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SHORING-UP DISTRESSED CROSS-BORDER LOANS

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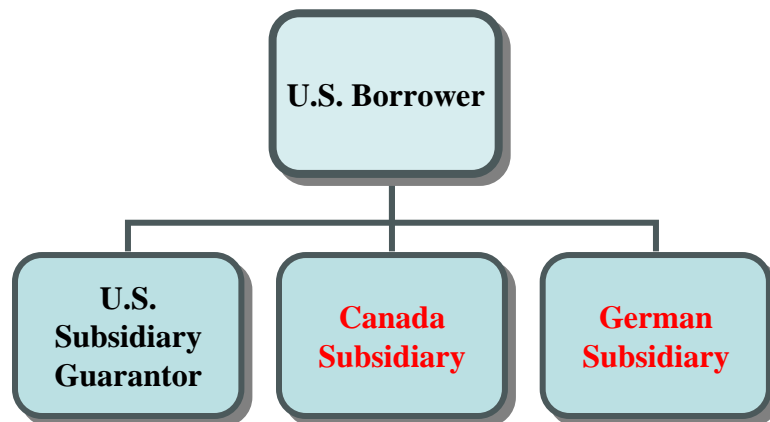
Prior to the 2008 credit crisis, U.S. lenders often did not require collateral or guaranties from foreign subsidiaries

Common reasons for exclusion:

- **Limit transaction costs**
 - Avoid involving non-U.S. local counsel; complexities of foreign law
- **Perceived sufficiency of U.S. credit support when loan was first made**
- **Avoid § 956 Deemed Dividends**
 - May be triggered by any of the following:
 - Foreign subsidiary guaranties debt of U.S. parent
 - Foreign subsidiary grants lien to secure debt of U.S. parent
 - Pledge of 2/3 or more of foreign subsidiary's voting shares to secure debt of U.S. parent
 - Amount of deemed dividend: Capped at foreign subsidiary's earnings not previously taxed in U.S.
- **Foreign law issues**
 - Corporate governance laws (corresponds to U.S. fraudulent conveyance laws)
 - Financial assistance laws (limit credit support for leveraged buy-outs)
 - Regulatory issues

Importance of shoring up distressed cross-border loan with available foreign assets and guaranties

- **Improve collateral coverage** (especially if operations have shifted outside of the U.S. since the original closing of the loan)
- **Limit risks in allocation fights**



If consolidated business is sold in an insolvency proceeding, how much of the sales price will be allocated to the operations of the U.S. entities (where the lender has liens) and how much will be allocated to the foreign subsidiaries (where the lender does NOT have liens)?

Consider:

- Existing indebtedness, wage and tax claims and other obligations of foreign subsidiaries
- U.S. vs. foreign asset values/EBITDA
- Intellectual property issues (including inter-company licenses)

Original reasons for excluding foreign credit support may no longer be relevant once loan becomes distressed

- **Limit transaction costs**
 - *Costs now may be justified to improve collateral position*
 - *Recent legal reforms may have streamlined the process (e.g., France)*
- **Perceived sufficient U.S. credit support when loan was first made**
 - *Now that loan is distressed, there is likely to be an increased need for additional credit support*
- **Avoid § 956 Deemed Dividends**
 - *There may now be little, if any, actual economic impact from such a dividend*
 - *May be significant NOLs to offset tax*
 - *Foreign subsidiary's undistributed earnings may have declined*
 - *Weigh borrower's tax costs vs. lender's need for additional credit support*

Original reasons for excluding foreign credit support may no longer be applicable once loan becomes distressed (cont.)

