



LevFin Academy™

CONDENSED TEACHING EDITION

The Leveraged Finance Book

A Practitioner's Guide

European leveraged finance from first principles to covenant mechanics, restructuring, analytical tools and selected contingent-right teaching sensitivities.

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This is the public condensed teaching edition. The restored long-form Book remains a private working draft. Participants who reserve a seat in either LevFin Academy cohort receive the then-current private draft as part of the cohort materials; it is not a public release and may change.

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PART I

FOUNDATIONS

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-

What Is Leveraged Finance

Before We Begin

This book exists because a guide of this kind was, for a long time, difficult to find.

There are good textbooks on capital structure, bond math and the theory of optimal leverage, and they are worth reading. What they rarely teach is how to read a credit agreement the way the job requires: against the borrower, assuming every definition was negotiated for a reason, and asking where the package actually holds if the credit deteriorates.

There are also excellent legal primers, written by the firms that draft these documents. But they were written by lawyers for lawyers, and they assume a baseline of legal sophistication that most credit analysts and portfolio managers don't have and shouldn't need.

What was missing was a book that started from where the practitioner stands: someone who needs to understand how leveraged finance works in practice rather than in theory or in law — the mechanics, the incentives, the games that get played and the moves available on both sides of the table.

This book is an attempt to fill that gap.

Who This Book Is For

If you work in leveraged credit as an analyst, associate, or portfolio manager, on either the buy side or the sell side, this book is written for you. It should also serve lawyers who want to understand how their documents are read by the people who invest on the basis of them, and students who want to see what this world actually looks like from the inside before deciding whether to enter it.

The book assumes a basic grounding in finance — you know what EBITDA is, you understand that debt has to be repaid, you've seen a balance sheet. Beyond that, everything is built from the ground up.

Why European Leveraged Finance

This book focuses on European leveraged finance. The American market matters; it is larger, older, and has produced most of the innovations (and most of the disasters) that shape our market. But the European market has its own personality. Its documentation borrows heavily from US high-yield bond precedent while operating under a different legal chassis — primarily English law, with all the interpretive and restructuring implications that brings. Its investor base and its restructuring tools are different, and its quirks are not well documented anywhere.

Most of what you'll read here has broader application: the logic of covenants, the economics of leverage, the dynamics between sponsors and creditors all cross borders. But when we get into documentation specifics, we're in European territory. If you work in US leveraged finance, much of this will be familiar; some of it will be usefully foreign.

What Makes This Book Different

There are good books on leveraged finance. Rosenbaum and Pearl cover valuation and LBO modelling thoroughly. Stowell provides a solid institutional overview. The legal primers from firms like Weil and Latham are technically

excellent.

What this book offers is a practitioner's perspective: structuring transactions, analysing credits, negotiating documentation, watching deals perform through multiple cycles. It is not the view of an academic or a lawyer, but of someone who had to make investment decisions based on these documents and live with the consequences.

Covenants receive more attention than valuation here because they shape the borrower's permitted actions and creditors' remedies when performance deteriorates. Pricing and documentation both matter: price compensates for risk, while documentation determines how that risk can change after closing.

The book also tries to be honest about what isn't known, and there is still plenty of that.

Leveraged finance is best understood as a problem of debt capacity, contractual allocation and downside resilience. It is not defined by one instrument, one rating label or one leverage multiple. A financing belongs in this field when repayment depends materially on sustained operating cash flow, the documents allocate meaningful control to creditors, and the capital structure has limited tolerance for forecast error.

The practical question is therefore not whether a borrower is called leveraged, but what must remain true for every promised payment to be made. The analyst starts with the obligor group, cash-generation perimeter, ranking, maturity profile and covenant package. Market labels help navigation; they do not replace that analysis.

1.1 How the market developed

The modern market developed through several overlapping changes: broader institutional ownership of below-investment-grade debt, growth in syndicated bank lending, repeated waves of acquisition financing, and the development of loan and bond documentation capable of distributing risk among many creditors. No single person or event explains that evolution. For teaching purposes, the useful historical point is that financing moved from bilateral balance-sheet lending toward a mixed ecosystem of banks, funds, securitisation vehicles and public or privately placed securities.

History matters because the instruments still reflect different origins. A revolving facility is designed around liquidity and repeated drawings; a term loan is organised around funded principal and lender voting; a bond is governed by an indenture and trustee structure; and private credit may combine concentrated ownership with negotiated reporting and amendment rights. The analyst should expect those institutional differences to appear in pricing, transfer rules, covenants and remedies.

Source note (retrieved 12 July 2026): PS01: FINRA, Bonds, <https://www.finra.org/investors/investing/investment-products/bonds>; PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf.

1.2 A working definition

For this book, leveraged finance means debt financing in which repayment is substantially dependent on enterprise cash flow and where leverage, credit quality or transaction purpose creates enhanced underwriting and monitoring risk. This is an analytical definition, not a claim that every regulator, bank or investor uses one universal threshold. The U.S. interagency guidance and ECB guidance illustrate how supervisory frameworks identify leveraged transactions, but each framework has its own perimeter and should be cited with its date and context.

A strong classification note separates four ideas. Credit quality asks how likely contractual payment is. Leverage measures debt relative to an earnings or cash-flow denominator. Transaction purpose asks whether the debt

funds an acquisition, distribution, refinancing or operating need. Instrument form describes whether the claim is a loan, bond or another obligation. Those ideas interact, but none is a perfect substitute for the others.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf.

1.3 The instrument map

A revolving credit facility provides committed liquidity up to an agreed limit and usually supports working capital, letters of credit or other short-term needs. A term loan funds principal at closing or during a specified availability period and then follows its own amortisation and maturity rules. A high-yield bond is a security issued under an indenture, with payment, redemption, covenant, default and amendment mechanics set out in that instrument. Direct lending describes an origination and ownership model rather than one fixed document form.

Do not infer ranking from the product name. A loan may be secured or unsecured, senior or subordinated, guaranteed by some entities and structurally junior to liabilities at non-guarantor subsidiaries. A bond may share collateral with loans, sit behind them by contract, or be structurally separated. The ranking analysis follows obligors, guarantees, collateral and intercreditor terms, not labels.

Source note (retrieved 12 July 2026): PS01: FINRA, Bonds, <https://www.finra.org/investors/investing/investment-products/bonds>; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

1.4 Scope and market boundaries

European and U.S. markets overlap but are not interchangeable. Currency, governing law, insolvency regimes, bank regulation, takeover requirements, settlement conventions and investor composition can change both process and documentation. This book uses public instruments to demonstrate mechanics and identifies the governing source at the point of use. It does not treat a selected agreement as proof of a market-wide custom.

Market-size statements are especially sensitive to perimeter. A total can vary depending on whether it includes institutional loans, private credit, drawn revolvers, bonds, distressed debt or only performing instruments. A defensible statistic must state its date, currency, geography, instrument universe and source. Where those fields are absent, the number should not be used.

Source note (retrieved 12 July 2026): PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>; PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>.

1.5 Debt capacity as a cash-flow problem

Debt capacity is the amount and shape of debt that a business can service through plausible operating paths while retaining enough liquidity to absorb volatility. The analysis begins with cash EBITDA only as a bridge. It then deducts cash taxes, capital expenditure, working-capital investment, lease or pension cash requirements,

restructuring costs and other recurring uses. The result must cover cash interest, scheduled principal and any mandatory prepayment while leaving a credible liquidity buffer.

A leverage ratio is a compact signal, not the answer. Two borrowers with identical debt-to-EBITDA can have different risk because one converts earnings to cash, has low cyclicity and faces distant maturities, while the other consumes working capital, requires heavy capital expenditure and faces refinancing soon. Capacity is scenario-dependent, so the base case must sit beside downside and severe-but-plausible cases.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf.

1.6 What makes leveraged finance distinctive

The field joins three disciplines. Credit analysis tests the borrower's ability and willingness to pay. Structuring allocates cash, collateral, guarantees, priorities and control. Distribution determines which investors can own the risk and on what terms. A financing can fail even when one discipline is sound: good assets cannot cure an unmanageable maturity wall, strong documentation cannot create cash flow, and attractive pricing cannot compensate for an unmodelled liquidity need.

The creditor's payoff is asymmetric. Contractual upside is largely limited to interest, fees and principal, while loss can consume a substantial part of the claim. That asymmetry changes the decision standard. The analyst looks first for paths to permanent impairment, then asks whether spread and structure compensate for the remaining risk.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf.

1.7 The cast of characters and the LBO connection

The borrower and its operating subsidiaries generate cash. A sponsor, where present, supplies equity and influences strategy. Arrangers or direct lenders underwrite and document debt. Institutional investors may acquire pieces of a syndicated loan or bond. Administrative agents, collateral agents and trustees perform only the functions assigned by the relevant instrument. Advisers contribute legal, accounting, commercial or market work within their mandates.

An LBO is a use of leveraged finance, not its entire universe. Acquisition debt is sized against the acquired business, but leveraged borrowers also refinance, fund capital expenditure, make acquisitions, extend maturities or recapitalise. In every case the discipline is the same: identify the source of repayment, map the claims on that source, and test the structure under adverse conditions.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Fictional teaching exercise: the fruit distributor

Fictional teaching facts. Orchard Distribution generates EUR 42 million of EBITDA. Maintenance capital expenditure is EUR 7 million, cash taxes are EUR 4 million, normal working-capital investment is EUR 3 million and other recurring cash costs below EBITDA are EUR 2 million. Proposed debt is EUR 210 million at an all-in cash rate of 7.0%, with EUR 5 million of annual scheduled amortisation. Opening cash is EUR 12 million and the minimum operating cash requirement is EUR 8 million.

The bridge produces EUR 26 million before debt service: $42 - 7 - 4 - 3 - 2$. Cash interest is EUR 14.7 million and amortisation is EUR 5 million, leaving EUR 6.3 million before discretionary uses. Gross leverage is 5.0x and cash debt-service coverage on these simplified inputs is 1.32x. Now reduce EBITDA by 15% while keeping the cash uses fixed. EBITDA becomes EUR 35.7 million, pre-debt-service cash becomes EUR 19.7 million and coverage falls to 1.00x. The lesson is not that 5.0x is acceptable or unacceptable; it is that modest operating pressure can eliminate the margin for error.

Classification exercise

For each of four fictional claims - a drawn revolver, a first-lien term loan, a secured bond and a holdco note - write five fields: obligor, guarantors, collateral, payment maturity and voting document. Do not rank the claims until all five fields are complete. Then explain whether the ranking conclusion arises from contract, collateral, entity location or a combination of those features.

1.8 The LBO as a financing application

A leveraged buyout is an acquisition financed with a combination of equity and debt, but there is no universal debt percentage or standard stack. The opening structure depends on purchase price, business risk, cash conversion, debt capacity, market access and the negotiated documents.

The acquisition model should reconcile purchase consideration, refinancing, fees, minimum cash, equity and each debt instrument. It should then project operating cash flow, interest, amortisation, liquidity and covenant headroom. A term loan, revolver or bond appears only if the transaction documents and funding plan include it; none is a required element of every LBO.

For creditors, the sponsor's projected equity return is context rather than repayment. Rebuild the model through downside cash flow and maturity, then identify which value-creation assumptions require additional debt, distributions or asset transfers.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Fictional teaching exercise: sources and uses

Fictional facts. Purchase consideration is EUR 300 million, fees are EUR 12 million and minimum cash is EUR 8 million. Equity contributes EUR 130 million. A term loan of EUR 180 million is issued at 99. Calculate cash sources, identify the funding gap and state whether additional equity, debt face amount or another source is required.

Practitioner review sequence

First pass. Define the borrower group, transaction purpose, debt instruments, ranking and source of repayment before calculating a ratio.

Second pass. Bridge EBITDA to cash available for debt service, construct base and downside cases and identify the earliest liquidity or covenant failure.

Sources-and-uses pass. Reconcile purchase consideration, fees, minimum cash, issue price, equity and funded debt before describing leverage. Treat instrument form and debt percentage as transaction-specific outputs rather than market constants.

Evidence pass. Cite each external definition or statistic with date and perimeter, label every invented input as fictional and treat a public instrument as evidence only for that instrument.

Legal, tax, regulatory and accounting boundary

This introduction does not reach conclusions about enforceability, fiduciary duties, insolvency outcomes, tax treatment, regulatory classification, guarantees, collateral, acquisition funding or distributions. Those questions depend on the facts, operative documents and jurisdiction and require qualified professional advice.

Primary-source map

Source note (retrieved 12 July 2026): PS01: FINRA, Bonds, <https://www.finra.org/investors/investing/investment-products/bonds>; PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>; PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

1.9 What Lies Ahead

This book moves from foundational concepts to technical detail.

Part I: Foundations establishes the building blocks — what leveraged finance is, who plays in it, the economics of leverage, the sponsor's perspective, and the art of the term sheet.

Part II: The Instruments looks closely at loans and bonds — their structures, documentation, and behaviour — and the vehicles that buy them, from high-yield and direct lending to CLOs.

Part III: Covenants is the technical heart of the book: how to read a credit agreement, the European-versus-US divide, and the financial-covenant and EBITDA machinery that governs what a borrower can do.

Part IV: Covenant Deep Dives works through the major covenants one by one — restricted payments, debt and liens, asset sales and change of control, events of default, and the incremental facility.

Part V: Amendment Mechanics and Restructuring covers what happens when someone wants to change the rules — liability-management exercises, amend-and-extend, guarantee and collateral architecture, and the UK and distressed toolkit.

Part VI: Analytical Tools turns to the quantitative craft — the credit-analysis framework, working capital, the rating agencies, and full corporate and LBO modeling, closing with worked case studies.

Part VII: Contingent Rights and Teaching Sensitivities develops a bounded teaching framework for contractual optionality, sensitivities and a fictional implementation blueprint. It does not purport to produce an issuer-specific fair value or trading signal.

Part VIII: Market and Regulatory Context steps outside the document — secondary trading and loan operations, the regulatory framework, tax, and ESG.

Part IX: The Profession steps back from the technical material to the craft of doing this work — what the discipline teaches over time, communication, career, and building a reputation.

Throughout, the aim is to balance technical rigour with practical perspective. There is no shortage of legal primers on these topics; what this book adds is the view from inside — structuring these transactions, negotiating these documents, and watching them perform through multiple cycles.

If a single thread connects everything that follows, it is that the documentation matters more than most people think, and that it matters most precisely when everyone wishes it didn't — when the company is struggling, when the sponsor is manoeuvring, when the restructuring advisers arrive. The covenants you analysed in quiet conditions become the terms on which the fight is conducted. Whether they protect you depends on whether you understood them before you needed them.

There are no absolute truths in leveraged finance, but there are patterns, principles, and hard-won lessons.

This book is an attempt to share them.

The Leveraged Finance Ecosystem

Introduction

Leveraged finance is less a product than an ecosystem: a set of institutions, incentives and relationships that together make it possible for highly indebted companies to access the capital markets.

Understanding this ecosystem matters because every transaction you encounter involves several parties with distinct and often conflicting motivations. The sponsor wants maximum leverage at minimum cost; the banks want to originate and distribute without holding the risk; the CLOs need assets that fit their mandates; the rating agencies need to justify their methodologies; the lawyers need to close the deal while protecting their clients; and the advisors need to get paid.

None of these motivations is improper in itself, but together they shape every deal. This chapter maps the participants so that you know who is sitting across the table, what they want and why they behave as they do.

A leveraged financing is a coordinated process among parties whose objectives overlap only partly. The borrower wants reliable capital and operating flexibility. Equity owners care about value creation and option preservation. Underwriters care about commitment risk and distribution. Investors care about repayment, downside protection and liquidity. Agents and trustees administer specified functions rather than providing an independent credit guarantee.

The correct way to study the ecosystem is to map decisions, information and incentives. Titles alone are misleading because the same institution may advise, underwrite, lend, distribute and trade, subject to its mandates and controls. Every role statement in this chapter is therefore bounded to the relevant function or cited instrument.

2.1 Borrowers and equity owners

A corporate borrower raises debt for acquisitions, refinancing, investment, working capital or shareholder transactions. A sponsor-owned borrower adds an equity owner with a defined investment thesis and exit horizon, but the creditor still lends to legal entities and contractual obligors. The analyst should separate the sponsor's incentives from the borrower's payment obligations. Equity support may be economically valuable without being legally committed.

The central borrower decision is not simply price. It is the combination of certainty, quantum, maturity, amortisation, covenant flexibility, reporting, portability, prepayment cost and execution risk. A lower initial spread can be inferior if the structure creates refinancing pressure or restricts the operating plan.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf.

2.2 Arrangers and underwriters

An arranger coordinates structuring, commitment, documentation and distribution within the agreed mandate. If it commits before investors are identified, it bears the risk that the debt cannot be distributed on the anticipated

terms. That risk is managed through underwriting approvals, market flex, syndication strategy and exposure limits. The exact rights arise from the commitment papers, not from the job title.

Origination begins with a financing case: transaction sources and uses, operating projections, debt capacity, structure and investor fit. Underwriting converts that case into a credit decision with named assumptions and conditions. Distribution then tests investor demand. These are distinct gates; successful origination does not itself prove acceptable underwriting or executable distribution.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

2.3 Institutional investors

Loan investors can include banks, CLOs and credit funds. Bond investors can include mutual funds, insurance accounts and other institutional portfolios. Private-credit funds may originate and retain loans with a concentrated lender group. Those categories are descriptive, not universal: mandate, regulation, liquidity terms and portfolio construction determine what a particular vehicle can own.

Investor behaviour follows constraints as well as conviction. A CLO manager considers eligibility and indenture tests. A daily-liquidity fund considers redemptions and portfolio liquidity. An insurance account considers its mandate and prudential treatment. A private fund considers drawdown capital, leverage, concentration and fund terms. The analyst should not turn those constraints into an unsupported claim that a class of investor must buy or sell.

Source note (retrieved 12 July 2026): PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>; PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>; PS13: EUR-Lex, Regulation (EU) 2017/2402, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32017R2402>; PS14: Federal Reserve, CLOs in the Financial Accounts of the United States, <https://www.federalreserve.gov/econres/notes/feds-notes/collateralized-loan-obligations-in-the-financial-accounts-of-the-united-states-20190920.html>; PS15: Federal Reserve Regulations, 12 CFR 244.9, <https://www.federalreserve.gov/frs/regulations/section-2449-open-market-clos.htm>.

2.4 Rating agencies and credit opinions

A rating is an external opinion produced under the agency's methodology. It can influence mandate eligibility, disclosure and pricing discussions, but it does not replace an investor's analysis. The rating process generally requires a defined issuer perimeter, financial information, capital structure and instrument terms. Any description of a particular rating or recovery assessment must cite the applicable public methodology and date.

The useful practitioner discipline is reconciliation. Compare the agency perimeter, debt adjustments, EBITDA treatment, recovery assumptions and instrument ranking with the internal model. Differences should be explained rather than averaged away. This chapter does not reproduce proprietary tables or imply that one rating category predicts a fixed default or recovery rate.

Source note (retrieved 12 July 2026): PS01: FINRA, Bonds, <https://www.finra.org/investors/investing/investment-products/bonds>.

2.5 Transaction advisers

Financial, accounting, commercial and legal advisers answer different questions. A financial adviser may coordinate valuation, process or financing alternatives. Accounting diligence may test quality of earnings, working capital, tax or carve-out information within its scope. Commercial work may examine market, customers and competition. Legal counsel drafts, negotiates and advises on law and documents. None of those workstreams should be treated as a substitute for another.

A strong diligence map assigns each material assumption to an owner, evidence source and unresolved question. For example, customer retention may sit with commercial diligence, EBITDA normalisation with accounting diligence, and guarantee capacity with legal counsel. The credit team integrates those answers into a single downside and documentation case.

2.6 Administrative agents and collateral agents

In the selected public credit agreement, the administrative agent performs functions allocated by the agreement, including specified notices, payments and lender administration. A collateral agent or security agent administers collateral-related rights under the applicable documents. The scope, discretion, protections and reliance rights must be read from the instrument. The title does not create an uncited monitoring duty or fiduciary standard.

Operationally, the agent is the hub for notices, assignments, borrowing requests, rate settings, compliance delivery and voting mechanics. A credit analyst should know which communications are effective only when delivered to the agent, which decisions require lender instructions, and which lender records control voting and payment allocation.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

2.7 Indenture trustees

A bond trustee acts under the indenture. The selected public indenture specifies authentication, payment administration, notices, defaults, directions, indemnities and other functions. The pre-default and post-default framework, and any duty language, must be stated from the relevant instrument and governing law. Broad claims that a trustee continuously monitors the issuer are not supportable without that analysis.

For the investor, the operational questions are concrete: who receives notices, who may declare or act after a default, what percentage may direct action, what indemnity may be required, and which rights remain individual. Those questions sit in the indenture and should be captured in the credit file before distress.

Source note (retrieved 12 July 2026): PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

2.8 The ecosystem in motion

A financing process moves through mandate, diligence, commitment, documentation, distribution, closing and post-closing administration. Information quality changes during that sequence. Early estimates become diligence findings; a term sheet becomes operative documents; expected allocations become lender records. Controls should identify which facts are provisional, which conditions remain open and which document governs each decision.

Incentive conflicts are managed through evidence and governance. The arranger's distribution objective does not answer the investor's downside question. The sponsor's operating plan does not prove liquidity. The rating

process does not establish lender consent. A robust transaction file records the independent conclusion of each decision maker.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Fictional teaching exercise: incentive and information map

Fictional teaching facts. Northbridge Services seeks a EUR 600 million term loan for an acquisition. The sponsor assumes EUR 75 million of annual synergies; accounting diligence validates EUR 30 million as specifically supported and identifies EUR 12 million of one-time implementation cost. The arranger has underwritten the full amount subject to agreed flex. A CLO account cannot own more than a stated concentration in the relevant industry under its own governing documents.

Prepare four columns in your working paper: party, decision, information needed and contractual source. The sponsor decides whether the equity return supports the price. The arranger decides whether to commit and how to distribute. The lender decides whether the supported cash flows and documents justify participation. The CLO manager separately tests eligibility and concentration. Do not convert the unsupported synergy difference into debt capacity, and do not assume the investor constraint applies to every CLO.

Role-boundary exercise

Using the cited public credit agreement and indenture, locate one operative provision for the administrative agent, collateral agent and trustee. Record the section, the stated function, who may give directions, and any stated condition to action. Rewrite each finding as an instrument-specific sentence. If the document is silent, record the silence rather than inferring a duty.

Practitioner review sequence

Decision map. Identify who commits capital, who advises, who administers and who has consent rights; keep economic influence separate from legal authority.

Evidence map. Assign every material assumption to a diligence source, date, owner and unresolved issue, then reconcile it to the downside model.

Document map. For agents and trustees, cite the exact instrument and section for authority, direction, protection, notice and payment mechanics.

Legal, tax, regulatory and accounting boundary

Agency, collateral administration, trustee conduct, adviser mandates and conflicts remain document- and jurisdiction-specific. Apply these descriptions only after checking the operative instruments and obtaining qualified finance counsel's advice on the governing law.

Primary-source map

Source note (retrieved 12 July 2026): PS01: FINRA, Bonds, <https://www.finra.org/investors/investing/investment-products/bonds>; PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>; PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS13: EUR-Lex, Regulation (EU) 2017/2402, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32017R2402>; PS14: Federal Reserve, CLOs in the Financial Accounts of the United States, <https://www.federalreserve.gov/econres/notes/feds-notes/collateralized-loan-obligations-in-the-financial-accounts-of-the-united-states-20190920.html>; PS15: Federal Reserve Regulations, 12 CFR 244.9, <https://www.federalreserve.gov/frs/regulations/section-2449-open-market-clos.htm>.

The leveraged finance ecosystem is a set of institutions with distinct roles and motivations:

1. Borrowers (sponsors and corporates) seek capital on the most favorable terms possible
2. Arrangers (banks) originate and distribute, earning fees while managing underwriting risk
3. Investors (CLOs, funds, private credit) provide capital, each with unique constraints and objectives
4. Rating agencies categorize risk, influencing pricing and investor eligibility
5. Advisors (accounting, legal, strategic) support transactions on both sides
6. Infrastructure (agents, trustees) enables the mechanics of lending and bondholding

The market has evolved to connect borrowers with capital efficiently. But "efficiently" does not mean "fairly" or "protectively." The terms that emerge reflect the balance of power among the participants, and for the past decade that balance has favored sponsors.

Knowing who sits across the table, what they want and how they get paid is necessary context for everything that follows.

Chapter 3 turns to the economics that drive this market: why leverage creates value, how pricing works, and the risk-return trade-offs that define credit investing.

The Economics of Leverage

Introduction

Why does leveraged finance exist?

The cynical answer is that people make money from it: sponsors, banks, investors, advisors. That answer only restates the question. The economic puzzle is why it is rational for a company to borrow at 8% when it could fund itself with equity, and why it is rational for an investor to lend to a company that might default.

This chapter answers those questions. It starts with the economics of leverage and why debt can create value even when it looks expensive, then turns to how pricing works in leveraged finance markets: what determines whether a loan prices at SOFR+400 or SOFR+500, and why one bond yields 7% and another 9%. It ends with the risk and return dynamics that govern credit investing—the relationship between yield, default, and recovery that determines whether a leveraged loan is a good investment or a trap.

These economics are worth understanding properly. Without them you're just pushing numbers around a spreadsheet; with them you understand why the numbers matter.

Leverage changes the distribution of outcomes rather than creating value by itself. Debt supplies capital with a contractual claim. Equity receives the residual after that claim. When enterprise value rises, a fixed debt balance can amplify the percentage return on equity; when value falls, the same structure accelerates equity loss and can impair creditors.

3.1 The fundamental logic of leverage

At entry, enterprise value equals debt plus equity, ignoring other claims for the moment. At exit, equity value equals enterprise value less net debt and any senior claims. The percentage equity return therefore depends on operating performance, exit valuation, cash generation, interest cost and the path of debt repayment. A leverage case that shows only the entry multiple and exit multiple omits the central cash-flow mechanics.

Debt also adds fixed or priority cash uses. Interest, amortisation, fees and hedging cash flows compete with working capital, capital expenditure and taxes. The correct model follows the cash waterfall period by period. It should not assume that accounting earnings are available for debt repayment or that a refinancing will occur simply because maturity arrives.

3.2 Return amplification and loss amplification

Suppose two buyers acquire identical fictional assets for EUR 100. Buyer A uses EUR 100 of equity. Buyer B uses EUR 60 of debt and EUR 40 of equity. If enterprise value becomes EUR 120 and debt remains EUR 60, Buyer A earns 20% while Buyer B's equity becomes EUR 60, a 50% gain. If enterprise value falls to EUR 80, Buyer A loses 20% while Buyer B's equity becomes EUR 20, a 50% loss. This simple comparison isolates capital structure; it excludes interest, taxes, fees and debt paydown.

The example is not an investment recommendation. In a full model, the leveraged case must deduct financing costs and track debt repayment. It must also test whether the borrower can survive the path to the exit value. A theoretically positive terminal equity value is irrelevant if liquidity fails earlier or creditors exercise contractual remedies.

3.3 Debt paydown and cash conversion

Debt paydown is value transfer only when it comes from sustainable cash generation rather than asset depletion or unpaid obligations. Build the bridge from EBITDA to operating cash flow, then to cash available after interest and mandatory principal. Separate recurring maintenance investment from discretionary growth spending. State how working capital behaves in growth and contraction rather than applying one permanent percentage.

A credible case also models restricted cash, trapped cash, non-guarantor cash and currency mismatches where relevant. Consolidated cash on a slide may not be available to the entity that owes the debt. The structure determines whether cash can move and whether doing so consumes covenant capacity or creates tax and legal issues.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf.

Fictional teaching exercise: leveraged and unleveraged returns

Fictional teaching facts. A business is acquired for EUR 500 million. Case U uses EUR 500 million of equity. Case L uses EUR 300 million of debt and EUR 200 million of equity. Ignore financing costs and transaction fees for this simplified comparison. Over four years the business generates EUR 95 million of cumulative cash after tax, capital expenditure and working capital. Case U retains or distributes the full EUR 95 million. Case L applies EUR 75 million to principal and retains EUR 20 million as excess cash. Exit enterprise value is EUR 575 million.

Case U produces total equity value or proceeds of EUR 670 million: EUR 575 million of enterprise value plus EUR 95 million of cash. The gain is EUR 170 million, or 34%. Case L net debt is EUR 205 million: $300 - 75 - 20$. Equity value is EUR 370 million, producing the same EUR 170 million absolute gain on EUR 200 million of opening equity, or 85%. If exit enterprise value falls to EUR 350 million, Case U produces EUR 445 million of total equity value or proceeds and loses EUR 55 million, or 11%. Case L equity falls to EUR 145 million and also loses EUR 55 million, equal to 27.5% of opening equity. The absolute value change is identical; leverage magnifies the percentage outcome because Case L begins with a smaller equity base.

3.4 Cost of capital as a scenario

A weighted-average-cost-of-capital calculation combines assumed costs and capital weights. It can help compare financing scenarios, but it is not an observable fact about a leveraged borrower. The weights change with market value and debt repayment; the cost of equity is an estimate; and the cost of debt must include price, fees, expected repayment and loss, not only coupon.

Use the calculation as a transparent sensitivity. State the debt and equity amounts, pre-tax debt cost, tax assumption, equity return assumption and weighting basis. Then vary leverage, cash interest and distress cost. Do not present one minimum as a precise optimal capital structure.

Tax effects and their limits

Interest can affect taxable income in some circumstances, but deductibility depends on jurisdiction, entity, instrument, limitation rules, losses and transaction facts. A teaching model may show an assumed tax benefit only when the assumption is explicit and separated from the operating cash-flow case.

The base credit case should remain viable without counting an uncertain tax benefit as free cash. Where the model includes a benefit, show timing, utilisation and reversal. Qualified tax counsel must determine whether the

assumption is available.

Financial-distress costs

Leverage can create costs before formal insolvency. Suppliers can shorten terms, customers can hesitate, management attention can shift, investment can be delayed and refinancing options can narrow. Formal restructuring can add professional fees, process delay and value uncertainty. Those effects are scenarios, not fixed percentages.

A downside model should include operational cash leakage, higher financing cost and delayed strategic actions before applying a terminal recovery. This prevents the analysis from treating distress as a single haircut at exit.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf.

Fictional teaching exercise: financing mix

Fictional assumptions. A EUR 400 million business can be financed with either EUR 120 million of debt at an 8% cash cost and EUR 280 million of equity with a 16% assumed required return, or EUR 240 million of debt at a 10% cash cost and EUR 160 million of equity with an 18% assumed required return. Ignore tax first and calculate the weighted assumed cost in each structure. Then introduce a separately stated 20% tax benefit on deductible interest and explain why the result remains conditional rather than a recommendation.

3.5 Fixed and floating-rate debt

A floating-rate loan generally references a benchmark plus a margin, subject to the instrument's benchmark, floor, reset and fallback provisions. A fixed-rate bond states a coupon, but the investor's yield also depends on purchase price, redemption assumptions and timing. The borrower compares expected cash cost and risk; the investor compares sensitivity, optionality and credit loss. Neither structure is inherently superior.

Rate risk must be integrated with credit risk. Higher benchmarks raise cash interest on unhedged floating debt and may reduce debt-service headroom. Falling benchmarks can reduce interest but may coincide with weaker demand or recession. A fixed coupon stabilises nominal interest until refinancing or redemption, while market value can still move with rates, spread and duration.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

3.6 The building blocks of spread

A credit spread compensates for a bundle of risks and market conditions. Expected default loss is one component, but liquidity, uncertainty, optionality, documentation, technical demand, capital treatment and transaction execution can also affect price. A spread is therefore an observed market clearing term, not a pure estimate of default probability.

For underwriting, separate three layers: borrower risk, instrument risk and market execution. Borrower risk covers cash generation, business volatility and leverage. Instrument risk covers ranking, collateral, maturity, covenants

and call terms. Execution covers investor demand, size, timing and comparables. This separation makes it easier to explain why two claims on the same group price differently.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf.

3.7 Expected return without proprietary data

A simple one-period teaching model can express expected value as the probability-weighted value of contractual performance and default outcomes. If a fictional instrument has a 96% probability of paying 107 at year-end and a 4% probability of paying 45, expected proceeds are 104.52: $0.96 \times 107 + 0.04 \times 45$. On an initial price of 100, the simplified expected return is 4.52%, before discounting, timing dispersion and transaction costs.

The model is only as credible as its assumptions. Default probability and recovery are not constants, and recovery depends on enterprise value, priority, costs and timing. No rating-agency default or recovery table is reproduced here. If an external dataset is later used, its licence, period, sample and methodology must be documented at the point of use.

3.8 Recovery and capital-structure location

Recovery analysis starts with a downside enterprise-value range, then deducts administrative and priority claims before allocating value through the legal and contractual waterfall. A senior label is not enough. Confirm obligors, guarantors, collateral, structural subordination, intercreditor terms and any debt that can rank ahead or share priority.

Time matters because a delayed recovery has a lower present value and may require additional funding. The model should show gross distributable value, costs, timing and claim amount. It should also disclose whether the analysis assumes a sale, reorganisation, enforcement or consensual solution, without presenting that scenario as a legal prediction.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS18: Delaware Code, Title 6, Article 9, <https://delcode.delaware.gov/title6/c009/index.html>.

3.9 Portfolio construction and concentration

Diversification can reduce issuer-specific volatility, but it does not eliminate common-factor risk. A portfolio of different borrowers may still be concentrated in one industry, sponsor, geography, maturity window or refinancing condition. Correlation tends to rise in stress, exactly when liquidity is most valuable.

A practical concentration review groups exposures by economic driver, not only legal name. It also tracks position size, liquidity, covenant headroom, maturity and downside severity. The purpose is not to claim that the market prices correctly or incorrectly; it is to expose which assumptions drive the portfolio loss distribution.

3.10 Borrower and investor decision framework

The borrower compares certainty, total cash cost, maturity, flexibility, prepayment optionality and refinancing risk. The investor compares expected cash flows, downside severity, documentation, liquidity and alternative uses of capital. The same feature can have opposite value: borrower call flexibility reduces refinancing friction but can shorten the investor's high-spread exposure.

The decision record should state assumptions rather than announce a single optimal instrument. For example, a floating-rate loan may be preferred under one interest-rate path and a fixed-rate bond under another. Sensitivity tables should vary benchmark, spread, price, repayment and recovery independently so that a result is not mistaken for a trading signal.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Fictional teaching exercise: cash yield and downside

Fictional teaching facts. Loan A is purchased at 99, pays a benchmark of 3.0% plus a 4.0% margin, has a 1.0% floor and amortises 1% of par during the year. Bond B is purchased at 96, pays a 7.5% coupon and is assumed for this exercise to remain outstanding for one year. Ignore taxes, fees and reinvestment. Calculate one-year cash income and ending value under a no-default case, then state which assumptions prevent the figures from being a full yield comparison.

For a separate downside, assume each claim has EUR 100 par. Enterprise value available to the creditor class is EUR 62 after costs. Loan A shares first priority with EUR 150 of equal-ranking claims and no other first-priority debt; Bond B is unsecured behind EUR 80 of priority claims. Build each recovery waterfall explicitly. Do not infer the result from the product name.

Sensitivity exercise

Construct a grid with benchmark rates of 2%, 3% and 5%, and operating EBITDA outcomes of base, minus 10% and minus 20%. Recalculate cash interest and debt-service coverage for the fictional borrower. Identify the first cell in which liquidity, rather than terminal enterprise value, becomes the binding constraint.

Practitioner review sequence

Reconcile enterprise value to equity value through every senior claim and net-debt component. Bridge EBITDA to cash and show the timing of interest, amortisation, fees, investment and working capital.

Expose capital weights, debt cash cost, fees, equity-return assumptions and tax assumptions. Present upside, base and downside paths and identify any liquidity failure before quoting a terminal return.

Separate benchmark, margin, floor, coupon, price, maturity, amortisation and call assumptions before comparing instruments. Show expected-loss inputs as scenarios, and build recovery from obligors, collateral and priority before adding costs and timing.

Legal, tax, regulatory and accounting boundary

These finance examples do not determine tax deductibility, debt-equity characterisation, distributions, insolvency, perfection or enforcement. Those consequences require fact- and jurisdiction-specific qualified review.

Primary-source map

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS18: Delaware Code, Title 6, Article 9, <https://delcode.delaware.gov/title6/c009/index.html>.

The Private Equity Perspective

A sponsor-backed financing is easiest to understand when the equity and credit cases are modelled separately and then reconciled. The sponsor asks whether the investment can generate an acceptable equity outcome across plausible exit paths. The creditor asks whether the borrower can meet contractual payments and preserve value before the sponsor receives that residual. Both analyse the same business, but their payoff functions and control rights differ.

This chapter uses fictional teaching structures rather than unnamed transactions or private dialogue. Public statistics are used only for bounded context. Fund terms, management fees, carried interest, hurdle arrangements and portfolio-company rights vary by vehicle and document, so the exercise states every assumption instead of presenting one structure as universal.

Understanding the sponsor as a counterparty

A sponsor usually contributes equity through acquisition and holding entities, appoints or influences the board, and pursues a value-creation plan over a finite investment horizon. That influence can improve strategic focus and access to capital, but it also creates incentives to preserve equity optionality. A creditor should neither assume unlimited support nor assume abandonment in stress. The analysis should identify committed equity, permitted distributions, follow-on funding options and the sponsor's control over major decisions.

The sponsor's reputation and relationship network are contextual factors, not sources of repayment. Convert qualitative observations into testable questions. Does the sponsor provide committed capital at closing? Can it cure a covenant and on what terms? Can value leave the restricted group? Does governance permit a sale, recapitalisation or acquisition without creditor consent? The documents and cash flows answer those questions.

Source note (retrieved 12 July 2026): PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>; PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

How a private equity fund is organised

A simplified fund includes investors that commit capital, a manager or adviser that selects and oversees investments, and one or more entities through which investments are held. Fund-level economics can include management fees, carried interest and contractual distribution rules. Those arrangements affect sponsor incentives, but the portfolio-company creditor is generally exposed to the borrower group and its documents rather than directly to the fund's assets.

For credit analysis, distinguish three layers. The fund layer controls capital calls and distributions under the fund documents. The acquisition-vehicle layer receives equity and incurs or holds transaction claims. The operating layer owns the business and generates cash. A statement that the sponsor has capital available does not prove that the borrower may demand it or that it will rank as equity when supplied.

Source note (retrieved 12 July 2026): PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>; PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>.

The investment process and the leverage decision

A disciplined acquisition model begins with enterprise value and sources and uses, then builds operating cash flow, debt service and exit value. Leverage can reduce the initial equity cheque and amplify the residual return, but it also consumes cash and narrows the range of operating outcomes the borrower can survive. The sponsor should therefore choose leverage together with liquidity, maturity, hedging and covenant flexibility rather than treat debt quantum as an isolated target.

The creditor should reconstruct the sponsor case rather than accept the headline return. Separate revenue growth, margin improvement, acquisitions, multiple change and debt paydown. Identify which components require additional capital or execution. Then reverse the analysis: hold the exit multiple constant, reduce operating performance, delay initiatives and add working-capital stress. The result shows how much of the equity thesis depends on favourable timing.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf.

Value creation and cash available for debt service

Value creation can arise from operating improvement, organic growth, acquisitions, capital allocation and a changed valuation at exit. Only some of those paths produce near-term cash for debt service. A margin improvement that requires restructuring cost, a growth plan that consumes working capital, or an acquisition programme that uses incremental debt may increase terminal value while worsening interim liquidity.

The credit model should divide each initiative into timing, cash cost, evidence and downside. For an add-back, ask when the saving is expected, what action creates it, what cash must be paid first and what happens if delivery is late. For an acquisition, show purchase price, financing, integration cost, pro forma EBITDA policy and headroom under debt, lien, investment and restricted-payment covenants.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

Capital structure and covenant negotiation

The sponsor values flexibility to run the business, refinance, acquire, reorganise and distribute value. Creditors value limits that protect repayment and priority. The negotiation therefore concerns capacity, conditions and information rather than labels. A large basket may be less important if it requires a ratio the borrower cannot meet; a small fixed basket may be more usable if it has no condition and can be reclassified.

Review the structure as a connected system. Debt capacity interacts with liens; investments interact with restricted payments and asset transfers; unrestricted subsidiaries can change the cash and collateral perimeter; incremental facilities interact with MFN protection and voting. A covenant summary that reads each provision alone can materially overstate protection.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07:

SEC EDGAR, *Carnival 2023 secured-notes indenture*,
<https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Portfolio-company oversight

Sponsor oversight may include board participation, budgets, management incentives, operating reviews and approval of material transactions. The creditor should focus on the information that reaches the borrower and lenders: monthly liquidity, covenant calculations, budget variance, customer concentration, capital expenditure and acquisition performance. Governance quality becomes credit-relevant when it changes the speed and reliability of corrective action.

An early-warning framework should define thresholds before stress. Examples include sustained negative variance, revolver usage, overdue payables, delayed reporting, covenant headroom, customer loss and unplanned capital expenditure. Escalation should lead to a revised thirteen-week cash flow, covenant forecast and funding plan, not simply a narrative assurance.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf.

Exit routes and their credit implications

An exit may occur through a sale, public offering, recapitalisation or another transfer. For creditors, the relevant questions are repayment, portability, change-of-control treatment, mandatory prepayment, redemption cost and the credit quality of any continuing obligor. An assumed exit date is not a contractual maturity solution unless a credible sale or refinancing process can be executed before liquidity is exhausted.

The downside model should test a delayed exit and a lower valuation simultaneously. It should also state whether debt is prepaid at par, at a premium, through a call schedule or through a contractual offer. Those mechanics come from the loan agreement or indenture and can change the equity value available at exit.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Sponsor choices in stress

When performance deteriorates, the sponsor compares the value of new money with the value of preserving optionality. Possible actions include an equity contribution, asset sale, covenant waiver, debt buyback, maturity extension, new priority financing or a broader restructuring. Each action changes value and control differently. The creditor should model the business without assuming a voluntary contribution, then analyse what terms could make support rational.

A constructive negotiation starts with a shared liquidity bridge and an agreed fact base. It then separates temporary liquidity, structural overleverage and operational underperformance. Temporary needs may be addressed with limited funding and milestones. Structural problems require a sustainable capital structure. Operational problems require a credible plan with funding, accountability and time.

Fund size, strategy and relationship effects

Fund size does not determine behaviour. Strategy, investment mandate, remaining fund life, concentration, governance and the economics of the specific position matter more. A larger sponsor may have more resources but also more layers of approval. A specialist sponsor may understand an industry deeply but operate with a narrower capital base. Replace stereotypes with questions about authority, incentives and available alternatives.

Repeated interactions can reduce information and execution friction, yet relationship value should not displace the documents. Credit approval should record which benefits are contractual, which are observable and which are assumptions. A relationship may support dialogue; it does not create collateral, guarantee coverage or a payment obligation.

Source note (retrieved 12 July 2026): PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>.

Fictional teaching exercise: sponsor return and creditor resilience

Fictional teaching facts. Cedar Components is acquired for EUR 800 million, equal to 10.0x EUR 80 million of EBITDA. The structure uses EUR 480 million of debt and EUR 320 million of equity. Debt costs 7.5% in year one. Maintenance capital expenditure is EUR 12 million, cash taxes are EUR 8 million, working-capital investment is EUR 6 million and scheduled amortisation is EUR 5 million. The sponsor expects EBITDA to reach EUR 110 million in year five and assumes a 10.0x exit multiple.

Build a base case and a downside. In the base case, EBITDA grows evenly, cash conversion follows the stated uses and all remaining cash reduces debt. In the downside, year-two EBITDA falls 15%, recovers only to EUR 90 million by year five, working-capital investment rises by EUR 4 million in the stress year and the exit multiple is 8.0x. Calculate annual interest, cash available for paydown, ending net debt, exit equity and gross equity multiple. Identify the first year in which liquidity or debt service, rather than terminal value, constrains the outcome.

Fictional teaching exercise: fund economics

Assume a fictional fund commits EUR 100 million to one investment and later receives EUR 170 million of gross proceeds. For this exercise only, assume a EUR 2 million annual management fee charged for four years, a return of contributed capital before carried interest, an 8% annual simple preferred return, 20% carry above that hurdle, no catch-up and a full clawback at fund termination. Calculate cash remaining after fees, the preferred amount and the provisional carry. Then explain why a portfolio-company lender cannot treat this fund waterfall as a committed source of borrower support.

Practitioner review sequence

Rebuild the sponsor model from sources and uses through annual cash flow, debt paydown and exit; separate each value-creation driver.

Map fund, acquisition-vehicle and operating-company entities; identify which capital is committed, callable, discretionary or unavailable to the borrower.

Read debt, lien, investment, restricted-payment, asset-sale, unrestricted-subsidiary and incremental provisions together before judging flexibility.

Model delayed exit, lower valuation, operational underperformance and working-capital stress; do not assume support or refinancing.

Legal, tax, regulatory and accounting boundary

The chapter does not determine fiduciary duties, fund obligations, guarantee capacity, equity-cure effect, distribution legality, control consequences or enforcement rights. Sponsor, finance, tax and restructuring counsel must verify those matters against the relevant fund, acquisition, finance and jurisdictional documents.

Primary-source map

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>; PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

The Art of the Term Sheet

A financing term sheet is a decision architecture. It translates the transaction plan into facility amount, purpose, maturity, economics, conditions, covenants, transfer rules and allocation of execution risk. It is not the final credit agreement, and its binding effect depends on the associated documents and governing law. The drafting objective is to make every commercial assumption traceable to an operative provision or an identified open point.

This chapter distinguishes commitment, mandate, market flex, clear-market language, certain-funds requirements, fee economics, original issue discount and MFN protection. Those concepts can interact, but they answer different questions. Combining them into one informal idea of funding certainty creates avoidable risk.

Understanding the commitment package

A commitment package commonly includes a commitment letter, term sheet and one or more fee letters, together with conditions, specified representations and documentation principles. The commitment letter identifies the parties, amount, purpose, availability and conditions to funding. The term sheet records commercial terms. Fee materials address compensation and may include flex economics. The package must be read as a whole, including incorporation clauses and priority provisions.

The analyst should build a commitment matrix. For each source of funds, record the committing entity, amount, currency, expiry, conditions, reduction rights, assignment rights and evidence of authority. Then reconcile the matrix to transaction sources and uses. A signed commitment is not sufficient if the amount, timing, conditions or entity do not match the acquisition obligation.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS08: UK Takeover Panel, Takeover Code Rule 2.7, <https://code.thetakeoverpanel.org.uk/tp/rules/rule-2/rule-2-7.html>; PS09: UK Takeover Panel, Takeover Code Rule 24.8, <https://code.thetakeoverpanel.org.uk/tp/rules/rule-24/rule-24-8.html>.

Facility structure and sizing

Sizing starts with uses: purchase price, refinancing, fees, taxes, minimum cash, working capital and any contingent payment. Sources must match by amount, currency and timing. A term facility may fund acquisition consideration; a revolving facility may remain undrawn for liquidity; a bridge may cover a planned capital-markets takeover. Each source needs a stated purpose and availability rule.

The term sheet should distinguish committed amount from expected funded amount. It should also state whether fees and OID reduce cash proceeds. If EUR 500 million face amount is issued at 98, gross cash proceeds are EUR 490 million before fees, while principal at maturity remains EUR 500 million. Sources and uses must reflect cash received, not only nominal debt.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS23: eCFR, 26 CFR 1.1273-1 and 1.1275-2, <https://www.ecfr.gov/current/title-26/part-1/section-1.1273-1>.

Pricing, maturity and amortisation

Pricing terms should identify benchmark, margin, floor, step-ups or step-downs, OID, upfront fees, commitment fees and default interest. Maturity must be linked to any springing or earlier-maturity condition. Amortisation, excess-cash-flow sweep, asset-sale prepayment and voluntary prepayment operate on different triggers and may apply in a stated order.

A single all-in number can hide different cash and accounting effects. Prepare a cash schedule showing issuance proceeds, fees paid, periodic interest, amortisation and redemption. Separately identify any tax or accounting analysis. The commercial term sheet should not state a generic tax result.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS23: eCFR, 26 CFR 1.1273-1 and 1.1275-2, <https://www.ecfr.gov/current/title-26/part-1/section-1.1273-1>.

Mandate and arranger rights

A mandate can allocate arranger roles, exclusivity, syndication control, information rights, publicity, indemnity and fees. Those rights are not the same as a funding obligation. The commitment package should state which entities arrange, which underwrite and which may assign. If multiple arrangers participate, title and economics should reconcile to actual commitment and responsibility.

The borrower should test the process under three states: successful distribution, partial distribution and no distribution before closing. For each state, identify who must fund, what terms may change, whether additional arrangers may be appointed and what happens after closing to residual exposure.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

Market flex

Market flex permits specified changes to improve distribution. Pricing flex can change margin, OID or fees. Structural flex can reallocate amounts, maturities or instrument form within agreed limits. Amount flex can resize a tranche or shift capacity. The document should define who may exercise flex, during what period, for what purpose and subject to which caps and protections.

Flex is not a blank cheque. The sources-and-uses model should show the maximum cash and principal effect of every permitted movement. If OID can increase, the borrower may need more face amount or equity to fund the same use. If a tranche can move between loan and bond form, maturity, call protection, covenants, collateral and settlement may change.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

Clear-market provisions

A clear-market provision generally restricts competing debt issuance or financing activity during a defined marketing period, subject to negotiated exceptions. Its function is to support distribution conditions; it should not be described as an automatic right to terminate funding unless the commitment documents expressly create that result. Scope, duration, affiliates, exceptions and remedy must be read from the text.

The borrower should list ordinary-course financing, existing programmes, acquisition debt, local facilities and permitted refinancings that must remain available. The arranger should identify which competing supply would materially affect distribution. The final clause should resolve that conflict explicitly rather than rely on an informal understanding.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

Certain funds in a UK public acquisition

In a UK public offer, the Takeover Code provisions cited here establish requirements concerning the firm offer announcement and cash confirmation. Financing analysis must begin with those rules and the exact acquisition structure. The financing conditions, specified representations and drawstop events should be narrower than a general corporate financing condition set where transaction certainty requires that result.

Do not use the phrase certain funds as a substitute for a closing checklist. Record every condition, evidence item, representation, default and termination right, then test whether it can prevent funding when the acquisition consideration is due. Separate the legal availability of funds from operational steps such as notices, account details, currency conversion and funds flow.

Source note (retrieved 12 July 2026): PS08: UK Takeover Panel, Takeover Code Rule 2.7, <https://code.thetakeoverpanel.org.uk/tp/rules/rule-2/rule-2-7.html>; PS09: UK Takeover Panel, Takeover Code Rule 24.8, <https://code.thetakeoverpanel.org.uk/tp/rules/rule-24/rule-24-8.html>.

Fees and original issue discount

Fees compensate for commitments, arrangement, underwriting, agency, ticking, utilisation or other agreed services and risks. OID means debt is issued for cash below its face amount. The two can have different payment recipients, timing and tax or accounting treatment. A term sheet should identify each item rather than compress them into one percentage.

For U.S. tax purposes, OID and qualified-reopening analysis follows detailed rules. A commercial model may show the cash arithmetic, but a tax conclusion must come from qualified review. The same boundary applies to amendment fees, consent payments and exchange economics.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS23: eCFR, 26 CFR 1.1273-1 and 1.1275-2, <https://www.ecfr.gov/current/title-26/part-1/section-1.1273-1>.

MFN yield protection

An MFN provision can protect an existing tranche when specified later debt is issued at a higher yield. The term sheet must define protected debt, excluded debt, comparison period, yield components, threshold and remedy. Yield may include margin, floor, OID and fees under a stated method. A label such as MFN does not reveal that calculation.

Build the formula before negotiation closes. State the assumed life used to convert OID or fees, how benchmark floors are compared, whether fixed-rate debt is included, and whether the remedy increases margin or permits another adjustment. Test a later financing with both a higher margin and deeper OID.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

From term sheet to operative documents

The term sheet sets commercial direction; the credit agreement and related documents create detailed rights and obligations. A term can change through definitions, qualifiers, exceptions and calculation rules even when the headline appears unchanged. The closing team should maintain an issues list that maps every term-sheet item to a document section and records any deviation.

Priority items include borrower and guarantor coverage, collateral, incremental capacity, mandatory prepayment, financial definitions, representations, covenants, events of default, voting, transfers and agent authority. A signed-off issues list should sit beside the final sources-and-uses and funds-flow documents.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Fictional teaching exercise: flex and funding certainty

Fictional teaching facts. An acquisition requires EUR 720 million at closing, including fees and minimum cash. Equity is fixed at EUR 270 million. The arranger commits a EUR 450 million term loan at 99 OID and may flex OID down to 97.5. No additional source is identified. Calculate cash proceeds at initial terms and maximum flex. At 99, proceeds are EUR 445.5 million and the transaction is EUR 4.5 million short before other fees. At 97.5, proceeds are EUR 438.75 million and the shortfall is EUR 11.25 million. The commitment amount balances nominal sources but not cash uses.

Revise the term sheet in two different ways: one with an equity backstop for the OID shortfall and one with authority to increase face amount subject to a leverage cap. For each, state who bears the risk and what documentary condition must be satisfied.

Fictional teaching exercise: MFN calculation

Assume an existing term loan pays benchmark plus 400 basis points with no OID. Six months later, a specified incremental loan is issued at benchmark plus 450 basis points and 98 OID. The fictional MFN compares margin plus OID amortised over four years, has a 50 basis point threshold and requires a margin increase for excess yield. OID contributes 50 basis points per year under the stated simplification, so new yield is 500 basis points over benchmark. The excess over existing yield is 100 basis points; after the 50 basis point threshold, the remedy is a 50 basis point margin increase. State why actual documents may produce a different result.

Practitioner review sequence

Reconcile committed face amount, issue price, fees, currency and timing to cash sources and uses under maximum flex.

Separate commitment, mandate, clear-market restriction, market flex and acquisition-funding conditions; identify the operative document for each.

Write the MFN formula, exclusions and remedy with a worked example before finalising the term sheet.

Map every agreed commercial term to the final credit agreement, fee letter, security document or funds-flow step.

Legal, tax, regulatory and accounting boundary

The chapter does not opine on binding effect, commitment enforceability, MAC standards, certain-funds sufficiency, takeover compliance, OID tax treatment, qualified reopening or MFN interpretation. Acquisition-finance and tax counsel must review the complete package and governing law.

Primary-source map

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS08: UK Takeover Panel, Takeover Code Rule 2.7, <https://code.thetakeoverpanel.org.uk/tp/rules/rule-2/rule-2-7.html>; PS09: UK Takeover Panel, Takeover Code Rule 24.8, <https://code.thetakeoverpanel.org.uk/tp/rules/rule-24/rule-24-8.html>; PS23: eCFR, 26 CFR 1.1273-1 and 1.1275-2, <https://www.ecfr.gov/current/title-26/part-1/section-1.1273-1>.

PART II

THE INSTRUMENTS

- 06 Anatomy of a Leveraged Finance Transaction
 - 07 Loans vs. Bonds
 - 08 Capital Structure - The Architecture of Leverage
 - 09 High-Yield Bonds
 - 10 Direct Lending and Private Credit
 - 11 CLO Mechanics and Impact on Leveraged Finance
-

Anatomy of a Leveraged Finance Transaction

A leveraged finance transaction is a sequence of controlled decisions from mandate through maturity. The parties repeatedly convert provisional information into commitments, documents, cash movements and continuing obligations. The analyst's task is to preserve one reconciled record of assumptions, approvals and governing terms as the transaction changes form.

6.1 Mandate and transaction perimeter

The process starts by defining purpose, acquisition or refinancing perimeter, borrower group, purchase consideration, existing debt, fees, minimum cash and timing. A mandate allocates arranging and advisory roles; it does not by itself establish final debt availability. The sources-and-uses model should have a named owner, version date and reconciliation to the legal structure.

Entity diagrams must distinguish acquisition vehicles, operating companies, guarantors, non-guarantors and excluded entities. That diagram drives diligence, financial modelling, collateral, funds flow and closing conditions. A consolidated presentation that hides the legal borrower can create a false impression of cash and asset access.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

6.2 Diligence and the credit case

Diligence should test the variables that can cause payment failure: revenue concentration, margin durability, working capital, capital expenditure, tax, pensions, litigation, regulation, cyclical and management execution. Each finding must map to the model, a document protection, a closing condition or an accepted residual risk.

The credit paper should separate verified historical information, management forecast, adviser adjustment and lender assumption. It should show base, downside and severe-but-plausible paths, covenant headroom and liquidity. Approval conditions must be written so the closing team can determine whether they are satisfied.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf.

6.3 Commitment and documentation

Commitment documents establish the funding promise and its conditions; operative finance documents establish the debt after closing. The drafting workstream must reconcile facility amount, purpose, maturity, economics, guarantees, collateral, covenants, defaults, voting, transfers and agent authority. Deviations from the approved term sheet should be visible, not buried in definitions.

A documentation tracker should record the section, issue, approved position, current draft, owner and deadline. High-risk definitions include EBITDA, indebtedness, liens, investments, restricted payments, subsidiaries, material adverse effect and pro forma calculations. Definitions can expand or contract every operative covenant that uses them.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

6.4 Syndication and price discovery

Distribution presents the credit and instrument to eligible investors and collects orders subject to the applicable process. Investor feedback can affect allocations and permitted flex. The arranger must keep commercial changes within commitment authority and update the borrower, credit approval and documents consistently.

An order book is not final funding until allocations, settlement requirements and conditions are satisfied. Controls should reconcile lender names, commitment amounts, assignments, KYC status, tax forms, settlement instructions and final economics. Unsupported claims about investor demand or forced selling should not appear in the credit record.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf.

6.5 Closing mechanics

The closing checklist converts legal conditions into evidence and cash movement. It should identify every deliverable, responsible party, form requirement, status and waiver authority. The funds-flow statement reconciles source amounts, issue prices, fees, debt repayment, purchase consideration, taxes, cash to balance sheet and account coordinates.

Run the funds flow as a double-entry control. Total sources must equal total uses; every payment must have a legal purpose and authorised account; face amount must reconcile to documents; cash proceeds must reflect OID and fees; and post-closing debt and cash must reconcile to the opening model.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

6.6 Post-closing administration

After closing, the borrower must manage notices, reporting, interest periods, compliance certificates, covenant tests, mandatory prepayments, collateral actions and corporate changes. The administrative agent maintains specified lender and payment functions under the agreement. The operational calendar should cite each deadline and required recipient.

A covenant calendar is not enough. The borrower also needs capacity tracking for debt, liens, investments, restricted payments and asset sales. Each use should record amount, basket, ratio, test date, reclassification and remaining capacity. That ledger becomes essential when transactions accumulate over several years.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

6.7 Amendments, refinancing and maturity

A financing continues to evolve through waivers, incremental debt, acquisitions, asset sales, repricing, extension and refinancing. Every change should update the model, covenant ledger, lender register and maturity profile. Voting analysis must identify the affected class, required threshold, individual rights and agent or trustee process.

Maturity planning begins well before the due date. The borrower should track market access, cash accumulation, prepayment cost, hedging, covenant headroom and any earlier-maturity trigger. The downside plan should identify what can be sold, extended or restructured without assuming that creditor consent will be available.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

Fictional teaching exercise: closing control

Fictional teaching facts. A borrower signs a EUR 400 million term facility at 98.5 OID and a EUR 75 million revolving facility that remains undrawn. Equity contributes EUR 210 million. Uses are EUR 565 million purchase consideration, EUR 18 million debt repayment, EUR 9 million fees and EUR 8 million opening cash. Term-loan cash proceeds are EUR 394 million, so total funded sources are EUR 604 million and total uses are EUR 600 million. Identify the EUR 4 million excess and specify whether it increases opening cash, reduces equity or reflects an error. No payment instruction should be released until the model, documents and funds flow use the same answer.

Add a condition requiring delivery of a solvency certificate and a collateral filing after closing. Place each item on the checklist with owner, timing, evidence, waiver authority and consequence. Explain why a post-closing covenant is not the same as a condition to funding.

Fictional teaching exercise: amendment vote

Assume the selected fictional facility has EUR 300 million held by six lenders. A requested amendment affects only the interest margin of a new extension tranche and leaves non-extending lenders' stated payment terms unchanged. Build the voting question in four steps: identify the operative provision, affected class, general threshold and any individual consent right. Do not supply a legal answer until the fictional agreement states those rules.

Practitioner review sequence

Maintain one reconciled transaction model, entity chart, issues list, closing checklist and funds flow with named owners and dates.

Separate verified history, forecast, adviser adjustment and lender assumption; map every material diligence finding to a decision.

Trace each commercial term into an operative document and each closing condition into objective evidence and waiver authority.

After closing, maintain reporting, covenant-capacity, lender-register and maturity-control records.

Legal, tax, regulatory and accounting boundary

Document hierarchy, conditions, voting, agency, trustee authority, transfers, settlement, collateral, guarantees, amendments and enforcement depend on the selected instruments and governing law. Qualified loan and bond counsel should advise on those matters for any live transaction.

Primary-source map

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

A leveraged finance transaction is a structured process that brings together borrowers seeking capital, banks seeking fees, and investors seeking yield:

1. The lifecycle spans origination through maturity, with distinct phases (mandate, documentation, syndication, closing, ongoing administration) each with specific dynamics
2. Documentation architecture includes credit agreements, security documents, intercreditor agreements, guarantees, and ancillary documents—each serving specific functions
3. Borrower's counsel drafts; lender's counsel reviews—creating an inherent asymmetry that has contributed to documentation deterioration
4. Loans and bonds differ structurally in covenant style (maintenance vs. incurrence), amendment mechanics (majority vs. supermajority), and enforcement paths
5. Reading documentation efficiently requires prioritizing definitions, financial covenants, and the key negative covenants that govern value leakage and structural dilution
6. The timeline creates pressure that favors precedent over innovation and can compress diligence and negotiation
7. Post-closing administration continues for years, with ongoing reporting, potential amendments, and the ever-present possibility of distress requiring creditor decisions

Understanding this anatomy prepares you for the detailed analysis that follows: every covenant and provision we examine sits within this broader structure. The credit agreement is best understood as the constitution of a multi-year relationship between borrowers and creditors.

Next: Chapter 7 compares the two core instruments of leveraged finance, loans and bonds, and how they behave in the same capital structure.

Loans vs. Bonds

Introduction

Understanding the differences between leveraged loans and high-yield bonds is fundamental to working in leveraged finance. Both raise debt capital, both sit in the capital structure and both carry covenants, so at first reading the two can look interchangeable. In practice, a credit agreement and an indenture are differently built documents, and comparing them line by line is less straightforward than it looks.

This chapter examines the structural, economic, and documentary differences between the two instruments — the differences that determine which creditors control enforcement, how amendments are approved, what happens in a restructuring, and ultimately who bears losses when things go wrong.

In Europe the distinction has become more nuanced. U.S. loans and bonds retain significant structural differences, while European leveraged loans have increasingly adopted "bond-style" covenant packages, which makes the two instruments more directly comparable. Even in Europe, though, material differences in security, guarantees, and amendment mechanics remain, and a practitioner needs to understand both the U.S. baseline and the European variations.

The comparison in this chapter is deliberately narrow. The loan mechanics are illustrated by the public MeridianLink credit agreement and the bond mechanics by the public Carnival secured-notes indenture. The documents are examples, not proof that every loan or bond follows the same rule. The practitioner should repeat the comparison with the instruments in the transaction being analysed.

7.1 Legal form and creditor relationship

The selected credit agreement creates revolving and term commitments among named loan parties and uses an administrative-agent framework. The selected indenture governs notes issued as securities and uses a trustee framework. Those architectures affect notices, transfers, voting and enforcement, but the operative answer always comes from the document and governing law.

A loan investor generally becomes a lender through the agreement's assignment or participation mechanics. A bond investor holds or acquires a security through the applicable holding and settlement arrangements. Credit analysis should record beneficial ownership, registered holder, voting channel and any minimum transfer or eligibility condition.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

7.2 Interest and payment mechanics

The public credit agreement illustrates benchmark-based interest, margins, floors or alternatives, interest periods and payment dates as stated in that agreement. The public indenture illustrates a fixed coupon and stated interest-payment dates for the notes. Price and yield remain separate from contractual coupon or margin.

For each instrument, build a cash schedule from principal, benchmark, margin or coupon, price, amortisation, fees, maturity and redemption. The comparison should use the same time horizon and explicit prepayment assumptions. A lower stated spread can still produce a higher effective cost if issue price or fees differ.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

7.3 Maturity, amortisation and prepayment

A loan can include scheduled amortisation, voluntary prepayment, mandatory prepayment and repricing protection under its agreement. A bond generally repays principal at maturity unless redeemed, repurchased or otherwise discharged under the indenture. The selected instruments contain their own conditions and prices.

Borrower optionality and investor reinvestment risk move in opposite directions. Model the earliest economically rational repayment as well as legal maturity. For bonds, read the call schedule and make-whole provisions. For loans, read premium periods, excess-cash-flow sweeps and asset-sale application.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

7.4 Covenants and calculation style

The selected credit agreement contains affirmative, negative and financial or incurrence-related provisions with detailed definitions and exceptions. The selected indenture contains covenants framed through its own restricted group, baskets and tests. It is unsafe to reduce the distinction to maintenance versus incurrence without reading the entire package.

Compare covenant systems through identical questions: what action is restricted, which entities are inside the perimeter, what conditions apply, which baskets or ratios create capacity, when is the test measured, can capacity be reclassified, and what is the consequence of failure? This method exposes differences without claiming a universal product rule.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

7.5 Guarantees, collateral and ranking

Both a loan and a bond can be secured and guaranteed. Compare the actual grantors, guarantors, excluded entities, collateral, release provisions and intercreditor arrangements. A shared first-lien label may still conceal different claim amounts, hedge priority, revolving exposure, release conditions or enforcement control.

Structural priority is analysed entity by entity. Debt at an operating subsidiary can be paid from that subsidiary's assets before value moves to a parent creditor. Contractual subordination, lien priority and guarantee coverage add separate layers. Present the resulting waterfall with stated assumptions and counsel review.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS18: Delaware Code, Title 6, Article 9, <https://delcode.delaware.gov/title6/c009/index.html>.

7.6 Voting and amendments

The selected agreement and indenture each establish general voting thresholds and protected matters. The analyst should not assume that the same percentage, class rule or individual consent applies across products. Identify the affected provision, holder universe, record date, class and any separately protected right.

Operational control also differs. Loan consents may flow through an administrative agent and lender register. Bond consents and directions may flow through holders and a trustee under the indenture and settlement structure. Time, evidence of holdings, indemnity and notice mechanics can affect execution.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

7.7 Defaults and remedies

Payment, covenant, representation, cross-default, judgment and insolvency provisions must be compared from the documents, including thresholds, grace periods and notice. A change-of-control put in a bond is not automatically the same as an event of default. An acceleration right is not the same as immediate collateral enforcement.

In stress, map the sequence: event, notice, cure, declaration, acceleration, direction, standstill, enforcement and proceeds application. Intercreditor and insolvency law may alter that sequence. The product name does not answer who controls action or how value is distributed.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

7.8 Transferability and liquidity

The selected loan agreement has assignment and participation rules, including conditions and administrative steps. The notes rely on securities transfer and the applicable offering and holding framework; Rule 144A governs a U.S. private-resale safe harbour for eligible transactions. Neither document guarantees a liquid secondary market.

Liquidity analysis should consider position size, settlement time, information access, eligibility, transfer restrictions, price transparency and market conditions. A claim that bonds or loans are always more liquid is not supportable without a dated and defined sample.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS10: eCFR, 17 CFR 230.144A, <https://www.ecfr.gov/current/title-17/chapter-II/part-230/section-230.144A>.

Two-document comparison exercise

Create a working paper with one column for the cited credit agreement and one for the cited indenture. Complete ten rows: obligors, guarantees, collateral, interest, maturity, voluntary repayment, mandatory repayment, covenants, amendment thresholds and default action. Each cell must contain a section reference or say not located. A blank may not be filled with a market assumption.

After completing the document facts, add a third column for analytical implication. Keep fact and inference separate. For example, a stated call premium is a fact; the effect on expected life is an inference that depends on refinancing economics.

Fictional teaching exercise: all-in cash cost

Fictional Loan L has EUR 100 face amount, is issued at 99, pays a 3% benchmark plus 4% margin and amortises 1% after one year. Fictional Bond B has EUR 100 face amount, is issued at 97, pays a 7.25% coupon and has no scheduled principal before maturity. Calculate first-year cash proceeds and interest under the stated assumptions. Then list the missing inputs required for a valid expected-cost comparison: fees, expected repayment date, call price, benchmark path, amortisation beyond year one and tax or accounting treatment.

Practitioner review sequence

Compare named instruments, not product stereotypes; cite the section supporting every operative statement.

Separate legal form, payment, maturity, optionality, covenants, priority, voting, defaults, transfers and liquidity.

Map obligors, guarantors, collateral and intercreditor control before drawing a ranking or recovery conclusion.

Keep document facts separate from economic inference and legal advice.

Legal, tax, regulatory and accounting boundary

English or European and U.S. finance counsel must review the loan-versus-bond comparison, particularly guarantee and collateral coverage, amendment rights, transfers, acceleration, intercreditor control and enforcement. The cited instruments support only their own terms.

Primary-source map

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS10: eCFR, 17 CFR 230.144A, <https://www.ecfr.gov/current/title-17/chapter-II/part-230/section-230.144A>; PS18: Delaware Code, Title 6, Article 9, <https://delcode.delaware.gov/title6/c009/index.html>.

Capital Structure – The Architecture of Leverage

Capital structure is the map of claims on a business and the rules that determine payment, control and loss allocation. A useful map is built legal entity by legal entity. It identifies each instrument, obligor, guarantor, collateral package, maturity, cash coupon, amortisation, covenant position and intercreditor relationship. A simple stack labelled senior, junior and equity cannot capture structural priority or leakage.

The analysis proceeds in two directions. The going-concern view tests cash interest, amortisation, liquidity and covenant headroom. The downside view allocates enterprise and asset value through priority, structural subordination and contractual arrangements. Both views are necessary because a company can remain solvent but face a maturity problem, or have adequate current liquidity while creditors are poorly positioned in a downside.

8.1 Sources and uses create the opening structure

Every capital structure begins with a sources-and-uses statement. Uses include consideration, refinancing, fees, taxes, minimum cash and other funded requirements. Sources include equity, funded debt, cash on balance sheet and any seller or contingent financing. Face amount and cash proceeds must be separated where debt is issued at a discount or with upfront fees.

The opening balance sheet should reconcile to the funds flow. For each new debt instrument, record principal, issue price, cash received, fees, interest basis, maturity and borrower. For each repaid instrument, record principal, accrued interest, premium and release mechanics. The result becomes the control total for later leverage and covenant analysis.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

8.2 Entity structure and structural priority

A parent creditor relies on value moving from subsidiaries through dividends, distributions, loans or asset transfers. Creditors of an operating subsidiary generally look first to that subsidiary's assets and cash under the applicable law and documents. This creates structural priority even when the parent debt is described as senior at its own entity.

Build an entity chart with ownership percentages, operating assets, cash generation, debt, guarantees and collateral. Mark restricted and unrestricted entities as defined by the relevant document. Then trace the legal path by which cash can reach each borrower. Consolidated EBITDA cannot be assumed to be fully available at every obligor.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

8.3 Contractual subordination and lien priority

Contractual subordination changes payment or enforcement rights by agreement. Lien priority concerns competing security interests in collateral. Structural subordination follows entity location. Those concepts can overlap but should be stated separately. A subordinated note at the same issuer differs from senior debt issued at a parent above operating liabilities.

For secured debt, identify collateral, grantor, perfection step, priority, exclusions, release conditions and enforcement control. Article 9 of the Delaware Code provides public statutory text for relevant U.S. security-interest questions, but application depends on asset type, debtor location, governing law and transaction facts. The model should state counsel assumptions rather than convert them into financial facts.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS18: Delaware Code, Title 6, Article 9, <https://delcode.delaware.gov/title6/c009/index.html>.

8.4 Revolvers, term loans and bonds in one structure

A revolving facility supports liquidity and may include letters of credit or ancillary exposure. A term loan provides funded principal and may amortise. A secured or unsecured bond adds its own coupon, maturity, redemption and covenant package. When instruments share collateral, intercreditor terms may allocate priority, voting and enforcement control.

The cash model should treat undrawn commitments separately from funded debt. Undrawn availability is a liquidity resource only if borrowing conditions can be met. It can also become funded senior exposure in stress. Recovery analysis should therefore include a case in which the revolver is fully drawn before enforcement.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

8.5 Guarantees and the credit perimeter

Guarantees can extend a claim to entities other than the primary borrower, but coverage is rarely synonymous with the entire consolidated group. Review guarantor accession, exclusions, release events, materiality tests and limitations. Compare guarantor EBITDA and assets with consolidated amounts using a transparent bridge.

A guarantee is not a substitute for cash analysis. A guarantor may have local liabilities, restricted cash, minority interests or legal limitations. The analyst should show both the contractual perimeter and the economic contribution of each entity, subject to legal review of validity and enforceability.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

8.6 Maturity architecture and refinancing dependency

A maturity schedule should include legal maturity, amortisation, springing maturity, call periods, hedging expiry and any material lease or pension cash need. Clustering can create refinancing dependency even when current leverage is manageable. A small earlier maturity can also pull forward the practical deadline for the entire structure.

Test a no-refinancing case. Project cash accumulation, mandatory debt reduction and liquidity through each maturity. Then test partial refinancing at a higher cost and lower capacity. The analysis should identify how much enterprise value or equity support is required if markets remain unavailable.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

8.7 Incremental and refinancing capacity

A capital structure is not static. Credit agreements can permit incremental facilities, incremental-equivalent debt, refinancing debt and other baskets subject to stated conditions. Bond indentures can permit additional debt and liens under their own tests. Capacity must be measured across every relevant covenant and intercreditor requirement.

A complete capacity model records fixed baskets, grower components, ratio capacity, reclassification, maturity limits, MFN protection, guarantor requirements, collateral sharing and voting. It also tests the use of capacity after EBITDA falls. Headroom created by a pro forma adjustment may disappear if the adjustment is not realised.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

8.8 Private credit in the architecture

Private credit can provide a concentrated lender group, tailored delayed-draw or acquisition capacity and a negotiated information package. Those features arise from the specific facility and ownership structure. They do not establish one standard leverage, covenant or pricing outcome.

When comparing private credit with syndicated debt, hold the transaction constant. Compare committed cash, certainty, maturity, amortisation, call protection, financial covenants, incremental capacity, transfer restrictions, lender concentration and amendment process. Use dated public aggregate sources only for market context.

Source note (retrieved 12 July 2026): PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>; PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>.

8.9 Downside waterfall

A downside waterfall begins with a range of enterprise values and a stated scenario date. Add or deduct non-operating assets, priority claims, costs and cash by legal entity. Allocate value first to claims with priority at the relevant entity or collateral, then through equal-ranking and subordinated claims. Show recoveries as ranges, not precise promises.

The waterfall should include sensitivity to a fully drawn revolver, reduced cash, additional permitted debt and delayed realisation. It should also show the effect of non-guarantor value. Counsel must confirm the assumed priority and enforcement path; the financial model then applies those assumptions consistently.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS18: Delaware Code, Title 6, Article 9, <https://delcode.delaware.gov/title6/c009/index.html>.

Fictional teaching exercise: opening capital structure

Fictional teaching facts. Atlas Packaging is acquired for EUR 900 million. Uses also include EUR 25 million of fees, EUR 15 million of existing-debt premium and EUR 10 million of minimum cash. Sources are EUR 350 million of equity, a EUR 450 million first-lien term loan issued at 99, and EUR 150 million of unsecured notes issued at 98. Cash proceeds are EUR 445.5 million and EUR 147 million, so total sources are EUR 942.5 million against EUR 950 million of uses. Calculate the funding gap and identify three ways to close it without pretending face value equals cash.

The borrower also has a EUR 75 million undrawn revolver sharing first-lien collateral. Build funded leverage at closing and stressed leverage after a full revolver draw. State separately the nominal commitment, funded amount and recovery claim assumption.

Fictional teaching exercise: entity waterfall

Atlas has an operating subsidiary worth EUR 500 million and a parent holding company with no independent assets. The operating subsidiary owes EUR 80 million of local priority liabilities and guarantees the EUR 450 million term loan. The unsecured notes are issued only by the parent and have no operating guarantee. Assume EUR 20 million of costs and no other value. Allocate value through the stated structure, then repeat with a EUR 75 million revolver draw sharing term-loan priority. Explain why the notes' senior label at the parent does not eliminate structural subordination.

Practitioner review sequence

Reconcile sources, uses, face amounts, cash proceeds, fees and opening debt before calculating leverage.

Map every entity, obligor, guarantor, collateral grantor, instrument and cash pathway.

Separate structural, contractual and lien priority; model undrawn senior commitments as a stress draw.

Build maturity, capacity and downside schedules that include additional permitted debt and non-guarantor value.

Legal, tax, regulatory and accounting boundary

Priority, perfection, guarantee validity, intercreditor control, cash movement, release and enforcement require secured-finance and restructuring counsel in each relevant jurisdiction. The financial waterfall is conditional on those legal assumptions.

Primary-source map

Source note (retrieved 12 July 2026): PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>; PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS18: Delaware Code, Title 6, Article 9, <https://delcode.delaware.gov/title6/c009/index.html>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

High-Yield Bonds

A high-yield bond is a security whose economic and legal features must be read through the offering materials, indenture and related security or intercreditor documents. This chapter uses the public Carnival secured-notes indenture as a document example. It does not infer a universal covenant, threshold, trustee duty or market price from that instrument.

The analyst separates four layers: issuer credit, instrument ranking, cash-flow terms and investor protections. Coupon and maturity describe only part of the claim. Redemption, change of control, additional-debt capacity, restricted payments, asset sales, defaults, amendments, transfer restrictions and trustee mechanics can change value materially.

9.1 Issuance and holding structure

The issuer creates notes under an indenture and delivers them through the applicable issuance and settlement framework. The indenture identifies issuer, guarantors, trustee, principal, interest, maturity and operative covenants. Investors should distinguish registered holder, beneficial owner and the party entitled to deliver a direction or consent.

Rule 144A is a U.S. private-resale safe harbour with specified conditions, including the qualified-institutional-buyer framework. It is not a credit conclusion. Transfer restrictions, legends and information rights should be read from the offering and security documents.

Source note (retrieved 12 July 2026): PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS10: eCFR, 17 CFR 230.144A, <https://www.ecfr.gov/current/title-17/chapter-II/part-230/section-230.144A>.

9.2 Coupon, price and yield

Coupon is the contractual interest rate on principal. Issue or purchase price determines cash invested. Yield depends on price, coupon, timing, redemption assumption and recovery. A bond issued below par can have a yield above coupon, but the calculation changes if the bond is redeemed before maturity or defaults.

Build cash flows date by date. Include accrued interest, settlement date, payment frequency, call price and any make-whole amount. A quoted yield should be labelled by convention and assumption, such as yield to maturity or yield to call. It should not be presented as a promised return.

Source note (retrieved 12 July 2026): PS01: FINRA, Bonds, <https://www.finra.org/investors/investing/investment-products/bonds>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

9.3 Redemption and borrower optionality

The selected indenture sets out optional-redemption provisions and prices for the notes. A call schedule can let the issuer repay at stated premiums after specified dates. A make-whole formula may apply in an earlier period. Equity-claw or other redemption rights, if present, must be read with their conditions and limits.

For credit valuation, model expected life rather than assume legal maturity. When spreads tighten, the issuer may refinance; when spreads widen, the bond may remain outstanding. That negative convexity can limit upside while extending downside exposure. The result is conditional on issuer incentives and document terms.

Source note (retrieved 12 July 2026): PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

9.4 Guarantees, security and ranking

A secured-notes label should be unpacked into issuer, guarantors, collateral, priority and release provisions. Compare the notes with revolving facilities, term loans, hedges, local debt and structurally senior liabilities. If collateral is shared, identify which agreement allocates control and proceeds.

The recovery model should not treat all consolidated enterprise value as directly available. Allocate value by entity and claim, include costs and test a full revolver draw. State whether guarantees and liens are assumed valid and perfected, subject to counsel review.

Source note (retrieved 12 July 2026): PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

9.5 Covenant architecture

An indenture can restrict additional debt, liens, restricted payments, asset sales, transactions with affiliates, mergers and other actions, subject to definitions, baskets, ratios and exceptions. The covenant package must be read as a system. Capacity in one covenant may depend on capacity or classification in another.

A covenant memo should identify the restricted group, testing time, pro forma rules, fixed and ratio capacity, builder amounts, reclassification, suspension or fall-away and consequences. Avoid copying specimen language; cite the selected indenture section and describe the mechanism in original prose.

Source note (retrieved 12 July 2026): PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

9.6 Change of control and asset sales

A change-of-control provision may require an offer to repurchase notes if the indenture's defined trigger occurs and any related conditions are met. That put is different from automatic acceleration unless the indenture states otherwise. Portability or rating conditions, where present, can change whether a transaction triggers the offer.

Asset-sale provisions define covered dispositions, permitted consideration and use of proceeds, then may require reinvestment, repayment or an offer. The analyst should trace the timetable and interaction with liens, investments and restricted payments.

Source note (retrieved 12 July 2026): PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

9.7 Defaults, acceleration and trustee process

The indenture specifies events of default, thresholds, grace or cure periods, notice and acceleration. Payment default, covenant default, cross-acceleration, judgment and insolvency may follow different rules. Record the exact trigger and affected series.

The trustee's authority, holder direction, indemnity and individual rights arise from the indenture and governing law. A default does not mean every remedy occurs automatically. Map declaration, rescission, direction, enforcement and proceeds application separately.

Source note (retrieved 12 July 2026): PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

9.8 Amendments, defeasance and discharge

The indenture distinguishes amendments that may be made without holder consent, amendments requiring a stated holder threshold and changes requiring additional or individual consent. The analyst should identify the holder universe, affected series and protected payment terms before stating a threshold.

Defeasance, covenant defeasance and satisfaction or discharge are distinct mechanisms with specified funding, opinion and procedural conditions. They should be described only from the indenture. Any tax-opinion requirement or tax consequence remains a matter for qualified tax counsel.

Source note (retrieved 12 July 2026): PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

9.9 Secondary-market analysis

Price can move because of benchmark rates, credit spread, liquidity, expected call date, covenant developments and issuer fundamentals. A price change is not evidence by itself that the market is correct or incorrect. The analyst should decompose the movement into observable cash-flow and risk assumptions.

A bond review records price source and time, accrued interest, position size, settlement, rating context, expected call, downside recovery and catalysts. It also identifies information gaps. The conclusion should be a conditional risk assessment rather than a claim of privileged execution knowledge.

Source note (retrieved 12 July 2026): PS01: FINRA, Bonds, <https://www.finra.org/investors/investing/investment-products/bonds>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Fictional teaching exercise: call schedule and return

Fictional teaching facts. A EUR 100 bond pays a 7.5% annual coupon in two equal instalments, is purchased immediately after a coupon date at 96, and may be called after one year at 103 or after two years at 101.5. Ignore accrued interest, taxes and transaction costs. Build cash flows for a one-year call, two-year call and maturity at year five at par. Calculate simple total cash proceeds in each path before computing any annualised yield.

Now assume the issuer's refinancing cost falls enough to make the one-year call economic. Explain why the investor's expected life shortens when the bond performs well, while a credit deterioration can extend the bond. Identify the document sections required to validate the fictional call assumptions in a live instrument.

Indenture navigation exercise

Using the cited public indenture, locate the definitions and operative sections for restricted payments, additional debt, liens, asset sales, change of control, redemption, events of default, amendments and trustee direction. For each item, write one sentence of document fact and one separate sentence of analytical implication.

Practitioner review sequence

Separate coupon, price, yield convention, expected call date and legal maturity.

Map issuer, guarantors, collateral, priority and intercreditor control before assigning recovery.

Read covenant capacity, change of control, asset sales, defaults and amendments from the selected indenture.

Treat trustee authority, defeasance, discharge and tax-opinion conditions as document-specific and counsel-reviewed.

Legal, tax, regulatory and accounting boundary

High-yield and tax counsel must review trustee duties, redemption, change of control, defaults, Rule 144A, amendments, defeasance, discharge, guarantees, security and tax-opinion descriptions against the selected offering and governing documents.

Primary-source map

Source note (retrieved 12 July 2026): PS01: FINRA, Bonds, <https://www.finra.org/investors/investing/investment-products/bonds>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS10: eCFR, 17 CFR 230.144A, <https://www.ecfr.gov/current/title-17/chapter-II/part-230/section-230.144A>.

Direct Lending and Private Credit

Direct lending describes a financing model in which a lender or concentrated group originates and holds a negotiated loan outside a broadly syndicated process. Private credit is broader and can include several strategies, structures and risk profiles. Neither term defines one leverage level, covenant package, return target or regulatory treatment.

The attraction for a borrower can be certainty, speed, confidentiality, tailored delayed-draw capacity or a smaller consent group. The trade-offs can include concentration of lender power, transfer limitations, call protection, reporting intensity and a different cost structure. The relevant comparison is transaction-specific and must include cash proceeds, flexibility and execution risk.

10.1 Defining the perimeter

A defensible market statement identifies whether it concerns sponsored or non-sponsored loans, senior or junior debt, performing or distressed strategies, fund-level or asset-level leverage, and a particular geography and date. Public private-fund statistics and the IMF's private-credit discussion provide bounded aggregate context, but they do not establish terms for an individual loan.

For transaction analysis, avoid market-size shorthand. Describe lender type, ownership concentration, facility structure, borrower size, use of proceeds and governing documents. Those fields explain economics better than a broad label.

Source note (retrieved 12 July 2026): PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>; PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>.

10.2 Origination and underwriting

A direct lender can underwrite with an expectation of retaining a substantial position, although co-investment, syndication or later transfer may still occur under the documents. The underwriting process should test business quality, cash conversion, leverage, liquidity, downside recovery, sponsor incentives and documentation in the same disciplined way as any credit decision.

Concentrated ownership can speed decisions but increases single-name and lender-group concentration. The credit paper should state final hold size, diversification, unfunded commitments and follow-on funding capacity. It should not assume that a fund can provide unlimited additional capital.

Source note (retrieved 12 July 2026): PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>; PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>.

10.3 Unitranche and layered structures

A unitranche may present one borrower-facing facility while lenders allocate economics or priority under separate arrangements. Other structures combine revolving, first-out, last-out, second-lien, subordinated or preferred claims. Labels do not determine ranking; the credit agreement, intercreditor or agreement-among-lenders terms do.

The borrower model should show one contractual payment schedule where appropriate, while the lender downside model should apply the actual internal waterfall. Counsel must confirm which arrangements bind the borrower, agents, lenders and third parties.

Source note (retrieved 12 July 2026): PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

10.4 Economics beyond headline spread

Total cash cost can include benchmark, margin, floor, OID, upfront fee, commitment fee, ticking fee, unused fee, call premium and amendment economics. Delayed-draw facilities add timing and availability assumptions. Compare cash cost under expected and downside drawings, not only on fully funded principal.

The lender evaluates income together with expected loss, liquidity, duration and capital usage. A contractual return target is not evidence of realised performance. Any aggregate return statistic requires a dated source, defined sample and methodology.

Source note (retrieved 12 July 2026): PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>; PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>.

10.5 Documentation and information

A concentrated lender group can negotiate financial covenants, reporting, board observation, budgets, liquidity tests and acquisition controls. The strength of those rights depends on definitions, cure periods, waivers, baskets and enforcement. A maintenance covenant is useful only if the test is timely, correctly calculated and connected to a meaningful consequence.

Information should feed a monitoring process. Monthly financials, liquidity, covenant headroom, variance and material events should update the downside model. The lender should define escalation triggers before deterioration rather than rely on relationship access alone.

Source note (retrieved 12 July 2026): PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

10.6 Amendments and concentrated voting

A small lender group can make amendments operationally simpler, but it can also concentrate negotiating leverage. The document should state majority, supermajority and individual consent rights, affiliate voting, replacement-lender mechanics and assignment. A bilateral facility can still require careful process and evidence.

In stress, distinguish liquidity support, covenant relief and permanent capital restructuring. New money may require priority, pricing or control changes. The analysis should show the value transferred by each proposal and the borrower's alternatives.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

10.7 Fund structure and liquidity

Private funds can have drawdown commitments, investment periods, borrowing facilities, distribution rules and finite terms. Those features affect asset-liability management and the ability to fund follow-ons. They vary by fund. Public statistics can describe populations, but institution-specific liquidity requires the fund documents and current portfolio data.

A lender underwriting an unfunded delayed draw should model both borrower utilisation and fund funding capacity. A borrower should confirm that the committed lender entity has authority and capacity under the financing documents.

Source note (retrieved 12 July 2026): PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>; PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>; PS11: EUR-Lex, Directive 2011/61/EU, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32011L0061>.

10.8 Comparison with syndicated loans and bonds

Hold transaction facts constant and compare certainty, amount, cash cost, maturity, amortisation, covenants, incremental capacity, prepayment, transfers, voting, disclosure and execution timetable. A broadly distributed instrument can provide market liquidity and scale; a direct facility can provide concentrated negotiation and tailored funding. Neither advantage is automatic.

The decision should include a fallback plan. If a syndicated execution weakens, identify flex and underwriter exposure. If a direct lender reduces capacity, identify alternative capital and timing. Execution certainty is a scenario, not a slogan.

Source note (retrieved 12 July 2026): PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Fictional teaching exercise: delayed-draw economics

Fictional teaching facts. A EUR 300 million term loan funds at closing and a EUR 100 million delayed-draw facility is available for two years. The funded margin is 6% over a 3% benchmark, the undrawn fee is 2%, and the draw is expected at month twelve. Ignore compounding and fees not stated. Calculate first-year cash interest and undrawn fee, then recalculate if EUR 50 million is drawn at month six and the remainder stays undrawn. Show the timing convention used.

Add a covenant that permits the acquisition funded by the draw only if pro forma leverage is at or below a fictional threshold. List the EBITDA, debt, cash and acquisition assumptions required at the test date. Do not conclude availability from commitment amount alone.

Fictional teaching exercise: concentrated amendment

Three lenders hold 50%, 30% and 20% of a fictional facility. The borrower seeks covenant relief and EUR 40 million of new priority money. Draft an analytical matrix showing each lender's existing claim, new-money participation, proposed priority, amendment vote and recovery under base and downside values. The exercise does not assign a legal threshold; insert the threshold only after reading the governing agreement.

Practitioner review sequence

Define the private-credit perimeter, facility, lender group, date and use of proceeds before making a market statement.

Compare total cash cost, certainty, flexibility, transfers, voting and downside rather than headline spread alone.

Model unfunded commitments at both borrower and lender level, and track monitoring data into the downside case.

Treat unitranche, first-out and last-out priority as document questions, not product definitions.

Legal, tax, regulatory and accounting boundary

Public sources support aggregate context only. Instrument priority, fund authority, regulatory treatment, transfer restrictions, voting and enforcement depend on specific documents and qualified advisers. No institution-specific capital, accounting or tax conclusion is made.

Primary-source map

Source note (retrieved 12 July 2026): PS04: SEC, Private Fund Statistics, <https://www.sec.gov/data-research/statistics-data-visualizations/private-fund-statistics>; PS05: IMF, April 2024 Global Financial Stability Report, Chapter 2, <https://www.imf.org/en/-/media/files/publications/gfsr/2024/april/english/ch2.pdf>; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS11: EUR-Lex, Directive 2011/61/EU, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32011L0061>.

CLO Mechanics and Impact on Leveraged Finance

A cash-flow CLO is a securitisation vehicle that acquires a portfolio of loans and issues liabilities with different payment priorities, together with a subordinated position. A manager selects and administers assets within the governing documents. The vehicle's indenture and related agreements, not the CLO label, determine eligibility, tests, cash diversion and voting authority.

This chapter explains the analytical logic through fully specified fictional tests. It does not reproduce a proprietary indenture, rating model, manager record or market dataset. The Federal Reserve materials and public regulations provide bounded structure and regulatory context.

