



McDermott  
Will & Emery

## The Credit Crunch

Proactive Steps in an Uncertain Financing Environment

**March 25, 2009**

**Michael Boykins**  
+1 312 984 7599  
mboykins@mwe.com

**Peter Humphreys**  
+1 212 547 5427  
phumphreys@mwe.com

**Gary B. Rosenbaum**  
+1 310 284 6133  
grosenbaum@mwe.com

1

## Problems

---

- Non-renewal or modification of credit lines
- Increased pricing for renewal and tightening of covenants
  - Addition of LIBOR floors
  - Equity cure right removal
- Potential breach of covenants raising possibility of event of default or termination / reduction of revolving credit facilities



The Credit Crunch – Proactive Steps in an Uncertain Financing Environment

2

## Problems

*Continued*

---

- Goodwill impairment issues
  - Annual test under FASB Rules
  - Negative Impacts on Net Income and Net Worth
  - Public company filings – Form 10-K
- “Going concern” qualification from external auditors raising need for waiver or modification under credit facility
  - “There is substantial doubt about our ability to continue as a going concern.”
  - Loan agreements generally require delivery of unqualified annual financial statements



McDermott  
Will & Emery

The Credit Crunch – Proactive Steps in an Uncertain Financing Environment

3

## Early warning signs of financial stress

---

- Upcoming loan maturity or amortization of debt
- Looming financial covenant defaults
- Failure to obtain proposed capital infusion
- Customer reduction in capital expenditures or other spending and deferral or termination of projects
- Loss or financial distress of major customer
- Product failure
- Significant adverse litigation result



McDermott  
Will & Emery

The Credit Crunch – Proactive Steps in an Uncertain Financing Environment

4

## Be proactive

---

- Analyze current debt structure to ascertain available options
- Explore other forms of financing well prior to termination of existing lines
- Address renewal issues (including pricing) early so as to give time to find more cost-effective financing
- Examine covenants regularly so as to anticipate problems
  - Commence “stress testing” of balance sheet
  - If necessary, start an early dialogue with lenders and auditors
- Identify potential defaults and discuss with lenders far in advance of their actual occurrence
- Consider impact of revolver drawdown



## Potential breaches of covenants

---

- Asset / liability tests
- Net worth covenants
- Earnings covenants (EBITDA)
- Indebtedness covenants
- Debt service / fixed charge coverage tests
- Cash flow coverage tests
- Working capital requirements
- Credit rating downgrades

**All of these are problematic in a declining market**



## Amend current financing

---

- Term facility
- Move from cash flow to asset-based credit facility
- Junior Capital
  - Move from second lien debt to mezzanine loans with higher pricing and equity components
- Secured borrowing
  - May allow covenant amendment
- Lengthen / shorten term of facilities
  - Lender may be more willing to vary covenants in shorter facility
  - Longer facility locks in capital source which may not be available in the future
  - Confirm ability to service debt with higher pricing due to increase in interest rate spread and payment of amendment fees



## Alternative forms of financing

---

- Move from revolving to term facilities
- Move from unsecured to secured borrowing
- Lengthen/shorten maturities of existing facilities
- Asset-backed market
- Corporate Bond market (144A and public)
- Stock issuance (144A and public)

**Look to trade flexibility for funding certainty**



## Debt restructuring

---

- Term loan buybacks
- Debt for debt exchanges
- Debt for equity exchanges
- Public company debt repurchase issues
  - “Quiet period” implications
  - Big-boy letters



## Asset-backed facilities

---

- Sales of receivables to conduit facilities
  - Availability in current market
- Advantages
  - Absence of covenants
  - May allow off-balance sheet treatment
- Disadvantages
  - Servicing and collection Issues



## Whole business financing

---

- Isolation of business lines in separate entity
- Enables higher credit rating for transaction



## Key steps for restructuring

---

- Start sooner rather than later (*i.e.*, while the borrower still has available cash)
- Review existing debt and equity documents
- Critical analysis of assets that are collateral versus those assets that do not serve as collateral for borrower's debt
- Review all options available for refinancing and/or restructuring borrower's debt



---

## Q & A

Join us on April 1 at 12:30 EDT for the  
*Raising Capital in a Changed World* webinar.  
For more information and to register, visit  
<http://www.mwe.com/info/raisingcapital/>.



McDermott  
Will & Emery

The Credit Crunch – Proactive Steps in an Uncertain Financing Environment

13