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The Legal 500 Country Comparative Guides

United States

ACQUISITION FINANCE

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This country-specific Q&A provides an overview of acquisition finance laws and regulations applicable in United States.

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UNITED STATES
ACQUISITION FINANCE

1. What are the trends impacting acquisition finance in your jurisdiction and what have been the effects of those trends? Please consider the impact of recent economic cycles, Covid-19, developments relating to sanctions, and any environmental, social, and governance ("ESG") issues.

The economic impact of COVID-19 related fiscal stimulus and supply chain disruptions, and the impact of macro-economic developments related to the war in Ukraine and related sanctions has led to accelerating inflation in the US and globally, which has in turn led to multiple continuing interest rate increases. These have slowed growth and depressed asset values, leading to both a decrease in M&A volume and an increase in the cost of debt financing to borrowers. This volatility resulted in broadly syndicated leveraged loans trading down in secondary markets and made new issuance punitively expensive, closing the window for syndicated leveraged lending.

Dislocations in the syndicated loan market resulting from depressed secondary trading prices created an opportunity for private credit to play an increasingly prominent role in US acquisition financings, including in larger "mega-unitranche" structures. Large investment banks and other arrangers of syndicated debt have struggled for most of the year to offload large commitments written during the frothy months at the end of '21 and early in 2022.

Backed by private credit and direct lending funds, volume for "core" middle market acquisition financing has remained relatively robust in the second half of 2022.

2. Please advise of any recent legal, tax, regulatory or other developments (including any reforms) that will impact foreign or domestic lenders (both bank and non-bank lenders) in the acquisition finance market in your jurisdiction.

2022 has brought some notable case law developments that will affect lender expectations in the US both in and out of bankruptcy. In October of 2022, "make-whole" premiums were ruled by the US Court of Appeals for the Fifth Circuit to be generally disallowed as unmatured interest in US bankruptcy proceedings, unless certain relevant exceptions applied, including if the debtor was solvent at the time of filing of the applicable bankruptcy case. This ruling adds to a growing and varied body of case law on the issue and casts additional doubt on whether lenders should expect for such amounts and other call premiums to be included in their secured claims in US bankruptcies.

Minority lender plaintiffs have also notched a series of recent victories in attacking non-pro rata uptiering liability management transactions, most recently in the New York court's denial of defendants' motion to dismiss in the *Boardriders* decision which, among other things, supported the possibility that liability management transactions negotiated with majority lenders that are not offered pro rata to all lenders may in certain circumstances violate the implied duty of good faith and fair dealing under New York law, separate and apart from whether the transaction complied with the relevant contractual provisions.

3. Please highlight any specific high level issues or concerns in your jurisdiction that should be considered in respect of structuring or documenting a typical acquisition financing.

Deal certainty is a central concern in US acquisition financings – certainty as to conditionality and terms. For conditionality, US acquisition agreements often lack a financing out, and a buyer is required to consummate an acquisition regardless of whether their financing sources fund. Consequently, buyers look to align financing and

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acquisition conditionality to ensure no daylight exists between the two. Sellers are motivated to seek the same alignment to ensure buyers will have the capital required to consummate the acquisition. Market practice has evolved to balance the interests of buyers as borrowers and their financing sources. Related provisions are often referred to as “SunGard” provisions, so-named after the company in the first deal to contain those provisions.

With respect to terms, buyers seek to negotiate them to the fullest extent possible prior to signing an acquisition agreement. Buyers often request their financing sources underwrite a precedent credit agreement to address terms beyond the scope of a typical term sheet alongside a very detailed term sheet. In private credit financings, financing have very limited ability to alter the agreed terms, which results in exceptional focus on underwritten terms. In syndicated financings, financing sources typically have additional flexibility to modify terms to ensure a successful syndication through “market flex” rights. Buyers seek to minimize “market flex” provisions and sellers seek to avoid flex provisions that go to financing quantum or conditionality.

4. What are the legal and regulatory requirements for banks and non-banks to be authorised to provide financing to, and to benefit from security provided by, entities established in your jurisdiction?

While there is no US federal regulatory framework applicable to non-bank lenders that are engaged in commercial lending in the US, a few US states require non-bank lenders to obtain a license prior to engaging in commercial lending activities (i.e., lending activities engaged in between corporate lenders and corporate/institutional borrowers for business or commercial purposes) under certain circumstances. The commercial lending licensing requirements of some of these states are generally triggered only when a commercial loan is secured by real property located in one of such states. However, in California, commercial lending license requirements may be implicated regardless of whether a commercial loan is secured by real property located in the state. As such, California is the state that is most often implicated in the commercial lending context due to the broad scope of California’s commercial lender licensing requirement. The US states that may impose commercial lending licensing requirements (unless an exemption from such licensing requirements applies), generally include, but are not limited to: California, Florida, Nevada, North Dakota, South Dakota and Vermont.

