitors to draw up the **first draft of the loan agreement** and then will negotiate this and any other documentation, such as security documents, with the borrower on behalf of all syndicate members. If there is more than one arranger, they may agree that one of them assumes this role, in which case they may be referred to as the documentation bank when acting in this capacity.

It has become common for larger borrowers to agree with the Arranger that the borrower's solicitors will draft the loan agreement as the borrower will want the loan agreement to be borrower friendly. Usually, the Arranger's lawyers will prepare the other finance and security documents.

**Syndication – best efforts or underwritten?**

The mandate letter will make it clear whether the Arranger has been appointed on a **best efforts** or **underwritten** basis.

When a loan is mandated on a best efforts basis, the Arranger will promise to use its ‘best efforts’ to assemble a syndicate of lenders willing to lend the required amount. This does not amount to a guarantee that the full amount will be raised. If the Arranger does not succeed, the borrower will not have access to the full funds required.

But the borrower may need certainty of funds…

The borrower can ask the Arranger to **underwrite** the entire loan or arrange for a small group of lenders to underwrite the loan. This means that if the full syndicate of lenders cannot be put together in time, the Arranger (and any fellow co-arrangers) will be obliged to make up any shortfall in the requested amount. The borrower will have to pay an underwriting fee for this as well as the usual arrangement fee. Acquisition finance transactions will usually be underwritten by the Arranger as the borrower needs to be certain that it will have funds available to complete the acquisition.

**Agent ​**

The Agent is typically a bank, usually part of the lending syndicate, appointed by the syndicate lenders under the loan agreement, upon the advice of the Arranger, to administer the facility. The Agent is agent of the lenders and not of the borrower. Note non-bank Agents are becoming increasingly common.​

This is an important role. The Arranger and the syndicate lenders formally appoint the Agent under the terms of the loan agreement (clause 33.1). The Agent administers the mechanics of the loan and will be the main point of contact between the syndicate and the borrower throughout the life of the loan, as far as the mechanics of the loan are concerned. ​

The Agent will be unwilling to assume any discretionary powers to manage the loan on behalf of the syndicate, as this may lead to liability in the event any of their decisions have unfortunate consequences. Agency fees are low and do not reflect risk.

In addition, the syndicate lenders are generally unwilling to delegate management functions to the Agent and deprive themselves of influence in decision-making.

The result is that the Agent’s duties are precisely defined and documented and are mainly restricted to administrative tasks (clause 33.3 (a)). The Agent will protect itself by seeking instructions from all or the requisite group of syndicate lenders, e.g.' the ‘**Majority Lenders**’. The Agent will not be liable for any actions it takes in accordance with those instructions (clause 33.2 (a)(i) (A) and (D)).

See below for the Agent’s main functions which include receiving and paying loan advances from the syndicate to the borrower and vice versa for payments of interest and principal from the borrower; receiving and forwarding documents and notices; determining the applicable interest rate; taking action on default; interpreting the provisions of the loan agreement; and administering loan transfers.

[Diagram with arrows from Main functions in the centre pointing to the following paragraphs in boxes – clockwise in the following order:

Paying agency (cl. 36.1)

Postman (cl. 33.3(b) and (d))

Determining interest rate

Limited monitoring (e.g. cl. 33.3(d)

Pro rata sharing (cl. 35)

Interpretation of loan agreement (see also cl. 33.7(c) to (e))

Action on default (cl. 29.20, cl. 33.3 (e) and (f))

Checking conditions precedent (cl. 4.1)

Administering loan transfers (cl. 30 and Sch 4 and 5)

**Majority Lenders**

A democracy exists within the syndicate. Most decisions tend to be delegated to majority control, usually set at 66 2/3% of total syndicate commitments (referred to as the ‘**Majority Lenders**’ – see definitions clause to check the majority threshold). Once a decision is made it is binding on all syndicate members.

