

Introduction to the LMA Schuldschein Loan Agreements and User Guide

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Genesis of the LMA Schuldschein Documentation

- > At the request of several members, the LMA initially considered the idea of producing standard-form documentation in 2013. At the time, however, the majority of key market players, for various reasons, did not think the time was right and the initiative was not taken further.
- > Instead, in 2014, a “Product Guide” was published by the LMA, setting out the key commercial elements and a description of the contents of some typical clauses in Schuldschein loan agreements, without containing any standard form documentation.
- > In 2016 a revised edition of the Product Guide was released.

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- > Since then, the market has formed the view that it would be beneficial for Schuldschein documentation to be standardised. This was driven by the following key considerations:
 - > the growing economic significance of Schuldschein loans, which partially substitute syndicated loans. Documentation for the latter was standardised at the end of the 1990s, resulting in a significant increase in efficiency for the primary and secondary markets;
 - > demand from the market for a standard format, particularly from international market players;

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- > protecting the essence of Schuldschein documentation – this would appear to be necessary, particularly in light of the increasing internationalisation of the market, new players consistently coming into the market and the resulting tendency to adopt structural elements from syndicated loans and securities when structuring Schuldschein loan terms, thus mixing together the economic and legal differences of the various contract forms in the process;
- > improving the efficiency of the Schuldschein market, and particularly of the documentation process, allowing the contracting parties to focus on the essentials;
- > facilitating transfers in order to further the development of a secondary market that is currently still quite limited;

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- > facilitating the use of receivables from Schuldschein loans for refinancing at central banks;
- > supporting new technology, such as blockchain and trading platforms;
- > facilitating the hedging of receivables from Schuldschein loans using credit derivatives and other forms of risk mitigation; and
- > establishing a fixed starting point for the purposes of regulatory classification of Schuldschein loan agreements, including for the purposes of US securities laws.

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- > Insurers subject to Solvency II can also avail themselves of the standard form (loan agreement with respect to a Schuldschein loan with negative pledge (*Darlehensvertrag über ein Schuldscheindarlehen mit Negativerklärung*)) published by the German Insurance Association (Gesamtverband der Deutschen Versicherungswirtschaft e. V.) in August 2018 in "Credit guide for Solvency II insurers – guidance for granting of corporate credits by insurers – Schuldschein loans" (Kreditleitfaden für Solvency II Versicherer – Orientierungshilfe für die Vergabe von Unternehmenskrediten durch Versicherer – Schuldscheindarlehen).
- > This differs from the Schuldschein Documents in some areas. Insurers subject to Solvency I, when they wish to ensure collateral pool eligibility of the loans disbursed by them, also often deviate from the Schuldschein Documents.

Assumptions underlying the LMA Schuldschein Documentation

- > The Schuldschein Documents are based on the following assumptions:
 - > the borrower is a German entity. The conscious decision was made not to put together a template for a Schuldschein loan for public-sector borrowers.
 - > the guarantor is a German entity.
 - > the Schuldschein loan agreement is governed by German law.
 - > the loan will be exclusively denominated and issued in euros.
 - > the borrower has a solid investment grade rating or, for borrowers that are not rated, an adequate level of creditworthiness.

Assumptions underlying the LMA Schuldschein Documentation

- > the contractual terms will be specifically and individually negotiated between the parties to the agreement, using the template agreement as a basis for the documentation.
- > the granting of the loan is permitted from a banking supervisory law perspective.
- > the paying agent is in Germany.

Assumptions underlying the LMA Schuldschein Documentation

- > There are currently two Schuldschein Documents; one with, and one without, an integrated (downstream) guarantee.
- > Some provisions, such as a right of voluntary prepayment in return for payment of a make-whole premium in cases of fixed-interest Schuldschein loans, were seen as being too specific to be included in the Schuldschein Documents, which merely represent an initial starting point for contract negotiations.
- > However, the User Guide does include comments and proposed wording for this and similar issues, which can be incorporated into the Schuldschein Documents where such a provision is required.

Assumptions underlying the LMA Schuldschein Documentation

- > Each Schuldschein Document can be used to create a stand-alone contract. Templates for ancillary contracts such as, for example, a paying agency agreement, have not yet been prepared.
- > In this context, users should continue to rely on the templates that have been available to date. Given that the paying agent is not a party to the Schuldschein loan agreement, users will need to ensure that the paying agency agreement reflects all duties assigned to the paying agent in the Schuldschein Document.
- > Likewise, no templates have been devised for agreements and documents relating to the placing of Schuldschein loan agreements, in particular, no engagement letter or marketing term sheet has been prepared. Here also, users should continue to use (their) tried and tested templates.