11.1 The vehicle and its capital structure

The CLO vehicle owns loan assets and finances them with debt tranches and subordinated capital. Cash from assets is applied through priority-of-payments rules. Senior liabilities are paid before junior liabilities and residual distributions, subject to the governing documents. The manager's authority, reinvestment period, trading limits and reporting are defined contractually.

The analyst should draw three maps: assets by borrower and industry, liabilities by priority and coupon, and accounts by permitted use. Then reconcile asset principal, liability principal, cash and any adjustments used by the tests.

Source note (retrieved 12 July 2026): PS14: Federal Reserve, CLOs in the Financial Accounts of the United States, <https://www.federalreserve.gov/econres/notes/feds-notes/collateralized-loan-obligations-in-the-financial-accounts-of-the-united-states-20190920.html>; PS15: Federal Reserve Regulations, 12 CFR 244.9, <https://www.federalreserve.gov/frs/regulations/section-2449-open-market-clos.htm>.

11.2 Interest and principal waterfalls

Interest proceeds generally pay expenses and liability interest in an ordered sequence before residual amounts, while principal proceeds follow their own rules for reinvestment or liability repayment. Exact categories and switches depend on the indenture. A missed or deferred junior payment is not necessarily the same as a payment default on a senior class.

Model timing carefully. Loan benchmarks, floors, margins, payment dates and defaults affect asset interest. CLO liabilities have their own benchmarks, spreads and dates. Basis mismatch and non-payment can reduce excess spread even when par value is unchanged.

Source note (retrieved 12 July 2026): PS14: Federal Reserve, CLOs in the Financial Accounts of the United States, <https://www.federalreserve.gov/econres/notes/feds-notes/collateralized-loan-obligations-in-the-financial-accounts-of-the-united-states-20190920.html>.

11.3 Overcollateralisation tests

An OC test compares an indenture-defined numerator based on collateral principal with the outstanding amount of specified liability classes in the denominator. The numerator may apply haircuts or exclusions. If the ratio falls below its threshold, the waterfall can divert cash from junior positions to repay senior debt or acquire eligible assets, as the indenture provides.

Do not calculate OC from accounting asset value unless the document says so. Record each asset's par, default status, discount treatment, CCC treatment and other adjustment. Reconcile the test numerator to the collateral report.

Source note (retrieved 12 July 2026): PS14: Federal Reserve, CLOs in the Financial Accounts of the United States, <https://www.federalreserve.gov/econres/notes/feds-notes/collateralized-loan-obligations-in-the-financial-accounts-of-the-united-states-20190920.html>; PS15: Federal Reserve Regulations, 12 CFR 244.9, <https://www.federalreserve.gov/frs/regulations/section-2449-open-market-clos.htm>.

11.4 Interest-coverage tests

An IC test compares defined interest proceeds with specified expenses and liability interest. The calculation depends on payment period, available proceeds, deferred amounts and the classes included. A strong current ratio can weaken rapidly if loans stop paying or liability benchmarks reset before asset income.

A stress model should reduce asset interest for defaults and non-accruals, vary benchmark basis and include senior fees. It should show which class first fails its threshold and how the resulting diversion changes later periods.

Source note (retrieved 12 July 2026): PS14: Federal Reserve, CLOs in the Financial Accounts of the United States, <https://www.federalreserve.gov/econres/notes/feds-notes/collateralized-loan-obligations-in-the-financial-accounts-of-the-united-states-20190920.html>.

11.5 Weighted average life and portfolio limits

Weighted average life measures contractual principal timing under the indenture's method and assumptions. A limit can constrain purchases of longer-dated loans as the transaction seasons. Other portfolio criteria can address maturity, diversity, ratings, concentration, collateral type and minimum spread.

A manager considering an amendment or extension should test the loan after the change, not rely on its original maturity. Eligibility and concentration are transaction-specific. An amendment that helps the borrower can reduce CLO flexibility even when current cash interest increases.

Source note (retrieved 12 July 2026): PS14: Federal Reserve, CLOs in the Financial Accounts of the United States, <https://www.federalreserve.gov/econres/notes/feds-notes/collateralized-loan-obligations-in-the-financial-accounts-of-the-united-states-20190920.html>; PS15: Federal Reserve Regulations, 12 CFR 244.9, <https://www.federalreserve.gov/frs/regulations/section-2449-open-market-clos.htm>.

11.6 CCC and defaulted assets

Indentures can apply special treatment to lower-rated or defaulted assets, including limits, valuation adjustments or haircuts. The exact definition and consequence must be read from the governing document. It is unsafe to claim that a downgrade automatically forces a sale.

The manager may compare holding, selling, amending and participating in new money subject to authority and tests. The analyst should show price, par impact, interest, recovery and test effect for each option without turning the calculation into an investment recommendation.

Source note (retrieved 12 July 2026): PS14: Federal Reserve, CLOs in the Financial Accounts of the United States, <https://www.federalreserve.gov/econres/notes/feds-notes/collateralized-loan-obligations-in-the-financial-accounts-of-the-united-states-20190920.html>; PS15: Federal Reserve Regulations, 12 CFR 244.9, <https://www.federalreserve.gov/frs/regulations/section-2449-open-market-clos.htm>.

11.7 Reinvestment and amendments

During a reinvestment period, principal proceeds may be reinvested if the indenture's conditions are met. After that period, reinvestment can be more limited. Loan amendments, extensions, exchanges and new-money opportunities should be tested against eligibility, maturity, concentration, par and manager authority.

Voting follows the CLO's ownership and decision framework. The manager may have authority to consent within limits, but liability holders and other parties can have rights under the indenture. No universal voting rule should be inferred.

Source note (retrieved 12 July 2026): PS14: Federal Reserve, CLOs in the Financial Accounts of the United States, <https://www.federalreserve.gov/econres/notes/feds-notes/collateralized-loan-obligations-in-the-financial-accounts-of-the-united-states-20190920.html>; PS15: Federal Reserve Regulations, 12 CFR 244.9, <https://www.federalreserve.gov/frs/regulations/section-2449-open-market-clos.htm>.

11.8 EU and U.S. regulatory perimeter

EU securitisation rules address definitions, due diligence, transparency and risk retention within their scope. U.S. regulations include provisions concerning open-market CLO definitions in the cited source. Application depends on structure, parties and date. The text should be reviewed against current law before use.

Regulatory rules should not be collapsed into an automatic asset-sale or capital conclusion. Record the regulated entity, rule, effective date, exposure and required action. Institution-specific prudential treatment remains specialist work.

Source note (retrieved 12 July 2026): PS13: EUR-Lex, Regulation (EU) 2017/2402, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32017R2402>; PS15: Federal Reserve Regulations, 12 CFR 244.9, <https://www.federalreserve.gov/frs/regulations/section-2449-open-market-clos.htm>.

Fictional teaching exercise: OC diversion

Fictional indenture rules. Adjusted collateral principal is EUR 480 million. Class A debt is EUR 300 million and Class B debt is EUR 100 million. The Class B OC ratio is adjusted collateral divided by Class A plus Class B, with a 118% threshold. The opening ratio is 120%. A EUR 20 million asset defaults and receives a 50% par haircut, reducing adjusted collateral by EUR 10 million. The ratio becomes 117.5%, so the fictional test fails. Under the stated exercise rule, EUR 8 million of interest proceeds is diverted to repay Class A. Recalculate the ratio after repayment: EUR 470 million divided by EUR 392 million equals approximately 119.9%.

Explain why the calculation cannot be transferred to another CLO without its definitions, thresholds, haircut rules and waterfall.

Fictional teaching exercise: IC and maturity extension

Fictional rules. Quarterly asset interest is EUR 9.0 million, senior expenses are EUR 0.5 million, Class A interest is EUR 4.0 million and Class B interest is EUR 2.0 million. The Class B IC ratio is available interest divided by Class A plus Class B interest, with a 130% threshold. Available interest is EUR 8.5 million, so the opening IC ratio is $8.5 / 6.0 = 141.7\%$ and the test passes. If EUR 1.2 million of asset interest becomes non-accrual, available interest falls to EUR 7.3 million and the ratio becomes $7.3 / 6.0 = 121.7\%$, so the test fails.

For the separate WAL exercise, assume total portfolio par of EUR 100 million, an opening WAL of 4.20 years, a maximum permitted WAL of 4.50 years and no other change in par or maturity. Extending a EUR 15 million loan by

two years adds $15 / 100 \times 2 = 0.30$ years. Revised WAL is 4.50 years. Under a rule requiring WAL not to exceed 4.50 years, the extension does not breach the limit but leaves no headroom.

Practitioner review sequence

Read the indenture definitions before calculating asset par, OC, IC, WAL or concentration.

Separate interest and principal waterfalls and model the cash diversion created by each failed test.

Test amendments and extensions for eligibility, par, maturity, concentration and manager authority.

State EU or U.S. regulatory scope, entity and effective date; avoid automatic sale or capital conclusions.

Legal, tax, regulatory and accounting boundary

CLO and securitisation counsel must review entity structure, indenture authority, test consequences, voting and EU or U.S. regulatory treatment. All numerical tests here are fictional and cannot substitute for an indenture calculation.

Primary-source map

Source note (retrieved 12 July 2026): PS13: EUR-Lex, Regulation (EU) 2017/2402, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32017R2402>; PS14: Federal Reserve, CLOs in the Financial Accounts of the United States, <https://www.federalreserve.gov/econres/notes/feds-notes/collateralized-loan-obligations-in-the-financial-accounts-of-the-united-states-20190920.html>; PS15: Federal Reserve Regulations, 12 CFR 244.9, <https://www.federalreserve.gov/frs/regulations/section-2449-open-market-clos.htm>.

PART III

COVENANTS

- 12 Reading a Credit Agreement
 - 13 European and U.S. Documentation - A Bounded Comparison
 - 14 Covenant Fundamentals
 - 15 Financial Covenants – The Quantitative Guardrails
 - 16 EBITDA – The Number That Rules Everything
-

Reading a Credit Agreement

A credit agreement should be read as a linked operating system, not a collection of isolated clauses. Definitions feed calculations; calculations determine capacity; capacity permits actions; actions can trigger reporting, prepayment, default or voting. A reliable reading method therefore moves repeatedly between the operative provision, every defined term it uses, related exceptions and the transaction facts being tested.

The method below is independently organised around evidence and reproducibility. It uses the public MeridianLink credit agreement as a worked document. It does not reproduce a proprietary clause taxonomy, model form or paid commentary. Every conclusion should identify the instrument, section, defined terms, assumptions and unresolved legal question.

12.1 Establish document authority

Begin with the executed agreement and all amendments, joinders, restatements and schedules. Record execution date, parties, governing law, effective date and document hierarchy. Confirm that the version is complete and that later amendments have been integrated or tracked. A search result or unsigned draft is not an authoritative instrument.

Create a document register that links the credit agreement to security documents, guarantees, intercreditor agreements, fee letters and material acquisition documents. Record which document controls if terms conflict. Keep public examples separate from the live transaction file.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

12.2 Build the party and facility map

Identify borrowers, guarantors, lenders, issuing banks, swingline lenders, administrative agent and collateral agent as defined in the agreement. Then list each facility, commitment, currency, availability period, purpose, maturity and amortisation. Link every facility to the entities that owe or guarantee it.

The party map prevents a common error: reading a consolidated covenant while assuming every entity is an obligor. Mark restricted and unrestricted subsidiaries, excluded subsidiaries and any entity whose assets or EBITDA are outside the guarantee or collateral perimeter.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

12.3 Read definitions as executable logic

A defined term should be rewritten as a calculation or decision tree. For Consolidated EBITDA, identify starting line, additions, deductions, caps, time periods, pro forma rules and discretion. For Indebtedness, identify included obligations, exclusions, guarantees, contingent claims and double-counting rules. Do not summarise a long definition with one adjective.

Build a dependency chain. If a covenant uses a leverage ratio, the chain may include debt, cash, EBITDA, test date, pro forma effect and transaction conditions. Record each cross-reference. A change to one component can affect

debt capacity, restricted payments, investments and pricing simultaneously.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

12.4 Convert an operative covenant into a test

For any proposed action, begin with the prohibition or requirement. State the action in plain facts: amount, entity, date, purpose, recipient and consideration. Then test the general rule, each relevant exception, any ratio or basket, conditions, reclassification and post-transaction consequences. Stop if a required fact is missing.

A basket ledger should record original amount, grower amount, prior uses, repayments, reclassification and remaining capacity. If the agreement permits reliance on more than one basket, record the allocation. A result without that audit trail cannot be reproduced later.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

12.5 Work through calculations and test dates

The same transaction can produce different capacity depending on measurement date, pro forma period, currency conversion and whether debt is treated as drawn. Record the test date before calculating. Identify which financial statements and certificates govern, and whether later events can change the result.

Show every input and source. If an adjustment depends on management certification or a reasonable-identification standard, record the evidence and approval. If the document grants discretion, describe the decision standard without assuming the discretion is unlimited.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

12.6 Follow money and collateral

Debt analysis should follow proceeds, repayment and collateral. For an incremental loan, record borrower, use, maturity, ranking, guarantors, collateral, MFN treatment and intercreditor accession. For an asset sale, record seller, asset, consideration, cash percentage, proceeds, reinvestment period and prepayment requirement.

Security and guarantee conclusions require the related documents. The credit agreement may describe obligations and collateral documents, but perfection, priority, release and enforcement can depend on separate instruments and law. Mark those interfaces for counsel.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS18: Delaware Code, Title 6, Article 9, <https://delcode.delaware.gov/title6/c009/index.html>.

12.7 Voting, amendments and lender identity

Locate the general amendment threshold and every separately protected matter. Identify the lender denominator, excluded votes, defaulting-lender treatment, affected classes and individual consent rights. Then identify who can sign, direct the agent and evidence ownership.

Do not quote a percentage without the question it answers. A majority may amend one covenant but not reduce principal, extend a payment date, release collateral or change pro rata sharing. The threshold and protected rights are document-specific.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

12.8 Defaults, notice and remedies

For each event of default, record trigger, materiality threshold, grace or cure period, notice, knowledge qualifier and affected entity. Distinguish an event that exists automatically from one that requires notice or expiration of time. Distinguish default from acceleration and acceleration from enforcement.

Build a remedy sequence: who determines or declares, who directs, what percentage is required, what standstill applies, what can be rescinded and how proceeds are distributed. Refer to intercreditor and insolvency analysis rather than assuming the credit agreement alone answers the sequence.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

12.9 Produce a reproducible reading record

A strong memo has five fields for every conclusion: fact pattern, operative section, defined-term chain, calculation and caveat. Attach the capacity ledger and source extracts. Separate document fact from commercial interpretation and legal advice.

Use uncertainty productively. If a clause supports two readings, state both, show the economic consequence and identify the issue for counsel or the agent. A confident unsupported answer is less useful than a bounded question with the right evidence.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

Document-reading exercise: proposed acquisition

Fictional teaching facts. A restricted subsidiary proposes a EUR 60 million acquisition funded with EUR 20 million of cash and EUR 40 million of incremental debt. The target contributes EUR 8 million of EBITDA before permitted pro forma adjustments. Prepare a reading record using the cited agreement: identify investment capacity, debt capacity, lien capacity, incremental conditions, leverage calculation, guarantee and collateral requirements, MFN treatment and any restricted-payment interaction. Every field must cite a section or be marked unresolved.

Then change one fact: the target will become an unrestricted subsidiary. Repeat the analysis and identify how the cash-flow, guarantee and covenant perimeter changes. Do not assume that investment permission creates debt or lien permission.

Document-reading exercise: consent request

A fictional borrower seeks to extend one term-loan class by two years and increase its margin, while non-extending lenders retain stated principal and maturity. Build the amendment analysis from the general threshold, class voting, extension provisions and protected rights. Record the affected lender denominator and evidence required from electing lenders. Leave the legal conclusion open for counsel.

Practitioner review sequence

Confirm executed document authority, amendments, parties, facilities and hierarchy before analysis.

Translate definitions into inputs and formulas, and trace every cross-reference used by the operative clause.

State facts, test date, basket or ratio, conditions, reclassification and remaining capacity.

Separate covenant permission from guarantee, collateral, intercreditor, voting and insolvency consequences.

Write a reproducible record with section citations, calculations and unresolved legal questions.

Legal, tax, regulatory and accounting boundary

The reading method identifies issues and document logic; it does not provide a legal opinion. English or European and U.S. finance counsel must validate interpretations, discretion, voting, agency, collateral, guarantee and remedy conclusions against the executed document set.

Primary-source map

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS18: Delaware Code, Title 6, Article 9, <https://delcode.delaware.gov/title6/c009/index.html>.

European and U.S. Documentation – A Bounded Comparison

There is no single European credit agreement and no single U.S. credit agreement. Documentation differs by governing law, borrower jurisdiction, instrument, sponsor, lender group, transaction and date. This chapter compares defined legal and documentary questions using selected public sources. It avoids claims that one side of the Atlantic always follows a particular result.

A useful comparison has four coordinates: governing law, obligor jurisdiction, selected instrument and proposition. For example, a New York-law agreement with English guarantors can require U.S. contract analysis and English corporate or insolvency analysis. Geographic labels are orientation; the legal map follows entities, assets and documents.

13.1 Start with authority and jurisdiction

Identify governing law for the credit agreement, guarantees, security documents and intercreditor agreement. Identify incorporation and asset location for every material obligor and grantor. Record court jurisdiction, service of process and any arbitration provision. Those fields determine which legal questions must be reviewed and by whom.

The ECB leveraged-transactions guidance provides supervisory context for relevant institutions in its scope. The U.S. interagency guidance provides a separate supervisory framework. Neither source dictates the commercial terms of every agreement, and neither should be treated as substantive contract law.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

13.2 Acquisition financing and funding certainty

UK public-acquisition financing must be analysed with the Takeover Code requirements applicable to the firm offer and cash confirmation. The commitment package should align funding conditions and drawstops with the acquisition timetable and certainty requirements. Private acquisitions and U.S. transactions use their own merger and financing documents.

Compare the actual conditionality package rather than the phrase certain funds. Record specified representations, acquisition-document conditions, marketing requirements, expiry and termination. Then test whether a financing condition can fail when purchase consideration becomes due.

Source note (retrieved 12 July 2026): PS08: UK Takeover Panel, Takeover Code Rule 2.7, <https://code.thetakeoverpanel.org.uk/tp/rules/rule-2/rule-2-7.html>; PS09: UK Takeover Panel, Takeover Code Rule 24.8, <https://code.thetakeoverpanel.org.uk/tp/rules/rule-24/rule-24-8.html>.

13.3 Borrower, guarantor and restricted-group perimeter

The selected U.S. public credit agreement defines borrowers, guarantors, restricted subsidiaries and excluded subsidiaries under its own terms. A European structure may include multiple jurisdictions and limitations driven by corporate benefit, financial assistance, capital maintenance, tax, works councils or local-law requirements. Those limits must be set out entity by entity.

Prepare a coverage schedule showing EBITDA, assets and cash by guarantor, non-guarantor and unrestricted entity. Add the legal reason for each exclusion and any post-closing accession obligation. Do not state that all material subsidiaries guarantee without reconciling the schedule.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS16: UK Companies Act 2006, section 678, <https://www.legislation.gov.uk/ukpga/2006/46/section/678>.

13.4 Financial-assistance questions

Section 678 of the UK Companies Act 2006 contains a public-company financial-assistance prohibition within its statutory scope. Application, exceptions and transaction steps require English legal advice. Other jurisdictions have different rules. The existence of acquisition debt alone does not provide a universal answer.

The closing checklist should identify target type, acquisition structure, proposed guarantees or security, timing and any required procedure. The financial model should not assume target assets support acquisition debt until counsel confirms the permitted structure.

Source note (retrieved 12 July 2026): PS16: UK Companies Act 2006, section 678, <https://www.legislation.gov.uk/ukpga/2006/46/section/678>.

13.5 Security and perfection

A U.S. secured transaction can involve Article 9 security interests together with mortgages, intellectual-property filings, control agreements and other asset-specific steps. European structures can require separate local-law security documents, registrations, notices, translations, corporate approvals and perfection steps. The comparison must be asset and jurisdiction specific.

Create a collateral matrix with grantor, asset, document, governing law, perfection step, deadline, priority evidence and release condition. The description in the credit agreement is only one part of that record.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS18: Delaware Code, Title 6, Article 9, <https://delcode.delaware.gov/title6/c009/index.html>.

13.6 Covenant architecture

The selected public U.S. agreement and indenture demonstrate detailed definition, basket and ratio systems. European leveraged agreements can also use negotiated baskets, ratios, financial covenants and sponsor protections. A reliable comparison asks the same questions of each instrument instead of assuming one regional template.

Compare restricted-group perimeter, EBITDA definition, debt and lien capacity, investments, restricted payments, asset sales, acquisitions, incremental debt, financial tests, cure rights, suspension and reporting. Record exact section references and test dates.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

13.7 Voting, classes and protected rights

General amendment thresholds, affected-class rules and individual protected rights vary by instrument. A loan agreement can have revolving, term and extension classes; a bond indenture has its own holder and series framework. Intercreditor agreements may add separate creditor-class decisions.

For each proposal, identify the provision changed, affected class, denominator, excluded votes, individual rights and execution channel. Do not apply a U.S. agreement threshold to an English-law agreement or a loan threshold to a bond.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

13.8 Defaults, acceleration and enforcement control

Compare the documents' payment, covenant, cross-default, judgment and insolvency triggers, including thresholds, notice and cure. Then separate acceleration from enforcement. Security-agent or collateral-agent authority, creditor directions, standstills and proceeds waterfalls may sit in other documents.

A cross-border group can face different insolvency proceedings and recognition questions by entity. The credit memo should state which law and proceeding it assumes and route legal consequences to qualified counsel.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS17: UK Companies Act 2006, Part 26A, <https://www.legislation.gov.uk/ukpga/2006/46/part/26A>; PS19: 11 U.S.C. section 303, <https://uscode.house.gov/view.xhtml?edition=prelim&hl=false&num=0&path=%2Fprelim%40title11&req=granuleid%3AUSC-prelim-title11-section303>; PS20: 11 U.S.C. section 362, <https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section362%28d%29>.

13.9 U.S. Chapter 11, schemes and restructuring plans

U.S. Chapter 11 and English schemes or Part 26A restructuring plans are distinct legal procedures. Section 362 of the U.S. Bankruptcy Code provides automatic-stay text within its scope; section 303 addresses involuntary cases. Part 26A of the Companies Act provides a statutory restructuring-plan framework. Outcomes depend on facts, classes, jurisdiction and court decisions.

A finance chapter should not announce which process will bind a creditor or deliver a specific priority result. It can identify the capital structure, governing documents, entity centre of main interests or jurisdictional facts, maturity, liquidity and creditor classes for counsel to analyse.

Source note (retrieved 12 July 2026): PS17: UK Companies Act 2006, Part 26A, <https://www.legislation.gov.uk/ukpga/2006/46/part/26A>; PS19: 11 U.S.C. section 303,

[https://uscode.house.gov/view.xhtml?](https://uscode.house.gov/view.xhtml?edition=prelim&hl=false&num=0&path=%2Fprelim%40title11&req=granuleid%3AUSC-prelim-title11-section303)

[edition=prelim&hl=false&num=0&path=%2Fprelim%40title11&req=granuleid%3AUSC-prelim-title11-section303;](https://uscode.house.gov/view.xhtml?edition=prelim&hl=false&num=0&path=%2Fprelim%40title11&req=granuleid%3AUSC-prelim-title11-section303)
PS20: 11 U.S.C. section 362, https://uscode.house.gov/view.xhtml?

[edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section362%28d%29](https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section362%28d%29).

13.10 Intercreditor structure

Intercreditor agreements can address ranking, payment blockage, turnover, enforcement control, standstill, releases, hedging and proceeds. The selected credit agreement and indenture may refer to intercreditor arrangements but do not establish a universal European or U.S. outcome.

Draw the creditor groups and identify which document binds each. For a proposed refinancing or priority change, test accession, voting, release and enforcement provisions. Keep contractual priority separate from insolvency-law priority.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement,

<https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; *PS07:*

SEC EDGAR, Carnival 2023 secured-notes indenture,

<https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Cross-border document matrix

Fictional teaching facts. A Luxembourg parent borrows under a New York-law credit agreement. Operating subsidiaries are incorporated in England, Germany and Delaware. The English and Delaware entities are proposed guarantors; material receivables are located in all three operating jurisdictions. Build a matrix for agreement law, guarantor law, security law, perfection step, corporate approval, financial-assistance question, insolvency procedure and required counsel. Do not fill a cell with a regional generalisation.

Add a proposed acquisition of a UK public company. Create a separate funding-certainty workstream tied to the Takeover Code sources, commitment conditions and cash confirmation. Explain why the acquisition workstream does not answer local security or guarantee questions.

Restructuring perimeter exercise

Using the same fictional group, assume liquidity expires in eight weeks and creditors sit at both parent and operating entities. Prepare a facts-only restructuring map: entity, debt, guarantee, collateral, governing law, maturity, cash, creditor class and possible statutory forum. Do not predict recognition, cramdown, stay or priority. List the legal questions for U.S., English, German and Luxembourg counsel.

Practitioner review sequence

For every comparison, name governing law, obligor jurisdiction, selected instrument and proposition.

Keep supervisory guidance, contract terms, corporate law, security law and insolvency law in separate analytical lanes.

Build guarantor, collateral, voting, intercreditor and proceeding matrices entity by entity.

Use statutory and public document sources at the point of use; route application and enforceability to qualified local counsel.

Legal, tax, regulatory and accounting boundary

Every jurisdictional comparison requires qualified review. English or European and U.S. finance and restructuring counsel should advise on guarantees, financial assistance, security, perfection, covenants, voting, defaults, intercreditor terms, Chapter 11, schemes and Part 26A plans as applicable to the facts.

Primary-source map

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS08: UK Takeover Panel, Takeover Code Rule 2.7, <https://code.thetakeoverpanel.org.uk/tp/rules/rule-2/rule-2-7.html>; PS09: UK Takeover Panel, Takeover Code Rule 24.8, <https://code.thetakeoverpanel.org.uk/tp/rules/rule-24/rule-24-8.html>; PS16: UK Companies Act 2006, section 678, <https://www.legislation.gov.uk/ukpga/2006/46/section/678>; PS17: UK Companies Act 2006, Part 26A, <https://www.legislation.gov.uk/ukpga/2006/46/part/26A>; PS18: Delaware Code, Title 6, Article 9, <https://delcode.delaware.gov/title6/c009/index.html>; PS19: 11 U.S.C. section 303, <https://uscode.house.gov/view.xhtml?edition=prelim&hl=false&num=0&path=%2Fprelim%40title11&req=granuleid%3AUSC-prelim-title11-section303>; PS20: 11 U.S.C. section 362, <https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section362%28d%29>.

Covenant Fundamentals

A covenant is a contractual promise, restriction, condition or information obligation. Its practical strength depends on the entities covered, defined terms, exceptions, calculation rules, testing time and consequence. This chapter builds a fresh covenant-reading framework from the selected public credit agreement and indenture rather than reproducing a private taxonomy or specimen wording.

The central discipline is to convert each covenant into an executable test. State the proposed action, identify the covered entity, locate the rule, trace definitions, calculate capacity, apply conditions and record the remaining headroom. A covenant label without that chain is not an analysis.

14.1 Affirmative and information obligations

Affirmative covenants can require financial reporting, notices, payment of obligations, maintenance of existence, insurance, books and access, subject to the document's qualifications. Information covenants provide the data needed to monitor credit and calculate other provisions.

Build an obligation calendar with deliverable, period, due date, recipient, certificate, grace period and responsible owner. Late delivery can matter even when financial performance is sound. The consequence must be read from the event-of-default provisions.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

14.2 Negative covenants

Negative covenants can restrict debt, liens, investments, restricted payments, asset sales, mergers, affiliate transactions and other actions. The general prohibition is only the beginning. Exceptions can be fixed baskets, grower baskets, ratio-based capacity, ordinary-course permissions or transaction-specific carve-outs.

Read related covenants together. Debt may require a lien; an investment may also be a restricted payment; an asset transfer may change the restricted group; an acquisition may require debt, liens and investment capacity. Permission under one section does not create permission under another.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

14.3 Maintenance and incurrence tests

A maintenance test is measured periodically or upon a stated condition regardless of whether the borrower takes a new action. An incurrence test is triggered by a proposed action. The exact testing event and consequence come from the document. A springing financial covenant can apply only when a usage or other condition is met.

For every test, record numerator, denominator, test date, pro forma period, permitted adjustments, cure, equity contribution treatment and consequence. Avoid describing a loan or bond as covenant-lite without specifying which maintenance test is absent and which incurrence controls remain.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

14.4 Restricted group and guarantor coverage

Covenants usually operate over a defined group. Unrestricted subsidiaries or excluded entities may sit outside some restrictions and guarantees. The perimeter can change through designation, acquisition, disposal or reorganisation. The analyst should reconcile consolidated financials to the covenant group.

Maintain a group schedule with ownership, EBITDA, assets, debt, guarantees, collateral and designation capacity. A transaction that moves value outside the restricted group can affect both cash available for debt service and downside recovery.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

14.5 Fixed, grower and ratio capacity

A fixed basket states an amount. A grower can scale with a defined financial measure. Ratio capacity depends on satisfying a specified ratio. Those forms can coexist and may be usable in an order chosen by the borrower. Record currency conversion, test date and whether capacity can be reclassified.

A grower is not simply a percentage of reported EBITDA unless the covenant definition says so. A ratio test is not complete until debt, cash, EBITDA, pro forma adjustments and transaction assumptions are reconciled. Show both gross and remaining capacity.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

14.6 Builder amounts and reclassification

A builder amount can accumulate from retained earnings, excess cash flow, equity contributions or other defined sources and be reduced by uses. The formula is document-specific. Reclassification can allow a transaction initially allocated to one basket to be moved to another after conditions are met, restoring capacity.

Create a roll-forward with opening amount, additions, deductions, uses, reclassifications and closing amount. Preserve evidence for every entry. Without a ledger, later capacity analysis can double count restored or consumed amounts.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07:

SEC EDGAR, Carnival 2023 secured-notes indenture,
<https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

14.7 Conditions and no-default tests

Capacity can be subject to no-default, pro forma compliance, purpose, maturity, ranking, guarantor or other conditions. A basket amount alone does not establish permission. Test conditions at the time and on the basis specified by the agreement.

Record whether a condition applies to use, designation, reclassification or only ratio capacity. A default can block one action while leaving another exception available. The conclusion should cite the exact clause.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement,
<https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture,
<https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

14.8 Suspension, fall-away and reinstatement

Some instruments can suspend or modify covenants when stated ratings or other conditions are met, and can reinstate them if conditions cease. The effect on transactions completed during suspension depends on the indenture. A springing test can similarly turn on or off with a stated trigger.

The monitoring file should record trigger, evidence, effective date, covenants affected, grandfathering and reinstatement. Do not state that covenants disappear permanently without the operative text.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement,
<https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture,
<https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

14.9 Breach, cure, waiver and default

A covenant breach may have a cure period, notice requirement or equity-cure mechanism, and may become an event of default only under the stated conditions. Waiver requires the applicable consent and can be limited in scope. Cure of one financial test may not cure a separate payment or reporting failure.

The response sequence is factual: identify breach date, knowledge, notice, grace, cure action, lender consent and continuing effect. Legal consequences and reservation of rights require counsel.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement,
<https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture,
<https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Fictional teaching exercise: covenant capacity stack

Fictional rules. A borrower may incur debt under a EUR 40 million fixed basket, a grower equal to the greater of EUR 25 million and 20% of Covenant EBITDA, and unlimited ratio debt if pro forma net leverage is no greater than 4.5x. Covenant EBITDA is EUR 160 million, net debt before the transaction is EUR 680 million and the borrower proposes EUR 70 million of new debt. The grower is EUR 32 million. If the borrower first allocates EUR 40 million to the fixed basket, it needs EUR 30 million elsewhere. Pro forma leverage for the full new debt is 4.6875x, so the

ratio route is unavailable under the stated rule. The grower can cover EUR 30 million, leaving EUR 2 million of grower capacity.

Now reduce Covenant EBITDA to EUR 140 million and assume EUR 10 million of the fixed basket was used earlier. Recalculate available capacity and identify the evidence needed for each input.

Fictional teaching exercise: connected covenants

A restricted subsidiary wants to acquire an asset for EUR 50 million, funded by EUR 35 million of new secured debt and EUR 15 million of cash. Prepare separate tests for debt, liens, investments or acquisitions, restricted payments if relevant, asset transfers and pro forma financial covenants. The exercise is complete only when every required permission is identified; one available basket cannot answer all sections.

Practitioner review sequence

State the action, entity, amount, date and purpose before reading the covenant.

Trace the prohibition, exceptions, definitions, ratio or basket, conditions and test date.

Maintain restricted-group, guarantor and capacity ledgers, including reclassification and builder roll-forwards.

Read related covenants together and separate breach, cure, waiver, default and remedy.

Legal, tax, regulatory and accounting boundary

Loan and bond counsel must verify maintenance and incurrence tests, restricted-group and guarantor scope, springing conditions, builder and reclassification mechanics, suspension, fall-away, cure and default consequences against each selected instrument.

Primary-source map

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Financial Covenants — The Quantitative Guardrails

A financial covenant converts selected accounting and contractual definitions into a periodic or transaction-triggered test. It is not simply a ratio printed on a compliance certificate. The test depends on the covered group, measurement period, debt, cash, EBITDA, permitted adjustments, testing date, cure rights and consequence.

This chapter uses fictional calculations and the selected public credit agreement for document mechanics. It does not rely on named transaction stories, uncited market thresholds or third-party covenant tables.

15.1 Define the covenant perimeter

Identify which borrower and subsidiaries are included in consolidated debt and EBITDA, and which cash is netted. Restricted and unrestricted subsidiaries, excluded subsidiaries, joint ventures and non-guarantors can affect the perimeter differently under the agreement. Reconcile the covenant group to reported financial statements.

Create a perimeter bridge for EBITDA, assets, debt and cash. Any amount outside the covenant group should be separately visible. A consolidated headline ratio can conceal debt at excluded entities or earnings unavailable to the borrower.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

15.2 Net leverage ratio

A net leverage ratio generally divides a defined debt measure net of permitted cash by Covenant EBITDA. The agreement determines which obligations count, how cash is limited, whether letters of credit or hedges are included and how pro forma transactions are treated. The ratio name does not answer those questions.

Show numerator and denominator separately. For debt, list each instrument and adjustment. For cash, identify entity, currency, restriction and cap. For EBITDA, show the full reconciliation. The final ratio should be reproducible to the smallest material input.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

15.3 Fixed-charge and interest coverage

A coverage ratio compares a defined earnings or cash-flow measure with defined charges. Fixed charges may include cash interest, scheduled rent, preferred dividends or other items depending on the document. Interest coverage may use cash interest, total interest or another definition.

Do not mix numerator and denominator periods. Record whether charges are historical, pro forma or annualised and whether capitalised or non-cash amounts are included. A coverage ratio can improve mechanically when excluded interest grows, so the definition requires the same attention as the result.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

15.4 Maintenance, incurrence and springing tests

A maintenance covenant is tested on scheduled dates or another stated basis. An incurrence test applies when a defined action is proposed. A springing maintenance covenant becomes active only when a stated condition, such as revolving usage, is met. The trigger and excluded usage must be calculated exactly.

Build a calendar showing test date, financial period, certificate deadline and threshold. For a springing test, add daily or period-end usage data and any minimum-liquidity or letter-of-credit adjustments. Do not assume the covenant is inactive because the revolver was undrawn on an arbitrary date.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

15.5 Test dates and pro forma effect

A transaction may be tested when committed, incurred, consummated or another date defined by the agreement. Limited-condition transaction provisions can fix or separate testing times. Acquisitions, disposals, debt repayment and cost savings can receive pro forma effect under specified rules.

The calculation sheet should state the test date, reference period, transaction assumptions and later events included or excluded. If the conclusion changes under a different date, both results should be escalated before the transaction proceeds.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

15.6 Headroom and forecast control

Covenant headroom is the distance between the calculated ratio and threshold, but a ratio-point difference is not a cash buffer. Translate headroom into the EBITDA decline, debt increase or cash reduction that would consume it. Then compare with forecast volatility and reporting lag.

A twelve- to eighteen-month covenant forecast should integrate monthly liquidity, quarterly tests, acquisitions, debt draws and planned adjustments. Include a reverse stress that solves for the first breach. This helps management act before a certificate date.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf.

15.7 Equity cures and other cure mechanics

An equity cure can permit a contribution to affect a financial-covenant calculation under the agreement's conditions. The document determines timing, amount, permitted number of cures, whether debt must be repaid, how the contribution enters EBITDA or debt and its effect on other covenants.

The cure model should show the minimum contribution, cash receipt, revised ratio, remaining liquidity and future-period effect. Do not assume a sponsor will contribute or that cure proceeds create general basket capacity.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

15.8 Suspension, fall-away and reinstatement

A covenant can cease, suspend or change when stated conditions are met, and can later reinstate. Record the trigger, evidence, effective date, covenants affected, treatment of completed transactions and reinstatement rule. Ratings, leverage, revolver usage or other conditions should not be inferred.

Maintain a status log even while a test is suspended. Debt, EBITDA and basket use during the period can affect reinstatement and later capacity. Counsel should confirm whether completed actions are grandfathered.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

15.9 Breach, waiver and default sequence

A failed calculation must be connected to reporting, cure, notice, waiver and event-of-default provisions. Record who calculates, who certifies, when a breach exists, whether a cure period applies and what lender vote can waive or amend the covenant.

The credit response should update liquidity and stakeholder plans immediately, without assuming acceleration. Default, acceleration and enforcement are separate legal stages.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

Fictional teaching exercise: net leverage and headroom

Fictional rules. Covenant Debt is EUR 525 million. The borrower has EUR 60 million of cash, but only EUR 40 million may be netted. Covenant EBITDA is EUR 115 million. Net leverage is therefore $(525 - 40) / 115 = 4.217x$. The threshold is 4.50x. Solve for the EBITDA decline that consumes headroom with debt and nettable cash unchanged: required EBITDA is $485 / 4.50 = \text{EUR } 107.78 \text{ million}$, so a decline of EUR 7.22 million, or about 6.3%, reaches the threshold.

Now assume a EUR 25 million acquisition is funded with debt and contributes EUR 8 million of permitted pro forma EBITDA. Recalculate debt, EBITDA and ratio. State the test date and evidence required for the adjustment.

Fictional teaching exercise: springing covenant

A EUR 100 million revolver has EUR 35 million drawn and EUR 10 million of outstanding letters of credit. Fictional rules exclude EUR 5 million of cash-collateralised letters of credit and make the covenant spring when usage exceeds 35% of commitments. Calculate adjusted usage and determine whether the test applies. Then reduce commitments to EUR 90 million and repeat.

Fictional teaching exercise: equity cure

Assume the fictional covenant permits cure proceeds to increase EBITDA solely for the test, capped at the amount required to comply. Debt is EUR 400 million, nettable cash is EUR 20 million, reported Covenant EBITDA is EUR 80 million and the threshold is 4.5x. Solve for the minimum cure amount: required EBITDA is $380 / 4.5 = \text{EUR } 84.44 \text{ million}$, so the simplified cure is EUR 4.44 million. List the document questions that remain before relying on the result.

Practitioner review sequence

Reconcile covenant group, debt, nettable cash and EBITDA to source records and definitions.

State test date, period, pro forma assumptions, threshold, headroom and reverse stress.

Model springing triggers, cure amount, cure frequency, cash receipt and future-period effect.

Trace failure through certificate, notice, cure, waiver, default, acceleration and remedy as separate steps.

Legal, tax, regulatory and accounting boundary

Finance counsel must verify ratio definitions, testing dates, limited-condition rules, equity cures, suspension, reinstatement, waiver and default consequences. All calculations are fictional and require independent arithmetic review when adapted.

Primary-source map

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

EBITDA — The Number That Rules Everything

Why Understanding Adjustments Might Save Your Portfolio

EBITDA is an analytical bridge, not cash and not enterprise value. In leveraged finance, Covenant EBITDA can differ materially from reported EBITDA because the agreement specifies additions, deductions, pro forma adjustments, exclusions and discretion. The correct response is not to accept or reject add-backs as a category; it is to reconstruct the definition and test each amount.

This chapter uses fictional figures and the selected public credit agreement. It removes undocumented dialogue, market-prevalence assertions and any suggestion that an EBITDA adjustment alone establishes fair value or investment opportunity.

16.1 Start from an identifiable financial line

The reconciliation should begin with the line required by the agreement, such as consolidated net income, and bridge through interest, tax, depreciation, amortisation and other specified items. Record financial-statement period, accounting framework, consolidation perimeter and source document.

Do not begin with a presentation labelled adjusted EBITDA and work backwards. The covenant calculation needs an auditable starting point. Differences between management reporting, lender reporting and audited accounts should be reconciled.

Source note (retrieved 12 July 2026): PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

16.2 Additions and deductions

Common categories can include transaction costs, restructuring charges, cost savings, synergies, unusual losses, stock compensation and other items, but the agreement controls inclusion. Some categories are historical expenses; others are forecasts. Some are capped individually or in aggregate. Deductions can apply to gains or amounts no longer expected.

For every adjustment, record category, amount, period, cash or non-cash status, action taken, expected timing, evidence, cap and approval. If one item could fit two categories, allocate it once.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

16.3 Cost savings and synergies

A cost-saving adjustment should identify a specific action, baseline cost, implementation expense, timing and responsible owner. A revenue synergy should identify customers, volume, price, probability and required investment. The agreement may allow projected amounts under a standard and within a period; those legal conditions do not prove the forecast will occur.

Run a realisation schedule. Show gross adjustment, cash implementation cost, amount achieved, amount remaining and expiry. The downside model should remove delayed or unsupported adjustments and retain the cash costs where they are still expected.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

16.4 Pro forma acquisitions and disposals

For an acquisition, identify target historical EBITDA, purchase accounting effects, cost adjustments, financing and the applicable reference period. For a disposal, remove the disposed business and any stranded costs as required by the definition. Avoid annualising a partial period without the document's permission and a stated method.

The pro forma bridge should reconcile reported group EBITDA, acquired or disposed amounts, permitted adjustments and final Covenant EBITDA. It should also reconcile debt and cash on the same test date.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

16.5 Caps, baskets and double counting

A cap can apply to one category or a group of categories and can be measured as an amount or percentage. The denominator used for a percentage cap may itself include or exclude adjustments. Build the cap formula explicitly and test circularity.

Double counting can arise when a saving appears in historical results and remains in a forecast adjustment, when an acquisition contribution is included twice, or when a one-time cost is both excluded and added back. Maintain a unique adjustment identifier and roll each item forward between periods.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

16.6 Cash conversion

After calculating Covenant EBITDA, bridge to cash. Deduct cash taxes, interest, capital expenditure, working capital, leases, pensions, restructuring payments and other uses. Separate maintenance and growth investment with evidence. An EBITDA add-back can increase covenant capacity while reducing current cash because implementation costs are paid.

Measure conversion over time rather than one quarter. Working capital and capital expenditure can be seasonal. A borrower with high Covenant EBITDA but weak conversion can satisfy an incurrence test and still face liquidity stress.

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf.

16.7 Certificates, discretion and evidence

The agreement may require a compliance certificate or officer certification and may grant judgement within stated limits. Record who signs, what is certified, supporting schedules and delivery date. The existence of discretion does not eliminate the need for evidence or consistency.

Create an adjustment file with invoices, board materials, project plans, payroll records or other support appropriate to the item. Mark assumptions that remain management estimates. External auditors may audit financial statements without opining on every covenant adjustment.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

16.8 Disputes and sensitivities

A dispute can concern category eligibility, amount, timing, cap, double counting or calculation method. Prepare the strict, borrower and expected cases with the exact disputed items isolated. This quantifies the effect on ratios and capacity without deciding the legal interpretation.

Sensitivity should vary adjustment realisation, cash implementation cost and timing independently. Do not turn the highest permitted number into the base forecast.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

Fictional teaching exercise: EBITDA reconciliation

Fictional rules. Consolidated net income is EUR 38 million. Interest is EUR 22 million, tax is EUR 8 million, depreciation and amortisation are EUR 12 million, eligible transaction costs are EUR 3 million, claimed cost savings are EUR 9 million and a gain on asset sale is EUR 4 million. The fictional definition adds the first five expense categories, deducts the gain and caps cost savings plus transaction costs at 15% of EBITDA before those two categories.

Pre-cap EBITDA excluding transaction costs and savings is $38 + 22 + 8 + 12 - 4 =$ EUR 76 million. The cap is EUR 11.4 million. Claimed transaction costs plus savings equal EUR 12 million, so EUR 0.6 million is excluded and Covenant EBITDA is EUR 87.4 million. Recalculate if only EUR 5 million of savings has documentary support.

Fictional teaching exercise: EBITDA to cash

Using Covenant EBITDA of EUR 87.4 million, deduct EUR 7 million of cash taxes, EUR 22 million of cash interest, EUR 14 million of capital expenditure, EUR 6 million of working-capital investment and EUR 5 million of restructuring cash cost. Calculate cash before principal. Then remove unsupported savings from Covenant EBITDA but keep the restructuring cash cost. Explain the difference between covenant capacity and liquidity.

Practitioner review sequence

Begin with the required financial line and reconcile the covenant group and period.

Give every adjustment an owner, source, category, cap, timing, cash cost and realisation status.

Prevent double counting and maintain a roll-forward across test periods.

Bridge Covenant EBITDA to cash and run strict, expected and borrower interpretation sensitivities.

Legal, tax, regulatory and accounting boundary

Finance counsel must review definition scope, discretion, certification, pro forma treatment, caps and dispute consequences. Accounting specialists should review source-line and reporting questions; the arithmetic requires independent recalculation.

Primary-source map

Source note (retrieved 12 July 2026): PS02: Federal Reserve, FDIC and OCC, 2013 Interagency Guidance on Leveraged Lending, <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>; PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

PART IV

COVENANT DEEP DIVES

- 17 The Restricted Payments Covenant
 - 18 Debt and Liens Covenants
 - 19 The Asset Sale Covenant and Change of Control
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-

The Restricted Payments Covenant

17.1 Introduction — Value Leakage and Why It Matters

The restricted payments covenant exists to solve one problem: how to stop equity holders from stripping value out of a leveraged company while the debt is still outstanding.

The lesson can be an expensive one. Consider a mid-market leveraged buyout. On paper the structure looked fine: stable EBITDA of about €100 million, leverage of 4.5x, and the sponsor putting in reasonable equity. The plan was the standard one: grow EBITDA, delever over five years, exit.

What nobody had paid attention to was the dividend policy. The credit agreement allowed dividends up to a defined capacity (the "basket" the company could pay out), and the sponsor's business plan included annual sponsor distributions starting in year two. From the sponsor's side this was unobjectionable: they had invested equity, the company was generating cash, and returning some of it was what the equity was for.

The lender's answer is that the incentives run the other way. The equity sits behind the debt, and its holders have an incentive to extract value: if leverage starts rising and cash flow starts declining, the equity's exit value gets compressed, and the rational move is to take out what they can, while they can, before the whole structure deteriorates. That is value leakage, and the lender is left watching dividends go out to the equity while leverage rises.

The restricted payments covenant is the contractual remedy. It provides that the company cannot pay dividends, make distributions, pay down junior debt or make other payments that extract value from the company, unless it is in compliance with its financial covenants and the payment fits within specific baskets the lenders have agreed to.

The architecture of these covenants has changed substantially over the past two decades. In the 1990s and early 2000s, restricted payments covenants were relatively simple: a company could pay dividends if leverage was below a certain level, full stop. The calculation was straightforward — calculate leverage, compare it to the threshold, and the answer followed.

By the mid-2000s, as leverage got more aggressive and sponsors more creative, restricted payments covenants became considerably more complicated. They incorporated multiple baskets, each with its own calculation methodology; carveouts for tax distributions, management compensation and ordinary course distributions to subsidiaries; "grower" baskets that expanded automatically as the company's earnings improved; and equity proceeds baskets that allowed distributions from the proceeds of new equity issuances.

The modern restricted payments covenant is a combination lock that has to be opened from several angles at once, and sponsors have become expert at working the mechanism.

This chapter is about that mechanism: how value can leak out of a leveraged company despite the existence of a restricted payments covenant, and how to draft and negotiate covenants that actually prevent the leakage.

The restricted-payments covenant controls defined transfers of value from the restricted group, subject to conditions, baskets and exceptions. It can address dividends, equity repurchases, junior-debt payments and certain investments, but the exact perimeter comes from the selected instrument. The analysis should trace value, entity and capacity rather than rely on the word leakage.

The fictional capacity ledger illustrates the mechanics without purporting to reproduce a live transaction or specimen clause. Operative terms must be taken from the relevant executed documents.

17.2 Identify the payment and recipient

State the amount, currency, payer, recipient, consideration, purpose and date. Determine whether the action is a dividend, distribution, equity repurchase, junior-debt payment, investment or another defined restricted payment. A transfer can fall into more than one analytical category, but it should be counted once under the document's rules.

Trace the cash through intermediate entities. A payment from an unrestricted subsidiary may not be governed in the same way as a payment from a restricted subsidiary, but the investment that funded it may have consumed capacity earlier.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

17.3 General conditions

A restricted payment can be conditioned on no default, ratio compliance, availability of a builder amount or another test. The conditions may differ between loan and bond instruments and between baskets. Record the test date and pro forma effect.

An amount of basket capacity does not override a failed condition. Conversely, one exception may not carry the conditions attached to another. Cite the selected route and every requirement.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

17.4 Builder amount

A builder amount is a document-defined roll-forward. It can begin with a base amount and increase through retained earnings, excess cash flow, equity contributions, returns on investments or other sources, while decreasing through uses. The formula and starting date must be reproduced exactly.

Maintain a ledger by period. Each addition needs a source and each use needs approval, date and basket allocation. Returns should not be added unless the document permits them, and the same equity contribution should not support more than one capacity claim without express authority.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

17.5 Fixed and ratio-based baskets

Fixed baskets provide stated amounts and can include grower mechanics. Ratio-based capacity can permit payments when leverage or another test is satisfied. The borrower may have allocation and reclassification flexibility under the instrument.

Model each route independently and then in combination. Record previous uses, restored amounts, currency conversion and conditions. The maximum theoretical capacity may not be available on the proposed date.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

17.6 Investments and unrestricted subsidiaries

An investment can move cash or assets to an entity outside the guarantor or restricted perimeter. Test investment capacity, restricted-payment interaction, asset-transfer rules, debt and lien consequences, and designation conditions. The receiving entity's later use of value may be less constrained.

A designation analysis should show net asset value transferred, debt, guarantees, collateral released, EBITDA removed and remaining basket capacity. Re-designation should follow its own conditions and valuation rules.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

17.7 Junior-debt payments and equity repurchases

The covenant can restrict repayment, redemption or acquisition of junior debt before stated maturity, subject to exceptions such as refinancings or scheduled payments. Equity repurchases can have separate baskets or conditions. Identify instrument, maturity, price and funding source.

A refinancing exception should be tested for permitted debt, maturity, ranking, obligor, amount and proceeds. Permission to refinance debt does not itself permit a dividend or collateral release.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

17.8 Capacity interaction and anti-duplication

Restricted-payment capacity interacts with investments, asset sales, debt, liens and unrestricted subsidiaries. Build a transaction map showing every covenant touched. Use unique transaction identifiers to prevent the same return, contribution or reclassification from restoring capacity twice.

The credit memo should show gross capacity, conditions, proposed use and remaining capacity under downside EBITDA. If a ratio route disappears in the downside, fixed or builder capacity may still remain and should be modelled separately.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Fictional teaching exercise: builder roll-forward

Fictional rules. Opening builder capacity is EUR 10 million. The formula adds 50% of cumulative consolidated net income, adds qualifying equity contributions and investment returns, and deducts prior restricted payments. Net income is EUR 30 million, qualifying equity is EUR 8 million, investment returns are EUR 4 million and prior uses are EUR 12 million. Capacity is $10 + 15 + 8 + 4 - 12 = \text{EUR } 25$ million before conditions. A proposed EUR 20 million dividend leaves EUR 5 million if all conditions are met.

Now assume EUR 3 million of the investment return was already used to restore an investment basket and the fictional agreement prohibits double counting. Recalculate and record the transaction-level ledger entry.

Fictional teaching exercise: unrestricted-subsidary transfer

A borrower proposes to transfer an asset with EUR 40 million of fair value and EUR 12 million of EBITDA to a newly designated unrestricted subsidiary. The asset is collateral and the subsidiary currently guarantees the facilities. Prepare separate tests for designation, investment, restricted payment, asset transfer, guarantee release, collateral release, leverage and builder capacity. Do not assume that one available investment basket answers the other consequences.

Practitioner review sequence

Identify payer, recipient, value, purpose and date, then classify the action under the selected definitions.

Test no-default, ratio and other conditions for the exact basket used.

Maintain builder, fixed, grower, ratio, investment and reclassification ledgers without double counting.

Map restricted-group, guarantee, collateral, debt, lien and asset-sale effects before value moves.

Legal, tax, regulatory and accounting boundary

High-yield and loan counsel must verify restricted-payment definitions, builder and basket formulas, investments, designation, reclassification, junior-debt payments, anti-duplication and covenant interactions against the selected instrument.

Primary-source map

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Debt and Liens Covenants

Introduction — The Twin Gatekeepers

Debt and liens covenants answer related but different questions. The debt covenant controls whether an obligation may be incurred or guaranteed. The liens covenant controls whether assets may secure obligations. A transaction that satisfies one can fail the other. Their economic effect depends on definitions, baskets, ratio tests, reclassification, obligor coverage, collateral and intercreditor terms.

The framework below uses functional descriptions rather than inherited deal nicknames or specimen wording. Public instruments support the mechanics; fictional drafting illustrations are labelled and do not purport to be market clauses.

18.1 Define indebtedness and the obligor

Identify borrower, guarantor, principal, maturity, payment, guarantee, lease, hedge or contingent exposure and any exclusions. The document's indebtedness definition determines whether an item counts and whether it is measured at principal, liability amount or another value.

Map debt by entity. Non-guarantor and unrestricted entities can create structural priority even when consolidated leverage is unchanged. Record which debt is guaranteed and which assets support it.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

18.2 Fixed, grower and ratio debt capacity

Debt capacity can arise from fixed baskets, growers, ratio tests, acquisition debt, refinancing debt, local facilities, capital leases and other categories. Each route has amount, purpose, maturity, ranking, obligor and condition. Reclassification can move an item between categories where permitted.

A debt-capacity schedule should show opening capacity, use, reclassification and remaining amount. Ratio capacity should be recalculated with the proposed debt and permitted pro forma EBITDA on the correct date.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

18.3 Incremental and equivalent debt

Incremental facilities can add loans under an existing agreement, while incremental-equivalent debt can use another instrument form if the agreement permits it. Conditions can address maturity, weighted average life, ranking, guarantors, collateral, MFN and no default.

The model should separate committed capacity from funded debt and show use of proceeds. An incremental commitment does not create cash until conditions are met and a lender funds.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

18.4 Liens and permitted security

For each lien, identify grantor, secured obligation, asset, priority, perfection, amount and permitted category. A lien exception can be limited to acquired assets, purchase-money obligations, local facilities or another purpose. Debt permission does not automatically include lien permission.

Maintain a collateral schedule that links each secured claim to documents and perfection evidence. Public Article 9 text provides a U.S. statutory reference, but asset-specific and cross-border questions require counsel.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS18: Delaware Code, Title 6, Article 9, <https://delcode.delaware.gov/title6/c009/index.html>.

18.5 Priority and priming risk

Priming can arise through new higher-priority liens, contractual payment priority, debt at a structurally senior entity or a transaction that changes collateral access. Analyse each route separately. A general prohibition may contain exceptions or amendment thresholds that affect protection.

Functional protection can include limits on lien subordination, payment subordination, non-pro-rata exchanges, collateral releases or transfers of material assets. The protection must be drafted and interpreted in the selected documents; a nickname is not analysis.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

18.6 Asset-transfer protection

An asset transfer can reduce collateral or move value outside the guarantor group. Test asset-sale, investment, restricted-payment, subsidiary-designation and collateral-release provisions together. Material intellectual property and other core assets should be identified by function and value rather than by an inherited clause label.

Fictional drafting illustration: a covenant could require specified lender consent before a borrower transfers identified core collateral to a non-guarantor or unrestricted entity, subject to negotiated ordinary-course and replacement-value exceptions. Counsel must draft the operative language; the illustration states only the control objective.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07:

SEC EDGAR, Carnival 2023 secured-notes indenture,
<https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

18.7 Guarantee coverage

Guarantee coverage should be measured from the actual guarantor schedule, not an assumed percentage. Reconcile guarantor EBITDA and assets to the covenant group and list jurisdictional, ownership, immateriality and other exclusions. Identify accession and release conditions.

A coverage metric can be misleading if share pledges, non-guarantor value or excluded subsidiaries are treated inconsistently. Show contractual guarantee coverage, collateral coverage and economic contribution as separate measures.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement,
<https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture,
<https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

18.8 Security-agent and intercreditor mechanics

A collateral or security agent can hold or administer security under the relevant documents. Intercreditor terms can allocate priority, enforcement control, standstill, turnover, releases and proceeds. The title of the agent does not determine discretion or duty.

For a proposed new secured tranche, record accession, lien rank, voting class, enforcement control, hedge treatment and release rights. The capital-structure diagram should match the legal documents.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement,
<https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture,
<https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

18.9 Restricted and unrestricted subsidiaries

Restricted-group status affects covenant coverage but does not itself establish guarantee or collateral. Unrestricted subsidiaries can have separate debt and liens outside some covenant restrictions, subject to designation and investment conditions. Re-designation can have its own tests.

Before designation, show value transferred, EBITDA removed, debt and liens created, guarantees released, remaining investment capacity and effect on ratios. The same schedule should be updated when the entity returns to the restricted group.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement,
<https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture,
<https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

18.10 Enforcement and downside integration

Debt and lien capacity should feed the downside waterfall. Include a case in which fixed baskets are fully used, the revolver is drawn and permitted structurally senior debt is incurred. Then allocate value by entity, collateral and priority.

Enforcement assumptions must be reviewed by counsel. The model should show the economic effect of delay, cost and different realisation values without predicting a legal outcome.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS18: Delaware Code, Title 6, Article 9, <https://delcode.delaware.gov/title6/c009/index.html>.

Fictional teaching exercise: debt and lien capacity

Fictional rules. A borrower has a EUR 50 million debt basket, a EUR 30 million lien basket and ratio debt if pro forma net leverage is no greater than 5.0x. Net debt is EUR 440 million and Covenant EBITDA is EUR 100 million. It proposes EUR 70 million of new secured debt. The full debt would produce 5.10x leverage, so ratio capacity is unavailable under the stated rule. The fixed debt basket covers EUR 50 million, but the lien basket covers only EUR 30 million. The remaining EUR 20 million cannot be secured under those routes even though debt capacity exists.

Now assume EUR 10 million of the debt basket and EUR 5 million of the lien basket were previously used. Recalculate and identify whether an unsecured, junior-secured or smaller financing could fit, subject to all other conditions.

Fictional teaching exercise: structural priority

A non-guarantor subsidiary owns assets worth EUR 120 million and can incur EUR 35 million of permitted local secured debt. Parent-level lenders have no guarantee from that subsidiary. Build recoveries under a downside in which the local debt is fully drawn and costs are EUR 5 million. Then compare with a structure in which the subsidiary becomes a guarantor and shares collateral, subject to counsel confirming validity and priority.

Fictional teaching exercise: functional protection

Draft a non-legal control specification for three risks: transfer of core collateral to a non-guarantor, subordination of existing liens and non-pro-rata exchange into higher-priority debt. For each, state protected action, covered entities, consent concept, permitted exceptions and evidence. Leave operative wording and enforceability to counsel.

Practitioner review sequence

Test debt and liens separately by obligor, amount, purpose, maturity, ranking and condition.

Maintain debt, lien, guarantee, collateral and restricted-group schedules with reclassification.

Replace named clause shorthand with the functional risk, operative provision and consent rule.

Run a downside with full revolver draw, basket use and structurally senior debt before estimating recovery.

Legal, tax, regulatory and accounting boundary

Secured-finance and restructuring counsel must verify indebtedness, liens, perfection, priming, priority, guarantee coverage, security-agent authority, intercreditor terms, restricted-group effects and enforcement. Drafting illustrations are fictional control objectives, not legal clauses.

Primary-source map

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS18: Delaware Code, Title 6, Article 9, <https://delcode.delaware.gov/title6/c009/index.html>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

The Asset Sale Covenant and Change of Control

The Asset Sale Covenant

Asset-sale and change-of-control provisions protect different risks. An asset-sale covenant can govern dispositions, consideration and use of proceeds. A change-of-control provision can create a repayment, offer or other consequence when its defined ownership or control trigger occurs. Neither provision should be described from market memory; the selected loan agreement or indenture controls.

This chapter replaces transaction anecdotes and uncited threshold claims with document-specific mechanics and fictional calculations. It distinguishes a bond repurchase offer from a loan event of default and treats portability as a defined condition rather than a general market concept.

19.1 Define the disposition

Identify seller, asset, buyer, consideration, fair-value evidence, currency, closing date and relationship between the parties. Then apply the document's asset-sale definition and exclusions. Ordinary-course sales, inventory, obsolete assets, permitted investments, casualty events or intra-group transfers can receive different treatment under the instrument.

Do not begin with proceeds. First determine whether the action is within scope and whether another covenant also applies. A transfer to an unrestricted subsidiary can implicate investments, restricted payments, collateral releases and subsidiary designation in addition to asset-sale rules.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

19.2 Consideration and fair value

An asset-sale covenant can require fair value and a minimum cash or cash-equivalent component, subject to definitions and exceptions. Record who determines value, the valuation date, non-cash consideration and any deemed-cash items. An internal estimate should not be presented as independent evidence.

For credit analysis, compare sale proceeds with the asset's EBITDA, replacement cost, collateral value and strategic role. A sale at stated fair value can still weaken the credit if it removes durable cash flow and proceeds are not applied to debt.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

19.3 Net proceeds

Net proceeds are calculated under the document. Permitted deductions can include transaction costs, taxes, debt repayment, reserves or other specified amounts. Create a bridge from gross cash received to net proceeds with

invoices, tax assumptions and reserve release dates.

The bridge should be updated when a reserve is released or a non-cash item is monetised if the instrument requires it. Without a roll-forward, amounts can escape the reinvestment or prepayment process.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

19.4 Reinvestment and repayment

The instrument can permit reinvestment for a stated period and purpose, require debt repayment, or lead to a bond repurchase offer. Record notice, commitment, expenditure and completion deadlines. A general intention to reinvest may not satisfy an operative condition.

Model three uses of proceeds: reinvestment, mandatory debt reduction and retention where permitted. Show resulting EBITDA, interest, leverage, liquidity and collateral. Deleveraging measured only by principal repayment can be offset by lost EBITDA.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

19.5 Asset-sale offer mechanics

A bond indenture can require an offer when excess proceeds exceed the stated conditions. The offer process, price, timing, permitted ranking debt and residual proceeds come from the indenture. A loan agreement can instead apply proceeds through mandatory prepayment provisions.

The analyst should map tender amount, eligible holders or lenders, pro rata allocation, settlement and remaining debt. Do not assume every creditor receives immediate par repayment.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

19.6 Change-of-control definition

A change-of-control trigger can refer to ownership, voting power, board control, sale of all or substantially all assets, a specified parent or another defined event. The exact percentage and acting-together concept, if any, must be read from the instrument. There is no universal threshold.

Draw ownership before and after the transaction, including intermediate entities and permitted holders. Then apply every limb of the definition and any exception. For complex reorganisations, identify the legal owner and controlling rights rather than relying on economic branding.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07:

SEC EDGAR, Carnival 2023 secured-notes indenture,
<https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

19.7 Put, prepayment and default consequences

A bond change-of-control provision can require an offer to repurchase at a defined price when the trigger and any additional condition occur. A loan agreement may require prepayment, create an event of default or use another mechanism. Those consequences are not interchangeable.

Record trigger date, notice, offer or repayment period, price, accrued interest, funding source and consequence of non-compliance. Acceleration and enforcement require separate analysis.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement,
<https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture,
<https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

19.8 Portability

Portability can allow a transaction to avoid a change-of-control consequence if defined conditions are satisfied. Conditions can involve leverage, rating, permitted holders, time or other document-specific tests. The label does not establish availability.

Test portability at the proposed transaction date using the agreement's definitions. Recalculate debt, cash and EBITDA and record any certification. Also analyse whether guarantees, collateral, management, reporting or restricted-group structure change despite the absence of a trigger.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement,
<https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture,
<https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

19.9 Interaction with other covenants

An asset sale can affect investments, restricted payments, liens, collateral releases, debt repayment and EBITDA. A change of control can interact with portability, acquisition debt, refinancing, mandatory prepayment and cross-default. Build a connected transaction checklist.

Capacity should be tested after the transaction as well as at closing. If EBITDA leaves the group, leverage and grower baskets can shrink. If debt is repaid, interest falls but liquidity may also decline.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement,
<https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture,
<https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Fictional teaching exercise: net proceeds and deleveraging

Fictional rules. A borrower sells an asset for EUR 90 million cash. Permitted deductions are EUR 3 million of transaction costs, EUR 7 million of current taxes and a EUR 5 million reserve. Net proceeds are EUR 75 million. The asset contributed EUR 12 million of Covenant EBITDA. Opening net debt is EUR 480 million and Covenant EBITDA is EUR 100 million. If all net proceeds repay debt, net debt falls to EUR 405 million and EBITDA falls to EUR 88 million,

producing leverage of 4.602x compared with 4.80x before the sale. The sale deleverages, but by less than a principal-only view suggests.

Release the EUR 5 million reserve six months later and assume the fictional covenant then requires application. Recalculate debt and document the proceeds roll-forward.

Fictional teaching exercise: change-of-control process

A fictional indenture requires a repurchase offer at 101% of principal plus accrued interest after a defined change of control. EUR 250 million principal remains outstanding and accrued interest is EUR 4 million. If all holders tender, gross cash required is EUR 256.5 million. Build the funds plan, notice timetable and sensitivity for 60% participation. Then list the definition, exception and portability facts that must be confirmed before assuming an offer is required.

Practitioner review sequence

Define seller, asset, buyer, consideration, fair value and every covenant touched by the disposition.

Bridge gross consideration to net proceeds and maintain reinvestment, reserve and repayment deadlines.

Apply the exact change-of-control definition, exception, portability condition and document-specific consequence.

Recalculate leverage, liquidity, collateral and covenant capacity after assets or ownership change.

Legal, tax, regulatory and accounting boundary

High-yield and loan counsel must verify asset-sale scope, consideration, proceeds, offers, prepayment, collateral release, change-of-control triggers, portability and covenant interactions. Fair-value, tax and enforcement questions require their own qualified review.

Primary-source map

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

Events of Default

An event of default is a contractually defined state that can permit specified creditor actions after applying thresholds, notice, grace and cure. It is not synonymous with business distress, covenant breach, acceleration, enforcement or insolvency. A disciplined analysis separates those stages and identifies who has authority at each one.

The selected public credit agreement and indenture illustrate document mechanics. Bankruptcy statutes provide public text for involuntary cases and the automatic stay. This chapter uses fictional fact patterns and does not predict a court outcome.

20.1 Payment defaults

Identify the payment, obligor, amount, due date, currency, payment location and any grace period. Principal, interest, fees and other amounts can follow different rules. Operational error, insufficient funds and disputed amount should be distinguished factually before applying the clause.

The response file should preserve payment instructions, account statements, notices and cure timing. A cured late payment may still have consequences under another agreement or disclosure obligation, which requires separate analysis.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

20.2 Cross-default and cross-acceleration

Cross-default can be triggered by a default under other debt, while cross-acceleration can require that other debt has been accelerated or become due early, depending on the definition. Threshold, covered debt, entity scope, exclusions and cure are critical.

Build a debt schedule with principal, obligor, agreement, status, threshold contribution and action taken by the other creditors. Do not state a cascade until every link in the chain is satisfied.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

20.3 Representation and warranty defaults

A representation can be tested when made, repeated or deemed repeated. An event-of-default clause may require material incorrectness, a cure period or another condition. Identify the exact representation, date, knowledge qualifier and impact.

The credit response should separate historical falsity, current remediation and continuing reliance. Counsel should determine whether a correction, waiver or amendment is required.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

20.4 Covenant defaults

Payment, financial, affirmative and negative covenant failures can have different notice and cure mechanics. A financial-covenant failure may be subject to an equity cure; a reporting failure may have a period after notice; an unauthorised debt incurrence may not be curable by later repayment under the same logic.

Record breach date, discovery, notice, cure action, certificate, waiver vote and current status. Do not assume that a commercial plan suspends the contractual clock.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

20.5 Judgment defaults

A judgment default can depend on amount, finality, enforcement, stay, bonding, insurance and time. The clause defines which judgments and entities count. A public announcement of litigation is not itself proof of the contractual trigger.

Collect the order, amount, parties, appeal or stay status, insurance evidence and dates. Route legal effect to litigation and finance counsel.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

20.6 ERISA and specialised regulatory defaults

Some agreements contain events tied to pension or ERISA matters, regulatory action or similar specialised risks. The definition, threshold and covered entities must be read from the agreement. The credit team should not interpret specialised law from a covenant summary.

Prepare a fact pack with plan or regulatory event, date, estimated liability, notice, agency or court document and affected entity. Qualified specialist counsel determines whether the contractual and legal thresholds are met.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

20.7 Insolvency events

Insolvency events can include voluntary proceedings, involuntary proceedings, inability-to-pay concepts, appointments, judgments or analogous events, with different conditions and covered entities. Section 303 of the U.S. Bankruptcy Code provides requirements for involuntary cases; the document may specify a dismissal period or material-entity threshold.

Automatic consequences can differ from defaults requiring declaration. Identify entity, filing, order, date, proceeding and contractual text. Cross-border recognition and equivalent proceedings require local counsel.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS19: 11 U.S.C. section 303, <https://uscode.house.gov/view.xhtml?edition=prelim&hl=false&num=0&path=%2Fprelim%40title11&req=granuleid%3AUSC-prelim-title11-section303>.

20.8 Notice, grace and cure

Create a default timeline from underlying event through notice, knowledge, grace, cure, event of default and any declaration. Use calendar dates and identify who may give effective notice. An informal email may not satisfy the contract, while a contractual period can run without commercial escalation.

A cure should address both the trigger and any continuing consequence. Record cash payment, corrective action, certificate and creditor acknowledgement where appropriate.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

20.9 Acceleration

Acceleration makes specified obligations due under the document after the required event and action. Identify who may declare, voting threshold, affected facilities or notes, automatic events, rescission and individual rights. Acceleration under one instrument can affect cross-default analysis elsewhere.

The liquidity model should show principal, accrued interest, premium, hedging termination and other amounts if acceleration occurs. It should not assume immediate payment or recovery.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

20.10 Remedies, collateral and the automatic stay

Enforcement follows security, intercreditor, agency and law. Direction, standstill, turnover, releases and proceeds allocation may sit outside the credit agreement. An event of default can create authority without determining the timing or economic wisdom of action.

Section 362 of the U.S. Bankruptcy Code provides automatic-stay text within its scope. The stay, relief, exceptions and application require bankruptcy counsel. A financial model may show delayed recovery and costs, but it should not state that a particular action is permitted.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS20: 11 U.S.C. section 362, <https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section362%28d%29>.

Fictional teaching exercise: cross-acceleration

Fictional rules. Facility A has a EUR 25 million threshold and is triggered only if other covered debt is accelerated. The borrower misses a EUR 8 million payment on Bond B and a EUR 22 million payment on Lease C. Bond B has not been accelerated; Lease C is excluded from covered debt. On those facts, no qualifying accelerated amount has been identified. Now assume Bond B holders validly accelerate EUR 80 million. Build the Facility A timeline, including notice and any cure, before concluding an event exists.

Fictional teaching exercise: default sequence

A fictional reporting covenant requires delivery by 31 March, has a ten-business-day cure after notice, and becomes an event of default only after that period. Effective notice is delivered on 4 April. Construct the calendar using stated fictional business days and identify the facts needed to determine the expiry. Then add a timely waiver signed by the required lenders and record its scope.

Fictional teaching exercise: accelerated liquidity

A borrower has EUR 300 million principal, EUR 6 million accrued interest, EUR 4 million of fictional break costs and EUR 20 million cash, of which EUR 8 million is minimum operating cash. Calculate the immediate funding gap if all amounts become due. Then build recovery timing cases of six, twelve and twenty-four months with separately stated costs rather than assuming acceleration equals recovery.

Practitioner review sequence

Identify trigger, entity, amount, threshold, materiality, notice, grace, cure and effective date for each alleged default.

Separate breach, event of default, declaration, acceleration, enforcement, insolvency and recovery.

Maintain a complete debt and legal-process schedule for cross-default, judgment and insolvency analysis.

Route bankruptcy, ERISA, litigation, regulatory and enforcement conclusions to the appropriate specialists.

Legal, tax, regulatory and accounting boundary

Finance, restructuring, bankruptcy, litigation and ERISA counsel must verify every trigger, notice, cure, acceleration, remedy, involuntary-case, automatic-stay, judgment and specialised-law proposition. The fictional exercises do not predict enforceability or court action.

Primary-source map

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS19: 11 U.S.C. section 303, <https://uscode.house.gov/view.xhtml?edition=prelim&hl=false&num=0&path=%2Fprelim%40title11&req=granuleid%3AUSC-prelim-title11-section303>; PS20: 11 U.S.C. section 362, <https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section362%28d%29>.

The Accordion and Incremental Facility

An incremental facility permits additional commitments or loans under conditions stated in the credit agreement. The feature is often called an accordion because the capital available under the document can expand, but the borrower has no cash until lenders commit, conditions are satisfied and funding occurs. Incremental-equivalent debt can extend capacity to another permitted instrument form.

The analysis combines capacity, leverage, maturity, ranking, guarantees, collateral, MFN, voting and use of proceeds. This chapter uses the selected public credit agreement, a public extension amendment and fictional examples rather than unnamed transactions or market-prevalence claims.

21.1 Basic mechanics

Identify the borrower request, incremental amount, facility type, currency, lenders, effective date and use of proceeds. The agreement can permit an increase to an existing class, a new term or revolving class, or another structure. Existing lenders may have no obligation to participate unless the document says otherwise.

The closing process typically requires commitments, an amendment or joinder, conditions, fees, legal opinions or other evidence. Update the lender register, commitment schedule, interest terms and repayment profile.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

21.2 Fixed capacity

A fixed incremental amount can be stated as a nominal basket and may include a grower. Record original amount, prior use, repayments that restore capacity if permitted, reclassification and remaining amount. The basket can have purpose, maturity or ranking limits.

Do not calculate capacity from the current agreement face amount alone. Amendments and earlier incremental facilities can change the ledger. Maintain an executed-document history.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

21.3 Ratio capacity

Ratio capacity allows an amount that satisfies a leverage, secured-leverage or coverage test under the agreement. Calculate debt and EBITDA with the proposed incremental financing and permitted pro forma transactions on the correct test date. State whether cash proceeds are netted and whether the debt is deemed fully drawn.

Unlimited ratio capacity is not economically unlimited. The denominator, business cash flow, lender appetite, maturity and other covenants still constrain funding. A permitted amount is not a committed amount.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

21.4 Growers, reclassification and ordering

A grower can scale a fixed amount with Covenant EBITDA or another measure. Reclassification can restore fixed capacity if ratio capacity becomes available. Ordering rules can determine whether ratio or fixed capacity is used first.

Build a capacity roll-forward for every borrowing date. Show EBITDA, ratio, fixed basket, grower, allocation, reclassification and remaining capacity. Repeat under downside EBITDA to reveal capacity that could disappear.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

21.5 Conditions and limitations

Conditions can include no default, representations, pro forma compliance, minimum maturity, weighted average life, pricing, purpose, guarantor coverage and collateral sharing. Different conditions can apply to acquisition financing or committed acquisitions.

Create a condition checklist with fact, evidence, owner and satisfaction date. If a limited-condition transaction changes the testing date, document that choice and any continuing conditions.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

21.6 MFN protection

MFN protection can adjust an existing tranche if specified incremental debt has a higher calculated yield. The agreement defines protected debt, exclusions, comparison period, yield components, threshold and remedy. Margin, floor, OID and fees can require a stated conversion method.

Run the calculation before funding. Show both new-debt yield and existing-debt yield under the document's assumptions. Record whether the remedy changes margin, applies automatically or requires another action.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

21.7 Incremental-equivalent debt

Incremental-equivalent debt can permit notes or other debt outside the agreement using shared capacity, subject to stated conditions. Test debt, liens, maturity, ranking, guarantees, collateral, intercreditor accession and MFN. A separate instrument can create a separate voting class and enforcement channel.

Update the complete capital structure, not only the credit-agreement debt schedule. The same capacity should not be counted once for loans and again for notes.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

21.8 Acquisition, refinancing and liquidity uses

Incremental debt can fund acquisitions, capital expenditure, refinancing or other permitted purposes. Each use engages different covenants and execution risks. Acquisition financing requires sources and uses, pro forma EBITDA and integration cost; refinancing requires maturity, premium and lien-release analysis.

For liquidity funding, model the burn rate and conditions to draw. New debt that extends runway without fixing structural cash deficits can increase loss severity. The credit paper should state milestones and exit funding.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

21.9 Voting and new classes

An incremental class can have its own lenders, pricing, maturity and voting interests. The agreement determines which amendments are class-specific, which require all or affected lenders, and how the agent administers the class. Existing lenders may be diluted in voting even when principal is unchanged.

Record pro forma lender holdings and denominators after funding. For a later amendment, identify which classes are affected and which votes are excluded.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

21.10 Jurisdiction and private-credit variations

A selected U.S. agreement and public amendment provide examples, but English-law or other European facilities can use different terminology, intercreditor arrangements and accession processes. Direct-lending facilities can concentrate approval among fewer lenders. Those differences are document facts, not regional constants.

The comparison should identify governing law, facility, lender group, capacity formula and consent rule. Avoid statements that one market always permits more capacity.

Source note (retrieved 12 July 2026): PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

Fictional teaching exercise: capacity stack

Fictional rules. Fixed incremental capacity is EUR 75 million. A grower equals 25% of Covenant EBITDA if greater; Covenant EBITDA is EUR 400 million, so fixed-plus-grower capacity is EUR 100 million. Ratio debt is permitted if pro forma first-lien net leverage does not exceed 4.5x. Existing first-lien net debt is EUR 1.65 billion. The borrower proposes EUR 250 million of new first-lien debt with no EBITDA increase. Pro forma leverage is 4.75x, so ratio capacity is unavailable; only EUR 100 million fits under the stated fixed route.

Now add an acquisition contributing EUR 50 million of permitted pro forma EBITDA. Pro forma leverage becomes $1.90 \text{ billion} / 450 \text{ million} = 4.222x$, so the full amount can satisfy the fictional ratio condition. Identify the acquisition, EBITDA and test-date evidence required before relying on it.

Fictional teaching exercise: MFN

Existing debt pays benchmark plus 375 basis points and was issued at par. New specified incremental debt pays benchmark plus 425 basis points and is issued at 98, with OID converted over four years. Under the fictional formula, OID contributes 50 basis points, so new yield is 475 basis points. If the threshold is 50 basis points, the excess over existing yield after threshold is 50 basis points. Calculate the stated margin remedy and list the exclusions that could change the result.

Fictional teaching exercise: voting dilution

Existing lenders hold EUR 300 million. A new EUR 150 million incremental class joins the same general voting pool under fictional rules. One existing lender holds EUR 90 million. Calculate its voting share before and after funding: 30% before and 20% after. Then identify matters that might use a class or affected-lender vote instead of the general pool.

Practitioner review sequence

Maintain fixed, grower, ratio and reclassification ledgers with exact testing dates and assumptions.

Test maturity, weighted average life, ranking, guarantees, collateral, purpose, no-default and other conditions.

Calculate MFN yield from the document's margin, floor, OID, fee, threshold and remedy rules.

Update capital structure, lender holdings, class voting and downside liquidity after every incremental financing.

Legal, tax, regulatory and accounting boundary

Finance counsel must verify capacity, test dates, reclassification, MFN, incremental-equivalent debt, class voting, maturity, ranking, guarantee, collateral and jurisdiction-specific mechanics. All exercises use fictional rules.

Primary-source map

Source note (retrieved 12 July 2026): PS03: ECB Banking Supervision, Guidance on leveraged transactions, https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf; PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

PART V

AMENDMENT MECHANICS AND RESTRUCTURING

- 22 Liability Management Exercises
 - 23 Amend and Extend Transactions
 - 24 Guarantee and Collateral Architecture
 - 25 UK Restructuring Tools
 - 26 Distressed Debt and Special Situations
-

Liability Management Exercises

A liability management exercise changes debt terms, priority, maturity, collateral, obligors or ownership outside a conventional refinancing or court process. The label covers different transactions with different consent and value effects. Analysis should begin with the documents and capital structure, then identify precisely what changes and which creditor groups bear or receive value.

This chapter discusses *Serta Simmons* through the revised Fifth Circuit opinion. Other examples are fictional, and any conclusion about enforceability remains tied to the relevant primary record, agreement and qualified legal advice.

22.1 Define the objective and constraints

The borrower may seek liquidity, maturity extension, interest reduction, covenant relief, deleveraging, new capital or a transfer of assets. Creditors may seek improved priority, economics, collateral or control. State the objective, liquidity runway and alternative paths before analysing technique.

Build a constraint map across debt, liens, investments, restricted payments, asset sales, amendments, sacred rights, pro rata sharing, intercreditor terms and insolvency law. A transaction must fit every required permission and process. Capacity in one provision does not answer consent or priority.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

22.2 Priority-changing exchange

A priority-changing exchange can offer participating creditors new debt with higher lien or payment priority while non-participants retain existing claims. The analysis should identify new-money amount, exchanged principal, participating holders, price, priority, collateral, voting, releases and treatment of non-participants.

The value transfer has at least three components: new liquidity supplied, priority gained and claim amount changed through exchange price or fees. Model each separately. A higher-priority claim can improve recovery even when face amount is reduced; non-participants can lose recovery without a change to stated coupon or maturity.

*Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS21: Fifth Circuit, revised *Serta Simmons* opinion, No. 23-20451, <https://www.ca5.uscourts.gov/opinions/pub/23/23-20451-CV0.pdf>.*

22.3 Serta Simmons and the revised Fifth Circuit opinion

The revised Fifth Circuit opinion in No. 23-20451 is the primary source for the appellate holding and reasoning concerning the *Serta* transaction. Any account should preserve the procedural posture, the credit-agreement

language at issue and the limits of the court's decision. A secondary summary cannot substitute for the opinion.

For teaching, separate three questions. First, what transaction steps occurred? Second, what provisions and definitions did the court analyse? Third, what did the court hold, and what issues did it not decide? Each proposition should be tied to the opinion before counsel assesses relevance to another agreement.

Source note (retrieved 12 July 2026): PS21: Fifth Circuit, revised Serta Simmons opinion, No. 23-20451, <https://www.ca5.uscourts.gov/opinions/pub/23/23-20451-CV0.pdf>.

22.4 Asset-transfer transaction

An asset-transfer transaction moves assets or equity interests to a different entity or covenant perimeter, potentially creating collateral for new debt. Test investment, asset-sale, restricted-payment, subsidiary-designation, guarantee-release, collateral-release, debt and lien provisions. Identify valuation and consideration.

The economic model should show EBITDA, assets, cash and debt before and after the transfer by entity. It should also show whether value returns to the original obligor and on what terms. A permitted transfer can still weaken existing creditors economically.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

22.5 Non-pro-rata exchange and open-market concepts

An agreement may distinguish assignments, purchases, exchanges, Dutch auctions and other acquisition methods. The analysis should not assume that an open-market label permits any non-pro-rata transaction. Read the definition, process, affiliate restrictions, cancellation rules and voting treatment.

For each participating lender, record old claim, cash or new debt received, priority, voting and remaining exposure. For non-participants, recalculate leverage, collateral coverage, voting share and maturity.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS21: Fifth Circuit, revised Serta Simmons opinion, No. 23-20451, <https://www.ca5.uscourts.gov/opinions/pub/23/23-20451-CV0.pdf>.

22.6 Cooperation arrangements

Creditors can enter agreements governing information, negotiation, transfers, voting or participation for a period. Scope, parties, term, permitted transfers, remedies and competition or other legal issues require counsel. A cooperation arrangement does not itself amend the borrower's debt documents.

The credit analyst should model how the arrangement changes execution probability and holder incentives without assuming enforceability. Identify participating principal, maturity, restrictions, termination events and the decision process for proposed transactions.

22.7 Functional defensive provisions

Defensive drafting should be described by the risk it addresses. Priority-change protection can restrict subordination of liens or payment without specified consent. Non-pro-rata protection can limit exchanges that

elevate selected lenders. Asset-transfer protection can restrict movement of core collateral or guarantees. Voting protection can address affiliate or newly issued debt.

Each control needs a defined action, covered entities, consent standard, exceptions and anti-evasion logic. The strongest-sounding phrase can fail if definitions, releases or amendment provisions permit a route around it. Operative drafting belongs to counsel.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS21: Fifth Circuit, revised Serta Simmons opinion, No. 23-20451, <https://www.ca5.uscourts.gov/opinions/pub/23/23-20451-CV0.pdf>.

22.8 Functional enabling provisions

Borrower flexibility can arise from fixed or ratio capacity, reclassification, subsidiary designation, refinancing provisions, purchase mechanics and amendment thresholds. Analyse the combined route rather than treating one basket as the transaction authority.

A capacity map should show every provision used, amount, test date, condition and residual capacity. Recalculate after the transaction because the new debt, transferred EBITDA and changed group can alter future ratios and baskets.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>.

22.9 Valuation and creditor outcomes

Construct a pre-transaction and post-transaction waterfall. Include new money, exchanged debt, existing debt, collateral, structural priority and transaction costs. Show enterprise-value ranges and timing. The comparison should distinguish liquidity benefit from priority transfer.

A transaction can extend runway and improve total enterprise value while transferring value among creditor groups. The decision record should show both effects. It should also compare a consensual alternative with the same liquidity amount and no priority change.

22.10 U.S. and English or European boundaries

U.S. and English or European transactions can differ in agreement terms, security trusts, intercreditor arrangements, corporate law, insolvency tools and court process. Those are not universal regional outcomes. Identify each governing law, entity, document and proposed step.

An English restructuring plan under Part 26A and a U.S. Chapter 11 process are statutory alternatives with their own requirements. The existence of a possible process does not establish that an out-of-court step is valid or invalid.

Source note (retrieved 12 July 2026): PS17: UK Companies Act 2006, Part 26A, <https://www.legislation.gov.uk/ukpga/2006/46/part/26A>; PS20: 11 U.S.C. section 362, <https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11->

section362%28d%29; PS21: Fifth Circuit, revised Serta Simmons opinion, No. 23-20451, <https://www.ca5.uscourts.gov/opinions/pub/23/23-20451-CV0.pdf>.

22.11 Process and governance

A controlled LME process needs current lender holdings, confidentiality controls, conflicts review, valuation, liquidity model, document analysis, board process and a complete alternatives record. Terms should be reconciled across exchange documents, amendments, new-money documents, intercreditor agreements and releases.

The closing file should record participation, consideration, new claims, collateral actions, voting, fees and post-transaction capital structure. Publication or teaching materials should use only public records or clearly fictional facts.

Source note (retrieved 12 July 2026): PS21: Fifth Circuit, revised Serta Simmons opinion, No. 23-20451, <https://www.ca5.uscourts.gov/opinions/pub/23/23-20451-CV0.pdf>.

Fictional teaching exercise: priority-changing exchange

Fictional facts. A borrower has EUR 400 million of equal-ranking first-lien debt and needs EUR 60 million of liquidity. Holders of EUR 240 million agree to exchange into a new priority tranche at 95 exchange value and provide all EUR 60 million of new money. The new tranche principal is EUR 288 million: EUR 228 million exchange principal plus EUR 60 million new money. Non-participants retain EUR 160 million. Assume collateral value after costs is EUR 360 million and the new tranche is paid first under the fictional structure. Allocate recovery and compare with a pari passu new-money alternative.

Then increase enterprise value by EUR 80 million to reflect the liquidity runway. Show separately the value created by additional runway and the value transferred by priority. Do not state that the transaction is legally permitted; list the document and counsel questions.

Fictional teaching exercise: asset transfer

A restricted subsidiary owns an asset worth EUR 100 million and generating EUR 14 million of EBITDA. The borrower proposes to move it to an unrestricted entity and raise EUR 55 million secured by that asset. Build the covenant map for investment, asset sale, restricted payment, designation, debt, liens, guarantee release and collateral release. Then recalculate restricted-group leverage and creditor recovery before and after.

Primary-record exercise: Serta opinion

Using only the revised Fifth Circuit opinion, prepare a three-column record: transaction fact stated by the court, agreement provision analysed, and holding or reasoning. Add a fourth column for questions the opinion does not resolve for a different agreement. Do not use a secondary case summary.

Practitioner review sequence

Define liquidity need, objective, alternatives and every document constraint before selecting a technique.

Map old and new claims, participating and non-participating creditors, collateral, priority, voting and consideration.

Use functional risk descriptions for defensive and enabling provisions; leave operative drafting and enforceability to counsel.

Compare pre- and post-transaction value, including liquidity benefit, priority transfer, costs and downside timing.

Tie every named-case proposition to the primary court record and its procedural limits.

Legal, tax, regulatory and accounting boundary

Mandatory U.S. and English or European restructuring counsel review is required for the Serta account, exchanges, asset transfers, cooperation arrangements, voting, intercreditor terms, enforceability, defensive drafting and statutory alternatives. Every case proposition must remain tied to a primary record.

Primary-source map

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS17: UK Companies Act 2006, Part 26A, <https://www.legislation.gov.uk/ukpga/2006/46/part/26A>; PS20: 11 U.S.C. section 362, <https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section362%28d%29>; PS21: Fifth Circuit, revised Serta Simmons opinion, No. 23-20451, <https://www.ca5.uscourts.gov/opinions/pub/23/23-20451-CV0.pdf>.

Amend and Extend Transactions

An amend-and-extend transaction changes the maturity or related terms of selected debt through the amendment, extension or exchange mechanics permitted by the governing documents. Participating creditors can become a new class or extension series while non-participants retain existing terms, subject to the agreement and any protected rights. The transaction can reduce near-term refinancing pressure without reducing principal.

This chapter uses the public Genuine/HireRight extension amendment as a document example and fictional economics for teaching. The discussion of consent payments and exit consents is tied to the cited primary judgments.

23.1 Diagnose the maturity problem

Build a monthly maturity and liquidity schedule that includes principal, amortisation, interest, call cost, hedging, leases and any springing maturity. Identify cash available, revolver capacity and operating minimum. The shortfall and timing define the extension objective.

Compare four paths using the same operating case: cash repayment, full refinancing, partial refinancing and extension. State market-access, fees, interest, collateral and covenant assumptions. An extension that merely delays an unsustainable cash deficit is not a complete solution.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

23.2 Extension proposal

The borrower should specify eligible debt, proposed maturity, margin, fees, OID, amortisation, covenants, collateral, ranking, conditions, election deadline and settlement. A term sheet should distinguish changes that apply only to extending lenders from changes requested from all lenders.

Create a sources-and-uses and interest schedule for expected participation levels. If non-extending debt remains, show its earlier maturity and payment priority.

Source note (retrieved 12 July 2026): PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

23.3 Election mechanics

An extension process can invite lenders to elect participation by a deadline and subject to acceptance or allocation. Record eligible holdings, election amount, signature authority, KYC or assignment conditions and treatment of oversubscription. The public extension amendment illustrates electing-lender and class mechanics in that instrument.

The closing file should reconcile elections to the lender register and new class. A soft indication is not an executed election. Participation assumptions in the model should be labelled until settlement.

