STAY CURRENT
A Client Alert from Paul Hastings

PAUL HASTINGS

March 2012

Recent Developments in Leveraged Finance

BY RICHARD E. FARLEY

Increased Disclosure By Lenders and Bankers in Corporate Acquirer LBOs Due To Strine's Opinion in *In Re El Paso Corporation Shareholder Litigation*

The fallout from Chancellor Strine's opinion in *In Re El Paso Corporation Shareholder Litigation*, which strongly criticized an M&A banker for not disclosing security ownership in a potential acquirer of his client, is now being felt. The opinion suggests a duty of banks and individual bankers (and possibly other advisors) to disclose to a client security ownership – regardless of the materiality to the net worth or earnings of the banker – in transaction counterparties of the client.

We have recently received a request from a corporate borrower contemplating an acquisition to have the lenders providing the financing commitment disclose whether they, institutionally, or any of the individual bankers providing advice to the borrower have any financial interest in the target or its private equity owner.

House of Representatives Passes JOBS Act Which Eliminates Restrictions on "General Solicitation" in Rule 144A Offerings and Exempts Issuers with Less Than $1.0 Billion of Revenue From SOX 404(b)

On March 8, 2012, the U.S. House of Representatives overwhelmingly passed (390 to 26) the "Jumpstart Our Business Startups Act" or "JOBS Act". The JOBS Act is currently being considered by the Senate and President Obama has indicated general support of the JOBS act.

Two provisions of the JOBS Act are directly relevant to high yield offerings and issuers. First, the JOBS Act would exempt an "emerging growth company" (defined as an issuer that had total annual gross revenues of less than $1.0 billion during its most recently completed fiscal year) from compliance with Section 404(b) of the Sarbanes Oxley Act of 2002. Section 404(b) currently requires an issuer with a public float of equity securities held by non-affiliates of $75 million or more to have its auditor attest to and report on management's assessment of the effectiveness of the issuer's internal control structure and procedures for financial reporting. Secondly, the JOBS Act would eliminate the prohibition on general solicitation or general advertising by issuers and initial purchasers in Rule 144A offerings. This would permit greater flexibility regarding the content of press releases and other communications relating to Rule 144A offerings.

Issues in the Form Non-Reliance Agreement Contained in the ABA Business Law Task Force on Delivery of Document Review Reports to Third Parties

An ABA business law task force has prepared a form Non-Reliance Agreement (the "Non-Reliance Agreement") for use where lenders' counsel is given the due diligence report prepared by sponsor's or

borrower's counsel. A number of problematic issues have arisen regarding the application of the last sentence of Paragraph 1 of the Non-Reliance Agreement in connection with bridge financing commitments to be replaced or refinanced with securities, particularly when a "securities demand" is included in the commitment documentation (as is nearly always the case in non-investment grade bridge financing commitments). The last sentence of Paragraph 1 reads as follows:

> "Notwithstanding anything to the contrary contained herein, in no event shall the Report be used by you or any other person in connection with your review of the Company in connection with any transaction involving the offer, sale, or issuance by the Company or any affiliate of the Company of any equity or debt security (and you agree and acknowledge that "Lender's affiliates" as used in the second sentence of paragraph 6 of this letter excludes such of your affiliates as may be participating in any such securities transaction)."

The issues identified to date are:

1. The same persons at banks and their outside law firms working on the bridge commitment will also be working on the securities offering. Separate teams for each would be prohibitively expensive.

2. A bridge commitment with a securities demand (and possibly even one without one) is a "transaction involving the offer, sale or issuance of…any equity or debt security". This language could prohibit using the report even for the bridge commitment only.

3. Many personnel at banks work for both the lender and the securities affiliate, and in the bridge context, it is often the securities affiliate that acts as arranger or even makes the bridge loan commitment. Therefore, excluding "Lender's affiliates" under these circumstances would exclude much of the bank's working group.

These issues will need to be addressed if the proposed Non-Reliance Agreement is to be widely utilized in the leveraged finance context.

In furtherance of addressing these issues, set forth below is a draft of proposed language addressing these concerns that we have sent to the ABA Task Force for their consideration.

> "Notwithstanding anything to the contrary contained herein, in no event shall the Report be used by you or any other person as part of any review of the Company or the Client in connection with any transaction involving the offer, sale or issuance by the Company, the Client, or any affiliate of the Company or the Client, of any equity or debt security (a "Securities Offering"), and you agree and acknowledge that "Lender's affiliates," as used in the second sentence of paragraph 6 of this letter excludes such of your affiliates as may be participating in any Securities Offering; *provided* that the foregoing shall not restrict the use of the Report in connection with an independent diligence review relating to the issuance of any financing commitment that may be replaced or refinanced in whole or in part with a potential Securities Offering, nor restrict any person or any Lender's affiliate, in each case that reviews the Report in connection with any such independent due diligence review, from participating in due diligence or any other activity in connection with any such Securities Offering."

We are advising our clients to require this or similar language in any non-reliance agreement based on the ABA Task Force Form.

If you have any questions concerning these developing issues, please do not hesitate to contact the following Paul Hastings lawyers:

New York

Richard E. Farley
1.212.318.6434
richardfarley@paulhastings.com