This style of decision making by Majority Lenders speeds up the process and prevents one minor lender effectively having a veto. A drawback of syndicated loans is the potential divergence of interests of the syndicate members. It is important both for lenders and the borrower that amendments and waivers can be made relatively easily, without one minor lender being able to block the process.

**Task: Read clauses 42.2 and 42.3 of the LMA Agreement and consider whether all decisions taken by a syndicate of lenders are by way of majority or whether some must involve unanimity.**

**Majority Lender decisions v unanimous consent**

Matters which usually require a Majority Lender decision include waiving certain defaults, amending the loan agreement (cl. 42.2(a)), determining whether a material adverse change has occurred regarding the borrower and directing the Agent to accelerate the facility (cl. 29.20).

However, a few matters are considered so important that they require unanimous consent. These will be specified in the loan agreement but usually include a change of borrower, a reduction in any amount paid to the lenders, an extension of payment dates or an increase in the total of the lenders’ commitments (see clause 42.3).

**Parties to a syndicated loan – correct the incorrect table!**

Cl. 33.1(a) The Arranger does not enter obligations under the Loan Agreement; its role ceases on signing.

Cl. 33.2(a) Neither the Arranger nor the Agent owes fiduciary duties under the Loan Agreement and are therefore not obliged to account for profits made.

Cl. 33.3(a) Neither the Agent or Arranger will be responsible for accuracy of information in the Information Memorandum.

Cl. 33.4 The Agent is appointed by the Arranger and Lenders as its agent.

Cl. 33.5 The Agent will not be liable for any exercise of its power if it acts in accordance with Majority Lender / all Lender instructions.

Cl. 33.8 The Agent’s duties are solely mechanical and administrative.

[Pen Symbol]

**Task:**

The clauses and statements do not match; take a moment to read the LMA clauses listed and match them to the correct descriptions in the table.

**Parties to a syndicated loan – correct table**

Cl. 33.1(a) The Agent is appointed by the Arranger and Lenders as its agent.

Cl. 33.2(a) The Agent will not be liable for any exercise of its power if it acts in accordance with Majority Lender / all Lender instructions.

Cl. 33.3(a) The Agent’s duties are solely mechanical and administrative.

Cl. 33.4 The Arranger does not enter into obligations under the Facility Agreement; its role ceases on signing.

Cl. 33.5 Neither the Arranger nor the Agent owes fiduciary duties under the Loan Agreement and are therefore not obliged to account for profits made.

Cl. 33.8 Neither the Agent or Arranger will be responsible for accuracy of information in the Information Memorandum.

[Pen Symbol]

**Task:**

The clauses and statements now match. Read on to explore in detail the roles of these parties in a syndicated loan.

**Security Trustee**

Where a syndicated loan is secured, a security trustee (sometimes labelled a 'Security Agent') will be appointed to hold the security effectively for the benefit of all the syndicate lenders.

One major advantage of this arrangement is that when a syndicate lender transfers its participation, the benefit of the security can be also transferred without the need for a separate formal arrangement. To achieve this the security must be created in favour of the security trustee for the benefit of the ‘Lenders’, defined as the lenders from time to time lending under the loan agreement.

This is sufficiently precise under English law for the creation of security for the benefit of the syndicate as a whole, notwithstanding that the identity of the lenders may change during the life of the loan. Local legal advice should be taken if security is being created other than under English law. Loan transfers will be considered in Workshop 7.

**Summary**

• A syndicated loan involves a group of lenders lending to a borrower under the umbrella of one single syndicated facility agreement. Syndicate lenders may join a syndicate to gain prestige/fees.

• Syndication may be necessary due to the size of a loan, limits imposed by individual lenders’ internal risk policies and large exposure regulations.

• The Arranger will be mandated to arrange the syndicated facility; this role will include advising the borrower, marketing the loan to attract potential syndicate members and negotiating the terms of the loan and any security.

• The Agent will be appointed to administer the mechanics of the facility during its term. This role is limited in scope and the Agent will, as far as possible, act in accordance with Majority Lender instructions to limit its own potential liability.

• A Security Trustee will be necessary if the facility is secured.