Source note (retrieved 12 July 2026): PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

23.4 Extension series and class formation

Extended debt can become a separate class or series with its own maturity, pricing and amortisation. Identify whether it shares guarantees and collateral, ranks pari passu, has separate voting, and is subject to the same mandatory prepayment. Update every schedule and definition affected by class creation.

Class formation can dilute general voting and create different incentives. Show lender holdings before and after, then analyse future amendments under both general and class-specific thresholds.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

23.5 Protected rights and maturity extension

Credit agreements can protect principal, interest, payment dates, pro rata sharing, collateral or other rights through individual, affected-lender or heightened consent. Extension provisions may create a mechanism for electing lenders without changing non-electing payment dates. The exact interaction requires counsel.

Do not assume that a maturity extension is permitted because non-extendors retain their stated date. Test amendment provisions, extension mechanics, class rules, intercreditor terms and any indirect effect on priority or payment.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

23.6 Economics of extension

Economics can include margin increase, OID, extension fee, consent fee, call protection and covenant change. Separate cash paid at closing from ongoing interest and principal. Calculate both borrower cash cost and lender cash flows under stated expected maturity.

Compare extension with refinancing using cash proceeds rather than face amount. Include underwriting fees, new OID, redemption premium, hedge cost, transaction expense and any retained non-extending debt.

Source note (retrieved 12 July 2026): PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>; PS23: eCFR, 26 CFR 1.1273-1 and 1.1275-2, <https://www.ecfr.gov/current/title-26/part-1/section-1.1273-1>.

23.7 OID and tax boundary

OID means debt is issued or treated for commercial modelling at a cash amount below face. An extension or exchange can create separate tax questions, including qualified-reopening or modification analysis in relevant U.S. circumstances. Commercial arithmetic does not determine tax treatment.

Show face amount, cash received, fees and principal repayment independently. Route tax classification, timing and holder or issuer consequences to qualified tax counsel.

Source note (retrieved 12 July 2026): PS23: eCFR, 26 CFR 1.1273-1 and 1.1275-2, <https://www.ecfr.gov/current/title-26/part-1/section-1.1273-1>.

23.8 Maturity, weighted average life and amortisation

Extension changes contractual principal timing. Calculate weighted average life from scheduled principal dates under a stated formula, and recalculate after extension and amortisation changes. For CLO-held loans, the lender may separately test the amended asset under its own indenture.

A longer maturity can improve borrower runway while increasing lender duration. It can also create maturity subordination if non-extending or other debt is paid earlier. Show each class on one timeline.

Source note (retrieved 12 July 2026): PS14: Federal Reserve, CLOs in the Financial Accounts of the United States, <https://www.federalreserve.gov/econres/notes/feds-notes/collateralized-loan-obligations-in-the-financial-accounts-of-the-united-states-20190920.html>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

23.9 Covenants and collateral

An extension can leave covenants unchanged, amend them for one class, or combine extension with broader relief. Test debt, liens, investments, restricted payments, financial covenants, mandatory prepayment, guarantors and collateral. Identify whether releases or new priorities affect only one class.

The borrower should not treat lender participation as consent to every amendment. Separate extension election, fee acceptance and covenant vote in the documents and closing record.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

23.10 Intercreditor and ranking

A new extension class may need accession or confirmation under intercreditor arrangements. Record lien rank, payment rank, enforcement control, standstill, turnover and proceeds sharing. A shared-security label does not establish identical maturity or voting rights.

Test the downside with non-extending debt outstanding. If that debt matures first, the borrower may use cash that would otherwise support the extended class. If new money receives priority, show the recovery transfer.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

23.11 Non-extending lender position

A non-extending lender retains the rights stated in its instrument, subject to valid amendments and the continuing capital structure. Its earlier maturity can be an advantage if paid, but can also create refinancing or default risk. Changes to collateral, covenants, voting or new debt can affect expected recovery.

Prepare a before-and-after schedule for principal, maturity, coupon, amortisation, voting share, collateral, priority and downside recovery for each lender class.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

23.12 Replacement-lender and disenfranchisement mechanics

Agreements can address replacement of lenders in specified circumstances and voting treatment for affiliates, defaulting lenders or other categories. The precise trigger, price, assignment, consent and timing come from the document. These mechanisms should not be described as a general power to remove dissent.

For a proposed extension, identify which lenders may be replaced or excluded from a vote, who determines eligibility and what evidence is required. Model the resulting denominator.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

23.13 Purchases, auctions and cancellation

A borrower or affiliate can acquire debt through methods permitted by the agreement, potentially including open-market purchases or Dutch auctions. Record purchase method, price, eligible sellers, cancellation, voting and pro rata implications. A purchase label does not answer whether the transaction can also change priority.

The capital-structure schedule should reduce principal only when the document provides for cancellation or another recognised treatment. Treasury or affiliate-held debt may have separate voting rules.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS21: Fifth Circuit, revised Serta Simmons opinion, No. 23-20451, <https://www.ca5.uscourts.gov/opinions/pub/23/23-20451-CV0.pdf>.

23.14 Consent payments and exit consents

Consent payments and exit consents require analysis of the exact instrument, solicitation, amendments and governing law. The Assenagon and Azevedo judgments are primary sources for their specific facts and holdings. They do not establish one rule for every transaction.

Prepare a primary-record table with payment or amendment facts, holder choice, legal issue, holding and limits. Counsel should assess any proposed consent structure. The economic model should show the position of participating and non-participating holders after the amendment.

Source note (retrieved 12 July 2026): PS24: BAILII, Assenagon v Irish Bank Resolution Corporation, <https://www.bailii.org/ew/cases/EWHC/Ch/2012/2090.html>; PS25: BAILII, Azevedo v Imcopa, <https://www.bailii.org/ew/cases/EWCA/Civ/2013/364.html>.

23.15 Response-deadline mechanics

Some agreements can specify consequences if a lender does not respond to a request within a defined process. The operative provision must state notice, response period, consequence, exclusions and safeguards. A colloquial label is not a substitute for the clause.

Fictional control specification: a request should identify the proposed action, complete documents, response deadline, delivery method, reminder process and consequence. Counsel must determine whether and how such a mechanism can be drafted and enforced.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>.

23.16 Structural adjustments

A structural adjustment can address redenomination, benchmark change, class mechanics or other operational restructuring under the document. It should not be used as an undefined route to alter ranking, principal or protected rights. Identify purpose, affected class, exchange rate, payment mechanics, voting and intercreditor effect.

Fictional control specification: a currency redenomination should state conversion date, published rate source, rounding, interest calculation, payment currency, hedge treatment and consent. Any priority or maturity change should be separately approved under the applicable rights.

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

23.17 Accounting and regulatory-capital boundary

Modification or extinguishment accounting depends on applicable standards, entity facts, cash-flow changes, fees and professional judgement. The financing team should provide complete old and new terms and cash flows to accounting specialists rather than state a generic result.

Regulatory-capital treatment depends on the regulated institution, exposure, rule, effective date and supervisory interpretation. CRR3 is a public legal source for its scope, but an extension does not produce one automatic capital outcome. Institution-specific analysis is required.

Source note (retrieved 12 July 2026): PS26: EUR-Lex, Regulation (EU) 2024/1623, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32024R1623>.

23.18 Closing and post-extension controls

The closing file should reconcile elections, lender holdings, class principal, fees, OID, maturity, amortisation, collateral, intercreditor accessions, votes and funds flow. Update the credit agreement, schedules, lender register, covenant model and maturity calendar.

After closing, track non-extending maturities, future refinancing, covenant divergence, call protection and interest cost. The extension should have milestones for the operating or capital action expected to solve the underlying maturity problem.

Source note (retrieved 12 July 2026): PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>.

Fictional teaching exercise: extension participation

Fictional facts. A EUR 500 million term loan matures in eighteen months. Lenders holding EUR 325 million elect to extend three years. The extended class receives a 75 basis point margin increase and a 1% extension fee; non-extendors retain the original maturity. Calculate the closing fee and class principals. If opening annual cash interest is based on a 7% all-in rate, calculate the incremental annual interest on the extended class from the margin increase only.

Now assume the borrower expects to repay EUR 100 million of non-extending debt from cash at original maturity. Build the maturity and minimum-cash schedule and identify any remaining refinancing gap.

Fictional teaching exercise: extension versus refinancing

Extension alternative: EUR 325 million extends with a 1% fee and 75 basis point margin increase; EUR 175 million remains due. Refinancing alternative: all EUR 500 million is refinanced at 98 OID with a 100 basis point higher margin and EUR 8 million of fees. Calculate immediate cash cost and cash proceeds for both alternatives, then model one year of incremental interest. State the assumptions needed to compare maturity certainty and call protection.

Fictional teaching exercise: lender class and voting

Before extension, one lender holds EUR 80 million of a EUR 500 million class. It extends EUR 50 million and leaves EUR 30 million unextended. Calculate its voting share in each new class if all extending principal is EUR 325 million and all non-extending principal is EUR 175 million. Then identify which future amendments require general, class or individual analysis under the fictional agreement.

Primary-record exercise: consent judgments

Using the Assenagon and Azevedo judgments only, create separate fact, issue, holding and limitation records. Do not merge the cases into one rule. Then write the unanswered questions that counsel must address for a new bond solicitation with different governing terms.

Practitioner review sequence

Diagnose maturity and liquidity first; compare cash repayment, refinancing, partial refinancing and extension on common assumptions.

Document eligible debt, elections, class formation, economics, maturity, amortisation, collateral, ranking and conditions.

Test protected rights, voting, intercreditor, replacement-lender, affiliate, purchase and consent mechanics from the selected documents.

Show extending and non-extending lenders separately through cash flow, voting, priority and downside recovery.

Route tax, accounting, regulatory capital and enforceability to qualified specialists; use primary judgments for case propositions.

Legal, tax, regulatory and accounting boundary

Finance and restructuring counsel must verify extension elections, class and maturity mechanics, ranking, protected rights, intercreditor terms, replacement and voting provisions, purchases, consent solicitations, response deadlines and structural adjustments. Tax, accounting and regulatory-capital conclusions require separate qualified specialists.

Primary-source map

Source note (retrieved 12 July 2026): PS06: SEC EDGAR, MeridianLink 2021 credit agreement, <https://www.sec.gov/Archives/edgar/data/1834494/000183449421000021/exhibit101-creditagreement.htm>; PS07: SEC EDGAR, Carnival 2023 secured-notes indenture, <https://www.sec.gov/Archives/edgar/data/815097/000081509723000066/exhibit103q32023.htm>; PS14: Federal Reserve, CLOs in the Financial Accounts of the United States, <https://www.federalreserve.gov/econres/notes/feds-notes/collateralized-loan-obligations-in-the-financial-accounts-of-the-united-states-20190920.html>; PS21: Fifth Circuit, revised Serta Simmons opinion, No. 23-20451, <https://www.ca5.uscourts.gov/opinions/pub/23/23-20451-CV0.pdf>; PS22: SEC EDGAR, Genuine/HireRight 2023 extension amendment, <https://www.sec.gov/Archives/edgar/data/1859285/000185928523000174/exhibit101-93023.htm>; PS23: eCFR, 26 CFR 1.1273-1 and 1.1275-2, <https://www.ecfr.gov/current/title-26/part-1/section-1.1273-1>; PS24: BAILII, Assenagon v Irish Bank Resolution Corporation, <https://www.bailii.org/ew/cases/EWHC/Ch/2012/2090.html>; PS25: BAILII, Azevedo v Imcopa, <https://www.bailii.org/ew/cases/EWCA/Civ/2013/364.html>; PS26: EUR-Lex, Regulation (EU) 2024/1623, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32024R1623>.

Guarantee and Collateral Architecture

24.0 Scope, date and professional boundary

This chapter is a finance-side teaching framework current to **12 July 2026**. It is not an opinion on the validity, perfection, priority, avoidance, release or enforcement of a guarantee or security interest. Those results depend on the governing law, the relevant entity, the asset, the transaction documents, registration and control steps, insolvency law and the facts at the relevant time. Qualified counsel in each relevant jurisdiction must own those conclusions.

Every company, document term, asset and amount below is fictional. The examples are not derived from a client, issuer, mandate, credit agreement, intercreditor agreement or private conversation. The chapter intentionally avoids named transaction anecdotes and does not reproduce market-form drafting.

The public authorities cited here illustrate why a disciplined secured-finance analysis separates creation, third-party effectiveness, priority and enforcement. They do not supply a universal cross-border answer. The UNCITRAL Model Law on Secured Transactions (https://uncitral.un.org/en/texts/securityinterests/modellaw/secured_transactions), for example, is a model text rather than the domestic law of every jurisdiction. In England and Wales, company-charge registration is addressed in Companies Act 2006 section 859A (<https://www.legislation.gov.uk/ukpga/2006/46/section/859A>) and consequences of non-registration are addressed in section 859H (<https://www.legislation.gov.uk/ukpga/2006/46/section/859H>). The operative domestic law and current advice control.

24.1 Learning objectives

After working through this chapter, the reader should be able to:

- ✦ 1. distinguish a guarantee from a security interest and state what each one does and does not establish;
- ✦ 2. map borrowers, issuers, guarantors, non-guarantors, asset owners, secured obligations and collateral pools before using a coverage percentage;
- ✦ 3. test creation, perfection or third-party effectiveness, priority, enforcement control, turnover and payment blockage as separate fields;
- ✦ 4. calculate guarantor coverage and structural-subordination sensitivities without double counting value;
- ✦ 5. trace accession, transfer and release mechanics through the life of an entity and asset; and
- ✦ 6. prepare a finance-side diligence pack that exposes open legal questions rather than replacing counsel.

Cross-references: capital structure in Chapter 8; credit-agreement reading in Chapter 12; covenant architecture in Chapter 14; debt and lien capacity in Chapter 18; asset sales and change of control in Chapter 19; events of default in Chapter 20; liability-management exercises in Chapter 22; and distressed recoveries in Chapter 26.

24.2 Core definitions

The labels below are analytical definitions for this chapter. They must be conformed to the selected documents and law before use in a transaction.

Term	Finance-side meaning	What remains to be proved
Guarantee	A contractual promise by one entity to answer for specified obligations of another	capacity, authority, scope, limitations, defenses, validity and enforceability
Security interest	A proprietary or similar interest intended to secure performance of an obligation	creation, attachment, asset description, perfection or third-party effectiveness, priority and enforcement
Collateral	The assets or rights stated to support secured obligations	ownership, existence, value, exclusions, competing rights and realizability
Perfection / third-party effectiveness	The steps required for the interest to have the intended effect against specified third parties	governing law, correct filing, registration, possession, control, notice and timing
Control	A legal or contractual form of control over an asset or enforcement process	whether the required control arrangement exists and is effective
Guarantor coverage	A stated metric comparing selected guarantor activity or assets with the selected group denominator	numerator, denominator, exclusions, measurement date and source quality
Structural subordination	The economic effect of value and claims sitting at different legal entities	entity ownership, local claims, guarantees, collateral and permitted cash movement
Turnover	A contractual obligation to hand specified receipts to another creditor or agent	trigger, scope, exclusions, timing and enforcement
Payment blockage	A restriction on making or retaining specified payments during defined conditions	blocked payments, trigger, duration, cure and permitted payments
Release condition	A condition under which a guarantee or security interest is stated to end or be released	satisfaction, evidence, agent mechanics and local filings
Accession	A process by which an entity becomes party to specified finance documents	required documents, approvals, representations, registrations and completion date

One vocabulary discipline prevents many errors: **ranking**, **security**, **guarantee** and **control** are not synonyms. A claim can rank senior as a contractual matter yet have limited collateral. A guarantee can add an obligor without giving an asset-specific priority. A security interest can exist while enforcement is controlled by another creditor group. An intercreditor turnover obligation may reallocate a receipt without changing the original claim's legal source.

24.3 The five-field credit-support test

Every credit-support statement should be decomposed into five fields.

Field	Question	Minimum evidence	Typical unresolved issue
Claim	Which entity owes which obligation to whom?	debt document, guarantee, accession record	obligation or guarantor limitation
Asset	Which entity owns the asset and is it within the collateral description?	asset register, title evidence, security document	excluded asset or ownership mismatch
Effectiveness	Which steps make the interest effective against the relevant third party?	filings, registrations, control or possession evidence	wrong jurisdiction, late step or lapsed record
Priority	Which competing claims or interests rank ahead, equally or behind?	lien search, intercreditor agreement, statutory priority analysis	local priority, set-off or statutory claim
Enforcement	Who can act, when and how are proceeds applied?	enforcement provisions, standstill and waterfall	control threshold, turnover or release dispute

This approach is deliberately stricter than saying that a facility has an “all-assets” package. That phrase does not identify the entities, excluded assets, local formalities, control arrangements, prior liens, statutory claims or enforcement route. The finance team should treat the phrase as a hypothesis to be tested, not as a completed conclusion.

24.4 Synthetic perimeter and guarantor-coverage calculations

Example 1: Arcstone Services group

Arcstone Holdings owns three operating subsidiaries. All amounts are selected teaching inputs in EUR millions.

Entity	Role	EBITDA	Total assets	Local funded debt	Guarantee status	Selected collateral
Arcstone Borrower	borrower	28	140	120	primary obligor	material movable assets and bank accounts, subject to exclusions
Delta Operations	guarantor	22	90	15	guarantor	receivables and equipment, subject to local steps
Harbor Distribution	non-guarantor	15	80	25	none	none for the facility
Meridian Software	guarantor	10	60	5	guarantor	shares and selected IP rights, subject to local review
Group		75	370	165		

Calculation 1: stated EBITDA coverage

If the selected metric includes the borrower and two guarantors, covered EBITDA is:

$$28 + 22 + 10 = \text{EUR } 60 \text{ million.}$$

Stated EBITDA coverage is:

$$60 / 75 = 80.0\%.$$

The percentage is mathematically correct for the selected data. It does not prove that 80% of enterprise value is available to the lenders. EBITDA can sit in entities with different assets, local claims, taxes, pension exposure, leases, working-capital needs and restrictions on cash movement.

Calculation 2: denominator and exclusion sensitivity

Assume the agreement's covenant report excludes a newly acquired non-guarantor with EUR 8 million of EBITDA during a grace period. A report that continues to use the old EUR 75 million denominator still shows 80.0%. The economic group denominator after acquisition is EUR 83 million, so economic coverage is:

$$60 / 83 = 72.3\%.$$

If the new entity later accedes as a guarantor, and its full EUR 8 million is included, coverage becomes:

$$68 / 83 = 81.9\%.$$

The lesson is not that one denominator is legally correct. The lesson is that the report must state whether it measures covenant compliance, economic perimeter or both. A grace period, immaterial-subsidary test, excluded-subsidary category or ownership threshold can create a valid documentary exclusion while still changing recovery risk.

Example 2: asset-coverage downside

The selected gross asset base of the borrower and guarantors is EUR 290 million. Counsel and the collateral team identify EUR 35 million of excluded assets, EUR 20 million of assets subject to prior liens and EUR 25 million of assets whose local perfection evidence is incomplete. A conservative finance-side “tested asset pool” is therefore:

$$290 - 35 - 20 - 25 = \text{EUR } 210 \text{ million.}$$

Compared with EUR 140 million of selected first-lien claims, the gross tested-asset ratio is:

$$210 / 140 = 1.50x.$$

This is not a liquidation recovery. It ignores realization discounts, priority costs, taxes, employee and pension claims, set-off, litigation, timing and enforcement expense. It is a diligence bridge showing where the nominal package narrows.

24.5 Asset lifecycle and effectiveness controls

Security analysis should follow the asset, not stop at closing. Assets are acquired, sold, substituted, transformed, moved between entities, deposited in new accounts, licensed, commingled or replaced by proceeds. Each event can alter ownership, collateral description, perfection steps, priority or release.

Lifecycle event	Finance question	Evidence to obtain	Counsel question
New subsidiary acquired	Is it inside the guarantor and collateral perimeter?	ownership chart, materiality test, accession timetable	obligation to accede; local limitations
Receivable generated	Is it covered and free of conflicting transfer restrictions?	receivables ledger, contract sample, filing/control evidence	creation, priority and anti-assignment effect
Bank account opened	Is it a collateral account and subject to required control?	bank list, account agreement, control record	effective control and competing bank rights
Equipment moved	Does relocation change governing law or registration?	asset register, location log	conflict-of-laws and new perfection step
Asset sold	Is sale permitted and is release automatic or conditional?	sale approval, proceeds path, release certificate	satisfaction of release conditions
IP licensed or transferred	Does value remain in the credit group and collateral pool?	licence/transfer record, valuation, entity map	ownership, security scope and release

In England and Wales, the public company-charge regime illustrates the importance of registration and timing; section 859A (<https://www.legislation.gov.uk/ukpga/2006/46/section/859A>) provides the registration route, while section 859H (<https://www.legislation.gov.uk/ukpga/2006/46/section/859H>) addresses consequences against a liquidator, administrator or creditor when a registrable charge is not delivered within the permitted period. That example must not be generalized to another jurisdiction or another asset category.

The same discipline applies to releases. A covenant may permit a disposition, but permission to sell does not by itself answer whether a security release is automatic, conditional, agent-driven or dependent on delivery of certificates and local filings. Chapters 18 and 19 should be read together with the release provisions and the asset-specific security documents.

24.6 Structural subordination and claim allocation

Structural subordination begins with separate legal entities. A parent creditor normally cannot assume direct access to a subsidiary's asset value merely because the subsidiary is consolidated in the accounts. The

practitioner should model each entity's assets and claims, upstreamable residual value and any guarantee or collateral path.

Calculation 3: entity-level residual

Assume Harbor Distribution, the non-guarantor, has selected realizable asset value of EUR 55 million. Before any upstream value, it faces:

- ♦ • EUR 25 million local funded debt;
- ♦ • EUR 8 million selected trade and employee claims; and
- ♦ • EUR 4 million realization and wind-down costs.

The simplified residual is:

$$55 - 25 - 8 - 4 = \text{EUR } 18 \text{ million.}$$

If only 70% of that residual is assumed to reach the parent after timing, tax and execution sensitivity, modelled upstream value is:

$$18 \times 70\% = \text{EUR } 12.6 \text{ million.}$$

The 70% is a selected finance assumption, not a legal conclusion. It must be replaced by a jurisdiction- and fact-specific view. No consolidated waterfall should also allocate the full EUR 55 million to the secured group; that would double count the same value.

The U.S. Bankruptcy Code offers another public illustration of the difference between a claim and collateral value: 11 U.S.C. section 506 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section506>) addresses secured status by reference to the value of the creditor's interest in the estate's interest in property. The statute and case-specific orders control in a U.S. case; the teaching point here is simply that the word "secured" does not make collateral value unlimited.

24.7 Intercreditor architecture

Four questions should be recorded separately.

Question	What to extract	Finance-side effect
Ranking	debt and lien ranking by claim and collateral pool	expected priority in value allocation
Control	who may direct enforcement, give instructions or release collateral	timing and process leverage
Turnover	receipts that must be handed over and permitted exceptions	cash retained versus redirected
Payment blockage	payments that cannot be made or kept during specified conditions	liquidity and debt-service constraints

A "first lien" label does not answer who controls enforcement. Pari passu liens do not necessarily mean identical guarantees, maturity, voting or economics. A junior creditor may be blocked from enforcement yet retain voting, information or litigation leverage. Conversely, a senior creditor can be economically covered but constrained by notice, standstill or agent mechanics.

Calculation 4: fictional collateral-proceeds waterfall

Assume EUR 130 million of gross proceeds from one collateral pool and the following selected ordering:

Step	Claim	Amount (EURm)	Paid (EURm)	Remaining proceeds (EURm)
1	enforcement and agent costs	7	7	123
2	first-out revolving claim	25	25	98
3	pari passu term claims	120	98	0
4	second-lien claim	40	0	0

The selected term-claim collateral recovery is $98 / 120 = 81.7\%$. The second-lien collateral recovery is zero in this pool. Neither result determines the creditors' total recovery: deficiency claims, guarantees, other collateral pools, negotiated plan value and disputed claims require separate analysis. The stated ordering is invented and does not describe any market form.

24.8 Accession, transfer and release

Example 3: acquisition and later disposition

Arcstone acquires Nova Testing, which contributes EUR 12 million of EBITDA and owns EUR 45 million of assets. The fictional agreement gives 60 days to complete specified accession and collateral steps, subject to documented exclusions. The closing report should show Nova in three states:

- ✦ 1. **Economic perimeter:** included from acquisition because Arcstone owns it.
- ✦ 2. **Covenant perimeter:** included or excluded according to the operative definitions and pro forma rules.
- ✦ 3. **Credit-support perimeter:** not treated as a completed guarantor until the required accession, authority, security and registration evidence is delivered.

On day 20, economic EBITDA is EUR 87 million but guaranteed EBITDA remains EUR 60 million. Economic coverage is $60 / 87 = 69.0\%$. If Nova completes accession on day 55, coverage becomes $72 / 87 = 82.8\%$, subject to the agreement's actual calculation rules.

Two years later, Arcstone sells Nova under a permitted disposition. The finance team should not mark the guarantee and collateral as released merely because the sale is permitted. It should obtain the release request, condition evidence, agent confirmation, proceeds application and local filing or register updates. The covenant permission, release mechanics and use of proceeds are linked but distinct tests.

Event	Required finance evidence	Status label
acquisition closes	ownership and consideration bridge	economic perimeter updated
accession due	obligation and deadline tracker	open until completed or waived
guarantee delivered	executed accession/guarantee evidence	counsel confirmation pending
security steps completed	asset schedule and filing/control evidence	asset-by-asset status
entity sold	permitted-disposition analysis	permission does not equal release
release completed	agent evidence and local updates	released only when verified

24.9 Practitioner deliverable

The minimum finance-side pack is:

Deliverable	Required fields	Primary owner
entity and claim map	entity, borrower/guarantor role, debt, assets, local claims	finance with counsel review
guarantor-coverage bridge	numerator, denominator, exclusions, date and source	finance
collateral matrix	asset, owner, document, effectiveness step, priority, release status	counsel/collateral team with finance tie-out
intercreditor summary	ranking, control, turnover, blockage and voting	counsel with finance read-through
lifecycle tracker	acquisition, accession, post-closing step, transfer and release deadline	transaction team
recovery sensitivities	entity residuals, collateral pools, costs, delays and deficiencies	finance/valuation with counsel flags

Every row should have an owner, date, source and status. Use “not yet verified” where evidence is missing. Do not convert a legal question into a zero, a blank cell or a confident narrative assumption.

24.10 Exercises and answer checks

Exercise 1: denominator discipline

The borrower and guarantors produce EUR 72 million of EBITDA. The consolidated group produces EUR 96 million, including EUR 9 million from a newly acquired entity still within an accession period and EUR 15 million from a permanently excluded non-guarantor.

- ♦ 1. Calculate economic guarantor coverage.
- ♦ 2. Calculate coverage excluding the accession-period entity from the denominator.
- ♦ 3. State why neither result proves recovery coverage.

Answer check. Economic coverage is $72 / 96 = 75.0\%$. The stated covenant-style denominator excluding the EUR 9 million entity is EUR 87 million, giving $72 / 87 = 82.8\%$, if the operative definitions permit that treatment. Neither result identifies asset ownership, local claims, collateral, effectiveness, priority or enforcement.

Exercise 2: release and double counting

A non-guarantor subsidiary has EUR 70 million of selected realizable value, EUR 30 million local debt, EUR 10 million other local claims and EUR 5 million costs. The model assumes 80% of residual value can be upstreamed. Separately, a consolidated recovery model allocates the full EUR 70 million to group collateral.

- ♦ 1. Calculate the selected upstream value.
- ♦ 2. Identify the modelling error.
- ♦ 3. List the release evidence needed if the subsidiary is sold.

Answer check. Residual value is $70 - 30 - 10 - 5 = \text{EUR } 25 \text{ million}$; selected upstream value is $25 \times 80\% = \text{EUR } 20 \text{ million}$. Allocating the full EUR 70 million elsewhere double counts the subsidiary value. A sale analysis should obtain permitted-disposition support, release-condition evidence, agent confirmation, proceeds treatment and required local filing/register updates.

24.11 Primary-source register and publication gate

Primary/public sources checked for this teaching draft on 12 July 2026:

- ✦ • UNCITRAL Model Law on Secured Transactions (https://uncitral.un.org/en/texts/securityinterests/modellaw/secured_transactions) - conceptual secured-transactions framework; not domestic law by itself.
- ✦ • Companies Act 2006 section 859A (<https://www.legislation.gov.uk/ukpga/2006/46/section/859A>) and section 859H (<https://www.legislation.gov.uk/ukpga/2006/46/section/859H>) - selected England-and-Wales company-charge registration context.
- ✦ • Insolvency Act 1986 section 245 (<https://www.legislation.gov.uk/ukpga/1986/45/section/245>) and section 176A (<https://www.legislation.gov.uk/ukpga/1986/45/section/176A>) - selected floating-charge and prescribed-part context; counsel must apply current consolidated law and facts.
- ✦ • 11 U.S.C. section 506 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section506>) - selected U.S. secured-claim context, not a general collateral opinion.

Publication requires exact-hash legal/compliance review of the final text. Any change to the examples, source date, jurisdictions, legal descriptions or calculations requires affected QA and review to be refreshed.

UK Restructuring Tools

25.0 Scope, date and legal boundary

This chapter covers the finance-side use of **Part 26 schemes of arrangement** and **Part 26A restructuring plans** under the Companies Act 2006 in **England and Wales**. The statutory summaries and primary-source links were checked on **12 July 2026**. They are educational orientations, not legal advice. The current consolidated legislation, procedural rules, court orders and judgments must be checked for a real matter.

Eligibility, jurisdiction, class composition, notice, voting entitlement, sanction, fairness, effectiveness, recognition, contract treatment and enforcement are legal conclusions for qualified England-and-Wales restructuring counsel. Where assets, entities, claims or counterparties sit outside the forum, local advice is required. In line with the owner-approved scope, this chapter uses a neutral recognition framework and does not state the law of any additional foreign jurisdiction.

All companies, claims, values, votes, documents, proposals and dates in the examples are fictional. No private mandate, client fact, quotation, personal experience or named restructuring is used.

25.1 Learning objectives

After completing this chapter, the reader should be able to:

- ♦ 1. distinguish the Part 26 and Part 26A statutory routes and explain why neither is only a vote-counting exercise;
- ♦ 2. map the convening, information, class, voting and sanction sequence for each route;
- ♦ 3. build a claim-level relevant-alternative and no-worse-off model using consistent valuation dates, costs, timing and assumptions;
- ♦ 4. separate legal eligibility and court discretion from finance evidence and implementation feasibility;
- ♦ 5. prepare a neutral cross-border effectiveness matrix without assuming that an England-and-Wales order has a universal foreign effect;
- ♦ 6. test standstill, supply, guarantee, security, intercreditor and cash implications alongside the proposed compromise; and
- ♦ 7. manage stakeholder, adviser, liquidity and implementation workstreams through a dated control plan.

Cross-references: events of default in Chapter 20; liability-management exercises in Chapter 22; amend-and-extend transactions in Chapter 23; guarantees and collateral in Chapter 24; distressed debt in Chapter 26; credit analysis in Chapter 27; and secondary-market/claims operations in Chapter 38.

25.2 Definitions and route discipline

Term	Controlled teaching definition	Required legal confirmation
Scheme of arrangement	A compromise or arrangement pursued under Part 26 of the Companies Act 2006	company eligibility, jurisdiction, class composition, statutory process and sanction
Restructuring plan	A compromise or arrangement pursued under Part 26A for a company within the statutory financial - difficulty gateway	gateway, classes, process, voting, sanction and any cross - class route
Class composition	Grouping of creditors or members for meeting and voting purposes	rights and differences relevant to consultation together; court determination
Convening stage	The stage at which the court is asked to direct meetings or otherwise address the proposed class process	evidence, notice, class issues and procedural directions
Sanction	Court approval of the compromise or arrangement after the relevant process	statutory compliance, discretion, fairness and order terms
Financial - difficulty gateway	The Part 26A threshold in section 901A (https://www.legislation.gov.uk/ukpga/2006/46/section/901A)	current law and company - specific evidence
Cross - class cram - down	The potential Part 26A route under section 901G (https://www.legislation.gov.uk/ukpga/2006/46/section/901G) despite a dissenting class	satisfaction of statutory conditions and court discretion
Relevant alternative	What the court considers most likely to occur if the plan is not sanctioned	evidence, valuation, timing, feasibility and legal analysis
No worse off	The statutory condition focused on members of a dissenting class compared with the relevant alternative	claim - level application, valuation and court determination
Sufficient connection	A jurisdictional concept used in considering whether the court should exercise jurisdiction	fact - specific legal analysis; not created mechanically by one document change
COMI	Centre of main interests, a concept used in certain cross - border insolvency frameworks	forum - specific facts and law; not a universal recognition answer
Recognition	Effect given by another forum to a proceeding, order or compromise	local law, public policy, due process, affected claim and enforcement route
Standstill	Contractual or statutory restriction on specified creditor action for a defined period	scope, parties, trigger, exceptions, expiry and remedy
Ipso - facto protection	A restriction on specified contractual termination or other action because of insolvency - related events	statute, contract, exclusions, safeguards and counterparty facts

The finance team should not use “scheme,” “plan,” “cram-down,” “moratorium” or “recognition” as interchangeable process labels. Each has its own source, perimeter and effect. A successful vote is not a sanction order. A sanction order is not evidence of foreign effectiveness. A finance model cannot decide class composition or court discretion.

25.3 Start with the problem and decision gates

Before selecting a route, define the problem to be solved.

Problem	Finance evidence	Legal/process question	Failure if ignored
maturity or payment cliff	13-week cash flow, maturity schedule, debt service	required consent or compromise route	insolvency before implementation
unsustainable leverage	operating cases, valuation and debt capacity	claims and rights to be altered	plan that does not create a viable capital structure
holdout class	holder register, rights map, vote scenarios	class composition and available binding route	failed vote or challenge
new-money need	sources/uses, priority, collateral and runway	authority, priority, consent and conditions	unfunded implementation
guarantee/security change	entity and collateral maps	release, continuation, accession and local effect	value leakage or incomplete implementation
cross-border claims/assets	jurisdiction matrix	local recognition or parallel step	order effective in one forum but not where needed

The decision gates are sequential:

- ♦ 1. **Eligibility and jurisdiction:** can the selected company use the route and should the court exercise jurisdiction?
- ♦ 2. **Class architecture:** which rights are being compromised and which creditors can consult together?
- ♦ 3. **Information and valuation:** can affected stakeholders test the proposal and the alternative?
- ♦ 4. **Vote:** has each class met the correct statutory threshold?
- ♦ 5. **Sanction:** should the court exercise its discretion on the evidence and order presented?
- ♦ 6. **Effectiveness:** are conditions, filings, funding, recognition and document steps completed before liquidity runs out?

25.4 Part 26 scheme: statutory finance map

Part 26 of the Companies Act 2006 (<https://www.legislation.gov.uk/ukpga/2006/46/part/26>) provides the statutory route. Section 895 (<https://www.legislation.gov.uk/ukpga/2006/46/section/895>) introduces the compromise-or-arrangement framework; section 896 (<https://www.legislation.gov.uk/ukpga/2006/46/section/896>) addresses the court-ordered meeting process; section 897 (<https://www.legislation.gov.uk/ukpga/2006/46/section/897>) addresses explanatory statements; and section 899 (<https://www.legislation.gov.uk/ukpga/2006/46/section/899>) addresses the agreement and court sanction mechanism. Counsel must apply the current provisions and any applicable procedural directions.

The finance-side sequence is:

Stage	Finance work	Counsel-led work	Control output
perimeter	reconcile entities, instruments, claims and affected rights	eligibility, jurisdiction and proposed compromise	scope memorandum
classes	compare rights before and under proposal	class composition and meeting structure	provisional class map
convening	prepare evidence on claims, valuation, liquidity and process	application, evidence and directions	court timetable and issues list
information	reconcile numbers across explanatory materials and model	legal disclosure requirements and notices	source-controlled creditor pack
meetings	reconcile admitted claims, attendance, proxies and votes	voting entitlement and meeting procedure	certified vote ledger
sanction	update valuation, fairness and implementation evidence	statutory compliance and court discretion	sanction evidence pack
effectiveness	fund, settle and implement document changes	order, conditions, filings and legal effect	closing checklist

Fictional Case 1: consensual scheme

Northbridge Components has two affected creditor classes: a revolving class and a term-loan class. Counsel has provisionally concluded that the rights require separate meetings. Selected claims and votes are:

Class	Claims present and voting (EURm)	Number voting	Yes value (EURm)	Yes voters	No value (EURm)	No voters
revolving	45	6	42	5	3	1
term loan	180	18	144	12	36	6

Calculation 1: scheme vote reconciliation

For the revolving class, yes value is $42 / 45 = 93.3\%$, and five of six voters support. For the term class, yes value is $144 / 180 = 80.0\%$, and 12 of 18 voters support.

On the selected data, each class exceeds 75% by value and has a majority in number among those present and voting. That is a finance reconciliation, not a legal certification. Counsel and the chair must determine entitlement, admission, proxies, class treatment and compliance with the statute and order. The court still decides sanction.

The model should also reconcile the denominator. If EUR 20 million of term claims did not vote, the 80.0% is measured against EUR 180 million present and voting, not EUR 200 million total outstanding. Reporting the result as 72.0% of total claims without explanation would use a different question and could mislead the reader.

Class construction: rights before labels

Class composition is not a spreadsheet clustering exercise. The starting point is the legal rights that each affected creditor holds before the compromise and the way those rights would be changed. Economic interests, recovery expectations and negotiating alignment can inform the evidence, but they do not replace the legal test. Two lenders with the same commercial label may have different guarantors, collateral, governing law, set-off rights, maturity, payment priority or recourse. Conversely, creditors with different coupons may still have rights sufficiently aligned for the selected analysis. Counsel owns the conclusion.

The finance team can make that legal work more reliable by producing a disciplined rights matrix:

Right field	Creditor A	Creditor B	Creditor C	Evidence source	Class relevance
primary obligor	Borrower	Borrower	Parent	executed debt instrument	entity recourse differs
guarantee	full selected group	full selected group	none	guarantees/accessions	recovery path differs
collateral	first lien pool	first lien pool	unsecured	security/intercreditor documents	priority differs
maturity	year 1	year 3	year 2	debt instrument	timing may affect rights
payment priority	pari passu	pari passu	structurally junior	instrument/entity map	relevant rights difference
proposed treatment	cash/debt mix	cash/debt mix	equity only	term sheet	compromise differs

This table is not a class opinion. It is a reconciliation that exposes the fields counsel must assess. Where the answer is unknown, the cell should say "open" and identify the required document. The team should not fill gaps with the proposed class label.

Information controls

The explanatory information should let an affected stakeholder understand the proposal, the rights altered, material assumptions, financial condition, valuation basis, relevant alternative and principal implementation risks. Section 897 (<https://www.legislation.gov.uk/ukpga/2006/46/section/897>) and section 901D (<https://www.legislation.gov.uk/ukpga/2006/46/section/901D>) are the primary statutory starting points for explanatory statements under the two routes. Counsel must determine the required content in the actual process.

Finance should operate a one-model rule. The board paper, valuation materials, explanatory statement, creditor presentation, vote ledger and implementation sources/uses should all reconcile to a controlled data set. At minimum, maintain:

- ♦ • a claims cut-off and bridge from ledger to voting schedule;
- ♦ • an entity and guarantee map tied to the relevant-alternative waterfall;
- ♦ • one forecast version with documented overlays;
- ♦ • a valuation bridge from enterprise value to distributable value;
- ♦ • a cost and timing schedule;
- ♦ • a schedule of disputed or contingent claims;
- ♦ • a log of changes after first circulation; and
- ♦ • a sign-off map showing who owns facts, calculations, legal descriptions and expert opinions.

If a downside forecast changes from a 15% revenue decline to a 20% decline, the team should not update only the headline recovery. It should update working capital, cash, financing need, valuation, relevant alternative, class recoveries, no-worse-off schedules and implementation runway. The change log should record the old and new assumptions and the reason.

25.5 Part 26A restructuring plan: gateway and process

Part 26A (<https://www.legislation.gov.uk/ukpga/2006/46/part/26A>) was inserted by the Corporate Insolvency and Governance Act 2020. Section 901A (<https://www.legislation.gov.uk/ukpga/2006/46/section/901A>) states the financial-difficulty and purpose gateway. Section 901C (<https://www.legislation.gov.uk/ukpga/2006/46/section/901C>) addresses the court-ordered meeting process; section 901D (<https://www.legislation.gov.uk/ukpga/2006/46/section/901D>) addresses explanatory statements; section 901F (<https://www.legislation.gov.uk/ukpga/2006/46/section/901F>) contains the class agreement and sanction route; and section 901G (<https://www.legislation.gov.uk/ukpga/2006/46/section/901G>) addresses sanction despite a dissenting class when its conditions are met. The official Corporate Insolvency and Governance

Act explanatory notes (<https://www.legislation.gov.uk/ukpga/2020/12/notes/division/6/index.htm>) provide additional public context, but the statute and current authorities control.

Feature	Part 26	Part 26A
gateway	no Part 26A financial-difficulty gateway	section 901A gateway and purpose
class approval	statutory value and number requirements for each class	75% in value of those present and voting in each approving class under section 901F
dissenting class	no Part 26A cross-class mechanism	potential section 901G route if conditions are met and court sanctions
relevant alternative	relevant to valuation/fairness evidence	central to the section 901G no-worse-off analysis
sanction	court order and discretion	court order and discretion, including on a cross-class route
recognition	forum-dependent analysis	forum-dependent analysis

Fictional Case 2: plan with a dissenting class

Sable Transit has four provisional classes. The figures are selected teaching inputs.

Class	Present-and-voting claim (EURm)	Yes value (EURm)	Yes percentage	Selected value in relevant alternative (EURm)
super-senior revolving	30	30	100.0%	30
first-lien term	170	136	80.0%	145
second-lien	90	54	60.0%	18
unsecured	40	34	85.0%	0

Calculation 2: plan voting

The second-lien class produces $54 / 90 = 60.0\%$, below the 75% value threshold. The other selected classes exceed 75%. The second-lien class is therefore dissenting on this teaching schedule. The result does not establish a section 901G outcome. Counsel and the court must determine class composition, claims admitted, whether the statutory conditions are met and whether sanction should be granted.

25.6 Relevant alternative and no-worse-off analysis

The relevant alternative is not a label selected to maximize support. It is the outcome the court considers most likely if the plan is not sanctioned. A model should therefore compare executable paths using one valuation date and transparent assumptions.

For Sable Transit, assume the selected relevant alternative is an accelerated sale after a three-month funding gap. The gross and net values are:

Item	Plan case (EURm)	Relevant alternative (EURm)	Evidence status
enterprise or sale value	340	285	selected valuation assumption
cash available at completion	12	8	liquidity model
new - money repayment	(30)	0	proposal term
process and professional costs	(12)	(20)	scoped assumption
trading and delay erosion	0	(15)	downside assumption
net distributable value	310	258	calculated

Calculation 3: net value and class waterfall

Plan value is $340 + 12 - 30 - 12 = \text{EUR } 310$ million. Relevant-alternative value is $285 + 8 - 20 - 15 = \text{EUR } 258$ million.

Assume for teaching purposes that both values are allocated in the following simplified order before negotiated equity or contingent value:

Class	Claim (EURm)	Plan value (EURm)	Relevant - alternative value (EURm)	Plan recovery	Alternative recovery
super - senior revolving	30	30	30	100.0%	100.0%
first - lien term	170	170	170	100.0%	100.0%
second - lien	90	90	58	100.0%	64.4%
unsecured	40	20	0	50.0%	0.0%

The waterfall is an invented finance model. It does not prove legal priority, claim allowance or the treatment the court would accept. It also does not establish the no-worse-off condition merely because the class average is higher. The analysis must be claim-level. Different members may have guarantees, set-off, security, contingent claims, contractual priorities, currencies or entity exposures that make an average comparison inadequate.

Valuation evidence architecture

The relevant-alternative model should show why the selected outcome is more likely than the plausible alternatives, not merely why it produces the lowest comparator. A useful structure is:

- ✦ 1. identify executable alternatives at the decision date;
- ✦ 2. state the operational and funding conditions for each;
- ✦ 3. estimate timing, costs and value using comparable assumptions;
- ✦ 4. assign probabilities only where the evidence supports them;
- ✦ 5. test which alternative is most likely, rather than averaging all outcomes into a synthetic process; and
- ✦ 6. preserve sensitivities so counsel and the valuation expert can test the conclusion.

For teaching, assume Sable Transit has three possible outcomes if the plan is not sanctioned:

Outcome	Selected probability	Gross value (EURm)	Costs/delay leakage (EURm)	Net value (EURm)	Execution evidence
accelerated going - concern sale	55%	285	27	258	buyer interest and interim funding assumed
administration sale after interruption	30%	245	35	210	lower continuity and higher costs
consensual extension	15%	300	18	282	insufficient creditor support on selected facts

The table does not establish the relevant alternative. It shows that the accelerated sale has the highest selected probability and should be tested as the most-likely comparator, while the other cases remain sensitivities. A probability-weighted average of $55\% \times 258 + 30\% \times 210 + 15\% \times 282 = \text{EUR } 247.2$ million may be useful for risk analysis, but it is not automatically the statutory comparator. Counsel and the valuation expert must determine how the legal test applies.

Timing consistency

Values should be compared at a common date or explicitly discounted. Suppose the plan distributes EUR 310 million at the end of month 3, while the selected alternative distributes EUR 258 million at the end of month 12. At a selected 12% annual discount rate, simplified present values at launch are:

- ♦ • plan: $310 / (1.12^{0.25}) = \text{EUR } 301.3$ million; and
- ♦ • alternative: $258 / 1.12 = \text{EUR } 230.4$ million.

The discount rate is invented. It does not decide the legal comparator or valuation methodology. It demonstrates why undiscounted numbers at different dates are not directly comparable. If costs, claim interest or interim distributions are included, apply them consistently to each case.

Valuation control checklist

Control	Required question	Failure prevented
valuation date	are plan and alternative measured from the same date?	timing mismatch
perimeter	are entities, assets, guarantees and claims consistent?	value/claim mismatch
operating case	do revenue, margin, capex and working capital reconcile?	incompatible forecasts
costs	are adviser, financing, sale and wind-down costs included?	gross-value overstatement
liquidity	can the alternative survive until execution?	impossible comparator
probability	is the most-likely path evidenced?	result-driven selection
claim mapping	does each holder receive value from the correct entity/claim?	class-average distortion
sensitivity	what changes the comparator or no-worse-off result?	false precision

Claim-level control

Holder	Class claim (EURm)	Plan value (EURm)	Alternative value (EURm)	Difference	Open issue
Second-lien A	50	50	32	18	confirm identical guarantee and collateral rights
Second-lien B	25	25	20	5	possible set-off requires counsel review
Second-lien C	15	15	6	9	disputed interest component

An average class recovery cannot resolve the open issues. The schedule must tie to the claims register, entity map and counsel's rights analysis.

25.7 Court discretion, evidence and fairness

Meeting the arithmetic threshold does not compel sanction. The finance team should support counsel and the court process with a controlled evidence pack rather than predict an outcome.

Evidence should include:

- ✦ • a reconciled historical and forecast financial base;
- ✦ • current liquidity, weekly cash flow and implementation runway;
- ✦ • a source-backed valuation range, not one point estimate;
- ✦ • the capital structure and claim register by entity;
- ✦ • the rights affected and consideration offered by class;
- ✦ • the relevant-alternative model, including timing, costs and feasibility;
- ✦ • vote reconciliation and holder/claim changes through the record date;
- ✦ • management, shareholder, sponsor and new-money contributions;
- ✦ • implementation steps, conditions and risks; and
- ✦ • a list of disputed facts and sensitivities.

The same number should not change between the valuation report, explanatory materials, board paper, creditor presentation and vote schedule without a documented bridge. If a forecast is updated, the team should record the source, reason, affected classes and whether supplemental information or adjournment advice is required.

25.8 Liquidity runway and implementation risk

Fictional Case 3: a plan that risks running out of cash

Elm Quay Foods starts with EUR 24 million of unrestricted cash. Weekly operating outflow is EUR 2.5 million before a EUR 6 million payroll and tax payment in week 5. Minimum operating cash is EUR 5 million.

Calculation 4: runway

After four weeks, cash is $24 - (4 \times 2.5) = \text{EUR } 14$ million. After the week-5 ordinary outflow and the EUR 6 million payment, cash becomes $14 - 2.5 - 6 = \text{EUR } 5.5$ million. The company is only EUR 0.5 million above minimum cash.

If sanction or funding completion slips by one week, another EUR 2.5 million outflow takes cash to EUR 3.0 million, below the selected minimum. A plan that is financeable at week 5 can fail at week 6.

Workstream	Base completion	Downside completion	Cash impact	Control response
convening/order	week 1	week 2	(2.5)	prepare evidence and resolve class issues early
creditor information/vote	week 3	week 4	(2.5)	lock data, claims and notice plan
sanction	week 5	week 6	(2.5)	reserve hearing and conditions plan
new money	sanction date	three days later	variable	escrow, conditions and fallback funding
implementation	same day	one week later	(2.5) plus fees	detailed closing checklist

The timetable is invented and is not a forecast of court availability. The finance conclusion is limited: timing has cash consequences and must be modelled. Counsel owns procedural timing; management owns the cash forecast; funding parties own commitment conditions.

25.9 Standstill, supply, security and intercreditor workstreams

A scheme or plan does not automatically create every protection that a stressed company needs. Contractual standstills, waivers, forbearance, the Part A1 moratorium and restrictions on termination of certain supply contracts

are distinct tools and require separate analysis. The public statutory sources include Part A1 of the Insolvency Act 1986 (<https://www.legislation.gov.uk/ukpga/1986/45/part/A1>) and section 233B (<https://www.legislation.gov.uk/ukpga/1986/45/section/233B>). Counsel must assess scope, eligibility, exclusions, safeguards and facts.

Topic	Finance question	Legal/document question	Required evidence
standstill	how much runway is purchased and at what cash cost?	parties, trigger, duration, exceptions and remedies	executed agreement and cash model
supply continuity	which suppliers are operationally critical?	statutory/contractual rights and exclusions	contract map and supplier plan
guarantee amendment	which claims and entities change?	consent, compromise and foreign effect	guarantee/entity matrix
security release or continuation	what collateral supports the post-plan debt?	release conditions, priority and filings	collateral and release checklist
intercreditor change	who controls enforcement and receives value?	voting, turnover, blockage and sacred rights	operative intercreditor agreement
new money	how much, when and on what downside assumptions?	authority, priority, collateral and conditions	sources/uses and commitment evidence

Permission under one covenant is not proof that another document, security interest or guarantee has changed. Chapters 18, 20, 22 and 24 should be reconciled to the operative documents.

25.10 Neutral cross-border effectiveness framework

The owner-approved scope does not name additional foreign jurisdictions. Use placeholders until qualified local advice is available.

Forum	Entity/asset/claim	Proposed England-and-Wales effect	Local question	Evidence owner	Status
Forum A	operating subsidiary guarantee	amend guarantee obligation	recognition, due process and enforceability	local counsel	open
Forum B	real estate collateral	continue or release security	local registration and insolvency effect	local counsel	open
Forum C	notes through a clearing system	compromise claim	governing law, holder mechanics and recognition	local counsel/operations	open
Forum D	cash account	apply or preserve security	control, set-off and transfer restriction	local counsel/treasury	open

Do not treat COMI, governing-law change, entity substitution, consent language or a sufficient-connection label as a universal solution. Recognition can depend on local legislation, public policy, notice, affected rights, procedural fairness and enforcement route. The UNCITRAL Model Law on Cross-Border Insolvency (https://uncitral.un.org/en/texts/insolvency/modellaw/cross-border_insolvency) is a public framework used in some jurisdictions, but enactments differ and must be checked locally.

Fictional Case 4: recognition complication

Harborfield Energy proposes to amend an England-law guarantee given by a subsidiary in Forum A and release security over an asset in Forum B. The plan model allocates EUR 18 million of value from those actions. Local advice is not yet available.

The correct finance treatment is not to count EUR 18 million as certain. Model at least three cases:

Case	Recognized/effective value (EURm)	Delay cost (EURm)	Net value (EURm)
full effect	18	1	17
delayed effect	18	5	13
no effect	0	3	(3)

The values are assumptions. They show why recognition and implementation are value variables, not boilerplate footnotes.

New money, governance and conditions

New money can be necessary to fund trading, fees and implementation. It can also change priority, governance and value allocation. The finance model should separate four questions:

- ♦ 1. How much liquidity is needed in the base and downside cases?
- ♦ 2. Which entity receives the funds and which entities benefit?
- ♦ 3. What interest, fees, priority, collateral, equity or control is given in return?
- ♦ 4. Which conditions must be satisfied before funding and what is the fallback if one fails?

Fictional Case 5: funding with a delayed condition

Birchline Medical needs EUR 28 million at implementation. A fictional lender commits EUR 32 million, with EUR 24 million funded at completion and EUR 8 million available after a collateral step. Uses at completion are EUR 12 million for overdue suppliers, EUR 6 million for fees, EUR 4 million for payroll/tax and EUR 8 million minimum cash, totaling EUR 30 million.

Completion-day sources are EUR 24 million new money plus EUR 5 million existing cash, or EUR 29 million. The company is EUR 1 million short before the delayed tranche. If minimum cash is reduced in the model merely to make the sources/uses balance, the model hides the problem. The team must accelerate the collateral step, arrange an interim bridge, reduce a real use with evidence or choose another path.

Funding control	Evidence	Owner	Blocking condition
commitment	signed commitment and permitted purpose	funder/counsel	commitment not effective
entity/cash path	sources/uses and account flow	treasury/finance	cash at wrong entity
priority/collateral	term sheet, documents and approvals	counsel	priority or security not effective
conditions	dated checklist with responsible party	transaction team	unsatisfied condition precedent
downside	weekly cash and delayed-close case	finance/management	liquidity breach before funding
governance	board/shareholder/creditor approvals	company/counsel	missing authority

Finance should show fees and consideration separately. A 4% fee on EUR 32 million is EUR 1.28 million. If capitalized, it may increase claims without adding operating cash. If paid in cash, it increases uses. If funded through equity or warrants, it changes value allocation. No single “new money amount” captures all three effects.

Implementation conditions register

Condition	Plan dependency	Evidence required	Consequence if late	Fallback
sanction order	legal effectiveness	sealed/order evidence and counsel confirmation	no binding effect	adjourn/alternative route
new - money documents	liquidity	executed documents and funds - flow	cash shortfall	interim facility or revised uses
security steps	funding/release	local filings, control and opinions as scoped	delayed draw or incomplete package	escrow/holdback if legally available
vote/claim reconciliation	distributions	final admitted claims and holder data	misallocation	reserve/dispute process
foreign effectiveness	affected cross - border rights	local advice and filings	incomplete compromise	parallel/local step
operational readiness	business continuity	supplier, payroll, systems and communications plan	value erosion	contingency funding and plan

25.11 Stakeholder and adviser workplan

Workstream	Core deliverable	Accountable owner	Required decision date
company/board	viability, alternatives and approvals record	board/management with advisers	before launch
finance	cash, valuation, claims and implementation model	finance adviser/CFO	continuous
restructuring law	eligibility, jurisdiction, classes, process and sanction	England - and - Wales counsel	before filing and each hearing
local law	recognition/effectiveness for each forum	local counsel	before launch or condition satisfaction
creditor engagement	holder map, NDAs, feedback and support	financial adviser/company	before solicitation
new money	commitment, conditions, priority and closing	funding parties and counsel	before sanction/implementation
operations	customers, suppliers, employees and contingency	management	through implementation
communications	consistent source - controlled messages	company and advisers	each stakeholder event

No adviser should sign outside the stated remit. Finance owns arithmetic and reconciliation. Valuation specialists own methodology and assumptions within their mandate. Counsel owns legal conclusions. Management owns the factual forecast and execution plan.

Creditor engagement and support control

Creditor engagement should be treated as an evidence and execution workstream, not as a substitute for the statutory process. The team should identify holders, decision makers, information status, claim amounts, transfer activity and stated concerns, while respecting confidentiality, competition, market-abuse and other applicable rules. Counsel and compliance should define the contact perimeter.

Engagement field	Controlled record	Why it matters
holder/entity	legal holder, beneficial position and adviser	vote, authority and communication path
claim	instrument, entity, amount and dispute status	class and value reconciliation
information status	public/restricted and NDA date	permitted communication and trading controls
decision authority	committee, fund, bank or agent process	realistic timetable and approvals
stated concern	value, priority, liquidity, governance or process	targeted evidence response
support status	no view, conditional, supportive or opposed	scenario planning, not vote certification
transfer/change	date, amount and evidence	denominator and solicitation updates

The support tracker should not convert informal feedback into a committed vote. “Constructive” is not a support level; “expected to support” is not a signed undertaking. Where a restructuring support agreement or lock-up is proposed, the executed document and counsel's analysis control its effect, conditions, releases, fees, termination rights and permitted transfers.

Stakeholder questions should be answered from the controlled source pack. If one class receives a revised forecast or valuation sensitivity, the team should ask whether other affected stakeholders or the court process require the same update. Selective provision of inconsistent assumptions creates both execution and credibility risk.

Management and board decision record

The board's record should distinguish the problem, alternatives, assumptions and adviser remits. A useful finance-side decision paper contains:

- ♦ 1. current liquidity and the first date cash falls below the selected operating threshold;
- ♦ 2. the capital structure and rights proposed to be affected;
- ♦ 3. the base and downside business cases;
- ♦ 4. the selected relevant alternative and competing alternatives;
- ♦ 5. valuation and claim recoveries by class;
- ♦ 6. funding needs, sources and conditions;
- ♦ 7. principal implementation, recognition and litigation risks;
- ♦ 8. employee, customer, supplier and operational consequences;
- ♦ 9. the proposed route, fallback route and decision deadlines; and
- ♦ 10. open matters owned by counsel, valuation, tax, accounting and local advisers.

The paper should not state that a route is legally available, fair or sanctionable unless the responsible professional has supplied that conclusion for the exact facts and date. Finance can state that a scenario has enough selected cash or produces a specified recovery; it cannot decide directors' duties, jurisdiction or court discretion.

Communication consistency check

Before any stakeholder event, reconcile the following numbers: EBITDA, cash, funding need, enterprise value, net distributable value, claims, class recoveries, implementation cost and timetable. If a press statement uses “fully funded,” the sources/uses and commitment evidence should support that description. If a creditor presentation says a class is unimpaired or no worse off, counsel and the claim-level schedule must support the exact usage. If the answer is not yet supported, use a narrower description.

The team should also maintain a dated question log. Each response should identify the source, owner and whether it changes the model or legal analysis. Repeated questions about one assumption are evidence that the pack may not explain the issue clearly enough. Update the explanation, not just the talking points.

25.12 Exercises and answer checks

Exercise 1: scheme denominator

A scheme class has EUR 150 million total claims. EUR 120 million is present and voting. Yes votes are EUR 93 million from eight holders; no votes are EUR 27 million from four holders.

- ♦ 1. Calculate yes value as a percentage of present-and-voting claims.
- ♦ 2. Calculate yes value as a percentage of total claims.
- ♦ 3. Explain which denominator belongs in the statutory vote reconciliation and what counsel must still verify.

Answer check. $93 / 120 = 77.5\%$; $93 / 150 = 62.0\%$. The statutory reconciliation uses the present-and-voting denominator under the applicable route and order. Counsel/chair must verify classes, entitlement, admission, proxies, number test and procedure.

Exercise 2: claim-level no-worse-off

A dissenting class has two holders. Holder A has a EUR 60 million claim and receives EUR 42 million under the plan versus EUR 36 million in the selected alternative. Holder B has a EUR 40 million claim and receives EUR 22 million under the plan versus EUR 25 million in the selected alternative.

- ♦ 1. Calculate each holder's difference.
- ♦ 2. Calculate the class average recovery under each case.
- ♦ 3. State why the average does not resolve the statutory question.

Answer check. A is EUR 6 million better; B is EUR 3 million worse. Plan class value is EUR 64 million, or 64%; alternative class value is EUR 61 million, or 61%. The average is higher under the plan, but B is worse on the selected figures. Rights, claim allowance, valuation and the statutory test require legal and expert review.

Exercise 3: liquidity delay

A company has EUR 19 million cash, EUR 4 million minimum cash, weekly burn of EUR 2 million and a EUR 5 million one-time payment in week 4. New money of EUR 12 million funds at the end of week 4 in the base case or the end of week 6 in the downside.

- ♦ 1. Calculate end-week-4 cash before new money.
- ♦ 2. Calculate end-week-6 cash before delayed new money.
- ♦ 3. Identify the first control response.

Answer check. End-week-4 cash is $19 - (4 \times 2) - 5 = \text{EUR } 6 \text{ million}$. End-week-6 cash before funding is $6 - (2 \times 2) = \text{EUR } 2 \text{ million}$, below minimum. The team must not assume implementation; it should accelerate conditions, secure interim liquidity or select another executable path with board and adviser review.

Appendix 25A: neutral source and procedure checklist

Before reviewer circulation, confirm:

- ♦ • exact statutory as-of date and consolidated provisions;
- ♦ • company eligibility and England-and-Wales jurisdiction analysis;

- ♦ • provisional classes and rights comparison;
- ♦ • claims register, holder list and vote denominators;
- ♦ • current cash, 13-week forecast and minimum liquidity;
- ♦ • valuation date, methodology, range and sensitivities;
- ♦ • relevant-alternative feasibility, timing and costs;
- ♦ • claim-level no-worse-off schedule where applicable;
- ♦ • explanatory information tied to one source model;
- ♦ • court timetable and procedural advice;
- ♦ • standstill, supply, guarantee, security and intercreditor workstreams;
- ♦ • neutral forum-by-forum recognition matrix;
- ♦ • new-money commitments, conditions and implementation steps; and
- ♦ • exact text, calculation and source hashes for qualified review.

Appendix use note

The checklist is not a substitute for the live procedural timetable. Convert it into a dated responsibility matrix for the selected company, route and court process. Each item should show the controlling source, responsible person, reviewer, due date, dependency and evidence of completion. A document marked “drafted” is not necessarily executed, filed, served, effective or funded.

The final pre-hearing review should reconcile the claims register, class map, explanatory information, valuation, cash forecast, vote schedule and implementation plan to the same version. The final pre-completion review should separately confirm the order, new-money funding, documents, releases, local effectiveness steps, distributions and operational communications. Any unresolved item should be visible to the board and professional owners; it should not be converted into a silent assumption merely to show a green status.

If the proposal changes after a vote or hearing, obtain procedural advice and refresh affected calculations. A change in consideration, class treatment, valuation, funding, timing or relevant alternative can alter more than one workstream. The control objective is traceability: a reviewer should be able to identify which exact fact, source and approval supports every material statement in the final pack.

25.13 Primary-source register and publication gate

Primary/public sources checked on 12 July 2026:

- ♦ • Companies Act 2006 Part 26 (<https://www.legislation.gov.uk/ukpga/2006/46/part/26>), including sections 895 (<https://www.legislation.gov.uk/ukpga/2006/46/section/895>), 896 (<https://www.legislation.gov.uk/ukpga/2006/46/section/896>), 897 (<https://www.legislation.gov.uk/ukpga/2006/46/section/897>) and 899 (<https://www.legislation.gov.uk/ukpga/2006/46/section/899>).
- ♦ • Companies Act 2006 Part 26A (<https://www.legislation.gov.uk/ukpga/2006/46/part/26A>), including sections 901A (<https://www.legislation.gov.uk/ukpga/2006/46/section/901A>), 901C (<https://www.legislation.gov.uk/ukpga/2006/46/section/901C>), 901D (<https://www.legislation.gov.uk/ukpga/2006/46/section/901D>), 901F (<https://www.legislation.gov.uk/ukpga/2006/46/section/901F>) and 901G (<https://www.legislation.gov.uk/ukpga/2006/46/section/901G>).
- ♦ • Corporate Insolvency and Governance Act 2020 explanatory notes (<https://www.legislation.gov.uk/ukpga/2020/12/notes/division/6/index.htm>).

- ✦ • Insolvency Act 1986 Part A1 (<https://www.legislation.gov.uk/ukpga/1986/45/part/A1>) and section 233B (<https://www.legislation.gov.uk/ukpga/1986/45/section/233B>).
- ✦ • UNCITRAL Model Law on Cross-Border Insolvency (https://uncitral.un.org/en/texts/insolvency/modellaw/cross-border_insolvency).

Publication requires exact-hash qualified England-and-Wales legal review. Any change to the legal source date, process description, class/vote calculations, relevant-alternative assumptions or recognition framework requires affected QA and review to be repeated.

Distressed Debt and Special Situations

26.0 Scope, date and professional boundary

This chapter presents a finance-side framework for distressed-credit analysis, out-of-court restructuring and selected **United States Chapter 11** mechanics. It also provides a high-level orientation to the European preventive-restructuring policy framework and cross-references the England-and-Wales tools in Chapter 25. In line with the owner-approved scope, it does not describe any additional named European national regime.

The primary-source links and statutory descriptions were checked on **12 July 2026**. This is not legal, tax, regulatory or investment advice. A real case requires the current U.S. Bankruptcy Code, Federal Rules of Bankruptcy Procedure, local rules, court orders, operative finance documents and qualified counsel. European outcomes depend on national implementation and local law. Finance professionals own arithmetic, source lineage and scenario discipline; counsel owns legal effect, claim treatment, priority, duties, voting and confirmation conclusions.

Every company, trade, claim, agreement, price, value and timeline below is fictional. No issuer, fund, mandate, court case, private trade or anonymous market story is used.

26.1 Learning objectives

After completing this chapter, the reader should be able to:

- ♦ 1. link operating deterioration, liquidity, debt service, market price and covenant evidence without treating any one indicator as dispositive;
- ♦ 2. compare amendments, exchanges, new money, asset transfers and other out-of-court tools by the rights changed and execution dependencies;
- ♦ 3. build entity-level enterprise-value, collateral and claim waterfalls without double counting;
- ♦ 4. distinguish statutory text, a case-specific court order and a modelling assumption in Chapter 11 analysis;
- ♦ 5. prepare a DIP sources-and-uses model with explicit priority, collateral, cost and delay assumptions;
- ♦ 6. map class, voting, plan and confirmation evidence without predicting legal outcomes;
- ♦ 7. evaluate claims-trading economics, information status, sanctions/KYC and settlement controls; and
- ♦ 8. compare Chapter 11 with a generic European preventive-restructuring orientation without implying equivalence.

Cross-references: financial covenants in Chapter 15; EBITDA in Chapter 16; events of default in Chapter 20; liability-management exercises in Chapter 22; amend-and-extend in Chapter 23; guarantees/collateral in Chapter 24; England-and-Wales tools in Chapter 25; credit analysis in Chapter 27; ratings in Chapter 29; and loan trading in Chapter 38.

26.2 Core definitions

Term	Controlled teaching definition	What requires case-specific review
Distress	A condition in which liquidity, solvency, debt service, refinancing or stakeholder pressure materially narrows available choices	financial facts, legal tests and time horizon
Liquidity runway	Time until available cash and committed funding fall below a selected operating or legal threshold	cash accuracy, availability conditions, minimum cash and timing
Enterprise value	Selected value attributed to operations before allocating claims and specified adjustments	methodology, date, scenarios and expert evidence
Claim	A right to payment or other bankruptcy-law claim within the relevant statutory framework	allowance, priority, amount, contingencies and objection
Allowed claim	A claim recognized for specified purposes under the applicable process	proofs, schedules, objections, orders and law
Administrative expense	A postpetition or process claim asserted to have specified administrative treatment	statutory basis, benefit, approval and amount
Automatic stay	The stay arising under 11 U.S.C. section 362 (https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section362) on the filing of a qualifying petition, subject to scope and exceptions	debtor/entity coverage, action, exception and relief from stay
DIP financing	Postpetition credit obtained by a debtor in possession or trustee under applicable authority	approval, priority, liens, milestones, budget and order terms
Priming lien	A lien proposed to rank senior or equal to an existing lien under the conditions in section 364(d) (https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section364)	inability to obtain credit otherwise, adequate protection and court authorization
Adequate protection	Protection of an interest in property as addressed in 11 U.S.C. section 361 (https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section361) and related provisions/orders	form, value, timing and sufficiency
Class	Claims or interests grouped for plan treatment and voting	substantial similarity, classification purpose and court determination
Impaired claim	A claim whose legal, equitable or contractual rights are altered under the selected plan analysis	statutory application and plan terms
Confirmation	Court confirmation of a plan under the applicable statutory requirements	all requirements, evidence, objections and court findings
Exchange offer	An out-of-court offer to exchange one instrument or claim for another package	eligibility, disclosure, consent, consideration and applicable law
Uptiering	A transaction in which selected debt is moved or issued into a higher-priority position	covenant capacity, consent, sacred rights, collateral and litigation risk
Dropdown	A transfer of assets or value to an entity or silo used in a financing or restructuring strategy	covenant capacity, value, duties, transfer validity and remedies
Claims trade	A purchase or sale of a claim or economic interest in a claim	title, transfer, documentation, information, KYC/sanctions, settlement and court-rule issues

Labels do not decide outcomes. “Secured,” “administrative,” “priming,” “impaired,” “fulcrum” and “money good” are propositions to be tested against documents, value and law.

26.3 Diagnose deterioration from linked evidence

Distress often appears first as a combination of small changes rather than one dramatic event. The analyst should connect operating, cash, document and market evidence through time.

Evidence stream	Early signal	Finance test	Common analytical error
operating	volume decline, customer loss, margin compression	driver-based EBITDA and cash sensitivity	treating management adjustment as cash
working capital	receivable stretch, inventory build, supplier tightening	cash conversion and weekly peak funding	relying on annual averages
liquidity	revolver draw, borrowing-base decline, trapped cash	available liquidity after conditions/minimum cash	counting undrawable or restricted cash
debt service	higher cash interest, hedge expiry, amortisation	monthly/quarterly debt-service schedule	using annual interest only
documentation	covenant headroom, reporting delay, consent need	operative definitions and first-breach date	inferring legal result from a model
market	price decline, spread widening, lower dealer depth	price-to-recovery and liquidity reconciliation	treating price as enterprise value
stakeholder	adviser hires, group formation, shorter terms	scenario and process map	claiming causation from rumor

Fictional Case 1: Caldera Packaging deterioration

Caldera begins a 13-week period with EUR 32 million of unrestricted cash and a EUR 20 million undrawn revolver. The revolver is a selected assumption and is available only while specified conditions are met. Minimum operating cash is EUR 8 million.

The first four weeks have EUR 3 million weekly operating cash burn. Weeks 5-8 improve to EUR 1 million weekly burn. A EUR 10 million semiannual interest payment falls in week 9. Weeks 9-13 are cash-neutral before interest. Assume no revolver draw in the base calculation.

Calculation 1: liquidity runway

Cash after week 4 is:

$$32 - (4 \times 3) = \text{EUR } 20 \text{ million.}$$

Cash after week 8 is:

$$20 - (4 \times 1) = \text{EUR } 16 \text{ million.}$$

After the week-9 interest payment, cash is:

$$16 - 10 = \text{EUR } 6 \text{ million.}$$

Caldera falls EUR 2 million below minimum cash in week 9. If the EUR 20 million revolver remains fully available, a EUR 10 million draw would restore cash to EUR 16 million and leave EUR 10 million undrawn. If a covenant, borrowing-base, default or representation condition blocks the draw, the apparent EUR 20 million liquidity source is not available. The model must carry both cases until the document question is resolved.

Caldera case	Week - 9 cash before draw (EURm)	Revolver draw (EURm)	Week - 9 cash after draw (EURm)	Undrawn revolver (EURm)	Minimum - cash status
draw available	6	10	16	10	above by 8
draw unavailable	6	0	6	0 available	below by 2

The early-warning conclusion is specific: an interest date and availability condition drive the liquidity break. It is not a legal conclusion that a draw can or cannot be made.

Cash-forecast control

A 13-week model should be a control system rather than a single forecast line. Separate receipts and payments by source, legal entity, currency, timing and confidence. Show restricted cash, uncommitted inflows and conditional borrowing separately from available liquidity. Reconcile weekly actuals to forecast and carry variances into the remaining weeks.

Forecast field	Base evidence	Downside question	Owner
customer receipts	invoice and collection history	what slips if customers shorten orders or dispute invoices?	finance/commercial
inventory and supplier payments	purchase orders and terms	what cash is required to maintain supply?	operations/procurement
payroll/tax	payroll calendar and filings	which payments cannot be deferred?	HR/tax/finance
interest/amortisation	debt schedule and hedges	what changes after default, hedge expiry or rate reset?	treasury/counsel
revolver/borrowing base	facility and current certificate	are conditions, reserves and representations satisfied?	treasury/counsel
restructuring costs	scoped adviser estimates	how do delay and litigation change cost?	transaction team
minimum cash	entity - level operating requirement	what breaks operationally below the threshold?	management

Do not solve a cash deficit by inserting an unexplained "management action." Name the action, amount, timing, approval, counterparty and downside. A delayed capex item can preserve cash but may damage operations; a stretched supplier payment can accelerate a supply interruption; a tax deferral may be unavailable. The model should show the trade-off.

26.4 Market price is an input, not a recovery conclusion

Price can reflect expected recovery, timing, coupon, settlement, liquidity, holder constraints, hedging, financing and risk appetite. A loan at 60 is not evidence that enterprise value equals 60% of debt. The analyst should reconcile price to a scenario-weighted cash-flow view.

Fictional Case 2: Vela Term Loan

Vela's fictional EUR 10 million face claim trades at 58. Assume the buyer pays EUR 5.8 million before accrued interest and settlement adjustments. The selected scenario set is:

Scenario	Probability	Recovery on face	Time to recovery	Present - value assumption
fast consensual exchange	25%	78%	0.5 years	12% annual discount rate
in - court reorganization	50%	62%	1.5 years	15% annual discount rate
severe downside sale	25%	35%	1.0 year	20% annual discount rate

Calculation 2: simplified scenario-weighted value

Using simple annual discounting for teaching:

- ♦ • exchange PV per 100 face: $78 / (1.12^{0.5}) = 73.7$;
- ♦ • reorganization PV: $62 / (1.15^{1.5}) = 50.3$; and
- ♦ • downside PV: $35 / 1.20 = 29.2$.

Scenario-weighted PV is:

$$25\% \times 73.7 + 50\% \times 50.3 + 25\% \times 29.2 = 50.9 \text{ per 100 face.}$$

The selected model produces 50.9 versus a price of 58. That gap is not automatically a sell signal. The assumptions may omit coupon receipts, default interest, fees, rights offerings, new-money participation, settlement cost, taxes or liquidity value. It does show that the buyer must identify which assumption justifies paying above the selected scenario-weighted PV.

26.5 Enterprise value, entities and claim waterfalls

Recovery begins with a legal-entity and claim map. Consolidated enterprise value is not one unrestricted cash pool.

Assume fictional Caldera has two relevant entities:

Entity	Selected gross value (EURm)	Cash (EURm)	Priority/local claims and costs (EURm)	Debt/guarantee structure
Caldera OpCo	230	12	27	EUR 180m first-lien borrower; guarantees parent notes
Caldera Distribution	70	5	25	EUR 30m local debt; no parent guarantee

Calculation 3: entity-level distributable value

OpCo's selected value after local priority claims/costs is:

$$230 + 12 - 27 = \text{EUR 215 million.}$$

Distribution's selected residual after local debt and other local claims is:

$$70 + 5 - 25 - 30 = \text{EUR 20 million.}$$

Assume 75% of Distribution residual is modelled as upstreamable after timing and execution sensitivity:

$$20 \times 75\% = \text{EUR 15 million.}$$

Selected group distributable value is therefore EUR 230 million (215 + 15), not EUR 317 million (230 + 70 + 12 + 5). The latter ignores claims/costs and double counts gross value.

Assume claims against the selected value pool are:

Claim	Amount (EURm)	Selected priority	Allocation (EURm)	Recovery
first-lien term/revolver	180	first	180	100.0%
parent unsecured notes with OpCo guarantee	90	after first lien in selected pool	50	55.6%
general unsecured claims	35	next for teaching only	0	0.0%

The waterfall is a finance sensitivity, not a legal-entitlement opinion. Claim allowance, collateral value, secured/deficiency portions, guarantees, priority, set-off, subordination and plan treatment require counsel and valuation review. 11 U.S.C. section 506 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section506>) is a primary statutory reference for secured-claim analysis in a U.S. case, but the actual property interest and valuation context control.

Valuation triangulation and market reconciliation

No one valuation method owns distress. The analyst should triangulate methods that answer different questions:

- ♦ • a cash-flow or DCF framework tests the operating plan and funding burden;
- ♦ • trading or transaction comparables provide market reference points, subject to business, cycle, leverage and liquidity differences;
- ♦ • asset-specific or liquidation analysis tests a downside floor after realization costs and priority claims;
- ♦ • market prices show the price of a claim at a date, not the value of the enterprise; and
- ♦ • exit-financing capacity tests whether the proposed capital structure can be funded at emergence or completion.

Assume Caldera produces selected normalized EBITDA of EUR 42 million. A low/base/high enterprise-value range at 4.0x/5.0x/6.0x is EUR 168/210/252 million. Add EUR 12 million cash, subtract EUR 18 million priority claims and costs, and add the EUR 15 million selected upstream value from Distribution. Net distributable values are:

- ♦ • low: $168 + 12 - 18 + 15 = \text{EUR } 177 \text{ million}$;
- ♦ • base: $210 + 12 - 18 + 15 = \text{EUR } 219 \text{ million}$; and
- ♦ • high: $252 + 12 - 18 + 15 = \text{EUR } 261 \text{ million}$.

These values differ slightly from the earlier EUR 230 million selected pool because the assumptions are deliberately independent sensitivities. The model must not silently choose whichever number supports the preferred transaction. It should bridge the cases, select a primary methodology only with evidence and preserve the alternatives.

Valuation control	Low	Base	High	Required challenge
normalized EBITDA (EURm)	38	42	46	add-backs, churn, capex and working capital
multiple	4.0x	5.0x	6.0x	comparability, cycle and distress discount
EV (EURm)	152	210	276	mathematical tie-out
cash/priority/upstream adjustment	9	9	9	entity ownership and claims
distributable value (EURm)	161	219	285	no double counting; counsel/valuation review

The second table uses both EBITDA and multiple sensitivities, producing a wider range. It is not a correction to the first calculation; it demonstrates interaction risk. A 1.0x multiple change on EUR 42 million EBITDA moves value by EUR 42 million. A EUR 4 million EBITDA change at 5.0x moves value by EUR 20 million. Together they can shift the fulcrum by more than one class.

26.6 Out-of-court tools: map rights exchanged

An out-of-court restructuring is a bundle of changes, not a label. Compare what each stakeholder gives, receives and must consent to.

Tool	Potential finance objective	Rights/evidence to map	Execution risks
amend and extend	move maturity and reset terms	maturity, pricing, covenants, fees, consents	insufficient participation; short runway
exchange offer	reduce debt or extend tenor	eligibility, consideration, priority, disclosure, exit consents	holdouts; unequal economics; litigation
new-money rescue	fund runway and implementation	sources/uses, priority, collateral, milestones, conditions	priming/consent dispute; inadequate size
debt-for-equity	reduce cash debt service	valuation, governance, dilution, approvals	ownership disagreement; regulatory/tax issues
asset sale	raise cash or simplify group	asset ownership, liens, release, proceeds use	value loss; trapped proceeds; execution delay
up-tiering or non-pro-rata exchange	create selected senior capacity	debt/lien baskets, sacred rights, open-market terms, collateral	challenge, holdout conflict, operational distraction
dropdown financing	create financing capacity around transferred value	investment/asset-sale capacity, entity, collateral, valuation	transfer challenge, value leakage, local constraints

Fictional Case 3: exchange plus new money

Ridgeton Services has EUR 200 million existing term debt. Participating lenders can exchange at 90 face value into new senior debt equal to 85% of surrendered face and fund new money equal to 10% of surrendered face. Assume 70% participation.

Calculation 4: participation and pro forma debt

Participating face is:

$200 \times 70\% = \text{EUR } 140 \text{ million.}$

New senior exchange debt is:

$140 \times 85\% = \text{EUR } 119 \text{ million.}$

New money is:

$140 \times 10\% = \text{EUR } 14 \text{ million.}$

Non-participating old debt remains EUR 60 million. Pro forma funded debt in this simplified schedule is:

$119 + 14 + 60 = \text{EUR } 193 \text{ million.}$

The face reduction is EUR 7 million, before fees, accrued interest and other claims. The transaction raises EUR 14 million cash but may increase priority ahead of non-participants. The model does not establish covenant capacity, validity, consent, priority or litigation outcome. Those are document and counsel questions.

The finance team should model at least three participation levels and show debt, cash, interest, priority and liquidity under each. A transaction that reduces face value but leaves inadequate runway is not a complete solution.

26.7 Chapter 11: controlled statutory orientation

Chapter 11 reorganizations are governed by Title 11, court orders and the Federal Rules of Bankruptcy Procedure. The following map is deliberately limited.

Topic	Primary statutory source	Finance implication	Boundary
automatic stay	11 U.S.C. section 362 (https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section362)	may alter enforcement timing and liquidity behavior	scope, exceptions and relief are legal questions
use/sale of property	section 363 (https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section363)	affects ordinary operations, collateral and sale scenarios	authorization and order terms control
postpetition credit	section 364 (https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section364)	DIP priority, collateral, budget and milestones affect value	court findings and financing order control
contract assumption/rejection	section 365 (https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section365)	impacts operations, cure and claims	contract and court treatment require counsel
administrative/priority claims	sections 503 (https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section503) and 507 (https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section507)	reduce distributable value and liquidity	allowance and priority are legal/court matters
plan filing	section 1121 (https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section1121)	affects process control and timing	statutory periods may change by order and circumstance
classification	section 1122 (https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section1122)	determines voting and treatment structure	substantial similarity and classification require counsel
disclosure/voting	sections 1125 (https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section1125) and 1126 (https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section1126)	shapes solicitation, class support and blocking positions	adequacy, eligibility and votes require legal process
confirmation	section 1129 (https://uscode.house.gov/view.xhtml?edition=prelim&req=granuleid%3AUSC-prelim-title11-section1129)	plan economics must fit statutory requirements	court findings; do not predict confirmability

The filing of a qualifying petition triggers the section 362 stay, subject to statutory scope and exceptions. It should not be described as automatic protection for every non-debtor affiliate, guarantor, manager or counterparty. Likewise, section 1121's initial debtor plan-filing period should not be turned into a prediction of case duration. The docket, orders, negotiations and facts matter.

The finance model should label each statement as one of:

- ✦ 1. **statutory text** linked to the current U.S. Code;
- ✦ 2. **court/order term** copied only from the actual docket/order and source-identified; or
- ✦ 3. **selected modelling assumption** used solely for sensitivity.

26.8 DIP financing and complete arithmetic

Section 364 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section364>) distinguishes several forms of postpetition credit. A senior or equal lien on already encumbered

property under section 364(d) requires the specified statutory conditions, including inability to obtain the credit otherwise and adequate protection. The court order, not a financing slide, determines approved rights.

Fictional Case 4: Horizon Parts DIP

Horizon proposes a six-month EUR 50 million commitment. Selected sources and uses are:

Source / use	EURm
DIP cash funding at closing	38.0
delayed-draw availability	12.0
total commitment	50.0
opening liquidity	8.0
critical operating payments	(15.0)
payroll and taxes	(9.0)
professional-fee reserve	(7.0)
interest and financing fees	(4.5)
working-capital support	(12.0)
minimum closing cash	(10.0)

Calculation 5: initial funding adequacy

Closing sources are EUR 46 million (38 + 8). Listed cash uses excluding the delayed draw total EUR 57.5 million (15 + 9 + 7 + 4.5 + 12 + 10). Initial funding therefore has an EUR 11.5 million shortfall:

$$46 - 57.5 = -\text{EUR } 11.5 \text{ million.}$$

The EUR 12 million delayed draw appears sufficient by EUR 0.5 million only if it is available before the cash need and all conditions are satisfied. Timing, budget variances and fees can eliminate that cushion.

Calculation 6: financing-cost bridge

Assume the EUR 38 million closing draw bears 10% annual cash interest for six months, a 2% upfront fee on the EUR 50 million commitment and a 1% exit fee on drawn principal of EUR 50 million at exit.

- ♦ • cash interest: $38 \times 10\% \times 6/12 = \text{EUR } 1.90 \text{ million};$
- ♦ • upfront fee: $50 \times 2\% = \text{EUR } 1.00 \text{ million};$ and
- ♦ • exit fee: $50 \times 1\% = \text{EUR } 0.50 \text{ million.}$

Selected total is EUR 3.40 million before legal fees, unused fees, default interest, OID, roll-up or additional draws. The example does not state market terms. A real model follows the commitment, budget and order exactly.

DIP control	Finance evidence	Legal/order evidence	Failure mode
amount/timing	13-week cash flow and variance	approved commitment and draw conditions	cash shortfall before draw
priority/liens	collateral and recovery sensitivities	section 364 findings and order	overstated collateral or recovery
adequate protection	value trend and cash payments	negotiated/court-approved package	unmodelled leakage or dispute
milestones	executable process timetable	financing order covenants/defaults	default before value-maximizing path
budget	sources/uses and variance	approved budget and permitted variances	blocked spending or liquidity miss
fees/interest	complete cost bridge	approved documents/order	understated administrative burden

26.9 Plan classes, voting and value break

Section 1122 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section1122>) addresses classification; section 1126 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section1126>) addresses acceptance; and section 1129 (<https://uscode.house.gov/view.xhtml?edition=prelim&req=granuleid%3AUSC-prelim-title11-section1129>) sets confirmation requirements. A finance team should model support and value without declaring a plan confirmable.

Assume a fictional impaired creditor class has EUR 120 million of allowed claims that vote: nine holders with EUR 84 million vote yes; six holders with EUR 36 million vote no.

Calculation 7: selected creditor-class vote

Yes value is $84 / 120 = 70.0\%$. Yes holders are $9 / 15 = 60.0\%$ in number.

For a non-insider class of claims, section 1126(c) contains value and number requirements. On the selected figures, the class exceeds two-thirds in amount and one-half in number. That arithmetic is not a legal vote certification. Allowed claims, exclusions, designation, solicitation, ballots and the court's process require counsel.

Class	Claim (EURm)	Low value allocation	Base value allocation	High value allocation	Practical issue
DIP/admin/priority	45	45	45	45	amount and allowance
first lien	180	155	180	180	collateral/value sensitivity
second lien	90	0	40	90	mathematical fulcrum shifts
unsecured	60	0	0	25	voting/litigation leverage despite low value

In the low case, value breaks in first lien. In the base case, it breaks in second lien. In the high case, unsecured creditors receive selected value. The "fulcrum" is therefore scenario-dependent and may differ from the constituency with practical control through liquidity, voting, litigation or new-money capacity.

Stakeholder leverage and negotiation map

The mathematical fulcrum is only one source of leverage. A class that appears covered may control collateral or near-term liquidity. A junior class with no selected recovery may hold a blocking vote, pursue a valuation objection or impose delay. Trade creditors, customers, employees and regulators can affect enterprise value without holding funded debt.

Stakeholder	Economic position	Potential leverage	Likely information need	Finance response
DIP/new - money lender	senior selected recovery	funding conditions and milestones	cash, collateral, process and budget	complete weekly model and downside
first lien	covered in base, impaired in low	collateral, consent, enforcement and vote	valuation floor and adequate protection	collateral/value sensitivities
second lien	base - case fulcrum	vote, litigation and new - money capacity	enterprise value and treatment	claim - level waterfall and alternatives
unsecured	out of money in base	class vote, committee and process rights	valuation upside and claims	preserve high case and dispute sensitivities
sponsor/equity	no selected legal - entitlement value	operational knowledge, funding and settlement	contribution and release economics	separate contribution from retained value
employees/suppliers	operational dependency	continuity and cash terms	payroll/supply plan	ring - fence critical operating needs

Negotiation analysis should ask what each group can fund, block, delay or litigate; what evidence changes its view; and what concession produces a more executable result. Do not allocate value to a junior class in the legal-entitlement waterfall merely because a settlement may be commercially useful. Show negotiated value separately and flag priority, gifting and confirmation issues for counsel.

A practical alternative matrix should include a fallback. If a consensual exchange needs 90% participation, model 70%, 80%, 90% and 100%. If a DIP depends on a sale milestone, model an extension and a failed sale. If a plan depends on one valuation, show the multiple/EBITDA range that moves the value break. The advice should survive a failed assumption.

26.10 Claims trading, settlement and information controls

Buying a claim does not only transfer an expected recovery. It can involve title, transfer documentation, accrued amounts, disputed status, information restrictions, KYC/sanctions, tax forms, voting cut-offs and court-rule procedures. The Federal Rules of Bankruptcy Procedure (<https://www.uscourts.gov/forms-rules/current-rules-practice-procedure/federal-rules-bankruptcy-procedure>) include rules on claims, transfers and groups/committees; the current rules, local rules and docket control.

Fictional Case 5: delayed claims settlement

An investor agrees to buy EUR 12 million face of an allowed unsecured claim at 42. The selected purchase price before adjustments is:

$$12 \times 42\% = \text{EUR } 5.04 \text{ million.}$$

Assume settlement occurs 20 days later than the selected base date, the buyer's funding cost is 8% per year and the parties' fictional contract allocates that financing cost to the buyer for teaching purposes.

Calculation 8: delay carry

$$5.04 \times 8\% \times 20 / 360 = \text{EUR } 0.0224 \text{ million, or EUR } 22,400.$$

If the claim is later reduced to EUR 10.5 million under a final order and the contract uses final allowed amount, base price becomes $10.5 \times 42\% = \text{EUR } 4.41$ million, a EUR 0.63 million reduction from the original EUR 5.04 million. The contract and order determine the real adjustment; the example shows why allowed amount and settlement terms belong in the price model.

Control	Question	Required evidence
claim identity	correct debtor, claim number, type and amount?	claims register and proof/order
transfer chain	seller owns what is being sold?	transfer documents and prior chain
economics	face, price, accrued items, distributions and adjustments?	confirmation and calculation
information	public-side, restricted or MNPI?	NDA, wall status and compliance approval
KYC/sanctions/tax	can parties and payment path clear?	onboarding and tax forms
voting	who controls ballot and record-date rights?	contract, ballot/order and settlement status
court rules	notice or disclosure required?	current federal/local rules and counsel advice

26.11 Generic European preventive-restructuring orientation

The Directive (EU) 2019/1023 (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32019L1023>) establishes an EU-level framework concerning preventive restructuring, discharge of debt and procedural efficiency. It requires implementation through national law and does not create one uniform European proceeding with identical thresholds, classes, stays, voting, court roles or recognition outcomes.

Analytical field	U.S. Chapter 11 orientation	Generic European orientation	Required caution
entry	voluntary/involuntary statutory routes under Title 11	national preventive/insolvency eligibility	do not equate financial difficulty or insolvency tests
stay	section 362 subject to scope/exceptions/orders	national stay rules within implemented framework	duration and affected actions vary
debtor control	debtor in possession subject to statute/court	national law may allocate control differently	governance and practitioner roles vary
new money	section 364 and financing order	national protection/priority depends on implementation	no assumed priming parity
classes/voting	sections 1122/1126 and case process	national class/voting/cram-down implementation	thresholds and tests vary
confirmation/sanction	section 1129 findings	national judicial/administrative confirmation	no universal standard
recognition	cross-border statutes/treaties/comity	forum-specific	obtain local advice

For England and Wales, Chapter 25 separately addresses Parts 26 and 26A. This chapter adds no named national regime. The practitioner should use the table only to organize questions for local counsel, not to infer equivalence.

Process-cost and delay sensitivity

Gross enterprise value is not distributable recovery. Fees, critical operating payments, DIP interest, adequate-protection payments, cure amounts, taxes, wind-down costs and exit financing can consume value before prepetition creditors receive it. Some items are claims; others are cash uses or value leakage. Do not deduct an item twice.

