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Unanimous Lender Consent Provisions: Protection?

Law360, New York (September 23, 2009) -- Credit agreements typically provide that any amendment permitting the release of “all or substantially all” of the collateral requires the unanimous consent of the lenders.

Many market participants expect that this provision provides protection against the agent and other lenders from consenting to the sale of the collateral and releasing the corresponding liens without the consent of all lenders.

Contrary to this perception, however, three recent court opinions^[1] have concluded that the amendment provision does not apply when the agent exercises remedies against the collateral consistent with the rights originally granted to the agent by the lenders, as such an exercise does not require an amendment to the credit agreement.

Typical Credit Agreement Provisions

In most cases, secured credit agreements provide that any amendment providing for a release of “all or substantially all” of the collateral requires the unanimous consent of the lenders.

At the same time, credit agreements and the accompanying collateral documents provide for the appointment of an agent to act on behalf of the lenders.

This appointment typically authorizes the agent, upon the occurrence and continuation of an event of default, to enforce the rights of the secured parties’ interest in the collateral, either at the agent’s discretion or as required upon the direction of the majority of the lenders under the credit agreement.

GWLS Holdings

In *In re GWLS Holdings*, shortly after the debtor filed for bankruptcy, the court permitted a credit bid made by the agent on behalf of the debtor's lenders, for the purchase of substantially all of debtor's assets.

All of the first lien lenders consented to the credit bid except for Grace Bay Holdings II LLC, a holder of \$1 million of \$337 million first lien loans.

The credit agreement at issue provided that no waiver, amendment, supplement or modification to the loan documents which releases "all or substantially all of the collateral" could occur without the prior written consent of all lenders.

However, (1) the credit agreement also authorized the agent to "take such actions to exercise such powers as are delegated to the agents by the terms [of the credit agreement and the other loan documents] ... " and (2) the collateral agreement permitted the agent, upon the occurrence and continuation of an event of default, to exercise "all rights and remedies of a secured party under the New York UCC or any other applicable law ...," which included the ability to "sell, lease, license, sublicense, assign, give option or options to purchase, or otherwise dispose of and deliver the collateral or any part thereof."

Additionally, the first lien intercreditor agreement provided that "the First Lien Collateral Agent and the First Lien Secured Parties" have the exclusive right to exercise remedies against the collateral.

Grace Bay argued that the terms of the first lien intercreditor agreement provided that not only the agent, but the agent and the first lien lenders together had the exclusive right to exercise remedies against the collateral.

In addition, Grace Bay argued that because any amendment to the loan documents releasing "all or substantially all of the collateral" required the prior written unanimous consent of the lenders, the credit bid could not proceed without Grace Bay's consent.

The court rejected both arguments and found that (1) the first lien intercreditor agreement permitted both the agent and the lenders to separately exercise rights and remedies against the collateral and (2) the plain meaning of the loan documents authorized the agent to act on behalf of the lenders.

Most importantly, the court held that since the release of the collateral resulted from an exercise by the agent of the rights granted to it pursuant to the existing loan documents, the actions taken by the agent did not constitute an amendment to the loan documents, and therefore, did not require the prior written consent of all of the lenders.

Chrysler Bankruptcy

In *Ind. State Police Pension Trust v. Chrysler LLC (In re Chrysler LLC)*, the United States Court of Appeals for the Second Circuit had reason to revisit the issues

presented in GWLS Holdings when Chrysler sought court approval to sell substantially all of its assets over the objection of some of the prepetition secured lenders.

Chrysler's credit agreement provided that the agent, at the direction of the majority lenders, could enforce rights and remedies against the collateral.

The objecting lenders, referring to the consent requirement contained in Chrysler's loan documents, argued that the proposed sale could not occur without the prior written consent of all of the lenders.

Similar to GWLS Holdings, the Second Circuit held that because the loan documents specifically permitted the agent to exercise rights against the collateral at the direction of the majority lenders, the enforcement action "required no amendment to the loan documents, [and therefore] Chrysler was not required to seek, let alone receive ..." unanimous lender consent.

Metaldyne Bankruptcy

In *In re Metaldyne Corp.*, a consortium of approximately 97 percent of the lenders bid for substantially all of Metaldyne's assets. The bid included a credit bid using the full \$425 million of amounts owing under Metaldyne's credit agreement.

One lender who owned approximately \$3.5 million of loans objected to the credit bid on the basis that (1) the release of the liens in connection with the credit bid could not occur without the consent of all of the lenders under the credit agreement and (2) the agent was not authorized to make the credit bid to the full extent of the loans.

Relying on the reasoning set forth in *GWLS Holdings* and *Chrysler*, the court rejected these arguments and found that the lenders had authorized the agent to "exercise any and all rights afforded to a secured party under the Uniform Commercial Code or other applicable law," including the right to exercise remedies against the collateral.

Given that the proposed conduct was permitted by the loan documents and did not require an amendment to the loan documents, the credit bid was permitted to take place without unanimous lender consent.

Conclusion

Although lenders have voting rights with respect to amendments and waivers relating to a release of "all or substantially all" of their collateral, these voting rights may not protect lenders in situations where 363 sales, credit bids and out-of-court restructurings have become more common.

Rather, as the *GWLS Holdings*, *Chrysler* and *Metaldyne* courts concluded, the loan documents expressly authorized the agent to exercise remedies against collateral upon

the occurrence and continuation of an event of default at the direction of less than all of the lenders.

Because all of the lenders had granted the agent this authority when the credit agreements were originally executed, the release of the lenders' collateral did not constitute an amendment or waiver to the loan documents, and therefore, the provision requiring the unanimous consent of the lenders in order to affect a release was not applicable.

Although the full impact of these decisions remains to be seen, given that the loan documentation in these cases were not "off market," the decisions mark a dramatic shift in market participants' expectations and are likely to raise a number of significant issues in the leveraged loan market going forward.

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