Assumptions underlying the LMA Schuldschein Documentation

- > The Schuldschein Documents are available in both the German and English language.
- > If the agreements are drafted in both languages then one version should be designated as the binding version and the other as being provided for information purposes only, in order to avoid a lack of legal certainty as a result of any potential differences between the two versions.
- > Irrespective of the language in which they are drafted, the Schuldschein Documents are governed by German law, as the Schuldschein loan agreement is a German-specific type of agreement, which can be lean in nature due to the relevant applicable German civil law provisions.

Key terms of the LMA Schuldschein Documentation

> **Floating or fixed interest rates**

- > The Schuldschein Documents provide for either floating (marked in red) or fixed (marked in blue) interest rates. When preparing the agreement, one or the other option is to be consistently selected throughout the agreement and all passages relating to the option not chosen are to be deleted.

> **Guarantee**

- > There is one Schuldschein Document with, and one without a (downstream) guarantee by a parent company of the borrower. Where the parties intend to amend the guarantee such that the Schuldschein loan is taken on by a sister or subsidiary company of the borrower, the parties will need to determine whether limitation language needs to be agreed for the guarantee, in particular in order to meet capital maintenance requirements and to rule out potential liability on the part of guarantor entities and/or their directors and officers. The Schuldschein Documents do not include proposals for this.

Key terms of the LMA Schuldschein Documentation

> **Clause 1 (*Definitions*)**

- > The definitions of terms repeatedly used in the Schuldschein Documents are found here. Terms defined in Clause 1 do not have distinguishing formatting (such as, for example, italics or bold font) in the remainder of the text; this is in order to prevent a situation where this distinguishing feature is not (consistently) used in the remainder of the text if the user adds new defined terms. Defined terms that are only used in one paragraph or in the definitions section are only defined in such paragraph or section.

> **Clauses 2 (*Disbursement; Purpose*) to 7 (*Taxation; Increased Costs*)**

- > Criteria for the disbursement of the loan;
- > calculation of interest, determination of the interest periods and interest payments;
- > repayment on maturity and prepayment;
- > payment mechanisms and paying agent; and
- > taxation and increased costs.

Key terms of the LMA Schuldschein Documentation

> **Clauses 8 (*General Undertakings*) to 10 (*Event of Default*)**

- > The following provisions are set out in the Schuldschein Documents as a starting point for the credit-related, transaction specific provisions:
 - > certain general undertakings, including a negative pledge, a disposals covenant and a pari passu undertaking;
 - > information undertakings; and
 - > rights of termination.

- > It is these sections in particular, that will have to be adapted to the specific transaction and, where applicable, modified. Given that the Schuldschein Documents are based on the assumption that the borrower has a solid investment grade rating or an adequate level of creditworthiness, financial covenants were deliberately not included in the template.

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> **Clause 11 (*Guarantee*)**

- > If a guarantee is being issued for the loan, provision should be made for the guarantee at this point and the numbering of the following clauses is to be adjusted accordingly.

> **Clause 11/12 (*Transfer*)**

- > The conditions for a transfer, the permitted transferees and the mechanics of the transfer are set out in this clause.

> **Clauses 12/13 (*Confidentiality*) to 15/16 (*Miscellaneous*)**

- > Certain standard (Schuldschein) loan agreement provisions are set out in these sections, including:
 - > confidentiality; and
 - > exclusion of joint and several liability on the part of the lenders and a declaration stating that the rights of the lenders in connection with the agreement are not joint and several.

Key terms of the LMA Schuldschein Documentation

> **Clauses 12/13 (*Confidentiality*) to 15/16 (*Miscellaneous*)**

- > Certain standard (Schuldschein) loan agreement provisions are set out in these sections, including:
 - > notices;
 - > AML/KYC-specific provisions;
 - > extensive exclusion of set-off on the part of the borrower;
 - > partial invalidity;
 - > governing law;
 - > jurisdiction;
 - > exclusion of the lender's general terms and conditions; and
 - > written form requirement for changes to the contract.

> **Annexes to the Schuldschein Document**

- > List of conditions precedent; and
- > a form of a transfer certificate.

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