Assume a selected base reorganization value of EUR 260 million. The initial model includes EUR 12 million professional fees, EUR 8 million DIP interest/fees and EUR 10 million minimum cash, producing EUR 230 million distributable value. A three-month delay adds EUR 4 million professional fees, EUR 3 million DIP cost and EUR 6 million operating erosion. Delayed distributable value becomes:

260 - 16 - 11 - 10 - 6 = EUR 217 million.

The delay reduces value by EUR 13 million. If the second-lien claim is the fulcrum, that reduction falls initially on its modeled recovery, not pro rata across all classes. The calculation should therefore flow through each scenario waterfall and vote/support analysis.

Cost or leakage	Cash use, claim or value adjustment?	Timing	Source/owner	Double-count check
professional fees	cash use / possible administrative expense	weekly/monthly	adviser scopes and court process	not also embedded in EV
DIP interest and fees	cash or capitalized claim	per financing terms	DIP model/order	not both cash use and full claim unless correct
cure/contract costs	case-specific cash/claim	assumption/closing	contract schedule/counsel	exclude from operating forecast if separately deducted
operating erosion	valuation or cash-flow effect	delay period	management/valuation	do not deduct EBITDA impact twice
minimum cash	retained liquidity, not a creditor recovery	completion	operating case	keep outside distributable value

The practical lesson is that speed can preserve value, but a faster path is not automatically better if it lacks notice, evidence, funding or legal feasibility. Compare net value and execution probability, not calendar length alone.

26.12 Practitioner deliverable and review boundary

The minimum distressed-credit pack is:

Deliverable	Minimum content	Primary owner
deterioration dashboard	operating, liquidity, debt service, covenant and market evidence by date	finance/credit
13-week cash flow	sources, uses, availability, minimum cash, variance and downside	management/finance
entity and claims register	debtor/entity, claim, amount, status, priority, guarantee, collateral and dispute	counsel with finance tie-out
valuation bridge	low/base/high enterprise, sale and liquidation values; costs and timing	valuation/finance
waterfall set	legal-entitlement sensitivity, collateral pools and negotiated-plan view kept separate	finance with counsel flags
alternatives matrix	economics, liquidity, consent, timing, litigation and fallback	adviser team
DIP model	commitment, draws, budget, fees, milestones, collateral and delay	finance/counsel
support/voting map	class, holder, claim, status, support and blocking position	counsel/adviser
claims-trade controls	title, amount, economics, information, KYC/sanctions and settlement	operations/compliance/counsel
source-and-assumption register	statement, source, date, owner, status and required refresh	workstream owner

Do not collapse legal-entitlement value and negotiated plan value into one recovery percentage. Do not count gross sale proceeds before DIP/admin leakage and costs as distributable value. Do not assume that a mathematically balanced plan is feasible or confirmable.

26.13 Exercises and answer checks

Exercise 1: value break

A fictional group has EUR 260 million net distributable value after costs. Claims are EUR 35 million DIP/admin, EUR 170 million first lien, EUR 90 million second lien and EUR 55 million unsecured.

- ♦ 1. Allocate the selected value in that order.
- ♦ 2. Identify the mathematical fulcrum.
- ♦ 3. Recalculate if value falls by EUR 50 million.

Answer check. Base allocation: DIP/admin EUR 35 million (100%), first lien EUR 170 million (100%), second lien EUR 55 million (61.1%), unsecured zero. Value breaks in second lien. At EUR 210 million value, after EUR 35 million DIP/admin only EUR 175 million remains; first lien receives EUR 170 million and second lien EUR 5 million (5.6%). The fulcrum remains second lien but is close to shifting into first lien. Legal priority and allowed claims require counsel.

Exercise 2: DIP shortfall and delay

A debtor has EUR 6 million opening cash and EUR 30 million initial DIP funding. Four-week uses are EUR 12 million operations, EUR 8 million payroll/tax, EUR 5 million fees and EUR 7 million minimum cash. A EUR 10 million delayed draw is available at the end of week 4, subject to conditions. Delay adds EUR 3 million uses.

- ♦ 1. Calculate initial surplus/shortfall before delayed draw.
- ♦ 2. Calculate cushion after delayed draw without delay.
- ♦ 3. Calculate cushion after delay.

Answer check. Initial sources are EUR 36 million; uses are EUR 32 million, so cushion is EUR 4 million. After EUR 10 million draw, cushion is EUR 14 million. After EUR 3 million delay uses, cushion is EUR 11 million, assuming the draw is available. The model must separately test draw conditions and timing.

Exercise 3: claims-trade return

An investor buys EUR 8 million face at 55, for EUR 4.4 million. One year later it receives EUR 5.2 million total cash. Ignore taxes and interim flows.

- ♦ 1. Calculate cash gain.
- ♦ 2. Calculate simple one-year return on purchase price.
- ♦ 3. State three missing items before calling the trade attractive.

Answer check. Gain is $5.2 - 4.4 = \text{EUR } 0.8$ million. Simple return is $0.8 / 4.4 = 18.2\%$. Missing items include probability/timing of recovery, financing and settlement costs, claim allowance/title, information and compliance constraints, alternative scenarios and liquidity.

Appendix 26A: source-and-assumption control sheet

Every model or statement should be tagged as follows:

Tag	Meaning	Example	Required refresh
statutory text	current primary law	section 364 conditions	legal update or source-date change
court/order term	actual docket/order provision	approved DIP milestone	amended or new order
document fact	executed finance/transfer term	interest or consent	amendment/waiver/new trade
company fact	sourced operating/cash data	cash balance	each reporting date
market observation	dated price or executable quote	loan price	observation timestamp
calculated	formula from identified inputs	runway or recovery	any input change
assumption	selected unsourced input	value, timing or cost	sensitivity and owner approval
counsel review	legal interpretation required	priority, stay or vote	exact-hash qualified review

Before publication or transaction use, confirm the entity map, complete claims, collateral pools, costs, liquidity, statutory source date, court/order terms, document version, model checks and professional owners.

26.14 Primary-source register and publication gate

Primary/public sources checked on 12 July 2026:

- ♦ • 11 U.S.C. section 361 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section361>) (adequate protection), section 362 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section362>) (automatic stay), section 363 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section363>) (use, sale or lease of property), section 364 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section364>) (obtaining credit), section 365 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section365>) (executory contracts and leases) and section 506 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section506>) (secured claims).
- ♦ • 11 U.S.C. sections 503 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section503>) and 507 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section507>) (selected administrative/priority context).
- ♦ • 11 U.S.C. sections 1121 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section1121>), 1122 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section1122>), 1125 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section1125>), 1126 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section1126>) and 1129 (<https://uscode.house.gov/view.xhtml?edition=prelim&num=0&req=granuleid%3AUSC-prelim-title11-section1129>) (selected plan, disclosure, voting and confirmation context).
- ♦ • Federal Rules of Bankruptcy Procedure (<https://www.uscourts.gov/forms-rules/current-rules-practice-procedure/federal-rules-bankruptcy-procedure>).
- ♦ • Directive (EU) 2019/1023 (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32019L1023>) on preventive restructuring and related matters, subject to national implementation.

Publication requires exact-hash review by qualified U.S. bankruptcy counsel, qualified counsel for any added jurisdictional statement, and a distressed-credit practitioner for finance and market mechanics. Any change to

statutory dates, legal descriptions, scenario assumptions or calculations requires affected QA and review to be repeated.

ANALYTICAL TOOLS

- 27 Credit Analysis Framework
 - 28 Working Capital and Cash Management in LBO Structures
 - 29 Rating Agencies in Leveraged Finance
 - 30 Corporate Financial Modeling
 - 31 LBO Modelling – A Complete, Self-Contained Build
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 - 33 Landmark Transactions – What the Public Record Shows
-

Credit Analysis Framework

Teaching and professional boundary. *This chapter presents an independently written leveraged-credit workflow using invented companies, assumptions and calculations. It is not a rating methodology, accounting opinion, legal opinion, investment recommendation or approval of a live credit. Financial statements, executed documents, applicable law and current professional advice control any real transaction. Public sources are identified at point of use and were checked on 12 July 2026.*

Credit analysis is not a hunt for one decisive ratio. It is a controlled argument about whether a borrower can meet its obligations through a range of plausible paths, what protects the lender when that argument is wrong, and which evidence would change the conclusion. The analyst's job is therefore to connect five things that are often presented separately: the business model, the accounting record, cash conversion, the debt documents and the value available in distress.

The 2013 U.S. interagency leveraged-lending guidance is addressed to supervised financial institutions, not to every lender or borrower. Within that perimeter, it emphasizes clear underwriting standards, cash-flow capacity, sustainable capital structures, collateral controls, enterprise-value discipline, risk ratings and stress testing. Those themes provide a useful public reference for this chapter's control architecture, but they do not supply a universal leverage limit or credit decision. Federal Reserve, "Agencies issue updated leveraged lending guidance," 21 March 2013 (<https://www.federalreserve.gov/newsevents/pressreleases/bcreg20130321a.htm>); FDIC, FIL-13-2013, 27 March 2013 (<https://www.fdic.gov/news/financial-institution-letters/2013/fil13013.html>).

27.0 Learning objectives

By the end of this chapter, the reader should be able to:

- ♦ 1. convert a credit question into an evidence plan, driver tree and explicit approval standard;
- ♦ 2. reconcile reported, adjusted and underwritten EBITDA before using leverage or coverage;
- ♦ 3. bridge earnings to free cash flow, debt service, minimum liquidity and covenant runway;
- ♦ 4. integrate business, sector, management, sponsor, documentation and refinancing risks into scenarios;
- ♦ 5. build an entity-level recovery analysis without double counting value or claims;
- ♦ 6. compare relative value using consistent dates, definitions, liquidity assumptions and downside outcomes; and
- ♦ 7. produce a committee output that separates facts, assumptions, calculations, judgments and unresolved evidence.

27.1 The vocabulary must be fixed before the model

The same label can describe different quantities in different workstreams. A disciplined review begins with a definition sheet rather than a ratio page.

Term	Working definition for this chapter	Control question
Reported EBITDA	EBITDA or a close operating-profit measure taken from the stated financial-reporting source, without analyst additions	Which statement, period, perimeter and accounting policy produced it?
Adjusted EBITDA	Reported EBITDA plus or minus identified management, transaction or reporting adjustments	Is every adjustment separately described and supported?
Underwritten EBITDA	The analyst's selected earnings base after evidence, timing, recurrence and realization haircuts	What was rejected, capped, delayed or sensitized?
Free cash flow (FCF)	Cash generated after the specifically stated cash taxes, interest, capital expenditure, working-capital movement and other recurring uses	Is the definition pre- or post-interest, pre- or post-debt amortization?
Cash conversion	The selected cash-flow numerator divided by the selected EBITDA denominator	Are numerator and denominator from the same period and perimeter?
Gross leverage	Gross debt divided by the stated EBITDA base	Which debt and which EBITDA definition?
Net leverage	Gross debt less eligible nettable cash, divided by the stated EBITDA base	Is the cash accessible, unrestricted and surplus to minimum needs?
Interest coverage	EBITDA or another stated earnings measure divided by cash interest	Does cash interest include floors, hedging, fees and drawn revolver cost?
Fixed-charge coverage	A stated cash-flow or earnings measure divided by interest plus other recurring fixed charges	Which leases, pensions, preferred distributions or maintenance capex are included?
Minimum liquidity	Cash that management must preserve to operate through ordinary volatility	Is it supported by a weekly or monthly cash profile?
Covenant headroom	Distance between the tested covenant result and the contractual threshold, calculated under the executed definition	What testing date, cure right, netting rule and pro forma adjustment apply?
Recovery	Value distributed to a claim divided by that claim's amount under a stated entity, priority, cost and timing scenario	Has value been allocated only once?
Relative value	Comparison of expected and downside outcomes across instruments on a common date and definition set	Are price, carry, liquidity, documentation and catalysts consistently measured?
Rating outlook	An agency-specific indicator concerning potential direction over the relevant horizon under that agency's definitions	Has the current agency definition been checked?
Watch	An agency-specific status indicating focused review for a possible rating action	Is it being confused with an actual rating change?

The accounting record and the credit record answer different questions. IAS 7 describes the presentation of cash-flow information and distinguishes operating, investing and financing activities; it does not define lender EBITDA, free cash flow, covenant EBITDA or distributable cash. IFRS Foundation, IAS 7 overview, checked 12 July 2026 (<https://www.ifrs.org/issued-standards/list-of-standards/ias-7-statement-of-cash-flows.html/>). Any non-GAAP or lender-defined measure in a credit analysis therefore needs its own bridge.

27.2 Start with the decision, not the data room

A broad instruction such as “analyse the credit” is not a decision standard. A useful mandate identifies the borrower perimeter, proposed instrument, holding period, decision owner and failure condition. Examples include:

- ♦ • Can the borrower service a proposed EUR 300 million term loan through a cyclical downside without relying on refinancing?
- ♦ • What debt level preserves at least EUR 20 million of minimum liquidity and 20% covenant headroom?

- ♦ • Which legal entities generate cash, which entities owe the debt, and what value reaches the lender in a restructuring?
- ♦ • Does a lower-priced junior instrument compensate for its weaker position after liquidity and loss severity are included?

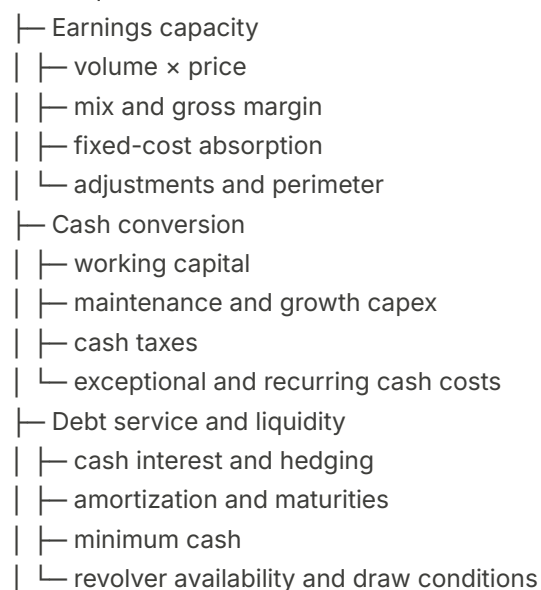
The decision standard then determines the evidence plan.

Table 27.1 — Evidence register

Evidence field	Preferred record	Typical failure	Analyst response
Historical revenue and margin	Audited statements and reconciled management detail	Perimeter changes hide organic decline	Build a like-for-like bridge
Current trading	Closed monthly accounts, orders, volumes and prices	Preliminary data is treated as final	Mark status and reconcile later
Forecast	Driver-based model with accountable assumptions	Growth is a plug	Tie each driver to volume, price, capacity or contract
Adjustments	Itemized schedule with source and timing	“Run rate” has no implementation evidence	Haircut, delay or reject
Cash flow	Bank statements, cash-flow statement and working-capital schedules	EBITDA is treated as cash	Build a cash bridge
Debt	Executed instruments and agent statements	Slide totals omit local or contingent debt	Reconcile by entity and instrument
Covenants	Executed agreement and compliance certificate	Marketing definition replaces legal definition	Use the executed definition; flag counsel questions
Collateral and guarantees	Entity chart, security and guarantee records	Consolidated assets assumed to support all debt	Map grantor, asset, claim and release conditions
Market evidence	Dated observable prices and terms	Stale or incomparable quotes	Record timestamp, size and liquidity
Rating information	Current agency publications and rating rationales	Rating label used as an investment conclusion	Treat as one external opinion and verify definitions

Figure 27.1 — Credit driver tree

Credit question



- | — Documentation and structure
 - | — obligors, guarantors and collateral
 - | — covenant capacity and headroom
 - | — priority and intercreditor controls
 - | — transfer, amendment and release mechanics
- └ Downside value
 - | — entity-level enterprise or asset value
 - | — costs and priority claims
 - | — timing and additional funding
 - └ claim waterfall and recovery

Synthetic example 1 — service network driver tree. A fictional testing-and-maintenance group reports 8% revenue growth. The analyst separates this into 3% price, 2% acquired revenue and 3% volume. The volume increase is then split between existing capacity and new technicians. If the hiring plan is the only route to 3% volume, the forecast must include recruitment cost, training time and working-capital requirements. A single revenue-growth cell is not an operating case.

27.3 Reconcile EBITDA before using it

Adjusted EBITDA is a claim, not a starting fact. Every addition should be tested on five dimensions:

- ♦ 1. **identity** — what cost or revenue is being adjusted;
- ♦ 2. **source** — where the amount is evidenced;
- ♦ 3. **recurrence** — whether the item is genuinely non-recurring;
- ♦ 4. **realization** — whether the benefit has been achieved; and
- ♦ 5. **overlap** — whether it appears elsewhere in the forecast or purchase-price bridge.

Worked calculation 1 — reported to adjusted to underwritten EBITDA

Fictional issuer **Asteron Field Services** reports EUR 56.0 million of EBITDA for the last twelve months. Management presents EUR 68.0 million of adjusted EBITDA.

Item	Management bridge (EURm)	Underwriting treatment	Underwritten amount (EURm)
Reported EBITDA	56.0	Starting record	56.0
Closed-site restructuring cost	4.0	Half supported as non-recurring; half resembles ordinary reconfiguration	2.0
Procurement savings	5.0	Contracts signed, but only 40% realized in the run rate	2.0
Acquisition synergies	3.0	No completed actions or owner; exclude	0.0
Total	68.0		60.0

The management adjustment is EUR 12.0 million. The underwritten addition is EUR 4.0 million, so underwritten EBITDA is:

EUR 56.0m + EUR 2.0m + EUR 2.0m = EUR 60.0m.

The EUR 8.0 million difference is not “conservatism” in the abstract. It is a documented judgment about recurrence and realization. If later evidence shows that procurement savings are fully in the run rate, the bridge can be updated without rewriting the history of the decision.

Table 27.2 — Adjustment challenge matrix

Adjustment type	Evidence that may support it	Frequent weakness	Scenario treatment
Cost already removed	Payroll, lease termination, supplier cancellation	Cash cost or stranded cost omitted	Include benefit and implementation cash separately
Run-rate saving	Executed contract and realized unit cost	Volume or inflation assumption offsets saving	Net the interaction
Acquisition contribution	Closed acquisition and post-close records	Pro forma period or perimeter inconsistent	Align period and ownership
Exceptional loss	Incident record and insurance status	Similar losses recur	Retain normalized recurring amount
Revenue synergy	Signed customer orders	Pipeline treated as contracted	Probability-weight or exclude
New-site EBITDA	Commissioning evidence and capacity ramp	Full utilization assumed immediately	Phase the ramp and working capital

Synthetic example 2 — distributor rebate. A distributor adds EUR 3 million of supplier rebates to adjusted EBITDA because the rebate was booked below its chosen operating measure. If the cash is contingent on annual purchase volume and the forecast assumes lower purchases, the analyst must model the condition rather than mechanically add the rebate. Presentation location does not determine economic availability.

27.4 Bridge earnings to cash

The earnings-to-cash bridge should be built before leverage is interpreted. A borrower can show stable EBITDA while cash weakens because receivables extend, inventory rises, supplier terms tighten, capital expenditure is deferred and then catches up, or cash taxes increase.

Figure 27.2 — Earnings-to-cash bridge

Underwritten EBITDA

- cash taxes
- maintenance capital expenditure
- working-capital outflow
- recurring cash items outside EBITDA
- = pre-interest free cash flow
- cash interest and recurring financing fees
- = post-interest free cash flow
- mandatory amortization
- = cash available for optional debt reduction / retained liquidity

Worked calculation 2 — cash conversion

Using Asteron's EUR 60.0 million underwritten EBITDA:

Cash item	EURm
Underwritten EBITDA	60.0
Cash taxes	(7.0)
Maintenance capex	(9.0)
Working-capital outflow	(5.0)
Recurring provisions and other cash items	(2.0)
Pre-interest FCF	37.0
Cash interest and recurring financing fees	(16.0)
Post-interest FCF	21.0

Pre-interest cash conversion is $37.0 / 60.0 = 61.7\%$. Post-interest cash conversion is $21.0 / 60.0 = 35.0\%$. Both percentages are mathematically correct, but they answer different questions. The first describes operating cash available before financing; the second describes cash retained after the selected interest burden. A committee paper must name the numerator.

Worked calculation 3 — gross and net leverage

Assume gross debt of EUR 300 million and reported cash of EUR 28 million. Of that cash, EUR 10 million is restricted and EUR 8 million is minimum operating cash. Eligible surplus cash is therefore EUR 10 million.

- ♦ • Gross leverage: $300 / 60 = 5.00x$.
- ♦ • Net debt: $300 - 10 = \text{EUR } 290\text{m}$.
- ♦ • Net leverage: $290 / 60 = 4.83x$.

Netting the full EUR 28 million would produce $272 / 60 = 4.53x$, but that result assumes cash is both accessible and surplus. The 0.30x difference is not a rounding issue; it is a structural and liquidity assumption. Chapter 28 develops the cash-access map, while Chapters 24 and 26 address entity and claim position.

Worked calculation 4 — coverage measures

With cash interest of EUR 16 million:

- ♦ • EBITDA interest coverage: $60 / 16 = 3.75x$.
- ♦ • Pre-interest FCF coverage: $37 / 16 = 2.31x$.
- ♦ • If annual mandatory amortization is EUR 8 million, fixed debt-service coverage using pre-interest FCF is $37 / (16 + 8) = 1.54x$.

The three ratios are coordinated but not interchangeable. EBITDA coverage ignores tax, capex and working capital. Pre-interest FCF coverage includes them. Debt-service coverage also includes scheduled principal. None answers whether the borrower has enough cash in the weakest month.

Synthetic example 3 — seasonal manufacturer. A manufacturer generates 70% of annual EBITDA in the second half but builds inventory in the second quarter. Annual post-interest FCF is positive, yet the low point occurs before the main selling season. The credit case needs a monthly or quarterly liquidity path; an annual cash number cannot prove the revolver will remain available at the trough.

27.5 Debt schedule, liquidity and covenant runway

Liquidity is path-dependent. Start with accessible cash, then show operating cash movement, mandatory debt service, financing costs, committed capacity and the conditions that govern access. A revolver should not be counted as available merely because it is undrawn: the borrower may face borrowing conditions, a springing test, a borrowing-base constraint, a clean-down or a default drawstop.

Table 27.3 — Debt schedule

Instrument	Opening balance (EURm)	Cash rate	Annual cash interest (EURm)	Amortization	Maturity	Structural note
Super-senior RCF	0	6.5%	0.0 before drawings	Bullet	2029	First in selected enforcement waterfall
First-lien term loan	240	5.0%	12.0	1% = 2.4	2031	Borrower and guarantor group
Local equipment facility	30	7.0%	2.1	5.0	2028	Claim at non-guarantor operating entity
Holdco note	30	6.3%	1.9	Bullet	2032	Relies on distributions from below
Total	300		16.0	7.4		

The weighted average interest rate is not enough. The equipment facility amortizes faster and sits at a different entity. The RCF may be undrawn today but can become the most senior funded claim in a downside. The holdco note has no direct claim on operating cash in this fictional structure.

Worked calculation 5 — twelve-month liquidity runway

Assume opening accessible cash of EUR 20 million, minimum cash of EUR 10 million and a EUR 40 million RCF. The table shows cash movement after operating receipts and disbursements but before RCF action.

Quarter	Base cash change (EURm)	Downside cash change (EURm)	Severe cash change (EURm)
Q1	(6)	(10)	(14)
Q2	(8)	(14)	(20)
Q3	+12	+5	(2)
Q4	+18	+10	+4
Full year	+16	(9)	(32)

- ♦ • Base case trough after Q2: $20 - 6 - 8 = \text{EUR } 6\text{m}$. To preserve EUR 10 million minimum cash, the borrower draws EUR 4 million.
- ♦ • Downside trough after Q2: $20 - 10 - 14 = \text{negative EUR } 4\text{m}$. It needs EUR 14 million of RCF drawings to preserve minimum cash.
- ♦ • Severe trough after Q2: $20 - 14 - 20 = \text{negative EUR } 14\text{m}$. It needs EUR 24 million at Q2. After Q3 it needs EUR 26 million; after Q4 it needs EUR 22 million.

The severe case appears funded because the peak draw is EUR 26 million against a EUR 40 million commitment. That is not yet an availability conclusion. The analyst must test whether the springing covenant, draw conditions and any letters-of-credit usage reduce actual capacity. If EUR 12 million is reserved for letters of credit, cash borrowing capacity is EUR 28 million and severe headroom at the trough is only EUR 2 million.

Worked calculation 6 — covenant headroom

Assume the executed covenant uses a fictional net-leverage definition with covenant EBITDA of EUR 64 million, permitted cash netting of EUR 20 million and a 5.50x threshold. Tested debt is EUR 300 million.

- ♦ • Covenant net debt: $300 - 20 = \text{EUR } 280\text{m.}$
- ♦ • Tested leverage: $280 / 64 = 4.38\text{x.}$
- ♦ • Maximum covenant net debt: $64 \times 5.50 = \text{EUR } 352\text{m.}$
- ♦ • Nominal net-debt headroom: $352 - 280 = \text{EUR } 72\text{m.}$

If a downside reduces covenant EBITDA to EUR 52 million and net debt rises to EUR 306 million after an RCF draw, tested leverage becomes $306 / 52 = 5.88\text{x}$, above the 5.50x threshold. The covenant breach appears before the annual case runs out of total committed liquidity. This is why covenant runway and cash runway must be shown together. Chapter 15 explains financial-covenant mechanics and Chapter 16 the sensitivity of EBITDA definitions.

Table 27.4 — Liquidity controls

Control	Base question	Downside question
Minimum cash	What is required for payroll, suppliers and volatility?	Does stress increase the requirement?
Revolver	How much is legally and operationally available?	Do drawstops, tests or LC usage reduce it?
Working capital	What is normal seasonality?	Do customers stretch payment or suppliers tighten terms?
Interest	What is fixed, floating and hedged?	What happens at the cap, floor or hedge expiry?
Maturity	What must be repaid from cash?	Is refinancing assumed before evidence supports it?
Covenant	What is tested and when?	Which scenario produces the first failure?

27.6 Put qualitative risk into the scenarios

Qualitative analysis is not a separate essay after the model. It identifies the mechanisms that change the model. The analyst should translate each material risk into a driver, timing path, observable indicator and possible response.

Table 27.5 — Risk-to-scenario translation

Risk	Financial transmission	Scenario variable	Early indicator
Customer concentration	Lost volume and negative operating leverage	Revenue retention and gross margin	Tender result, order backlog, churn
Input-cost inflation	Margin compression and working-capital need	Unit cost, inventory and payable days	Purchase orders and supplier notices
Labour scarcity	Capacity limit and wage pressure	Utilization, headcount and wage rate	Vacancies, overtime and attrition
Contract repricing lag	Temporary margin compression	Price realization delay	Renewal calendar and customer notices
Management execution	Delayed savings or capex overrun	Realization rate and cash cost	Milestone completion and owner accountability
Sponsor distribution	Reduced cash and higher debt	Distribution and incremental debt	Board materials and covenant capacity
Documentation flexibility	Leakage or priority dilution	Debt, lien and investment capacity	Compliance certificate and amendment activity
Refinancing risk	Higher interest or maturity wall	Exit rate, amortization and fees	Market access and maturity coverage

Synthetic example 4 — customer loss. A healthcare-services supplier derives 22% of revenue from one customer. A downside should not simply cut EBITDA by 22%. It should model lost revenue, avoided variable cost, stranded fixed cost, working-capital release, restructuring cash and the time needed to replace volume. If EUR 22 million of revenue carries a 35% contribution margin, the first-year EBITDA effect before mitigation is EUR 7.7 million, not EUR 22 million. If management removes EUR 2 million of fixed cost after six months at a EUR 1 million cash cost, the timing bridge matters.

Synthetic example 5 — sponsor support. A sponsor may have capital and incentives, but support is not a repayment source unless legally committed and available on its terms. The base case can show a voluntary equity contribution as an upside or mitigation, while the lender case should remain viable without it unless the commitment is enforceable and funded. Track record informs judgment; it does not create an obligation.

Worked calculation 7 — qualitative event translated into liquidity

Assume the customer-loss example reduces EBITDA by EUR 7.7 million, releases EUR 3.0 million of working capital, requires EUR 1.0 million of restructuring cash and saves EUR 1.0 million of fixed cost in the first year.

- ♦ • EBITDA reduction after first-year fixed-cost saving: $7.7 - 1.0 = \text{EUR } 6.7\text{m}$.
- ♦ • Cash effect before interest and tax: $-7.7 + 3.0 - 1.0 + 1.0 = \text{negative EUR } 4.7\text{m}$.

The EBITDA decline and cash decline differ because the working-capital release partially offsets the operating loss while restructuring uses cash. In later periods the working-capital benefit does not repeat. The analyst should therefore avoid applying the first-year cash conversion mechanically to the second year.

27.7 Entity and claim architecture comes before recovery

Recovery analysis begins with a map of entities, assets and claims. Consolidated enterprise value is not automatically available to every creditor. Guarantees, collateral, local liabilities, intercompany claims, super-senior facilities, enforcement costs and time all affect distribution. Chapter 24 develops guarantee and collateral architecture; Chapter 26 develops distressed value and process boundaries.

Figure 27.3 — Entity and value waterfall

Operating Sub A (guarantor) — cash / assets —
└─ Guarantor value pool
Operating Sub B (guarantor) — cash / assets —
└─
└─ enforcement / process costs
└─ super-senior claims
└─ first-lien claims

Local Sub C (non-guarantor) — local value — local debt — residual upstream value

Holdco — share value and permitted distributions — holdco note

Worked calculation 8 — entity-level recovery

Fictional downside values and claims:

Value pool	Gross value (EURm)	Prior deductions (EURm)	Value reaching first-lien pool (EURm)
Guarantor operations	210	15 process and enforcement costs	195
Guarantor IP company	60	0	60
Non-guarantor local subsidiary	35	30 local debt	5
Total available before super-senior claim	305	45	260
Less super-senior RCF and hedging			(25)
Available to EUR 250m first-lien term loan			235

First-lien recovery before discounting for time is $235 / 250 = 94.0\%$. The EUR 35 million non-guarantor value is not added in full: local debt is paid from that fictional pool first. The EUR 60 million IP value is not counted again inside operating value; it is separately valued. If operating value already included the IP cash flows, the analyst would need to remove one of the two values.

Worked calculation 9 — timing and recovery present value

Suppose the EUR 235 million distribution is received in two years and the analyst uses a 12% annual discount rate for this synthetic sensitivity.

Present value = $235 / (1.12^2) = \text{EUR } 187.34\text{m}$.

Present-value recovery is $187.34 / 250 = 74.9\%$. The discount rate is an explicit teaching assumption, not a market quote or legal conclusion. The gap between 94.0% nominal and 74.9% present-value recovery shows why timing, additional funding and process cost matter.

Synthetic example 6 — asset value versus enterprise value. A fleet operator owns assets with a headline appraisal of EUR 100 million. If the going-concern forecast already includes the cash flows from that fleet, adding EUR 100 million to enterprise value double counts the same economic resource. Asset value may instead support a liquidation sensitivity or a separate secured pool, depending on ownership, liens, costs and legal realization.

27.8 Relative value needs one clock and one definition set

Relative value is not “the cheaper bond looks better.” Compare instruments using the same measurement date, horizon, default assumptions, recovery definitions, transaction costs and liquidity haircut. Documentation and catalysts are part of the comparison because two claims on the same issuer can have different obligors, collateral, maturity, call protection or amendment exposure.

Worked calculation 10 — one-period synthetic relative-value comparison

Assume one-year outcomes solely for teaching. Probabilities are analyst assumptions, not rating-derived default rates.

Input	Instrument A	Instrument B
Purchase price	96	93
Performance - case year - end proceeds, including cash coupon	103	101
Assumed default probability	6%	8%
Default - case proceeds	55	45
Liquidity/transaction - cost deduction	0.50	1.00

Expected proceeds before liquidity deduction:

- ♦ • A: $(94\% \times 103) + (6\% \times 55) = 100.12$.
- ♦ • B: $(92\% \times 101) + (8\% \times 45) = 96.52$.

After the stated deduction, expected proceeds are 99.62 for A and 95.52 for B. Simplified expected returns are:

- ♦ • A: $(99.62 / 96) - 1 = 3.77\%$.
- ♦ • B: $(95.52 / 93) - 1 = 2.71\%$.

The output does not prove A is attractive or B is unattractive. It shows that B's lower price does not compensate for the selected probability, recovery and liquidity assumptions. A proper analysis would add timing distributions, reinvestment, call behavior, taxes where relevant, scenario dependency and a current evidence record.

Rating outlooks and watches should be recorded as agency-specific signals, not converted into automatic price moves. Chapter 29 defines the source/version controls; Chapters 34 and 36 show how to keep teaching sensitivities separate from observed spread or fair value.

27.8A Business quality, management and refinancing

Numbers need a business explanation. A credit model should identify why customers buy, what makes them stay, which costs are fixed, where capacity sits and who controls the decisions that can add or remove debt. The point is not to award a qualitative score; it is to locate the operating mechanisms that determine cash and loss.

Revenue quality

Contracted revenue can still be volume-sensitive, cancellable or exposed to customer failure. Recurring revenue can require recurring sales effort and service expenditure. Backlog can include framework agreements with no minimum purchase. The analyst should therefore separate contracted minimums, recurring but cancellable activity, order backlog, pipeline and one-time projects. For each category, record price reset, termination, renewal, concentration and cash-collection terms.

Revenue resilience should then be tested through a cohort or bridge. Opening customers plus wins, losses, price and volume should reconcile to closing revenue. If the forecast depends on price, show the renewal calendar and lag. If it depends on volume, show capacity and customer demand. If it depends on acquisition, separate acquired EBITDA from organic performance and from any underwritten synergy.

Cost structure and operating leverage

Classify costs by economic behavior rather than financial-statement caption. Labour may be fixed over a quarter but variable over two years. Rent may be contractually fixed but reducible only after a lease expiry. Outsourcing may create variable cost while increasing supplier concentration. In the downside, state which costs move immediately, which move with delay and which require cash to remove.

An analyst who cuts revenue by 10% and leaves margin unchanged has assumed away operating leverage. An analyst who cuts every cost by 10% has assumed perfect flexibility. A more useful case identifies contribution margin, stranded cost, mitigation timing and implementation cash. That structure also allows management performance to be monitored against milestones rather than against a single EBITDA result.

Management and control environment

Management quality should be evidenced through forecasting accuracy, cash discipline, reporting, capital allocation and response to misses. Charisma, access and presentation quality are not substitutes. Compare prior budgets with actual results, record when adverse information was surfaced and inspect whether the team can reconcile EBITDA, cash and debt without unexplained plugs.

Controls matter most when the credit becomes stressed. A borrower that closes monthly accounts slowly, lacks entity-level cash visibility or cannot reconcile debt documents may have less time to act. The downside should include decision and reporting lag where material. The committee can then require specific reporting as a condition rather than merely calling governance “weak.”

Sponsor and financial policy

The sponsor analysis should cover transaction history, acquisitions, dividends, leverage choices, equity contributions and governance rights using attributable evidence. The lender case should not assume voluntary support. Conversely, it should not assume maximum extraction merely because capacity exists. Model the actions that are permitted, economically rational and consistent with the selected scenario, then identify document protections and monitoring triggers.

Incremental debt, distributions and acquisitions can change the numerator, denominator and entity perimeter at the same time. A pro forma acquisition may add EBITDA, consume cash, create debt and move assets outside the existing guarantor group. Review those effects together. Chapter 24 supplies the guarantor and collateral map; Chapters 15, 18, 19 and 21 provide the relevant covenant and debt-capacity context.

Refinancing as a scenario, not a plug

Maturity analysis should separate legal maturity, expected repayment, call or prepayment economics and the date at which a refinancing must begin. A base case may assume refinancing only if the assumption is visible and sensitized. Show required proceeds, expected debt balance, interest rate, fees, minimum cash and the market conditions or operating performance needed to execute.

For a EUR 250 million maturity, refinancing at par with 2% fees requires EUR 255 million before any minimum-cash or transaction requirement. If the new facility is limited to 4.5x underwritten EBITDA and forecast EBITDA is EUR 50 million, gross debt capacity is EUR 225 million. The EUR 30 million gap must be filled through cash, equity, asset proceeds, amortization or a different structure. Calling the maturity “refinanceable” does not close the gap.

Table 27.6A — Qualitative evidence to scenario map

Topic	Evidence	Model transmission	Committee condition
Customer retention	Cohort, contracts, renewal calendar	Revenue and working capital	Monthly retention and top-customer report
Cost flexibility	Payroll, leases, supplier terms	Margin and restructuring cash	Cost-action milestones
Management control	Budget accuracy and close timetable	Forecast confidence and response time	Timely monthly reporting
Sponsor policy	Attributable transaction history	Debt, distributions and equity cases	Leakage and debt controls
Refinancing	Maturity, proceeds need and market terms	Rate, fees and liquidity	Early refinancing plan and minimum runway

Qualitative conclusions should end in a testable proposition. “Strong market position” becomes a retention, margin or pricing assumption. “Supportive sponsor” becomes a case with and without committed equity. “Manageable maturity” becomes a proceeds bridge. When the statement cannot be translated or evidenced, it belongs in the open-items register, not the credit conclusion.

27.9 Integrated synthetic credit case — Asteron Field Services

This case assembles the chapter's modules. All figures are invented and denominated in EUR millions unless stated otherwise.

Business and capital structure

Asteron provides inspection, testing and maintenance services to industrial customers. Revenue is diversified across 600 customers, but the top customer represents 14%. Roughly 65% of work is scheduled or recurring under framework agreements; volumes remain dependent on customer maintenance budgets. Technicians are the main capacity constraint.

The financing consists of a EUR 240 million first-lien term loan, a EUR 40 million undrawn super-senior RCF and EUR 60 million of other debt, including EUR 30 million at a non-guarantor subsidiary. Opening reported cash is EUR 28 million; eligible surplus cash for the credit analysis is EUR 10 million.

Table 27.6 — Scenario assumptions

Driver	Base	Downside	Severe
Revenue growth	4%	(6%)	(14%)
EBITDA margin	15.0%	12.5%	10.0%
Working-capital movement	EUR 5m outflow	EUR 2m inflow	EUR 7m inflow
Maintenance capex	EUR 9m	EUR 8m	EUR 7m
Cash interest	EUR 16m	EUR 17m	EUR 19m
Restructuring cash	0	EUR 2m	EUR 5m

The working-capital inflow in the downside reflects lower activity and is not assumed to recur. The severe case also assumes that the revolver rate rises and no sponsor equity is provided.

Table 27.7 — Scenario outputs

Output	Base	Downside	Severe
Underwritten EBITDA	60.0	50.0	38.0
Pre-interest FCF	37.0	31.0	21.0
Post-interest FCF	21.0	14.0	2.0
Year-end gross debt	292.6	300.0	318.0
Eligible surplus cash	10.0	4.0	0.0
Net leverage	4.71x	5.92x	8.37x
EBITDA interest coverage	3.75x	2.94x	2.00x
Peak RCF draw	4	14	26
Covenant result	Pass	Marginal/fails under selected definition	Fail

Base year-end gross debt assumes EUR 7.4 million of mandatory amortization and no optional prepayment: $300 - 7.4 = 292.6$. Downside debt remains at EUR 300 million because the borrower uses cash generation to preserve liquidity and fund costs. Severe debt rises to EUR 318 million after drawings net of scheduled changes.

Table 27.8 — Credit judgment

Question	Evidence-based conclusion	Open evidence
Business resilience	Recurring work supports visibility, but labour capacity and customer budgets create operating leverage	Contract retention, technician productivity and renewal calendar
Earnings base	EUR 60m is supported only after rejecting EUR 8m of management adjustments	Monthly realization of procurement savings
Cash conversion	Base conversion is sound; quarterly seasonality creates a revolver need	Weekly cash forecast and customer collections
Leverage	Base leverage is elevated but deleverages modestly; downside reverses that path	Debt terms, hedging and permitted cash netting
Liquidity	Total commitment covers modeled trough, but LC usage leaves little severe-case headroom	RCF availability, draw conditions and LC schedule
Covenants	Downside may breach before total liquidity is exhausted	Executed definition, testing dates and cure mechanics
Recovery	First-lien nominal recovery is strong in the selected case but timing reduces present value	Entity values, lien records and process assumptions
Sponsor	Incentive may support mitigation; no support is underwritten	Fund capacity and any binding commitment

Provisional committee posture

The fictional credit would be **proceed-with-conditions for further underwriting**, not approved. Conditions would include: (1) a completed entity and collateral map; (2) confirmation of revolver availability and covenant mechanics; (3) evidence supporting the EUR 4 million underwritten adjustments; (4) a monthly liquidity case through the seasonal trough; (5) a documented hedging and interest sensitivity; and (6) downside controls on additional debt, leakage and collateral release. This posture is a teaching output, not transaction advice.

27.10 Credit committee output

A committee paper should make the decision easy to challenge. It should not hide open evidence in an appendix or present model precision as fact.

Before drafting the recommendation, reconcile conflicts among sources. Audited financial statements may use one perimeter, current management accounts another and the covenant certificate a third. None should be silently promoted as the single truth. Record the conflict, identify why the perimeters differ and select the measure appropriate to each question. For example, an acquisition completed halfway through the period may be consolidated in the latest balance sheet, partially reflected in reported earnings and included for a full period in a permitted covenant pro forma calculation. The committee paper should show all three views rather than label one "EBITDA."

Sector evidence requires the same discipline. A public industry statistic can frame a question but cannot substitute for borrower evidence. Define geography, customer segment, product, period, sample and measurement method before comparing a borrower with a benchmark. If a services borrower reports lower churn than a public sector average, determine whether the company measures logos, revenue or contracts and whether acquisitions reset the denominator. Unsupported "market standard" statements should be converted into diligence questions or removed.

The recommendation should also state its expiry conditions. A credit conclusion can become stale after a material acquisition, dividend, covenant amendment, ratings action, earnings miss or refinancing. Setting a decision date and refresh triggers prevents a committee paper from becoming permanent authority for a changed borrower.

Table 27.9 — Committee template

Section	Required content	Prohibited shortcut
Recommendation	Decision, amount, instrument, conditions and expiry	"Support" without conditions or perimeter
Sources	Dated evidence register and conflicts	Unattributed market statements
Business	Driver tree, concentration and resilience	Generic sector description
Earnings	Reported - to - underwritten bridge	Adjusted EBITDA copied from a presentation
Cash	Cash bridge, seasonality and minimum liquidity	Annual FCF only
Debt	Entity -level debt schedule and maturity profile	One consolidated debt number
Downside	Base, downside, severe and first breakpoint	Uniform EBITDA haircut with no mechanism
Covenants	Executed definitions, headroom and timing	Marketing covenant ratio
Recovery	Entity and claim waterfall, costs and timing	Enterprise value divided by debt
Relative value	Common date, definitions, liquidity and alternatives	Price comparison alone
Open items	Owner, deadline and decision impact	"To be confirmed" without consequence

Table 27.10 — Monitoring and escalation

Metric	Baseline	Warning	Escalation question
Revenue retention	96%	<92%	Which customers and contribution margins are lost?
EBITDA adjustment realization	EUR 4m	<EUR 2m	Does underwritten EBITDA need to be reset?
Receivable days	58	>68	Is liquidity pressure operational or customer-specific?
Accessible liquidity	EUR 30m	<EUR 18m	Are draw conditions and minimum cash still satisfied?
Net leverage	4.8x	>5.3x	Is the increase earnings-led, cash-led or debt-led?
Covenant headroom	20%+	<10%	What is the first breach date under the executed definition?
Top-customer share	14%	>18%	Has concentration risen through churn elsewhere?

27.11 Practitioner exercises

Exercise 1 — EBITDA bridge

A fictional borrower reports EUR 80 million of EBITDA and EUR 18 million of adjustments: EUR 6 million restructuring, EUR 5 million procurement, EUR 4 million acquisition synergies and EUR 3 million litigation cost. Evidence supports EUR 3 million of restructuring, EUR 2 million of procurement and the full litigation cost as exceptional; acquisition synergies remain a plan.

Task: Calculate underwritten EBITDA and list the evidence still needed.

Answer check: Underwritten additions are $3 + 2 + 0 + 3 = \text{EUR } 8\text{m}$; underwritten EBITDA is EUR 88 million. Evidence should cover cash implementation cost, recurrence, realized procurement pricing, litigation status, period alignment and overlap with the forecast.

Exercise 2 — Liquidity breakpoint

Opening accessible cash is EUR 15 million, minimum cash EUR 8 million and cash-available RCF capacity EUR 25 million. Quarterly cash changes are negative EUR 9 million, negative EUR 12 million, positive EUR 6 million and positive EUR 10 million.

Task: Calculate peak draw and year-end draw, preserving minimum cash.

Answer check: After Q1, draw EUR 2 million to restore cash to EUR 8 million. After Q2, draw another EUR 12 million, so peak draw is EUR 14 million. Q3 reduces the draw to EUR 8 million and Q4 repays it fully, leaving EUR 2 million above minimum cash. The facility appears sufficient, subject to draw conditions and other usage.

Exercise 3 — Recovery without double counting

Enterprise value of a guarantor business is EUR 180 million and includes an owned brand. A separate appraisal values the brand at EUR 40 million. Process costs are EUR 10 million, super-senior claims EUR 20 million and first-lien claims EUR 200 million.

Task: Calculate recovery if the enterprise value already includes the brand.

Answer check: Do not add the EUR 40 million again. Value for first lien is $180 - 10 - 20 = \text{EUR } 150\text{m}$; recovery is $150 / 200 = 75\%$ before timing. A separate brand value may be used only in an alternative case that removes it from enterprise value or proves a distinct pool.

Exercise 4 — Relative value diagnosis

Two fictional instruments have the same issuer. Instrument X is first lien, price 98, one-year performance proceeds 105 and default proceeds 65. Instrument Y is unsecured, price 90, performance proceeds 99 and default proceeds 30. Assume default probabilities of 5% and 8%, respectively, and ignore timing and costs.

Task: Calculate simplified expected returns and identify at least four missing controls.

Answer check: X expected proceeds are $(95\% \times 105) + (5\% \times 65) = 103.0$; return is $103 / 98 - 1 = 5.10\%$. Y expected proceeds are $(92\% \times 99) + (8\% \times 30) = 93.48$; return is $93.48 / 90 - 1 = 3.87\%$. Missing controls include evidence for probabilities and recoveries, liquidity, timing, call behavior, documentation, transaction cost, tax, catalyst and scenario dependency.

Appendix 27A — Source and evidence checklist

- ✦ 1. Record the exact decision, borrower perimeter, instrument, date, currency and units.
- ✦ 2. Tag every material number as reported fact, management claim, analyst assumption or calculation.
- ✦ 3. Reconcile historical periods for acquisitions, disposals and accounting changes.
- ✦ 4. Preserve the reported-to-adjusted-to-underwritten EBITDA bridge.
- ✦ 5. Tie cash-flow inputs to cash records and explain non-cash or timing differences.
- ✦ 6. Reconcile debt by entity, instrument, funded amount, commitment, maturity and priority.
- ✦ 7. Use executed covenant definitions and record unresolved legal interpretation for counsel.
- ✦ 8. Map cash accessibility, minimum cash and revolver conditions.
- ✦ 9. Show base, downside, severe and first-breakpoint cases with formulas.
- ✦ 10. Build recovery by entity and claim; prevent value and claim double counting.
- ✦ 11. Time-stamp market prices, terms, ratings and public sources.
- ✦ 12. Record open evidence, accountable owner, deadline and decision impact.

Appendix 27B — Committee quality-control checklist

- ✦ • **Arithmetic:** every displayed total and ratio recalculates from displayed inputs.
- ✦ • **Definitions:** numerator, denominator, period, perimeter and units are explicit.
- ✦ • **Cash:** annual FCF is reconciled to the intra-year liquidity trough.
- ✦ • **Covenants:** the executed definition, testing date and cure assumptions are visible.
- ✦ • **Structure:** obligors, guarantors, collateral, non-guarantors and local claims are mapped.
- ✦ • **Downside:** stresses follow operating mechanisms rather than arbitrary percentages alone.
- ✦ • **Recovery:** costs, priority, timing and entity location are shown once.
- ✦ • **Relative value:** instruments use one date and consistent outcome definitions.
- ✦ • **Sources:** current public or controlled records are cited at point of use.
- ✦ • **Boundaries:** accounting, legal, tax, ratings and transaction-specific conclusions are referred to the appropriate professional.

The framework is complete only when another reviewer can trace the recommendation from source to assumption, from assumption to formula and from formula to decision. A polished ratio page without that chain is presentation, not underwriting.

Working Capital and Cash Management in LBO Structures

Teaching and professional boundary. *This chapter is an independently written finance-side framework using invented companies, accounting policies, transaction definitions and numbers. IFRS terminology is used only as a clearly identified educational reference point. The executed acquisition agreement, financing documents, applicable accounting policies, governing law and jurisdiction-specific tax and legal advice control a real transaction. No private agreement, closing statement or client fact is reproduced.*

Working capital can move value three times in one transaction. It affects the purchase price at closing, the cash required to operate after closing and the borrower's capacity to service debt. The same receivable, inventory balance or supplier liability can therefore appear in an accounting schedule, a price-adjustment mechanism, a liquidity forecast and a leverage analysis. The analyst's central control is to keep those uses connected without allowing the same item to be counted twice.

The chapter uses IFRS presentation concepts as of 12 July 2026 only to establish a public accounting reference point. IAS 1 addresses current and non-current presentation, while IAS 7 addresses the statement of cash flows. Neither standard supplies the transaction definition of net working capital, determines whether cash is legally accessible, or allocates value between buyer and seller. IFRS Foundation, IAS 1 overview (<https://www.ifrs.org/issued-standards/list-of-standards/ias-1-presentation-of-financial-statements/>); IFRS Foundation, IAS 7 overview (<https://www.ifrs.org/issued-standards/list-of-standards/ias-7-statement-of-cash-flows.html/>), checked 12 July 2026.

28.0 Learning objectives

By the end of this chapter, the reader should be able to:

- ♦ 1. keep accounting working capital, transaction net working capital, operating working capital and available liquidity separate;
- ♦ 2. construct a target and closing true-up under one definition, hierarchy, policy set and cut-off;
- ♦ 3. compare completion accounts and locked-box mechanisms without treating either as universally preferable;
- ♦ 4. map unrestricted, restricted, trapped and minimum cash by legal entity and permitted use;
- ♦ 5. analyse physical and notional pooling, upstreaming, working-capital facilities, super-senior priority and excess-cash-flow sweeps;
- ♦ 6. prevent overlap among working capital, EBITDA adjustments, debt-like items, leakage and purchase-price adjustments; and
- ♦ 7. prepare an independent-accountant dispute package and connect the result to funding and post-closing liquidity.

28.1 Definitions and the four measures

Term	Finance-side definition used here	What controls in a live case
Accounting working capital	Current assets less current liabilities, or another clearly stated accounting presentation subtotal	Applicable reporting framework and policies
Operating working capital	Operating receivables plus operating inventory and selected operating assets, less operating payables and selected operating liabilities	Analyst definition and cash-cycle purpose
Transaction net working capital	The exact assets and liabilities included in a purchase-price adjustment	Executed acquisition agreement and accounting hierarchy
Target	Agreed benchmark against which closing transaction NWC is compared	Agreement, schedule and target methodology
True-up	Purchase-price adjustment produced by comparing actual closing NWC with target under the agreed direction	Agreement formula and dispute process
Locked box	Price mechanism anchored to accounts at a date before closing, typically combined with leakage controls	Executed agreement and specified accounts
Completion accounts	Post-closing accounts used to determine one or more price adjustments	Executed agreement, policies and timetable
Leakage	Transfer of value within the agreement's defined leakage perimeter during the locked-box period	Defined permitted and prohibited leakage
Restricted cash	Cash whose use or exchange is constrained under the applicable facts or framework	Account terms, regulation, contracts and accounting evidence
Trapped cash	Cash not practically or legally available to the relevant debt-paying entity on the required timetable	Entity, legal, tax and document analysis
Minimum cash	Cash the business needs to operate through ordinary volatility	Operating model and liquidity policy
Cash pooling	Arrangement coordinating account balances or funding among participating entities	Bank documents, entity participation and local advice
Notional pooling	Arrangement in which balances may be notionally offset for interest without necessarily transferring legal ownership	Pool agreement and bank mechanics
Excess cash flow (ECF)	Contract-defined cash-flow amount used to determine a mandatory prepayment	Executed financing definition and ordering
Debt-like item	Transaction classification for a liability or economic obligation treated like debt for price purposes	Executed transaction definition
Independent accountant	Expert appointed under a transaction dispute mechanism to determine specified accounting items	Appointment clause, remit and standard of review

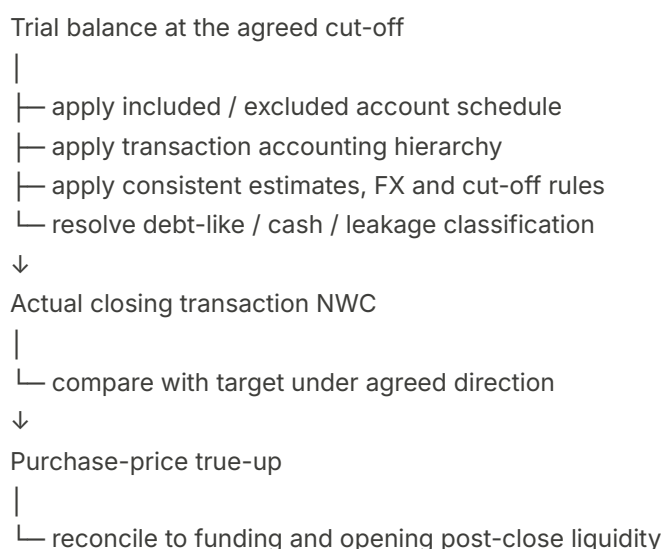
These definitions produce four separate measures:

Table 28.1 — The four-measure control

Measure	Illustrative formula	Primary purpose	Common error
Accounting working capital	Current assets – current liabilities	Financial-statement presentation	Treated as the transaction definition
Operating working capital	Receivables + inventory – payables	Cash-cycle analysis	Includes cash, debt or tax without explanation
Transaction NWC	Included assets – included liabilities	Purchase-price adjustment	Target and actual use different policies
Available liquidity	Accessible cash + usable facilities – minimum cash needs	Debt-service and survival analysis	Consolidated cash treated as immediately fungible

The four measures may start from overlapping ledger accounts, but they are not interchangeable. Transaction NWC might exclude cash and debt, include selected accruals, or apply specific classification rules. Operating working capital may exclude items that do not move with revenue. Available liquidity then asks a different question: which cash and facilities can actually be used by the entity that must make the payment?

Figure 28.1 — Target and true-up flow



28.2 Target construction and the one-policy rule

A target should represent the working capital expected to be delivered with the business under the agreed perimeter and policy set. It is not necessarily the last reported balance, a twelve-month average or a seller-selected normalized number. The method should reflect seasonality, growth, acquisitions, changes in supplier terms and exceptional events.

The **one-policy rule** requires target and actual to use:

- ♦ • the same included and excluded accounts;
- ♦ • the same accounting hierarchy and estimation methods;
- ♦ • the same foreign-exchange approach;
- ♦ • the same treatment of overdue, doubtful or disputed balances;
- ♦ • the same cut-off and accrual principles; and
- ♦ • the same classification boundary among working capital, cash, debt-like items and leakage.

Table 28.2 — Definition hierarchy

Priority	Record	Purpose
1	Specific transaction definition and schedule	Controls included/excluded items
2	Specific transaction accounting policies	Controls classification and measurement
3	Agreed illustrative examples	Resolves identified fact patterns if drafted consistently
4	Stated historical accounting policies	Fills gaps only within the contractual hierarchy
5	Applicable accounting framework	Residual reference, subject to agreement

The order is fictional and must not be assumed in a live contract. The executed document determines its own hierarchy. The practitioner should convert that hierarchy into a line-by-line schedule before calculating the target.

Worked calculation 1 — closing true-up

Fictional acquisition **Northbank Components** has a target transaction NWC of EUR 32 million. Closing balances under the agreed schedule are:

Included item	EURm
Trade receivables	47
Inventory	31
Other included operating assets	4
Trade payables	(39)
Included accruals	(16)
Actual transaction NWC	27

Actual NWC is $47 + 31 + 4 - 39 - 16 = \text{EUR } 27\text{m}$. If the agreement provides a euro-for-euro increase when actual exceeds target and a decrease when actual is below target:

True-up = $27 - 32 = \text{negative EUR } 5\text{m}$.

The purchase price decreases by EUR 5 million. That arithmetic is simple; the dispute usually concerns whether each balance belongs in the schedule and whether the same policy produced both target and actual.

Synthetic case 1 — buyer and seller direction. If actual NWC were EUR 35 million against the same EUR 32 million target, the adjustment would be positive EUR 3 million. The buyer receives more operating working capital but pays for it under the selected mechanism. This does not show that the buyer is economically better off: the quality and collectability of receivables and inventory still matter.

Worked calculation 2 — two-way target sensitivity

Assume actual closing NWC is EUR 34 million.

Target (EURm)	Actual less target (EURm)	Price direction
30	+4	Increase by 4
32	+2	Increase by 2
34	0	No adjustment
35	(1)	Decrease by 1
38	(4)	Decrease by 4

Each EUR 1 million change in target moves price by EUR 1 million in this fictional straight-line mechanism. The sensitivity does not determine the correct target; it shows why the evidence supporting the target is economically material.

28.3 Seasonality and growth

A twelve-month average can misstate the working capital needed at closing if the business is seasonal or growing. The analyst should reconcile monthly balances to revenue and operating drivers, then identify which month or weighted period resembles the expected closing state.

Worked calculation 3 — seasonal target

Fictional distributor **Boreal Outdoor Supply** has the following transaction NWC profile:

Month	Revenue (EURm)	Receivables	Inventory	Payables	Transaction NWC
January	18	24	30	(20)	34
April	22	28	42	(26)	44
July	34	38	55	(34)	59
October	28	33	39	(29)	43
December	20	25	28	(23)	30

The simple average of the five displayed observations is $(34 + 44 + 59 + 43 + 30) / 5 = \text{EUR } 42\text{m}$. A July closing at EUR 42 million would understate the displayed July requirement by EUR 17 million. A December closing target of EUR 42 million may overstate ordinary year-end needs by EUR 12 million. The target should use a complete agreed dataset and account for expected growth rather than selecting the most favorable observation.

Synthetic case 2 — growth-adjusted target. Suppose next year's unit volumes are expected to be 10% higher and days metrics are stable. A working-capital target may need a volume adjustment. The analyst should apply the increase to the relevant receivables, inventory and payables drivers, not multiply the final target blindly if product mix and payment terms change.

Table 28.3 — Seasonality diagnostics

Diagnostic	Calculation	Interpretation
Receivable days	Receivables / revenue × period days	Collection timing and customer mix
Inventory days	Inventory / cost of sales × period days	Stock build, lead times and obsolescence
Payable days	Payables / purchases or cost base × period days	Supplier funding and term sustainability
Cash conversion cycle	Receivable days + inventory days – payable days	Directional operating-cash cycle
Monthly NWC / revenue	Transaction NWC divided by stated revenue period	Seasonality and scale comparison

The denominators must be consistent. Using annual revenue with month-end balances or cost of sales with a sales-tax-inclusive payable balance can create false precision.

28.4 Completion accounts and locked box

Completion accounts and locked-box mechanisms allocate different risks; neither removes diligence or drafting work.

Table 28.4 — Controlled comparison

Field	Completion accounts	Locked box
Price anchor	Closing balance sheet or specified closing measures	Historical balance sheet at locked-box date
Post-close adjustment	Usually present for specified measures	Usually limited; leakage claims may remain
Main accounting risk	Closing classification, estimate and cut-off	Reliability and aging of locked-box accounts
Main conduct risk	Actions affecting closing balances	Value transfer during locked-box period
Evidence focus	Closing trial balance, reconciliations and policies	Locked-box accounts, leakage covenant and cash bridge
Dispute focus	Included items, policies and measurement	Leakage identity, permitted leakage and amount

Synthetic case 3 — locked-box leakage. The locked-box date is 31 December and closing is 30 April. The fictional agreement identifies management fees to the seller group as leakage unless specifically permitted. A EUR 1.2 million fee is paid in February, of which EUR 0.4 million is listed as permitted leakage. The finance schedule records EUR 0.8 million of potential non-permitted leakage. Whether the item legally meets the definition is a document question; the calculation simply preserves the amount and evidence.

Worked calculation 4 — leakage and value bridge

Assume equity value at the locked-box date is EUR 180 million. Permitted leakage is EUR 0.4 million, non-permitted leakage is EUR 0.8 million and a fictional ticking amount adds EUR 1.5 million under the selected example.

Closing equity payment before other adjustments = $180 + 1.5 - 0.8 = \text{EUR } 180.7\text{m}$.

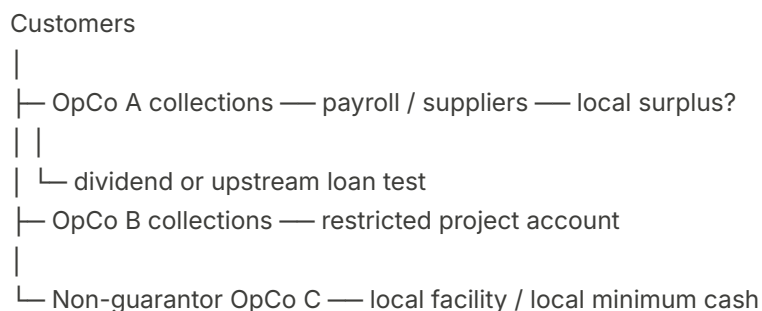
Permitted leakage is already reflected in the agreed economics and is not deducted again in this example. The schedule must avoid treating the same EUR 0.8 million as both leakage and a debt-like item unless the agreement expressly produces both consequences.

28.5 Cash is an entity-level resource

Consolidated cash can be distributed across entities, accounts, currencies and purposes. The credit question is not "how much cash does the group report?" It is "how much cash can the relevant obligor use, by the required date, after minimum operating needs and documented constraints?"

IAS 7 defines cash and cash equivalents for financial-reporting purposes and IAS 1 addresses current classification, including restrictions relevant to classification. Those presentation rules do not decide whether a lender may net cash, whether a subsidiary may upstream it, or whether a transaction agreement treats it as cash. IFRS Foundation, IAS 7 and IAS 1, checked 12 July 2026 (<https://www.ifrs.org/issued-standards/list-of-standards/ias-7-statement-of-cash-flows.html/>).

Figure 28.2 — Entity cash map



Permitted upstream cash

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Borrower / debt-service account

- |— interest and amortization
- |— minimum operating cash
- |— optional prepayment / retained liquidity

Table 28.5 — Cash-access register

Entity	Reported cash	Restriction or need	Accessible to borrower in model	Evidence required
Borrower	16	EUR 6m minimum cash	10	Bank statements and cash forecast
Guarantor OpCo A	12	EUR 3m local operating need	9	Distribution and document review
Project OpCo B	8	Restricted project account	0	Account and project terms
Non-guarantor OpCo C	12	EUR 10m trapped/local need	2	Local legal, tax and financing review
Total	48		21	

Worked calculation 5 — available liquidity

Assume a EUR 30 million revolver, of which EUR 4 million is used for letters of credit. Cash borrowing capacity is EUR 26 million. Accessible cash from Table 28.5 is EUR 21 million.

Gross available liquidity = 21 + 26 = EUR 47m.

If the borrower must retain a separate EUR 5 million contingency buffer not already included in the entity minimums, decision liquidity is EUR 42 million. That remains conditional on draw availability. The EUR 27 million difference between reported cash of EUR 48 million and accessible cash of EUR 21 million must not disappear inside a net-debt ratio.

Synthetic case 4 — trapped cash. A foreign non-guarantor generates cash but has a local facility, tax exposures and minority ownership. The finance model includes only the amount supported as available on the required timetable. It does not assert that a dividend or loan is legally permitted; that conclusion belongs to relevant advisers and executed documents.

28.6 Pooling, facilities and liquidity concentration

Cash pooling can reduce idle balances and improve interest economics, but the pool label does not prove cash is legally transferred, universally available or insulated from bank and entity risk.

Table 28.6 — Pool architecture

Field	Physical pool	Notional pool	Analyst control
Balance movement	Funds may transfer to a concentration account	Balances may remain in participant accounts	Confirm actual bank mechanics
Legal ownership	May change through transfers or intercompany positions	Often remains with participant, subject to documents	Do not infer fungibility
Interest	Calculated on concentrated balance	May be calculated on offset balances	Reconcile rate and fee terms
Credit exposure	Intercompany and bank exposures may arise	Set-off, guarantee or cross-default terms may matter	Map participant and counterparty risk
Restrictions	Entity, account, facility and local rules	Same, plus notional - pool eligibility	Obtain legal/tax review by relevant jurisdiction

Worked calculation 6 — notional-pool availability

A fictional pool contains three entities:

Entity	Account balance (EURm)	Eligible for notional offset?	Borrower - access assumption
A	+14	Yes	8 after minimum cash
B	+6	No	0
C	(9)	Yes	(9) drawing

The eligible notional net is $14 - 9 = \text{EUR } 5\text{m}$, but that is not the same as cash available to the borrower. Under the stated access assumptions, Entity A contributes EUR 8 million and Entity C uses EUR 9 million, so the group has a net EUR 1 million liquidity use. Entity B's EUR 6 million cannot be included merely because it appears in the consolidated cash balance.

Synthetic case 5 — pool restriction. If the bank removes Entity C from the pool after a covenant event, interest and funding economics change even if legal account balances do not. The downside model should test participant loss, bank concentration and replacement-funding time.

28.7 Supplier finance and the working-capital boundary

Supplier finance arrangements can affect liabilities, cash flows and liquidity risk. In May 2023 the IASB issued amendments to IAS 7 and IFRS 7 requiring additional disclosures about supplier finance arrangements, effective for annual periods beginning on or after 1 January 2024. The IFRS Foundation's public summary identifies terms, balance-sheet presentation, payment-date ranges and liquidity-risk information as disclosure areas. IFRS Foundation, "IASB increases transparency of companies' supplier finance," 25 May 2023 (<https://www.ifrs.org/news-and-events/news/2023/05/iasb-increases-transparency-of-companies-supplier-finance/>).

That accounting disclosure development does not decide transaction classification. The analyst should ask:

- ♦ • Is the liability included in transaction NWC, treated as debt-like, or excluded from both under the agreement?
- ♦ • Has the supplier already been paid by the finance provider?
- ♦ • Do payment terms differ from ordinary trade terms?
- ♦ • Is there concentration with the same bank that provides other liquidity?
- ♦ • What happens to cash needs if the arrangement is withdrawn?

Table 28.7 — Supplier-finance control

Record	Amount	NWC treatment	Debt-like treatment	Liquidity treatment
Ordinary trade payables	28	Included	Excluded	Normal payment profile
Supplier-finance liabilities	12	Excluded in fictional transaction definition	Included once	Repayment and withdrawal stress
Accrued capex	3	Excluded	Included once	Near-term cash use

The EUR 12 million supplier-finance liability cannot reduce NWC and also reduce price as debt-like unless the agreement deliberately specifies both effects. A control schedule should show one classification and the reason.

28.8 Excess-cash-flow sweeps

An ECF sweep follows the executed definition. The headline sweep percentage is only the last step. The analyst must build the defined base, deductions, credits, leverage step-downs, declined proceeds treatment and application order.

Table 28.8 — Fictional ECF build

Component	EURm
Consolidated net income starting point	26
Non-cash charges added	+8
Working-capital outflow deducted	(5)
Capital expenditure deducted	(9)
Specified cash taxes and other deductions	(4)
Fictional ECF base	16

Worked calculation 7 — sweep amount

Assume a 50% sweep rate and EUR 3 million of eligible voluntary-prepayment credit.

- ♦ • Gross sweep: $16 \times 50\% = \text{EUR } 8\text{m.}$
- ♦ • Net mandatory prepayment: $8 - 3 = \text{EUR } 5\text{m.}$

If the working-capital outflow had already reduced net income or another component under the fictional definition, deducting it again would be wrong. If the executed definition uses a different starting point or excludes a credit, the calculation changes. Chapter 25 of the Covenants Bible and Chapter 21 of this Book provide the wider debt-document context.

Synthetic case 6 — sweep and revolver interaction. A borrower generates EUR 5 million of ECF but expects a EUR 12 million seasonal cash need two months later. The finance analysis should show both the mandatory payment under the selected definition and the resulting revolver draw. A sweep can reduce term debt while increasing super-senior borrowing; gross debt reduction is not necessarily equal to the sweep amount at the seasonal trough.

28.9 Prevent double counting

Double counting can arise across four bridges:

- ♦ 1. EBITDA adjustments;

- ✦ 2. transaction NWC;
- ✦ 3. debt-like items and cash; and
- ✦ 4. leakage or other price claims.

Worked calculation 8 — overlap control

Fictional closing items:

- ✦ • EUR 12 million supplier-finance liability;
- ✦ • EUR 3 million accrued capex;
- ✦ • EUR 2 million unpaid annual bonus;
- ✦ • EUR 4 million receivable impairment already reflected in receivables.

Assume the fictional transaction definition excludes supplier finance and accrued capex from NWC and treats both as debt-like. The unpaid bonus remains in NWC. The receivable impairment already reduces the receivable balance.

Item	NWC effect	Debt-like effect	Other effect	Counted price effect
Supplier finance	0	(12)	0	(12)
Accrued capex	0	(3)	0	(3)
Unpaid bonus	(2)	0	0	(2 through NWC)
Receivable impairment	Included in net receivable	0	No separate claim	Reflected once
Total distinct downward effect				(17)

If the seller's EBITDA bridge also adds back the EUR 2 million bonus as non-recurring, the underwriting model must decide whether the expense is truly exceptional and whether the cash liability remains. Adding back the expense does not erase the closing cash obligation.

Table 28.9 — Double-count matrix

Item	EBITDA	NWC	Debt-like	Leakage	Control
Restructuring provision	Possible adjustment	Possible accrual	Possible debt-like item	Usually separate	Identify expense and cash obligation
Supplier finance	May affect metrics	Trade-liability question	Financing question	Not ordinarily leakage	One transaction classification
Deferred capex	Possible EBITDA-neutral	Usually excluded	Potential debt-like	Not ordinarily leakage	Reconcile commitment and cash timing
Management fee	Expense or add-back	Accrual possible	Possible payable	Possible leakage	Prevent triple claim
Bad-debt reserve	EBITDA and receivable effect	Net receivable	Usually not debt-like	Not leakage	Do not deduct gross receivable again

28.10 Downside liquidity after closing

The closing price mechanism and the post-close liquidity model should share an opening balance sheet. A buyer that receives a favorable NWC true-up may still face a liquidity problem if receivables are poor quality, inventory is obsolete or supplier terms normalize.

Worked calculation 9 — opening liquidity bridge

Assume purchase-price funding provides EUR 18 million of opening borrower cash. Closing NWC is EUR 5 million below target, producing a EUR 5 million price reduction. Of the shortfall, EUR 3 million arises from lower inventory and EUR 2 million from higher payables.

The EUR 5 million price reduction does not automatically add EUR 5 million to operating cash. It reduces funding paid to the seller, but the business may need to rebuild inventory and pay suppliers. If inventory rebuild uses EUR 3 million and payable normalization uses EUR 2 million during the first quarter, the economic benefit reverses through operating cash.

Opening cash after these uses is $18 - 3 - 2 = \text{EUR } 13\text{m}$. If minimum cash is EUR 10 million, the immediate cushion is only EUR 3 million.

Worked calculation 10 — four-quarter downside liquidity

Assume opening accessible cash of EUR 13 million, minimum cash of EUR 10 million and cash-available RCF capacity of EUR 25 million.

Quarter	Operating cash change	Mandatory interest/amortization	Net change	Required closing draw to preserve EUR 10m
Q1	(4)	(3)	(7)	4
Q2	(6)	(3)	(9)	13 cumulative
Q3	+7	(3)	+4	9 cumulative
Q4	+11	(3)	+8	1 cumulative

Peak draw is EUR 13 million in Q2. Year-end draw is EUR 1 million. The annual net change before draws is negative EUR 4 million, but the intra-year peak determines facility need. If EUR 8 million of the RCF is reserved for letters of credit, remaining cash capacity is EUR 17 million and Q2 headroom is EUR 4 million.

28.11 Independent-accountant disputes

An independent-accountant mechanism is not a second negotiation of the transaction. The dispute package should identify each item, the contract provision, the accounting hierarchy, the parties' positions, evidence, amount and decision requested. Legal questions about contractual interpretation may fall outside the accountant's remit; the executed clause controls.

Table 28.10 — Dispute register

Item	Buyer position	Seller position	Amount at issue	Evidence	Specialist boundary
Supplier finance	Debt-like, excluded from NWC	Trade payable in NWC	12	Agreements, payment terms, ledger	Contract and accounting review
Obsolete inventory	Reserve required	Reserve inconsistent with historical policy	4	Aging, sales, policy	Accounting determination
Unpaid bonus	Included liability	Exceptional and excluded	2	Payroll plan, accrual	Definition and accounting review
February fee	Non-permitted leakage	Permitted service charge	0.8	Invoice, services, schedule	Contract interpretation

The schedule should calculate the maximum, minimum and uncontested amount. If the four items above were entirely buyer-favorable, exposure is EUR 18.8 million; if entirely seller-favorable, it is zero. That range is not a forecast of the determination. It identifies funding and negotiation sensitivity.

Quality of working capital

A numerical target does not establish quality. Two businesses can deliver the same transaction NWC while carrying very different collection, obsolescence and supplier risks. The analyst should therefore supplement the balance with aging and movement schedules.

For receivables, analyse invoice date, due date, payment history, credit notes, disputes, concentration and post-close collections. A receivable that is current under a 120-day contractual term has a different liquidity profile from one due in 30 days. A large balance collected immediately after closing may validate existence and timing, but it may also be offset by a credit note or customer claim. Preserve gross balance, allowance and evidence separately.

For inventory, split raw materials, work in progress and finished goods. Record age, demand, lead time, ownership, location and reserves. Higher inventory can support service levels or signal slow-moving stock. A transaction target based on book value should not be interpreted as proof of realizable cash value. If the operating forecast assumes inventory reduction, show whether that reduction is compatible with revenue and supplier lead times.

For payables, distinguish ordinary trade terms, overdue balances, disputed invoices, capex creditors, taxes, payroll, supplier finance and amounts owed to related parties. Extending payable days can create a temporary cash benefit but may trigger supplier action or reverse after closing. The target methodology should not normalize receivable days while preserving an unsustainable payable extension unless the evidence supports that asymmetry.

Table 28.10A — Quality diagnostics

Balance	Quality field	Cash implication	Evidence
Receivables	Aging, disputes, concentration, credit notes	Collection delay or shortfall	Subsequent receipts and customer records
Inventory	Age, turns, reserve, location, ownership	Rebuild or write-off	Movement, sales and count records
Payables	Due dates, overdue status, supplier concentration	Normalization or supply interruption	Supplier statements and payment history
Accruals	Basis, reversal and payment timing	Near-term cash use	Calculation and subsequent settlement
Supplier finance	Provider, terms and due dates	Funding concentration and withdrawal risk	Program and bank records

Cut-off and manipulation resistance

Closing mechanisms can create incentives to accelerate collections, delay supplier payments, reduce purchases or change classification around the measurement date. The finance review should not presume misconduct; it should design controls that reveal timing effects.

Compare daily or weekly cash movement around closing with historical patterns. Review goods received but not invoiced, unbilled revenue, returns, rebates, credit notes and manual journals. Reconcile physical inventory movement with invoices and title. For a fast-closing service business, review accrued labour and subcontractor cost. For a distributor, review goods in transit and supplier ownership terms. The legal conclusion on title or risk of loss belongs to transaction counsel; the finance schedule identifies the item and amount.

If EUR 8 million of supplier payments normally due before month-end are paid three days after closing, closing cash may be EUR 8 million higher and payables EUR 8 million higher. Depending on the transaction definition, the NWC true-up may offset some or all of that benefit. The analyst should show both balances and avoid claiming an economic gain until the mechanism is applied.

Locked-box performance bridge

The locked-box period needs a cash and value bridge even when price is fixed. Start with the locked-box accounts, add operating profit and cash conversion, subtract capex, tax, financing and permitted value transfers,

and reconcile to closing cash and debt. Investigate unexplained differences rather than assuming the ticking amount compensates for them.

Suppose fictional locked-box net debt is EUR 70 million. During the four-month period, the business generates EUR 9 million of operating cash before interest, spends EUR 3 million on capex, pays EUR 2 million interest and makes EUR 1 million permitted leakage. Expected closing net debt before other movements is $70 - 9 + 3 + 2 + 1 =$ EUR 67m. If reported closing net debt is EUR 72 million, the EUR 5 million difference requires a reconciliation across working capital, tax, acquisitions, FX, restricted cash and classification. It is not automatically leakage.

Completion-accounts timetable

The workplan should align physical stock counts, bank confirmations, cut-off testing, draft delivery, review periods, dispute notices and expert determination. A short contractual timetable does not reduce the evidence needed; it increases the importance of prepared account mappings and issue owners. Before signing or closing, create a dry-run schedule using a recent month-end. That exposes ambiguous definitions while the parties can still resolve them deliberately.

The finance team should also reserve liquidity for the potential true-up. A buyer expecting a EUR 4 million upward adjustment should show how it will fund EUR 4 million plus any tax, interest or dispute cost under the actual agreement. A seller expecting a downward adjustment should avoid treating the full headline price as distributable before the process closes.

Finally, preserve a versioned issues log. Each proposed adjustment should have an amount, contractual reference, evidence owner, submission date, counterparty response and funding consequence. Separate agreed items from unresolved items and from matters deliberately reserved for legal or accounting determination. This prevents a late spreadsheet from silently changing the purchase-price bridge or the opening liquidity case. When an item is resolved, update the closing statement, sources and uses and first-hundred-days forecast together so the three artifacts remain reconcilable.

Table 28.11 — Evidence pack

Evidence class	Minimum record
Contract	Executed definition, hierarchy, schedules, examples and dispute clause
Accounting	Trial balance, account mapping, policies, estimates and cut-off support
Commercial	Customer and supplier terms, inventory movement and operational explanation
Cash	Bank statements, settlement evidence and post-close cash forecast
Governance	Position owner, review record, submission dates and reserved rights
Reconciliation	Target, actual, price bridge, funding bridge and opening liquidity

28.12 Coordinate price, funding and the first hundred days

The working-capital workstream is incomplete if it stops at the purchase-price adjustment. The closing statement should connect to sources and uses, opening debt, cash left in the business and the first operating forecast. This connection tests whether the buyer is funding the same requirement twice or not at all.

Consider a fictional transaction with EUR 200 million headline equity value, a EUR 32 million NWC target, EUR 20 million of cash treated as cash-free/debt-free value and EUR 150 million of acquisition debt. Actual NWC is EUR 27 million, so the price true-up is negative EUR 5 million. The business must also retain EUR 12 million of minimum cash at closing.

The funding schedule should show:

Funding bridge	EURm
Headline equity value	200
NWC true-up	(5)
Other selected price adjustments	0
Equity purchase price	195
Refinance selected existing debt	60
Fees and expenses	10
Minimum cash funded at closing	12
Total uses	277
Acquisition debt	150
Sponsor equity	127
Total sources	277

The EUR 5 million NWC shortfall reduces purchase price, but the EUR 12 million minimum-cash requirement remains a separate use. If the shortfall reflects depleted inventory or extended payables, the first-hundred-days forecast should include normalization. The sponsor cannot assume the price reduction permanently finances debt reduction while the business simultaneously needs the cash to restore operations.

The first-hundred-days bridge

Build the bridge weekly or monthly for the most volatile period. At minimum, include collections, supplier payments, payroll, tax, capex, interest, amortization, integration cash, inventory rebuild and any working-capital facility. Reconcile each opening balance to the closing statement.

Table 28.12 — First-hundred-days controls

Control	Closing record	Forecast link	Failure signal
Receivables	Customer-level aging and cut-off	Collection curve	Collections below opening quality assumption
Inventory	Quantity, cost and reserve	Sales and purchase plan	Rebuild or obsolescence above case
Payables	Supplier aging and agreed terms	Payment schedule	Rapid normalization or supplier hold
Supplier finance	Provider, due dates and classification	Facility withdrawal case	Concentrated near-term payment need
Minimum cash	Entity-level operating requirement	Weekly trough	Cash transferred away from operating entity
Revolver	Commitment, LC usage and draw conditions	Draw and repayment schedule	Availability below modeled peak
ECF/sweep	Contract-defined timing	Mandatory prepayment	Sweep precedes seasonal need

Working-capital facilities

Receivables facilities, inventory finance and supplier-finance arrangements can support liquidity while also changing priority, eligible assets and cash-flow timing. The finance analysis should record advance rates, reserves, concentration limits, eligibility, recourse, termination events and account control. Those fields are transaction-specific. Do not treat facility size as cash availability without an eligible-borrowing-base calculation and document review.

For example, a fictional EUR 25 million receivables facility has an 80% advance rate against EUR 24 million of eligible receivables, a EUR 2 million concentration reserve and EUR 6 million already drawn. Gross borrowing base is $24 \times 80\% = \text{EUR } 19.2\text{m}$. After the reserve it is EUR 17.2 million; undrawn availability is $17.2 - 6 = \text{EUR } 11.2\text{m}$, subject to all other conditions. The headline commitment overstates current availability by EUR 13.8 million.

Foreign currency and cut-off

When the target and actual include multiple currencies, specify the rate source, date and treatment of remeasurement. Applying historical average rates to the target and spot rates to actual can create a true-up driven by FX methodology rather than operating performance. The same principle applies to cut-off: goods shipped, services received, credit notes and rebates require one stated recognition boundary. A dispute schedule should separate quantity, price, FX and policy effects so the parties can see what actually moved.

Governance after closing

Assign owners for collections, inventory, supplier terms, pool access and facility reporting. Monitor both balance and days metrics, because growth can increase balances even when days are stable. Compare realized cash with the underwriting bridge and explain variance by volume, price, mix, timing and one-off items. If the first-hundred-days plan depends on releasing “excess” cash, confirm that the cash is accessible after minimum needs and document restrictions. A spreadsheet transfer does not move legal ownership or eliminate tax and creditor consequences.

28.13 Practitioner exercises

Exercise 1 — true-up and overlap

A target is EUR 25 million. Closing receivables are EUR 40 million, inventory EUR 20 million, payables EUR 24 million and included accruals EUR 8 million. A EUR 6 million supplier-finance liability is excluded from NWC and treated as debt-like.

Task: Calculate NWC, the true-up and total distinct downward price effect.

Answer check: NWC is $40 + 20 - 24 - 8 = \text{EUR } 28\text{m}$. True-up is positive EUR 3 million. Supplier finance creates a separate negative EUR 6 million debt-like effect. Net distinct effect is negative EUR 3 million ($+3 - 6$). Do not also deduct supplier finance in NWC.

Exercise 2 — cash access

Four entities report cash of EUR 10 million, EUR 9 million, EUR 7 million and EUR 5 million. Minimum cash is EUR 4 million, EUR 3 million, EUR 2 million and EUR 2 million. The third entity's remaining cash is restricted; the fourth entity's remaining cash is unavailable to the borrower in the model.

Task: Calculate modeled accessible cash.

Answer check: Entity 1 contributes 6; Entity 2 contributes 6; Entities 3 and 4 contribute zero. Accessible cash is EUR 12 million. Reported cash is EUR 31 million, so the EUR 19 million difference must remain visible.

Exercise 3 — ECF and seasonal liquidity

Fictional ECF is EUR 24 million, sweep rate 50% and eligible prepayment credit EUR 4 million. The resulting payment occurs before a seasonal EUR 9 million cash outflow. Opening surplus cash above minimum is EUR 8 million.

Task: Calculate the mandatory prepayment and subsequent borrowing need.

Answer check: Gross sweep is EUR 12 million; net prepayment is EUR 8 million. That uses all surplus cash. The later EUR 9 million seasonal outflow therefore requires a EUR 9 million draw, subject to availability. Term debt falls by EUR 8 million while super-senior debt rises by EUR 9 million at the trough.

Appendix 28A — Working-capital schedule template

Schedule field	Required entry
Account number and description	Exact ledger identity
Legal entity and currency	Ownership and FX perimeter
Included/excluded	Transaction definition reference
Target policy	Historical or agreed treatment
Actual policy	Confirmation of consistent treatment
Cut-off evidence	Invoice, receipt, dispatch or service date
Aging/quality	Overdue, obsolete, disputed or impaired amount
NWC treatment	Asset or liability amount
Debt-like/cash/leakage treatment	Separate classification, if any
Overlap flag	EBITDA, NWC, debt-like, leakage or other
Source and reviewer	File, date and accountable person
Dispute status	Agreed, open, submitted or resolved

Appendix 28B — Cash and dispute checklist

- ♦ 1. Reconcile reported cash to bank accounts by entity and currency.
- ♦ 2. Separate restricted, trapped and minimum cash from surplus accessible cash.
- ♦ 3. Record pool participants, bank rights, guarantees, set-off and removal conditions.
- ♦ 4. Map revolver commitments, LC usage, draw conditions and covenant interaction.
- ♦ 5. Reconcile transaction NWC to the exact definition and hierarchy.
- ♦ 6. Use one policy set for target and actual.
- ♦ 7. Test seasonality, growth, acquisitions and supplier-term changes.
- ♦ 8. Classify supplier finance, accrued capex, bonuses and provisions once for price.
- ♦ 9. Reconcile true-up or leakage outcomes to funding and opening liquidity.
- ♦ 10. Build a post-close monthly or quarterly cash runway through the trough.
- ♦ 11. Give the independent accountant only matters within the appointed remit.
- ♦ 12. Obtain accounting, legal and tax review for the exact retained propositions.

The governing discipline is simple to state and difficult to execute: one ledger item, one documented definition, one price treatment and one cash consequence. The analyst should be able to move from closing balance sheet to purchase-price bridge to opening liquidity without losing or duplicating a euro.

Rating Agencies in Leveraged Finance

Teaching, source and endorsement boundary. *This chapter is independently written from public materials checked on 12 July 2026. It does not reproduce a proprietary methodology, licensed dataset, agency model or unpublished rating analysis. Fitch Ratings, Moody's Ratings and S&P Global Ratings have not reviewed, approved or endorsed this chapter. Their current criteria, definitions and transaction-specific publications control their work. The synthetic cases and calculations below are the author's teaching devices, not ratings, rating predictions or investment recommendations.*

A credit rating is one external opinion within a larger credit process. It can affect distribution, investment mandates, documentation and structured-credit tests, but it does not replace independent analysis. The leveraged-finance practitioner must keep three records separate:

- ♦ 1. what an agency's current public terminology and criteria say;
- ♦ 2. what a selected instrument or investor document does with a rating; and
- ♦ 3. what the practitioner independently concludes about cash flow, loss and value.

Combining those records creates false precision. A rating category is not a universal probability of default, an instrument notch is not a fixed recovery percentage, and a split rating does not reveal which agency is "right."

The chapter is intentionally operational rather than predictive. It explains how to control facts, versions, document consequences and independent recovery work. It does not forecast a rating, state what information would guarantee a category, or compare agency "strictness." If a future edition adds a novel interpretation of agency criteria, an unpublished process claim or a prediction of agency action, that proposition must be removed, rewritten from current public material or routed to a qualified ratings practitioner before publication.

A public methodology can be summarized only within its stated scope and date. It may depend on related sector, group-linkage, recovery, hybrid, country or structured-finance criteria. The absence of a factor from this teaching chapter does not mean the agency ignores it. Conversely, a factor listed in public criteria does not prove how much weight it received in a particular committee decision. Transaction-specific rationale and the agency's own publications remain necessary.

29.0 Learning objectives

By the end of this chapter, the reader should be able to:

- ♦ 1. distinguish issuer, family, instrument and recovery constructs under each agency's current terminology without treating labels as interchangeable;
- ♦ 2. prepare a controlled information package and manage factual review, confidentiality, appeal and publication stages;
- ♦ 3. build an independent simplified recovery bridge while keeping agency methodology and analyst judgment separate;
- ♦ 4. extract rating-linked terms and CLO tests from the selected executed documents and current criteria;
- ♦ 5. analyse split ratings, outlooks and watches without assuming a fixed pricing response; and
- ♦ 6. discuss issuer-pays conflicts, oversight, sponsor support and fees without alleging bias, quoting generic ranges or implying agency endorsement.

29.1 Definitions and construct map

The following definitions are deliberately bounded. Agency terms must be read in the current agency publication identified in the source register.

Term	Educational meaning used here	Control
Issuer credit rating	An agency opinion concerning an issuer's general creditworthiness under that agency's definition	Do not assume it is an instrument rating
Corporate Family Rating (CFR)	A Moody's construct whose exact current definition belongs to Moody's published definitions	Do not translate it mechanically into another agency's issuer rating
Issuer Credit Rating (ICR)	An S&P Global Ratings construct whose exact current definition belongs to S&P's published definitions	Confirm local/foreign currency and other qualifiers where relevant
Issuer Default Rating (IDR)	A Fitch construct whose exact current definition belongs to Fitch's published criteria and rating definitions	Keep issuer default risk separate from instrument loss severity
Instrument rating	An opinion assigned to a specified obligation, incorporating the agency's applicable treatment of issuer risk and instrument features	Identify obligor, guarantee, collateral, ranking and jurisdiction
Recovery rating	An agency-specific opinion or scale concerning relative recovery prospects under its criteria	Do not treat as a promised cash recovery
Loss given default (LGD)	Loss severity conditional on default in a stated analytical framework	State whether it is a model input, output or agency construct
Notching	Difference between linked issuer and instrument rating levels under the applicable framework	No universal number or direction applies
Outlook	Agency-specific indication concerning possible rating direction over a stated horizon	Not itself a rating change
Watch	Agency-specific focused review status, sometimes branded differently by agency	Confirm direction, scope and definition
Preliminary rating	A rating status subject to the agency's stated conditions and final documentation or information	Not a final unconditional outcome
Appeal	Agency process through which identified issues may be reconsidered under current procedures	Not a negotiation for a desired category
Surveillance	Ongoing monitoring of an existing rating under the agency's process	Record information obligations and triggers
NRSRO	A credit rating agency registered with the U.S. Securities and Exchange Commission as a nationally recognized statistical rating organization	Registration is a regulatory status, not endorsement of a specific rating
CLO concentration test	Test in a selected CLO indenture concerning portfolio composition, often using rating-related definitions	The selected indenture and incorporated criteria control

Table 29.1 — Construct map, not equivalence table

Analytical level	Moody's terminology to verify	S&P terminology to verify	Fitch terminology to verify	What the practitioner records
Issuer or group	Corporate Family Rating and other applicable issuer constructs	Issuer Credit Rating and applicable qualifiers	Issuer Default Rating and applicable qualifiers	Entity perimeter, support and debt-paying capacity
Instrument	Instrument - specific rating	Issue credit rating	Instrument rating	Obligor, guarantee, collateral, rank and maturity
Recovery/loss	Applicable LGD or recovery framework	Applicable recovery and issue - rating framework	Recovery Rating and instrument - rating criteria where applicable	Independent claim waterfall and sensitivities
Directional signal	Outlook and review status under current definitions	Outlook and CreditWatch under current definitions	Outlook and Rating Watch under current definitions	Exact status, date and scope; no automatic price assumption

The table intentionally avoids placing rating symbols side by side. Cross-agency symbols and constructs can look similar while differing in scope, definition and analytical path. Use each agency's current definitions: Moody's, Rating Symbols and Definitions, public document endpoint (<https://ratings.moody.com/api/rmc-documents/53954>); S&P Global Ratings, Ratings Definitions (<https://www.spglobal.com/ratings/pt/regulatory/article/-/view/sourceId/504352>); Fitch Ratings, corporate criteria page (<https://www.fitchratings.com/criteria/corporate-finance>), all checked 12 July 2026.