While New York does have a commercial lending licensing requirement, such requirement is only applicable to business and commercial loans in a principal amount of US$ 50,000 or less that also meet other specified conditions.

5. Are there any laws or regulations which govern the advance of loan proceeds into, or the repayment of principal, interest or fees from, your jurisdiction in a foreign currency?

U.S. Federal law does not impose any restrictions or controls on either the advancement of loan proceeds in foreign currencies or the payment of interest or fees (or repayment of principal) in a foreign currency. Rather, such restrictions will often depend on the ability of individual lending institutions to provide loans in a particular foreign currency or otherwise to receive payments in such foreign currency. Lenders should take into account federal sanctions and anti-money laundering laws which require financial institutions to implement due diligence procedures with respect to their customers to prevent the transfer of cash to certain prohibited countries and persons.

6. Are there any laws or regulations which limit the ability of foreign entities to acquire assets in your jurisdiction or for lenders to finance the acquisition of assets in your jurisdiction? Please include any restrictions on the use of proceeds.

Special rules may apply depending on the industry and asset, but typical areas of regulatory approval for acquisitions (or financings thereof) include US antitrust regulations, foreign direct investment laws applicable to the industry and asset (for example CFIUS approvals), along with customary sanctions, anti-money laundering and KYC rules that apply to lenders generally.

7. What does the security package typically consist of in acquisition financing transactions in your jurisdiction and are there any additional security assets available to lenders?

Typically non-investment grade acquisition financing transactions are supported by “all asset” liens (subject to agreed exceptions) over the assets of the target and its subsidiaries and an equity pledge by a holding company in the top tier operating company.

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8. Does the law of your jurisdiction permit (i) floating charges or any other universal security interest and (ii) security over future assets or for future obligations?

For personal property, yes to both.

9. Do security documents have to (by law) include a cap on liabilities? If so, how is this usually calculated/agreed?

No and would be uncommon for personal property. For real property, caps are sometimes agreed to reduce any mortgage recording tax or title fees.

10. What are the formalities for taking and perfecting security in your jurisdiction and the associated costs and timing? If these requirements are different for different asset classes, please outline the main points to note for each of these briefly.

For personal property, a security or pledge agreement describing the collateral either specifically or by asset classes would create the security interest. Perfection can generally be accomplished by filing a UCC financing statement. Perfection by possession or "control" is either permissible or, for some assets, required for perfection. Certain assets are subject to special perfection rules such as noting the lien on the certificate of title for motor vehicles or making certain federal filings, e.g. for registered copyrights or aircraft. For real property, execution and delivery of a mortgage or deed of trust and their recordation in the real estate recording office is generally required.

11. Are there any limitations, restrictions or prohibitions on downstream, upstream and cross-stream guarantees in your jurisdiction? Please also provide a brief description of any potential mitigants or solutions to these limitations, restrictions or prohibitions.

US guarantees fall into three categories, namely (i) "downstream" guarantees whereby a parent company guarantees the debt of its subsidiary, (ii) "upstream" guarantees whereby a subsidiary guarantees the debt of its parent entity, and (iii) "cross-stream" guarantees whereby a subsidiary guarantees the debt of a sister company. Hence, US companies are generally permitted to guarantee and secure the obligations of another group member, subject to certain considerations and limitations. To be enforceable, the guarantee needs to comply with certain general principles like receipt and sufficiency of consideration and, in some states, be in writing and duly executed by the guarantor to comply with the Statute of Frauds. However, showing direct corporate benefit to the is not necessary to determine sufficiency of consideration where such intercorporate guarantee benefits the group as a whole. In insolvency proceedings, corporate benefit consideration is relevant to determine whether such guarantee can be challenged as a fraudulent transfer under the US Bankruptcy Code.

12. Are there any other notable costs, consents or restrictions associated with providing security for, or guaranteeing, acquisition financing in your jurisdiction?

For personal property, generally only nominal filing costs, with more substantial filing taxes in some states. Additionally, for assets with specific perfection requirements, such as certificates of title for motor vehicles, costs can rise based on the number of such assets. Real estate recording fees and title insurance can be substantial but costs vary widely among US jurisdictions.