- **Foreign law issues**
 - **Corporate governance laws** (corresponds to U.S. fraudulent conveyance laws)
 - *Loan restructure may involve significant corporate benefit to foreign subsidiaries*
 - *Especially if additional loan proceeds are made available to foreign subsidiaries*
 - *May help foreign subsidiaries avoid insolvency*
 - **Financial assistance laws** (limit credit support for leveraged buy-outs)
 - *Likely would not apply to additional loans made in a restructure*
 - *Laws may have changed since original closing (e.g., England, October 2008 for private companies)*
 - **Regulatory issues**
 - *May not apply to obtaining foreign collateral/guaranties (as opposed to making a foreign loan)*
 - *Laws may have changed (e.g., Canada, withholding tax limitation, January, 2008)*

Initial steps to shore up foreign collateral/guaranties

1. Consider timeline -- avoidance/preference periods

- ***Importance of starting the process early***

Often takes longer to obtain foreign (than domestic) collateral/guaranties

- Need to evaluate foreign laws
 - Need to involve people that are located outside of the country and that may be new to the transaction (e.g., foreign lawyers, business people and directors)
 - Increased formalities/complexities (e.g., involved notary process, document translation and powers of attorney)
 - Foreign directors may be hesitant to act due to potential personal liability
- ***Evaluate preference exposure***

Initial steps to shore up foreign collateral/guaranties (cont.)

2. Review existing loan file with respect to foreign collateral/guaranties

- **Identify existing foreign collateral/guaranties and consider need to update collateral documents/filings**
 - Assets acquired post-closing may require updates (there may be no “floating lien” concept in the foreign jurisdiction)
 - Review collateral locations (e.g., Germany – lien on inventory only extends to inventory located at specific locations described in collateral documents)
 - Review anti-assignment clauses in sales contracts (may invalidate liens on resulting accounts receivable)
- **Review priority of existing liens**
 - Update lien searches (if available)
 - Review status of any “preferential claims”, such as
 - Wage and tax claims
 - Unsecured creditor carve-outs (e.g., U.K., Belgium, Finland and Sweden)
 - Insolvency costs (e.g., Germany)
 - Review retention-of-title claims on inventory and equipment (and extended ROT claims in Germany)
- **Identify available additional foreign collateral/guaranties**

Implementing additional foreign credit support

1. Regulatory issues

- **Making new loans to foreign subsidiaries**
 - Consider need for governmental approvals
 - “One-off” exceptions (e.g., Canada, Germany)
 - Requisite level of lending activity (e.g., Netherlands)
 - Need for governmental approval (e.g., India)
 - Withholding taxes
 - Repatriation issues
- **Obtaining liens/guaranties (often fewer regulatory hurdles)**

Implementing additional foreign credit support (cont.)

2. Guaranties

- **Corporate governance**
 - Strict vs. liberal approach to defining “corporate benefit”
 - Canada, Mexico and the United Kingdom are examples of the more liberal approach, and may consider overall benefit to the “corporate group”
 - Laws in other countries may be stricter and require that specific and direct consideration be received by the guarantor
 - May be easier to demonstrate corporate benefit during a loan work-out
 - Structuring techniques
 - Access to loan proceeds
 - Guaranty fee
- **Financial assistance laws (consider when guarantying acquisition loans)**

Implementing additional foreign credit support (cont.)

3. Issues re liens on specific asset types

- **Accounts receivable**
 - Choice of law issues (law of receivable owner, account debtor or governing law of sales contract?)
 - Future receivables (may require collateral updates)
 - May need to notify account debtors
 - Priority issues (e.g., U.K. “floating charges”; level of cash dominion)
- **Inventory/Equipment**
 - Retention-of-title claims
 - Future inventory/equipment (may require collateral updates)
 - Availability of non-possessory liens (e.g., Switzerland)
 - Priority issues (e.g., U.K. “floating charges” re inventory)
- **Real estate**
 - Foreign ownership restrictions
- **Intellectual property**
 - Consider inter-company issues
 - May be difficult to obtain lien on certain forms of IP
- **Shares/Equity pledges**
 - Choice of law issues (generally best practice to have pledge governed the law of the issuer (*i.e.*, the law of the foreign subsidiary))

Implementing additional foreign credit support (cont.)

4. Enforcement considerations

- **Foreign enforcement options**
- **Quality/efficiency of foreign courts**
- **Availability of self-help remedies (e.g., security trust in Mexico)**
- **Likely forum for bankruptcy/insolvency proceedings**
 - Increased willingness of U.S. bankruptcy courts to accept jurisdiction
 - Centre of Main Interests (COMI)
 - UNCITRAL Model Law
 - Chapter 15 of U.S. Bankruptcy Code
 - EU Insolvency Regulation (all EU members, except Denmark)