29.2 What public criteria can and cannot do

Public criteria explain the agency's stated analytical framework, scope and limitations. They support a disciplined reading of a published rating, but they do not enable an outsider to reproduce a committee decision from a few ratios. The current Fitch Corporate Rating Criteria dated 9 January 2026 describe a global framework for non-financial corporate IDRs and instrument ratings and identify business profile, financial profile, governance and operating environment as relevant factors. The criteria also state that factor importance can vary. This chapter uses only that high-level public description. Fitch Ratings, Corporate Rating Criteria, 9 January 2026 (<https://assets.fitchratings.com/downloadFile?reportType=report&sfReport=false&slug=corporate-finance%2Fcorporate-rating-criteria-09-01-2026>).

Moody's public rating definitions and public corporate loss-given-default materials use Moody's own constructs; S&P's public rating definitions use S&P's constructs. A practitioner should record document title, publication or effective date, sector scope, geography, rating type and any related criteria. A screenshot or remembered threshold is not version control.

Table 29.2 — Source/version record

Field	Required entry
Agency and publishing entity	Exact name shown on source
Document title	Complete public title
Publication/effective date	Date shown by agency
Access date	Date retrieved for the analysis
Scope	Issuer, instrument, recovery, sector and geography
Related criteria	Documents the source says should be read with it
Supersession status	Active, replaced, archived or unclear
Permitted use	Independent summary, link and limited factual extraction
Prohibited use	Copying proprietary text/tables, implying endorsement or reconstructing licensed models

The document owner should refresh the record before publication and before a live transaction. A methodology can change while an old PDF remains accessible. An agency's current criteria index is therefore a better starting point than a local file name.

29.3 The controlled information package

The rating workstream should begin with the same reconciled facts used by lenders and investors, while respecting authorization, confidentiality and applicable policy. The agency remains responsible for its own analysis and committee outcome.

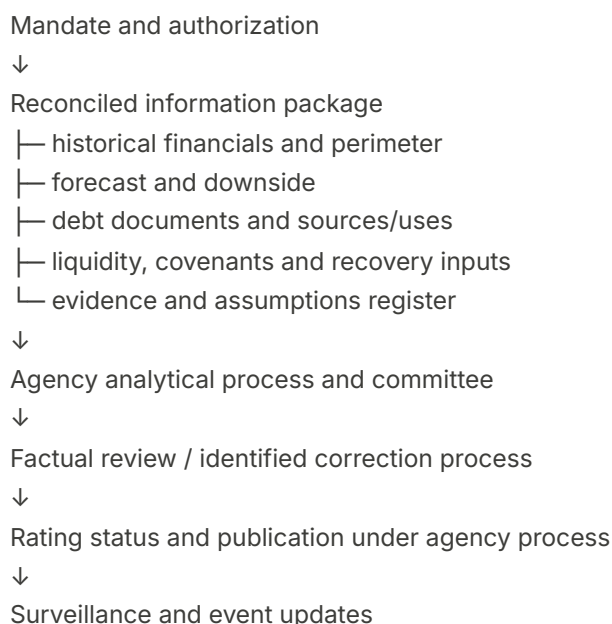
Figure 29.1 — Controlled rating-process flow

Table 29.3 — Information-package control

Workstream	Package content	Reconciliation test
Historical financials	Audited statements, perimeter changes and adjustments	Ties to source and lender model
Forecast	Operating drivers, cash flow, debt service and downside	Same base facts across recipients
Transaction	Sources and uses, debt terms, guarantees and collateral	Ties to executed or latest controlled documents
Liquidity	Cash access, revolver, maturities and minimum cash	Entity -level bridge
Recovery	Entity values, claims, costs, priority and timing	No double -counted value or claims
Management policy	Acquisitions, distributions, leverage and support assumptions	Separate intention from binding commitment
Evidence register	Source, date, status and accountable owner	Open items are visible

The package should distinguish audited fact, current trading, management forecast, arranger assumption and analyst sensitivity. Tailoring the facts supplied to different agencies to seek a preferred outcome can create accuracy, disclosure and compliance concerns. Before non-public information is shared, the transaction team should confirm authorization, confidentiality, information barriers and the intended disclosure perimeter with its legal and compliance advisers. This chapter does not state a universal sharing rule.

Synthetic case 1 — factual review. Agency Delta receives a debt schedule showing a EUR 50 million local facility as unsecured. The executed local document shows specified collateral. The issuer's team provides the exact document reference and a corrected entity/claim schedule. The correction request is factual; it does not ask the agency to select a rating category. If the legal effect of the collateral is uncertain, counsel's advice and the agency's own analysis remain separate.

Table 29.4 — Challenge protocol

Type of issue	Appropriate response	Inappropriate shortcut
Factual error	Provide source, exact correction and affected schedule	Argue that the rating “feels low”
Perimeter mismatch	Reconcile entities and transaction steps	Present only the more favorable perimeter
Forecast misunderstanding	Explain formula, timing and evidence	Replace downside with management aspiration
Methodology question	Cite current public criteria and ask for clarification through the agency process	Claim a fixed outcome from an old case
Committee outcome	Use the agency's current appeal/review process where available	Treat relationship pressure as analytical evidence

29.4 Independent expected-loss and recovery arithmetic

A lender may use expected-loss arithmetic as a teaching or portfolio tool, but that arithmetic is not an agency rating. Inputs must be independently sourced or labeled assumptions.

Worked calculation 1 — expected-loss identity

Assume a fictional one-year probability of default of 4.0% and loss given default of 55.0%.

Expected loss = 4.0% × 55.0% = 2.20%.

If exposure is EUR 100 million, simplified expected loss is EUR 2.2 million. The result ignores timing, migration, correlation, discounting, fees and scenario variation. It is not a crosswalk to any rating category and the assumptions are not derived from agency symbols.

Worked calculation 2 — claim waterfall

Fictional enterprise value at default is EUR 320 million. Process and priority costs are EUR 20 million. Super-senior claims are EUR 40 million, first-lien claims EUR 200 million and unsecured claims EUR 160 million.

Step	Value available (EURm)	Distribution (EURm)	Residual value (EURm)
Gross enterprise value	320	—	320
Process and priority costs	320	(20)	300
Super-senior claims	300	(40)	260
First-lien claims	260	(200)	60
Unsecured claims	60	(60)	0

Simplified first-lien recovery is $200 / 200 = 100\%$. Unsecured recovery is $60 / 160 = 37.5\%$. These are scenario outcomes, not agency recovery ratings. A real case would require entity location, guarantees, collateral, insolvency costs, claim allowances, timing and legal review.

Worked calculation 3 — recovery sensitivity without notching bands

Keep costs and claims unchanged and vary gross enterprise value.

Gross EV (EURm)	Value after costs and super-senior (EURm)	First-lien recovery	Unsecured recovery
260	200	100.0%	0.0%
320	260	100.0%	37.5%
380	320	100.0%	75.0%
220	160	80.0%	0.0%

The table deliberately does not translate recoveries into notches. Fitch's public corporate recovery and instrument criteria dated 2 August 2024 describe Fitch's applicable framework and should be read with related current criteria; Moody's and S&P apply their own current frameworks. An external analyst should not invent a universal recovery-to-notch scale. Fitch Ratings, Corporates Recovery Ratings and Instrument Ratings Criteria, 2 August 2024 (<https://assets.fitchratings.com/downloadFile?reportType=report&sfReport=false&slug=corporate-finance%2Fcorporate-recovery-ratings-instrument-ratings-criteria-02-08-2024>); Moody's, public corporate LGD methodology endpoint (<https://ratings.moody's.com/api/rmc-documents/65773>).

Figure 29.2 — Keep the analytical lanes separate

Agency lane Practitioner lane
 Current public criteria Executed documents
 Agency information process Independent evidence plan
 Agency committee Cash-flow and downside model
 Published rating/rationale Entity and claim waterfall
 Agency surveillance Relative-value and monitoring view

Shared factual reconciliation
but no presumed common outcome

29.5 Instrument ratings and notching

Instrument analysis begins with the obligor and claim, not with a desired notch. The practitioner should map:

- ♦ • issuer and instrument identity;
- ♦ • borrower, issuer and guarantor perimeter;
- ♦ • collateral and asset location;
- ♦ • contractual and structural priority;
- ♦ • super-senior, pari passu and junior claims;
- ♦ • maturity, payment terms and contingent claims;
- ♦ • governing law and enforcement jurisdiction; and
- ♦ • current agency criteria applicable to the instrument.

Notching can move in different directions or not at all depending on the agency's framework and case. A secured label does not itself prove higher recovery; a guarantee does not itself prove value if the guarantor lacks assets or the claim has limitations. Do not publish a generic "secured debt is one notch higher" rule.

Synthetic case 2 — same issuer, different instruments. Northstar Packaging has a secured loan at operating subsidiaries, an unsecured bond at the same borrower and a holdco note above the operating group. The practitioner builds three claim maps. The operating loan has direct collateral but shares it with a revolver and hedging claims. The unsecured bond relies on residual operating value. The holdco note relies on permitted distributions and share value. The case demonstrates different economic positions; it does not predict how any agency will rate them.

Table 29.5 — Instrument input record

Input	Loan	Operating - company bond	Holdco note
Primary obligor	Named operating borrower	Named operating issuer	Holding company
Guarantees	Selected operating guarantors	Selected guarantors	None in fictional case
Collateral	Selected assets	None	Share interest only if specified
Priority	First lien subject to super - senior claims	Unsecured residual	Structurally dependent on upstream value
Maturity	2030	2031	2032
Practitioner output	Claim waterfall	Residual recovery	Distribution/share - value sensitivity
Agency output	Determined only by agency under current criteria	Same	Same

29.6 Rating-linked terms in executed documents

A rating has contractual effect only where a document assigns one. Common fields to extract include pricing grids, covenant suspension, collateral release, replacement mechanics, investment eligibility and structured-credit tests. The analyst should not generalize from product labels.

Table 29.6 — Trigger register

Field	Required extraction
Rating object	Issuer, family, instrument or specified debt rating
Agency set	Named agencies and substitution mechanics
Threshold	Exact category or condition
Number required	One, two, all or another stated combination
Outlook/watch	Whether expressly relevant
Timing	Effective date and observation mechanics
Reversal	What happens after downgrade or withdrawal
Default condition	Whether a default blocks the effect
Consequence	Margin, covenant, collateral, eligibility or other result

Synthetic case 3 — rating-linked margin. A fictional loan provides a 25 basis point margin reduction only when two named agencies assign at least the specified instrument rating and no event of default is continuing. Agency A upgrades the instrument; Agency B does not. The margin does not change in this invented example because the two-agency condition is not met. No assumption is made about why Agency B differs.

29.7 CLO tests: read the selected indenture

CLO note ratings, collateral eligibility, concentration tests, weighted-average measures, overcollateralization tests and interest-coverage tests depend on the selected indenture and incorporated definitions. The label “CCC bucket” is not enough. Extract the rating source, adjustment or selection rules, threshold, measurement date, excess treatment and waterfall consequence.

Worked calculation 4 — fictional CLO concentration consequence

Assume a fictional CLO has EUR 200 million of portfolio par. Its selected indenture permits a 7.5% bucket for assets classified under the specified rating definition. Actual bucket par is EUR 18 million.

- ♦ • Permitted amount: $200 \times 7.5\% = \text{EUR } 15\text{m.}$
- ♦ • Excess amount: $18 - 15 = \text{EUR } 3\text{m.}$

Assume solely for this exercise that the indenture values excess assets at 60% of par for the selected OC numerator. The haircut is $3 \times (100\% - 60\%) = \text{EUR } 1.2\text{m.}$ Adjusted numerator is $200 - 1.2 = \text{EUR } 198.8\text{m.}$

If the relevant note balance is EUR 160 million:

- ♦ • Unadjusted OC ratio: $200 / 160 = 1.250\text{x.}$
- ♦ • Adjusted OC ratio: $198.8 / 160 = 1.2425\text{x.}$

Whether that passes depends on the actual trigger. The exercise does not state a market-standard bucket, valuation rule or trigger; every figure is invented. A failed test may redirect cash under the selected waterfall without legally forcing an asset sale. Manager behavior and market prices require separate evidence.

Table 29.7 — CLO document fields

Field	Why it matters
Rating definition and agency	Determines the classification source
Selection or adjustment rule	Resolves multiple, withdrawn or unavailable ratings
Bucket threshold	Determines permitted concentration
Excess treatment	Determines par, market-value or other adjustment
Measurement date	Determines when the test is run
Cure mechanics	Determines permissible response
Waterfall effect	Determines cash consequence
Reporting evidence	Allows the result to be reproduced

29.8 Split ratings, outlooks and watches

A split rating means agencies reached different opinions under their respective criteria, information and assumptions. The difference may arise from issuer perimeter, financial policy, sector assessment, recovery treatment, group linkage, forecast, event risk or another factor. It does not by itself establish an error, a favorable agency or a pricing penalty.

Synthetic case 4 — diagnosing a split. Agency Alpha's public rationale emphasizes high leverage and weak free cash flow; Agency Beta's public rationale gives more weight to recurring revenue and liquidity. The practitioner does not average symbols. The practitioner creates a proposition table: which facts are common, which assumptions differ, what evidence could change each view, and whether the selected investor mandate uses one rating, the lower rating or another rule.

Table 29.8 — Split-rating diagnosis

Question	Evidence
Is the rated entity the same?	Rating action and legal entity name
Is the instrument the same?	ISIN/CUSIP or exact obligation
Are dates aligned?	Rating-action and financial-information dates
Are assumptions different?	Published rationales and sensitivities
Does an investor document select a rating?	Executed mandate or indenture
Is a price claim supported?	Dated observable market evidence with controls

An outlook or watch should be captured exactly as published, including direction and date. It is not a promised future action. Do not model an automatic basis-point move from an outlook change without a defined dataset, event window and controls for concurrent credit and market information.

29.9 Conflicts, oversight and independence

The issuer-pays model creates a potential conflict that regulatory frameworks and agency controls are intended to address. A potential conflict does not prove bias in a particular rating. The proper practitioner response is to

preserve consistent information, identify engagement terms, separate commercial and analytical workstreams, and rely on public regulatory and agency disclosures rather than anonymous claims.

In the United States, the SEC's Office of Credit Ratings examines and monitors registered NRSROs and administers rules affecting them. Registration is a legal status; it is not SEC approval of a specific rating. SEC, Office of Credit Ratings, checked 12 July 2026 (<https://www.sec.gov/about/divisions-offices/office-credit-ratings>).

In the European Union, ESMA states that it is the direct supervisor of EU credit rating agencies, and Regulation (EC) No 1060/2009 provides the EU regulatory framework, as amended. Exact application and current consolidated law require legal review. ESMA, Credit Rating Agencies, checked 12 July 2026 (<https://www.esma.europa.eu/esmas-activities/investors-and-issuers/credit-rating-agencies>); EUR-Lex, consolidated Regulation (EC) No 1060/2009 (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02009R1060-20250117>).

Table 29.9 — Conflict controls

Risk	Control
Inconsistent facts across agencies	One reconciled package and change log
Commercial pressure on analysis	Separate roles and follow agency/firm controls
Selective disclosure	Authorized perimeter and complete material facts
Methodology version drift	Source/version register and refresh date
Alleged shopping	Evidence-based selection record; avoid unsupported allegation
Fee influence claim	Use engagement facts; do not infer rating outcome
Confidential information	Legal/compliance approval and information barriers

Fees and surveillance charges should be taken from the actual engagement. This chapter provides no generic fee, timing or success range. Sponsor support should be treated similarly: ownership, incentives and remaining equity may inform qualitative analysis, but no repayment support exists unless it is committed and available under its terms.

Surveillance and event discipline

The rating record continues after initial publication. Build an event calendar covering financial reporting, acquisitions, disposals, refinancing, distributions, covenant events, major litigation, management-policy changes and maturity milestones. The calendar is a workflow tool, not a prediction of agency action. For each event, record the public or authorized information supplied, the agency publication date and any change to rating, outlook or watch status.

A practitioner should also preserve the difference between **factual update**, **agency sensitivity** and **analyst scenario**. A factual update might be a completed acquisition or reported earnings. An agency sensitivity is the agency's own published statement under its current rationale. An analyst scenario is the practitioner's independent model. Copying an agency sensitivity into the lender model without reconciling definitions can create an apparently precise but unsupported trigger.

Sponsor support and financial policy

Sponsor ownership may affect financial policy, acquisition appetite, distributions and willingness to inject capital. The credit package should document the downside both with and without voluntary support. A history of equity

contributions is evidence of past conduct, not a legally committed future source. Likewise, remaining equity value does not establish that the sponsor will protect a particular instrument.

If an agency publication discusses group linkage or support, use the applicable current agency criteria and exact entity facts. Do not combine terminology across agencies or convert a qualitative support assessment into a cash amount unless a binding commitment and funding mechanics support it.

Withdrawal and missing information

A rating can be withdrawn or become unavailable under agency-specific circumstances. The contractual consequence depends on the selected document's replacement, selection or fallback terms. The practitioner should not assume that withdrawal equals downgrade, that another agency's rating automatically substitutes, or that an investor mandate remains satisfied. Record the exact status and route the document consequence to the relevant legal and compliance workstream.

29.10 Practitioner workflow

- ✦ 1. Identify the exact issuer, instrument, transaction and decision.
- ✦ 2. Freeze the agency source/version register.
- ✦ 3. Reconcile historical financials, current trading, forecast and debt perimeter.
- ✦ 4. Build the independent cash-flow, liquidity and recovery view from Chapters 27 and 26.
- ✦ 5. Map each agency construct without cross-agency translation.
- ✦ 6. Extract every rating-linked term from the selected instrument or investor document.
- ✦ 7. Record rating, outlook, watch and rationale dates.
- ✦ 8. Separate factual corrections from requests for analytical reconsideration.
- ✦ 9. Preserve confidentiality, conflicts and authorization controls.
- ✦ 10. State what the rating does not prove.

29.11 Practitioner exercises

Exercise 1 — label mapping

A presentation lists a Moody's CFR, an S&P instrument rating and a Fitch IDR in one row titled "issuer rating."

Task: Redesign the row.

Answer check: Create separate fields for agency, exact construct, rated entity or instrument, rating, outlook/watch, action date, rationale date and source/version. Do not average or translate the symbols. The S&P instrument rating belongs in an instrument field, not automatically an issuer field.

Exercise 2 — trigger extraction

A fictional bond suspends selected covenants only when two named agencies assign specified ratings to the notes, no default is continuing and the ratings remain effective. One agency upgrades the issuer but not the notes; the other upgrades the notes.

Task: Does suspension occur?

Answer check: Not under the stated fictional terms because both required note ratings are not present. The issuer upgrade is not substituted for an instrument rating. A live conclusion requires the executed clause.

Exercise 3 — split-rating diagnosis

Two agencies publish different instrument ratings. One rationale uses a lower cash-flow forecast; the other assumes a higher recovery value. The instrument, date and entity are otherwise aligned.

Task: Identify the correct analytical response.

Answer check: Reconcile forecast and recovery assumptions, rebuild the independent downside, record the agencies' current criteria and rationales, and test the effect under relevant investor documents. Do not call one agency wrong, infer bias or claim a fixed price effect without evidence.

Appendix 29A — Public source/version register

Source ID	Public source	Date/scope used	Permitted use in this chapter
RAT - MDY - DEF	Moody's Rating Symbols and Definitions (https://ratings.moodys.com/api/rmc-documents/53954)	Public endpoint checked 12 July 2026	Construct names and definitions; verify current version before use
RAT - MDY - LGD	Moody's public corporate LGD methodology endpoint (https://ratings.moodys.com/api/rmc-documents/65773)	Public endpoint checked 12 July 2026	High-level source route only; no proprietary table reproduction
RAT - SP - DEF	S&P Global Ratings Definitions (https://www.spglobal.com/ratings/pt/regulatory/article/-/view/sourceId/504352)	Public page checked 12 July 2026	S&P construct definitions; verify current version
RAT - FIT - CORP	Fitch Corporate Rating Criteria (https://assets.fitchratings.com/downloadFile?reportType=report&sfReport=false&slug=corporate-finance%2Fcorporate-rating-criteria-09-01-2026)	9 January 2026, global non-financial corporates	High-level framework summary only
RAT - FIT - RR	Fitch Corporates Recovery Ratings and Instrument Ratings Criteria (https://assets.fitchratings.com/downloadFile?reportType=report&sfReport=false&slug=corporate-finance%2Fcorporate-recovery-ratings-instrument-ratings-criteria-02-08-2024)	2 August 2024; verify active/related criteria before use	Source route for Fitch recovery/instrument framework; no copied tables
REG - US - OCR	SEC Office of Credit Ratings (https://www.sec.gov/about/divisions-offices/office-credit-ratings)	Checked 12 July 2026	NRSRO oversight description
REG - EU - ESMA	ESMA Credit Rating Agencies (https://www.esma.europa.eu/esmas-activities/investors-and-issuers/credit-rating-agencies)	Checked 12 July 2026	EU supervisory perimeter at high level
REG - EU - CRA	EUR-Lex consolidated CRA Regulation (https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02009R1060-20250117)	Consolidation identifier dated 17 January 2025	Regulatory source route; legal application reserved

Appendix 29B — Publication and review checklist

- ♦ • Every agency term is attributed to the correct agency.
- ♦ • No symbol, recovery band, fee, timetable or pricing effect is presented as universal.
- ♦ • Criteria title, date, scope and supersession status are recorded.
- ♦ • No proprietary methodology text, table, scorecard or licensed dataset is copied.
- ♦ • Synthetic probabilities, recoveries and CLO terms are visibly labeled.

- ✦ • Ratings, outlooks and watches are not treated as recommendations or guaranteed future actions.
- ✦ • Rating-linked consequences are tied to executed documents.
- ✦ • Factual review is separated from pressure for a desired outcome.
- ✦ • Conflict language describes controls and does not allege bias without evidence.
- ✦ • Confidential information is shared only under applicable authorization and controls.
- ✦ • Legal and regulatory statements remain bounded to official public sources.
- ✦ • Any retained novel, predictive or interpretive agency claim is removed, rewritten or routed to a qualified ratings practitioner.

The final discipline is to let each record do its own job. The agency owns its opinion. The document owns its contractual consequence. The practitioner owns the independent credit and recovery analysis. When those three are kept separate, ratings become useful evidence rather than a substitute for judgment.

Corporate Financial Modeling

Purpose and analytical boundary

This chapter uses Europa Packaging, a wholly fictional company, to demonstrate how a corporate credit model turns operating assumptions into cash flow, debt capacity and downside analysis. Every company-specific input in the companion workbook is synthetic. No client, employer, transaction, paid-research or private-company information is used.

The workbook is a teaching model, not a fairness opinion, valuation opinion, covenant certificate, tax computation or recommendation to finance a real borrower. Its EBITDA is an accounting-style teaching measure. A contractual covenant calculation must be rebuilt from the operative credit documents and reviewed with counsel.

The companion file is LevFin_Academy_Synthetic_Corporate_Credit_Model.xlsx. It opens on a Dashboard and contains seven supporting sheets: Assumptions, Operating Model, Debt Schedule, Financial Statements, Scenarios, Checks and Sources Audit.

What the model is designed to answer

A credit model should answer a small number of decision questions clearly:

- ✦ What operating assumptions produce the forecast?
- ✦ How much cash does the business generate after tax, working capital and capital expenditure?
- ✦ Can the company service interest while maintaining minimum liquidity?
- ✦ How quickly can debt decline under the selected case?
- ✦ Which assumptions move leverage and coverage most sharply?
- ✦ Does the workbook calculate correctly, and is it sufficiently supported for the decision being made?

The final question has two parts. Calculation integrity asks whether the formulas, statements and schedules tie. Decision readiness asks whether the inputs, definitions and sources are reliable enough for the intended use. A model can pass the first test and fail the second. The workbook makes that distinction explicit on both the Dashboard and Checks sheets.

Architecture before formulas

Good models separate inputs, calculations, outputs and controls.

- ✦ Assumptions contains values the user may change. These cells are shown in blue.
- ✦ Operating Model converts revenue, margin and working-capital drivers into forecast operating results.
- ✦ Debt Schedule calculates interest, mandatory amortisation, liquidity draws, repayments and cash sweeps.
- ✦ Financial Statements integrates the income statement, cash flow statement and balance sheet.
- ✦ Dashboard and Scenarios present selected outputs rather than creating new assumptions.
- ✦ Checks proves mechanical integrity and identifies readiness limitations.
- ✦ Sources Audit records the origin and classification of every material input class.

Time moves from left to right. Actual results sit to the left of forecast periods. Formula patterns remain consistent across each forecast row. Assumptions are held in dedicated cells rather than embedded as numbers inside

formulas.

This structure is deliberately simple. Transparency matters more than formula density. A long formula that combines operating logic, financing logic and scenario selection in one cell may be compact, but it is harder to audit and easier to break. The model instead uses short formulas and visible intermediate steps.

Start with an explicit assumption set

The Assumptions sheet contains three operating cases: Base, Upside and Downside. The selected case is controlled by one dropdown cell. Forecast revenue growth and EBITDA margin change with that selection; the rest of the workbook updates by formula.

Europa Packaging starts with synthetic 2024 revenue of EUR 500 million and EBITDA of EUR 80 million. The capital structure begins with EUR 250 million of term debt, EUR 20 million of cash and a EUR 75 million undrawn revolving facility. These are teaching inputs, not observations about a real issuer.

Other assumptions include cost of goods sold as a percentage of revenue, receivable days, inventory days, payable days, capital expenditure, tax, interest rates, minimum cash, scheduled term-loan amortisation and the proportion of excess cash applied to debt.

The key discipline is classification. Each input must be one of the following:

- ♦ a sourced fact;
- ♦ a clearly identified management or lender assumption;
- ♦ a scenario assumption;
- ♦ or a synthetic teaching input.

An unlabeled number is not an assumption; it is an audit problem.

Build the operating forecast

Revenue is projected from the prior period and the selected growth rate:

Forecast revenue = Prior-period revenue x (1 + selected growth rate)

EBITDA is calculated from forecast revenue and the selected EBITDA margin:

EBITDA = Revenue x EBITDA margin

Cost of goods sold is modeled separately so that inventory and payable balances can use a cost base rather than revenue. Depreciation and amortisation is linked to revenue in this compact teaching model. A transaction model may instead require asset-category or vintage schedules, but the modeler should add complexity only when it changes a decision.

The operating build therefore creates a visible chain:

Revenue -> COGS -> EBITDA -> D&A -> EBIT

Each line has a single purpose. If the selected scenario changes, the operating results change without rewriting any forecast formula.

Model working capital from operating drivers

Working capital is often where an apparently profitable forecast loses cash. The workbook models receivables, inventory and payables using days assumptions:

Accounts receivable = Revenue x DSO / 365

Inventory = COGS x DIO / 365

Accounts payable = COGS x DPO / 365

Net working capital equals receivables plus inventory less payables. The cash-flow statement uses the period-on-period change. An increase in net working capital consumes cash; a decrease releases cash.

The sign matters. The model displays the balance-sheet asset and liability values as positive amounts, then deducts an increase in net working capital in the cash flow statement. This is easier to audit than reversing signs in several schedules.

A real underwriting model should replace broad days assumptions with the best available operational evidence. Seasonality, customer mix, supplier terms and acquisition effects can make a year-end days calculation misleading. The synthetic model does not claim to capture those company-specific effects.

Roll forward capital expenditure and PP&E

Capital expenditure is calculated as a percentage of revenue. Closing property, plant and equipment follows a simple roll-forward:

Closing PP&E = Opening PP&E + Capex - D&A

The opening balance in each forecast period equals the prior period's closing balance. This produces a continuous schedule and a direct tie to the balance sheet.

For businesses with long construction cycles, major maintenance programmes or multiple asset lives, a separate capex and depreciation schedule may be required. The correct question is not whether the model is sophisticated; it is whether the schedule is sufficiently detailed for the decision.

Integrate the financial statements

The income statement calculates EBIT, cash interest, earnings before tax, cash tax and net income. The cash flow statement starts with net income and adds back D&A before deducting capex and the increase in net working capital.

The resulting measure is free cash flow before financing:

FCF before financing = Net income + D&A - Capex - Change in NWC

The financing section then records revolver draws or repayments, mandatory term-loan amortisation and the excess-cash sweep. Ending cash flows to the balance sheet.

The balance sheet carries cash, receivables, inventory, PP&E, other assets, payables, term debt, revolver debt, other liabilities and equity. Equity rolls forward by net income because the teaching case assumes no dividends or new equity during the forecast.

The balance-sheet check is:

Total assets - Total liabilities - Equity

It must equal zero in every period, subject only to immaterial rounding. Passing this check is necessary, but not sufficient, for a reliable model.

Model debt and liquidity without hiding circularity

The Debt Schedule uses opening debt balances to calculate cash interest. This is a deliberate teaching simplification. It avoids an interest-cash-debt circular reference while keeping the formula chain visible.

The liquidity sequence is:

- ♦ Add free cash flow before financing to opening cash.
- ♦ Pay mandatory term-loan amortisation.
- ♦ Draw the revolver if cash would otherwise fall below the minimum-cash requirement.
- ♦ Repay any outstanding revolver from available excess cash.
- ♦ Apply the selected percentage of remaining excess cash to the term loan.
- ♦ Carry closing cash and debt into the next period.

The model also calculates undrawn revolver capacity. A negative result would indicate that the synthetic commitment is exceeded and should cause a failed check.

This sequencing matters. Liquidity is not the same as earnings, and a model should not assume that positive EBITDA prevents a cash shortfall. Taxes, capital expenditure, working capital, interest and mandatory repayments all sit between EBITDA and available liquidity.

Read the credit outputs

The Dashboard highlights six measures across the actual and forecast periods:

- ♦ Revenue;
- ♦ EBITDA;
- ♦ Net debt;
- ♦ Net leverage;
- ♦ Interest coverage;
- ♦ Free cash flow before financing.

Net debt is calculated as term debt plus revolver debt less cash. Net leverage divides net debt by the model's EBITDA. Interest coverage divides EBITDA by cash interest.

These ratios are analytical teaching measures. They are not contractual covenant calculations. A real credit agreement may define debt, cash netting, EBITDA, interest expense and pro forma adjustments differently. The operative definitions control any compliance conclusion.

The selected Base case shows the synthetic company generating positive cash flow and reducing net debt over the forecast. That result is not a forecast about an investable company. It demonstrates how operating assumptions, cash conversion and financing mechanics connect.

Use scenarios and sensitivities correctly

A scenario changes a coherent set of assumptions together. The workbook's Base, Upside and Downside cases use different growth and margin paths.

A sensitivity isolates a smaller set of drivers. The Scenarios sheet includes an illustrative grid that varies constant revenue growth and the 2029 EBITDA margin. Each cell recalculates an exit net-leverage estimate from the selected row and column assumptions.

The grid is intentionally labelled as illustrative. It uses a simplified free-cash-flow conversion factor and does not replace the integrated forecast. Its purpose is to show direction and breakpoints, not to manufacture precision.

The modeler should ask:

- ♦ Which driver creates the largest change in leverage?
- ♦ Does a downside case create a liquidity draw?
- ♦ At what point does interest coverage become uncomfortable?
- ♦ Which assumptions are correlated and should move together?
- ♦ Is the sensitivity changing the underlying economics or merely changing a displayed answer?

A pasted table of outputs is not a sensitivity. The cells must be formula-driven and linked to explicit inputs.

Checks and readiness

The Checks sheet tests five mechanical areas:

- ♦ the maximum absolute balance-sheet difference;
- ♦ the maximum difference between cash-flow and debt-schedule ending cash;
- ♦ negative debt balances;
- ♦ revolver commitment headroom;
- ♦ source-classification completeness.

Those checks roll into a Calculation Integrity status. The companion workbook passes these checks and contains no external workbook links or formula-error values.

Practical exercises

Use the workbook to perform the following exercises:

- ♦ Change the selected scenario from Base to Downside. Record the change in 2029 EBITDA, net debt, leverage and coverage.
- ♦ Increase DSO by ten days. Trace the effect through receivables, free cash flow, cash and net debt.
- ♦ Reduce the cash-sweep percentage to zero. Compare closing cash and term debt.
- ♦ Increase the term-loan interest rate by 200 basis points. Identify the effect on interest coverage, tax and free cash flow.
- ♦ Reduce the revolver commitment. Determine whether any forecast period breaches the liquidity check.
- ♦ Review a forecast formula across all periods. Confirm that its structure is consistent and that any change comes from an assumption cell.

For each exercise, distinguish the mechanical result from the credit conclusion. A ratio movement tells you what the model calculates. It does not, by itself, explain whether the business can actually deliver the assumptions.

Source and rights note

The Europa Packaging facts and figures are original synthetic teaching inputs created for this chapter. General cash-flow-statement architecture is cross-checked against the IFRS Foundation's IAS 7 materials. The lease-

accounting boundary is identified in the Sources Audit sheet with the IFRS Foundation's IFRS 16 page. Spreadsheet formula behavior is cross-checked against official Microsoft Excel documentation. No third-party prose or private research is reproduced.

The workbook hash, formula audit, visual review and source classifications are recorded in a model evidence record. These materials identify the workbook used for the chapter and enable a reader or reviewer to reproduce the analysis; they do not convert a teaching model into advice about a live transaction.

Companion workbook evidence binding

The exact companion workbook bound to this chapter is LevFin_Academy_Synthetic_Corporate_Credit_Model.xlsx SHA-256 177cf64be29ea74c86f074d70edf5e51458c12ed1845ce57f217aff8525e852b. That hash identifies the synthetic model used for the chapter's mechanical evidence; it does not replace legal, tax, accounting or covenant review for a live transaction.

LBO Modelling — A Complete, Self-Contained Build

***Clean-room teaching chapter.** Every company, instrument, number, formula and scenario in this chapter is fictional and independently created for this edition. No private model, mandate, lender presentation, proprietary template or licensed dataset is used. The model is displayed completely in the chapter; there is no companion workbook. Legal, tax and accounting outcomes are not determined here. Contract terms and the work of appropriately qualified advisers control a real transaction.*

An LBO model is a controlled chain of claims about cash. It begins with the price paid, continues through the operating forecast, follows cash through interest, tax, investment and debt repayment, and ends with an equity value at exit. A polished return cell is not a model if the reader cannot reconstruct that chain. Equally, a model can be arithmetically perfect and economically wrong if it mixes periods, silently changes definitions, ignores liquidity or assumes away the order in which facilities operate.

This chapter builds one complete five-year synthetic model for **Northstar Testing Services**, a fictional provider of industrial inspection and certification services. The case is designed to make the hard parts visible: original-issue discount, cash and PIK interest, mandatory amortisation, a cash sweep, minimum cash, revolver logic, interest circularity, a value-creation bridge, credit breakpoints and sponsor-return sensitivities. The model is intentionally small enough to audit on paper and complete enough to show how the pieces interact.

Learning objectives

By the end of the chapter, you should be able to:

- ♦ 1. build sources and uses without confusing debt face amount with cash proceeds;
- ♦ 2. connect entry enterprise value, acquired debt, acquired cash and equity purchase price;
- ♦ 3. forecast revenue, EBITDA, depreciation, capital expenditure and working-capital investment with explicit units and timing;
- ♦ 4. distinguish cash interest from PIK interest and explain where each appears in cash flow and debt balances;
- ♦ 5. order minimum cash, revolver draws, mandatory amortisation and voluntary cash sweeps without hidden plugs;
- ♦ 6. identify and solve the interest–debt–sweep circularity rather than masking it;
- ♦ 7. calculate exit enterprise value, equity proceeds, MOIC and IRR from reconciled balances;
- ♦ 8. separate operating improvement, multiple movement, debt reduction and transaction friction in a value bridge;
- ♦ 9. test returns and credit capacity under exit, EBITDA, interest, PIK and liquidity sensitivities; and
- ♦ 10. perform independent model QA from displayed checks rather than trusting a green spreadsheet cell.

Cross-references are deliberate. Chapter 3 supplies the three-statement foundation; Chapters 4 and 6 explain debt and restricted-payment mechanics; Chapters 8, 15 and 16 develop leverage, interest and cash-flow analysis; Chapter 21 addresses valuation; Chapters 27 and 28 cover underwriting and working capital; Chapter 30 develops corporate modelling; Chapter 32 applies the same discipline from a lender's perspective; and Chapter 36 returns to downside decision-making.

31.1 Model boundary, units and timing

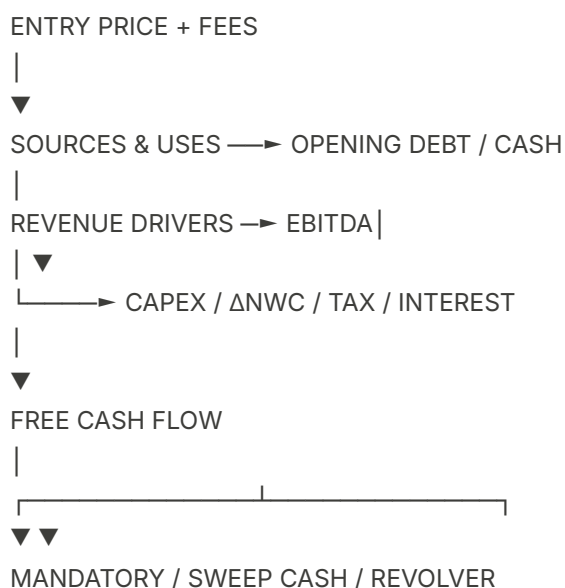
The first control is a written model boundary. Northstar is acquired at the end of Year 0. Entry sources and uses occur at closing. The operating forecast covers Years 1–5. All income-statement and cash-flow items are annual flows. Debt, cash and enterprise value are point-in-time balances at year-end. Currency is euros and all displayed financial amounts are **€ millions**, except per-turn ratios and percentages. Rounding is for presentation; the formulas use unrounded values.

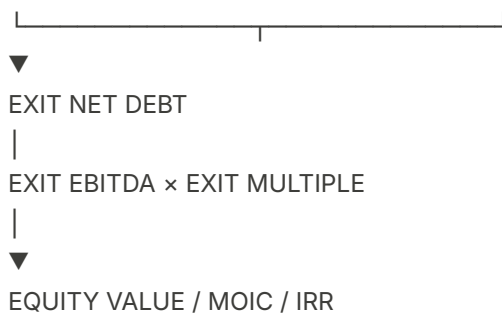
The model does not purport to apply a particular accounting standard or tax code. Depreciation is a teaching assumption equal to 3.0% of revenue. Cash tax is a simplified 25% of positive teaching-model taxable income. PIK interest is assumed to reduce the teaching tax base, but that is an input, not a statement about deductibility in any jurisdiction. OID is treated as a reduction in cash proceeds at closing while debt is recorded at face amount. A real accounting and tax analysis may differ.

Table 31.1 — Control conventions

Field	Convention	Why it matters
Currency	Euro	Prevents mixed-currency debt and earnings
Display unit	€m	Every table uses the same scale
Closing date	End of Year 0	Separates entry balances from Year 1 flows
Forecast periods	Five annual periods	Matches the exit-horizon calculation
Flow timing	Full-year	Revenue, EBITDA, capex, tax and working capital
Balance timing	Year-end	Cash, debt and exit value
Interest basis	Average opening and pre-sweep ending balance where stated	Makes repayment timing visible
Minimum cash	€10.0m	Cash below this level requires financing support
Cash sweep	50% of excess cash after mandatory amortisation	Leaves half of excess cash on balance sheet
Tax basis	Simplified teaching formula	Not tax advice or a statutory computation
Rounding	One decimal displayed; unrounded calculation	Avoids false reconciliation failures

Figure 31.1 — Formula lineage





This lineage is the audit trail. If a return changes, the reviewer should be able to move upstream until the first changed assumption or formula is found.

31.2 Definitions that must not drift

Sources and uses reconcile every cash requirement at closing to debt cash proceeds and sponsor equity. **Entry enterprise value** is the value assigned to operations before net debt. **Equity purchase price** is the amount paid to acquire the equity after the selected debt and cash adjustments. **Original-issue discount**, or OID, is the difference between debt face amount and issue proceeds in this teaching model. **Cash interest** is paid in the period; **PIK interest** is capitalised into principal and consumes no current-period cash.

Mandatory amortisation is scheduled principal repayment. A **cash sweep** is the modelled voluntary repayment from a defined share of excess cash. A **revolver** is the short-term liquidity facility drawn when cash would otherwise fall below the stated minimum. **Minimum cash** is an operating-liquidity assumption, not distributable value. **Circularity** occurs when a debt repayment changes interest, interest changes cash flow, and cash flow changes the debt repayment.

At exit, **enterprise value** equals the selected exit EBITDA multiplied by the selected exit multiple. **Equity value** equals enterprise value less net debt in this model. **MOIC** is exit equity proceeds divided by invested sponsor equity. **IRR** is the annualised discount rate that equates the initial outflow and final inflow; with one investment at closing and one receipt after five years, $IRR = MOIC^{(1/5)} - 1$. The **value bridge** explains the change from sponsor investment to exit proceeds through EBITDA growth, multiple change, net-debt reduction and transaction friction. **Debt capacity** is an output of a selected leverage, coverage or liquidity constraint; it is never the amount a business should borrow merely because a formula permits it.

31.3 The Northstar entry case

Northstar has Year 0 revenue of €320.0m and EBITDA of €64.0m, a 20.0% margin. The sponsor agrees a 10.0x entry multiple, producing €640.0m of enterprise value. Existing debt is €120.0m and acquired cash is €10.0m. Therefore equity purchase price is €640.0m – €120.0m + €10.0m = €530.0m. The transaction refinances the €120.0m debt and incurs €18.0m of fees.

Table 31.2 — Entry assumptions

Assumption	Value	Formula or boundary
Year 0 revenue	€320.0m	Synthetic input
Year 0 EBITDA	€64.0m	Synthetic input
EBITDA margin	20.0%	64.0 / 320.0
Entry multiple	10.0x	Synthetic valuation input
Entry enterprise value	€640.0m	64.0 × 10.0x
Existing debt refinanced	€120.0m	Closing use
Acquired cash retained	€10.0m	Closing balance and minimum cash
Equity purchase price	€530.0m	640.0 – 120.0 + 10.0
Transaction fees	€18.0m	Closing use
Total uses	€668.0m	530.0 + 120.0 + 18.0

Financing has three funded tranches. The €280.0m term loan is issued at 98, so it contributes €274.4m of cash but creates €280.0m of face debt. The €140.0m notes and €40.0m PIK tranche are issued at par. Sponsor equity is the residual cash source.

Table 31.3 — Complete sources and uses

Uses	€m	Sources	Face €m	Issue price	Cash proceeds €m
Equity purchase price	530.0	Term loan B	280.0	98.0	274.4
Refinance existing debt	120.0	Senior notes	140.0	100.0	140.0
Fees	18.0	PIK tranche	40.0	100.0	40.0
		Sponsor equity	—	—	213.6
Total uses	668.0	Total cash sources			668.0

Three checks follow immediately. Sources minus uses equals zero. Opening gross debt is $280.0 + 140.0 + 40.0 = €460.0\text{m}$. Opening net debt is $460.0 - 10.0 = €450.0\text{m}$, or $450.0 / 64.0 = 7.03\text{x}$ Year 0 EBITDA. The sponsor invests €213.6m even though the operating equity value implied by enterprise value and net debt is €190.0m. The €23.6m difference is €18.0m of fees plus €5.6m of term-loan OID. That transaction friction must reappear in the value bridge.

Mini-example 1 — face debt is not a cash source. If the modeller enters €280.0m as both term-loan face and cash proceeds, the model understates sponsor equity by €5.6m and overstates returns. The debt schedule can still look correct because face principal is €280.0m; the error sits at closing. The fix is to keep separate fields for face, issue price and proceeds.

31.4 Operating forecast

The model uses explicit growth and margin assumptions rather than an EBITDA growth plug. Revenue grows 6.0% in Year 1, 5.0% in Years 2–3 and 4.0% in Years 4–5. EBITDA margin rises from 20.0% in Year 0 to 22.0% in Year 5. No acquisition, disposal or foreign-exchange effect is assumed.

Depreciation equals 3.0% of revenue. Capital expenditure equals 4.0% of revenue. Working-capital investment equals 1.5% of the annual increase in revenue. The working-capital formula is deliberately simple so that it can be

reproduced: it is not an accounting working-capital definition or a purchase-price true-up. Chapter 28 explains why those concepts must not be mixed.

Table 31.4 — Operating assumptions

Assumption	Y1	Y2	Y3	Y4	Y5
Revenue growth	6.0%	5.0%	5.0%	4.0%	4.0%
EBITDA margin	20.5%	21.0%	21.5%	21.8%	22.0%
Depreciation / revenue	3.0%	3.0%	3.0%	3.0%	3.0%
Capex / revenue	4.0%	4.0%	4.0%	4.0%	4.0%
ΔNWC / change in revenue	1.5%	1.5%	1.5%	1.5%	1.5%
Teaching cash -tax rate	25.0%	25.0%	25.0%	25.0%	25.0%

Table 31.5 — Operating forecast

€m except percentages	Y0	Y1	Y2	Y3	Y4	Y5
Revenue	320.0	339.2	356.2	374.0	388.9	404.5
Growth	—	6.0%	5.0%	5.0%	4.0%	4.0%
EBITDA	64.0	69.5	74.8	80.4	84.8	89.0
EBITDA margin	20.0%	20.5%	21.0%	21.5%	21.8%	22.0%
Depreciation	9.6	10.2	10.7	11.2	11.7	12.1
EBIT	54.4	59.4	64.1	69.2	73.1	76.9
Capex	—	13.6	14.2	15.0	15.6	16.2
Working - capital investment	—	0.3	0.3	0.3	0.2	0.2

Formula lineage matters more than apparent precision. Year 3 revenue is $\text{€}356.16\text{m} \times 1.05 = \text{€}373.97\text{m}$. Year 3 EBITDA is $\text{€}373.97\text{m} \times 21.5\% = \text{€}80.40\text{m}$. Year 3 depreciation is $\text{€}373.97\text{m} \times 3.0\% = \text{€}11.22\text{m}$. Year 3 capex is $\text{€}373.97\text{m} \times 4.0\% = \text{€}14.96\text{m}$. Working-capital investment is $1.5\% \times (\text{€}373.97\text{m} - \text{€}356.16\text{m}) = \text{€}0.27\text{m}$. Each formula uses the same period and unit.

The margin expansion contributes roughly half of EBITDA growth. If margin stayed at 20.0%, Year 5 EBITDA would be $\text{€}404.48\text{m} \times 20.0\% = \text{€}80.90\text{m}$, $\text{€}8.09\text{m}$ below the modelled $\text{€}88.99\text{m}$. That difference is not free: an underwriting committee should demand an operating explanation, milestones and a downside case. Chapter 32 demonstrates that lender discipline.

31.4.1 Building the operating case without an EBITDA plug

The cleanest operating build begins below the headline. Revenue should be decomposed into the fewest drivers that explain the business without pretending to precision the evidence cannot support. A testing-services company might use customer sites, jobs per site and revenue per job. A subscription business might use customers, retention and average revenue. A manufacturer might use volume, mix and price. Northstar uses a single revenue-growth assumption because the case is about model mechanics, but a transaction model should retain the driver evidence behind that percentage.

The same rule applies to margin. A margin should be the result of an operating hypothesis: price, labour productivity, utilisation, procurement, footprint or mix. If the model enters 22.0% because that is the margin needed for the target return, the return is circular at the economic level even if the spreadsheet has no circular reference. A useful control is to write beside every margin change the operational event that makes it possible, the date by which it must occur, the cash cost required and the evidence that would disprove it.

Three forecast layers should remain separate. The **management case** records the plan supplied by the business. The **underwritten case** records the assumptions the investment team is willing to own. The **downside case** records a coherent adverse path rather than applying a percentage haircut to every line. The model may display all three, but it should not copy management's EBITDA into the underwritten case while quietly replacing only capex and working capital. That hybrid often preserves the optimistic earnings numerator and imports the conservative cash uses, producing a case no one actually believes.

Capex requires the same discipline. Maintenance capex protects the existing earnings base; growth capex is intended to create additional capacity or revenue. This chapter uses one 4.0% ratio and makes no accounting claim. A real model should identify the operational projects, cash timing and whether management EBITDA includes benefits before the spending occurs. If a downside case cuts growth capex, it should also remove the growth the capex was expected to deliver. Otherwise the model manufactures free cash flow by keeping the benefit and deleting the cost.

Working capital is path-dependent. Northstar's formula charges 1.5% of incremental revenue, so declining revenue would mechanically release cash. A stressed business can instead consume cash as customers pay more slowly, inventory rises or suppliers shorten terms. The modeller should therefore test both the ratio and the direction. Chapter 28 distinguishes accounting working capital from transaction working capital; the cash-flow schedule here needs an operating cash assumption, not a purchase-price definition.

Finally, keep evidence status visible. Historical facts should reconcile to a named source and date. Management assumptions should be labelled as management. Underwriting changes should have an owner and reason. Formula outputs should never be typed inputs. This separation allows a reviewer to challenge the economic judgment without damaging the arithmetic chain.

31.5 Debt terms, interest and circularity

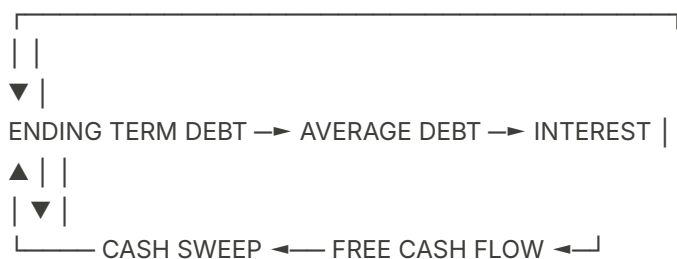
Table 31.6 — Debt and liquidity terms

Instrument	Opening face €m	Cash rate	PIK rate	Scheduled principal	Maturity assumption	Other term
Revolver	0.0	9.0%	—	None	Beyond model horizon	€40.0m commitment; supports €10.0m minimum cash
Term loan B	280.0	6.0%	—	€2.8m annually	Beyond model horizon	50% excess-cash sweep
Senior notes	140.0	8.0%	—	Bullet	Beyond model horizon	No voluntary repayment in base case
PIK tranche	40.0	—	10.0%	Bullet	Beyond model horizon	Interest capitalises annually

Cash interest on the term loan uses the average of opening principal and ending principal before the effect of the current-period cash sweep is finalised. Notes interest is 8.0% of opening notes. Revolver interest uses average opening and ending revolver. PIK interest is 10.0% of opening PIK principal and is added to ending PIK principal.

The cash sweep creates a circularity. A larger sweep reduces ending term debt. Lower average debt reduces interest. Lower interest increases free cash flow. Higher free cash flow increases the sweep. A model that calculates interest solely on opening debt avoids the circle but makes an implicit timing assumption. A model that uses average debt should solve it explicitly.

Figure 31.2 — The controlled circularity



Stop only when successive sweep estimates differ by less than €0.000001m.

The iterative solution is straightforward. Start with a zero sweep. Calculate ending term debt, average term debt, cash interest, tax, free cash flow and a new sweep. Replace the old sweep with the new value and repeat. The final model converges well within 100 iterations. An algebraic solution is possible, but iteration is easier to audit and generalises when the waterfall has more tiers.

Teaching cash tax is:

Cash tax = $25\% \times \max(0, \text{EBITDA} - \text{depreciation} - \text{cash interest} - \text{PIK interest})$.

Free cash flow before debt service is:

FCF = EBITDA – cash interest – cash tax – capex – working-capital investment.

Mandatory amortisation is paid first. The sweep is:

Sweep = $50\% \times \max(0, \text{FCF} - \text{mandatory amortisation})$.

Ending cash is:

Opening cash + FCF – mandatory amortisation – sweep + revolver draw – revolver repayment.

If ending cash would fall below €10.0m, the model draws the revolver up to the commitment. If cash is above €10.0m and revolver is outstanding, the revolver is repaid before a term-loan sweep. The base case does not need the revolver.

31.5.1 Liquidity ordering and the revolver

Minimum cash is a constraint, not a valuation reserve. If the model starts a year with €10.0m and generates negative €8.0m after required payments, the business has not “used minimum cash” and ended at €2.0m under the stated convention. It has drawn €8.0m of revolver and ended at €10.0m. If only €5.0m of commitment remains, the model ends with a €3.0m unfunded deficit. Hiding that deficit in negative cash or an oversized revolver obscures the date on which the capital structure fails.

Facility ordering must be written before formulas are built. This chapter applies cash in the following order: operating uses, cash interest, teaching cash tax, capex and working capital; then mandatory term amortisation; then revolver repayment to the minimum-cash floor; then the 50% term sweep; then retained cash. Another agreement could define excess cash flow differently, exclude specified proceeds, allow voluntary prepayment discretion or require a different sequence. The model must implement the selected terms rather than a generic waterfall.

Revolver availability also is not necessarily equal to commitment less drawings. Letters of credit, ancillary facilities, borrowing-base limits, currency sublimits, default conditions and representations can reduce availability. Northstar assumes none of those constraints. The simplification is acceptable because it is explicit. It would not be acceptable to describe €40.0m as legally available in a live transaction without reading the executed documents and testing the conditions.

Intra-year timing can invalidate a comfortable annual result. A company may receive most cash in the fourth quarter but pay interest, bonuses, tax and inventory in the second. An annual model nets those movements and can show no revolver even though the business needs one for six months. When seasonality or a narrow cushion matters, add a monthly or quarterly liquidity schedule. Chapter 32 uses eight quarters to show how a springing covenant and a liquidity breakpoint can occur inside an annual forecast.

The interest calculation should follow the same timing choice. Average-balance interest approximates repayment through the period. Opening-balance interest assumes repayment at period-end. Daily interest would be more precise but is unnecessary for this pedagogical model. The important control is consistency: do not calculate base interest on averages, downside interest on opening balances and sensitivity interest on closing balances without disclosing the change.

Table 31.7 — Interest, tax and free cash flow

€m	Y1	Y2	Y3	Y4	Y5
EBITDA	69.5	74.8	80.4	84.8	89.0
Cash interest	(27.6)	(26.9)	(26.0)	(24.9)	(23.8)
PIK interest	4.0	4.4	4.8	5.3	5.9
Depreciation	(10.2)	(10.7)	(11.2)	(11.7)	(12.1)
Teaching taxable income	27.7	32.8	38.4	42.9	47.2
Cash tax	(6.9)	(8.2)	(9.6)	(10.7)	(11.8)
Capex	(13.6)	(14.2)	(15.0)	(15.6)	(16.2)
Working-capital investment	(0.3)	(0.3)	(0.3)	(0.2)	(0.2)
FCF before debt service	21.1	25.2	29.6	33.4	37.0

Table 31.8 — Complete debt and cash schedule

€m	Y0	Y1	Y2	Y3	Y4	Y5
Opening term loan	—	280.0	268.1	254.0	237.8	219.7
Mandatory amortisation	—	(2.8)	(2.8)	(2.8)	(2.8)	(2.8)
Cash sweep	—	(9.2)	(11.2)	(13.4)	(15.3)	(17.1)
Ending term loan	280.0	268.1	254.0	237.8	219.7	199.9
Senior notes	140.0	140.0	140.0	140.0	140.0	140.0
Ending PIK principal	40.0	44.0	48.4	53.2	58.6	64.4
Revolver	0.0	0.0	0.0	0.0	0.0	0.0
Ending gross debt	460.0	452.1	442.4	431.1	418.3	404.3
Ending cash	10.0	19.2	30.4	43.8	59.1	76.2
Ending net debt	450.0	432.9	412.1	387.3	359.3	328.1
Net leverage	7.03x	6.23x	5.51x	4.82x	4.24x	3.69x

Mini-example 2 — PIK is not free. The €40.0m PIK tranche becomes $40.0 \times 1.10^5 = €64.42\text{m}$. It consumes no cash interest during the forecast, but it adds €24.42m of principal. If a modeller excludes PIK from exit debt because it never appeared in cash interest, exit equity and MOIC are overstated by the same €64.42m balance, not merely by the €24.42m increase.

Mini-example 3 — the Year 1 sweep circle. The converged Year 1 sweep is €9.15m. Ending term debt is $280.0 - 2.8 - 9.15 = €268.05\text{m}$. Average term debt is €274.03m, producing €16.44m of term interest. Add €11.20m of note

interest and cash interest is €27.64m. That interest feeds tax and FCF, and 50% of post-amortisation FCF returns to the €9.15m sweep. The loop reconciles.

31.6 Exit value and sponsor return

The base case exits at the end of Year 5 at 10.0x Year 5 EBITDA. Exit enterprise value is €88.986m × 10.0 = €889.864m. Exit net debt is €328.124m. Sponsor equity proceeds are therefore €561.741m.

Table 31.9 — Base exit and return

Metric	Formula	Result
Exit EBITDA	Year 5 EBITDA	€89.0m
Exit multiple	Input	10.0x
Exit enterprise value	88.986×10.0	€889.9m
Exit gross debt	Debt schedule	€404.3m
Exit cash	Cash schedule	€76.2m
Exit net debt	$404.3 - 76.2$	€328.1m
Sponsor equity proceeds	$889.9 - 328.1$	€561.7m
Sponsor equity invested	Sources and uses	€213.6m
MOIC	$561.7 / 213.6$	2.63x
Five-year IRR	$2.6299^{(1/5)} - 1$	21.3%

Mini-example 4 — MOIC does not contain time. A 2.63x result in five years is a 21.3% IRR. The same 2.63x in three years is 38.0%; in seven years it is 14.8%. Never compare sponsor outcomes using MOIC alone when holding periods differ.

The base return should not be read as proof of debt safety. Year 1 net leverage is still 6.23x, and the model relies on margin expansion plus revenue growth. Returns can remain attractive under an exit multiple while liquidity or covenant protection fails earlier. A lender asks whether cash survives each period and what recovery protects the claim. A sponsor asks what equity remains at exit. Chapter 32 puts those questions side by side.

31.7 Value-creation bridge

The bridge starts with sponsor equity invested, not the €190.0m entry operating equity value. EBITDA growth at the unchanged 10.0x multiple adds $€(88.986 - 64.000) \times 10.0 = €249.864\text{m}$. There is no multiple change in the base case. Net debt falls by $€450.000\text{m} - €328.124\text{m} = €121.876\text{m}$. Transaction fees and OID of €23.6m explain why sponsor investment exceeded entry operating equity value.

Table 31.10 — Value bridge

Bridge item	€m	Check
Sponsor equity invested	213.6	Starting point
EBITDA growth at 10.0x	+249.9	$(89.0 - 64.0) \times 10.0x$
Exit-multiple change	0.0	$(10.0x - 10.0x) \times 89.0$
Net-debt reduction	+121.9	450.0 – 328.1
Fees and OID friction	(23.6)	18.0 + 5.6
Exit equity proceeds	561.7	Reconciles to Table 31.9

This bridge is diagnostic. It says 72% of the increase from sponsor investment to exit proceeds comes from EBITDA growth, 35% comes from net-debt reduction and negative 7% comes from transaction friction; percentages sum to 100% of the €348.1m increase after rounding. It does not prove that EBITDA growth is operationally achievable. The bridge identifies where the return is coming from so that the underwriting can attack the right assumptions.

31.8 Sensitivities and breakpoints

A two-way sensitivity is not a set of forecasts. It is a map of mechanical exposure. The following table changes Year 5 EBITDA and the exit multiple while holding exit net debt at the base €328.1m. Each cell displays MOIC / five-year IRR.

Table 31.11 — Exit EBITDA and multiple sensitivity

Exit EBITDA change	8.0x	9.0x	10.0x	11.0x	12.0x
(10%)	1.46x / 7.9%	1.84x / 12.9%	2.21x / 17.2%	2.59x / 20.9%	2.96x / 24.3%
(5%)	1.63x / 10.3%	2.03x / 15.2%	2.42x / 19.3%	2.82x / 23.0%	3.21x / 26.3%
Base	1.80x / 12.4%	2.21x / 17.2%	2.63x / 21.3%	3.05x / 25.0%	3.46x / 28.2%
+5%	1.96x / 14.4%	2.40x / 19.1%	2.84x / 23.2%	3.28x / 26.8%	3.71x / 30.0%
+10%	2.13x / 16.3%	2.59x / 20.9%	3.05x / 25.0%	3.50x / 28.5%	3.96x / 31.7%

The table exposes a key asymmetry. At 8.0x and 10% lower EBITDA, the sponsor still receives 1.46x, but a lender cannot infer safety from that positive equity outcome. The path may require additional liquidity before exit, and actual recoverable enterprise value can be lower than a going-concern multiple implies.

Table 31.12 — Return and credit breakpoints

Question	Formula	Breakpoint	Interpretation
Exit multiple for 2.00x MOIC	$(2 \times 213.6 + 328.1) / 89.0$	8.49x	Below this, base EBITDA and debt do not deliver 2.00x
Exit multiple for 20% IRR	$(213.6 \times 1.20^5 + 328.1) / 89.0$	9.66x	Base 10.0x leaves 0.34x of multiple cushion
EBITDA for 2.00x at 9.0x	$(2 \times 213.6 + 328.1) / 9.0$	€83.9m	5.7% below base Year 5 EBITDA
Maximum exit net debt for 1.50x at 9.0x	$89.0 \times 9.0 - 1.5 \times 213.6$	€480.5m	A return threshold, not a debt - capacity recommendation
Year 5 PIK at 12%	40.0×1.12^5	€70.5m	€6.1m above the 10% base balance
Revolver liquidity floor	Commitment less required draw	€40.0m	Draws cannot exceed commitment; minimum cash is not a plug

Sensitivity design should preserve causal consistency. A lower EBITDA path usually also changes tax, cash sweep, interest and exit net debt. Table 31.11 deliberately holds net debt constant to isolate two variables. A full downside must rerun the entire model. The reviewer should label which kind of sensitivity is being shown.

31.8.1 A full-path downside

The full downside removes the base case's comfortable growth path. Year 1 revenue is flat, Year 2 revenue falls 3.0%, and growth recovers to 2.0%, 3.0% and 4.0%. EBITDA margin falls to 18.0% in Year 1 and 16.0% in Year 2, then recovers gradually to 18.5% in Year 5. Capex rises to 4.5% of revenue. The same debt terms, tax convention and 50% sweep remain. The exit multiple falls to 8.5x. This is a coherent path: weaker trading reduces EBITDA, cash flow and debt repayment while the exit valuation also contracts.

Table 31.12A — Full-path downside

€m except ratios	Y1	Y2	Y3	Y4	Y5
Revenue	320.0	310.4	316.6	326.1	339.2
EBITDA	57.6	49.7	52.2	57.1	62.7
Cash interest	27.8	27.4	27.1	26.8	26.3
FCF before debt service	11.4	6.3	8.1	11.7	15.9
Cash sweep	4.3	1.7	2.6	4.4	6.6
Ending net debt	442.6	440.8	437.5	431.2	421.1
Net leverage	7.68x	8.88x	8.38x	7.56x	6.71x
Revolver	0.0	0.0	0.0	0.0	0.0

At 8.5x Year 5 EBITDA, downside exit enterprise value is €62.74m × 8.5 = €533.31m. Subtracting €421.12m of net debt leaves €112.20m for the sponsor. MOIC is 112.20 / 213.60 = 0.53x, and the five-year IRR is negative 12.1%. The business does not need the revolver in this annual case, yet sponsor value is impaired. Liquidity survival and a successful equity return are different tests.

The lender should not stop at the absence of a revolver draw. Year 2 net leverage is 8.88x and interest coverage using EBITDA divided by cash interest is only 1.81x. The debt balance hardly falls because PIK accretion offsets term repayment. If the facility had a 7.0x maintenance test, the case would require a covenant analysis even though minimum cash is preserved. If debt matures before the operating recovery, refinancing risk becomes the

binding constraint. A complete credit view therefore layers liquidity, covenant, maturity and recovery tests rather than selecting the one that passes.

The full-path downside also shows why a two-way terminal sensitivity can flatter risk. In Table 31.11, 10% lower EBITDA at 8.0x still produced 1.46x because net debt was held at the base €328.1m. The full downside generates much lower EBITDA and €93.0m more net debt. Re-running the path converts a positive sensitivity cell into a capital loss. Isolated sensitivities explain exposure; integrated scenarios test survival.

Figure 31.3 — The cash waterfall and the point of failure

EBITDA
 └ cash interest
 └ cash tax (teaching assumption)
 └ capex
 └ working-capital investment
 = free cash flow before debt service
 └ mandatory amortisation
 └ repay revolver to minimum cash
 └ 50% term-loan sweep
 └ retained cash

If the total is negative: draw revolver → test commitment → record funding deficit.

31.9 Lender view versus sponsor view

Both perspectives use the same model but ask different questions. The sponsor focuses on entry price, exit value and equity compounding. The lender focuses on cash interest, mandatory payment, minimum liquidity, leverage path and recovery if the operating plan fails. The model should not maintain two contradictory versions of EBITDA or cash. It should maintain one controlled dataset and display perspective-specific outputs.

Table 31.13 — One model, two questions

Model area	Sponsor question	Lender question
Entry valuation	Is the price compatible with target returns?	How much equity absorbs first loss?
EBITDA forecast	What creates enterprise - value growth?	What evidence supports debt service?
Cash flow	How quickly can debt be reduced?	Is cash sufficient each period?
PIK	Does non - cash funding protect early equity?	How quickly does the claim grow ahead of exit?
Cash sweep	How much flexibility remains?	How much deleveraging is contractually or operationally credible?
Exit multiple	What market assumption drives proceeds?	What recovery remains without relying on the exit case?
Sensitivity	What preserves MOIC and IRR?	What breaks liquidity, coverage or leverage first?

The most important conflict is timing. Sponsor equity can have positive terminal value even if the company encounters an earlier liquidity shortfall. A terminal model that does not include the intervening cash path can report a valid Year 5 equity value for a business that could not finance Year 2. That is why the revolver and minimum-cash logic are not optional.

31.9.1 Debt capacity is a multi-constraint output

Debt capacity should not be calculated as one leverage multiple multiplied by EBITDA. That equation produces one constraint, not a financing recommendation. A complete capacity analysis tests at least five dimensions: opening leverage, cash-interest coverage, intra-period liquidity, scheduled maturity or amortisation, and downside recovery. The binding dimension can change through time. Northstar opens with high leverage, but the base case's minimum cash is comfortable. The full downside preserves annual liquidity yet fails the equity-return test and carries leverage above 8.0x. A more seasonal case could exhaust the revolver before an annual leverage ratio is measured.

Start with leverage using a controlled numerator and denominator. Gross, net, senior secured and total leverage answer different questions. Cash should be netted only if it is accessible to the relevant debt perimeter and not required for operations. EBITDA should use the same scope and period as the debt balance. A pro forma denominator can be useful, but the model should display the adjustments and a version without them. Calling every result "leverage" invites the reader to compare unlike measures.

Coverage asks whether earnings or cash can absorb interest and fixed charges. EBITDA / cash interest is easy to calculate but ignores capex, working capital and tax. A post-capex cash coverage measure is more conservative but depends on how maintenance spending is estimated. The best practice is to show several clearly named measures rather than choose the one that produces the desired answer. A ratio above 1.0x can still coexist with a cash shortfall when working capital or mandatory amortisation is large.

Liquidity capacity must be path-based. Add opening cash, committed availability and cash generation; subtract the required uses in the period; preserve minimum cash; and cap draws at actual assumed availability. Include fees and interest on incremental borrowing. If the facility has a springing test or borrowing condition, show it as a separate gate. The model can identify the economic consequence of a selected covenant assumption, but it cannot determine the legal availability of a draw without the operative document analysis.

Maturity capacity asks whether debt can be repaid or refinanced when due. A five-year model with six-year debt can hide the question just beyond the horizon. Extend the forecast through the first material maturity or calculate the refinance amount and the EBITDA, rate, leverage and coverage needed to support it. A terminal enterprise value is not a refinancing source unless a sale is part of the approved plan.

Recovery capacity is the final constraint. Estimate value at the correct entity, map each claim, deduct costs and apply a clearly labelled teaching waterfall. Do not assume that enterprise value automatically reaches every creditor. Guarantees, security, structural subordination and intercreditor terms are document- and law-dependent. Chapter 32 displays a synthetic entity-and-claim waterfall while keeping those legal assumptions bounded.

The output should therefore be a range with a named binding constraint. For example: "€460m of opening debt fits the selected entry structure, but downside leverage and maturity refinancing, not base-case liquidity, constrain the risk." That statement is more informative than "capacity is 7.0x." It tells the committee which assumption must be defended and which evidence should be monitored.

31.10 Common modelling failures

A hidden source plug. Sponsor equity is sometimes entered as a round number while fees or OID are left unreconciled. Sponsor equity should be the explicit residual after all cash sources and uses.

Cash and debt with different dates. Subtracting Year 4 cash from Year 5 debt corrupts net debt. Every net-debt calculation needs one date.

PIK in the cash-flow statement. PIK interest affects the debt balance and the teaching tax formula here, but it is not cash paid. Subtracting it as cash and capitalising it into principal double counts the burden.

A sweep larger than available cash. Sweep formulas must operate after minimum cash and revolver ordering. A term-loan repayment that drives cash below the floor is a model error.

Revolver as an unlimited plug. The facility has a €40.0m commitment. A required draw above that amount creates an unfunded deficit, not more revolver debt.

Interest circularity switched off without disclosure. Opening-balance interest is a legitimate simplified convention if documented. It is not legitimate to present it as average-balance interest.

Tax rate applied to EBITDA. Even in a simplified model, the tax base must be defined. This chapter deducts depreciation, cash interest and PIK interest solely as a teaching convention.

A multiple sensitivity that silently fixes equity value. Enterprise value, net debt and equity value must remain distinct. Change the multiple, recalculate enterprise value, and subtract the same-date net debt.

IRR from rounded MOIC. Use unrounded proceeds and investment. A displayed 2.63x can correspond to slightly different IRRs depending on the underlying values.

Returns as credit approval. A sponsor's positive expected value neither proves debt service nor establishes recovery. Credit analysis requires its own downside and claim waterfall.

31.10.1 A disciplined construction sequence

Build in modules and make each module pass before adding the next. First, create a control section containing units, dates, scenario, currency and sign conventions. Second, build sources and uses and refuse to proceed until the closing cash check is zero. Third, enter the operating assumptions and forecast revenue through working capital. Fourth, calculate cash flow before financing without any debt sweep or revolver. Fifth, build each debt instrument from opening face amount to ending face amount. Sixth, add cash and PIK interest with a documented timing convention. Seventh, add mandatory amortisation, minimum cash, revolver logic and voluntary sweep in the agreed order. Eighth, solve circularity. Ninth, calculate exit value and returns. Tenth, build sensitivities and QA outside the main formulas.

This sequence matters because it localises errors. If sources and uses fail before the operating model exists, the problem is at closing. If the debt roll-forward fails after interest is added, the problem is in financing rather than revenue. Large models are not difficult because multiplication is difficult; they are difficult because an error can travel through thousands of dependent cells. Modular checks stop that travel.

Signs should be consistent. One convention uses positive revenue and EBITDA, negative cash costs and positive debt balances. Another uses every cash-flow line as a positive use beneath a subtotal. Either can work. Mixing conventions creates formulas such as "subtract a negative capex" and makes review harder. This chapter displays cash uses in parentheses in narrative tables but stores their magnitudes as positive values in the formula explanations. The QA recalculates economic direction, not typography.

Scenario control also should be singular. If a model has a selector for Base, Downside or Severe, all scenario-dependent assumptions should respond to that control. Hard-coding a downside margin into one formula while the model header still says Base is more dangerous than a visible error. A reviewer should trace every scenario switch, confirm the active case and inspect whether debt terms or valuation assumptions change for a legitimate reason.

Avoid false precision. A forecast that displays revenue to six decimals is not more credible than one displayed to one decimal. Preserve unrounded values for calculations, but present the level of precision supported by the inputs. The Year 5 EBITDA in Northstar is €88.986433536m mathematically; €89.0m is the meaningful displayed result. The exact value remains available for reconciliation.

Version control is substantive. Record the model version, date, owner and input changes. A committee paper should state the model hash or stable version identifier so that the return, leverage and sensitivity shown can be reproduced. If an operating assumption changes after committee, rerun the debt schedule and returns; do not paste a new EBITDA into the output page. A conclusion tied to old bytes is historical evidence, not current approval.

Finally, separate model review from investment judgment. The model reviewer answers whether formulas, timing, units and stated assumptions are implemented correctly. The investment decision-maker answers whether the assumptions and risk are acceptable. One person may perform both roles, but the questions should not be merged. "The model works" must never mean "the deal works."

31.11 Independent QA

The checks below are model outputs, not decorative labels. A check passes only if the underlying formula is independently recalculated.

Table 31.14 — Displayed QA and sensitivity checks

#	Check	Recalculation	Result
1	Sources equal uses	$668.0 - 668.0$	PASS
2	Entry EV	64.0×10.0	€640.0m
3	Equity purchase price	$640.0 - 120.0 + 10.0$	€530.0m
4	TLB proceeds	$280.0 \times 98\%$	€274.4m
5	Sponsor equity residual	$668.0 - 274.4 - 140.0 - 40.0$	€213.6m
6	Opening gross debt	$280.0 + 140.0 + 40.0$	€460.0m
7	Opening net leverage	$(460.0 - 10.0) / 64.0$	7.03x
8	Year 3 revenue	356.16×1.05	€373.97m
9	Year 3 EBITDA	$373.97 \times 21.5\%$	€80.40m
10	PIK roll-forward	40.0×1.10^5	€64.42m
11	Term roll-forward	$280.0 - 5 \times 2.8 - \text{cumulative sweeps}$	€199.85m
12	Exit net debt	$404.27 - 76.15$	€328.12m
13	Exit EV	88.986×10.0	€889.86m
14	Exit equity	$889.86 - 328.12$	€561.74m
15	MOIC	$561.74 / 213.60$	2.6299x
16	IRR	$2.6299^{(1/5)} - 1$	21.34%
17	Value bridge	$213.6 + 249.864 + 121.876 - 23.6$	€561.74m
18	Minimum cash	$\text{min}(\text{ending cash})$	€19.15m; no draw

The model also checks that every debt balance is non-negative, cumulative mandatory amortisation does not exceed original principal, revolver draw is between zero and €40.0m, cash never falls below €10.0m after financing, annual cash changes reconcile, and the sensitivity table uses one exit date and one net-debt definition.

31.11.1 Independent review protocol

An independent review starts from outputs and works backward. Recalculate sponsor equity from sources and uses without using the model's residual. Recalculate one forecast year from prior-year revenue and the stated assumptions. Recalculate one interest period from opening and ending debt. Rebuild one sweep iteration. Reconcile ending cash to opening cash plus flows. Reconcile every debt instrument. Recalculate exit equity, MOIC and IRR. Rebuild at least three sensitivity cells, including a corner. Finally, compare the value bridge with the movement in equity value.

Then attack the model economically. Remove margin expansion. Delay revenue growth. Increase the cash interest rate. Increase PIK. Hold back working-capital release. Increase minimum cash. Reduce revolver commitment. Bring maturity inside the forecast. Use an exit multiple below entry. The objective is not to produce a dramatic downside; it is to identify the variable that causes the first breach of liquidity, covenant, maturity or return tolerance.

Review comments should be classified. A **formula defect** means the model does not implement its stated assumption. A **control defect** means the model can produce an inconsistent state without warning. An **assumption challenge** means the formula works but the input lacks support. A **scope limitation** means the model intentionally omits something, such as intra-year liquidity. A **specialist dependency** means the model uses a legal, tax or accounting assumption that must be confirmed outside the model. Clear classification prevents an economic disagreement from being "fixed" by overwriting a formula.

31.12 Exercises

Table 31.15 — Questions

Exercise	Task
1	Change TLB issue price from 98 to 97 while holding face debt and uses constant. Calculate sponsor equity and opening net leverage.
2	Recalculate Year 1 ending term debt if the sweep percentage is 75% and all other converged Year 1 FCF inputs are held constant. State why a full model would require a fresh circularity solve.
3	Calculate the exit multiple required for a 2.00x MOIC using base Year 5 EBITDA and exit net debt.
4	Change PIK rate from 10% to 12%. Calculate Year 5 PIK principal and the direct reduction in exit equity if no other variable changes.
5	A downside quarter opens with €10.0m cash and no revolver. EBITDA is €42.0m; cash interest is €30.0m; capex is €15.0m; working-capital investment is €5.0m; tax and mandatory amortisation are zero. Calculate the revolver draw required to preserve €10.0m minimum cash.

Before reading the answers, write the formula, unit and timing beside each result. A numerically correct answer with an unstated date or mixed unit should not pass review.

Appendix 31A — Formula register

Table 31.16 — Core formulas

Output	Formula
Entry EV	Year 0 EBITDA × entry multiple
Equity purchase price	Entry EV – acquired debt + acquired cash
Debt cash proceeds	Face amount × issue price
Sponsor equity	Total uses – debt cash proceeds
Revenue	Prior revenue × (1 + growth)
EBITDA	Revenue × EBITDA margin
Depreciation	Revenue × 3.0%
Capex	Revenue × 4.0%
Working-capital investment	1.5% × annual revenue increase
Cash tax	25% × max(0, EBITDA – depreciation – cash interest – PIK interest)
FCF before debt service	EBITDA – cash interest – cash tax – capex – ΔNWC
Sweep	50% × max(0, FCF – mandatory amortisation) after revolver ordering
Ending PIK	Opening PIK × 1.10
Net debt	Gross debt – cash
Exit EV	Exit EBITDA × exit multiple
Exit equity	Exit EV – exit net debt
MOIC	Exit equity / sponsor equity invested
IRR	$\text{MOIC}^{(1/5)} - 1$

Appendix 31B — Exercise answers

Table 31.17 — Answer key

Exercise	Answer and check
1	TLB proceeds fall from €274.4m to $280.0 \times 97\% = €271.6\text{m}$; sponsor equity rises by €2.8m to €216.4m. Face debt is unchanged, so opening net leverage remains 7.03x.
2	Holding converged Year 1 FCF of €21.11m constant, post-amortisation excess cash is $21.11 - 2.80 = €18.31\text{m}$; a 75% sweep is €13.73m and ending TLB is $280.0 - 2.8 - 13.73 = €263.47\text{m}$. A full average-balance model must re-solve because the larger sweep reduces interest and increases FCF.
3	$(2.00 \times 213.6 + 328.124) / 88.986 = 8.49\text{x}$.
4	$40.0 \times 1.12^5 = €70.49\text{m}$, versus €64.42m at 10%; direct exit-equity reduction is €6.07m if all else is fixed.
5	Pre-financing cash is $10.0 + 42.0 - 30.0 - 15.0 - 5.0 = €2.0\text{m}$; the draw required to restore €10.0m is €8.0m.

Appendix 31C — Review and release boundary

This chapter is self-contained and intentionally has no workbook. A reviewer can reproduce every displayed output from the tables and formula register. That does not make the chapter a transaction model or approval tool. A real LBO requires documented facility terms, financial-reporting policies, tax analysis, legal analysis, accounting treatment, currency and hedging assumptions, intra-year liquidity, acquisition perimeter, management evidence and independent validation.

The complete chapter must be rehashed after any edit. A qualified LBO modeller should validate the formulas, circularity, sensitivities and answers against the exact chapter bytes. Any retained legal, tax or accounting conclusion would require the appropriate bounded specialist review. Publication, distribution or transaction use is not authorised by this teaching model.

Synthetic Credit Case — Asteron Mission-Critical Components

Advanced clean-room teaching case. *Asteron, its markets, facilities, financials, covenants, documents and events are wholly fictional. Every number and formula was independently created for this edition. No real issuer, private mandate, proprietary model, licensed dataset or live credit decision is used. The five-year annual forecast and eight-quarter liquidity bridge are fully displayed; there is no companion workbook. Legal, tax, accounting, security, guarantee and covenant outcomes are selected teaching assumptions, not advice or conclusions about any actual transaction.*

Credit work becomes difficult when individually reasonable observations must be joined into one decision. Revenue can recover while liquidity fails. EBITDA can cover cash interest while mandatory investment consumes cash. A covenant can look breached but not apply until a draw threshold is crossed. Enterprise value can support first-lien recovery while leaving an unsecured claim with nothing. The purpose of this case is to make those joins explicit.

Asteron manufactures precision components and provides aftermarket maintenance for fictional automated production lines. The case begins with a controlled Year 0 dataset, builds five annual periods under Base, Downside and Severe scenarios, then opens the Severe case into eight quarters. The quarterly bridge identifies the first revolver draw, the first springing-covenant test, the amount of covenant headroom and the remaining liquidity. The final section constructs an entity-and-claim recovery waterfall and a committee recommendation.

Learning objectives

After completing the case, you should be able to:

- ♦ 1. separate synthetic facts, modelling assumptions, selected document terms and unresolved evidence;
- ♦ 2. reconcile revenue, EBITDA, depreciation, capex, working capital, cash interest, tax and free cash flow for five annual periods;
- ♦ 3. roll each debt instrument and cash balance without hidden financing plugs;
- ♦ 4. compare Base, Downside and Severe paths using coordinated definitions;
- ♦ 5. explain why annual cash flow can conceal an intra-year liquidity or covenant breakpoint;
- ♦ 6. calculate a springing senior-secured net-leverage test only when its selected draw condition applies;
- ♦ 7. distinguish a maintenance test from an incurrence condition or internal monitoring threshold;
- ♦ 8. allocate synthetic value by entity and claim without double counting cash or enterprise value;
- ♦ 9. identify the operational evidence that would confirm or disprove the underwriting case; and
- ♦ 10. deliver a bounded teaching recommendation rather than a live approval.

The case draws on the framework in Chapter 27, the working-capital controls in Chapter 28, the corporate and LBO modelling disciplines in Chapters 30–31, and the leverage, liquidity, covenant and recovery tools in Chapters 8, 15–16, 18–21 and 24. Chapters 29, 34 and 36 provide adjacent ratings, relative-value and committee perspectives.

32.1 Control page: units, dates and evidence classes

All financial amounts are **€ millions**. Percentages and turns are labelled separately. Year 0 is the latest completed annual period. Years 1–5 are forecast years. Q1–Q4 compose Severe Year 1; Q5–Q8 compose Severe Year 2. Income-statement and cash-flow values are period flows. Debt, cash and enterprise value are end-of-period balances. Calculations use unrounded values and display one or two decimals.

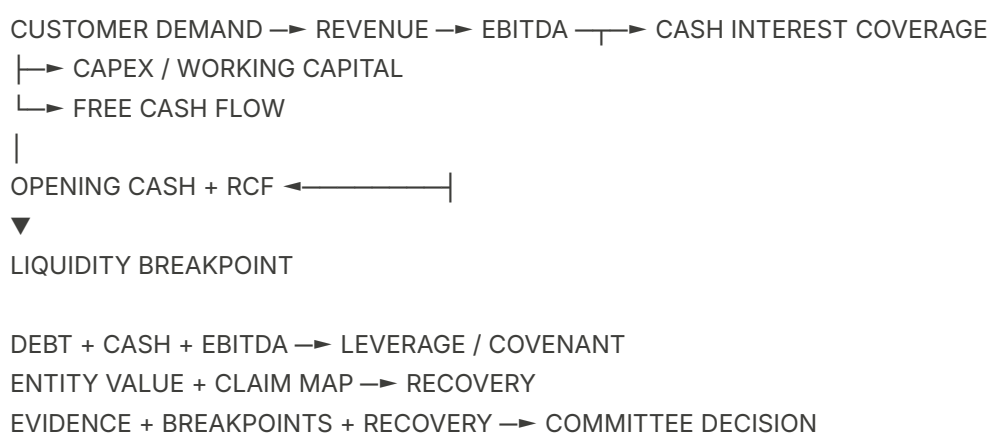
The model uses four evidence labels:

- ♦ • **SYNTHETIC FACT** — a fixed case input, such as Year 0 revenue or opening debt;
- ♦ • **ASSUMPTION** — an underwriting choice, such as future margin or capex;
- ♦ • **SELECTED TERM** — a fictional document mechanic used only for the exercise; and
- ♦ • **OPEN EVIDENCE** — information a real committee would require before deciding.

Table 32.1 — Case control record

Field	Value	Evidence class
Case company	Asteron Mission - Critical Components	Synthetic fact
Currency / unit	Euro / €m	Control
Historical period	Year 0	Synthetic fact
Annual forecast	Years 1–5	Scope decision
Liquidity bridge	Q1–Q8	Scope decision
Opening cash	€25.0m	Synthetic fact
Minimum cash	€15.0m	Assumption
Revolver commitment	€50.0m	Selected term
Tax convention	25% of positive teaching taxable income	Assumption; not tax advice
D&A convention	3.0% of revenue	Assumption; not an accounting conclusion
Recovery date	End of Q8	Assumption

Figure 32.1 — Credit driver tree



32.2 Business and dataset

Asteron derives 60% of Year 0 revenue from aftermarket maintenance and replacement parts and 40% from original-equipment projects. The aftermarket portion is assumed to be more recurring but not guaranteed; the project portion is more exposed to customer deferral. No customer name is supplied. The top-five customer concentration is a synthetic 34% of revenue. A real review would need contract duration, cancellation rights, backlog conversion, pricing history, customer profitability and receivables ageing. None is inferred here.

Year 0 revenue is €500.0m and EBITDA is €75.0m, a 15.0% margin. Maintenance and growth capex together are €22.5m, or 4.5% of revenue. Opening gross debt is €450.0m: a €300.0m first-lien term loan and €150.0m HoldCo notes. Opening cash is €25.0m, so net debt is €425.0m and net leverage is $425.0 / 75.0 = 5.67x$.

Table 32.2 — Controlled Year 0 dataset

Item	Value	Formula / boundary
Revenue	€500.0m	Synthetic fact
Aftermarket share	60.0%	Synthetic mix assumption
Project share	40.0%	Synthetic mix assumption
EBITDA	€75.0m	Synthetic fact
EBITDA margin	15.0%	$75.0 / 500.0$
Capex	€22.5m	4.5% of revenue
Term loan B	€300.0m	Selected debt
HoldCo notes	€150.0m	Selected debt
Revolver	€0.0m	Opening balance
Cash	€25.0m	Opening balance
Net debt	€425.0m	$300.0 + 150.0 - 25.0$
Net leverage	5.67x	$425.0 / 75.0$

Table 32.3 — Open evidence plan

Driver	Required evidence in a real case	Disconfirming signal
Aftermarket resilience	Renewal, churn, service interval and installed-base data	Deferrals or cancellations rise despite installed base
Project revenue	Backlog by date, cancellation and milestone terms	Backlog converts later or at lower margin
Price / cost	Invoice-level price, labour and material bridge	Price fails to offset labour or input inflation
Margin recovery	Site-level productivity and restructuring milestones	Savings lag while one-off costs recur
Capex	Asset register, project list and maintenance requirement	Deferred maintenance or safety spending rises
Working capital	Receivable ageing, inventory turns, supplier terms	Collections slow or suppliers shorten terms
Liquidity	Cash by entity, RCF usage, LC and ancillary utilisation	Reported cash is trapped or availability is lower
Recovery	Entity map, guarantees, collateral and claim schedule	Value sits outside the relevant claim perimeter

32.2.1 Turning qualitative risk into model variables

The business description matters only when it changes a cash, covenant or recovery variable. "Mission-critical" is not a number. It can support a revenue-resilience assumption only if customers cannot defer service without a measurable operational consequence and contracts or observed renewal history support that inference.

"Aftermarket" is not automatically recurring. The evidence plan therefore asks how much work is scheduled, cancellable, usage-driven or discretionary.

Customer concentration should enter at least one scenario. If the top five customers represent 34% of revenue, the model should not assume that all 34% disappears; nor should it ignore the concentration. A bounded stress might delay one large project, reduce renewal at one account and lengthen receivables for the concentrated customer group. The resulting revenue, margin and working-capital effects should be modelled in the same periods. A revenue haircut without the collection effect can understate liquidity stress.

Margin quality also needs a bridge. Year 0 EBITDA of €75.0m is a synthetic fact, but a real underwriter would reconcile reported EBITDA to adjusted EBITDA and then to underwritten EBITDA. Add-backs should be grouped by type, dated and linked to evidence. Realised savings differ from planned savings; recurring run-rate effects differ from one-time costs; revenue synergies differ from cost removal. This case avoids add-backs entirely so that covenant and cash analysis use one visible numerator. That simplicity is a control, not a statement that add-backs never exist.

Capex has both an amount and a consequence. If a Severe case cuts capex below maintenance requirements, later revenue or margin should weaken, or operational risk should rise. Asteron's Severe case instead increases capex to 5.0% of revenue, representing the cash needed to stabilise operations during disruption. The assumption worsens liquidity but avoids the incoherent result of a stressed business preserving full earnings while eliminating essential investment.

Working capital transmits operating stress into cash. Revenue decline can release receivables and inventory mechanically, but distress can reverse that benefit through slower collections, excess inventory and tighter supplier terms. The annual Severe case therefore uses explicit cash inputs instead of a fixed percentage. The quarterly bridge allocates investment and release seasonally. This is why the model can show a Q3 draw and a Q4 repayment even though annual revenue is lower.

Finally, sponsor support should not be assumed. A sponsor may have economic reasons to contribute equity, but the lender cannot treat that contribution as committed liquidity without an enforceable and funded arrangement. The committee can evaluate an equity cure, new money or asset sale as a remedy, but the unremedied case must display the breakpoint first. Otherwise the model makes the solution arrive exactly when needed because the solution was typed into the cash line.

32.3 Selected debt and covenant terms

The fictional debt structure is intentionally simple. The €300.0m term loan and revolver are assumed to be obligations of the operating group and to share a selected first-lien recovery class. The €150.0m notes are issued at HoldCo and, for this teaching waterfall, have no direct OpCo guarantee or collateral claim. That is a scenario assumption, not a legal conclusion. A real result requires the executed guarantee, security and intercreditor documents and jurisdiction-specific analysis.

The term loan pays 6.5% cash interest and amortises €3.0m each year. The notes pay 8.0% cash interest and are bullet. The revolver pays 9.0% on average drawn balance and has a €50.0m commitment. The annual Base and Downside models sweep 50% of excess cash after mandatory amortisation. The Severe case suspends voluntary sweep once the revolver is required.

Table 32.4 — Debt terms

Instrument	Opening €m	Cash rate	Amortisation	Commitment / maturity assumption	Selected recovery position
Revolver	0.0	9.0%	None	€50.0m commitment	First- lien OpCo class
Term loan B	300.0	6.5%	€3.0m annually	Beyond Year 5	First- lien OpCo class
HoldCo notes	150.0	8.0%	Bullet	Beyond Year 5	HoldCo claim; no OpCo guarantee in case

The case includes a springing maintenance test: senior-secured net leverage must not exceed 5.50x when revolver drawings exceed 35% of the €50.0m commitment. The trigger is therefore drawings above €17.5m. For the exercise, senior-secured net debt equals term loan plus revolver less cash, and LTM EBITDA is the sum of the latest four quarterly EBITDA values. Letters of credit and cash-netting limitations are assumed absent. Those simplifications are selected terms, not descriptions of market practice.

Two other ratios are monitoring tools. Total net leverage of 6.00x is a selected incremental-debt condition; failing it does not by itself create a maintenance breach unless the company takes the action to which the condition attaches. EBITDA / cash interest of 2.00x is an internal early-warning threshold, not a contractual event of default in this case.

Table 32.5 — Definitions and consequences

Measure	Formula	Level	Consequence in this case
Springing senior-secured net leverage	$(TLB + RCF - \text{cash}) / \text{LTM EBITDA}$	Maximum 5.50x	Tested only when RCF draw exceeds €17.5m
RCF trigger	$RCF / €50.0m$	Greater than 35.0%	Activates springing test
Total net leverage	$(TLB + \text{notes} + RCF - \text{cash}) / \text{EBITDA}$	6.00x	Incremental-debt condition only
Cash-interest coverage	$\text{EBITDA} / \text{cash interest}$	2.00x	Internal watch threshold
Minimum liquidity	Cash after financing	€15.0m	Revolver draws preserve floor until commitment is exhausted

The distinction between consequence types is essential. A ratio can fail economically while no contractual test applies. Conversely, a springing test can activate suddenly when one more euro of revolver is drawn. The analyst should calculate both economic stress and the selected document consequence, then keep the legal application subject to the operative documents and qualified review.

