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Coronavirus (COVID-19) Impacts Access to Working Capital Under Credit Facilities

The Coronavirus (COVID-19) pandemic has, or likely will have, negative economic consequences for many, including companies facing significantly reduced cash flow and unprecedented liquidity concerns as they attempt to meet obligations like payroll. Companies may need to utilize their credit facilities for working capital.

While the access to credit facilities is critically important, the negative economic conditions caused by COVID-19 could limit that access. Companies should understand the terms of their credit facilities to assess their ability to access capital, avoid being in default and proactively work to address any potential issues. In doing so, consideration to the following concerns must be given:

- **Financial Covenant Compliance.** Typical covenants cover items such as cashflow, debt service ratios and profitability. Companies impacted by the pandemic and potentially now out of compliance with financial covenants should likely request a waiver of those covenants for a period of time or an outright amendment of loan documents to address the potential long term effects of COVID-19.
- **Payment Default.** It goes without saying that the failure to pay principal and interest when due will constitute an event of default, triggering acceleration of outstanding debt and a shutdown of a credit facility. If it is clear a company cannot service existing debt and will be unable to make principal and/or interest payments, they should likely get ahead of the issue and speak with the lender to seek a waiver, forbearance or amendment to address the anticipated payment default.
- **Material Adverse Change.** Lenders may put a loan into default and/or suspend draws on a loan if there is a material adverse change in the borrower's business or prospects. As a practical matter, it is unlikely in the short-term that lenders will call a default to accelerate

principal and interest payments and foreclose on assets, as they would virtually have to default an overwhelming amount of outstanding loans as many may now have suffered such material adverse changes caused by COVID-19. However, in the medium to long term, default issues will need to be addressed and lenders may be forced to take dramatic action. As such, proactive discussions with lenders now many make sense to seek guidance, waivers and necessary amendments to address this "new normal". Whether or not a material adverse change provision will be used to suspend future advances is a much trickier question and the answer will vary on a case by case basis, but lenders are more likely to suspend advances in the short term rather than default and accelerate payment schedules. Borrowers with carefully negotiated loan documents may have exceptions to the material adverse change provisions for those arising out of general economic conditions such as COVID-19.



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- **Reporting Requirements.** Some borrowers have affirmative obligations to provide regular financial reporting and “information regarding the financial, assets and operations of its group as lenders may reasonably require”. It is very likely that lenders will be looking carefully at financial information provided, and will be requesting additional information as they must assess the financial wherewithal of borrowers. Borrowers should be aware of this as well as their lenders’ likely ability to require additional information. These requests may put a strain on already limited staff and resources.
- **Cross Defaults.** Loan documents very often contain provisions providing for an event of default and/or a suspension of the ability to draw on a credit facility if there are defaults under other loans or defaults under specified material agreements. As such, borrowers should not assume that defaulting on one obligation will not impact other loans.
- **Shutdown.** The suspension of a borrower’s business activities in normal situations would constitute an event of default. Some loan documents may contain exceptions for shutdown in extraordinary circumstances, such as COVID-19 or government order.

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