13. Is it possible for a company to give financial assistance (by entering into a guarantee, providing security in respect of acquisition debt or providing any other form of financial assistance) to another company within the group for the purpose of acquiring shares in (i) itself, (ii) a sister company and/or (iii) a parent company? If there are restrictions on granting financial assistance, please specify the extent to which such restrictions will affect the amount that can be guaranteed and/or secured.

Generally, the US does not have any restrictions on "financial assistance" that would prohibit providing guarantees or security to support borrowings to finance the acquisition of a target company. However, there may be regulatory issues to consider when the guarantee or security provider is a specialized or regulated entity. Fraudulent transfer issues are also relevant when guarantees and/or security are provided to support borrowings to acquire another company. The company and the lenders will need to be comfortable with the

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solvency of the guarantors and security providers, requiring solvency representations to this effect.

14. If there are any financial assistance issues in your jurisdiction, is there a procedure available that will have the effect of making the proposed financial assistance possible (and if so, please briefly describe the procedure and how long it will take)?

N/A

15. If there are financial assistance issues in your jurisdiction, is it possible to give guarantees and/or security for debt that is not pure acquisition debt (e.g. refinancing debt) and if so it is necessary or strongly desirable that the different types of debt be clearly identifiable and/or segregated (e.g. by tranching)?

N/A

16. Does your jurisdiction recognise the concept of a security trustee or security agent for the purposes of holding security, enforcing the rights of the lenders and applying the proceeds of enforcement? If not, is there any other way in which the lenders can claim and share security without each lender individually enforcing its rights (e.g. the concept of parallel debt)?

Yes.

17. Does your jurisdiction have significant restrictions on the role of a security agent (e.g. if the security agent in respect of local security or assets is a foreign entity)?

Not typically.

18. Describe the loan transfer mechanisms that exist in your jurisdiction and how the benefit of the associated security package can be transferred.

The administrative agent maintains a register and transfers are recorded by the administrative agent. Credit Agreements frequently limit who can become a lender either by entity type and/or net worth and may include a list of disqualified transferees. Consent of the Agent and in some cases the Borrower may also be required.

19. What are the rules governing the priority of competing security interests in your jurisdiction? What methods of subordination are used in your jurisdiction and can the priority be contractually varied? Will contractual subordination provisions survive the insolvency of a borrower incorporated in your jurisdiction?

For most personal property, priority follows the order of perfection; however, for categories of personal property with multiple methods of perfection, certain methods are afforded priority even over a prior secured interest perfect solely by filing a UCC financing statement. Priority rules for real property vary among jurisdictions. A secured party entitled to priority may subordinate its security interest to the security interest of another secured party. A creditor may also subordinate its right to payment. Generally, these contractual agreements will be respected in bankruptcy.

20. Is there a concept of “equitable subordination” in your jurisdiction whereby loans provided by a shareholder (as a creditor) to a company incorporated in your jurisdiction are subordinated by law upon insolvency of that company in your jurisdiction?

Yes, shareholder loans are not automatically subordinated but may be at greater risk of being equitably subordinated. The doctrine of equitable subordination can apply if the offending creditor engaged in some type of inequitable conduct which resulted in injury to other creditors of the debtor or conferred an unfair advantage to such offending creditor.

21. Does your jurisdiction generally (i) recognise and enforce clauses regarding

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choice of a foreign law as the governing law of the contract, the submission to a foreign jurisdiction and a waiver of immunity and (ii) enforce foreign judgments?

Yes, subject to certain exceptions and limitations.

22. What are the requirements, procedures, methods and restrictions relating to the enforcement of collateral by secured lenders in your jurisdiction?

For personal property, outside of bankruptcy, a creditor would avail itself of a number of "self-help" options to foreclose without need for judicial intervention, including the ability to dispose of the relevant collateral in a public or private sale meeting certain commercial reasonableness and notice criteria.

23. What are the insolvency or other rescue/reorganisation procedures in your jurisdiction?

The Bankruptcy Code is the primary corporate insolvency law in the US, which provides alternative regimes for reorganization under chapter 11 or liquidation under chapter 7. Each state also has statutes that provide rules for of receivership or assignment for the benefit of creditors, which can vary substantially by state.

Chapter 11 is a court-supervised process to restructure a company's debts. The process is designed to allow the company to operate in the ordinary course, emerge with a stronger balance sheet, and maintain board and management in control of operations, subject to court oversight and the rights of parties in interest to be heard. The company is characterized as a "debtor-in-possession." The goal is for the company to develop a plan of reorganization with major stakeholders to restructure its debts.