32.4 Annual operating scenarios

The Base case grows revenue 5.0% annually. Margin rises from 15.5% to 16.5%. Capex remains 4.5% of revenue and working-capital investment equals 2.0% of annual revenue growth. The Downside case has flat Year 1 revenue, a slow recovery and margins that fall to 13.5% before recovering. The Severe case reduces Year 1 revenue by 10%, Year 2 by a further 5%, and margins to 11.0% and 9.0%. Severe capex is 5.0% of revenue, and restructuring cash costs are €4.0m, €6.0m and €3.0m in Years 1–3.

Table 32.6 — Scenario assumptions

Assumption	Base	Downside	Severe
Revenue path	+5% each year	0%, +1%, +2%, +3%, +3%	–10%, –5%, 0%, +2%, +3%
EBITDA margin path	15.5% to 16.5%	14.0%, 13.5%, 13.5%, 14.0%, 14.5%	11.0%, 9.0%, 10.0%, 11.0%, 12.0%
Capex / revenue	4.5%	4.5%	5.0%
ΔNWC	2% of revenue increase	2% of revenue increase	Explicit annual cash inputs
Restructuring cash cost	None	€2.0m in Y2–Y3	€4.0m, €6.0m, €3.0m in Y1–Y3
Cash sweep	50% after amortisation	50% after amortisation	None once revolver is required

Table 32.7 — Base operating forecast

€m except percentages	Y0	Y1	Y2	Y3	Y4	Y5
Revenue	500.0	525.0	551.3	578.8	607.8	638.1
EBITDA	75.0	81.4	88.2	93.8	99.7	105.3
EBITDA margin	15.0%	15.5%	16.0%	16.2%	16.4%	16.5%
Depreciation	15.0	15.8	16.5	17.4	18.2	19.1
Capex	22.5	23.6	24.8	26.0	27.3	28.7
Working-capital investment	—	0.5	0.5	0.6	0.6	0.6

Teaching cash tax is 25% of positive EBITDA – depreciation – cash interest. This is a modelling convention, not tax advice. Interest uses average term and revolver balances. Free cash flow before debt service is EBITDA – cash interest – teaching cash tax – capex – ΔNWC – restructuring cash cost.

Table 32.8 — Base cash flow and debt

€m except ratios	Y1	Y2	Y3	Y4	Y5
Cash interest	31.2	30.4	29.5	28.5	27.4
Teaching cash tax	8.6	10.3	11.7	13.2	14.7
FCF before debt service	17.5	22.1	25.9	30.0	33.9
Mandatory amortisation	3.0	3.0	3.0	3.0	3.0
Cash sweep	7.2	9.6	11.5	13.5	15.4
Ending TLB	289.8	277.2	262.8	246.3	227.8
Ending RCF	0.0	0.0	0.0	0.0	0.0
Ending cash	32.2	41.8	53.3	66.7	82.2
Ending net debt	407.5	385.4	359.5	329.5	295.6
Net leverage	5.01x	4.37x	3.83x	3.31x	2.81x
Cash-interest coverage	2.61x	2.90x	3.17x	3.49x	3.84x

Base cash generation is not the decision; it is the reference. Year 1 FCF before debt service is $81.38 - 31.17 - 8.61 - 23.63 - 0.50 = €17.47\text{m}$. After €3.0m amortisation, half the €14.47m excess is swept and half remains as cash. Ending cash is $25.0 + 17.47 - 3.0 - 7.23 = €32.23\text{m}$. Ending net debt is $289.77 + 150.0 - 32.23 = €407.53\text{m}$.

32.5 Annual downside and severe paths

The Downside retains positive free cash flow, but leverage remains near 6.0x for three years. The Severe case requires revolver support in Year 1, reaches €26.5m of required draw in Year 2 and exceeds the €50.0m commitment in Year 4. Once required draw exceeds commitment, the model records an unfunded deficit; it does not create an unlimited revolver.

Table 32.9 — Downside summary

€m except ratios	Y1	Y2	Y3	Y4	Y5
Revenue	500.0	505.0	515.1	530.6	546.5
EBITDA	70.0	68.2	69.5	74.3	79.2
FCF before debt service	10.3	6.9	7.7	12.9	16.4
Ending net debt	414.7	407.8	400.1	387.2	370.7
Net leverage	5.92x	5.98x	5.75x	5.21x	4.68x
Cash-interest coverage	2.24x	2.21x	2.27x	2.46x	2.68x
Ending RCF	0.0	0.0	0.0	0.0	0.0

Table 32.10 — Severe summary and liquidity requirement

€m except ratios	Y1	Y2	Y3	Y4	Y5
Revenue	450.0	427.5	427.5	436.1	449.1
EBITDA	49.5	38.5	42.8	48.0	53.9
FCF before debt service	(8.6)	(21.9)	(15.9)	(9.5)	(6.1)
TLB after amortisation	297.0	294.0	291.0	288.0	285.0
RCF required for €15m cash	1.6	26.5	45.3	57.8	66.9
RCF commitment	50.0	50.0	50.0	50.0	50.0
Unfunded deficit	0.0	0.0	0.0	7.8	16.9
Net leverage before deficit	8.76x	11.84x	11.03x	10.02x	9.03x
Cash-interest coverage	1.57x	1.18x	1.25x	1.36x	1.52x

32.5.1 Reading the annual scenarios correctly

The Base case deleverages through both EBITDA growth and cash retention. Net debt falls €129.4m by Year 5, while EBITDA rises €30.3m. An analyst should separate those effects. If all deleveraging is described as “cash paydown,” the underwriting misses that a large portion of the leverage improvement comes from the denominator. If the margin case fails, leverage remains higher even before cash flow is recalculated.

The Downside is not a default case. It is a weak-credit case. Cash-interest coverage remains above 2.0x, no revolver is drawn and net debt declines, but leverage stays between 5.75x and 5.98x through Year 3. That path may be acceptable or unacceptable depending on price, maturity, documentation and recovery. The model supplies the risk shape; it does not substitute for a decision.

The Severe case has two phases. In Years 1–2, lower earnings, restructuring cash costs and investment consume liquidity. In Year 3, EBITDA begins to recover, but cash flow remains negative and required RCF draw rises to €45.3m. In Year 4, the business may be improving operationally while liquidity fails because cumulative burn exceeds commitment. Recovery in the income statement arrives after the financing breakpoint. A turnaround can be economically credible and still arrive too late for the existing capital structure.

Cash taxes fall to zero in Severe Years 2–4 under the teaching formula. That is not a tax conclusion and should not be treated as a source of certainty. A real company may pay tax in entities or jurisdictions that do not share losses, face limitations on interest deductions, or have instalments and prior-year liabilities. A lender downside should test cash tax as a separate input when the cushion is narrow.

The annual Severe table also distinguishes required draw from funded draw. A model that permits €57.8m on a €50.0m facility has not discovered additional liquidity; it has concealed a €7.8m deficit. Once the commitment is reached, the next euro of cash use requires a new source or an unpaid obligation. The output should record both the capped balance and the unmet cash requirement.

The Severe annual table identifies the direction but not the intra-year date. Year 2 reports €26.5m of required revolver at year-end. It does not show whether the 35% springing trigger was crossed in Q5 or Q8, whether the covenant failed when activated, or how much availability remained at that moment. The quarterly bridge answers those questions.

32.6 Eight-quarter Severe liquidity bridge

The quarter pattern is not a mechanical division by four. Revenue and working capital are seasonal. Q1–Q4 revenue totals €450.0m and Q5–Q8 totals €427.5m. Margins fall from 12.0% in Q1 to 9.0% in Q5–Q8. Capex is 5.0% of revenue. Working-capital outflow is positive when cash is invested and negative when cash is released. Restructuring costs are paid in Q2, Q3, Q5 and Q6.

Table 32.11 — Quarterly operating inputs

€m except margin	Q1	Q2	Q3	Q4	Q5	Q6	Q7	Q8
Revenue	105.0	115.0	120.0	110.0	100.0	110.0	115.0	102.5
EBITDA margin	12.0%	11.0%	10.5%	10.5%	9.0%	9.0%	9.0%	9.0%
EBITDA	12.60	12.65	12.60	11.55	9.00	9.90	10.35	9.23
Capex	5.25	5.75	6.00	5.50	5.00	5.50	5.75	5.13
ΔNWC outflow / (release)	5.00	3.00	(2.00)	(7.00)	4.00	3.00	(2.00)	(4.50)
Restructuring cash cost	0.00	2.00	2.00	0.00	3.00	3.00	0.00	0.00

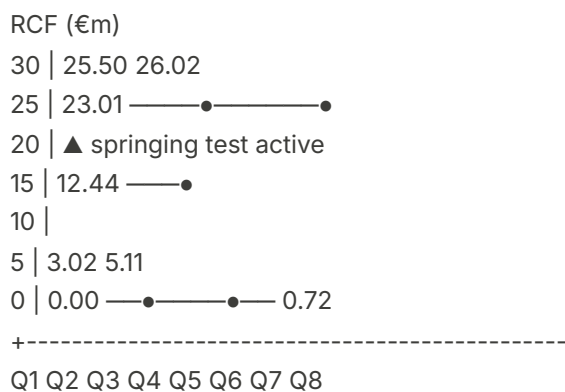
Quarterly cash interest includes 6.5% on average TLB, 8.0% on notes and 9.0% on average revolver. Mandatory TLB amortisation is €0.75m per quarter. Cash is held at €15.0m by drawing or repaying the revolver. The bridge assumes the draw is available until the €50.0m commitment is reached; it does not opine on legal draw conditions.

Table 32.12 — Eight-quarter liquidity bridge

€m	Q1	Q2	Q3	Q4	Q5	Q6	Q7	Q8
Opening cash	25.00	18.73	15.00	15.00	15.00	15.00	15.00	15.00
EBITDA	12.60	12.65	12.60	11.55	9.00	9.90	10.35	9.23
Cash interest	(7.88)	(7.90)	(7.94)	(7.90)	(7.97)	(8.21)	(8.35)	(8.37)
Capex	(5.25)	(5.75)	(6.00)	(5.50)	(5.00)	(5.50)	(5.75)	(5.13)
ΔNWC cash flow	(5.00)	(3.00)	2.00	7.00	(4.00)	(3.00)	2.00	4.50
Restructuring cost	0.00	(2.00)	(2.00)	0.00	(3.00)	(3.00)	0.00	0.00
Mandatory amortisation	(0.75)	(0.75)	(0.75)	(0.75)	(0.75)	(0.75)	(0.75)	(0.75)
Cash before financing	18.73	11.98	12.91	19.40	3.28	4.44	12.50	14.48
RCF draw / (repayment)	0.00	3.02	2.09	(4.40)	11.72	10.56	2.50	0.52
Ending RCF	0.00	3.02	5.11	0.72	12.44	23.01	25.50	26.02
Ending cash	18.73	15.00	15.00	15.00	15.00	15.00	15.00	15.00
Remaining RCF availability	50.00	46.98	44.89	49.28	37.56	26.99	24.50	23.98

The first draw occurs in Q2. A Q4 working-capital release repays most of it, so the annual Year 1 ending draw is only €0.72m. That small year-end number hides Q3 peak usage of €5.11m. In Year 2, cash burn accelerates. Q5 draws €11.72m and Q6 draws €10.56m. The 35% trigger is crossed in Q6 because €23.01m is 46.0% of the €50.0m commitment.

Figure 32.2 — Liquidity path and covenant activation



Trigger = €17.50m. It is not crossed until Q6.

32.7 Quarterly covenant breakpoint

LTM EBITDA is the sum of the latest four quarters. At Q6, it is $Q3\ 12.60 + Q4\ 11.55 + Q5\ 9.00 + Q6\ 9.90 = €43.05m$. Q6 ending TLB is $300.0 - 6 \times 0.75 = €295.50m$. Senior-secured net debt is $295.50 + 23.01 - 15.00 = €303.51m$. Senior-secured net leverage is therefore $303.51 / 43.05 = 7.05x$, above the selected 5.50x maximum.

Table 32.13 — Covenant activation and headroom

Quarter	LTM EBITDA €m	Ending TLB €m	RCF €m	RCF utilisation	Test active?	Senior net leverage	Headroom / (shortfall) €m
Q4	49.40	297.00	0.72	1.4%	No	5.72x	Not applicable
Q5	45.80	296.25	12.44	24.9%	No	6.41x	Not applicable
Q6	43.05	295.50	23.01	46.0%	Yes	7.05x	(66.73)
Q7	40.80	294.75	25.50	51.0%	Yes	7.48x	(80.85)
Q8	38.48	294.00	26.02	52.0%	Yes	7.93x	(93.41)

Headroom is calculated as $5.50 \times \text{LTM EBITDA} - \text{senior-secured net debt}$. At Q6, permitted debt under the selected ratio is $5.50 \times 43.05 = \text{€}236.78\text{m}$; actual senior-secured net debt is $\text{€}303.51\text{m}$, so shortfall is $\text{€}66.73\text{m}$ using unrounded balances. This is an economic calculation under selected terms. Whether cash can be netted, EBITDA adjusted, a cure used or a breach declared depends on the actual documents and applicable law in a real case.

The internal 2.00x coverage watch also fails. LTM cash interest is $\text{€}32.02\text{m}$ at Q6, so coverage is $43.05 / 32.02 = 1.34\text{x}$. That failure is an early-warning condition, not a contractual default in the exercise. Keeping the two consequences separate prevents the committee from overstating or understating the problem.

32.7.1 From ratio output to document question

A covenant calculation has four layers: the economic data, the contractual definitions, the activation condition and the consequence. The economic data say what Asteron's debt, cash and EBITDA are under the case. The selected definitions say which of those amounts enter the numerator and denominator. The activation condition says the test is dormant until revolver drawing exceeds $\text{€}17.5\text{m}$. The consequence would be determined by the fictional document process, which this chapter does not try to turn into a legal opinion.

Each layer can change the result. If only $\text{€}5.0\text{m}$ of cash were eligible for netting, Q6 senior-secured net debt would increase by $\text{€}10.0\text{m}$. If $\text{€}8.0\text{m}$ of permitted EBITDA adjustments were supported, LTM EBITDA would rise to $\text{€}51.05\text{m}$ and leverage would fall, though it would still need to be tested against the selected definition and cap. If $\text{€}6.0\text{m}$ of letters of credit counted toward revolver utilisation, the trigger could activate earlier. A correct analysis does not choose among those alternatives; it reads the exact terms, records the evidence and calculates each applicable result.

Headroom should be expressed in both turns and euros. Q6 is 1.55 turns above the 5.50x maximum, but the $\text{€}66.73\text{m}$ debt shortfall is more actionable. It shows the amount by which senior-secured net debt would have to fall, holding EBITDA fixed, or the amount of EBITDA required to close the gap, holding debt fixed. The required LTM EBITDA at current debt is $303.51 / 5.50 = \text{€}55.18\text{m}$, $\text{€}12.13\text{m}$ above the case result.

A cure or amendment should never be inserted as a free formula. An equity contribution may affect cash, debt or covenant EBITDA only as the selected document permits and only for the allowed period and purpose. An amendment may require consent, fees, new economics and conditions. The model can run a transparent sensitivity—for example, $\text{€}25.0\text{m}$ of new equity used entirely to repay the revolver—but the committee should see the pre-remedy breach, the remedy assumptions and the residual gap separately.

Timing governs action. Q5 leverage is already 6.41x, but the selected springing test is dormant. That does not make Q5 safe; it creates a short window in which management and lenders can act before the draw activates a failing test. The monitor should therefore flag both the economic deterioration and the expected trigger date. Waiting for a formal test can consume negotiating time and remaining liquidity.

32.8 Liquidity breakpoint beyond Q8

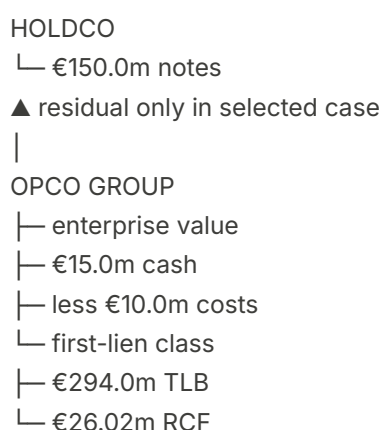
At Q8, remaining revolver availability is €23.98m. If the next two quarters require €12.0m and €15.0m of additional draw after interest, the commitment is exhausted during Q10. Q9 leaves €11.98m. Q10 needs €15.0m, producing a €3.02m funding deficit. The breakpoint is not “Year 3”; it is the point in Q10 when cumulative required draw reaches the remaining commitment.

This extrapolation is a sensitivity, not a forecast. Management action could reduce capex, improve collections, raise equity, sell assets, amend facilities or restructure obligations. Each action has its own timing, execution, document, legal and value consequences. The credit conclusion should state the cash date before giving credit to a remedy.

32.9 Recovery at the end of Q8

Recovery begins with the entity and claim map. The teaching case places operating enterprise value and €15.0m of cash at the OpCo group. It deducts €10.0m of selected administration and enforcement cost before creditor distributions. TLB and RCF share the first-lien class. HoldCo notes receive only value remaining after that class and assumed upstream availability. No value is counted twice.

Figure 32.3 — Selected entity and claim waterfall



Available OpCo value → first lien → residual to HoldCo notes.

Actual guarantees, security, priority and upstreaming require document and legal analysis.

Table 32.14 — Value sensitivity

Scenario	Enterprise value €m	Plus cash	Less costs	Distributable value €m
Low	200.0	15.0	(10.0)	205.0
Mid	250.0	15.0	(10.0)	255.0
High	300.0	15.0	(10.0)	305.0
Upper	350.0	15.0	(10.0)	355.0

Table 32.15 — Claim waterfall

Scenario	First-lien claim €m	First-lien recovery €m	First-lien recovery	Residual for notes €m	Notes recovery
Low	320.02	205.00	64.1%	0.00	0.0%
Mid	320.02	255.00	79.7%	0.00	0.0%
High	320.02	305.00	95.3%	0.00	0.0%
Upper	320.02	320.02	100.0%	34.98	23.3%

The waterfall is not a valuation opinion. It is a sensitivity. Enterprise value must be supported independently, and the applicable entity perimeter, cash accessibility, claims, costs, guarantees, collateral, priority and intercreditor provisions must be validated. A consolidated multiple cannot be poured into every entity. If €50.0m of Upper-case value is moved outside the selected OpCo claim perimeter and no value is assumed to return, distributable OpCo value falls from €355.0m to €305.0m; first-lien recovery falls from 100.0% to 95.3% and note recovery falls to zero.

Table 32.16 — Structure sensitivity

Change from Upper case	Distributable OpCo value €m	First-lien recovery	Notes recovery	Teaching point
None	355.0	100.0%	23.3%	Base selected waterfall
€50m value outside selected claim perimeter	305.0	95.3%	0.0%	Entity location matters
Costs increase from €10m to €20m	345.0	100.0%	16.7%	Costs absorb junior recovery first
Enterprise value falls to €250m	255.0	79.7%	0.0%	Price is not par recovery

32.9.1 Constructing recovery without double counting

The recovery build starts from one valuation perimeter. Asteron's operating enterprise value is assigned once to the OpCo group. Cash is then added once and costs deducted once. The model does not value the operating business, add the same subsidiaries separately and then add their cash flows again. It also does not give HoldCo notes a second claim on value already distributed to the first-lien class.

Enterprise value is not a recovery fact. It is a sensitivity driven by sustainable earnings, the selected valuation method, required investment, market conditions and the time needed to realise value. The Low-to-Upper range should be challenged with an earnings bridge. If the business requires €25.0m of annual capex to sustain €50.0m of EBITDA, a multiple based on a low-capex peer can overstate value. If restructuring costs continue, they may reduce distributable value or sustainable earnings. The recovery table keeps the range explicit rather than selecting the value that repays par.

Entity allocation comes next. Consolidated EBITDA does not identify where value sits or which creditor can reach it. A real model needs legal entities, ownership, debtors, guarantors, collateral, cash, intercompany claims and local obligations. The €50.0m outside-perimeter sensitivity demonstrates the economic consequence without asserting why value is outside or whether it can move. The legal result depends on actual documents, corporate and insolvency law, and facts.

Claims must be measured on one date. Principal, accrued interest, hedging, letters of credit, administrative claims, employee obligations, taxes and costs can change the denominator. Asteron's selected first-lien claim is only TLB plus RCF at Q8. That simplification makes the arithmetic reproducible, but a real claim schedule would require evidence and specialist review. Omitting a claim can overstate every junior recovery.

Costs should be sensitised because they sit ahead of the residual in this teaching waterfall. Increasing costs from €10.0m to €20.0m leaves first lien whole in the Upper case but reduces note recovery from 23.3% to 16.7%. At lower enterprise values, costs reduce first-lien recovery directly. Timing matters too: a longer process can create professional fees, operating losses and new-money claims while value deteriorates.

Finally, compare recovery with price only after definitions and dates align. A loan trading at 80 is not evidence of 80% recovery; the price reflects time, liquidity, optionality, risk appetite and competing scenarios. A 79.7% Mid-case first-lien recovery is likewise not a price target. It is one output under one value, cash, cost and claim set. Chapter 26 develops the distinction between price and recovery.

32.10 Reconciliations and checks

The case is answer-checkable without a workbook. The following controls cover operating, cash, debt, covenant and recovery logic.

Table 32.17 — Reconciliation register

#	Check	Recalculation	Result
1	Year 0 EBITDA margin	$75.0 / 500.0$	15.0%
2	Opening net debt	$300.0 + 150.0 - 25.0$	€425.0m
3	Opening net leverage	$425.0 / 75.0$	5.67x
4	Base Y2 revenue	525.0×1.05	€551.25m
5	Base Y2 EBITDA	$551.25 \times 16.0\%$	€88.20m
6	Base Y1 FCF	$81.375 - 31.17 - 8.61 - 23.625 - 0.50$	€17.47m
7	Base Y1 ending cash	$25.0 + 17.47 - 3.0 - 7.23$	€32.23m
8	Severe annual Y2 RCF required	Prior RCF plus cash deficit	€26.48m
9	Q2 RCF draw	$15.0 - 11.98$	€3.02m
10	Q4 Year 1 ending RCF	$5.11 - 4.40$	€0.72m
11	Q6 LTM EBITDA	$12.60 + 11.55 + 9.00 + 9.90$	€43.05m
12	Q6 senior-secured net debt	$295.50 + 23.01 - 15.00$	€303.51m
13	Q6 springing leverage	$303.51 / 43.05$	7.05x
14	Q6 covenant shortfall	$5.50 \times 43.05 - 303.51$	(€66.73m)
15	Q8 remaining availability	$50.00 - 26.02$	€23.98m
16	Mid first-lien recovery	$255.0 / 320.02$	79.7%
17	Upper note recovery	$34.98 / 150.0$	23.3%
18	Value conservation	First-lien recovery + note recovery	Equals distributable value

Additional controls require annual revenue to equal the sum of its quarters, ending cash to equal opening cash plus cash flow plus financing, each debt balance to roll from opening to ending, revolver never to exceed €50.0m without a recorded deficit, covenant tests to activate only after the selected trigger, LTM EBITDA to use four contiguous quarters, and recovery distributions never to exceed distributable value.

32.11 Committee analysis

Table 32.18 — Credit scorecard

Dimension	Base	Downside	Severe	Committee interpretation
Revenue / margin	Growth and expansion	Slow recovery	Two-year contraction and margin shock	Evidence must focus on aftermarket resilience and project deferral
Cash flow	Positive and rising	Positive but thin	Negative through Year 5	Severe path needs new liquidity or action
Liquidity	No RCF	No RCF	Q2 first draw; €26.0m at Q8	Q10 exhaustion under continued-burn sensitivity
Covenant	Comfortable trend	Total leverage near 6x	Springing test activates and fails Q6	Document analysis and remedy timing are critical
First-lien recovery	Not stressed	Not stressed	64%–100% sensitivity	Value and entity perimeter drive outcome
Notes recovery	Equity-like tail	Vulnerable	0% in three of four values	Structural position dominates

The teaching recommendation is **do not approve on the Base case alone**. The case needs a credible evidence-backed response to three breakpoints: Q6 covenant activation, the Q10 continued-burn liquidity date and the recovery dependence on value remaining inside the OpCo claim perimeter. A real decision would also require current management evidence, documents, legal review, tax and accounting analysis, pricing and relative value. None is supplied here.

The monitor list should be causal. Monthly aftermarket renewals test recurring demand. Project backlog conversion tests revenue timing. Gross margin and labour productivity test the margin bridge. Receivables ageing and inventory test working-capital cash. Capex commitments test cash flexibility. Cash by entity and RCF availability test liquidity. The guarantee, collateral and intercreditor package tests recovery perimeter. A watch item without a decision threshold is merely a data request.

32.11.1 Decision alternatives and action clock

A committee should compare alternatives at the same date and under the same data. **Approve unchanged** would rely on the Base case and accept the Severe breakpoints; the case evidence does not support that outcome. **Approve with less debt or more equity** could improve leverage, interest and liquidity, but the amount must be modelled and committed. **Approve with structural protections** could improve monitoring or recovery, but their legal effect must be documented and reviewed. **Defer for evidence** preserves optionality but may lose transaction access. **Decline** avoids exposure but also gives up any risk-adjusted return. The model does not choose by itself; it makes the trade-offs visible.

Suppose the proposed structure adds €25.0m of sponsor equity and reduces opening TLB by the same amount. Opening net debt falls from €425.0m to €400.0m and leverage from 5.67x to 5.33x. Annual cash interest falls before any change in operating performance. In Q6, term debt would also be approximately €25.0m lower, reducing the covenant shortfall but not eliminating the €66.73m gap. The committee should therefore avoid describing €25.0m as a complete cure. It is one mitigation whose effect can be measured.

An action clock begins before Q6. Q1 monitoring should validate the revenue and working-capital assumptions. The first Q2 draw shows that cash conversion is weaker than the minimum-cash requirement. Q3 peak usage tests whether the Q4 release is credible. Q4 repayment provides temporary relief but should not reset concern because Year 2 starts with lower margin and restructuring costs. By Q5, economic leverage is 6.41x even though the springing test is dormant. That is the last full quarter before the selected Q6 trigger.

Each monitor needs a threshold and response. If aftermarket renewal falls below the underwritten level, move revenue to the Severe path. If receivables ageing consumes an additional €5.0m, reduce availability and

recalculate the trigger date. If Q5 ending RCF exceeds €17.5m, activate the selected covenant test immediately. If remaining availability falls below the next two quarters' projected burn plus a contingency, begin a financing or amendment plan rather than waiting for exhaustion. If value migrates outside the selected first-lien perimeter, rerun recovery by entity.

The recommendation should record what would change it. Evidence of stronger contract retention, earlier margin recovery and sustainable working-capital release could support the Downside rather than Severe path. A committed equity contribution or larger facility could extend runway, subject to terms and availability. Conversely, repeated "one-time" cash costs, lower accessible cash, reduced revolver availability or unsupported EBITDA adjustments would worsen the conclusion. A decision with no falsification conditions cannot be monitored.

The final committee output should fit on one controlled page: recommendation; current version and hash; Base, Downside and Severe leverage and liquidity; first breakpoint and date; recovery range by claim; top evidence gaps; required protections; and next decision thresholds. Append the model and evidence register, but do not force the decision-maker to discover the conclusion among tables.

32.12 Questions

Table 32.19 — Advanced practitioner questions

#	Question
1	Recalculate Base Year 3 revenue from Base Year 2.
2	Recalculate Base Year 2 EBITDA and margin.
3	Reconcile Base Year 1 FCF before debt service.
4	Identify the first quarter with a revolver draw and calculate the draw.
5	Identify the first quarter in which the springing covenant applies. Explain why it did not apply in Q5.
6	Calculate Q6 senior - secured net leverage and debt headroom or shortfall.
7	Calculate Q8 remaining revolver availability.
8	Calculate Mid - case first - lien and note recoveries.
9	Calculate Upper - case note recovery.
10	If Q9 and Q10 require €12m and €15m of additional draw, identify the liquidity breakpoint and deficit.

Appendix 32A — Input register

Table 32.20 — Inputs by type

Type	Inputs
Synthetic facts	Year 0 revenue, EBITDA, capex, debt and cash; business mix
Base assumptions	5% growth, margin path, 4.5% capex, 2% incremental-revenue NWC
Downside assumptions	Growth and margin path; Y2–Y3 restructuring cost
Severe assumptions	Revenue contraction, margin path, 5% capex, explicit NWC and restructuring cash
Selected terms	Rates, amortisation, RCF commitment, trigger and covenant formula
Recovery assumptions	Q8 date, value range, €10m costs, selected entity and claim perimeter
Open evidence	Customer, backlog, margin, capex, NWC, cash access, documents and value support

Appendix 32B — Formula register

Table 32.21 — Core calculations

Output	Formula
Revenue	Prior period revenue $\times$ (1 + growth) or explicit quarterly input
EBITDA	Revenue $\times$ EBITDA margin
Depreciation	3.0% $\times$ revenue
Cash tax	25% $\times$ max(0, EBITDA – depreciation – cash interest)
FCF before debt	EBITDA – interest – tax – capex – Δ NWC – restructuring cash
Ending cash	Opening cash + FCF – amortisation – sweep + RCF draw – repayment
Net debt	TLB + notes + RCF – cash
Total net leverage	Net debt / EBITDA
Springing leverage	(TLB + RCF – cash) / LTM EBITDA when trigger applies
Covenant headroom	5.50 $\times$ LTM EBITDA – senior-secured net debt
Distributable value	Enterprise value + cash – selected costs
First-lien recovery	min(first-lien claim, distributable value)
Notes recovery	min(notes claim, max(0, value after first lien))

Appendix 32C — Sensitivity and control notes

The Base, Downside and Severe cases are internally coherent paths, not probability-weighted outcomes. The quarterly bridge is one selected seasonality pattern. Recovery values are sensitivities, not appraisals. RCF availability assumes no letters of credit, ancillary use, borrowing-base limit or draw-condition failure. Covenant EBITDA contains no add-backs. Cash is fully nettable in the selected formula. Actual documents may produce different definitions and consequences.

No accounting framework is asserted. Depreciation and tax are teaching formulas. No tax deduction, legal remedy, perfection, priority, guarantee validity, cash upstreaming or covenant cure is concluded. Those questions must be handled by the relevant qualified specialist using the operative facts, documents, jurisdiction and date.

Appendix 32D — Answer key

Table 32.22 — Answers

#	Answer
1	$€551.25m \times 1.05 = €578.81m$.
2	$€551.25m \times 16.0\% = €88.20m$; margin is 16.0% by construction.
3	$81.375 - 31.17 - 8.61 - 23.625 - 0.50 = €17.47m$ after rounding.
4	Q2; cash before financing is €11.98m, so draw is $15.00 - 11.98 = €3.02m$.
5	Q6; draw is €23.01m, above €17.50m. Q5 draw of €12.44m is only 24.9% of commitment, so the selected test is not active.
6	Senior net debt is $295.50 + 23.01 - 15.00 = €303.51m$; leverage is $303.51 / 43.05 = 7.05x$; shortfall is approximately $236.78 - 303.51 = €66.73m$ using unrounded balances.
7	$50.00 - 26.02 = €23.98m$.
8	First lien receives $255.0 / 320.02 = 79.7\%$; no value remains, so notes recover 0.0%.
9	Residual is $355.0 - 320.02 = €34.98m$; notes recover $34.98 / 150.0 = 23.3\%$.
10	Q9 leaves $23.98 - 12.00 = €11.98m$; Q10 needs €15.0m, so availability is exhausted during Q10 and deficit is €3.02m.

Appendix 32E — Release boundary

This case is an educational decision exercise, not a live approval, valuation, rating, legal opinion or investment recommendation. Its completeness means that every displayed result can be reproduced from displayed inputs. It does not mean the assumptions are appropriate for any real company.

Any edit changes the exact chapter hash and invalidates downstream bindings. A credit specialist and modelling specialist should validate the exact final text and calculations. Counsel must review any retained synthetic covenant, guarantee, security or priority language within its stated jurisdictional scope. The final manuscript must be rebuilt, rehashed and pass publication controls before any release decision.

Landmark Transactions — What the Public Record Shows

33.1 How to use transaction case studies

A transaction case study is useful only if it keeps three layers separate.

The first layer is the **documented fact**: who acted, when, through which entity, for what disclosed consideration, under which agreement or court process. The second is the **documented mechanism**: the financing instrument, voting threshold, contractual exception, restructuring tool or change of control that the primary record actually describes. The third is the **credit inference**: what an analyst can learn about leverage, priority, liquidity, documentation or execution risk.

The first two layers should be sourced. The third must be labelled as analysis. A filing can establish the consideration paid; it does not, without more, establish a sponsor's realised return. A judgment can decide the meaning of a particular agreement; it does not automatically rewrite every agreement governed by the same law. A company release can report completion of a restructuring; it does not prove that every creditor received the value later attributed to it by market commentary.

This chapter applies that discipline to five transactions using the public primary sources cited in each section: Alliance Boots, Hertz, Adler, Casino and Serta Simmons Bedding. Each section distinguishes what the record supports from what remains inference or is not established.

33.2 Alliance Boots: control changed in stages

The documented sequence

In 2007, KKR and Stefano Pessina used AB Acquisitions Limited to acquire joint control of Alliance Boots through a public bid. That identity and structure are recorded in the European Commission's merger decision. The record does not support describing the 2007 buyers as Clayton, Dubilier & Rice and Merrill Lynch Global Private Equity. European Commission, Case M.4674 — KKR / Stefano Pessina / Alliance Boots (18 June 2007) (<https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX%3A32007M4674>)

The later combination with Walgreens was a separate, staged transaction. In June 2012, Walgreens announced an initial investment of approximately \$6.7 billion for 45% of Alliance Boots, consisting of \$4.0 billion in cash and 83.4 million Walgreens shares. The agreement also gave Walgreens an option to acquire the remaining 55%. The release said Walgreens planned to finance the initial cash payment with existing cash and new borrowings and had received commitments for a \$3.5 billion bridge facility. These were announced terms and financing intentions at that date, not a retrospective statement of realised economics. Walgreen Co. SEC-filed joint release (19 June 2012) (<https://www.sec.gov/Archives/edgar/data/104207/000119312512274469/d369203dex992.htm>)

Walgreens completed the first step on 2 August 2012. On 31 December 2014, the reorganised Walgreens Boots Alliance completed the second step and acquired the remaining 55% for £3.133 billion in cash and 144.3 million shares. Those completion facts appear in the company's 2015 Form 10-K. Walgreens Boots Alliance 2015 Form 10-K (<https://www.sec.gov/Archives/edgar/data/1618921/000114036115038791/form10k.htm>)

The credit lesson

The useful lesson is not that a familiar asset necessarily produces a particular sponsor return. It is that the analyst must reconstruct **which transaction** is being analysed. The 2007 take-private, the 2012 minority investment and the 2014 completion were distinct steps with different buyers, consideration and financing consequences.

A credit review should therefore answer four questions before calculating leverage or returns:

- ♦ Is the model measuring the 2007 acquisition, the 2012 first step, the 2014 second step, or the combined ownership period?
- ♦ Is the stated consideration equity value, cash paid, stock issued, enterprise value, debt assumed, or some combination?
- ♦ Which liabilities remained at the operating group, and which were refinanced or introduced at each step?
- ♦ Does the analysis use contemporaneous information, or does it import later outcomes into an earlier underwriting case?

The public records cited here establish ownership and consideration facts. They do not by themselves establish the opening and closing debt stack, cash leakage, dividends, fees, covenant capacity or investor-level cash flows required for a return calculation. Any such calculation belongs in a separate, fully sourced schedule.

33.3 Hertz: reconstruct sources and uses before telling the story

The documented transaction

On 21 December 2005, investment funds associated with Clayton, Dubilier & Rice, The Carlyle Group and Merrill Lynch Global Private Equity acquired all of Hertz's common stock from a Ford subsidiary. Hertz later reported \$4.379 billion of cash consideration, \$10.116 billion of debt refinanced or assumed, and \$447 million of transaction fees and expenses. It also reported \$2.295 billion of sponsor equity contributions. The transaction was a whole-company acquisition; it should not be described as a 2006 acquisition of a European Hertz carve-out. Hertz 2007 Form 10-K (<https://www.sec.gov/Archives/edgar/data/47129/000104746908002304/a2183325z10-k.htm>)

The same filing identifies part of the acquisition financing: \$1.8 billion of 8.875% senior dollar notes, \$600 million of 10.5% senior subordinated notes and €225 million of 7.875% senior euro notes. It also describes other facilities and fleet-related financing. Those disclosures matter because a vehicle-rental business can have both corporate acquisition debt and financing associated with revenue-earning equipment. Combining every liability into one undifferentiated leverage number can obscure economic and structural differences.

The credit lesson

Hertz is a useful sources-and-uses case because the filing separates several amounts that are often collapsed in a narrative:

- ♦ cash paid for the shares;
- ♦ debt refinanced or assumed;
- ♦ transaction fees and expenses;
- ♦ sponsor equity; and
- ♦ specific debt instruments used in the transaction.

The first analytical control is a reconciliation. Total funding sources should explain cash consideration, refinancing needs, fees and any required cash balance. The second is classification. Corporate debt, fleet financing, asset-backed facilities, operating liabilities and off-balance-sheet commitments may have different recourse, collateral, amortisation and cash-flow characteristics. The third is currency. A structure containing dollar and euro notes

introduces translation, hedging and cash-generation questions that a single reported leverage ratio does not answer.

The filing is a reliable source for the transaction amounts it reports. It does not justify a general claim that leverage of this scale is sustainable, that an IPO or refinancing was certain, or that a particular debt tranche was attractive. Those are separate conclusions requiring dated forecasts, instrument terms and market prices.

33.4 Adler: a statutory threshold is not the end of the court's analysis

The documented proceeding

The Adler case arose from a restructuring plan under Part 26A of the Companies Act 2006 involving six classes of senior unsecured notes. The High Court sanctioned the plan in 2023. The Court of Appeal's January 2024 judgment describes itself as the first appeal to that court concerning a Part 26A restructuring plan and addresses the use of cross-class cram-down where not every class has approved the plan by the required majority. Court of Appeal, *AGPS Bondco plc (Adler)*, [2024] EWCA Civ 24 (<https://www.judiciary.uk/wp-content/uploads/2024/01/Adler-Approved-Judgment-for-circulation.pdf>)

For cross-class cram-down, the judgment explains two statutory preconditions. In simplified terms, the dissenting class must be no worse off under the plan than in the relevant alternative, and an in-the-money class must approve the plan by the required 75% in value of those present and voting. The Court of Appeal emphasised that satisfying those conditions does not create a presumption that the court should sanction the plan. The court must still exercise its discretion in light of the circumstances.

The judgment also distinguishes a vertical comparison from a horizontal comparison. The vertical comparison asks how a class fares under the plan relative to the most likely alternative. The horizontal comparison considers the treatment of different classes under the plan, including whether differences are justified. That distinction matters because a plan can clear the statutory floor for a dissenting class while still raising a separate question about how restructuring benefits are allocated.

The credit lesson

The case supports a disciplined three-stage review of a Part 26A proposal:

- ♦ **Relevant alternative:** identify what is most likely to happen if the plan is not sanctioned and test the evidence supporting that counterfactual.
- ♦ **Statutory conditions:** test no-worse-off and the approving in-the-money class using the actual rights and valuation evidence.
- ♦ **Discretion and fairness:** examine class treatment, differences in priority or maturity, allocation of restructuring benefits, and the reasons advanced for differential treatment.

This is more rigorous than saying that a 75% vote automatically binds everyone or that no-worse-off automatically compels sanction. It is also more precise than treating Adler as a scheme of arrangement under Part 26 or as a German StaRUG proceeding. The teaching point is tied to the judgment and the statutory process it considered.

The judgment is a primary legal source, but this chapter is not a substitute for advice on another plan. Class constitution, governing documents, jurisdiction, valuation evidence and the relevant alternative can differ materially. Qualified counsel must approve any statement that applies the decision beyond its facts.

33.5 Casino: use the actual French process and dates

The documented restructuring

Casino's public restructuring archive identifies an accelerated-safeguard process in France, including materials for classes of affected parties and a 26 February 2024 announcement that the court had approved the proposed accelerated-safeguard plans. The archive provides the relevant company releases and process documents rather than a generic label such as "European cram-down." Groupe Casino financial-restructuring archive (<https://www.groupe-casino.fr/en/investors/financial-restructuring/>)

Casino later reported that the transactions contemplated by the plans approved by the Paris Commercial Court on 26 February 2024 were implemented on 27 March 2024. The company said the implementation changed control in favour of France Retail Holdings S.à r.l., ultimately controlled by Daniel Křetínský. Groupe Casino completion release (<https://www.groupe-casino.fr/realisation-effective-de-la-restructuration-financiere-du-groupe-casino/>)

Those dates and that process displace a narrative that places the restructuring in 2020-2022 or treats it as an undefined liability-management exercise without a European restructuring tool. The precise legal consequences, creditor recoveries and class treatment must be derived from the approved plans, judgments and transaction documents, not inferred from the completion headline.

The credit lesson

Casino illustrates why a restructuring timeline should be built from dated primary documents. A robust timeline identifies at least:

- ♦ the opening of the process and the entities covered;
- ♦ the perimeter of affected and unaffected claims;
- ♦ the formation and voting of affected-party classes;
- ♦ court approval;
- ♦ conditions to effectiveness;
- ♦ capital, debt and ownership changes at implementation; and
- ♦ the post-implementation maturity, liquidity and governance profile.

The company archive establishes a process and completion sequence. It does not, standing alone, prove the value received by each creditor or the later performance of the reorganised business. Those questions require the plan terms, instrument-level treatment and post-restructuring financial information.

For a leveraged-finance analyst, the practical lesson is to avoid jurisdiction-free vocabulary. "Cram-down," "safeguard," "scheme," "plan" and "exchange" are not interchangeable. The governing procedure determines who votes, how classes are formed, what conditions apply, what the court decides and when the transaction becomes effective.

33.6 Serta Simmons Bedding: defined terms can decide the transaction

The documented dispute

Serta Simmons Bedding's 2016 financing included first-lien and second-lien syndicated loans. The first-lien agreement contained pro-rata-sharing provisions and an exception that permitted specified non-pro-rata transactions, including Dutch auctions and "open market purchases." In 2020, Serta and participating lenders completed an uptier transaction. The participating lenders provided \$200 million of new financing in exchange for first-out super-priority debt and exchanged approximately \$1.2 billion of existing loans for approximately \$875 million of second-out super-priority debt. Other lenders did not participate. These facts and the relevant

agreement provisions are described in the Fifth Circuit's opinion. Fifth Circuit, *In re Serta Simmons Bedding*, revised 14 February 2025 (<https://www.ca5.uscourts.gov/opinions/pub/23/23-20451-CV0.pdf>)

The litigation later reached the Fifth Circuit through Serta's Chapter 11 proceedings. On the contractual issue, the court concluded that an open-market purchase under the agreement referred to a purchase on the relevant secondary market for the loans. Because the 2020 transaction was privately negotiated outside that market, the court held that it did not receive the protection of the agreement's open-market-purchase exception. The opinion also addresses separate bankruptcy-plan issues; those holdings should not be compressed into a single slogan about uptiers.

The credit lesson

Serta demonstrates the importance of an exact documentary chain:

- ♦ identify the pro-rata-sharing rule;
- ♦ identify the protected or “sacred” right and the amendment threshold;
- ♦ identify each exception to pro-rata treatment;
- ♦ reconstruct the amendments and transfers that implemented the transaction;
- ♦ identify participating and excluded lenders by instrument and class;
- ♦ follow the court's construction of the actual defined and undefined terms; and
- ♦ separate the contract holding from later confirmation, indemnity and equal-treatment issues in bankruptcy.

The case should not be described as an accounting gain-on-extinguishment transaction, and the public record cited here does not establish that Congress or a state legislature responded by banning uptiers. Nor does the opinion create a universal rule that every non-pro-rata exchange is invalid. It interprets a particular agreement and resolves issues presented in the associated bankruptcy appeals.

For underwriting, the forward-looking question is not whether a document contains a familiar label. It is whether the operative provisions, amendment thresholds, transfer mechanics and exceptions work together in the way the proposed transaction assumes. A label supplied by the parties cannot substitute for that analysis.

33.7 Comparative map

Alliance Boots

Primary mechanism in this chapter: 2007 public-bid take-private followed by a 2012/2014 staged strategic combination

What the public record establishes: Buyer identities, ownership percentages, announced/completed consideration and staged control

What this chapter does not claim: Sponsor return, full debt history, covenant capacity or investment attractiveness

Hertz

Primary mechanism in this chapter: 2005 whole-company sponsor acquisition

What the public record establishes: Sponsors, transaction date, cash consideration, debt refinanced/assumed, fees, sponsor equity and disclosed note financing

What this chapter does not claim: That all liabilities have identical recourse; sustainability or an investment conclusion

Adler

Primary mechanism in this chapter: UK Part 26A restructuring plan and appeal

What the public record establishes: Six note classes, statutory conditions, cross-class cram-down framework and continuing sanction discretion

What this chapter does not claim: Advice on another plan or a jurisdiction-independent cram-down rule

Casino

Primary mechanism in this chapter: French accelerated safeguard

What the public record establishes: Company-reported process archive, court-approval date, implementation date and control change

What this chapter does not claim: Instrument-level recoveries or post-restructuring performance

Serta

Primary mechanism in this chapter: 2020 uptier and subsequent Fifth Circuit appeal

What the public record establishes: Agreement structure, transaction mechanics and court construction of "open market purchase," plus distinct bankruptcy holdings

What this chapter does not claim: A universal prohibition on non-pro-rata exchanges or a legislative reform claim

33.8 A repeatable primary-source case method

For any future case, build the file in this order:

Step 1 — Define the event

Write one sentence specifying the entity, transaction or proceeding, date range, jurisdiction and analytical question. If the sentence combines two transactions, split the case.

Step 2 — Establish an identity and chronology table

Record legal entity names, sponsors, issuer/borrower, key agreements, court or regulator, announcement, signing, approval and completion dates. Resolve conflicting names before writing prose.

Step 3 — Reconstruct cash, debt and control

Separate equity value, enterprise value, cash consideration, stock consideration, assumed or refinanced debt, fees, new-money debt, exchanged debt and sponsor equity. Reconcile what can be reconciled and label what cannot.

Step 4 — Read the operative text

For a financing, use the actual credit agreement, indenture, offering document or filing. For a restructuring, use the statute, plan, explanatory statement and judgment. For a corporate transaction, use the merger filing, issuer filing and completion release. A summary is a discovery aid, not the authority.

Step 5 — Separate fact from inference

Mark every sentence as documented fact, management statement, court holding, assumption, calculation or analyst judgment. Forward-looking statements remain forward-looking; they do not become facts because the

transaction later completed.

Step 6 — State the boundary

End each case with what the sources do not establish. This prevents a reader from treating an illustrative lesson as a verified return, legal opinion or recommendation.

33.9 Closing perspective

The common lesson across these transactions is source discipline. Alliance Boots shows why ownership stages must not be collapsed. Hertz shows why purchase consideration, refinanced debt, fees and financing instruments must be reconciled separately. Adler shows that a statutory threshold is only one part of a court-supervised restructuring analysis. Casino shows why the actual jurisdiction and process dates matter. Serta shows how the construction of a few words in a particular agreement can determine whether a transaction fits an exception.

The cases are not templates that mechanically predict the next deal. They are demonstrations of a method: identify the entity, reconstruct the chronology, read the operative document, reconcile the numbers, distinguish holding from inference, and state what remains unknown. That method is durable even when structures, markets and laws change.

Chapter source list

- ✦ European Commission, Case M.4674 — KKR / Stefano Pessina / Alliance Boots (18 June 2007) (<https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX%3A32007M4674>)
- ✦ Walgreen Co. SEC-filed joint release (19 June 2012) (<https://www.sec.gov/Archives/edgar/data/104207/000119312512274469/d369203dex992.htm>)
- ✦ Walgreens Boots Alliance 2015 Form 10-K (<https://www.sec.gov/Archives/edgar/data/1618921/000114036115038791/form10k.htm>)
- ✦ Hertz 2007 Form 10-K (<https://www.sec.gov/Archives/edgar/data/47129/000104746908002304/a2183325z10-k.htm>)
- ✦ Court of Appeal, *AGPS Bondco plc (Adler)*, [2024] EWCA Civ 24 (<https://www.judiciary.uk/wp-content/uploads/2024/01/Adler-Approved-Judgment-for-circulation.pdf>)
- ✦ Groupe Casino financial-restructuring archive (<https://www.groupe-casino.fr/en/investors/financial-restructuring/>)
- ✦ Groupe Casino completion release (<https://www.groupe-casino.fr/realisation-effective-de-la-restructuration-financiere-du-groupe-casino/>)
- ✦ Fifth Circuit, *In re Serta Simmons Bedding*, revised 14 February 2025 (<https://www.ca5.uscourts.gov/opinions/pub/23/23-20451-CV0.pdf>)

CONTINGENT RIGHTS AND TEACHING SENSITIVITIES

- 34 From a Quoted Spread to a Teaching Reconciliation
- 35 A Guarded Taxonomy of Contingent Rights
- 36 Building and Validating Teaching Sensitivities
- 37 Designing a Fictional Teaching Estimate

The earlier Parts of this book explain instruments, covenant architecture and distress. This Part adds a narrower analytical lens: selected contractual rights can sometimes be represented as contingent-payoff analogies after the operative drafting has been mapped. The analogy is a way to organise questions and sensitivities. It is not the contract, a legal conclusion, a market price or an investment recommendation.

Every live-document application must begin with the agreement, identify the relevant entities and conditions, and receive qualified legal review. The numerical framework in this Part is deliberately limited to synthetic teaching inputs and design requirements. It does not rely on a private model or claim that an unperformed calculation has been run.

From a Quoted Spread to a Teaching Reconciliation

34.1 A quoted spread is an observation, not an itemised bill

A loan margin, bond yield or price is an observable market term at a particular time. It is not a receipt showing the amount paid for each covenant, risk factor or contractual permission. The observed term can reflect expected credit loss, uncertainty around that loss, liquidity, funding conditions, risk appetite, technical supply and demand, call protection, documentation, taxes and other instrument-specific features. The relative importance of those factors changes across instruments and dates.

This distinction matters because a neat decomposition can create false confidence. An analyst may be able to define teaching components, but the existence of labels does not prove that the components are separately priced or additive. If two components respond to the same state variable, adding them can count the same economic effect twice. If the baseline is not calibrated to an observed instrument, the unexplained remainder is a model residual rather than evidence that the market is wrong.

The safe objective is therefore a teaching reconciliation. Begin with an explicit baseline, test selected features under consistent assumptions, and retain any difference as unexplained. Do not call the difference fair value, compensation, cheapness, richness or mispricing unless a separate calibrated-price framework has passed its evidence and review gates.

34.2 Map the legal right before choosing an analogy

A credit agreement creates rights, obligations, permissions, conditions and remedies. Some may support contingent-payoff analogies; others may not. The mapping starts with the legal object rather than an option label.

For each feature, record the obligor or holder, the permitted or required action, the trigger, testing time, conditions, blockers, consent threshold, exceptions, reclassification rules, duration and consequence. Then check interactions with definitions and other covenant families. A debt-incurrence permission, for example, may depend on a ratio, available capacity, permitted-debt category, lien permission, restricted-subsidiary status, pro forma calculations and reclassification mechanics. Calling it a call option before completing that map hides the analysis that matters.

Only after the rights map is complete should the analyst ask whether an option-like analogy improves understanding. A permission that can be exercised only in specified states may resemble a contingent right. A springing test may resemble a barrier. A sunset may resemble an expiry. These are teaching comparisons. They do not alter who may act, when the clause applies, or what the governing law permits.

34.3 A disciplined component record

Each teaching component should have a standard record:

- ✦ Legal object: the actual clause, defined terms and affected entities.
- ✦ State variable: the financial, operational or transactional condition used in the teaching model.
- ✦ Exercise rule: who can act and under which contractual assumptions.
- ✦ Baseline: the counterfactual against which the sensitivity is measured.
- ✦ Horizon: the dates over which the comparison is made.
- ✦ Cash-flow mapping: how the assumed state changes cash flow, priority, timing or recovery in the model.

- ♦ Dependency map: other features that respond to the same states or cash flows.
- ♦ Output unit: currency value, capacity, probability under the stated measure, or a spread-equivalent teaching unit.
- ♦ Evidence status: qualitative taxonomy, synthetic sensitivity, calibrated estimate, or unresolved.
- ♦ Limitations: assumptions that could reverse or invalidate the result.

The record prevents an analyst from moving directly from a colourful clause description to a precise-looking number. It also lets a reviewer challenge the legal state separately from the model mechanics.

34.4 Same issuer, different documents: a synthetic comparison

Consider two entirely fictional facilities issued by the same synthetic borrower on the same date. Facility A permits less incremental debt, uses a leverage-gated restricted-payment construct and preserves a change-of-control put unless a tighter portability test is satisfied. Facility B permits more incremental debt, allows a broader restricted-payment pathway and uses a looser portability test. Assume for the exercise that the operating forecast, opening leverage, maturity, base rate, margin and recovery convention are otherwise identical.

The documents are not interchangeable merely because the quoted margins match. Facility B can expose the lender to different future states under the synthetic assumptions. That conclusion is qualitative until the clauses, borrower actions, state dynamics and payoff consequences have been modelled. It does not establish how many basis points separate the facilities or where either should trade.

The practitioner output is a transparent difference map: which states are reachable, what action becomes available, what cash flow or priority changes in the teaching model, and which assumptions drive the result. That output can improve diligence even when no defensible price is available.

34.5 Rules for a teaching reconciliation

Use one sign convention and one baseline throughout. Recalculate each component with all unrelated assumptions held constant. Where interactions are material, calculate the combined effect as well as the standalone effects and show the overlap explicitly. Do not force the components to sum to the observed spread.

If a currency present-value sensitivity is translated into a spread-equivalent teaching unit, disclose the denominator and units. A RiskyPV01 or duration-based conversion can translate an assumed value change, but it cannot validate the numerator. The converted figure remains a teaching sensitivity unless the legal state, cash flows, market inputs, calibration instruments and model diagnostics have been independently validated.

The end product should make uncertainty more visible, not less. A range with clear assumptions is more useful than a single number whose precision cannot be defended.

34.6 Chapter boundary

This chapter establishes a disciplined reconciliation framework. It does not assert that every contractual permission is an option, that spread must equal a sum of clause values, or that a lender is paid an itemised amount for each feature. Chapter 35 develops a guarded taxonomy; Chapter 36 specifies how synthetic sensitivities may be built; Chapter 37 defines a fictional implementation workflow without claiming a completed run.

A Guarded Taxonomy of Contingent Rights

35.1 The structural-model starting point

Merton's 1974 structural model represents a stylised firm's equity at a single horizon with the payoff $\max(V - D, 0)$, where V is firm value at that horizon and D is the promised debt payment. Under the model's assumptions, risky debt can be represented as riskless debt less a put-like default component. This is a model identity, not a legal description of limited liability, enforcement or insolvency. Merton, "On the Pricing of Corporate Debt" (1974) (<https://doi.org/10.1111/j.1540-6261.1974.tb03058.x>)

The Black-Scholes framework supplies related contingent-claim mathematics under restrictive assumptions about trading, volatility, rates and exercise. Those assumptions must be stated before the formula is used. A familiar equation does not make a real credit agreement complete or tradable as a derivative. Black and Scholes, "The Pricing of Options and Corporate Liabilities" (1973) (<https://doi.org/10.1086/260062>)

Real leveraged credits can default before maturity, contain several debt layers, include guarantees and collateral across entities, and move discontinuously after operational or legal events. Structural models can be extended with barriers, multiple claims or jump processes, but each extension introduces new assumptions and model risk. The model should be chosen because it fits the teaching question, not because its output looks sophisticated.

35.2 The rights-first template

Every analogy in this chapter follows the same order.

First identify the legal object. Quote or summarise the operative provision only within the applicable rights and quotation limits. Record the defined terms and affected entities.

Second identify the trigger and decision-maker. State who may act, what must be true, what calculation date applies, which consent is needed and which blockers or exceptions qualify the right.

Third state the analogy. Explain why a call-, put-, barrier-, extension- or exchange-like comparison may help organise the payoff or timing.

Fourth disclose assumptions. These include the state variable, horizon, exercise behaviour, cash-flow mapping, recovery and waterfall, information set and enforceability assumption.

Fifth state the failure modes. The clause may interact with another covenant, the assumed action may be irrational, a consent may be unavailable, the legal interpretation may differ, or the model may omit an important state.

Finally label the evidence status. A qualitative analogy is not a numerical value. A synthetic sensitivity is not a calibrated market price.

35.3 Redemption and prepayment rights

Optional redemption can support a call-like analogy because the issuer may repay under specified terms. The legal and economic details remain decisive: non-call periods, make-whole formulas, fixed-call schedules, soft-call protection, equity claws, notice periods, permitted funding sources and accrued interest can produce different cash flows.

The model must use the actual synthetic dates and formula chosen for the exercise. It should not collapse several redemption mechanisms into one generic call. If the right belongs to a borrower or issuer, the exercise rule must reflect that holder's assumed incentives; automatic exercise at the most adverse time for the lender may overstate the sensitivity.

35.4 Debt, lien and restricted-payment capacity

Debt and lien covenants create conditional capacity, not a free-standing traded option. Fixed baskets, ratio baskets, incremental facilities, incremental-equivalent debt, reclassification and most-favoured-nation provisions can interact. A capacity model must track the same defined EBITDA, debt, cash netting, dates and entity perimeter used by the synthetic agreement.

Restricted-payment capacity can be fixed, leverage-gated or cumulative. A builder or available-amount construct may be path-dependent because capacity can grow and be used over time. The model must track its starting amount, additions, deductions, floors, carry rules, permitted uses and blockers. Capacity is not the same as exercise, and exercise is not automatically a loss to the lender.

35.5 Change of control, portability and asset-sale mechanics

A change-of-control put can support a put-like teaching analogy only after the triggering event, exceptions, purchase price, notice and payment mechanics are mapped. Portability may prevent or modify the trigger if specified conditions are met. The analyst must not assume that every ownership change creates a put or that every portability test extinguishes one.

Asset-sale provisions can require reinvestment, debt repayment or an offer to creditors after defined transfers and time periods. The teaching model should follow the actual synthetic sequence: gross proceeds, permitted deductions, reinvestment window, application hierarchy and any offer mechanics. The provision is not a generic lender put.

35.6 Maintenance tests, springing tests and equity cures

A maintenance covenant applies under its stated test and period. A springing covenant is tested only in the utilisation states specified by the agreement. An equity cure may permit specified proceeds or deeming to remedy a breach, subject to caps, frequency limits and other conditions.

These features can support barrier-like or contingent-remedy analogies, but the legal right comes first. A sensitivity should identify the assumed breach state, cure amount, availability and resulting cash flow. It must not describe a teaching sensitivity as the market value of a legal remedy.

35.7 Liability-management interactions

Uptier, drop-down and related liability-management structures can depend on interactions among debt, lien, investment, restricted-payment, purchase, voting, guarantee and collateral provisions. An apparent permission in one clause may be constrained elsewhere. The relevant capacity and legal outcome are document- and fact-specific.

A scenario tree can help organise borrower and creditor choices, but it cannot establish legality, availability or probability by itself. Any live transaction analysis requires the operative documents, current facts and qualified legal review. The safe teaching output is a map of assumed states and dependencies, not a prediction that a transaction can or will occur.

35.8 Documentation controls the result

Leverage ratios can be compared with strikes, springing tests with barriers and sunsets with expiries. Those comparisons remain analogies. The agreement controls the actual right, and legal interpretation precedes modelling. Chapter 36 turns only legally mapped, synthetically specified features into teaching sensitivities.

Building and Validating Teaching Sensitivities

36.1 Define the question before choosing the method

A model should answer a defined question. Closed-form methods can illustrate a simple single-horizon payoff. A lattice can represent several decision dates. Monte Carlo can represent path-dependent synthetic states. A structural model can test sensitivity to firm value, leverage, horizon and volatility. A scenario or decision tree can organise strategic choices.

None of those methods is automatically best. A closed-form formula is unsuitable for a cumulative basket with prior uses; a simulation is unnecessary if a simple deterministic bridge answers the question. Method selection is part of the evidence record and must explain why the chosen structure fits the feature.

36.2 Inputs are model-specific

Volatility can be important in a structural model, but it is not a universal master input. A hazard rate belongs to a reduced-form credit framework; default frequency in a structural model emerges from the chosen value process, leverage, barrier and horizon. Recovery depends on instrument, entity, collateral, priority and the assumed workout or insolvency state. EBITDA may drive a covenant trigger without being the economic underlying of the entire firm.

For each input, disclose definition, unit, base value, range, source class, synthetic rationale, period, scenario, owner and reviewer. Where an input is not observable, state the estimation method and uncertainty. Do not use a precise point estimate merely because the software requires one.

36.3 Standalone sensitivity and interaction effect

For a feature F, a simple teaching sensitivity can be defined as:

$\Delta PV(F) = PV \text{ with } F \text{ under stated assumptions} - PV \text{ of the baseline under the same assumptions}$

The baseline and all unrelated assumptions must remain fixed. If two features interact, calculate the combined effect:

$\text{Interaction}(F,G) = \Delta PV(F \text{ and } G) - \Delta PV(F) - \Delta PV(G)$

A non-zero interaction shows why standalone sensitivities cannot simply be added. The model should either report the interaction separately or allocate it through a disclosed rule. Hiding it inside one component makes the decomposition appear more certain than it is.

36.4 From currency sensitivity to spread-equivalent units

A currency present-value change may be translated into a spread-equivalent teaching unit using an appropriate duration or RiskyPV01 denominator. The exact sign convention, notional, currency, curve date, cash-flow dates and denominator units must be stated. The conversion answers a narrow question: what parallel spread change would produce the same modelled value change under the selected cash-flow convention?

It does not prove that the feature is priced at that spread, that the instrument should trade there, or that the market is mispricing the credit. If the numerator is an uncalibrated synthetic sensitivity, the converted output remains

uncalibrated.

36.5 Validation and reproducibility

A distributable numerical teaching example requires an immutable input catalogue, formulas or code, versioned assumptions, scenario identifiers, random seed where applicable, output map and independent validation. The reviewer should be able to reproduce every displayed value from the supplied artefact.

Validation must test arithmetic, units, sign conventions, convergence, calibration, holdout behaviour, stability under reasonable changes, dependency logic and double counting. It must also compare model outputs with simple bounds and limiting cases. A model that produces a precise output but fails a basic monotonicity or reconciliation test should fail closed.

36.6 Presentation rules

Report ranges and sensitivities before point estimates. Separate legal state, synthetic input, model assumption, calculation and analyst judgment. Use “teaching sensitivity” or “spread-equivalent teaching unit” rather than “price” unless the calibrated-price gate has been satisfied.

Do not place an uncalibrated output beside a market quote and label the difference cheapness, richness, compensation or mispricing. Do not convert a sensitivity into a recommendation. The useful output is an auditable account of which assumptions matter and where the framework is incomplete.

36.7 A practitioner validation drill

A classroom implementation can test the workflow without pretending to price a live instrument. Start with one fictional provision and write a one-page rights map. A second reviewer should be able to identify the holder, trigger, conditions, blockers, dates and consequence without reading the model. If the map is unclear, the numerical work should not begin.

Next build a baseline with the feature switched off and a comparison with it switched on. Reconcile every changed cash flow and state variable. If more than one line changes, explain the causal chain rather than reporting only the net result. Repeat the exercise at the low and high ends of every material input range.

Then pair the feature with the most likely overlapping provision. Calculate both standalone sensitivities, the combined sensitivity and the interaction term. A reviewer should challenge whether the overlap reflects genuine interaction, an inconsistent baseline or double counting. Where the result is translated into a spread-equivalent unit, repeat the reconciliation in currency and verify the denominator independently.

Finally run directional and boundary tests. A zero-capacity basket should not generate an exercise benefit. A redemption right outside its permitted dates should not affect cash flow. A recovery assumption should matter only in states where the model applies it. A model that fails these simple tests should not be rescued by calibration or more simulation paths. Record the failure, correct the mechanics and rerun the entire validation set.

The drill's deliverable is not a trade view. It is an evidence pack showing the rights map, baseline, formula lineage, input ranges, interaction analysis, checks and reviewer conclusions. That is the standard a numerical teaching example must meet before it is placed in front of a reader.

Designing a Fictional Teaching Estimate

37.1 Scope and evidence boundary

This chapter specifies a future numerical exercise for Calzada Packaging, a wholly fictional borrower. Every proposed entity, financial value, covenant term and market input would be an independently authored synthetic assumption. No model run is performed and no numerical output, price, spread, probability, ranking or recommendation is reported here.

The purpose is to define an implementation that a reader could reproduce and challenge. A future edition may include results only after the artefact, lineage and independent validation described below exist.

37.2 Synthetic input catalogue

The exercise begins with an input catalogue rather than a narrative. Each row should contain a unique input identifier, definition, unit, currency, sign, period or date, scenario, value, synthetic rationale, permitted range, owner, reviewer, version and no-real-issuer-resemblance flag.

The catalogue would cover synthetic historical income-statement, balance-sheet and cash-flow values; operating drivers; debt instruments; interest and amortisation; liquidity; taxes; covenant definitions; and the contingent-right features selected from Chapter 35. The financial statements and debt schedule must reconcile before the optionality layer is added.

37.3 Scenario and simulation design

Base, upside and downside cases are scenarios, not a probability distribution. If a future implementation uses simulation, it must disclose the stochastic variables, distribution choices, correlations, floors, transition rules, horizon, periodicity, path count, random seed and convergence test. The path count should be justified by stability of the outputs rather than chosen as a round number.

Simulated states would be synthetic teaching states. They would not be risk-neutral paths or real-world forecasts unless the calibration and measure were separately defined and evidenced. The implementation must keep those interpretations distinct.

37.4 Feature mapping

The future exercise may test six feature families, each under a rights-first record:

- ✦ A structural default component, using disclosed firm-value, debt, horizon, volatility and recovery assumptions.
- ✦ A builder-basket sensitivity, tracking synthetic capacity accumulation and prior use along each path.
- ✦ An equity-cure sensitivity, applying synthetic cure conditions, caps and breach states.
- ✦ An excess-cash-flow sweep sensitivity, applying the synthetic cash-flow definition and prepayment hierarchy.
- ✦ A redemption sensitivity, applying synthetic call dates, prices and make-whole assumptions.
- ✦ A portability sensitivity, applying the synthetic change-of-control and leverage-test states.

Capacity is not exercise; exercise is not automatically loss; and a modelled loss is not automatically market price. The implementation must preserve those distinctions in its outputs.

37.5 Output and reconciliation protocol

Each component would first be reported in its natural unit: capacity, cash flow, currency present value or state frequency under the selected measure. If currency components are combined, the sign convention and interaction effects must be explicit. An unexplained remainder must remain visible.

A spread-equivalent teaching conversion may be added only after the underlying present value and denominator are validated. It must be labelled as a conversion of the synthetic model output, not a fair spread. No aggregate may be used to claim that document optionality dominates default risk for an actual credit.

37.6 Validation gates

Before numerical results can be shown to readers, the future artefact must pass these gates:

- ✦ all synthetic inputs are catalogued and hash-bound;
- ✦ the three financial statements, debt schedule, cash and covenants reconcile;
- ✦ formulas or code are versioned and mapped to displayed outputs;
- ✦ simulation settings and seeds reproduce exactly;
- ✦ convergence and stability tests pass;
- ✦ standalone components and interaction effects reconcile;
- ✦ limiting cases and directional checks behave as expected;
- ✦ legal assumptions are reviewed separately from model mechanics;
- ✦ an independent reviewer reproduces the displayed outputs; and
- ✦ The fictional design should also be checked for originality, confidentiality and any unintended resemblance to a real issuer or private transaction.

Until every gate passes, the chapter remains a design specification. It does not claim that a simulation was run, that the features have market values, or that a security is cheap, rich or suitable for any reader.

37.7 Practitioner checklist

Begin with the document and legal entity map. Define the teaching question. Build a reconciled synthetic financial model. Select only the features relevant to that question. State the baseline and counterfactual. Disclose inputs, units and ranges. Test dependencies and interactions. Preserve the unexplained remainder. Label the output correctly. Obtain independent legal and model review before any promotion from taxonomy to a numerical teaching estimate.

The method is valuable when it makes assumptions and limits easier to challenge. It fails when a familiar option label or precise-looking number replaces the underlying document analysis.

37.8 Implementation handoff and evidence pack

A future model builder should receive a frozen specification rather than an open-ended request to “price the document.” The handoff should identify the selected synthetic clauses, required financial schedules, state variables, output units, scenario set, validation tests and prohibited conclusions. Any change to that specification should be versioned so that a reviewer can distinguish a corrected model from a changed question.

The completed evidence pack should contain the synthetic input catalogue; the fictional agreement extracts authored for the exercise; the integrated financial model; formula or code inventory; dependency graph; scenario and simulation configuration; calculation-engine version; random seed; convergence results; component and

interaction reconciliations; output-to-manuscript map; and independent review notes. Each file should carry a cryptographic hash. The chapter text should cite the exact artefact and cell, range or output identifier behind every displayed number.

Validate a fictional teaching estimate in four layers. First, test whether the synthetic rights map matches the stated assumptions without implying a legal conclusion. Second, check formulas, states, units, calibration, convergence and reproducibility. Third, ensure the labels do not imply price, recommendation or certainty. Fourth, confirm that the inputs and narrative neither identify nor reconstruct a real borrower or private transaction.

Promotion is fail-closed. A taxonomy may be published as taxonomy. A design may be published as design. A synthetic sensitivity may be published only with its evidence pack. A calibrated-price claim would require a separate and materially higher standard, including dated market data, calibration instruments, fit diagnostics, holdouts and independent model-risk approval. If the evidence supports only the lower tier, the language must remain at that tier.

MARKET AND REGULATORY CONTEXT

- 38 Secondary Market Trading and Loan Operations
 - 39 The Regulatory Framework for European Leveraged Finance
 - 40 Interest-Limitation Rules in Leveraged Finance
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-

Secondary Market Trading and Loan Operations

Scope, purpose and boundary

This chapter turns a credit view into a controlled secondary-loan workflow. It is written for education as at **12 July 2026**. Every company, amount, trade and mark below is fictional. The chapter does not reproduce Loan Market Association (LMA) or Loan Syndications and Trading Association (LSTA) forms, private trades, dealer quotations or confidential information. Current executed documents, incorporated trading terms, applicable law and a firm's approved procedures control an actual trade. Legal and compliance conclusions require qualified advisers.

The LMA says that documentation, market practice, guidance and loan operations are among its core activities, and the LSTA publicly identifies primary and secondary settlement, delayed-compensation resources and operational tools among its standards work. Those sources support a process framework, not a universal rule for any individual transaction. See the LMA overview (<https://www.lma.eu.com/about-us>) and LSTA Operations & Standards (<https://www.lsta.org/content-areas/operations-standards/>).

Learning objectives

After completing the chapter, the reader should be able to:

- ♦ 1. compare a near-par and a distressed opportunity through price, expected recovery, liquidity, transferability, information and settlement rather than through a label alone;
- ♦ 2. apply the hierarchy among the credit agreement, trade confirmation, incorporated market terms and settlement instrument, while recognising LMA/LSTA differences;
- ♦ 3. distinguish an assignment from a participation, including lender-of-record status, direct borrower rights and grantor exposure;
- ♦ 4. reconcile purchase price, accrued interest, fees, delayed settlement and financing carry from displayed assumptions;
- ♦ 5. test consent, eligible-assignee, disqualified-lender, affiliate and participation provisions before assuming that a trade can settle as proposed;
- ♦ 6. construct a mark hierarchy and a readiness process that preserve source, time, size, liquidity and override evidence; and
- ♦ 7. operate within public/private information controls and escalation boundaries around a stressed or restructuring credit.

1. The operating vocabulary

Table 38.1 uses deliberately functional definitions. A market label never overrides the documents.

Term	Working meaning for this chapter	Control question
Par trade	A market description generally used for a performing-loan trade processed under the applicable par workflow	Which incorporated terms and settlement mechanics did the parties actually select?
Distressed trade	A market description generally used where credit or documentation risk calls for a distressed workflow	What additional representations, title or claim risks does the selected documentation allocate?
Assignment	A transfer intended to make the buyer the lender of record for the assigned interest after required steps occur	Has every consent, eligibility, minimum amount, form and agent step been satisfied?
Participation	A contractual exposure between grantor and participant in which the grantor generally remains lender of record	What cash-flow, voting, information and insolvency exposure remains to the grantor?
Lender of record	The person recorded by the facility agent as holding the relevant commitment or loan	Does the buyer obtain direct rights against the borrower or only against a grantor?
Grantor risk	The participant's counterparty and structural exposure to the participation grantor	Are received cash, voting directions and insolvency consequences adequately addressed?
Trade date	The date on which the parties agree the economic trade, subject to the governing trade documents	Which price, amount, accrued-interest treatment and conditions were agreed then?
Settlement date	The date the transfer and related payment become effective under the selected process	Has legal effectiveness been distinguished from the parties' economic allocation?
Readiness	The state in which the responsible party has completed the specified documents, data and actions needed for settlement	Which readiness definition applies and when was each item completed?
Delayed compensation	A document-based economic adjustment for qualifying settlement delay	Do the incorporated terms provide it, from when, and subject to which readiness conditions?
Purchase price	The principal amount multiplied by the agreed price, adjusted only as the documents require	Is price quoted per 100 of principal, and which adjustments sit outside it?
Eligible assignee	A transferee that satisfies the facility's negotiated eligibility definition	Is eligibility tested on the intended settlement date and for the relevant tranche?
Disqualified lender	A person captured by a negotiated disqualified-institution or similar restriction	Which list, supplement mechanism, affiliate rule and consequence applies?
Dealer indication	A non-binding price or market-level communication whose reliability depends on context	What time, size, side, instrument and liquidity qualification accompanied it?
Pricing service	A third-party evaluated-price or data service	Is the methodology observable, current and appropriate for this position?
Public-side information	Information approved under the firm's controls for use by personnel permitted to trade	Has status been confirmed by the authorised compliance process rather than inferred?

2. Start with a tradable credit thesis

A loan analyst should not stop at "buy at 98" or "recovery is 70." The investable thesis connects the borrower, instrument, document position and operational route. Chapters 7, 9–13, 20, 22–23, 26 and 29 supply the credit, covenant, capital-structure, restructuring and ratings inputs. Chapter 39 supplies the regulatory perimeter.

Table 38.2 is a compact research-to-trade file.

Workstream	Minimum evidence	Output before execution
Credit	dated financials, debt schedule, liquidity bridge, catalysts, downside	base and downside cash outcomes
Instrument	facility, tranche, currency, maturity, interest basis, amortisation	instrument identifier and economic terms
Entity and ranking	borrower, guarantors, collateral, intercreditor position	entity/claim map and recovery range
Documents	current credit agreement and amendments; transfer section; confidentiality terms	restriction matrix and open legal points
Market	executable or indicative evidence with timestamp, side and size	price range and liquidity confidence
Information	public/private status and wall-cross history under firm policy	compliance clearance or stop
Counterparty	approved entity, capacity, settlement instructions	counterparty approval and identity match
Operations	form, agent, consents, KYC, tax and cash details	named owner for every readiness item
Governance	mandate fit, limits, approvals, conflicts and sanctions controls	recorded approval or rejection

Process diagram A — the controlled path

Credit question

- > evidence and downside
- > exact facility/tranche
- > transfer and information tests
- > price/size/counterparty agreement
- > confirmation and incorporated terms
- > readiness and agent process
- > cash/interest/fee reconciliation
- > settlement, position record and post-trade review

The feedback loop matters. If the buyer is ineligible, if the seller cannot provide the needed record, or if the analyst receives restricted information, the correct response may be to change structure, change timing or stop.

Operations is part of underwriting because it determines whether and how the intended exposure can exist.

3. Par and distressed are workflows, not valuation conclusions

The same loan may be described differently as circumstances change. Price below 90 does not itself prove a distressed legal category; price near 100 does not remove transfer, settlement or credit risk. Use the multi-factor comparison in Table 38.3.

Dimension	Near-par performing case	Stressed/distressed case	Required evidence
Price	small discount or premium may dominate short-period return	price embeds a wider and often disputed outcome range	dated bid/offer context and size
Recovery	usually a tail scenario but still required	central to value; entity and claim mapping critical	valuation, priority, costs and timing
Liquidity	may have more observable axes or quotes	depth can fragment by holder and claim	more than one source where feasible
Transferability	routine processing may still face restrictions	amendments, defaults or lists may complicate it	current executed documents
Information	public-side research may be sufficient	restructuring access can create wall-cross choices	compliance status and records
Settlement	standard workflow may be faster	title, claims and documentation diligence may expand	selected terms and readiness log

Fictional Trade 1 — a near-par assignment

Northbridge Components has a EUR 600 million term facility. Atlas Fund agrees to buy EUR 8 million from Meridian Bank at 98.75. The credit case assumes stable cash generation; the document review shows that an assignment requires agent processing, borrower consent subject to specified exceptions, a EUR 1 million minimum transfer and an eligible-assignee test. Atlas is not on the supplied disqualified-lender list, but that alone does not establish eligibility.

Calculation 38.1 — base purchase price

Displayed inputs: principal = EUR 8,000,000; price = 98.75 per 100.

Purchase price = $8,000,000 \times 98.75\%$ = EUR 7,900,000.

That amount is not a full settlement statement. Accrued interest, fees, repayments, currency adjustments and document-specific compensation must be separately reconciled. Atlas records the price source, timestamp, side and size; counsel and operations confirm the transfer route. "Near par" did none of that work.

Fictional Trade 2 — a distressed participation

Blue Quay Logistics has missed a forecast and is negotiating with creditors. Cedar Credit wants EUR 5 million of economic exposure, but a direct assignment cannot be completed within its timing requirement because the proposed buyer is not yet approved under the facility. Seller Pine Bank offers a participation at 64.00.

The participation may avoid an immediate change in lender of record, but it is not a universal workaround. Cedar must assess Pine's credit, the participation's payment and voting mechanics, information-sharing limits, the facility's participation restrictions and applicable law. Cedar's recovery model concerns Blue Quay; its legal exposure also concerns Pine.

Calculation 38.2 — price versus modeled cash recovery

Displayed inputs: principal = EUR 5,000,000; price = 64%; modeled cash recovery in 24 months = 72% of principal; no interim cash; ignored for simplicity: fees, tax and default interest.

Cash paid = $5,000,000 \times 64\%$ = EUR 3,200,000. Modeled recovery = $5,000,000 \times 72\%$ = EUR 3,600,000. Gross gain = $3,600,000 - 3,200,000$ = EUR 400,000. Simple two-year return = $400,000 / 3,200,000$ = 12.50%.

The calculation is not an annualised return and does not reflect timing uncertainty or grantor failure. If estimated resolution costs reduce cash recovery to 66%, gross gain falls to EUR 100,000. The price is observable; the

recovery remains a scenario.

4. Which document controls which question?

Neither "LMA trade" nor "LSTA trade" is a complete answer. The association workflow, selected documentation, governing facility and transaction facts must align. Do not mix a timing convention from one market with a compensation rule from another. Do not reproduce or improvise standard forms.

Table 38.4 gives a question hierarchy rather than a priority opinion.

Layer	Typical subject	Analyst/operations check
Underlying facility documents	debt rights, transfer route, eligibility, consent, minimums, voting, confidentiality	obtain the current agreement and all effective amendments
Oral/electronic trade agreement	identity, facility, amount, price, expected form and date	preserve an authorised trade record and resolve ambiguity promptly
Trade confirmation	selected transaction details, representations and incorporated terms	verify legal names, amount, price, trade type and elections
Incorporated market terms	standard settlement and economic allocation selected by the parties	use the correct version and effective date; obtain advice on conflicts
Settlement instrument	assignment, transfer certificate, participation or other implementation	confirm it achieves the intended exposure and matches the facility
Agent/borrower process	registers, notices, consents, KYC and administrative actions	track status, evidence and dependencies without treating silence as approval
Internal records	approvals, marks, position, cash, P&L and compliance status	reconcile front, middle and back office to the same trade identity

The LMA describes its documents as being kept under review for primary and secondary markets; the LSTA's public operations page distinguishes settlement and delayed-compensation resources. Therefore, version and election discipline is essential. A convention date is not a guaranteed legal settlement date. The actual documents determine when economic adjustments begin, which readiness conditions matter and how an unmatched or failed settlement is handled.

5. Assignment versus participation

Table 38.5 forces the structural questions that labels conceal.

Feature	Assignment	Participation
Lender of record	intended to change after effective transfer steps	grantor generally remains lender of record
Direct borrower claim	buyer generally seeks direct facility rights	participant generally claims against grantor under participation
Consent and eligibility	facility transfer tests commonly central	facility and participation terms still require review
Voting	transferred facility voting rights subject to documents	participant directions depend on participation terms and retained discretion
Cash path	agent pays registered holder	grantor receives and passes amounts under participation
Counterparty exposure	seller exposure usually changes after effective settlement, subject to surviving terms	participant bears continuing grantor performance and insolvency risk
Information	facility/confidentiality framework applies	information flow also depends on participation and grantor permissions
Exit	direct transfer under facility rules	transfer or elevation depends on participation and facility mechanics

Fictional Trade 3 — restricted transferee

Falcon Ridge Capital bids 71.50 for EUR 12 million of Solace Retail's term loan. Its name resembles an affiliate of a person on a disqualified-lender list. The credit agreement contains definitions for disqualified institutions, controlled affiliates, separately managed funds and consequences of a non-permitted transfer. The team cannot decide the issue from a spreadsheet name match.

The buyer supplies its full legal identity and ownership/control information through the approved channel. Operations checks the applicable list version and supplements. Counsel construes the definitions and consequences. Compliance checks sanctions and conflicts. Until resolved, the trade is not marked “ready.” A participation is not automatically permitted: the participation restriction and disclosure consequences are independently tested.

Eligibility field	Evidence	Status choices	Owner
legal entity and capacity	constitutional/authority and onboarding record	clear / incomplete / escalated	counterparty team
eligible - assignee definition	facility clause and facts	meets / does not meet / legal review	counsel
disqualified - lender test	dated list, supplements, affiliate facts	clear / possible match / restricted	counsel + operations
borrower/agent consent	clause, request and response	obtained / deemed where valid / pending / refused	operations
minimum amount and hold	facility calculation	passes / waiver needed	operations
participation restriction	facility and proposed terms	permitted / conditional / prohibited / uncertain	counsel

This is Table 38.6. A prohibited transfer is not universally void: possible consequences depend on the documents and law. The educational control is to identify the issue, preserve evidence and escalate—not to predict the legal result.

6. Settlement economics and readiness

Accrued-interest reconciliation

Suppose Northbridge's EUR 8 million loan pays 6.60% per year and the agreed allocation gives the buyer 17 days of accrued interest on an Actual/360 basis. Ignore withholding and compounding.

Calculation 38.3 — accrued interest

Accrued interest = $8,000,000 \times 6.60\% \times 17/360$ = EUR 24,933.33.

If the selected terms instead allocate that period to the seller, the arithmetic does not change but the direction of the settlement item does. The deal team must identify the governing allocation before inserting the number.

Delay and financing carry

Fictional Trade 4 — delayed settlement

Horizon Debt buys EUR 10 million of Tern Data at 96.25. The parties expected a short settlement, but buyer KYC was incomplete for 11 calendar days; after completion, an agent processing dependency lasted another 8 days. The incorporated terms must determine whether any delayed-compensation mechanism applies, its start date and readiness effects. The following is only an internal cost-of-carry illustration.

Calculation 38.4 — buyer funding carry

Displayed inputs: cash price = EUR 9,625,000; internal funding rate = 5.20%; measured delay = 19 days; Actual/360.

Funding carry = $9,625,000 \times 5.20\% \times 19/360$ = EUR 26,415.28.

Breaking the period into 11 buyer-not-ready days and 8 later days gives EUR 15,293.06 and EUR 11,122.22 respectively. That attribution is useful operational evidence, but it does not establish contractual entitlement.

Calculation 38.5 — price move versus carry

On day 19, an executable bid for the same size is 95.50.

Mark movement = $10,000,000 \times (95.50\% - 96.25\%)$ = -EUR 75,000. Combined pre-fee economic movement = $-75,000 - 26,415.28$ = -EUR 101,415.28.

The position may economically belong to one party from the trade date while legal title has not transferred. Accounting, capital and risk treatment are outside this simplified example and require the firm's policies.

A settlement statement template—not a legal form

Table 38.7 reconciles fictional numbers without prescribing allocation.

Item	Formula/evidence	Buyer pays/(receives), EUR
Principal purchase price	$10,000,000 \times 96.25\%$	9,625,000.00
Agreed accrued - interest item	documented amount	31,166.67
Principal repayment after trade	agent notice; assumed for illustration to reduce buyer payment	(250,000.00)
Transfer fee allocated to buyer	invoice/selected terms	2,500.00
Document-based delay item	assumed agreed after review	(9,800.00)
Net cash	sum	9,398,866.67

The control total is $9,625,000 + 31,166.67 - 250,000 + 2,500 - 9,800 = 9,398,866.67$. Each line needs a direction, currency, source and approval. Principal and interest events occurring between trade and settlement should also update the position quantity and future accrual base.

Process diagram B — readiness and exceptions

Trade captured

-> confirmation matched?

-> buyer and seller documents complete?

-> facility eligibility/consent complete?

-> agent/KYC/tax/cash data complete?

-> intervening events reconciled?

yes -> release cash and instrument under controls

no -> identify responsible dependency -> escalate -> recalculate -> re-test

7. Mark hierarchy and valuation governance

A mark is an evidence record, not a single number detached from market conditions. The strongest source may change with instrument, size and market state.

Table 38.8 sets a hierarchy that a firm can adapt.

Level	Candidate evidence	Required metadata	Principal limitation
1	completed arm's-length trade in same instrument and relevant size	date/time, size, side, settlement context	may be stale or idiosyncratic
2	executable bid/offer in relevant size	source, timestamp, side, size, expiry	one-sided or withdrawn liquidity
3	multiple dealer indications	contributors, time window, sides and dispersion	non-binding and potentially clustered
4	pricing-service evaluation	service, timestamp, methodology status	may lag abrupt credit events
5	comparable instruments	adjustment bridge for ranking, maturity, spread and liquidity	basis risk
6	model or recovery value	full assumptions, scenarios and governance	judgment-heavy; not a market quote

For each position, preserve: instrument and tranche; currency; source; timestamp and time zone; bid, offer or mid; size; whether executable; accrued-interest convention if relevant; observed dispersion; liquidity qualification;

chosen mark; override amount; approver; and next review event. A valuation committee can accept a lower-level source only with an explicit rationale.

Calculation 38.6 — controlled mark selection

For a EUR 6 million position, evidence at 16:00 is: executable EUR 2 million bid at 82.00; dealer indications of 81.25/82.75 and 80.75/82.50; pricing service at 83.20; model recovery value at 86.00. Policy requires an exit-side mark and a size adjustment when the executable evidence covers less than half the position. The committee applies a documented 0.75-point size adjustment to the 82.00 bid.

Selected mark = $82.00 - 0.75 = 81.25$. Position value = $6,000,000 \times 81.25\% = \text{EUR } 4,875,000$.

The adjustment is an invented policy assumption, not a market standard. The record explains why 83.20 and 86.00 were not selected. If the 82.00 bid expires, the hierarchy must be rerun.

8. Information and creditor-conduct controls

Creditors may receive confidential budgets, restructuring proposals, lender presentations or steering-committee materials. “Confidential” and legally defined “inside information” are not interchangeable, and the perimeter can include securities or related instruments beyond the loan. In the EU, Regulation (EU) No 596/2014 supplies the Market Abuse Regulation framework; in the UK, the FCA explains the onshored UK MAR and its prohibitions on insider dealing and unlawful disclosure. See EU MAR (<https://eur-lex.europa.eu/eli/reg/2014/596/oj>) and the FCA's UK MAR overview (<https://www.fca.org.uk/markets/market-abuse/regulation>). Scope and conclusions are jurisdiction- and instrument-specific.

Fictional Trade 5 — the information stop

An analyst covering Blue Quay is invited to a lender call that will present a non-public liquidity forecast and proposed exchange terms. The invitation asks recipients to accept confidentiality. Before joining, the analyst sends the materials to the authorised compliance contact. The portfolio manager does not instruct the analyst to “just stay public” while reading them. Compliance and counsel determine the wall-cross process, affected instruments, restricted-list action and permitted communications. The trade order is held pending that process.

A minimum control sequence is:

- ♦ 1. identify the information, source, time, recipients and confidentiality terms;
- ♦ 2. stop dissemination and trading decisions until authorised review where status is uncertain;
- ♦ 3. identify potentially affected issuers and instruments rather than assuming the cash loan is the only relevant asset;
- ♦ 4. record wall-cross consent, restrictions, cleansing events and access changes under policy;
- ♦ 5. separate factual voting analysis from coordination, conflicts and conduct questions; and
- ♦ 6. escalate sanctions, antitrust, market-abuse, fiduciary, confidentiality or privilege questions to the responsible specialists.

Correct credit analysis does not cure an information-control breach. Equally, the fact that a borrower is private does not prove that market-abuse rules are irrelevant: the instrument and issuer perimeter must be tested.

9. Short orientation: loan credit derivatives

A loan credit derivative can transfer specified credit risk without transferring the cash loan itself. Conceptually, an analyst should distinguish the **reference obligation or entity**, the **defined credit events**, the **settlement method**,

the **counterparty**, collateral and close-out exposure, and any **basis risk** between the hedge and the owned loan. A hedge can reduce one loss pathway while introducing documentation, valuation, liquidity and counterparty risks.

This orientation intentionally stops there. It does **not** teach derivatives documentation, confirmation terms, legal characterization, regulatory treatment, collateral mechanics or pricing. A cash-loan purchase and a derivative position are not interchangeable because their rights, cash flows and event definitions may differ. Any transaction requires approved documentation, specialist valuation, legal, regulatory, tax, accounting, operations and compliance review.

10. Integrated operating routine

The practitioner can use six gates:

- ♦ 1. **Exposure gate:** identify exact borrower, facility, tranche, entity, ranking and desired amount.
- ♦ 2. **Credit gate:** document facts, scenarios, recovery and catalysts with dates and sources.
- ♦ 3. **Tradability gate:** test eligibility, consent, minimums, disqualified persons, affiliates and participation restrictions.
- ♦ 4. **Information gate:** establish public/private status and permitted personnel, instruments and actions.
- ♦ 5. **Economic gate:** match price, quantity, accrual, fees, intervening events, carry and downside.
- ♦ 6. **Settlement gate:** match confirmation and terms, complete readiness, reconcile cash/title/position and record exceptions.

No single gate substitutes for another. A strong recovery model cannot make an ineligible buyer eligible; a technically complete assignment cannot make an unattractive price attractive.

11. Exercises and answer checks

Exercise 38.A — assignment or participation?

Orion Fund wants EUR 7 million of a EUR facility. Direct assignment needs borrower consent; the request is pending. Bank Vale offers a participation at the same price. List five questions that must be answered before Orion treats the participation as equivalent.

Answer check: At minimum: lender-of-record status; direct claim versus grantor claim; Vale counterparty/insolvency risk; voting and enforcement directions; cash and information flow; participation restrictions; confidentiality; elevation/transfer; tax/accounting/regulatory treatment. The expected answer is not “use the participation.”

Exercise 38.B — settlement arithmetic

Principal is EUR 4 million, price 93.50, allocated accrued interest EUR 18,400, a EUR 100,000 post-trade principal repayment reduces cash due, and a EUR 1,750 fee is paid by the buyer. Calculate net cash.

Answer check: $4,000,000 \times 93.50\% = 3,740,000$; then $3,740,000 + 18,400 - 100,000 + 1,750 = \text{EUR } 3,660,150$. The documents must still determine the direction and eligibility of each item.

