

## Importance of Reviewing Existing Financing Agreements During COVID-19 Crisis

By: Jennifer Santangelo, Maulin Vidwans and Andrew Marrinucci

*Finance Alert*

3.23.20

U.S. banking regulators, including the Federal Deposit Insurance Corporation (FDIC), Consumer Financial Protection Bureau, Conference of State Bank Supervisors, Federal Reserve, National Credit Union Administration and Office of the Comptroller of the Currency, issued a joint statement on March 9, 2020, urging financial institutions to “work constructively with borrowers and other customers” in communities affected by the COVID-19 pandemic.

While prudent loan relief from financial institutions is widely encouraged in times of worldwide crisis, financial institutions should examine their existing financing agreements for the significant provisions detailed below as the COVID-19 crisis continues to unfold.

### Material Adverse Effect/Material Adverse Change

Almost every financing agreement contains a material adverse effect or material adverse change provision, which will vary from agreement to agreement based on the specific transaction and negotiations between the parties. These provisions should be reviewed carefully because the occurrence of such an event will often prohibit borrowers from borrowing under their existing credit facilities and may constitute an event of default in some financing agreements.

### Financial Covenants

Most financing agreements require the maintenance of certain financial covenants, which typically include leverage, interest or fixed charge coverage ratios. Because these ratios are calculated based on a borrower’s earnings before interest, tax, depreciation and amortization (EBITDA), an unexpected decrease in revenue will likely have a negative impact on the borrower’s financials and, in turn, may result in a breach of a financial covenant. While financial covenants are often tested on a quarterly basis, it may be prudent for lenders and borrowers to have timely discussions regarding updated financial projections in order to negotiate potential amendments or waivers before such an event of default is triggered.

### Go Dark Provisions/Government Shutdown

Financing agreements often include covenants that borrowers will continue to operate their business in compliance with all local, state and federal laws. Such covenants would technically be triggered in the event a borrower does not comply with government regulations to cease business operations. Lenders should be aware of any provisions that trigger an event of default if a borrower “goes dark” or fails to operate their business for a stated period of time, even if such actions are in compliance with applicable local, state and federal laws.

### Reporting Requirements

Most financing agreements include a requirement that the borrower provide annual audited financial statements within a certain period of time after its fiscal year-end. We expect that many borrowers will have difficulty complying with these time periods as accounting firms will not have access to their clients to conduct and complete audits within the required timeframe. Lenders should discuss this possibility with their borrowers when negotiating potential amendments and waivers.

## LENDER-SPECIFIC CONSIDERATIONS

Many of the sections above will be applicable to both lenders and borrowers, however, the following sections highlight lender-specific considerations. Lenders face tough decisions during a crisis when analyzing new advance requests and amendment or waiver negotiations with borrowers.

### Requests for Additional Information

Lenders should take advantage of provisions in their financing agreements which allow them to request business information, updated projections and financial information from their borrowers in addition to what is routinely required in the agreements. This will enable lenders to more effectively and pre-emptively address anticipated issues and potential defaults that will arise during the next several months and for the remainder of the calendar year.

### Waivers and Amendments

Lenders should anticipate a substantial increase in requests for waivers and amendments from borrowers. It is important for lenders to confirm that their loan to value and collateral coverage is sufficient before any amendment or waiver is entered into. Lenders should always obtain the necessary internal approvals for any modification and discuss the process of properly reserving their rights with legal counsel prior to entering any forbearance or pre-workout negotiations with a borrower. Time is of the essence in crisis situations, but it is important for lenders to properly reserve their rights when negotiating modifications or certain rights of the lender may be lost in the process.

### Conditions to Advance Requests

If a lender determines that a condition to funding has not been met, the lender can either (i) fund the advance, while properly reserving its rights under the terms of the applicable financing agreement or (ii) refuse to grant the advance request by providing notice to the borrower accompanied by a detailed explanation of such rejection. In such situations, all amendments to existing financing agreements should contain the lender's reservation of rights in order to maintain the lender's rights and remedies while providing the borrower the short term flexibility it may urgently need.

If you have questions or would like more information as the COVID-19 crisis continues to unfold, please contact Jennifer Santangelo ([santangeloj@whiteandwilliams.com](mailto:santangeloj@whiteandwilliams.com); 215.864.7199), Maulin Vidwans ([vidwansm@whiteandwilliams.com](mailto:vidwansm@whiteandwilliams.com); 215.864.6369) or Andrew Marrinucci ([marrinuccia@whiteandwilliams.com](mailto:marrinuccia@whiteandwilliams.com); 215-864-6224).

As we continue to monitor the novel coronavirus (COVID-19), White and Williams lawyers are working collaboratively to stay current on developments and counsel clients through the various legal and business issues that may arise across a variety of sectors. Read all of the updates [here](#).

This correspondence should not be construed as legal advice or legal opinion on any specific facts or circumstances. The contents are intended for general informational purposes only and you are urged to consult a lawyer concerning your own situation and legal questions.