Chapter 7 is a court-supervised process used to liquidate a company in an orderly manner. These cases do not involve the filing of a plan of organization. Instead, a bankruptcy trustee marshals and sells the debtor's non-exempt assets and uses the proceeds to pay holders of claims in accordance with the Bankruptcy Code. Typically, secured creditors will be paid from the value of their collateral, subject to the potential to surcharge for the costs of preserving and realizing the collateral.

24. Does entry into any insolvency or other process in your jurisdiction prevent or delay secured lenders from accelerating their loans or enforcing their security in your jurisdiction?

Yes, the automatic stay under the bankruptcy code would apply in appropriate circumstances.

25. In what order are creditors paid on an insolvency in your jurisdiction and are there any creditors that will take priority to secured creditors?

Certain administrative claims will be paid first. Next, secured parties will be paid in order or priority followed by unsecured or under-secured claims.

26. Are there any hardening periods or transactions voidable upon insolvency in your jurisdiction?

Transfers on account of an antecedent debt made within the 90 days prior to the bankruptcy filing when the debtor was insolvent are avoidable if they permit the creditor to receive more than they would in a hypothetical chapter 7 liquidation. The 90 day period is extended to one year for insiders. There are a variety of statutory defenses and safe harbors to preference claims.

27. Are there any other notable risks or concerns for secured lenders in enforcing their rights under a loan or collateral agreement (whether in an insolvency or restructuring context or otherwise)?

For personal property, secured creditors generally must proceed in a commercially reasonable manner or risk losing their deficiency and potentially being liable for damages.

28. Please detail any taxes, duties, charges or related considerations which are relevant for lenders making loans to (or taking security and guarantees from) entities in your jurisdiction in the context of acquisition finance, including if any withholding tax is applicable on payments

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(interest and fees) to lenders and at what rate.

The US federal government generally imposes a 30% withholding tax on interest paid to non-US lenders on a debt obligation of a US person (and certain non-US persons engaged in trade or business in the US). For this purpose, payments with respect to any original issue discount, if not considered less than de minimis, are also treated as interest income and subject to such withholding tax.

If a lender is qualified for the benefits of an applicable double taxation treaty between the US and its country of residence, the withholding tax may be reduced or eliminated.

Alternatively, a non-US lender may qualify for exemption under the "portfolio interest exemption" (PIE). To qualify, the lender must neither (i) be a controlled foreign corporation related to the borrower or a bank receiving interest on an extension of credit entered into in the ordinary course of its trade or business nor (ii) own (directly, indirectly or by attribution) equity representing 10% or more of the borrower's total combined voting power of all voting stock (or, if the borrower is a partnership, 10% or more of its capital or profits interest). The PIE is only available for debt in "registered form" for US federal income tax purposes, and does not apply to certain contingent interest, such as interest determined by reference to any receipts, sales, cash flow, income or profits of, or the fluctuation in value of property owned by, or dividends, distributions or similar payments by, the borrower or a related person.

To claim an exemption or reduction under an applicable double taxation treaty or the PIE, the beneficial owner of interest must generally submit a completed IRS Form W-8BEN-E (or, if an individual, IRS Form W-8BEN).

If interest paid to a non-US lender is effectively connected with such lender's trade or business in the US, such interest will not be subject to US federal withholding if such lender submits a completed IRS Form W-8ECI, but will generally be subject to net income tax in the US and, for foreign corporations, branch profits taxes.

Other exemptions may be available for foreign governments or governmental entities assuming they provide the applicable completed IRS Form W-8EXP.

Withholding taxes may also apply upon: (i) payment to a US person that does not demonstrate an exemption by providing an applicable completed IRS Form W-9, (ii) payment of US source interest and certain other amounts to entities treated as "Foreign Financial Institutions" not eligible for an exemption from FATCA withholding tax, and (iii) payment of various fees (such as letter of credit fees), modifications to debt obligations, and various adjustments on debt obligations convertible into stock.

Payments under a guarantee are generally similarly treated, with the source of payments for US federal income tax purposes generally determined based on residence of the borrower. If the lender is receiving security proceeds, such transaction may generally be treated as a payment on the loan. Under certain circumstances, the lender may be treated as the owner of the foreclosed property, resulting in adverse tax consequences (especially cases of US real property held by a foreign lender).

29. Are there any other tax issues that foreign lenders should be aware of when lending into your jurisdiction?

Continuous and regular lending to US borrowers may result in the US government considering such person as engaged in US trade or business, requiring the lender to file a US tax return and pay income taxes on income attributable to such trade or business. Any activities considered secondary trading are generally exempted from such rules, irrespective of continuity or regularity. As such, foreign lenders should take care to limit the extent and scope of their origination activities. If foreign lenders that are engaged in extensive origination activity are also qualified for the benefits of a double taxation treaty and do not have a permanent establishment in the US, the foreign lenders may be protected under the rules of such treaty.