Exercise 38.C — mark and information decision

A pricing service shows 77.00, yesterday's EUR 1 million trade was 76.25, and today's EUR 5 million executable bid is 74.50. Your EUR 5 million position is marked 77.00. Separately, the analyst has just received a confidential restructuring term sheet. What should happen?

Answer check: Preserve all metadata; escalate the mark because same-size executable exit evidence conflicts with the service; record any override. Stop or hold affected trading and dissemination under the authorised information-control process; identify relevant instruments and recipients. Do not infer a legal conclusion from “confidential,” but do not trade while status is unresolved.

Appendix 38.A — neutral trade-readiness checklist

This is a control prompt, not an association form.

- ♦ • [] Legal entity names, capacity, counterparty approval and settlement instructions match.
- ♦ • [] Facility, borrower, tranche, currency, principal, price, trade date and selected trade type match.
- ♦ • [] Current facility agreement and effective amendments are available.
- ♦ • [] Eligible-assignee, disqualified-lender, affiliate, minimum-hold and minimum-transfer tests are recorded.
- ♦ • [] Consent, notice, agent and borrower steps are identified with evidence and owner.
- ♦ • [] Participation restrictions are independently tested if a participation is proposed.
- ♦ • [] Confirmation, incorporated terms, elections and version date are verified by authorised personnel.
- ♦ • [] KYC, sanctions, tax forms, cash accounts and signatures are complete under policy.
- ♦ • [] Information status, restricted-list and wall-cross records are current.
- ♦ • [] Accrued interest, repayments, fees, delay items and currency are reconciled line by line.
- ♦ • [] Readiness dates and responsible dependencies are evidenced, not assumed.
- ♦ • [] Cash, legal effectiveness, agent register and internal position records reconcile after settlement.
- ♦ • [] Valuation source, timestamp, side, size, liquidity and override rationale are retained.
- ♦ • [] Exceptions are escalated; unresolved items remain open rather than being forced to green.

Appendix 38.B — dated public-source register

Sources reviewed 12 July 2026:

- ♦ 1. Loan Market Association, About Us (<https://www.lma.eu.com/about-us>) — public description of LMA documentation, market-practice and operations functions. No form text used.
- ♦ 2. Loan Syndications and Trading Association, Operations & Standards (<https://www.lsta.org/content-areas/operations-standards/>) — public description of settlement, operational and delayed-compensation resources. No proprietary resource reproduced.
- ♦ 3. Regulation (EU) No 596/2014 (<https://eur-lex.europa.eu/eli/reg/2014/596/oj>) — official EU Market Abuse Regulation text; application requires current legal analysis.
- ♦ 4. Financial Conduct Authority, Market Abuse Regulation (<https://www.fca.org.uk/markets/market-abuse/regulation>) — official UK orientation, updated by the FCA; not a substitute for the law or advice.

The sources establish public framework points only. They do not validate any fictional trade or prescribe a settlement outcome.

The Regulatory Framework for European Leveraged Finance

Scope, date and professional boundary

This chapter provides an educational map of the **EU/ECB prudential framework with a bounded UK comparison**, reviewed to **12 July 2026**. It contains no national-law modules. Directives still require transposition, options and effective dates may differ, supervisory judgments are institution-specific, and internal bank policy can be more restrictive than the regulatory baseline. Every institution, borrower, amount and case is fictional.

The chapter is not legal, regulatory, capital, accounting, investment or transaction-specific advice. A live conclusion requires the current legislation, national implementation, competent-authority materials, permissions, consolidated perimeter, supervisory decisions and firm policy. Chapters 2, 7, 10, 11, 29 and 38 provide product, syndication, ratings and trading context.

Learning objectives

After completing this chapter, the reader should be able to:

- ✦ 1. separate enacted law, a directive awaiting or subject to national implementation, supervisory guidance, Pillar 2 judgment, institution policy and observed market behaviour;
- ✦ 2. apply the ECB's leveraged-transaction identification, governance and exceptional-leverage expectations only within the relevant supervisory perimeter;
- ✦ 3. map CRR3/CRD6 concepts across standardized and internal-ratings-based (IRB) credit risk, risk-weighted assets (RWA), large exposures, buffers, the output floor, leverage and liquidity constraints;
- ✦ 4. analyse underwriting, syndication, distribution, sell-down and final-hold risk as distinct exposure states;
- ✦ 5. compare a bank, a loan-originating alternative investment fund (AIF)/private-credit vehicle and a collateralised loan obligation (CLO) without describing a non-bank as unregulated; and
- ✦ 6. identify conduct, distribution, securitisation, supervisory-review and national-implementation interfaces without inventing a universal leverage or capital rule.

1. Source hierarchy before ratio analysis

Regulatory work begins by asking **who, what, where and when**. "Basel," "ECB limit," "PRA cap" or "AIF rule" is incomplete.

A controlled regulatory statement should therefore fit one sentence pattern: **for this entity, at this consolidation level, for this exposure or activity, on this date, this identified source creates this requirement or expectation, subject to these stated assumptions and unresolved implementation points**. If the file cannot complete that sentence, the proposition remains an open issue. The discipline prevents a rule written for a bank from migrating into a borrower covenant, a fund limit from being treated as bank capital, or supervisory guidance from being presented as enacted law.

Table 39.1 — source hierarchy and evidential weight

Layer	Typical instrument	What it can establish	What it cannot establish alone
Enacted directly applicable law	EU regulation, as amended and in force	binding requirement within its legal scope	institution-specific supervision or national options without further work
Directive	EU directive and transposing measures	EU legislative requirement and transposition obligation	the exact national operative rule before checking implementation
Technical standards/guidelines	binding standards where adopted; authority guidelines	detailed methods or supervisory expectations within scope	an automatic borrower covenant or commercial outcome
Supervisory guidance	ECB or PRA supervisory publication	how a supervisor expects in-scope firms to govern risks	a generally applicable statutory prohibition
Pillar 2/SREP decision	confidential institution-specific decision	additional requirements or expectations for that institution	a market-wide percentage
Institution policy	risk appetite, underwriting standard, limit or model overlay	the firm's approved operating constraint	the legal minimum or another firm's policy
Market observation	public deal or aggregate data	evidence of behaviour for the specified sample and date	regulatory causation without analysis

Core definitions

Table 39.2 — prudential vocabulary

Term	Working definition
Leveraged transaction	A transaction captured by the applicable supervisory or institution definition; it is not one universal statutory product category.
Supervisory guidance	A published statement of supervisory expectations that must be read within its stated legal and institutional perimeter.
Pillar 1	Generally applicable minimum prudential requirements calculated under the governing rule set.
Pillar 2	Supervisory assessment and measures addressing institution-specific risks not fully captured by Pillar 1.
Buffer	A capital layer or requirement with its own legal basis, perimeter and consequence; it is not interchangeable with the Pillar 1 minimum.
RWA	Exposure amounts after applying the relevant regulatory risk measurement; different risk types and methods contribute to total RWA.
Standardized approach	Rule-based regulatory treatment using prescribed exposure classes, risk weights and recognition conditions.
IRB	An approved internal-ratings-based approach using specified internal estimates subject to regulatory requirements and supervision.
Large exposure	A concentration measure governed by exposure-value and eligible-capital concepts; it is not simply credit-risk RWA.
Output floor	A floor on an institution's aggregate risk-weighted exposure amount derived by reference to standardized calculations, subject to transition.
Leverage ratio	A non-risk-based capital measure using a regulatory exposure measure.
Underwriting risk	Risk that an institution commits to fund or purchase before the intended distribution is completed.
Distribution risk	Risk that expected sell-down fails, is delayed or occurs on worse terms.
Loan-originating AIF	An AIF that meets the applicable legislative definition associated with originating loans, subject to perimeter and implementation.
CLO	A tranchised securitisation vehicle whose liabilities and asset eligibility are governed by transaction documents and applicable regulation.
SREP	The supervisory review and evaluation process through which the competent authority assesses an institution and may apply measures.

2. One transaction, several constraint owners

The borrower does not “have” a regulatory capital ratio. The bank, fund, CLO, arranger and investor each face different rules and documents.

Table 39.3 — regime/entity/product map

Actor or vehicle	Primary question	Relevant source families	Common analytical error
ECB - supervised bank	How should the institution identify, approve, measure and hold/distribute the exposure?	CRR/CRD, ECB guidance, SREP, internal policy	treating 6.0x as a borrower - law ceiling
Other EU bank	Which competent authority, implementation and prudential methods apply?	CRR, national CRD implementation, EBA/authority materials	assuming all ECB expectations bind identically
UK bank	Which PRA rules, permissions, supervisory expectations and policy apply?	UK legislation, PRA Rulebook, supervisory statements	importing an EU ratio or claiming a universal PRA multiple
AIF/AIFM	Is the vehicle loan - originating, open/closed, leveraged and within applicable fund rules?	AIFMD as amended, implementation, fund documents	calling private credit "unregulated"
CLO	Is the asset eligible and how do securitisation, retention, diligence, disclosure and transaction tests apply?	EU securitisation framework, investor rules, indenture, collateral criteria	treating a CLO constraint as bank capital or fund law
Distributor/investor	What conduct, product, client and mandate rules apply?	MiFID/conduct framework, permissions, mandate	inferring suitability from credit quality alone

Diagram A — attach the rule to the right object

Borrower and facility

- > bank commitment: CRR/CRD + supervisor + bank policy
- > AIF loan/investment: AIFM/AIF rules + fund documents
- > CLO asset: securitisation perimeter + indenture/tests
- > investor purchase: investor prudential/conduct/mandate rules

Same borrower != same regulatory treatment

3. ECB leveraged-transaction guidance

The ECB published its *Guidance on leveraged transactions* in May 2017 for relevant significant credit institutions under ECB Banking Supervision. The document expects an institution's definition to capture, among other things and subject to its scope and exclusions, transactions where post-financing leverage exceeds **4.0 times Total Debt to EBITDA** and transactions involving specified financial-sponsor ownership. It also states that transactions with Total Debt to EBITDA above **6.0 times at inception** should remain exceptional, be justified and form part of escalation. Read the official ECB guidance (https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf).

Three controls follow:

- ♦ • 6.0x is a supervisory expectation in that framework, **not** a statutory borrower ceiling, covenant definition or automatic prohibition.
- ♦ • Total Debt and EBITDA must follow the applicable guidance and institution methodology; a deal model's "net leverage" cannot be substituted silently.
- ♦ • Identification is only the first step. Governance covers risk appetite, underwriting and syndication, monitoring, stress testing and management information.

Fictional Case 1 — identification and escalation

Europa Bank, an in-scope fictional institution, considers a EUR 450 million acquisition financing for Caldera Services. At inception, documented Total Debt is EUR 720 million. The institution's controlled EBITDA calculation is EUR 120 million. The buyer is a financial sponsor. No exclusion is assumed.

Calculation 39.1 — leveraged-transaction identification

Total Debt / EBITDA = EUR 720m / EUR 120m = 6.0x.

The sponsor criterion and the leverage result are recorded independently. If the bank's policy defines "above 6.0x" consistently with the guidance, exactly 6.0x is not mathematically above 6.0x; internal policy may nevertheless impose an escalation at or near that level. If debt is EUR 738 million, leverage is $738 / 120 = 6.15x$, entering the exceptional-leverage analysis. The decision file should show definitions, source dates, permitted adjustments, exclusions, policy thresholds and approval—not merely the ratio.

Fictional Case 2 — adjustment governance

Helix Packaging reports EBITDA of EUR 95 million. The deal team proposes EUR 18 million of adjustments: EUR 6 million already realised, EUR 5 million contracted with evidence, and EUR 7 million aspirational. Debt is EUR 610 million.

EBITDA basis	Amount, EURm	Debt/EBITDA
reported	95	6.42x
plus realised item only	101	6.04x
plus realised and evidenced contracted item	106	5.75x
all proposed adjustments	113	5.40x

This is Table 39.4 and an analytical sensitivity, not a statement of which adjustments the ECB or bank must accept. The institution applies its controlled definition and records why each item is included. The range shows why governance of EBITDA matters more than presenting one polished ratio.

4. From exposure to capital stack

CRR3—Regulation (EU) 2024/1623—amended the Capital Requirements Regulation, while CRD6—Directive (EU) 2024/1619—amended the Capital Requirements Directive. The regulation and directive have different legal mechanics. CRD6 implementation must be checked in the relevant Member State; this chapter does not supply that national layer. See CRR3 (<https://eur-lex.europa.eu/eli/reg/2024/1623/oj>) and CRD6 (<https://eur-lex.europa.eu/eli/dir/2024/1619/oj>).

For a credit exposure, the workflow is not "loan × 8%." It is:

- ♦ 1. identify obligor, product, exposure class and consolidation perimeter;
- ♦ 2. determine exposure value and permitted credit-risk-mitigation effects;
- ♦ 3. apply the institution's permitted standardized or IRB treatment;
- ♦ 4. aggregate credit, market, operational and other relevant RWA;
- ♦ 5. apply the full own-funds requirement and buffer stack at the proper level;
- ♦ 6. test leverage ratio, large-exposure, liquidity, stress and supervisory constraints separately; and
- ♦ 7. overlay firm limits and management buffers.

Fictional Case 3 — standardized/IRB sensitivity, not a capital conclusion

Nordbank holds a EUR 100 million fictional corporate exposure. For teaching only, the standardized treatment produces a 100% risk weight; an approved IRB calculation produces EUR 62 million of RWA before the output-floor calculation. Ignore credit conversion, mitigation, expected-loss deductions and all other exposures.

Calculation 39.2 — exposure-level RWA sensitivity

Standardized RWA contribution = $100\text{m} \times 100\%$ = EUR 100m. Illustrative IRB RWA contribution = EUR 62m.
Difference = EUR 38m.

Applying 8% to those numbers would yield EUR 8.00 million and EUR 4.96 million, but neither is the bank's required or allocated capital. The full institution stack, output floor, Pillar 2, buffers, deductions, stress, leverage and internal allocation remain unmodeled.

Table 39.5 — separate prudential questions

Measure	Numerator/denominator concept	What it asks	Why it differs from the others
Standardized credit RWA	prescribed exposure and risk-weight framework	rule-based credit-risk contribution	does not use the bank's IRB result
IRB credit RWA	approved risk parameters and formulas	modeled credit-risk contribution	subject to permission, input floors and output floor
Large exposure	exposure value relative to eligible capital base	single-name/group concentration	not a risk-weighted capital percentage
Leverage ratio	Tier 1 capital relative to exposure measure	non-risk-based balance-sheet constraint	exposure measure differs from RWA
Liquidity metrics	eligible liquid resources and cash-flow assumptions	short/longer-horizon liquidity resilience	not a credit-loss measure
Stress result	losses/capital/liquidity under scenario	resilience under adverse path	scenario- and governance-dependent

Capital-stack illustration

Assume the institution has EUR 1.20 billion total RWA after all applicable calculations. For teaching only, use an 8.0% Pillar 1 total-capital minimum, a 2.5% capital-conservation buffer and a fictional 1.5% selected institution-specific requirement. Exclude other buffers, quality composition, management margin and restrictions.

Calculation 39.3 — incomplete but reconciled stack

Pillar 1 amount = $1,200\text{m} \times 8.0\%$ = EUR 96m. Conservation-buffer amount = $1,200\text{m} \times 2.5\%$ = EUR 30m. Fictional institution-specific amount = $1,200\text{m} \times 1.5\%$ = EUR 18m. Displayed stack = $96 + 30 + 18$ = EUR 144m, or 12.0% of RWA.

Table 39.6 documents what is missing.

Layer	Included?	Live - file question
Pillar 1 minimum	simplified	composition by CET1, Tier 1 and total capital?
Pillar 2 requirement	fictional proxy	actual SREP decision and capital - quality split?
capital - conservation buffer	simplified	current scope and consequence?
countercyclical/systemic buffers	no	which rates and consolidation levels apply?
Pillar 2 guidance/management margin	no	confidential expectation and internal target?
deductions/distributions restrictions	no	available own funds and stack interaction?

The illustration teaches reconciliation, not a "12% rule."

5. Output floor: aggregate, transitional and often misunderstood

The output floor constrains the benefit from internal models by comparing the institution's aggregate risk-weighted exposure amount with a percentage of the standardized-based amount. It is not calculated as a separate floor on each leveraged loan. CRR3 provides a transitional factor of **55% for 1 January to 31 December 2026**; the operative text and all adjustments must be checked for the institution.

Fictional Case 4 — aggregate output-floor effect

Bank Arco has, after the relevant aggregation and adjustments in this deliberately simplified example:

- ♦ • pre-floor total RWA under internal-model calculations: EUR 480 million;
- ♦ • standardized-based aggregate amount for floor purposes: EUR 1.00 billion; and
- ♦ • 2026 transitional factor: 55%.

Calculation 39.4 — aggregate floor

Floor amount = $1,000\text{m} \times 55\%$ = EUR 550m. Post-floor RWA = $\max(480\text{m}, 550\text{m})$ = EUR 550m. Uplift = $550\text{m} - 480\text{m}$ = EUR 70m, or 14.58% of 480m.

If pre-floor RWA were EUR 600 million, the EUR 550 million floor would not bind. Allocating the EUR 70 million uplift to businesses or facilities is a management methodology; it does not turn the aggregate legal calculation into a per-loan statutory floor.

Table 39.7 — output-floor controls

Control	Required record
perimeter	entities and consolidation level in both sides of the comparison
date	applicable transitional factor and effective rules
standardized base	complete standardized - based calculation and permitted adjustments
internal - model amount	approved approaches and current model permissions
aggregation	credit, market, operational and other relevant components
management allocation	clearly labelled internal attribution, separate from legal calculation

6. Underwriting, distribution and final hold

A financing changes risk state over time. An arranger may approve an underwriting commitment larger than its intended final hold. Regulatory and internal limits must follow the actual and contingent exposure, not the marketing plan.

Fictional Case 5 — sell-down shortfall

Europa Bank underwrites EUR 600 million for Lumen Health and intends to retain EUR 90 million. At signing it expects to distribute EUR 510 million. At funding, investor orders support only EUR 390 million at acceptable terms, leaving a EUR 210 million hold.

Unexpected hold = 210m – 90m = EUR 120m. Sell-down achieved = 390m / 510m = 76.47% of planned distribution.

This is **Calculation 39.5**. The bank must assess underwriting and syndication risk, limits, valuation, funding, liquidity, concentration, capital and escalation at each stage. The 76.47% number does not prove a breach or a capital amount.

Table 39.8 — exposure-state control

Stage	Exposure question	Evidence	Governance response
mandate	what commitment may arise?	mandate and approval terms	approve capacity and risk appetite
underwriting	what is legally committed and conditional?	executed commitment documents	reserve limit, funding and distribution capacity
syndication	what has investors' legally reliable support?	allocations and conditions	track concentration, price and execution risk
funding	what must the bank fund now?	utilisation/funding notice	reconcile actual exposure and liquidity
settlement	which transfers are legally effective?	agent/register and cash evidence	do not count unsettled intentions as completed sell-down
final hold	what remains after effective distribution?	position and exposure systems	capital, concentration, monitoring and hedging review

Distribution can move exposure to another regulated actor; it does not make risk disappear from the financial system. A transaction-level claim that "regulation caused the sell-down" requires evidence separating capital, liquidity, risk appetite, pricing, investor demand and document constraints.

Diagram B — underwriting risk over time

Approved mandate

-> committed underwriting

-> funded exposure

-> allocated but unsettled distribution

-> legally settled sell-down

-> final hold

At every arrow: amount, legal status, counterparty, liquidity, capital, concentration, valuation and escalation are re-tested.

7. Large exposures, leverage and liquidity are separate gates

Suppose a bank records EUR 135 million of large-exposure value to a connected client group and has EUR 900 million of the relevant eligible capital measure. The teaching ratio is $135 / 900 = 15.0\%$. That is **Calculation 39.6**, not a compliance conclusion: aggregation, exemptions, mitigation, trading-book treatment, eligible-capital definition and the current legal limit must be verified.

The same financing can be acceptable under modeled credit RWA yet fail an internal single-name limit. It can fit a large-exposure test yet create leverage-ratio pressure because the leverage ratio is non-risk-based. It can fit both and still strain liquidity because underwriting cash outflow precedes distribution. These are different denominators and different risk questions.

8. AIF/private credit and CLOs: different regulation, not no regulation

Directive (EU) 2024/927 amended AIFMD, including provisions for loan-originating AIFs. Its text sets commitment-method leverage limits of **175% of NAV for an open-ended loan-originating AIF** and **300% for a closed-ended loan-originating AIF**, subject to definitions, exclusions, transition, competent-authority powers and national implementation. See Directive (EU) 2024/927 (<https://eur-lex.europa.eu/eli/dir/2024/927/oj>). This chapter does not state the operative outcome in any Member State.

For a fictional closed-ended loan-originating AIF with EUR 240 million NAV and EUR 660 million commitment-method exposure:

Leverage ratio = $660 / 240 = 275\%$.

This **Calculation 39.7** is below 300% arithmetically, but it does not establish compliance: classification, exposure methodology, exclusions, implementation, transition, fund documents and authority measures remain to be tested.

A CLO is different again. EU Regulation 2017/2402 defines a securitisation through tranching credit risk and establishes a framework including due diligence, risk retention and transparency for specified parties. See the EU Securitisation Regulation (<https://eur-lex.europa.eu/eli/reg/2017/2402/oj>). A CLO also operates under its indenture, collateral eligibility, concentration, coverage and other transaction tests. A bank exposure to a CLO, an AIF purchase of a loan and a CLO purchase of the same loan can therefore produce different regulatory and document analyses.

Table 39.9 — bank/AIF/CLO comparison

Dimension	Bank	Loan - originating AIF/private - credit vehicle	CLO
governing perimeter	banking law, supervision and permissions	AIFM/AIF law, implementation and fund terms	securitisation law, vehicle and transaction documents
capital/leverage lens	own funds, RWA, leverage and buffers	AIF leverage and risk/liquidity framework where in scope	tranche, coverage and regulatory treatment for parties/investors
origination/underwriting	credit and syndication governance	origination definition, policies and portfolio rules	often acquisition subject to collateral eligibility; facts control
concentration	prudential and internal single - name/group limits	fund law, risk management and mandate limits	indenture concentration and portfolio tests plus applicable law
liquidity	regulatory liquidity plus funding plan	open/closed structure and liquidity - management requirements	liability and reinvestment structure, asset cash flows and tests
distribution	underwriting/sell - down and conduct controls	transfer, retention and originate - to - distribute questions where applicable	issuance, risk retention, disclosure and investor diligence

9. Bounded UK comparison

The UK comparison is methodological. A UK bank must be analysed under current UK legislation, the PRA Rulebook, permissions, supervisory statements and institution-specific requirements. The PRA describes its supervisory approach as judgment-based and forward-looking; consult the PRA approach to banking supervision (<https://www.bankofengland.co.uk/prudential-regulation/publication/pras-approach-to-supervision-of-the-banking-and-insurance-sectors>) and the PRA Rulebook (<https://www.prarulebook.co.uk/>).

Do not import the ECB 4.0x identification or 6.0x exceptional-leverage reference into a UK file as if it were a universal PRA rule. Equally, absence of that exact metric does not mean absence of prudential constraint. The UK file should identify the applicable credit-risk approach, capital stack, concentration, leverage, liquidity, stress, underwriting governance and firm policy from current sources. This chapter makes no claim that the PRA imposes one market-wide leverage multiple.

Table 39.10 — EU/ECB versus UK review file

Question	EU/ECB file	UK file
legal base	current CRR plus applicable CRD implementation	current UK legislation and PRA rules
supervisor	ECB and/or competent national authority as applicable	PRA, with other authorities where relevant
leveraged-finance guidance	test ECB guidance perimeter and institution policy	identify applicable PRA materials and firm policy; do not import ECB ratio automatically
internal models	EU permissions and CRR3 framework	UK permissions and current UK framework
institution-specific layer	SREP/Pillar 2 decisions and internal margin	PRA supervisory requirements and internal margin
conduct/distribution	EU conduct/product rules by actor and product	FCA/PRA perimeter by actor and product

10. Conduct, distribution and national implementation limits

Prudential acceptability does not decide whether a product may be offered to a client, whether information is properly disclosed, or whether a conflict is managed. Conduct rules attach to the service, instrument, firm and client classification. Securitisation diligence attaches to specified parties and positions. Fund rules attach to the AIFM/AIF perimeter. Market-abuse and confidentiality controls can constrain syndication and secondary trading, as discussed in Chapter 38.

For any directive, the practitioner records:

- ♦ • publication, transposition deadline and relevant application dates;
- ♦ • national implementing measure and competent authority;
- ♦ • available options, thresholds, grandfathering and transition;
- ♦ • entity, consolidation and product perimeter; and
- ♦ • whether the proposition is law, guidance, policy or an assumption.

Because this chapter excludes national modules, any point whose answer depends on a Member State is marked **local implementation required** rather than guessed.

11. Exercises and answer checks

Exercise 39.A — classify the source

A bank credit paper says, “The borrower is prohibited from exceeding 6.0x because ECB law caps leverage.” Correct the statement.

Answer check: The ECB's 2017 guidance says in-scope institutions should treat transactions above 6.0x Total Debt/EBITDA at inception as exceptional, justified and escalated. It is not a statutory borrower ceiling or covenant definition. Confirm the institution perimeter, controlled debt/EBITDA definitions and internal policy.

Exercise 39.B — aggregate output floor

In 2026, simplified pre-floor aggregate RWA is EUR 720 million and the standardized-based amount is EUR 1.40 billion. Use 55%.

Answer check: $1,400 \times 55\% = \text{EUR } 770\text{m}$; post-floor RWA is $\max(720, 770) = \text{EUR } 770\text{m}$; uplift is EUR 50 million. Do not assign the result mechanically to one loan.

Exercise 39.C — perimeter map

The same EUR 30 million loan is considered by an EU bank, a loan-originating AIF and a CLO. List the first three different questions for each.

Answer check: Bank: exposure treatment/approach, concentration, capital/liquidity/underwriting policy. AIF: loan-originating classification, implementation and leverage/liquidity/mandate rules. CLO: collateral eligibility and transaction tests, securitisation duties/retention/diligence perimeter, settlement and concentration. “The AIF and CLO are unregulated” fails.

Appendix 39.A — primary-source register

Reviewed 12 July 2026; live work must recheck status and amendments.

- ♦ 1. ECB, Guidance on leveraged transactions (May 2017) (https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.leveraged_transactions_guidance_201705.en.pdf) — supervisory identification, governance and syndication expectations for stated perimeter.
- ♦ 2. Regulation (EU) 2024/1623 (CRR3) (<https://eur-lex.europa.eu/eli/reg/2024/1623/oj>) — official amending regulation, including output-floor implementation.
- ♦ 3. Directive (EU) 2024/1619 (CRD6) (<https://eur-lex.europa.eu/eli/dir/2024/1619/oj>) — official directive; national implementation must be checked.
- ♦ 4. Directive (EU) 2024/927 (AIFMD amendment) (<https://eur-lex.europa.eu/eli/dir/2024/927/oj>) — loan-origination provisions; implementation, transition and perimeter required.
- ♦ 5. Regulation (EU) 2017/2402 (<https://eur-lex.europa.eu/eli/reg/2017/2402/oj>) — EU securitisation framework, subject to amendments and actor-specific scope.
- ♦ 6. PRA, Approach to supervision (<https://www.bankofengland.co.uk/prudential-regulation/publication/pras-approach-to-supervision-of-the-banking-and-insurance-sectors>) — official supervisory orientation.
- ♦ 7. PRA Rulebook (<https://www.prarulebook.co.uk/>) — current UK rule source; identify the exact firm, rule and date.

Appendix 39.B — jurisdiction and perimeter matrix

File field	EU/ECB entry	UK entry	Evidence status
legal entity and group	institution and consolidation perimeter	PRA - authorised entity and group	required
competent authority	ECB/NCA allocation	PRA and any relevant FCA perimeter	required
legal rules	current CRR and national CRD implementation	current UK legislation/PRA rules	required
supervisory guidance	ECB guidance if in scope	applicable PRA supervisory material	required
Pillar 2	current SREP decision	current institution - specific PRA requirement	confidential specialist input
credit - risk method	standardized/IRB permission and conditions	current UK method/permission	required
output floor	aggregate CRR3 calculation and transition	current UK implementation and transition	separate calculations
concentration	large - exposure and internal limits	UK rules and internal limits	required
leverage/liquidity	applicable EU measures and policy	applicable UK measures and policy	separate gates
product/actor interfaces	AIF, CLO, conduct, securitisation	UK fund, conduct and securitisation perimeter	specialist review
national/local point	local implementation required	not an EU national module	do not infer

The matrix deliberately ends with evidence status. A regulatory proposition without the correct entity, product, source and date is not ready for credit approval or publication.

Interest-Limitation Rules in Leveraged Finance

Educational and tax boundary. *This independently written chapter was checked against public primary or governmental sources on 12 July 2026. It is an orientation for credit modelling, not tax advice, a tax return, a legal opinion or a structuring recommendation. It covers only the common EU baseline in Article 4 of the Anti-Tax Avoidance Directive (ATAD), the UK Corporate Interest Restriction (CIR), and a bounded comparison with U.S. Internal Revenue Code Section 163(j). Domestic law, elections, entity classification, consolidation, tax attributes and facts can change every result. A qualified tax adviser must own the actual computation and advice for every affected entity and period.*

Interest expense in a lender model is not the same thing as deductible interest in a tax computation. The first is normally a contractual cash-flow amount. The second is a legal and tax result produced by a particular rule, taxpayer, group, period and set of elections. A leveraged-finance practitioner should therefore model a range of possible cash-tax consequences without claiming to determine the tax return.

This chapter does not compare acquisition structures or holding jurisdictions. It does not recommend where debt should sit, describe treaty access, price related-party debt, determine beneficial ownership, calculate Pillar Two liabilities, or conclude that a deduction is available. Those subjects require a separate, expressly scoped and adviser-led workstream.

40.0 Learning objectives

By the end of this chapter, the reader should be able to:

- ♦ 1. separate book interest, cash interest, tax-interest and deductible interest in a controlled model;
- ♦ 2. explain the ATAD Article 4 baseline without treating it as the law of every Member State;
- ♦ 3. build a preliminary UK CIR screen while preserving the de minimis, debt-cap, group-ratio, carryforward and allocation questions for advisers;
- ♦ 4. compare the high-level U.S. Section 163(j) formula with the EU and UK approaches without asserting equivalence;
- ♦ 5. translate possible interest disallowance into cash tax, liquidity, covenant headroom and debt-service sensitivities;
- ♦ 6. prepare an evidence pack and question list that allows qualified tax advisers to complete the actual analysis; and
- ♦ 7. communicate tax uncertainty to a credit committee without presenting a teaching proxy as a filed result.

40.1 Controlled vocabulary

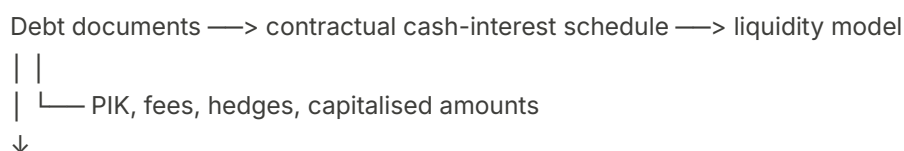
The terms below are educational labels. The applicable legislation and adviser-approved computation control.

Term	Meaning in this chapter	Modelling control
Book interest	Finance expense recognised in the selected financial statements	Reconcile non-cash and capitalised items
Cash interest	Contractual interest paid during the model period	Check payment dates, hedging and PIK components
Tax-interest	A jurisdiction-defined measure used in an interest-limitation computation	Never equate mechanically to book or cash interest
Deductible interest	Interest or similar expense allowed as a deduction for the relevant taxpayer and period after applicable rules	Adviser-owned output
Exceeding borrowing costs	ATAD term broadly comparing deductible borrowing costs with taxable interest or economically equivalent revenue	Article 2 and domestic implementation control
Tax EBITDA	A tax-law-derived earnings measure used in a limitation, not financial-statement EBITDA	Build from the tax computation, not the credit model
Interest capacity	A modelled or statutory amount against which relevant net interest is compared	Label whether it is a proxy or legal result
Disallowed interest	Amount not deducted in the current period because of a limitation	It may not equal a permanent cash cost
Carryforward	A tax attribute potentially available in a later period under specified conditions	Track owner, expiry, continuity and utilisation conditions
Group ratio	A rule that may use a group's external financing relationship to earnings	Method, election and definitions differ by regime
Debt cap	An additional ceiling linked to a measure of group financing expense	Do not infer it from gross debt alone
ATAD	Council Directive (EU) 2016/1164, as amended, setting minimum anti-avoidance rules	Member-State implementation determines the domestic result
CIR	The UK's Corporate Interest Restriction in Part 10 TIOPA 2010	HMRC guidance is useful but legislation and current advice control
Adjusted taxable income (ATI)	The U.S. Section 163(j) tax base after statutory adjustments	It is not automatically accounting EBIT or EBITDA
Business interest income	U.S. statutory category of interest income properly allocable to a trade or business	Section 163(j) definitions and regulations control
Floor plan financing interest	A specific U.S. statutory category included in the Section 163(j) limitation formula	Do not generalise beyond its definition
Permanent difference	Tax treatment that is not expected to reverse in a later period	Distinguish from a timing difference and uncertain attribute
Cash-tax sensitivity	A scenario showing how an assumed deduction changes tax paid	Use an explicit assumed tax rate, not a jurisdiction conclusion

40.2 Three ledgers, one reconciliation

A useful credit model keeps contractual cash, accounting presentation and tax treatment in separate ledgers. The reconciliation matters more than the label.

Figure 40.1 — Interest data flow



Financial statements —> book finance expense
 |
 ↓
 Entity tax computations —> tax-interest and tax-earnings measures
 |
 ↓
 Applicable limitation —> current deduction / disallowance / attribute
 |
 └─> cash-tax and credit sensitivity

Table 40.1 — Minimum interest reconciliation

Line	Model question	Evidence owner
Gross contractual interest	Which instrument, entity, currency and period?	Treasury / finance
Cash versus PIK	What is actually paid and when?	Debt schedule
Fees and economically similar amounts	Which amounts enter accounting or tax measures?	Accounting and tax
Hedge receipts/payments	Are they included, excluded or separately treated?	Treasury and tax
Interest income	Which entity earns it and how is it classified?	Tax
Tax - interest expense	What does the applicable regime include?	Tax adviser
Tax earnings base	Which statutory adjustments apply?	Tax adviser
Current - period deduction	Which cap, exemption, election or allocation applies?	Tax adviser
Carryforward attribute	Who owns it and what controls later use?	Tax adviser

The practitioner should not start with consolidated EBITDA and multiply it by 30%. Consolidated EBITDA may include earnings from entities outside the tax perimeter, accounting adjustments absent from tax EBITDA, or value that cannot support the taxpayer claiming the deduction. The apparent simplicity of a percentage does not remove perimeter risk.

Synthetic example 1 — ledger mismatch. Alder Components Group records EUR 62 million of consolidated finance expense. The cash schedule shows EUR 55 million paid, EUR 4 million PIK and EUR 3 million of fee amortisation. The tax team identifies a different provisional tax-interest number after entity, hedge and classification adjustments. The credit analyst uses EUR 55 million in the current cash bridge, the accounting amount in the reporting reconciliation, and an adviser-provided range in the cash-tax model. None of the three is silently substituted for another.

40.3 The EU ATAD baseline

Article 4 of ATAD establishes an interest-limitation rule for taxpayers within its scope. At a high level, exceeding borrowing costs are deductible up to 30% of the taxpayer's EBITDA as defined for the rule. Article 4 also contains options and parameters concerning a monetary threshold, taxpayer treatment within a group, standalone entities, financial undertakings, infrastructure projects, carryforwards or carrybacks, and group-based tests. The directive is a minimum framework, not a uniform tax computation for every Member State.

The authoritative starting point is Council Directive (EU) 2016/1164, Article 4, EUR-Lex (<https://eur-lex.europa.eu/eli/dir/2016/1164/oj/eng>), checked 12 July 2026. A live analysis must then use the current domestic

implementing law, administrative material and advice for each relevant taxpayer. This chapter intentionally adds no Member-State module.

Table 40.2 — ATAD baseline versus domestic answer

Question	What the directive provides at framework level	What remains domestic/adviser work
Taxpayer perimeter	Rule applies to taxpayers within the directive's scope	Entity, fiscal unity/grouping and permanent-establishment treatment
Interest measure	Exceeding borrowing costs concept	Detailed inclusions, exclusions and ordering
Earnings base	Tax-adjusted EBITDA concept in Article 4	Domestic tax starting point and adjustments
Percentage	30% baseline	Implemented options and interaction with other rules
Threshold	Directive permits a safe-harbour amount up to the specified level	Whether and how adopted
Group relief	Directive contains group-related options	Domestic elections, tests and evidence
Carryforward	Directive permits specified approaches	Actual duration, ownership and utilisation
Exceptions	Directive addresses selected taxpayers/projects	Domestic scope and conditions

Worked calculation 1 — ATAD-style baseline screen

Assume a fictional taxpayer has EUR 180 million of a teaching proxy for tax EBITDA and EUR 75 million of a teaching proxy for exceeding borrowing costs. Ignore every domestic option, threshold, group rule and other tax provision solely to show the arithmetic.

Baseline capacity = 30% × EUR 180m = EUR 54m

Screened excess = EUR 75m – EUR 54m = EUR 21m

The EUR 21 million is not a domestic disallowance. It is a question routed to local tax advisers. They must replace both proxy inputs, confirm the law and determine any threshold, exemption, group treatment, carryforward and interaction.

Worked calculation 2 — sensitivity to tax earnings

Keep the EUR 75 million interest proxy but vary the tax-EBITDA proxy.

Proxy tax EBITDA (EURm)	30% screen (EURm)	Amount above screen (EURm)
220	66	9
180	54	21
140	42	33
100	30	45

This table demonstrates procyclicality: if the earnings measure falls while financing cost remains fixed, the screened excess grows. It does not predict deduction, carryforward utilisation or tax paid.

Synthetic example 2 — perimeter first. Birch Services has EUR 210 million of consolidated credit-model EBITDA, but only EUR 145 million sits in the provisional taxpayer perimeter supplied by advisers. A 30% calculation on EUR 210 million produces EUR 63 million; the same arithmetic on EUR 145 million produces EUR 43.5 million. The EUR

19.5 million gap is not a tax planning opportunity. It is evidence that the model needs an entity-to-tax-perimeter bridge before it can inform liquidity.

40.4 UK Corporate Interest Restriction orientation

The UK CIR applies through a worldwide-group framework using UK tax measures and specified group-account measures. HMRC's overview describes a GBP 2 million annual de minimis, the default fixed-ratio method, a 30% relationship to aggregate tax-EBITDA, and a fixed-ratio debt cap. It also describes an elective group-ratio method, reactivation of restricted interest, and the limited carryforward period for unused interest allowance. The full rules contain definitions, elections, allocation and administration that a teaching screen cannot resolve.

Current governmental orientation is in HMRC Corporate Finance Manual CFM95140 (<https://www.gov.uk/hmrc-internal-manuals/corporate-finance-manual/cfm95140>), updated 14 November 2025 and checked 12 July 2026. Carryforward terminology is summarised in CFM98220 (<https://www.gov.uk/hmrc-internal-manuals/corporate-finance-manual/cfm98220>). The legislation and qualified UK tax advice control.

Table 40.3 — UK CIR workpaper layers

Layer	Preliminary model field	Why adviser confirmation matters
Worldwide group	Ultimate parent, consolidation perimeter, period	Statutory group and period definitions apply
UK group companies	Entity list and UK tax status	Membership and periods can differ from credit perimeter
Aggregate net tax - interest expense	Entity tax - interest income and expense	Tax definitions, ordering and allocations apply
Aggregate tax - EBITDA	Entity - level tax amounts and adjustments	It is not consolidated adjusted EBITDA
De minimis	Annualised group amount	Period length and group application matter
Fixed - ratio amount	30% proxy	Debt cap can be lower
Debt cap	Adviser - provided ANGIE - based computation	Cannot be inferred from loan interest alone
Group - ratio method	Election flag and adviser output	QNGIE, group EBITDA and related definitions apply
Attributes	Disallowed amounts and unused allowance by period	Different carryforward rules and conditions apply
Allocation	Company - by - company restriction/reactivation	Reporting company and return mechanics apply

Worked calculation 3 — simplified UK fixed-ratio screen

Assume a fictional UK group has provisional aggregate net tax-interest expense of GBP 48 million, aggregate tax-EBITDA of GBP 120 million and an adviser-provided fixed-ratio debt cap of GBP 41 million. Ignore brought-forward capacity and all other adjustments for this screen.

30% amount = $30\% \times \text{GBP } 120\text{m} = \text{GBP } 36\text{m}$

Preliminary basic interest allowance = lower of GBP 36m and GBP 41m = GBP 36m

Amount above preliminary allowance = $\text{GBP } 48\text{m} - \text{GBP } 36\text{m} = \text{GBP } 12\text{m}$

The GBP 2 million de minimis is not added to the GBP 36 million. HMRC explains it as a minimum level below which net tax-interest expense does not produce a restriction; actual application and the complete interest allowance

computation belong in the adviser workpaper. The GBP 12 million is therefore a provisional downside input, not a filed restriction.

Worked calculation 4 — debt-cap downside

Use the same GBP 48 million net tax-interest expense and GBP 120 million aggregate tax-EBITDA, but suppose advisers calculate the fixed-ratio debt cap at GBP 28 million.

Percentage amount = GBP 36m

Preliminary basic interest allowance = lower of GBP 36m and GBP 28m = GBP 28m

Amount above preliminary allowance = GBP 20m

The second limit changes the screened amount by GBP 8 million. A credit model that applies only 30% of tax EBITDA would miss this downside.

Synthetic example 3 — forecast volatility. Cedar Health's acquisition model shows stable accounting EBITDA, but its provisional UK tax-EBITDA bridge is lower in Year 2 because of tax-specific items identified by advisers. Rather than overwrite the credit forecast, the team adds a separate tax-base sensitivity and asks the tax adviser to confirm the statutory treatment. The credit paper reports a cash-tax range and identifies the unconfirmed bridge as an open condition.

40.5 Bounded U.S. Section 163(j) contrast

Section 163(j) limits the business-interest deduction, subject to statutory definitions, exceptions and entity-specific rules. In simplified form, the statutory ceiling combines three components: 30% of ATI, any business interest income, and any floor plan financing interest. Disallowed business interest may be carried forward under the statute, with special rules for partnerships and S corporations and exceptions for specified businesses or taxpayers.

Use the current text of 26 U.S.C. §163 (<https://uscode.house.gov/view.xhtml?req=%28title%3A26+section%3A163+edition%3Aprelim>) and the IRS Section 163(j) questions and answers (<https://www.irs.gov/newsroom/questions-and-answers-about-the-limitation-on-the-deduction-for-business-interest-expense>), both checked 12 July 2026. The IRS page records recent statutory changes affecting ATI and ordering for tax years beginning after specified dates. A live model must fix the taxpayer's tax year and use current U.S. tax advice; this chapter does not generalise across historical periods.

Table 40.4 — Bounded comparison, not equivalence

Field	ATAD common baseline	UK CIR orientation	U.S. Section 163(j) orientation
Core earnings relationship	30% of rule-defined EBITDA	Default fixed - ratio relationship to aggregate tax - EBITDA	30% of ATI within statutory sum
Interest income	Embedded in exceeding borrowing costs concept	Tax - interest income/expense measures	Business interest income is a stated component
Additional cap	Domestic options and implementation	Fixed or group - ratio debt cap	Floor plan financing interest is a stated component, not a debt cap
Group treatment	Domestic implementation/options	Worldwide - group and UK - group framework	Taxpayer/entity rules, including special partnership/S corporation treatment
Threshold/exception	Directive permits options	De minimis and other statutory provisions	Gross - receipts and specified trade/business provisions, among others
Carryforward	Domestic implementation	Multiple attribute concepts and time rules	Statutory disallowed - interest carryforward subject to applicable rules

Worked calculation 5 — Section 163(j) formula screen

Assume fictional U.S. taxpayer Delta Manufacturing has USD 45 million of business interest expense, USD 3 million of business interest income, USD 100 million of ATI and no floor plan financing interest.

Preliminary limitation = USD 3m + (30% × USD 100m) + USD 0m = USD 33m

Amount above preliminary limitation = USD 45m – USD 33m = USD 12m

This result assumes the limitation applies and omits taxpayer classification, exceptions, other tax provisions, carryforwards and detailed regulations. It is a model screen only.

Synthetic example 4 — date control. Delta's five-year model originally uses one ATI definition for every period. The tax adviser notes that statutory changes apply from different tax-year start dates. The analyst versions the ATI bridge by period and adds an explicit "law/current advice" input instead of hard-coding a permanent financial-statement proxy.

40.6 From disallowance screen to cash-tax risk

A screened interest excess affects credit only through an explicit bridge. The model needs an assumed tax rate, taxable-profit base, timing, attributes, payments and entity cash access. A disallowance can increase current tax, create or enlarge an attribute, or interact with losses and other rules. This chapter models only a conservative current-cash illustration.

Worked calculation 6 — cash-tax sensitivity

Assume a fictional entity has EUR 70 million of taxable profit before relevant interest, EUR 45 million of interest expense, and a purely synthetic 25% tax rate. Compare full current deduction with a scenario in which only EUR 36 million is currently deducted.

Line	Full-deduction case (EURm)	Limited-deduction case (EURm)
Profit before interest	70.00	70.00
Current interest deduction	(45.00)	(36.00)
Simplified taxable amount	25.00	34.00
Tax at assumed 25%	6.25	8.50
Incremental current cash tax	—	2.25

Incremental cash tax = (EUR 45m – EUR 36m) × 25% = EUR 2.25m

No jurisdictional tax rate or deduction is asserted. If the EUR 9 million difference may be carried forward, the model separately records a potential attribute but gives it no liquidity value until advisers confirm ownership, timing and utilisation evidence.

Table 40.5 — Credit transmission channels

Tax uncertainty	Immediate model effect	Secondary credit question
Lower current deduction	Higher cash tax	Minimum-liquidity and revolver headroom
Delayed attribute use	Later tax benefit than base case	Discounted value and refinancing horizon
Lower tax earnings	Smaller percentage-based screen	Downside procyclicality
Debt-cap constraint	Capacity below percentage amount	External financing and group-perimeter dependency
Entity mismatch	Deduction and cash arise in different places	Cash access and debt service
Adviser or filing delay	Uncertain payment timing	Cash reserve and reporting covenant process

Synthetic example 5 — covenant bridge. Elm Distribution has EUR 18 million of base-case minimum liquidity and EUR 7 million of headroom above its internal minimum. A tax sensitivity adds EUR 3 million of current cash tax and EUR 2 million of professional and compliance contingency across two periods. Headroom falls to EUR 2 million. The committee does not call the tax outcome determined; it records that the financing has little capacity to absorb an adverse adviser conclusion.

40.7 Scenario design and governance

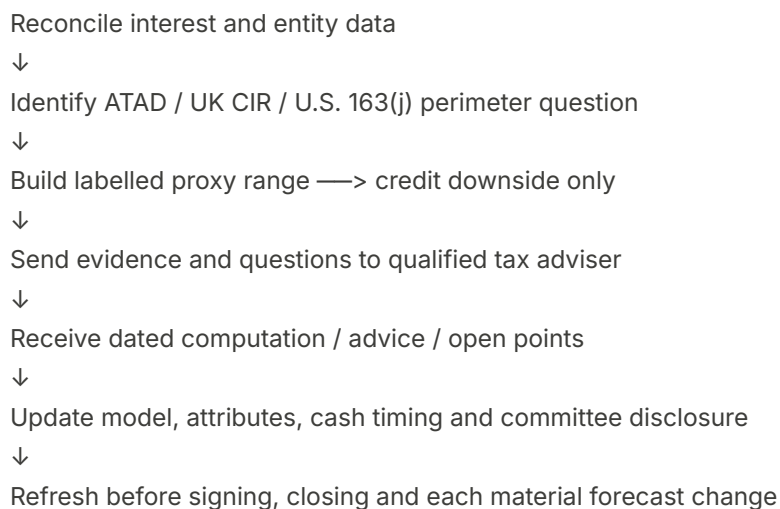
Tax uncertainty should not be hidden in a single “tax rate” cell. Use at least three scenarios:

Table 40.6 — Scenario architecture

Scenario	Deduction assumption	Attribute assumption	Credit use
Adviser-informed base	Latest confirmed computation or bounded estimate	Only evidenced use within forecast	Underwriting base
Conservative delay	Lower current deduction or later utilisation	No benefit before confirmed date	Liquidity and covenant downside
Severe/perimeter break	Materially lower capacity and no near-term attribute value	Zero within financing horizon	Survival and refinancing test

Each scenario should state which input is law, adviser conclusion, management forecast or analyst assumption. If no adviser work exists, the base case cannot be presented as tax-confirmed.

Figure 40.2 — Decision and escalation flow



40.8 What this chapter excludes

Interest-limitation analysis is not a substitute for the rest of tax diligence. The following are routing flags only.

Table 40.7 — Excluded subjects and routing

Subject	Why it is excluded here	Required owner
Transfer pricing and debt capacity	Requires accurate delineation, functional analysis and current law	Qualified transfer-pricing/tax adviser
Withholding tax and beneficial ownership	Depends on payment, recipient, treaty/directive, domestic anti-abuse and facts	Relevant jurisdiction tax counsel
Acquisition debt push-down	Structure- and jurisdiction-specific; no result follows from a label	Transaction tax counsel
Hybrids and entity classification	Instrument/entity treatment can differ across regimes	Cross-border tax counsel
Tax groups and losses	Formation, continuity and utilisation are local-law questions	Domestic tax adviser
Pillar Two	Jurisdictional GloBE calculations and charging rules exceed this module	Pillar Two specialist
VAT and fee recovery	Supply, recipient and use require separate analysis	Indirect-tax adviser
GAAR and anti-abuse	Legal conclusion based on facts, purpose and law	Qualified tax counsel

The model may include a reserve or sensitivity for an excluded subject only if its source and status are stated. It must not convert that reserve into a structuring recommendation.

40.9 Adviser evidence pack

The most useful practitioner output is a reconciled, question-led pack rather than a proposed tax answer.

Table 40.8 — Minimum adviser request

Pack component	Required fields
Entity map	Legal entity, residence, ownership, borrower/guarantor role and tax status
Debt map	Creditor, debtor, principal, currency, rate, cash/PIK, fees and maturity
Interest reconciliation	Book, cash and provisional tax - interest by entity and period
Earnings bridge	Credit EBITDA to provisional tax measure, with each adjustment sourced
Group/perimeter file	Accounting group, tax group and regime - specific perimeter
Forecast	Base and downside tax earnings, interest, losses and material transactions
Attributes	Opening disallowed interest/allowance/losses, owner, vintage and evidence
Questions	Applicable law/date, elections, caps, exceptions, allocation and filing timing
Deliverable	Dated calculation, assumptions, open points, sensitivity and accountable reviewer

40.9.1 Change control after the first adviser output

A confirmed computation is not permanent. The credit team should reopen the tax workpaper when the debt amount, rate, instrument, borrower, acquisition perimeter, forecast tax earnings, accounting group, tax year, ownership or applicable law changes. The change log should show the prior input, revised input, reason, model effect, adviser notified, adviser response and approval date.

Version control is particularly important when a commitment paper is based on an indicative financing but the final capital structure includes a different term loan, revolving facility, PIK instrument or hedge. An old tax conclusion should not be copied forward merely because the total debt number looks similar. Classification and entity placement may matter even when gross leverage is unchanged.

The committee file should also identify the horizon covered by advice. A closing-date computation may not support a five-year forecast if interest rates, earnings, group attributes or statutory definitions vary. For each forecast period, record whether the tax line is adviser-confirmed, mechanically rolled forward, or independently stressed. Mechanically rolled figures must remain visibly provisional.

Table 40.9 — Tax model change triggers

Trigger	Immediate action	Credit output
Debt quantum or pricing changes	Refresh interest reconciliation	Cash tax and liquidity range
Borrower/entity changes	Reopen taxpayer and group perimeter	Entity - level debt - service test
EBITDA downside	Refresh tax - earnings proxy with advisers	Procyclical disallowance case
Acquisition/disposal	Reassess group, periods and attributes	Closing and post - close cases
Law/guidance change	Date - stamp and rerun affected periods	Committee change note
Election/return decision	Replace proxy with authorised computation	Attribute and payment schedule

40.10 Exercises

Exercise 40.1 — find the false precision

A credit paper states: “The group may deduct 30% of consolidated EBITDA under ATAD.” Identify at least five defects.

Answer check. It confuses a directive baseline with domestic law; uses consolidated credit EBITDA rather than rule-defined tax EBITDA; omits taxpayer and group perimeter; ignores exceeding borrowing costs and domestic options; and claims a deduction without adviser analysis. Further defects include date, carryforward, threshold, group test and interaction omissions.

Exercise 40.2 — UK screen

A fictional UK group has GBP 150 million provisional aggregate tax-EBITDA, GBP 54 million aggregate net tax-interest expense and a GBP 38 million adviser-provided fixed-ratio debt cap. Ignore all other items. Calculate the percentage amount, preliminary allowance and amount above it.

Answer check. Thirty per cent of GBP 150 million is GBP 45 million. The lower debt cap gives a preliminary GBP 38 million allowance. The amount above the screen is GBP 16 million. This is not the filed CIR result.

Exercise 40.3 — liquidity translation

Assume a EUR 12 million screened reduction in current deduction, a synthetic 25% tax rate and no attribute value inside the financing horizon. Base minimum-liquidity headroom is EUR 8 million. What is the simplified effect?

Answer check. Incremental current cash tax is EUR 3 million. Headroom falls to EUR 5 million before timing and other effects. The answer is a sensitivity, not tax advice.

Appendix 40.A — Dated source register

Source	Function	Check ed	Use boundary
Council Directive (EU) 2016/1164 (https://eur-lex.europa.eu/eli/dir/2016/1164/oj/eng)	ATAD common framework, especially Article 4	12 July 2026	Not a substitute for domestic implementation
HMRC CFM95140 (https://www.gov.uk/hmrc-internal-manuals/corporate-finance-manual/cfm95140)	UK CIR governmental overview	12 July 2026	Guidance; legislation and advice control
HMRC CFM98220 (https://www.gov.uk/hmrc-internal-manuals/corporate-finance-manual/cfm98220)	UK CIR carryforward terminology	12 July 2026	Do not build a return from the summary
26 U.S.C. §163 (https://uscode.house.gov/view.xhtml?req=%28title%3A26+section%3A163+edition%3Aprelim)	Current statutory text	12 July 2026	Taxpayer, period and regulations still required
IRS Section 163(j) Q&A (https://www.irs.gov/newsroom/questions-and-answers-about-the-limitation-on-the-deduction-for-business-interest-expense)	Governmental orientation and change flags	12 July 2026	Not transaction-specific advice

Appendix 40.B — Committee disclosure template

- ♦ 1. **Perimeter:** entities, periods and regimes screened.
- ♦ 2. **Status:** confirmed adviser output, preliminary adviser range, or analyst proxy.

- ✦ 3. **Inputs:** tax-interest and tax-earnings bridge with source dates.
- ✦ 4. **Base case:** current deduction, cash tax and attribute use included in underwriting.
- ✦ 5. **Downside:** incremental cash tax, timing, liquidity and covenant effect.
- ✦ 6. **Excluded work:** transfer pricing, withholding, structuring, Pillar Two or other modules not completed.
- ✦ 7. **Open evidence:** missing computations, elections, returns or ownership data.
- ✦ 8. **Decision:** reserve, condition, covenant, pricing response or escalation.
- ✦ 9. **Owner and refresh date:** named tax adviser/workstream owner and next update.

The committee should approve the credit exposure, not the tax treatment. Any sentence that predicts a deduction, exemption, treaty outcome or lawful structure must be replaced by a qualified, dated adviser conclusion or removed.

ESG in Leveraged Finance

Teaching, regulatory and claims boundary. *This chapter was independently written from public sources checked on 13 July 2026. It does not provide legal, regulatory, assurance, accounting, environmental, investment or transaction-specific advice. A sustainability label does not establish lower credit risk, additionality, lawful disclosure, Taxonomy alignment, regulatory compliance or a pricing benefit. Every live instrument must be analysed through its executed documents, current data, applicable law and qualified advisers. All companies, amounts and cases below are fictional.*

Environmental, social and governance information matters to leveraged finance when it changes cash flow, capital expenditure, access to markets, documentation, information quality or recovery. The analytical discipline is the same as for any other credit factor: define the claim, identify the perimeter, reconcile the evidence, calculate the consequence and state uncertainty.

This chapter separates three questions that are often blurred:

- ✦ 1. **Instrument mechanics:** what the selected loan or bond documents require and what happens if a metric is or is not achieved.
- ✦ 2. **Corporate credit:** how sustainability-related risks, dependencies and investment affect EBITDA, cash, liquidity and enterprise value.
- ✦ 3. **Regulatory function:** which EU rule addresses which entity, product, disclosure or provider, at which date.

None of those questions can be answered from the letters "ESG" alone.

41.0 Learning objectives

By the end of this chapter, the reader should be able to:

- ✦ 1. distinguish sustainability-linked instruments from use-of-proceeds instruments and trace each claimed effect to documents, data and verification;
- ✦ 2. design a material KPI and sustainability performance target (SPT) with a controlled baseline, perimeter, unit, timetable and restatement policy;
- ✦ 3. calculate margin-ratchet economics and identify incentive, selection and reporting weaknesses without alleging misconduct or intent;
- ✦ 4. map SFDR, the EU Taxonomy, CSRD/ESRS, the European Green Bond regime and the EU ESG-ratings regulation to their distinct addressees and functions;
- ✦ 5. translate transition expenditure and sustainability risks into EBITDA, free cash flow, liquidity, leverage and recovery scenarios;
- ✦ 6. assess ESG-rating, lender, investor and CLO mandate evidence without assuming universal definitions or demand effects; and
- ✦ 7. prepare a claim-and-evidence record suitable for credit committee review and specialist escalation.

41.1 Controlled vocabulary

Term	Educational meaning used here	Control
Sustainability-linked loan (SLL)	Loan whose financial or structural characteristics can vary with achievement of specified sustainability objectives	Executed facility and current principles control
Use-of-proceeds instrument	Financing whose proceeds are allocated to specified eligible projects or assets	Allocation, tracking and reporting are central
KPI	Quantitative or qualitative performance indicator selected for the instrument	Must have definition, source, perimeter and owner
SPT	Calibrated level of performance for a KPI by a specified observation date	Ambition and comparability require evidence
Baseline	Starting value against which performance is evaluated	Record date, perimeter, method and assurance status
Observation date	Date or period at which achievement is measured	Do not confuse with reporting or margin-adjustment date
Margin ratchet	Contractual change in interest margin tied to specified conditions	Direction, size, timing and fallback are document-specific
Absolute metric	Measure expressed as a total quantity, such as tonnes of emissions	Can rise even when intensity improves
Intensity metric	Measure normalised by output, revenue or another denominator	Denominator changes can drive the result
Scope 1 emissions	Direct greenhouse-gas emissions from sources owned or controlled by the reporting undertaking under the selected reporting method	State gases, organisational boundary, method and exclusions
Scope 2 emissions	Indirect greenhouse-gas emissions associated with purchased or acquired energy under the selected reporting method	Identify location-based or market-based treatment and source data
Perimeter	Entities, operations, geographies, scopes and activities included	M&A, disposals and outsourcing can change it
Restatement	Recalculation of baseline or reported data under defined circumstances	Must not be improvised after performance is known
Additionality	Claimed effect beyond what would otherwise have occurred	Requires a counterfactual; a label alone does not prove it
Greenwashing risk	Risk that a sustainability claim is unclear, unsupported, overstated or misleading	Discuss evidence weakness, not presumed intent
External verification	Review performed by an independent qualified provider under an identified scope	Not the same as a financial-statement audit
Taxonomy eligibility	An activity is described within delegated criteria	Eligibility is not alignment
Taxonomy alignment	Claimed satisfaction of applicable substantial-contribution, DNSH, minimum-safeguard and technical criteria	Current criteria and evidence control
Double materiality	ESRS concept considering impacts and financial risks/opportunities under the applicable framework	Reporting conclusion belongs to the undertaking and advisers
SFDR	EU disclosure regime directed principally at financial market participants, financial advisers and financial products	Not a corporate ESG score or SLL label
ESRS	European Sustainability Reporting Standards used under the applicable corporate-reporting framework	Version and effective date must be fixed

Term	Educational meaning used here	Control
European Green Bond (EuGB)	Voluntary designation governed by Regulation (EU) 2023/2631	Not interchangeable with every green bond
ESG rating	Opinion, score or combination concerning an entity, instrument or product's ESG profile or related characteristics under a stated method	Method, date, scope and provider matter
Transition plan	Time-bound plan concerning movement toward stated environmental or other sustainability objectives	A plan is not evidence of delivery or funding capacity
Principal adverse impact (PAI)	SFDR-related disclosure concept for specified adverse sustainability indicators	Do not transplant mechanically into borrower covenants

41.2 Instrument architecture: performance linkage versus proceeds allocation

An SLL links terms to the borrower's performance against selected KPIs and SPTs. The purpose of a use-of-proceeds instrument is different: funds are allocated to eligible projects or assets, with controls over selection, management and reporting. A general corporate-purpose SLL can therefore be credible without a green project pool, while a green bond can allocate proceeds correctly without changing its coupon when the issuer's enterprise-wide emissions move.

The March 2025 Sustainability-Linked Loan Principles

(https://www.lma.eu.com/application/files/2317/4481/8026/Sustainability-Linked_Loan_Principles_-_26_March_2025_.pdf) and related public guidance

(https://www.lma.eu.com/application/files/3517/4298/0872/Guidance_on_Sustainability-Linked_Loan_Principles_-_26_March_2025.pdf), issued by the relevant loan-market associations, describe a voluntary market framework.

This chapter summarises the operational disciplines without reproducing proprietary forms or treating the principles as legislation.

The SLLP organise that framework around five core components. First, **selection of KPIs** asks whether the chosen measures connect directly to significant operating impacts and management priorities. Second, **calibration of SPTs** addresses the level, timing and ambition of the performance expected for those KPIs. Third, **loan characteristics** connect achievement or failure to an identified economic or structural consequence in the loan. Fourth, **reporting** provides the recurring information needed to calculate and monitor performance. Fifth, **verification** supplies the external check required by the applicable framework and documents. These components are a voluntary market-principles architecture, not statutory safe harbours, an assurance standard or proof that a particular SLL is credible. The March 2025 source and executed facility must be read in full for a live transaction.

Table 41.1A — Five-component SLLP control map

SLLP component	Credit-team control question	Limitation
KPI selection	Is the metric material, measurable and tied to the core business?	Selection does not establish target ambition
SPT calibration	Is the target dated, evidence-based and beyond the supported baseline trajectory?	No universal percentage proves ambition
Loan characteristics	What exact term changes, by how much and from which date?	A ratchet does not prove environmental or social impact
Reporting	Who reports what data, on which perimeter and timetable?	Borrower reporting is not independent verification
Verification	What provider checks which metric, criteria, period and exceptions?	Verification scope may be narrower than the public claim

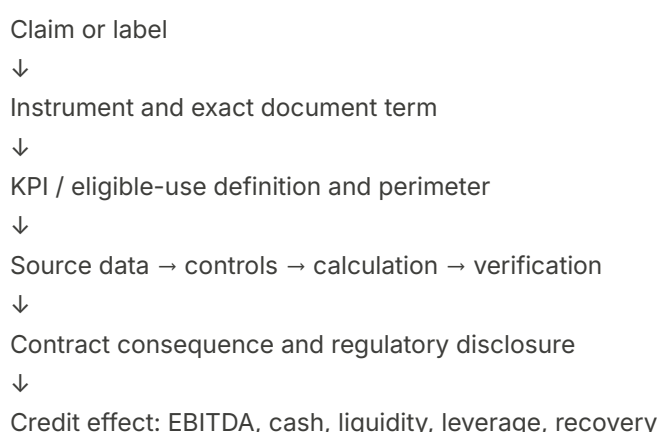
Table 41.1 — Instrument comparison

Field	Sustainability-linked structure	Use-of-proceeds structure
Core question	Did the borrower meet specified SPTs?	Were proceeds allocated to eligible uses?
Financing use	May be general corporate purposes	Restricted by eligible-project framework
Economic link	Margin or another characteristic may change	Usually no performance ratchet is required by the label alone
Data focus	Enterprise/perimeter KPI performance	Project eligibility, allocation and impact information
Failure consequence	Contractual ratchet/fallback under selected documents	Reallocation, reporting or other document consequence
Evidence	KPI calculation, baseline, target and verification	Project register, allocation, unallocated proceeds and review
Main analytical error	Treating a small ratchet as proof of material impact	Treating allocation as proof of enterprise-wide improvement

Synthetic case 1 — materiality before label. Arbor Packaging proposes an SLL tied only to office electricity, which represents less than 1% of its documented energy consumption. Its manufacturing heat and purchased materials drive much larger impacts and transition costs. The lender does not allege that the proposed KPI was chosen to mislead. It asks management to demonstrate materiality, coverage and ambition, and treats the label as unsubstantiated until that evidence exists.

Synthetic case 2 — allocation is not performance. Beacon Transit issues a fictional green bond to finance electric-bus charging equipment. The proceeds register and external review address allocation. The credit model separately tests utilisation, electricity prices, maintenance, grants and residual diesel-fleet costs. The use-of-proceeds label does not itself prove EBITDA growth, emissions reduction or repayment capacity.

Figure 41.1 — Claim-to-evidence chain



41.3 KPI and SPT design

A credible KPI is material to the borrower's business and measurable on a consistent basis. A credible SPT adds a dated performance level supported by baseline evidence, historical series, business plan, external reference points where suitable and clear treatment of structural change. "Industry leading" is not a calculation.

Table 41.2 — KPI control record

Field	Required specification	Failure mode
Metric	Exact numerator, denominator and unit	Undefined “reduction”
Perimeter	Entities, sites, scopes, products and exclusions	Selective coverage
Baseline	Period, value, source, method and assurance	Moving starting point
SPT	Value, date and measurement window	Target without timing
Ambition evidence	History, forecast, capex and relevant benchmark	Business-as-usual target
M&A/disposals	Predetermined adjustment method	Opportunistic re-basing
Method change	Trigger, governance and comparability bridge	Unexplained discontinuity
Reporting	Format, timing and responsible officer	Late or incomplete data
Verification	Provider, scope, standard and exceptions	Ambiguous assurance claim
Consequence	Ratchet, fallback, cure and effective date	No document-to-calculation link

Worked calculation 1 — absolute and intensity metrics can diverge

Fictional Crest Materials produces 1.0 million units and emits 100,000 tonnes in the baseline year, or 0.100 tonne per unit. In the test year, output rises 20% to 1.2 million units and emissions rise 8% to 108,000 tonnes.

Absolute emissions change = $108,000 / 100,000 - 1 = +8.0\%$

Test-year intensity = $108,000 / 1,200,000 = 0.090$ tonne per unit

Intensity change = $0.090 / 0.100 - 1 = -10.0\%$

Both statements are arithmetically true. An intensity target may capture production efficiency, but it does not establish an absolute reduction. The documents and public claim should identify which question the KPI answers.

Worked calculation 2 — SPT calibration and distance to target

Crest's fictional baseline energy intensity is 4.0 MWh per tonne of output. The SPT requires a 15% reduction by the observation date.

Target intensity = $4.0 \times (1 - 15\%) = 3.40$ MWh per tonne

Reported performance is 3.48 MWh per tonne.

Improvement = $1 - 3.48 / 4.0 = 13.0\%$

Distance to SPT = $3.48 - 3.40 = 0.08$ MWh per tonne

The SPT is missed under this simplified calculation. Whether rounding, verification exceptions, a grace period or a contractual fallback applies is a document question.

Synthetic case 3 — denominator movement. Delta Foods' waste-intensity KPI improves because tonnes of product sold rise following an acquisition, while total waste also rises. The committee records the numerator, denominator and acquisition bridge. It does not state that management manipulated the figure; it concludes only that an intensity metric needs an absolute companion indicator and a predetermined M&A policy.

41.4 Restatement, reporting and verification

Restatement is necessary when the agreed methodology says the original baseline is no longer comparable. It is also a source of discretion risk. The facility should identify triggers, materiality thresholds, calculation governance, lender information and verification before a structural change occurs.

Worked calculation 3 — KPI restatement after an acquisition

Fictional Echo Components begins with 100,000 tonnes of emissions and EUR 200 million of revenue: baseline intensity is 500 tonnes per EUR million. It later acquires a business with 30,000 tonnes and EUR 50 million of baseline-period revenue. Under a fictional document rule requiring full like-for-like re-basing:

Restated emissions = 100,000 + 30,000 = 130,000 tonnes

Restated revenue = EUR 200m + EUR 50m = EUR 250m

Restated intensity = 130,000 / 250 = 520 tonnes per EURm

For a 10% reduction SPT, the restated target is $520 \times 90\% = 468$ tonnes per EURm. Actual combined intensity at the observation date is 462. The target is met by 6 tonnes per EUR million under the fictional restatement. Against the unadjusted 500 baseline, a 10% target would be 450 and would be missed by 12. The example shows why the pre-agreed rule and verification matter; it does not say which approach a live deal should use.

Table 41.3 — Restatement decision record

Question	Evidence
Has a contractual trigger occurred?	Acquisition/disposal size and exact clause
Is the change inside the KPI perimeter?	Entity/site/scope mapping
Are historical data available on a comparable method?	Source systems and methodology bridge
Who calculated the restatement?	Named function and workpaper
Who approved it?	Governance record required by documents
Was it independently checked?	Verification report and exceptions
How did it change achievement?	Old-versus-restated calculation
How was it disclosed?	Borrower report and lender notice

Verification should specify the subject matter, criteria, period, level of assurance or agreed procedure, exclusions and findings. “Externally verified” is incomplete if the provider checked only part of the perimeter or did not opine on SPT achievement.

41.5 Margin-ratchet economics and incentive quality

The ratchet must be calculated, not described as “meaningful” by default. Economic materiality depends on debt quantum, basis-point adjustment, duration, probability of achievement, symmetry and the cost of the underlying programme.

Worked calculation 4 — annual margin effect

Assume a fictional EUR 450 million term loan has a 7.5 basis-point downward adjustment if an SPT is met and a 7.5 basis-point upward adjustment if it is missed.

Annual interest change = EUR 450m × 0.075% = EUR 0.3375m

The distance between the down and up states is EUR 0.675 million annually. If the verified programme requires EUR 8 million of annual operating cost plus EUR 30 million capital expenditure, the ratchet is not the business case for the investment. It may still create governance or signalling value, but that claim needs separate evidence.

Table 41.4 — Ratchet-quality questions

Feature	Stronger control	Risk to test
Symmetry	Clear up/down or justified alternative	Reward without meaningful downside
Size	Calculated against expected debt and tenor	Headline bps on rapidly amortising debt
KPI count	Material measures with transparent weighting	One easy KPI offsets a missed material KPI
Fallback	Defined result for late/unverified reporting	Silence treated as achievement
Timing	Observation, report and margin dates aligned	Benefit before evidence
Amendments	Controlled consent and disclosure	Target reset after performance is visible
Cumulative effect	Modelled with amortisation and refinancings	Annual figure multiplied blindly by tenor

Weaknesses can arise from immature data, unclear documents, poor calibration or unforeseen perimeter change. A reviewer should describe the weakness and its consequence rather than alleging that a party intended to game the structure.

41.6 EU regulatory map: correct addressee, correct function

The EU sustainable-finance framework contains distinct instruments. Similar vocabulary does not make them interchangeable.

Table 41.5 — Regime and function map as of 13 July 2026

Framework	Principal function/addressee	What it does not prove
SFDR, Regulation (EU) 2019/2088	Sustainability-related disclosures by financial market participants/advisers and for financial products	That a borrower, loan or company is “Article 8” or “Article 9”
EU Taxonomy, Regulation (EU) 2020/852	Classification and disclosure framework for environmentally sustainable economic activities	That an eligible activity is aligned, or a loan is low risk
Accounting Directive/CSRD and ESRS	Corporate sustainability reporting for undertakings within the applicable scope	That every leveraged borrower reports, or every disclosed target is achieved
European Green Bond Regulation (EU) 2023/2631	Voluntary EuGB designation, external-review regime and specified/optional bond disclosures	That every green or sustainability-linked bond is a EuGB; it is not a loan regime
ESG Ratings Regulation (EU) 2024/3005	Transparency and integrity framework for in-scope ESG rating activities/providers	That different providers must produce the same rating or that a score predicts default

41.6.1 SFDR and the Taxonomy

SFDR is a disclosure regime with defined addressees and product concepts. Its current text and regulatory technical standards must be checked at the relevant date: Regulation (EU) 2019/2088, consolidated text (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02019R2088-20260702>) and Delegated Regulation (EU) 2022/1288 (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02022R1288->

20230220). A lender's SFDR obligations may influence information requests or portfolio classification, but they do not automatically become borrower representations.

The EU Taxonomy Regulation (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32020R0852>) defines a framework for environmentally sustainable activities and six environmental objectives. Alignment requires the applicable legal conditions and technical screening criteria, including substantial contribution, no significant harm and minimum safeguards. Eligibility merely indicates that an activity is covered by criteria. Neither status is a general credit rating.

41.6.2 CSRD and ESRS effective-date control

Corporate reporting scope and standards changed materially during 2025–2026. Directive (EU) 2026/470 amended the Accounting Directive and CSRD framework, including scope thresholds and value-chain provisions, with transposition questions remaining relevant. Use the current consolidated Accounting Directive (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02013L0034-20260318>), Directive (EU) 2026/470 (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32026L0470>) and applicable national implementation; never use an old CSRD summary as a live perimeter opinion.

The first ESRS set appears in Delegated Regulation (EU) 2023/2772 (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02023R2772-20250101>). The Commission announced adoption of revised standards on 3 July 2026. At the review date, users must verify Official Journal publication, scrutiny, entry into force, application date and transitional treatment before replacing the operative text. The Commission's 3 July 2026 update (https://finance.ec.europa.eu/news/commission-adopts-revised-sustainability-reporting-standards-2026-07-03_en) is a change flag, not permission to treat draft or newly adopted wording as already applicable.

41.6.3 European Green Bonds and ESG ratings

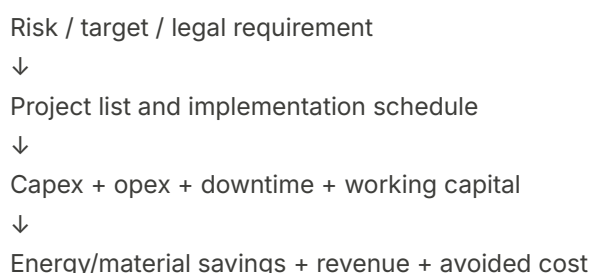
Regulation (EU) 2023/2631 (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02023R2631-20240109>) applies its main EuGB framework from 21 December 2024 and includes a supervised external-review architecture plus optional disclosure templates for certain other bonds. The designation is voluntary. Allocation and review do not prove additionality, repayment or enterprise-wide sustainability.

Regulation (EU) 2024/3005 (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32024R3005>) applies from 2 July 2026, subject to its transitional provisions. It addresses in-scope ESG-rating activities and providers. A rating must still be captured with provider, method, objective, scale, date, entity/instrument perimeter, data coverage and conflicts disclosures. The regulation does not make unlike ratings comparable.

41.7 Transition expenditure through the credit model

Transition plans become credit evidence only when translated into projects, dates, approvals, costs, benefits and funding. The analyst should distinguish maintenance capex, compliance capex, growth capex, decommissioning, grants, operating savings and revenue assumptions.

Figure 41.2 — Transition-to-credit bridge



↓

EBITDA → free cash flow → liquidity → leverage

↓

Failure/delay case → stranded value → recovery

Worked calculation 5 — transition project economics

Fictional Forge Glass plans EUR 36 million of equipment capex. Expected annual energy savings are EUR 7 million, but maintenance and monitoring cost EUR 2 million per year.

Annual net cash benefit before tax = EUR 7m – EUR 2m = EUR 5m

Simple payback = EUR 36m / EUR 5m = 7.2 years

If the debt maturity is four years, a 7.2-year payback does not make the project uneconomic, but the refinancing case cannot assume full recovery of capex during the existing tenor. The model should include construction timing, ramp-up, downtime, price sensitivity and residual value.

Worked calculation 6 — downside liquidity

Forge opens the year with EUR 24 million cash and EUR 18 million available revolver; minimum cash is EUR 10 million. Before transition capex, projected operating cash generation is EUR 12 million, cash interest is EUR 10 million and mandatory amortisation is EUR 4 million. Transition capex is EUR 22 million.

Pre-draw closing cash = 24 + 12 – 10 – 4 – 22 = EUR 0m

It must draw EUR 10 million to restore minimum cash, leaving EUR 8 million revolver headroom. In a downside, operating cash generation falls by EUR 6 million and capex overruns by EUR 5 million. The additional EUR 11 million need produces a total draw of EUR 21 million, exceeding availability by EUR 3 million. The sustainability project may be necessary, but the financing is not resilient to the stated downside.

Worked calculation 7 — transition risk and recovery

Assume fictional going-concern enterprise value of EUR 400 million, EUR 15 million process costs, EUR 40 million super-senior claims and EUR 300 million first-lien claims. Base first-lien value after costs and super-senior claims is EUR 345 million, so recovery is capped at 100%.

If delayed transition expenditure and lost customers reduce enterprise value to EUR 300 million:

First-lien value = EUR 300m – EUR 15m – EUR 40m = EUR 245m

First-lien recovery = EUR 245m / EUR 300m = 81.7%

This is a synthetic sensitivity, not an environmental valuation rule. A real analysis requires entity, collateral, priority, liability and timing review.

Synthetic case 4 — necessary capex, insufficient liquidity. Forge's equipment is important to customer retention and energy performance, yet the downside case shows a EUR 3 million funding gap. The committee response is a larger liquidity reserve, delayed distribution or added equity—not a conclusion that the project should be cancelled because it carries an ESG label.

41.8 Ratings, CLOs and investor mandates

An ESG rating may assess impact, risk, exposure, management or a combination, at issuer, instrument or product level. Direction and scale can differ. Record the method before comparing scores.

Table 41.6 — Rating evidence record

Field	Required entry
Provider and regulated entity	Exact name and status checked at date
Product	Rating, score, data product or second-party opinion
Objective	Risk, impact, alignment or another stated construct
Rated object	Issuer, instrument, project, fund or other perimeter
Scale/direction	What high and low values mean
Data date/coverage	Period, estimates, exclusions and controversies
Method version	Public method and effective date
Change reason	Data, method, event or corrected error
Permitted use	Licence/document restrictions and decision purpose

CLO and investor mandates must be read from the selected indenture, investment guideline or side letter. No universal “ESG-compliant loan” definition, exclusion list or pricing effect applies across vehicles.

Worked calculation 8 — selected mandate bucket

A fictional CLO document limits a defined monitored bucket to 15% of a EUR 500 million collateral balance. Current exposure is 13%, or EUR 65 million. A proposed EUR 15 million asset adds 3 percentage points if the denominator is unchanged.

Pro forma bucket = (EUR 65m + EUR 15m) / EUR 500m = 16%

Excess over selected limit = 16% – 15% = 1 percentage point, or EUR 5m

The calculation says nothing about another CLO or whether the asset satisfies the document's definition. The selected executed document and trustee/manager process control.

Synthetic case 5 — ratings disagree. Grove Services receives a strong score from a provider focused on management and disclosure but a weaker score from one focused on exposure. The analyst does not average the numbers. The source record explains the different objectives and uses underlying operating data in the credit case.

Synthetic case 6 — mandate, not market claim. A lender says “ESG demand supports pricing.” The committee has one fund guideline excluding a defined activity but no dataset connecting the asset to spread or allocations. It records that the selected mandate affects that investor's eligibility and removes the unsupported universal pricing statement.

41.9 Claims, controls and credit committee output

Table 41.7 — Claim substantiation matrix

Proposed claim	Minimum evidence	Safe credit formulation
"SLL target met"	Document formula, data, restatement and verification	"Reported as met under specified method; exceptions noted"
"Taxonomy aligned"	Activity, criteria, DNSH, safeguards and current review	State percentage/perimeter/source; avoid company-wide label
"CSRD compliant"	Applicable scope, law, standards, report and assurance	Attribute conclusion to qualified owner
"Green bond"	Framework, allocation and review	Identify exact designation; do not infer credit quality
"Lower funding cost"	Comparable transaction or controlled dataset	Separate ratchet arithmetic from market pricing claim
"ESG rating improved"	Same provider, product, method and dates	Explain whether data, method or performance changed
"Transition funded"	Approved project budget and sources	Show liquidity and downside gap

Table 41.8 — Committee output

Section	Required content
Instrument	SLL/use-of-proceeds/ordinary facility and exact consequence
KPI/SPT	Materiality, baseline, perimeter, target and verification
Regulatory perimeter	Applicable/non-applicable/uncertain by regime and date
Operating bridge	Risk, project, capex, opex, savings and timing
Liquidity	Base, downside, minimum cash and funding gap
Recovery	Value/cost/claim sensitivity and evidence
Investor constraints	Selected document definitions and headroom
Claims	Supported, qualified, removed or escalated
Open work	Owner, evidence needed and decision deadline

41.10 Exercises

Exercise 41.1 — intensity versus absolute result

A borrower reduces emissions intensity from 0.50 to 0.44 tonne per unit while production rises from 100,000 to 130,000 units. Calculate absolute emissions in each period and identify the claim supported.

Answer check. Baseline emissions are $0.50 \times 100,000 = 50,000$ tonnes. Test-year emissions are $0.44 \times 130,000 = 57,200$ tonnes, a 14.4% increase. Intensity fell 12%, but absolute emissions rose. The evidence supports an intensity-improvement claim only.

Exercise 41.2 — ratchet materiality

A EUR 300 million loan offers a 5-basis-point margin reduction for one year. The sustainability programme costs EUR 4 million operating expense in that year. Calculate the interest saving and compare it with programme cost.

Answer check. Interest saving is $\text{EUR } 300\text{m} \times 0.05\% = \text{EUR } 0.15\text{m}$. It equals 3.75% of the EUR 4 million cost. The ratchet cannot be described as funding the programme, though other incentives may exist.

Exercise 41.3 — transition liquidity

Opening cash is EUR 20 million, minimum cash EUR 8 million and revolver availability EUR 12 million. Pre-capex cash flow is positive EUR 4 million. Required transition capex is EUR 24 million. What draw is needed to retain minimum cash, and is there a gap?

Answer check. Pre-draw closing cash is $20 + 4 - 24 = \text{EUR } 0\text{m}$. An EUR 8 million draw restores minimum cash, leaving EUR 4 million availability. There is no base gap, but only EUR 4 million downside headroom.

Appendix 41.A — Dated source and effective-date register

Source	Function	Status/date control used	Checked
LMA/APLMA/LSTA Sustainability - Linked Loan Principles, March 2025 (https://www.lma.eu.com/application/files/2317/4481/8026/Sustainability-Linked_Loan_Principles_-_26_March_2025_.pdf)	Voluntary SLL market framework	Current public version located; not legislation	13 Jul 2026
SLLP Guidance, March 2025 (https://www.lma.eu.com/application/files/3517/4298/0872/Guidance_on_Sustainability-Linked_Loan_Principles_-_26_March_2025.pdf)	Market-practice explanation	Use as guidance only	13 Jul 2026
SFDR consolidated text (https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02019R2088-20260702)	Financial-market disclosure regime	Consolidated version dated 2 Jul 2026	13 Jul 2026
SFDR Delegated Regulation 2022/1288 (https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02022R1288-20230220)	Regulatory technical standards	Check current status before live use	13 Jul 2026
Taxonomy Regulation 2020/852 (https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32020R0852)	Sustainable-activity framework	Delegated criteria and disclosures also required	13 Jul 2026
Accounting Directive consolidated 18 Mar 2026 (https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02013L0034-20260318)	Current corporate-reporting base	National transposition remains relevant	13 Jul 2026
Directive (EU) 2026/470 (https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32026L0470)	2026 CSRD/scope amendments	Entered into force 18 Mar 2026; apply with transposition analysis	13 Jul 2026
ESRS Delegated Regulation 2023/2772, consolidated (https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02023R2772-20250101)	First ESRS set	Fix applicable version and reporting year	13 Jul 2026
Commission revised - ESRS adoption update, 3 Jul 2026 (https://finance.ec.europa.eu/news/commission-adopts-revised-sustainability-reporting-standards-2026-07-03_en)	Change alert	Verify OJ publication, scrutiny, force and application before use	13 Jul 2026
European Green Bond Regulation 2023/2631 (https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02023R2631-20240109)	EuGB and related bond disclosures	Main framework applies from 21 Dec 2024; other provisions have specified dates	13 Jul 2026
ESG Ratings Regulation 2024/3005 (https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32024R3005)	ESG-rating-provider framework	Applies from 2 Jul 2026 subject to transition	13 Jul 2026

Appendix 41.B — KPI and public-claim review checklist

- ♦ 1. State the exact instrument, borrower, document and version.
- ♦ 2. Identify whether the structure is performance-linked or use-of-proceeds.
- ♦ 3. Define each KPI numerator, denominator, unit, perimeter and source system.
- ♦ 4. Record baseline date, value, method, assurance status and historical series.
- ♦ 5. Record each SPT, observation period, ambition evidence and business-plan dependency.
- ♦ 6. State M&A, disposal, methodology and error-restatement rules before testing performance.
- ♦ 7. Recalculate every reported value and preserve the workpaper.
- ♦ 8. Identify verification provider, scope, criteria, level and exceptions.

- ✦ 9. Tie achievement to the exact margin, fallback, reporting and effective-date clause.
- ✦ 10. Calculate the ratchet in currency across expected debt and duration.
- ✦ 11. Separate SFDR, Taxonomy, CSRD/ESRS, EuGB and ESG-ratings functions.
- ✦ 12. Verify source consolidation, amendment, adoption, entry-into-force and application dates.
- ✦ 13. Translate transition projects into capex, opex, downtime, savings and financing.
- ✦ 14. Run downside liquidity, leverage and recovery rather than reporting narrative only.
- ✦ 15. Read CLO and investor constraints from the selected executed document.
- ✦ 16. Attribute ratings by provider, product, objective, method, date and perimeter.
- ✦ 17. Remove generic pricing, demand, additionality or credit-benefit claims without evidence.
- ✦ 18. Escalate legal, regulatory, reporting, assurance and environmental conclusions to qualified specialists.

A chapter, term sheet or committee paper passes this checklist only when its claims are reproducible and its unresolved judgments are visible. Passing does not supply release authority or specialist approval.

PART IX

THE PROFESSION

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-

What Experience Teaches

What the Work Teaches

This chapter is different from the others. The rest of the book deals in frameworks, mechanics and definitions; this one is personal. Take what is useful and leave the rest.

The Weight of It

The honest place to start is that much of this career is difficult — not difficult in the way that sounds impressive at dinner parties ("oh, the hours, the pressure, you know how it is"), but difficult in the way that accumulates quietly over years, until you look up and realize you are tired in a way that sleep does not fix.

The balance varies by role, firm and market cycle. For some practitioners, long periods of frustration sit alongside less frequent moments of genuine satisfaction: deals stop, analysis is not used, internal priorities change and new deadlines arrive before the last task has settled.

And then, every once in a while, something clicks: a deal closes and you played a real part in it, a piece of analysis turns out to matter, someone you respect notices what you did. For a few days, you feel like maybe this was all worth it.

Then the feeling fades, and you're back where you started.

Demanding work can gradually erode energy, attention and perspective. That is a practical reason to reassess workload, recovery time and support rather than to treat strain as proof of commitment.

Where This Started

Where people come from explains something about why they end up in this field and why they stay.

In many places, wearing a suit signals having made it to the other side. A parent who comes home each evening dressed impeccably — suit pressed, tie straight, hair combed back in a way that signals seriousness and success — represents something to a child who doesn't yet understand the work itself: not struggling, having crossed over to where life is more stable, more dignified, safer.

That image stays. The suit becomes a symbol of something you want before you know what it is.

Popular culture can also shape early ideas about finance. Films such as *Wall Street* present a stylised image of status, confidence and proximity to power. That image is not a reliable description of the work, and readers should separate the attraction of the image from the ethics and reality of the profession.

It takes time to understand that the image of success and the experience of success are different things. The skyline and the deals are real, but achievement can feel different from the inside than it looked from the outside.

No Map, No Shortcuts

For many, there is no map: no connections in the industry, no family friends who can make introductions, no university network that opens doors automatically. Some come from places that don't produce investment bankers, with nothing in their background to suggest they belong in this world.

Many in this field are also not good at the social part — not shy, exactly, but people who find the normal rhythms of professional socializing genuinely difficult. The small talk at conferences, the dinners where you are supposed to be "building relationships," the instinct for knowing what to say and when to say it: none of that comes naturally to everyone. It can be managed over the years, but it still costs energy that seems to come free to other people.

Conventional networking can be harder for people whose strengths or communication styles lie elsewhere. That can require deliberate strategies, but it is not a verdict on professional potential: preparation, reliability, substantive expertise and smaller one-to-one relationships can also build trust.

Not everyone enters through a structured analyst programme. Self-directed learning can be valuable, but mistakes should be bounded by supervision, review, checklists and escalation rather than treated as an acceptable substitute for training.

Experience can deepen understanding when it is paired with reflection and feedback. It complements, rather than outranks, formal teaching and knowledge shared by colleagues.

Career progression, compensation and confidence vary widely. An unconventional route may create additional obstacles, but those outcomes are not predetermined; access to feedback, sponsorship, opportunity and an inclusive culture also matter.

The Territory Nobody Talks About

Sustained-pressure work is worth discussing plainly because it shapes judgment, relationships and the ability to keep performing well over time.

Even when performance looks intact, sustained pressure can reduce energy, concentration and perspective. Pause, speak with someone you trust and reconsider the conditions under which you are working rather than treating that experience as an unavoidable badge of the job.

Deadlines and job levels can change without resolving the underlying pressure. Do not defer support on the assumption that the next closing, quarter-end or promotion will necessarily make the problem disappear.

If work feels persistently unmanageable, step away from the immediate task and contact a trusted person or an appropriate local support service. This is a personal reflection on working life, not health guidance.

The most admirable people in this industry are not the ones who sacrificed everything; they are the ones who figured out how to be genuinely good at what they do without losing themselves in the process. That is a skill worth learning, however imperfectly.

What to Tell Someone Starting Out

To someone earlier in the career — someone who has some technical skills but hasn't yet figured out the larger game — there are a few things worth saying. They tend to be learned late and imperfectly, and advice is always easier to give than to follow.

Protect breaks and use some of them, when appropriate, to maintain relationships. Shared meals can help, but rest, dietary needs, caregiving, religious practice and personal preference also matter; relationship-building should not turn every break into another work obligation.

Think about what you are known for — not in a self-promotional way, but strategically. Ask yourself what comes to mind when people think of you, and what makes them seek you out rather than someone else. Too many years can be spent being the person who chases opportunities; the better position is being the person opportunities come looking for.

Technical excellence matters, but it is rarely the only source of professional value. Trust, judgment, reliability and the effect you have on colleagues and clients can be harder to replicate than any single modelling task.

This is advice about things that do not come naturally, which is precisely the point: these lessons tend to be learned the hard way, and later than they should be.

The Thing That Kept Me Going

So why go deep on the technical side, knowing at some level that other things matter more for career progression — why write a book about covenants and documentation?

The honest answer is that it is hard to do otherwise.

Some people are motivated by the deals themselves, by the money, by the status. Those things are not without pull, but they are not what actually drives the work that goes deepest.

What drives that work is understanding. The holy grail is always the same: getting to the bottom of how something actually works — the fundamentals, the core logic, the why underneath the how.

The aim is to understand leveraged finance the way a watchmaker understands a watch: not just how to use it, but how all the pieces fit together and why it works the way it does. That pursuit can be the through-line of a career, even when it is not the most strategic use of time.