30. What is the regulatory framework by which an acquisition of a public company in your jurisdiction is effected?

The two primary means of acquiring public companies in the US, by tender offer and by shareholder vote and, in each case, a subsequent merger, are subject to US federal regulation by the Securities and Exchange Commission (SEC), which administers and enforces notice and disclosure requirements. The legal framework for acquisitions of public companies is otherwise a product of corporate law, which varies from state to state. By far, the most common state where public companies are incorporated is Delaware, and Delaware law provides both a one-step merger option, and a two-step tender offer option, as well as a tender offer followed by short form squeeze out option without the need for a shareholder vote. Upon meeting certain

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conditions, a tender offer with respect to a Delaware public company that achieves a greater than 50% threshold may be able to squeeze out the minority shareholders under the short-form merger statute without needing to proceed to a shareholder vote and deal with SEC disclosure requirements and timing delays resulting from a shareholder meeting.

31. What are the key milestones in the timetable (e.g. announcement, posting of documentation, meetings, court hearings, effective dates, provision of consideration, withdrawal conditions)?

For take private transactions adopting a tender offer structure, after announcement, the first key milestone is filing a Schedule TO and offer to purchase with the SEC. After tender offer materials are finalized (including SEC review and resolution of any SEC comments), the offer is mailed to the target stockholders and remains open for at least 20 business days. Upon tendering of a majority of the shares, the tender offer will be consummated and the buyer will have obtained control of the target. Shareholders are generally permitted to withdraw tendered shares during the pendency of the tender offer and the acquirer may withdraw the tender offer under certain circumstances. If a "short-form" merger is available, the buyer will squeeze out the remaining minority shareholders in exchange for the same cash consideration provided to accepting shareholders in the tender offer. If not available, the buyer will file proxy materials for a shareholder vote which, after SEC approval and review, are mailed to target shareholders. After the target shareholder meeting has occurred and the merger is approved, the merger proceeds to closing and merger consideration is then paid to shareholders. In a one-step merger structure, after announcement, the buyer immediately files preliminary proxy materials with the SEC. After SEC review and resolution of SEC comments, proxy materials are mailed to the target shareholders and the meeting is scheduled. The merger closes once the target shareholders approve the merger and merger consideration is then paid to shareholders. Closing of take private transactions are also generally subject to receipt of requisite regulatory clearances or approvals (e.g., antitrust or merger control).

32. What is the technical minimum acceptance condition required by the regulatory framework? Is there a squeeze out procedure for minority hold outs?

Subject to supermajority approval or special voting requirements in the target's governing documents, a bare majority is generally sufficient to approve a merger.

33. At what level of acceptance can the bidder (i) pass special resolutions, (ii) de-list the target, (iii) effect any squeeze out, and (iv) cause target to grant upstream guarantees and security in respect of the acquisition financing?

Assuming Delaware law applies (and unless the charter or bylaws specifies otherwise), (i) stockholder resolutions generally require a majority vote, (ii) de-listing would occur when the acquisition is consummated, so in a one-step merger generally after securing the majority stockholder vote and any requisite regulatory clearances or approvals, at which time the buyer would control the target and the de-listing would be effectuated upon closing the merger at that time, (iii) in a two-step merger, after the stockholders tender a majority of the shares and any requisite regulatory clearances or approvals are obtained, the buyer may execute a squeeze out merger as a second step without needing a further stockholder vote and (iv) granting guarantees and security would occur at closing date.

34. Is there a requirement for a cash confirmation and how is this provided, by who, and when?

There are no formal regulatory cash confirmation requirements. However, it is fraudulent for a person to announce its intention to conduct a tender offer without a reasonable belief that it will have the means to complete it, and Schedule TO and offer to purchase or proxy materials, as applicable, will each provide information as to the acquiror's financing arrangements and sources of funds.

35. What conditions to completion are permitted?

Generally, restrictions on permissible conditions to completion of take private transactions are governed primarily by market convention, negotiating leverage, regulatory requirements applicable to take private transactions (including antitrust and merger control) and the desire of the parties for deal certainty. Unlike certain funds deals in the United Kingdom that are subject to the takeover code, there is no similar regime mandating limits on conditionality for US take private transactions.

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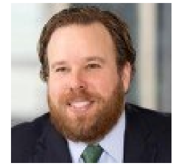

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