This book records a working synthesis of leveraged-finance concepts. It is not the final word: transaction documents, market practice and law change, and readers should verify the current documents and obtain professional advice where appropriate.

By this point, the preceding chapters have established how covenants work, how deals are structured and why they sometimes fail. The chapters that follow add three advanced professional perspectives before the book closes.

Other lessons do not fit neatly into technical chapters: expertise is not the only contributor to longevity, relationships can shape outcomes, and external markers of success may feel different from the inside.

Hard periods should not be faced alone. Ask early for practical help from people you trust and use the support arrangements available in your circumstances.

This personal reflection differs from the technical chapters. Readers should treat it as one perspective, not as evidence that every leveraged-finance career follows the same path.

Good luck.

Communication and Stakeholder Management

Introduction

Some credit losses, deal breakdowns and missed opportunities are worsened by communication failures even when the underlying analysis is competent. Communication cannot repair weak credit, but it can improve decision quality, escalation and stakeholder alignment.

Leveraged finance uses quantitative analysis: leverage, coverage, liquidity, cash-flow waterfalls and stress cases. A sound model is necessary, but the decision also depends on explaining the assumptions, limits and risks clearly enough for others to challenge them.

Failures at that interface can be costly, although the effect depends on the decision and cannot be reduced to a universal amount.

Synthetic teaching scenario: Northbridge Media Services seeks financing during an economic downturn. Contracted revenue and low working-capital needs appear supportive, but the lender must test renewal, customer concentration, sponsor assumptions and downside liquidity before recommending approval. Northbridge is entirely fictional.

The team showed its downside numbers but did not explain which revenue was contractually protected, which assumptions remained exposed to recession and what evidence supported the sponsor's operating plan. The committee therefore had difficulty distinguishing model output from the underlying credit thesis.

The committee approved a smaller hold, and syndication was weak. That outcome could have reflected credit quality, market conditions, pricing, structure or communication; the example should not attribute causation to presentation alone.

The business later underperformed. That result confirms that a clearer story would not have cured the credit. Better communication could only have produced a better-informed approval, a clearer monitoring plan and a more accurate record of why investors did or did not participate.

The practical lesson is narrower: a technician must be able to explain what the model assumes, what could falsify the thesis and what decision is being requested. Presentation is part of governance, not a substitute for substance.

Technical texts often devote less space to communication than the job requires. Durable careers generally combine analytical competence, judgment, integrity and the ability to communicate with different stakeholders; no single trait guarantees advancement.

Communication matters because leveraged-finance decisions require committees, investors, borrowers and control functions to understand the evidence, limits and requested action. It should support independent challenge rather than persuade every stakeholder to trust the presenter.

Strong technical performance alone may not prepare someone for roles that require leadership, client work and decision-making. Communication can broaden a career, but advancement also depends on judgment, conduct, opportunity, firm structure and results.

This chapter is not a primer on grammar or public speaking; there are plenty of those. It is a practitioner's guide to the specific communication problems you will meet in leveraged finance: the frameworks that work, the mistakes

practitioners make and watch others make, and the hard-won lessons that may spare you from learning them at full price.

Start with the credit committee presentation, because that is where many careers gain momentum or stall.

The Credit Committee Presentation: Winning Skeptics One Slide at a Time

A credit committee is an independent decision body, not an adversary whose job is simply to say no. Members' experience and mandate vary; the presenter's responsibility is to supply complete, accurate and challengeable information.

Your job in a credit committee presentation is to enable an informed decision: state the recommendation, surface the material risks and make the evidence easy to test. A fair rejection is a valid outcome.

The first principle is Barbara Minto's pyramid principle, articulated for business writing and speaking: lead with your conclusion, support it with three to five key points, and back those points with data. It is the inverse of how most analysts naturally present deals.

Most analysts want to open with industry background, then the borrower's competitive position, then the financial analysis in full detail, and only at the end recommend approval. That order is backward. The committee wants the recommendation first, and then to understand why it is the right one.

Here is how to structure a credit committee presentation:

Slide one, the conclusion: 'We recommend a commitment of \$X at a margin of Y basis points to finance SponsorCo's acquisition of Acme Corp. Entry leverage is 3.5x under the stated definition and is projected to decline to 2.8x by year three. The recommendation rests on contractual cash flow, the downside case and specified structural protections.' Do not call a leveraged credit 'investment-grade equivalent' without a defined, evidenced methodology.

Keep the opening slide concise, but include any qualification essential to understanding the recommendation. The appropriate level of detail depends on committee policy and the transaction.

Then present three to five supporting points that answer the committee's likely concerns. For the fictional media borrower, address recession resilience, contracted cash flow, sponsor support, leverage and structural protection.

Each supporting point gets three to four minutes: show the data, walk through a scenario, take a question, move to the next point. If a point needs more than five minutes to explain, either you have not worked out what you are trying to say or the point is not as central as you thought.

What committee members actually want addressed is the question of what single thing could go wrong with the deal and how the lender is protected if it does. They do not expect you to pretend nothing can go wrong; they expect evidence that you have thought carefully about the risks and have either mitigated them or are being compensated for them.

Composite illustration: a covenant-lite term loan for a business-services company had material customer concentration. The largest two customers represented approximately eighteen and twelve percent of revenue, so the downside case had to test the loss or reduction of either relationship.

The presentation led with the concentration risk, stated what was known about contract duration and switching alternatives, and separated verified facts from management's diversification plan. That allowed the committee to debate the evidence rather than first discover a buried risk.

If the customer later reduced spending, the monitoring plan and diversification milestones would help the lender respond; they would not prove that the original approval was correct. Use the example to show governance, not hindsight validation.

There is a broader principle here about committee presentations: you owe the committee a discussion structured so that a no, if it comes, is a deliberate and informed rejection of the deal, not the residue of feeling tricked toward approving something unsound. The best committees have high standards, and they respect a presenter who respects them enough to show the hard realities of the deal plainly.

On tough questions, the first rule is not to be defensive. A committee member who challenges your recommendation is doing the job, not attacking you. Defensiveness costs credibility immediately, along with the thirty seconds of committee time it takes you to compose yourself. Develop the habit of treating a hard question as an opportunity rather than a threat.

Composite illustration: a healthcare lender challenged an underwriting assumption about patient collections. A sound response would state the assumption, show the sensitivity, acknowledge the data gap and commit to a specific follow-up rather than improvise certainty.

The value of that exchange is not that being heard determines a vote. It is that the concern enters the record, the sensitivity can be tested and the surveillance team receives a concrete metric to monitor.

Presenting risk without losing your audience takes some care. The temptation is to soft-pedal risk because you want the approval. That is a mistake, and an unnecessary one: credit committees do not require deals to be risk-free. They require you to be honest about the risks and to show that the economics of the transaction compensate you for bearing them.

A lender cannot eliminate risk. The task is to identify and quantify material risks, test mitigants and decide whether structure and expected return are adequate under policy. Present sponsor, market, business, operational, execution and financial risks without implying that any checklist is exhaustive.

Bearing and composure matter more in person than most analysts appreciate, and on video calls, which are now common, you have to be deliberate about them: sit up, look at the camera, speak clearly, pause between points, and do not rush. Nerves make you rush, rushing produces mistakes, and the committee senses the nervousness.

Across committee settings, calm and clear delivery can help the audience follow the analysis. If you do not know an answer, say so, identify what you will verify and follow up; do not bluff.

Some mistakes reliably kill credibility. The first is citing numbers you do not understand. If you are presenting EBITDA leverage or debt service coverage, be able to explain from first principles why the metric matters and how it is calculated; if a committee member drills into your math and finds an error, the rest of the presentation is wasted.

Composite illustration: if a presenter does not support the recommendation, that disagreement should be surfaced before committee. The team should reconcile the evidence, record any dissent and decide who can present the case accurately.

Before committee, decide what the evidence supports and identify unresolved uncertainty. Intuition can be a prompt for further testing, but it is not usually right by definition and should not displace documented analysis or escalation.

The third mistake is being surprised by a fair question. If you have presented a deal with high leverage and someone asks about the leverage, that is not an ambush; it is the question you should have expected. Anticipate the hard questions, build them into the presentation, and show that you thought about the committee's likely concerns before the meeting started.

As for templates and frameworks, here is a structure that holds up consistently:

Opening slide: your recommendation in one clear sentence—a statement, not a question or a hypothetical: "We recommend approval of X."

Next slides: the borrower and the sponsor—who they are, what they have done, what is known about their management quality. Keep this brief unless the sponsor's track record is a major positive or negative.

Then the deal dynamics: what is being financed, what the capital structure looks like, the leverage at entry and where it stands in year three. This is baseline material and it belongs early.

Then the business and the market: what the company is, what it does, why it matters, its competitive position, and the trends behind it. This is where the story gets told; do not bury it.

Then the key value driver: the one thing that has to happen for this credit to perform, whether volume, EBITDA margin, or multiple contraction. Name it, quantify it, and stress-test it.

Then the downside case: what happens if that key value driver does not materialize—where the leverage goes, whether the borrower can still service the debt, and what the recovery looks like.

Then the risk factors by category (sponsor, market, business, operational, execution), each with a sentence or two on mitigation.

Then the covenants and protections: the surveillance mechanism, and how the lender will know when things start to go wrong.

Then the conclusion: restate the recommendation and make clear why you are comfortable with the risk and the return.

The structure is neither fancy nor creative; it has survived repeated use, which is worth more. It is also defensible: if a committee member challenges you on any point, they are challenging something you explicitly presented, not something you buried or left out.

One more point on credit presentations: know the room. Committees have different personalities. Some are process-oriented and want every box checked; some are technical and want to drill into the modeling; some are risk-focused and want to hear what could go wrong; some are relationship-focused and want to understand the client and the sponsor.

Spend five minutes before the presentation working out which kind of committee you are walking into, and adjust the emphasis accordingly: airtight covenants for the process-oriented committee, a model that withstands drilling for the technical one, risk mitigation up front for the risk-focused one, and the sponsor's story told well for the relationship-focused one.

The best committee presentations are built on that principle. They are not generic; they are tailored to the people in the room, and they respect those people enough to address what they actually care about rather than what the presenter thinks they should care about.

The Credit Memo: Where Your Analysis Becomes Real

A credit presentation lasts thirty minutes; a credit memo outlives it by years. People will still be reading your memo on the deal five years from now, when the credit is performing well or badly, trying to understand what you were thinking and whether you had properly identified and quantified the risks.

That is why the credit memo is arguably the most important document a credit professional writes.

The structure of a credit memo is standard: executive summary, business overview, financial analysis, risk factors, and recommendation. What separates a competent memo from an insightful one is how you use that structure—the information you choose to highlight and the narrative you run through the quantitative analysis.

Take the executive summary first. It is read by busy people scanning for the essentials; they are not reading the memo for the minutiae of the business model, they want the recommendation and the reasons for it. The summary should be brief—two pages is a good target—and should contain:

One sentence: your recommendation.

One or two paragraphs: the business overview—what the company is and why it matters.

Two or three bullet points: the key investment highlights—what is good about this credit.

Two or three bullet points: the key risks—where the credit is vulnerable.

Two or three paragraphs: the financial summary—entry leverage, trajectory, and sensitivity.

One paragraph: your conclusion—why the highlights are enough to offset the risks.

Nothing else belongs there. Someone who reads only your executive summary should understand exactly why you are recommending approval or rejection.

The business overview section is where many memos go wrong. Analysts write a detailed industry analysis: market trends, competitive dynamics, regulatory environment. All of it may be relevant context, but most people skimming a memo do not care about the industry overview as such; they care about understanding the specific business in question and why it matters.

A business overview should start from one question: what does this company do, and why is that valuable? If the answer does not fit in a paragraph, the business is not yet understood well enough to recommend approving a credit. Once that is answered, move to the competitive position, the market trends, and the regulatory environment—always in terms of how those factors bear on this specific company.

Hypothetical example: 'SpecialChem manufactures specialty adhesives and sealants used in automotive and aerospace applications. Its credit case depends on customer concentration, switching costs, programme duration and the extent to which content per vehicle offsets production cyclicalities.' Any market-share or customer claim should be sourced to current diligence.

That single paragraph establishes what the company does, why it matters, and which trends drive the business. The rest of the overview can then cover the company's competitive advantages, its customer base, its geographic footprint, and its growth strategy, but the core narrative is already in place.

On quantitative precision versus narrative: credit writing needs both. The numbers tell you whether the credit pencils; the narrative tells you whether it makes sense. For a mature, stable business in a consolidating industry the narrative may be simple—the company is losing market share, margins are being compressed, and the sponsor's thesis is that it can stabilize margins and consolidate the space. You then show the numbers that would prove that narrative right or wrong.

For a growth business in an industry being disrupted, the narrative is more demanding. You have to explain how the disruption changes the economics of the business, why this company is positioned to win in the new environment, and what the timeline looks like. Then you stress-test whether the company can finance that transition.

The best credit memos blend the two elements so that the joins do not show: the numbers carry a story, and a reasonable person reading the memo would find that story persuasive.

On presenting negative information: when you uncover weaknesses in the credit, you have two choices. You can bury them in the risk section and hope nobody notices, or you can acknowledge them directly, explain how you have thought about them, and show that you believe the credit is sound despite them.

The second approach is almost always better. If something is obviously wrong with the credit, do not pretend otherwise: name it, quantify it, and explain why you are comfortable with it anyway. If you cannot get comfortable with it, do not recommend approval.

Composite illustration: a draft memo noted customer concentration and a prior customer loss. A reviewer moved the point to a footnote and described the loss as non-recurring without sufficient evidence.

Weak treatment of customer concentration can leave monitoring and covenant design underdeveloped if a material relationship later deteriorates. State the risk, quantify the downside and identify the evidence and controls supporting any mitigation.

A credit memo is part of the decision record. If a credit later underperforms, reviewers should be able to see the material risks considered, the evidence used, the uncertainty retained and the approval rationale. Knowingly obscuring a material risk is a governance and conduct problem and may also raise legal or policy issues.

It is instructive to watch credit memos evolve over a career. At the analyst level they are methodical: every section present, every calculation shown, because the analyst is proving to a supervisor that thorough work has been done. At the VP level they tighten; there is more selectivity about what to include and what to emphasize, since the credit committee already knows how to read a balance sheet and does not need every calculation walked through. At the MD level they become more selective still, often written for a committee that will spend perhaps ten minutes on the document, and the focus shifts to the judgment calls, to which decisions were easy and which were hard, and to what has changed in the analysis since the borrower was last reviewed.

The analysis does not get worse with seniority; the communication of what matters gets more efficient.

As for what good and bad credit writing look like in practice: a good memo lets someone who is not an expert in the business read the recommendation section and understand why the deal is happening. A bad memo lets you read the first half and still be unsure what the company actually does or why the sponsor is interested.

A useful risk section focuses on material risks, evidence, mitigants and residual exposure. Its length relative to the positive section is not a quality test; a difficult credit may properly require more space for risks.

A good memo reads as though the author believed in the recommendation. A bad one reads like someone going through the motions.

Something that matters more than people think: a good memo is simply well written. Not flowery, not creative—clear. A sentence says one thing; a paragraph is about one idea; the same term means the same thing throughout; jargon appears only where it is necessary. You write to be understood, not to sound smart.

Some of the best credit memos come from people who write clearly everywhere: their emails are clear, their explanations in meetings are clear, and that clarity transfers to the memo. Some of the worst come from people who appear to believe that credit writing requires a different and more complicated register than normal communication. It does not.

Managing the Syndication Process: Selling Your Conviction

Credit approval is one gate; a syndicated deal must also attract investors on acceptable terms. The relative difficulty varies by market, structure, price and borrower.

Syndication is where communication moves from internal persuasion to external sales: you are no longer convincing colleagues but people whose own money and reputation are on the line.

Communication with the borrower during syndication starts before the bank meeting, before the presentation deck is even finalized. You set expectations with the sponsor and the borrower about what the syndication process will look like, what investors will care about, and what feedback you expect to hear.

Hypothetical example: before launching a deal at leverage above recent comparables, the arranger should tell the sponsor that investors are likely to challenge the level and align on a response grounded in business fundamentals and downside analysis.

The discussion should identify the evidence supporting the proposed leverage, acknowledge contrary comparables and agree who will answer each question. It should not script a defensive claim or reveal confidential information beyond the approved syndication materials.

Prepared answers can improve clarity, but they do not establish that investors were persuaded or that the leverage was appropriate. Record feedback and adjust the structure or price when the evidence requires it.

The initial lender presentation is one part of syndication. Audience, format, duration, recording and permitted materials vary by market, transaction and policy; the process may be virtual, in person or delivered through separate investor calls.

Here is how to structure a bank meeting presentation:

Opening remarks: you, the arranger, briefly explain the deal—why it is being done, why investors should care, and the context. Three to five minutes.

Sponsor remarks: the sponsor explains why the acquisition is strategic, what the plan is, and what value they intend to create. Ten to fifteen minutes. The sponsor must be well prepared and confident here; if the sponsor sounds uncertain, investors will be uncertain.

Business overview: often given by the sponsor's operating team or management—what the business is, how it works, and what the competitive position looks like. Twenty to thirty minutes.

Financing overview: the arranger explains the sources and uses, capital structure, pricing, amortisation, debt-service burden, covenant package and key sensitivities. Do not present sponsor equity returns as though they were lender returns.

Investment highlights: a brief recap of why this is a good deal. Five to ten minutes.

Q&A: investors ask questions, and this can run long if they are interested.

Most of the time, deals are not won in the bank meeting room. They are won beforehand—in how the sponsor was prepared, in the materials sent out, in the one-on-one conversations with key investors. The meeting itself is where investors confirm that the deal is as described and that the sponsor is credible.

The lender presentations and information memoranda you circulate are often where the actual persuasion happens. The IM is a detailed document—often fifty to a hundred pages—that walks through the business, the market, the financials, and the risks, and it is the document investors will refer back to when doing their own analysis.

An information memorandum should be comprehensive without being overwhelming. Investors need to find the information they are looking for without wading through five pages of boilerplate to reach a critical data point. Use tables, charts, and clear formatting, and make the document easy to navigate.

The risk section of the IM matters particularly, because it is where you show that you have thought about what could go wrong. Be specific and avoid vague language: do not just write "competitive risk." Explain what the competitive risk is, what the barriers to entry look like, and what would have to change for competitive intensity to increase.

Managing investor questions and concerns during syndication is where your communication skills get tested. Investors ask hard questions; some are skeptical, and some have legitimate concerns. Your job is to address those concerns clearly and honestly.

Hypothetical example: in a lender presentation for a recapitalisation, an investor may ask how technology could disrupt the borrower's service model over the life of the debt.

A credible answer would acknowledge the risk, identify verified investment and operating milestones, explain what evidence is still missing and show the downside if the mitigation fails. Management optimism is not a substitute for diligence.

Investor support, if it follows, may reflect many factors. The point is simply that a specific, testable response is more useful than dismissing the disruption risk.

Then there is the feedback loop: relaying market feedback to the borrower. During syndication you hear from dozens of investors, and some will raise concerns or point out weaknesses in the deal thesis. You need a process for passing this back to the borrower and the sponsor, because the feedback will often inform how the deal is managed from there.

Composite illustration: if several investors identify customer concentration that the sponsor has underweighted, record the feedback, validate the data and test whether a diversification plan is credible. Do not promise that a first-hundred-days plan will make investors comfortable.

Handling negative feedback constructively means resisting the urge to be defensive. Legitimate concerns will matter whether or not you engage with them, so address them head-on rather than hoping they are forgotten. Where a concern rests on incomplete information, supply the information. Where it rests on an investor's own biases or experience in a different asset class, acknowledge it and explain why you think it is less relevant in this context.

The roadshow raises the question of in-person versus virtual. For larger deals, you may visit major investors' offices with the sponsor to present the deal. This is expensive and time-consuming, but it is often necessary for large syndications or for sponsors without an established relationship with the investment community.

In-person roadshows differ from virtual ones. In person you can read the room: you can tell when an investor is genuinely interested rather than politely listening, the side conversations over lunch or coffee tell you more about what an investor actually cares about, and rapport builds in a way that is harder over video.

That said, virtual roadshows have been standard since the pandemic, and they work. In some respects they are more efficient: you reach more investors without the travel, and the session can be recorded so investors can share it with their investment committee. The trade-off is the loss of some of the relationship-building that happens in person.

Choose format based on audience, complexity, accessibility, confidentiality, cost and investor preference. Neither in-person nor virtual delivery is inherently better for a large or educational deal, and recording requires explicit approval.

Negotiating with Counterparties: The Art of Getting What You Need

Leveraged finance is full of negotiation: documentation with counsel, terms with the borrower, positions with other lender groups, capital structure with the sponsor. These negotiations can make or break a deal, and they call for specific communication skills.

The first principle of effective negotiation in leveraged finance is to understand the other side's constraints and incentives. Every party in a transaction has constraints: the borrower on how much leverage it can take, driven by lender requirements; the sponsor on how much equity they are willing to put in, driven by return hurdle rates; other lenders on what their credit policy allows; your own credit committee on portfolio limits and risk appetite.

If you understand these constraints, you negotiate more effectively, because you propose solutions that work within them rather than asking the other party to violate their own stated policy.

Hypothetical negotiation: a sponsor requested a three-year maintenance-covenant holiday, while lenders wanted earlier financial visibility. That is not the same as 'five years of covenant-lite status'; cov-lite ordinarily describes a facility without a term-loan maintenance covenant, often with a springing RCF test.

The parties should identify the underlying concern: operating flexibility, avoiding a technical default, early warning, or control. Any compromise must be expressed in precise testing, information and cure provisions.

A bespoke outcome might combine an initial covenant holiday with later step-in testing or enhanced reporting. It should not be labelled covenant-lite without checking the actual structure, and counsel must draft and review the effect.

The documentation negotiation is where many people miss communication opportunities. The markup process is simple in form: one side's counsel produces a draft agreement, the other side provides comments, and the drafts go back and forth. It can be adversarial, but it does not have to be.

A useful habit: when reading a counterparty's comments on a draft, work out not just what they are asking for but why—whether it is a matter of principle, a belt-and-suspenders concern, or something driven by their credit committee or their counsel's standard practice.

When responding to comments, address the underlying concern. If a lender requests monthly financial statements for visibility, a possible alternative is quarterly financial statements plus agreed monthly management accounts or KPIs, subject to feasibility, confidentiality and the document's definitions.

Email versus phone versus in person: choosing the medium is underrated. Email is efficient—you can send a message at midnight and the point is recorded. It is also efficient at creating misunderstandings: tone is hard to convey, and a message that seems straightforward to the writer can read as aggressive or dismissive to the recipient.

A useful rule: use email to confirm decisions and document agreements, but if you are trying to move someone off a position or understand why they hold it, pick up the phone or ask for a call. Calls beat email for negotiation because you can hear tone, clear up misunderstandings in real time, and often reach creative solutions faster than you can in writing.

In person is best for initial negotiations on genuinely substantive points: you can read body language, see whether someone is truly dug in or defending a position for show, and build rapport more easily. Video calls are a reasonable middle ground, though not quite as good as being in the room.

Multi-party negotiations are where communication becomes genuinely complex. A deal may involve a sponsor, a borrower, a lead arranger, co-arrangers, other lender groups, and counsel for the borrower, the lenders, and the sponsor. Each party has slightly different interests, some aligned and some not.

What matters is understanding clearly where alignment and misalignment sit, and structuring the negotiation accordingly. Sometimes you negotiate bilateral agreements first (arranger with borrower on the business terms, arranger with sponsor on the capital structure) and then bring those into the broader negotiation. Sometimes you get everyone aligned early, because any bilateral agreement will affect the others.

Composite illustration: a restructuring with several creditor groups may use bilateral and multilateral sessions in a sequenced process, but only after counsel maps information-sharing, privilege, antitrust, conflicts, voting and confidentiality constraints.

Sequencing can reduce open issues, but bilateral agreements can prejudice absent parties or fail to bind them. Map who has authority at each stage, which parties are affected and which decisions remain subject to sponsor, lender or committee approval.

When to push and when to concede is a matter of judgment. If something genuinely matters to credit quality, push; if it matters to the relationship but is not critical to the credit, concede. The common mistake is treating every point as equally important.

A useful negotiating style can be described as "reasonable but not soft." Be willing to move on points that do not matter materially to the credit, because the other party should feel the process is fair. But where something matters—a covenant, a restriction, a payment priority—hold the line if moving would materially affect the dynamics. Have clear reasoning behind each position, and be able to explain why you are pushing on some things and not on others.

Do not infer a negotiating style from a party's nationality or continent. Communication norms vary by individual, institution, legal system, language, mandate and transaction, and broad regional stereotypes can cause the very misunderstanding they purport to prevent.

In a cross-border deal, ask each participant about decision authority, process, documentation, timing, language and escalation preferences. Treat those answers as deal-specific rather than as evidence about Americans, Europeans or Asians generally.

Adapt the process to the preferences actually expressed, document decisions and confirm understanding. A faster close cannot be attributed to cultural tailoring without evidence.

Stakeholder Management in Restructuring: When Everything Gets Harder

Restructuring is where the stakes of communication are highest. Working through a restructuring—a covenant amendment, a refinancing, or a full debt exchange—means managing parties with conflicting interests, dealing with asymmetric information, and usually operating under time pressure.

Communicating with a distressed borrower is different in kind from communicating with a healthy one. The healthy borrower is trying to optimize; the distressed borrower is trying to survive. Its tone with you will vary: sometimes desperate, sometimes angry, sometimes resigned. You need to remember that you are not having a normal business conversation.

Composite illustration: when a distressed borrower's finance team is overwhelmed, begin by clarifying the immediate facts, required deliverables, decision owners and deadlines. Do not diagnose the individual or assume that a written message is always preferable.

A concise written action list can help after the call, provided it is accurate, appropriately privileged or confidential and clear about consequences. Counsel and the relevant decision-makers should review material default or remedy communications.

Creditor groups can have different priorities because of lien position, contractual ranking, maturities, holdings, hedges, liquidity needs and expected recoveries. Do not assume all first-lien, second-lien, loan or note holders share one objective.

The communication problem is that you cannot say the same thing to everyone, because their interests differ, yet your messages to the different groups cannot diverge so far that you are caught in a contradiction.

Communicate verified business facts consistently across creditor groups while tailoring analysis to each group's rights. Any differential disclosure must comply with confidentiality, MNPI, privilege, equal-information and negotiation rules; do not use selective pessimism or optimism as leverage.

Advisors often serve as communication intermediaries. Most restructurings involve financial advisors, legal advisors, sometimes insurance advisors, all of them parties to the process, and they frequently end up carrying messages between groups with conflicting interests—particularly where the borrower has to stay in the middle between creditor groups.

Composite illustration: a restructuring adviser may gather authorised positions from creditor groups and test structures against each group's rights and constraints. The adviser cannot promise a solution that works for everyone or share one group's confidential position without authority.

Press and public communication in a restructuring is its own problem. A restructuring often attracts media interest, particularly for a large or well-known business, and two questions need answering: what is being communicated to the public, and who is doing the communicating.

Public communication is ordinarily led by the borrower or issuer through authorised spokespeople, with legal, regulatory and communications review. Lenders should not coordinate public messaging or speak to the press unless authorised and permitted by law, confidentiality duties and policy.

Information can affect negotiating leverage, but possession does not create a simple hierarchy of power. Borrowers, sponsors and creditor groups hold different information, rights and constraints; access must be lawful, authorised and consistent with confidentiality and market-abuse rules.

This is why access to information—management calls, financial reporting, operational metrics—matters so much in distressed situations. The more information you hold, the stronger your position in any negotiation.

Distressed processes may involve material non-public or inside information. Trading, disclosure, wall-crossing, restricted-list and recordkeeping consequences depend on jurisdiction, instrument, role and facts. Follow legal and compliance instructions before communicating or trading.

Do not signal that you possess restricted information or improvise what can be shared. Use approved participants, channels and scripts, and ask legal or compliance before any communication where information barriers may apply.

Then there is leaked information and the rumor mill. Any restructuring, especially a large one, generates rumors: employees wonder whether they will lose their jobs, customers wonder whether the company will survive, suppliers wonder whether they will get paid. Some of those rumors rest on accurate information; some are speculation.

Do not assume where a leak originated. Preserve evidence, notify legal and compliance, follow the incident-response plan and ensure that any correction or disclosure is made only by an authorised party.

Responses to rumours must be authorised and legally reviewed. 'No comment' may or may not be appropriate; the issuer's disclosure obligations, confidentiality restrictions, market-abuse rules and accuracy of any statement control.

Internal Communication

Managing up—communicating with senior bankers and portfolio managers—is a skill junior people tend to underestimate. Your senior people do not know everything you know about a particular credit; they are running multiple credits, relationships, and responsibilities at once. If you want them positioned to advocate for your deal or support your recommendation, you have to keep them informed.

A useful rule: do not let a portfolio manager be surprised in front of the credit committee. If something about a credit has changed in a way that might affect approval, the PM needs to know before the committee meeting—which means getting to them ahead of time, walking through the issue, and explaining what has changed and what it means.

This is not office politics; it is respect for the person ultimately responsible for the portfolio, who needs the information to do the job. It also makes your own life easier, because a PM who is already comfortable with your analysis is not going to blindside you in committee with a different point of view.

Managing across—coordinating with legal, compliance, operations—is where communication breaks down in many organizations. Credit, legal, and compliance people have different incentives and work in different worlds: credit wants to move fast and get deals done, legal wants the documentation right, compliance wants everything properly reported and clear of regulatory issues.

None of these incentives is bad; they are simply different. Managing across the functions means understanding what each group cares about and involving it at the right point in the process.

With legal, the aim is to involve them early enough that you are not asking them to fix something at the last minute, but not so early that a preliminary discussion gets bogged down in documentation questions. Once it is reasonably clear the business terms will work, brief legal on the structure and the key issues, and run the documentation process in parallel with the syndication discussions.

With compliance, identify relevant risks early, which may include sanctions, anti-bribery and corruption, conflicts, market conduct, client classification and transaction-specific regulatory issues. The applicable regime depends on the entities and jurisdictions; use the firm's approved monitoring and escalation process.

Managing down—mentoring junior team members—is where your communication style propagates. If you communicate clearly, junior people learn to communicate clearly; if you communicate imprecisely, they will too.

When mentoring junior people, it helps to explain the "why" behind communication choices: why we lead with that point instead of this one, why the risks are presented first instead of buried, why the email was structured the way it was.

Synthetic coaching scenario: an analyst submits a memo that is too long and poorly organised. The reviewer revises one section with the analyst, identifies its decision purpose and asks the analyst to apply the same principles independently to the rest of the document.

The weekly update is how stakeholders stay informed. If you are managing a credit or a transaction, you are probably sending one, and they are easy to do badly: they turn into laundry lists of the past week's activity with no clear sense of what matters.

A good weekly update has a clear structure: the status of the transaction or the credit situation, what is being worked on, what is being waited on, and what the next step is. If something has changed or new information has arrived, lead with that; if the week was routine, be brief.

It is common to receive daily updates from team members that run longer than the weekly update, which is a sign of disorganization. If you are sending daily updates, they should carry genuinely material news; otherwise you are

creating noise.

On escalating problems: when something goes wrong with a credit or a deal, the first instinct is often to try to solve it before anyone knows it exists. That is usually a mistake. If the problem is real, the longer you wait to escalate it, the worse it gets.

Hypothetical example: a material revenue decline should be escalated promptly while the analyst validates the source and begins diagnosis. The team should distinguish preliminary data from confirmed fact and follow the reporting protocol.

That does not mean escalating every small issue. Escalate what is material, what requires senior-level decision-making, and what gets worse the longer it goes undisclosed. A useful test: would your boss rather hear about this problem from you in its early stages or from the credit committee in the middle of a default? If the answer is "from me in the early stages," then escalate early.

On the concise email: email cuts both ways. It lets you communicate asynchronously and creates a record of what was said; it also gives people room to be long-winded and lets important information get buried in the process.

A concise email should front-load the decision or question, provide enough context and end with clear owners and next steps. One screen is a useful discipline for routine updates, not a universal limit for matters that require a complete or legally adequate record.

Composite example: a long restructuring email can obscure the required decision. Preserve any context needed for an adequate record, then lead with the recommendation, alternatives, evidence and requested action.

A concise follow-up can be useful, but do not assume one screen is always enough or publish a private quotation without confirmation. Link or attach the underlying record when the decision requires it.

Building and Maintaining Client Relationships

Building long-term relationships with sponsors and borrowers is where the practitioner's view of the business matters. Deals are transactional; relationships run for years. Approach every interaction as a transaction and you will do tolerably on individual deals while missing the chance to build something durable.

Some sponsor and borrower relationships extend across multiple transactions and market conditions. They endure when the parties communicate candidly, perform reliably and respect mandate, confidentiality and conflict boundaries rather than treating every interaction as isolated.

That means being patient when they ask for terms a lender does not want to give, because their incentives differ. It means telling them honestly when they appear to be making a mistake, rather than going along with whatever they want. And it means staying engaged between transactions, rather than calling only when there is a deal to discuss.

A transactional relationship is one where you are there to execute a specific transaction; an advisory relationship is one where the client treats you as a trusted advisor. The move from one to the other happens slowly, and it rests on demonstrating that you understand their business, that you have their interests in mind, and that you can be trusted with sensitive information.

Moving from transactional to advisory requires showing up differently: offering perspective on their business and strategy rather than only on the deal you are executing, understanding their constraints and objectives, and being able to say no to things that do not work for them, not just to things that do not work for you.

Hypothetical example: if a proposed acquisition appears strategically weak even though the financing is acceptable, an adviser can state the concern, evidence and limits of the mandate. Avoid predicting that the sponsor will regret the deal within a year.

Candid advice can strengthen trust, but it can also be wrong. Separate evidence from judgment, state the limits of the mandate and avoid predicting how one piece of advice will affect a client's decision or future relationship.

Delivering bad news—repricing, downgrades, covenant concerns—is a skill the job requires. There are times when you must tell a client something they do not want to hear: the market has moved and their pricing is now below market; the credit rating is being downgraded; covenant compliance is a concern.

Deliver bad news clearly, directly, and respectfully. Do not sugarcoat it and do not bury the lede: say what is going on, explain why it is happening, and set out what you are going to do about it.

Hypothetical repricing: if comparable new loans price thirty basis points tighter than an existing borrower's loan, the borrower may request a lower margin. The lender must assess relationship value, amendment economics, consent mechanics and the alternative risk of refinancing.

A clear call would say: 'Comparable market pricing has tightened. Subject to approvals and documentation, we are prepared to discuss reducing the margin to the following level.' The lender, not the borrower, would be accepting lower pricing on the asset.

A repricing can reduce lender income and may preserve a relationship or reduce refinancing risk. Those trade-offs should be quantified rather than presented as a verified relationship success.

Managing expectations across the lifecycle of a deal is where consistency in communication matters. What you promise during the sales process you must deliver during the transaction and afterward. If you have said you will be a supportive lender and will work with the borrower if problems arise, then when problems do arise you have to actually be supportive and willing to work with them.

Any flexibility on covenant testing must be contained in the executed documents or a properly authorised amendment or waiver. A lender should not make an informal promise to disregard a test or delay remedies.

A documented, authorised waiver process can support a relationship, but relationship considerations do not override lender duties, voting mechanics, credit judgment or policy.

Follow-up means staying engaged between transactions. It helps to check in with important clients at least once a quarter even when there is no active transaction: a brief call to ask how the portfolio companies are doing, whether there is anything to help with, and to pass on relevant market information. The point is to stay on their radar and to maintain the relationship.

Appropriate hospitality may help relationships, but a baseball game is not inherently more effective than professional communication. Apply gifts, entertainment, anti-bribery, expense, conflicts and equal-access policies.

Repeat business is the foundation of a sustainable credit business. Do good work on one deal and maintain the relationship, and you will get the next one; do good work on ten deals and the next deals multiply. Give a client a bad experience and their next deal goes to someone else.

Repeat work may follow trust and good execution, but mandate outcomes also depend on price, capability, conflicts and competition. Treat repeat business as a possible outcome, not proof of a causal relationship.

Cross-Cultural Communication in Global Finance

Working across time zones and cultures has become standard in global leveraged finance over the past fifteen years. Deals span European sponsors, Asian borrowers, Middle Eastern lenders, and African operating companies, and each of those regions carries its own communication norms, cultural expectations, and business practices.

Time zones are a logistics problem with a communication component. With sponsors in Europe and borrowers in Asia, getting everyone on the same call at an hour reasonable for all parties is difficult. The way to manage it is to acknowledge the constraint and to run a clear protocol for asynchronous communication.

Hypothetical cross-time-zone process: circulate a clear decision paper through approved channels, set a realistic comment period and reserve live time for unresolved issues. Forty-eight hours may be too long or too short, and data-location, confidentiality and recordkeeping rules still apply.

An asynchronous process can work when expectations and records are clear, but do not claim it did work for an unidentified deal without evidence. Monitor whether the process creates delay, exclusion or information-security risk.

Communication preferences differ across people and organisations. Ask whether participants prefer direct proposals, formal written process, additional context, bilateral discussion or more time for internal consultation.

Hierarchy and process can matter in any organisation. Establish who can decide, who must be consulted and how disagreement should be recorded; do not infer those features from a European label.

Indirect disagreement and relationship-building occur across cultures and institutions. Check understanding explicitly and provide more than one channel for concerns, without assuming that an Asian participant will avoid direct disagreement.

Country, firm, role, language and individual preference produce more variation than continental labels capture. Use observed behaviour and stated preferences, not stereotypes, to adjust communication.

Composite illustration: a participant's silence in a group meeting should not be treated as agreement. A bilateral follow-up can ask directly whether the participant supports the proposal and whether any concern was difficult to raise in the larger forum.

If the follow-up identifies a concern, document it and test a revised structure. The lesson is to confirm assent, not to generalise about how a regional lending group communicates.

Language matters in cross-border deals. Not everyone involved is a native English speaker, and even people highly proficient in English may be less precise in it than in their own language. That has implications for how you communicate.

First, speak more slowly and clearly, use shorter sentences, avoid idioms and slang, and check for understanding more often.

Second, take care with written communication. Misunderstandings emerge from email exchanges where something was ambiguous in English and the parties interpreted it differently.

Use plain language to explain commercial intent, but do not paraphrase away legal effect or give legal advice outside your role. Non-native speakers should have adequate time, qualified counsel and, where appropriate, an agreed translation; the executed language and governing-law rules control.

Hypothetical example: if a finance officer says the covenant operates differently from their understanding, stop and ask counsel to confirm the drafting, explanation and any required amendment. Do not treat a commercial paraphrase as authoritative legal interpretation.

Composite illustration: if sponsor and lender expectations on leverage differ, clarify whether the issue is maximum leverage, pricing, return threshold, credit policy or portfolio concentration. A higher return hurdle does not by itself explain a more aggressive leverage ratio.

Once the actual constraint is identified, the parties can test alternatives. Do not describe a lender as gouging or claim that clarification resolved the matter without evidence.

Rapport is personal and situational. Learn what builds trust for the people involved rather than assigning preferences to a culture.

Avoid dividing counterparties into high-context and low-context blocs. Ask each person how they prefer to build trust, exchange drafts, make decisions and resolve disagreement.

Invest in both relationship quality and execution: learn the counterparty's stated preferences, respect boundaries, communicate clearly and deliver what was promised. Do not prescribe personal familiarity based on perceived culture.

Effective cross-border communicators adapt to the people, mandate and process in front of them and revisit assumptions when the evidence changes.

Communication in Crisis: When the Stakes Are Highest

When a portfolio company hits trouble—covenant breach, unexpected loss of a customer, departure of a key executive, competitive disruption—the communication protocols need to shift immediately. Normal cadences no longer apply.

The immediate protocol in a crisis starts with the facts: you need to understand what happened and why, talk to the borrower, understand their perspective, and work out what information you need in order to make decisions.

Then inform the internal stakeholders: the portfolio manager needs to know; the credit committee may need to know; the trading desk may need to know if there is a mark-to-market issue to manage; compliance may need to know if there are regulatory implications.

Then settle the external communication strategy: whether you will ask the borrower to notify the other lenders, whether you will meet the other lenders as a group, and on what timeline that should happen.

Then there is the board call, and the problem of structuring difficult conversations. In a crisis you may be on calls with the borrower's board, other lenders, or your own credit committee—high-stress conversations in which everyone is trying to understand what is happening and what happens next.

Structure these calls with a clear agenda, present the facts cleanly, and be explicit about what you are asking people to do or decide.

Composite crisis example: after a material customer-loss notice, a board call should separate known facts, open questions, financial implications, immediate workstreams and requested decisions. Management, counsel and the chair should agree roles.

A structured agenda can improve a board or committee meeting, but minutes, privilege, disclosure obligations and delegated authority must also be managed. Use only fictional examples or duly authorised public records when illustrating board dialogue.

Having that structure and sticking to it made the conversation more productive. The news was still bad, but people understood what was happening and what the plan was.

Managing information flow during a restructuring matters because information is currency there. The operative question is what you are sharing, with whom, and when.

In a restructuring, share information only when authorised, for a legitimate purpose and through approved channels. Adequate information can reduce distrust, but broader disclosure is not presumptively better and may

breach confidentiality, market-abuse, privilege or data-protection obligations.

That said, there are legitimate reasons not to share information: MNPI restrictions, confidentiality agreements with the borrower, and strategic reasons not to reveal your hand before you are ready.

Be transparent about process without signalling restricted content. Use a legal- or compliance-approved explanation of participation and information constraints, and do not list what you know or imply that undisclosed facts exist.

Potential sanctions, anti-bribery and corruption, market-conduct, disclosure or reporting issues should be escalated promptly through the firm's legal and compliance process. The relevant people and timing depend on the facts; preserve confidentiality and avoid unsupported conclusions.

The right people include the compliance function, the legal function, the credit team, and senior management. What you cannot afford is ambiguity about what the concern is or how serious it is.

Hypothetical compliance example: when a potential sanctions issue is identified, the alert should state verified facts, uncertainty, interim controls, owners and escalation path. Recipients should not infer legal conclusions beyond the compliance or legal assessment.

A written assessment can align stakeholders, but distribution, privilege, need-to-know and recordkeeping must be controlled. Do not claim that one memo fixed the issue without evidence.

On press management and reputation: a credit in default or restructuring often attracts media interest, and you need to decide how you are going to respond.

Generally the borrower handles press communications. As a lender, though, you may need to think about how the coverage affects your own reputation: if the press reports that you are being harsh with a struggling borrower, that can affect your relationships with other sponsors and borrowers.

A lender should not shape the borrower's press position informally. Any external response must be accurate, authorised and reviewed for confidentiality, privilege, market disclosure and regulatory obligations.

A default or restructuring may require a regulatory filing or other public announcement when applicable law, listing rules or the issuer's disclosure controls require it. Private-company situations may remain confidential. Counsel should determine the obligation and timing.

The press release should be factual, explain what happened in plain English, and outline the path forward. It should not be defensive and it should not make excuses; it should acknowledge the situation and set out the plan to address it.

What Experience Teaches About Communication

Across careers, strong communication often accompanies effective leadership, but no observation of hundreds of professionals proves that communicators are the most successful or that technical ability matters less. Treat the characteristics below as useful practices, not causal findings.

Good communicators in finance share several characteristics. First, they are clear: they can explain complex things in simple terms, take a hundred pages of analysis and extract the five key points, and tell the difference between what matters and what does not.

Second, they are honest. They do not sugarcoat and they do not hide: if something is wrong with a credit they say so, and if they do not know something they say that too. Over time this builds trust, because people learn that when this person says something is fine, it actually is fine.

Third, they are consistent. They treat people with respect in good times and bad, follow through on what they say, and maintain relationships over decades. That consistency creates loyalty, and the loyalty translates into repeat business.

Fourth, they listen. They work to understand the other person's perspective and constraints, and they ask questions before making assumptions; they are genuinely trying to understand, not just trying to persuade.

Fifth, they adapt. Different people need different information presented in different ways, and these communicators can be data-focused when someone needs data, narrative-focused when someone needs narrative, efficient with efficient people, and relationship-focused with relationship-focused people.

Clarity beats complexity. People with sophisticated views of a deal often bury those views in complexity—jargon and elaborate constructions deployed to sound smart. The trouble is that complexity makes a view harder to attack but also harder to understand, and a view people cannot understand is a view they cannot act on.

The best communicators are disciplined about clarity. They have thought their analysis through, which is precisely why they can explain it simply; they do not need complexity, because they are not using it to hide uncertainty or weakness. Clarity is a sign of deep thinking, not shallow thinking.

Communication matters from the start of a career: junior work also affects records, controls and decisions. Its form changes with seniority as responsibility for clients, committees and teams expands.

A senior person's reputation can affect how efficiently a committee processes a recommendation, but it must not substitute for evidence, independent challenge or consistent approval standards. Better analysis should be surfaced regardless of rank.

The compounding works through reputation. Once you are known to communicate clearly and honestly, that reputation follows you: new clients trust you faster, credit committees approve your deals more readily, sponsors want to work with you. The communication skills that built the reputation accumulate over time into a significant career advantage.

On building a personal communication toolkit: people have different strengths. Some write well but are less comfortable in person; some are excellent presenters but struggle in one-on-one negotiations; some manage up well but are less comfortable delivering bad news.

The successful practitioners are the ones who have identified their strengths and weaknesses and built a toolkit that compensates for the weaknesses while making use of the strengths.

If you are not a natural writer, you invest in becoming a better one, because written communication carries so much weight in this business. If you are not a natural public speaker, you practice public speaking. If you struggle with difficult conversations, you keep frameworks and scripts that help you navigate them.

Few people are naturally good at public speaking, and nervousness before presentations is common. One remedy is a routine that settles you before big presentations. Another is volume of practice, so that when you present to a credit committee you are not working out what to say but executing something already thought through—which reduces the anxiety and improves the execution.

Mentoring others in communication is worth the effort precisely because the skill compounds over a career: junior people who develop it early benefit from it for decades.

Invest time in coaching junior people on writing, presenting, negotiating, and managing relationships: give feedback on their memos, have them present to you before they present to a committee, run role-plays of difficult conversations. It takes time, but it accelerates their development.

Composite coaching example: revise a difficult memo section together, explain the structure and have the analyst apply the principles to a new section before review. Keep the employee anonymous and do not claim a later title as proof of causation.

Writing can improve through repeated, specific feedback and deliberate practice. Coaching may support development, but it does not by itself determine promotion or career outcomes.

Conclusion

This chapter opened with a composite case in which communication weakened the decision process, while the later credit loss reflected the underlying business and structure. Communication can improve understanding and governance; it does not determine whether a weak credit performs.

The lesson is that communication is not an ancillary skill in leveraged finance but a core one, arguably the core one. The technical ability to model a deal is necessary but not sufficient: you also need to communicate the model to skeptics, manage stakeholders with different interests, deliver bad news without damaging relationships, and negotiate effectively across cultures and time zones.

The practitioners who have built the most successful careers are generally not the ones who chased the last basis point in their models; they are the ones who invested in communicating well, having understood that in a business built on relationships and trust, communication is the foundation.

If you are early in your career in leveraged finance, invest in communication skills now: take the time to write clearly, practice your presentations, seek feedback from senior people, think through difficult conversations before you have to have them, work at understanding other people's perspectives and constraints, and build relationships before you need them.

People who handle communication, relationships, trust and integrity well can build durable careers, but security, respect and success also depend on technical quality, conduct, results, opportunity and the institution in which they work.

Those elements matter most, and they are also the ones you can influence directly, day to day, through the choices you make about how you communicate.

Career Advice — What Nobody Tells You

This is the chapter many people would have wanted at twenty-five, convinced they had no idea what they were doing and that everyone around them was smarter, better prepared, and somehow born understanding leveraged buyouts. Some of what becomes obvious later is worth knowing early: most of any training program is also just learning on the job; the people ahead of you feel roughly the same blend of confidence and fraud in roughly the same proportions; and a career in leveraged finance is less a clearly marked mountain path than a dense forest in which you occasionally look up and realize you have made real progress without quite knowing how you got there.

Most career advice in leveraged finance books is terrible. It is either viciously practical in a way that strips out all context ("here's how to model an LBO") or aggressively motivational in a way that bears almost no resemblance to the actual experience of working in this industry. The aim here is to be honest. That means acknowledging that this career is often exhausting, sometimes demoralizing, occasionally brilliant, frequently tedious, and capable of being genuinely meaningful if you approach it with the right mindset. It also means talking about the people who get left behind, the trades everyone makes between money, time and dignity, and the fact that the best people in this industry are not always the ones at the top of the compensation ladder.

This is not a field guide to breaking into credit investing; other parts of this book cover that, and the technical skills are teachable — they are just work. The subject here is the part nobody really teaches: how to build a career in leveraged finance that is sustainable, satisfying, and aligned with who you actually are rather than who you thought you were supposed to become.

The First Steps into a World You Don't Understand Yet

People often get into leveraged finance almost by accident. The common path runs through an economics degree, decent grades and no clear idea what to do with your life, beyond knowing that you like solving problems, you're decent with numbers, and you want to make more money than your parents did — not the noblest motivation, but an honest one. An internship at a boutique investment bank turns into a full-time analyst offer, which you take because it seems like the next logical step and because the alternative, uncertainty, is terrifying.

A structured analyst programme at a large bank is one route into leveraged finance, not the traditional route for everyone. Entry points also include regional banks, private-credit platforms, rating agencies, law firms, advisory firms, corporate finance teams and adjacent roles. The quality of training, supervision and substantive exposure matters more than any short list of firm names.

Hiring criteria vary by employer and role. From a practitioner perspective, recurring themes include analytical capability, judgment, communication, reliability, ethical conduct and evidence of learning.

Reliability matters: agree the requirement, deliver on time or escalate early and use review controls. Promotion depends on broader performance, judgment, conduct, opportunity and institutional criteria; it cannot be attributed to a zero-error record.

Third, they want some evidence that you are not going to be a catastrophic human being to work with. They want to hear about times you've worked in teams, how you handled conflict, what you learned from failure. The honest version is that this last piece is about fit — not just intellectual fit, but whether you are someone the team actually wants to spend fifty to seventy hours a week with.

Interview formats vary and may include credit cases, modelling, document analysis, writing or behavioural assessment. Prepare to explain the reasoning, assumptions and limits of your work rather than memorise a

template.

The case study is often the easier part of the interview, though. The harder part, which nobody really teaches, is managing the five other conversations that day. The senior person's question is often not testing your knowledge; it is testing whether you will defend your work or cave the moment someone challenges it. The operations person is assessing whether you respect the infrastructure of the organization or will be dismissive about things that do not seem directly related to "the work." And in the quiet moment with the person who would be your boss, you are trying to work out whether this is someone who will actually develop you or just burn you up on project work.

Networking in this field is often described as essential, and it is, but most of the advice about it is actively harmful. Most people approach it as a transaction: have coffee with this person and extract value, build a relationship with this potential client, attend the conference and work the room. That approach works badly. What works is being genuinely interested in people, staying in touch with them for reasons that are not immediately about you, and being the person who is helpful rather than helpful-seeking.

Look across the people who have materially influenced a career and the pattern is often broader than formal mentors: peers, colleagues at other firms, lawyers and people met through shared work. Healthy relationships are reciprocal over time; asking for appropriate advice or help does not turn them into extraction.

Synthetic teaching scenario: a mentor invites a junior colleague to an authorised meeting because the colleague has a defined role, then gives specific feedback on preparation and communication.

You can ask a potential mentor for a bounded conversation or periodic check-in, while accepting that they may lack time or see a conflict. A direct manager can sometimes be an effective mentor, but the evaluative relationship should be acknowledged and additional perspectives may help.

Getting into leveraged finance is typically a matter of small decisions in sequence. You take the analyst role because it seems like a good opportunity at the time. You work hard and deliver quality work, which opens the next door. You have good luck with some of the deals you work on early (they go well, you learn a lot, you meet interesting people) and bad luck with others, but by then you have developed enough capability to learn from the failures rather than be destroyed by them. There is no blueprint; there is a willingness to show up, to try to do good work, to be open to luck when it comes, and to think carefully about the next decision rather than assuming there is only one possible path.

The First Three Years: Learning to Build in the Dark

The first year can involve substantial uncertainty while unfamiliar terminology, models and documents become routine. Feeling stretched is common; unclear priorities or an unmanageable workload should be discussed early with a manager or trusted colleague.

With repeated modelling, document review and credit discussions, unfamiliar concepts gradually become routine. The questions become narrower and more useful: not simply what leverage means, but why two investors may evaluate the same leverage-ratio step-down differently.

Timely review is part of learning, but speed does not excuse an unvalidated model. Agree the scope and deadline, build a controlled first pass, flag uncertainties and obtain review before the work informs a decision.

The technical skills are demanding but learnable: building controlled models, reading documents with counsel where appropriate, analysing financial performance and asking disciplined questions about the business and downside. Mastery requires instruction, practice, review and continuing learning.

Junior professionals will make mistakes. The useful response is to identify the effect, escalate it promptly, correct it, improve the control and understand whether training, workload or supervision contributed.

When a mistake occurs, disclose it promptly, explain the impact and containment, and agree corrective action. A short acknowledgement can help, but one script does not determine whether someone is worth developing.

Hours vary materially by role, firm and deal cycle. Late nights or weekend work can occur, but chronic fatigue is neither a reliable operating model nor a mark of professional quality. Judge the role by its actual pattern and whether that pattern is sustainable for you.

Seniority does not guarantee lighter hours or greater control; responsibility can increase even as task mix changes. Assess the actual team, staffing model, travel, on-call expectations and flexibility rather than relying on title-based assumptions.

Errors can involve assumptions, data, formulas or interpretation. Use version control, source checks, reconciliations, independent review and post-mortems to reduce recurrence; do not assume every error becomes a lesson automatically or only happens once.

Junior team members should ask questions and raise good-faith concerns, especially about accuracy, conduct, safety or control failures. Calibrate the method and evidence, but do not let rank prevent timely escalation through the channels available to the team.

Hypothetical example: a junior analyst who doubts a growth assumption should present the evidence and sensitivity. The accountable decision-maker—not simply 'the boss'—must ensure that the assumption is tested and the dissent recorded where material.

A sound early-career reputation rests on reliability, quality, curiosity and conduct. The objective is not error-free work but work built and reviewed under appropriate controls, with uncertainties and mistakes surfaced promptly.

The Transition: From Executing to Thinking

Somewhere between year three and year five, if you are on a reasonable path, you shift from executing other people's ideas to beginning to have ideas of your own. You start to lead small parts of deals. You are in the room when the team decides what to work on, not just once the decision is made. Depending on the firm you might be called an associate, a senior analyst or a VP, but the transition is real regardless of the title.

This is where the job starts to feel different. The hours are still substantial, but some of them now go to thinking about strategy rather than just modeling. You are responsible for maintaining quality but also for delegating some of the work. You begin to interact with clients, not as a spectator but as someone representing the firm.

The shift from executor to manager is harder than most people anticipate. As a junior analyst the job is clear: build this model, analyze this document, answer this question. Managing other people's work is much less clear. You have to delegate effectively, which means trusting others to do good work, which means not micromanaging — hard when it is ultimately your name on the output. You have to communicate what you want clearly enough that people can execute without you standing over them. And you have to be confident enough to push back when something isn't right, without being so controlling that people feel treated like children.

Composite leadership example: an associate coordinating two analysts defines roles, reviews critical cells and assumptions, reconciles outputs and escalates unresolved issues. Confidence follows validation; it is not a substitute for it.

Leadership is not perfection, but it does require controls proportionate to the stakes. Define ownership, review critical work, encourage escalation and learn from misses; confidence is not a substitute for quality assurance.

Client interaction is a different skill from the technical work, and a lot of people underestimate how important it is to develop it early. When you are junior you are mostly invisible to clients: you are building the model or doing the

analysis, but the client barely knows you exist. As you move up, you start to represent the firm — presenting the analysis, fielding the questions, holding the relationship.

This is fundamentally about communication and trust. Clients need to trust that you understand the situation, that you are honest with them about the risks and opportunities, and that you are not just telling them what they want to hear. They also need to find you credible. Technical knowledge helps, but credibility comes mostly from thinking seriously about their business, asking intelligent questions, and being forthcoming when you don't know something.

If a client asks a question you cannot answer, say what you know, what you need to verify and when you will respond. Do not promise next-day delivery unless feasible, and do not assume every client is satisfied by the same response.

The value of an MBA is role-, school-, geography- and candidate-specific. It may support a transition, network or formal recruitment channel, but it is neither required for credit investing nor a reliable route to any particular platform. Check current hiring evidence before deciding.

Evaluate tuition, living costs, foregone compensation, immigration or licensing effects, financing risk and the probability of achieving the intended transition. Full-time, part-time and executive programmes have different trade-offs; none is generally the better choice.

A move to an investing role can offer a different mix of compensation, autonomy and accountability, but none is necessarily better. Fund strategy, mandate, resources, vesting, performance and culture determine the actual experience.

Sell-side and buy-side roles differ, but the boundary is not uniform. A fund professional ordinarily invests capital entrusted by clients or limited partners under a mandate, not simply the employee's and partners' own capital. Measures of performance and relationship responsibilities vary by platform.

There is no generally easiest career stage for a move. Readiness depends on role fit, transferable skills, track record, mandate, hiring market and personal constraints; junior and senior transitions can both work.

The Mid-Career Inflection Point: The Fork in the Road

Somewhere between year seven and year twelve you will face a significant fork in the road. You are probably at a point where you could stay and keep moving up within the organization: you have built a track record, you produce good work, you are known in the industry. And you are probably wondering whether to stay or to try something different. The decision is often not made on purely rational grounds, and that is fine.

The available paths include staying on the sellside and moving toward senior roles (director, MD track); moving to the buyside as a portfolio manager or senior analyst; moving to advisory work at a restructuring firm or strategic advisory; or moving in-house to work for a company, a portfolio company or an operating platform. There are other options too (starting something yourself, moving into public markets, teaching), but those are the main ones.

Compensation varies widely by geography, firm, product, seniority, revenue attribution, fund performance and year. Evaluate a move using current, role-specific evidence with a defined population rather than a timeless dollar range.

Additional income generally has diminishing marginal utility, but the point at which that matters is personal and depends on taxes, dependants, debt, location, security and goals. Avoid assigning universal happiness thresholds or describing higher earnings as mainly ego.

Deferred compensation, vesting and lifestyle commitments can make a move costly. Model the after-tax cash flows, forfeitures, risk and non-financial effects without caricaturing people by age, mortgage, school costs or

income.

A useful framework for evaluating a move is to treat it as an investment decision. Consider the expected returns — not just financial ones, though those matter, but learning, autonomy, impact and enjoyment. Consider the risks: what is the downside if it doesn't work out, and can you afford that downside. And consider the optionality: whether the move opens up other opportunities or closes them down.

For a sell-side-to-buy-side move, compare scenarios for compensation, carry, learning, autonomy, fund risk and re-employment. Savings can reduce liquidity risk but do not establish that the move makes sense; significant personal financial decisions may warrant independent tax, legal or financial advice.

Building your network as a senior professional is different from the networking you did when you were junior. You are no longer trying to get in the door; you are expanding your sphere of influence and creating opportunities. You are probably going to conferences, writing, speaking at industry events, sitting on boards of industry organizations. All of that matters for building a network, but in different ways than you might expect.

The most valuable part of being a senior professional is being a resource for people. You have enough knowledge and enough connections to be useful: someone wants to make a transition and asks for advice; someone is thinking about starting a fund and wants to talk it through; someone has a deal they are trying to understand and wants a perspective. Being generous with that (actually spending time on people's problems and trying to be helpful) is how you build and maintain a network. It is not transactional and not about getting something back; it works because you have enough security and success to afford generosity.

Managing your career like an investment is a useful metaphor: you are building an asset that compounds. Early on you invest heavily in skills and reputation, maximizing long-term value rather than short-term returns. As you move up, you protect the asset and grow it. You think about risk, such as the concentration risk of only knowing one type of deal; about diversification, perhaps developing skills in several areas rather than one specialism; and about exit value — what your human capital is worth if you ever need to leave this particular position.

Some mid-career professionals gain more influence over workload; others take on broader client, investment or management demands. Assess and negotiate the actual role rather than assuming that career stage creates work-life balance.

The Senior Years: What It Means to Lead

By the time you have been in this industry twelve years or more, you have accumulated a certain amount of credibility and authority, whether you wanted it or not. You are probably deciding what the team works on, responsible for developing talent, and a name that matters in the industry. And you are probably wrestling with different questions from the ones you wrestled with earlier in your career.

Being a senior practitioner is partly technical — you know credit analysis in a deep way, you understand the market, you can identify risks other people miss. But it is also significantly about judgment, relationships, and the ability to think strategically about complex situations. A senior person is not just someone who is better at the technical work; they understand the context in which the work is happening and can make decisions that account for it.

Revenue generation and investment acumen are two different measures of success, and which one matters more depends on where you are. At a sellside firm, revenue generation matters enormously: the firm needs you to bring in clients, manage relationships and produce deals. On the buy-side, investment acumen matters more: the firm needs you to make good calls on what to invest in and what to avoid. Most senior people who succeed have both, but they usually lean into one or the other. There are incredibly smart investors who struggle with client

management, and great rainmakers who are less good at the actual investment decisions; the smartest firms arrange to have both and structure roles accordingly.

Managing teams and developing talent is probably the thing that matters most in a senior role, and it is also the thing people are least prepared for. The job is not just to make good investment decisions; it is to make them while making sure there are other people coming along who can do what you do. Otherwise you are merely delaying the day the firm has to work out how to replace you.

Develop people by combining coaching, practice, feedback and opportunities while recognising individual interests and support needs. Aptitude is not fixed, and managers should avoid writing off capability as something that cannot be developed.

The role of relationships at a senior level is probably more important than at any other point in a career. By then your value is partly your judgment, but it is also substantially the relationships you hold: clients who trust you and bring you deals; professionals across the industry who will take your call and do you a favor; people who work for you or have worked for you and whom you helped develop. These relationships are valuable in several ways: directly, because they mean deal flow and information; as a reflection of your reputation; and because they make the work enjoyable.

The industry looks quite different from the top than from the ground. When you are junior, you assume the people at the top have it all figured out — perfect confidence, perfect information. In reality, even at the senior level you are making decisions with incomplete information, uncertain, trying to work out what you don't know. What you have that junior people lack is experience with previous situations that were similar, better intuition for what questions to ask, and enough security that the uncertainty no longer cripples you.

Senior professionals should remain close enough to the mechanics to ask good questions and review critical outputs. Experience can accelerate sense-checking, but no one can know immediately that a model is sound; documented review and challenge remain necessary, and junior staff are professionals rather than merely production capacity.

The competitive dynamics among peers at a senior level can be surprisingly hard. You came up with these people, you know them well, in many cases you have worked together directly — and now you are competing with them for resources, recognition, deals and advancement. That can be more stressful than competing with people you don't know, because the relationships are real. Friendships do get damaged by competition at the senior level; some people manage to maintain them while competing effectively, because they keep a mature perspective on it.

The healthiest senior cultures accept that there is competition but also genuine collaboration. People compete while sharing information, referring deals to each other, and supporting each other's development of junior people. It is not zero-sum: you can hold high standards and high competitiveness while being collegial and generous, and the most respected people at senior levels are the ones who manage both at once.

Technical Skills That Never Stop Mattering

Throughout a career in leveraged finance, certain technical skills matter more than others, and they matter differently depending on where you are in the progression. A few never stop being relevant.

Credit analysis sits at the top of the list: the skill of looking at a business and understanding whether it can service its debt, what could go wrong, and what the downside scenarios look like. Junior analysts do it, senior professionals do it, partners at funds do it. The mechanics and the tools change, but the underlying skill of judging credit quality is evergreen — partly because credit investing is fundamentally about preserving capital, which never stops mattering.

What credit analysis means changes across a career, though. When you are junior it means reading financial statements accurately, understanding what leverage ratios mean, knowing what questions to ask. As you get more senior it becomes pattern recognition — this company is starting to show some of the same dynamics seen in another company ten years ago that ended badly. It widens into the broader context (what is happening in the supply chain, to the customer base, in labor markets) and into having opinions about what sustainable leverage is for a particular industry. The skills are cumulative, but they are not just more of the same; they are qualitatively different.

Financial modelling remains relevant, although the task changes with seniority and role. Senior practitioners may focus more on assumptions, sensitivities and review, but do not claim that experience compresses four hours of work into one without sacrificing control.

Documentation expertise is valuable because economic rights depend on the actual agreements. Investors should understand the commercial effect while qualified counsel advises on legal interpretation. Compensation effects are firm- and market-specific and should not be asserted without evidence.

Restructuring knowledge becomes especially useful in stressed markets. Professionals without prior downturn experience can prepare through training, simulations, documented precedents and experienced legal and financial advisers; lack of cycle experience does not mean they will be lost.

Market intuition is another skill that develops over time and is hard to teach: the ability to read flows, sentiment and technical dynamics in a way that informs your investment thesis. It means recognizing that even a credit you think is sound deserves caution when a dysfunctional market is pricing it away from fundamentals; noticing when a sector is getting too much attention and when it is being ignored; seeing when leverage is pricing in growth the company probably cannot achieve. Part instinct and part pattern recognition, it is built by paying attention to what is actually happening in the market over a long period, and by talking to other people who are paying attention.

Writing is the most undervalued skill in finance. The ability to write clearly and persuasively makes an enormous difference to a career, and people underestimate it. Your analysis is only useful if other people can understand it; your recommendations are only valuable if you can articulate why you are making them; your views on the market are only worth something if you can communicate them. Yet most people never invest in improving their writing, treating it as something you either have or you don't. You can absolutely improve it — by writing a lot, by reading how other smart people write, and by being willing to cut the weak parts and rework them.

Public speaking and presentation skills matter more at the senior level, but they matter throughout. Being able to walk into a room, communicate something clearly, answer questions and handle disagreement is a skill that compounds. Many people fear public speaking their whole careers and push themselves to do it anyway; it gets easier, and they get better than they were, even if they still feel nervous before presentations. Nerves are fine. What matters is that you prepare, know what you are going to say, and stay focused on communicating the information rather than on what people think of you.

Staying current is a discipline. Credit investing has changed substantially over the past two decades: the instruments have evolved, the risks have changed, the participants have changed, the amount of technology has changed. If you are not constantly reading, talking to people and updating your mental models, you go stale and you miss the shifts and the signals. The senior people who stay sharp are the ones who treat staying current as part of the job rather than something for their free time.

The Emotional and Psychological Dimension

Career advice in leveraged finance almost always ignores the emotional and psychological dimension, which is a major omission. The job does things to you: it teaches certain ways of thinking, exposes you to stress, shapes your identity. None of that is inherently bad, but it deserves acknowledging.

A recurring career experience is the sense that you have not yet earned your place, even after years of strong work. Treat that feeling as a prompt to seek specific feedback, compare evidence with self-perception and keep learning rather than as a verdict on your ability.

What to do with impostor syndrome is acknowledge it and move forward anyway. You are never going to feel completely certain, never going to be completely sure you are the best person for the decision. You make the best judgment you can with the information you have, and you accept that you might be wrong. That is what experienced decision-making actually is: not perfect confidence, but good judgment held with humility about your limitations.

Dealing with failure is something everyone has to do and nobody much discusses. Anyone in this business has been wrong about credit: recommended passing on companies that turned out to be great investments, invested in companies that didn't work out, lost money on deals, lost clients, had junior people leave because they weren't good at developing them. These things are genuinely painful when they happen, and particularly painful early in a career, when each one feels like it matters enormously.

Failure can provide information when it is analysed honestly. It does not follow that someone with fewer losses took too little risk, or that the people who take the most risk earn the best returns. Evaluate decisions against mandate, process, risk-adjusted outcomes and information available at the time.

Credit decisions and market dislocations can be stressful. Effects vary, and the text should not state sleep, relationship or health outcomes as inevitable; monitor fatigue and seek support when stress persists or impairs functioning.

Sustainable working habits are personal, but sleep, exercise, time away from screens and regular contact with people outside the immediate deal team can help preserve perspective. The point is not to prescribe a routine; it is to build one that lets you make sound decisions repeatedly.

High-pressure finance is easier to navigate when people can speak honestly about workload and ask for help without theatre. Team leaders should make priorities explicit, staff work realistically and respond constructively when someone says the load is no longer workable.

When you are struggling with the work, tell someone you trust early. Silence usually narrows the available options; a timely conversation can create practical choices about priorities, staffing and time away.

Experience through a dislocation can build perspective, but markets do not recover on a guaranteed timetable and firms or investments may fail. Resilience comes from preparation, support, controls and learning, not an assurance that the next cycle will resolve favourably.

The comparison trap bites particularly hard in leveraged finance because the industry is relatively small and everyone knows what everyone else is making and what opportunities people have gotten. It is easy to struggle with this at various points in a career: someone you know makes MD before you do; someone you came up with at a different firm raises a billion-dollar fund while you are still where you were; someone leaves for a prestigious platform. It feels as if you should have done it first, as if you are falling behind. This is not a productive way to think about a career, but it is a seductive one, because there is always someone doing something more impressive than you.

The antidote, applied with mixed success, is to remember that you don't actually know other people's situations. The person promoted early may be stuck in a role they hate; the person who raised a fund may be under enormous stress because the fund isn't performing; the person at the prestigious platform may net less because the salary didn't cover the higher-cost location. You see one or two dimensions of their situation, so the comparison is not very informative. More importantly, your career is your career; its success should be measured against your own goals and values, not against what other people are doing.

People find meaning in different aspects of work at different stages. Do not assume juniors care mainly about money or learning, or that senior professionals require impact to avoid hollow work.

The relationship between work and identity is something many people in this industry wrestle with. Over a career in leveraged finance, the work becomes a big part of who you are, and it is worth remembering that it is not your entire identity. You have other interests, other relationships, other dimensions to your life. If your identity is entirely wrapped up in the work, then when something happens to it (you get fired, you retire, you move into a different role) you lose your sense of self. The aim is an identity bigger than the job, even if nobody manages it perfectly all the time.

Relationships and Networking

It bears repeating: relationships are the single most valuable asset you can build in a career in leveraged finance — not relationships in the transactional sense, maintained to extract value, but real ones, where you actually care about the other person and there is mutual interest in each other's success.

The most valuable relationships in this industry tend to be with people scattered across firms and geographies. Early in a career you work closely with certain analysts and associates, go through difficult periods together, collaborate on deals, learn from each other. Some of those people end up at different firms; some move to the buy-side; some go into law; some go in-house. Years later, that is a network of intelligent people across the industry — valuable sometimes in direct ways (a client connection, a deal opportunity, an introduction to someone you need to meet) and sometimes just as people to talk to about the work and the challenges.

A useful networking principle is to engage with genuine interest, offer appropriate help, maintain boundaries and keep in touch without calculating an immediate return.

The mentor-mentee relationship is worth more attention, because a lot of people get it wrong. A good one is not the mentor telling the mentee what to do; it is the mentor asking good questions and helping the mentee think through situations, opening doors and making introductions, and being honest about what they see in the mentee — the strengths and the areas that need development.

Asking for help can be appropriate and need not signal weakness. Potential mentors may prefer a specific, bounded request, but coffee, monthly meetings and personal disclosure are not requirements; respect time, accessibility and professional boundaries.

Being a mentor is also an important part of a senior career. A lot of senior people don't realize how valuable they could be if they invested in developing other people. A specific piece of advice, seemingly insignificant at the time, can change someone's trajectory, and that is genuinely rewarding. It is also good for the industry: if everyone who reaches a senior level brings other people along, the talent pipeline improves; if people just extract value and don't give back, it weakens.

Cross-functional relationships build over time and are valuable in ways that are sometimes overlooked. You work closely with lawyers on documentation, with operations people on portfolio management, with compliance people on regulatory issues. These are probably not people you think of as part of your "network," but they are essential. The lawyers who understand your business model and have worked deals with you end up knowing a lot about what you do and how you think; when you need something complex done, you call them because they understand the context. The operations people who have dealt with your portfolio and helped you through difficult periods become strategic partners. These relationships matter.

Industry conferences and events can be useful, but select them for substance, audience, cost and relevance. Prioritise a small number of meaningful conversations and learning opportunities over maximising the number of introductions.

Professional platforms can help maintain contact and share approved work, but usefulness depends on audience and policy. External posts should be accurate, sourced, accessible and cleared where required; avoid claiming that authenticity alone drives engagement.

Long-standing relationships can create opportunities and support, but their value is not guaranteed or reducible to a fixed timeline. Maintain relationships without an expectation of return.

Money and Compensation

It's worth being straightforward about compensation, because a lot of career advice in this space dances around it.

Compensation can be attractive, but it varies widely by geography, role, firm, seniority, performance and year. Use a current, attributable survey with a disclosed methodology and population when comparing ranges.

Buy-side compensation is especially dispersed because salary, bonus, deferred awards and carry depend on mandate, fund terms, vesting and performance. Compare offers only after defining the instrument, time horizon and downside.

These are genuinely large numbers, particularly relative to most other industries, and they are one of the reasons people are attracted to the field.

It is important to understand how compensation is used as a retention tool in this industry. You get a decent salary, but the real compensation comes through bonuses paid at the firm's discretion and through equity or carry that vests over time. That ties you to the firm, because leaving means giving up unvested compensation. It is not necessarily nefarious (the firm has invested in your development and wants to retain people), but it is definitely a feature of the business model.

Prepare for compensation discussions with current, lawful market evidence and a record of responsibilities and results. Consider salary, bonus, deferred compensation, carry, benefits, tax, vesting and forfeiture terms. Review contractual changes and obtain advice where appropriate.

Negotiate from an honest account of your contribution and alternatives. Do not bluff about leaving or use confidential competing offers improperly; understand the relationship and contractual consequences of any ultimatum.

Cash, equity and carry have different liquidity, concentration, vesting, tax and valuation features at every career stage. Evaluate the actual instrument and downside instead of relying on a generic seniority rule.

When money should drive decisions and when it shouldn't is worth thinking about carefully. It should drive them when you are working toward a particular financial goal: buying a home, paying off debt, achieving financial security. It should not when the point is accumulation for its own sake, or when the choice is going to make you significantly unhappy.

People do make decisions entirely on compensation (staying at a firm they are unhappy at because the pay is high, moving to another role primarily because it pays more), and sometimes those decisions work out and sometimes they don't. When they fail, it is usually because the person discovers that money alone does not make the job tolerable. They are still unhappy; they are just unhappy and making more money.

The marginal utility of income often declines, but its practical effect varies with personal circumstances and goals. Avoid claiming that an additional million dollars cannot change a life meaningfully.

The Industry's Evolution and Your Career

Leveraged finance has changed substantially over the past two decades, and those changes matter for how you think about your career.

Leveraged finance has broadened across banks, institutional credit, private-credit platforms and other providers. The scale and direction of change should be supported by a dated source if quantified; avoid implying that earlier markets consisted of only a handful of firms.

Direct lending has become an important financing channel and career path, although its scale and relative importance vary by segment and period. Readers should use current market data rather than treating it as the single biggest structural shift by assertion.

Technology continues to change data collection, modelling, workflow and monitoring, while spreadsheets remain widely used. Professionals should understand tool capabilities, limitations, data lineage, validation, security and governance rather than assuming newer analytics are inherently better.

Environmental, social and governance requirements vary by investor mandate, jurisdiction, product and time. Treat material environmental and social risks within the credit analysis and comply with applicable disclosure and anti-greenwashing rules; do not label the subject a trend or passing fad without current evidence.

Financial regulation changed materially after 2008, but the effect on private credit is jurisdiction- and entity-specific. Refer readers to current legal and compliance advice instead of asserting that regulation is steadily increasing everywhere.

Cross-border capital is important, but deals remain shaped by local law, currency, tax, insolvency, regulation and investor mandates. Capital does not flow freely in a literal sense, and neither domestic history nor the decline of geographic arbitrage should be stated without evidence.

What the next twenty years look like is genuinely uncertain, which is probably healthy. Artificial intelligence is likely to affect this industry in ways that cannot be fully predicted; changes in the regulatory environment could materially shift the business model; market structure shifts could create opportunities or challenges. The best guess is that the fundamentals of credit investing do not change: you are still analyzing companies, still trying to understand whether they can service their debt, still taking risks for potential returns. But the context in which you do that work will keep evolving.

Positioning yourself for an evolving market means staying flexible and staying current. If you build skills in one area and the industry shifts, you want to be able to adapt. This is why broad exposure early in a career matters: different types of deals, different geographies, different industries. You are not locked into one particular approach, and as the industry changes you can move your skills to what matters in the new environment.

Diversity and Inclusion

It's worth being honest about diversity in leveraged finance, because most people aren't willing to be.

Representation in senior finance roles differs by country, institution and dataset. Avoid turning the composition of one room or one personal experience into an industry-wide conclusion.

For a practitioner, the useful questions are concrete: who receives access to assignments, how performance is evaluated, whether sponsorship is available and whether outcomes are reviewed with evidence.

Diverse perspectives can improve challenge and reduce shared blind spots when teams are inclusive and evidence is heard. That is a sound governance objective, but it is not proof that every diverse team makes better investment decisions; define and measure the relevant outcome.

For a team leader, practical habits include using clear selection criteria, widening access to assignments and sponsorship, checking outcomes and making it safe to raise concerns.

People whose background aligns with established norms may encounter fewer barriers. Discuss access and outcomes through evidence and individual experience without treating any person as representative of an entire category or assuming an absence of discrimination.

Senior professionals can widen opportunity by making decisions against clear criteria, mentoring and sponsoring consistently, challenging observed bias and reviewing the outcomes of their own staffing choices.

What Experience Actually Teaches

Over the course of a career, only some of the lessons actually stick, and only some of the wisdom transfers.

Patience can be valuable, but long-term success has no single pace. Balance depth and deliberate development with timely action when a role is not providing learning, fair treatment or opportunity.

Intellectual humility supports sound investing because it encourages testing, updating and acknowledgement of uncertainty. It is one contributor to long-term performance, not a proven biggest predictor.

Knowing when you have found the right role is something you get better at over time. Early in a career you might take any role because you are grateful to have it. Over time you get pickier: you learn what kind of work energizes you, what kind of team environment you need, what kind of compensation structure matters to you. When a role aligns on all of those, it feels different — you don't mind working hard because you are working on things you care about, the time disappears, you are engaged.

The difference between success and fulfillment is real, and they are not always the same thing. There are very successful people who are not fulfilled: they made MD, they are making a lot of money, and they are not happy. There are people moderately successful by industry standards who are deeply fulfilled, because they are doing work that matters to them, with people they like, in an environment that treats them well. Success is usually visible to the outside world; fulfillment is usually visible only to you. The question worth asking yourself is which one actually matters to you.

Advice to someone early in the career: you are not necessarily behind; help others where appropriate; keep the work in perspective; build transferable skills; and invest in relationships as well as compensation. Leveraged-finance decisions matter to investors, borrowers, employees and communities, so perspective should not become dismissal of their consequences.

Sharing knowledge through teaching, writing and mentoring can sharpen thinking and support others. People may also limit sharing for confidentiality, intellectual-property, workload or regulatory reasons; do not attribute restraint to insecurity.

This chapter addresses the human experience that technical career advice often omits. Its guidance is general: individual career paths, market cycles and workplace experiences vary, and confidential transaction or employment information should not be inferred from the examples.

The truth of a career in leveraged finance is that it can be genuinely rewarding and genuinely difficult, and it is rarely boring. The money is real and meaningful; so is the intellectual challenge; so, at times, are the stress and the hours. Navigating it well means making choices aligned with your values, investing in relationships, staying curious and humble, and remembering that this is a means to a life rather than the entirety of a life. Done that way, it can be a career you look back on with real satisfaction.

This field can offer challenging work, learning and relationships, and it can also impose costs in time, stress and uncertainty. Financial security, global networks and fulfilling work are possible outcomes, not promises.

The challenge is holding all of that as true simultaneously. The job is genuinely valuable, and sometimes it is a trap. You are probably capable of more than you think, and you are probably also doing things that don't need to be done as intensely as the industry does them. The best career in leveraged finance is one where you are aware of all of that, where you make conscious choices about what you are optimizing for, and where you are willing to change course if what you thought you wanted turns out to be different from what actually makes you happy.

That is what a career in this industry ultimately teaches: to pay attention to your own experience, to be willing to adapt, and to understand that a successful career is ultimately the one that feels successful to you, not the one that looks successful to everyone else.

Building Your Personal Brand in Leveraged Finance

Professional reputation long predates social media. In leveraged finance it has traditionally been built through technical quality, conduct, reliability and relationships; digital channels now make parts of that reputation more visible and portable. Long or unsafe hours are not a credibility credential.

The fundamentals remain important, but digital publication, professional networks and virtual events have added new routes to visibility. Their value depends on role, employer and regulatory context.

This chapter addresses professional reputation rather than follower counts. Credibility can affect opportunities, relationships and influence, but it does not by itself guarantee job security, deal flow, negotiating power or advancement.

A durable professional reputation starts with competent, ethical work and responsible communication. Public visibility should accurately reflect the work and remain within employer, client, confidentiality and regulatory boundaries.

Over recent decades, professional platforms and lower-cost publication tools have expanded the ways expertise can become visible. Speaking and publishing existed long before social media, so the change is one of access and distribution rather than the creation of entirely new routes.

The sections that follow work through the main vectors in turn: LinkedIn strategy, thought leadership, conference participation, the writing discipline, the networking approach, mentorship responsibilities, and career positioning across the transitions that make up a leveraged finance career. The aim is a framework concrete enough to act on — a brand that generates opportunities, amplifies your work and supports the career you actually want, rather than one that merely looks impressive on paper.

LinkedIn Strategy for LevFin Professionals: Building an Audience That Matters

LinkedIn can support professional visibility, but its value varies by audience, employer policy and role. Use it deliberately rather than treating it as either essential or a waste of time.

Hypothetical example: a senior banker posts periodic commentary on publicly available European LBO developments. The commentary identifies its sources, distinguishes fact from opinion and avoids confidential deal details or investment recommendations.

Useful public work may lead to professional conversations, but connection growth, mandates and career moves cannot be promised or attributed to posting without evidence. Focus on the quality, accuracy and relevance of the work rather than a fixed timeline.

Post only material that is accurate, useful and authorised for public release. Add value through original analysis of public or properly licensed information—not through information that is confidential, material non-public, inside, client-owned or outside an approved communications process. Precision should match the evidence; not every market observation is accurate to a decimal point.

Choose a cadence that you can sustain without sacrificing quality or compliance. There is no evidence-based rule that posting more than every ten days looks desperate or that a slower cadence loses momentum.

Possible subjects include public market structure, transaction mechanics, historical case studies, career development and analysis of published market news. Use current examples, cite sources and avoid implying that

observations from live deals are publishable.

Promotional content may be appropriate when it is accurate, transparent, approved and useful to the intended audience. Separate education from solicitation and follow employer, advertising, financial-promotion and recordkeeping rules.

A relevant audience is more useful than a large undifferentiated one, and engagement metrics are not proof of professional credibility. Evaluate whether the work reaches appropriate readers and supports useful, compliant discussion.

Three things matter in building a LinkedIn audience that is worth anything to a career. First, consistency beats virality: the aim is not a viral post but showing up as a reliable, thoughtful source of perspective month after month, which compounds. Second, usefulness beats cleverness: write for someone genuinely busy — your Managing Director, or a sponsor you want to work for — and ask whether that person would find the piece valuable or interesting; if not, do not post it. Third, engagement runs both ways: respond thoughtfully when people comment, and engage with what others post that interests you. You are building a community, not broadcasting into a void.

Potential formats include sourced analysis of public credit events, covenant packages, underwriting conditions and career topics. Never use confidential transaction documents or client information without documented authority, and ensure legal interpretation is reviewed where necessary.

Synthetic teaching scenario: a professional publishes an article explaining the current Sustainability-Linked Loan Principles using the official text and clearly separating analysis from law. Success is measured by accuracy and the quality of discussion, not by assumed comments, shares, client conversations or mandates.

Avoid manipulative engagement tactics, unsupported claims and commentary outside your competence. Political, religious or personal content is not categorically prohibited, but it should be assessed against law, employer policy, audience, conflicts and the professional context.

An audience is a possible consequence of useful work, not proof of expertise. Value should be assessed by the quality of interaction and professional outcomes, not unsupported comparisons between connection counts.

Thought Leadership: Writing Articles and Developing Perspectives on Market Developments

Thought leadership has become a slightly cringe-inducing term, mainly because it is overused, often applied to people who have not actually thought very deeply about anything, and frequently deployed as cover for what is really just marketing. The honest version of the term is worth reclaiming: developing a genuine perspective on important developments in the market you inhabit, and sharing it in a way that helps others understand those developments better.

Few people set out with the goal of "becoming a thought leader." What actually happens is that you work on a lot of deals, pay close attention to what is working and what is not, read voraciously, follow market developments, think about implications, and over time develop perspectives on the industry that seem worth sharing. The vehicle for sharing them often starts with articles.

External articles often begin with analysis of public trends or properly authorised research. Never derive publication content from live deal work merely by making it 'general enough'; obtain employer and client approval, protect confidential and privileged information, and comply with market-abuse and communications rules.

Writing can sharpen thinking and create a public record, but publication does not make a view authoritative in a negotiation. The quality of evidence and the governing documents remain controlling.

Hypothetical example: a sourced article could compare leverage definitions in published agreements, identify the economic consequences and explain the limits of the sample. It should not be described as arising from a

confidential negotiation.

Useful writing may lead to enquiries, but outcomes vary and should not be converted into a promised return on time. Any client or mandate example must respect confidentiality, conflicts and attribution requirements.

The path to meaningful thought leadership in leveraged finance does not require being the world's most famous expert. It requires being an expert in something specific that other people care about, and the more niche the expertise, the more valuable it often is. There is no need to position yourself as a generalist voice on the entire leveraged finance market. Far better to be known for deep expertise in something specific — Nordic LBO structures, European covenant frameworks, debt capital markets dynamics in mid-market and lower mid-market deals, the intersection of sponsor strategy and debt structuring. Those are the areas where extensive work gives you real perspective and genuine authority.

Write within demonstrated competence, but do not rely on transaction count alone. Use public or licensed evidence, disclose the limits of the sample, avoid legal conclusions outside your role and obtain required review before publication.

A safe content framework has four gates: identify a topic you understand; determine what has changed using current public sources; test whether the analysis adds a useful, supportable perspective; and confirm that every example is public, licensed or expressly approved for disclosure. If any confidential, inside or client-owned information is needed, do not publish it.

The writing itself requires discipline. Research the subject, draft a complete argument, edit for evidence and clarity and obtain informed feedback before submitting or sharing the work. The time and number of revisions should match the topic, risk and publication process rather than a fixed formula.

Potential topics should be current and sourceable: covenant-framework changes, debt management in different markets, continuation-fund financing, subscription facilities, asset-based lending, regulatory change and liability-management structures. Historical examples such as negative interest rates should be labelled by period, and legal claims should be reviewed.

Published work forms part of a public record and may affect professional reputation. Quality, accuracy and compliance matter more than a target article count.

Consistent, useful work may lead journalists or organisers to seek comment. Any media engagement should follow employer approval, confidentiality, market-conduct and recordkeeping requirements.

Conference Speaking: How to Get Invited, How to Prepare, the Circuit That Matters

A first conference invitation may be intimidating, particularly when other panelists are more senior. Whether to accept depends on topic competence, employer approval, preparation time and the event's audience—not on a fabricated date, city or job title.

Declining is not necessarily a mistake. Accept only when you can contribute responsibly and comply with employer and client obligations; a panel appearance does not by itself alter a career trajectory.

A good panel can begin useful conversations, but no attendance or commercial outcome should be assumed. Discuss event outcomes only when they are accurate and authorised for disclosure.

Speaking can be one professional-development channel. Frequency should match the role, expertise, workload and employer expectations; no annual target applies universally.

The first rule of speaking as a brand-building tool is that the right conferences matter and the wrong ones waste time. If you are building a brand in leveraged finance, speak where your relevant audience will actually be: major

European or global LBO conferences, regional sponsor dinners, law firm seminars on deal structures, banking conferences, debt capital markets forums, industry association events. Not every local business breakfast or regional networking event. Be selective.

Seek speaking roles transparently: propose useful topics, demonstrate relevant expertise and follow organiser and employer processes. Do not condition help assembling a panel on receiving a slot where that would create a conflict or undisclosed quid pro quo.

Panels can benefit from informed disagreement, but prior relationships are not required. Preparation, balanced moderation, evidence and a range of perspectives matter more than whether panelists already know one another.

Too many conference panels make it obvious that the five people on stage had never met before the conference, prepared individually, and are taking turns delivering pre-written remarks while the moderator nods. Those are dull and unhelpful. The panels people actually remember are the ones with genuine interaction, where a comment prompts a real response and you can sense people thinking on their feet rather than reading slides.

An effective preparation process: when the invitation arrives, typically a couple of months before the event, contact the co-panelists immediately and suggest a call. The aim of that call is to learn their perspective on the topic, their firm's perspective, the issues they are thinking about right now, and the one thing each wants to make sure gets discussed. Take notes, form your own view of what matters, and arrive at the panel understanding the actual positions in the room.

For the panel itself, prepare perhaps three or four points you want to make — the substance of each, not a script. Then be ready to make them without reciting them: if the conversation moves in a different direction you can adapt, if a question draws out a point early you can acknowledge it and move to something else, and if a co-panelist says something you disagree with you can engage with it honestly. The conversation is much better for it.

Choose events based on audience, substance, cost, conflicts and relevance. Speaking may support visibility and relationships, but it does not guarantee deal flow.

International invitations may follow sustained, relevant work, but no age or fixed period in a regional niche is a prerequisite. Opportunity depends on expertise, audience, language, access and professional context.

Public speaking can differentiate some professionals, but talent and willingness are not opposites. Treat anxiety respectfully, prepare carefully and seek support; do not disparage visible speakers as less talented.

Writing as a Career Accelerator: From Internal Memos to Published Articles to Books

One of the things that can accelerate a career beyond what deal flow alone would make possible is a consistent discipline around writing, and it often starts in a surprisingly unglamorous place: internal memos.

Synthetic teaching scenario: a junior professional receives feedback that clear writing matters because leveraged finance produces credit papers, term sheets, presentations and client communications. Writing is one important capability among technical judgment, conduct and execution.

Internal work should meet the standard appropriate to its purpose, controls and audience. 'Publishable' is not always the right test because internal materials may contain confidential, privileged or preliminary information that must never be published.

Repeated practice and feedback can improve writing under pressure, synthesis and anticipation of reader questions. Do not claim that exactly one hundred memos produces those capabilities or disparage people who develop them differently.

External writing must not be derivative of internal or client work unless the relevant intellectual-property, confidentiality, privilege, MNPI and employer-approval issues have been resolved in writing. Anonymising a deal is not necessarily sufficient.

There is no mandatory career-stage progression from internal to external writing. Publish only when the work is accurate, useful, authorised and within your competence; a successful late career does not require a public cadence.

A book is not something to write lightly, and it demands serious thought about what is actually worth a full book. Published articles, contributed chapters and extensive writing are one thing; a complete book is a different commitment. You are undertaking to organize everything you think you know about a topic and present it in a way that is compelling, useful and rigorous for a reader who may spend fifty hours with your words.

Internal memos should be as long as their purpose and governance require. Accuracy, traceability, clarity and decision usefulness matter more than a ten-to-twenty-page norm, and confidential internal work is not a rehearsal for publication.

External articles must earn attention through useful, supportable analysis, but length varies by outlet and topic. Avoid a fifteen-hundred-to-five-thousand-word rule and never equate novelty with using information that others do not know.

A book is a sustained project whose length, research and editing needs vary widely. Do not promise that sixty to one hundred thousand words can be researched, drafted and quality-controlled in roughly two hundred hours; plan based on scope, sourcing, legal review and editorial standards.

A book may support learning, reputation and professional relationships, but it may also generate little income or opportunity. Any commercial, consulting or mandate benefit is contingent and must not be promised.

Professional credibility should stand on the quality and traceability of the work. Career duration, transaction counts and mentoring claims add little unless they are accurate, relevant and appropriate to disclose.

Writing can support learning at any career stage. Choose internal, external or long-form work based on purpose, competence, audience and approvals rather than an early-, mid- and late-career formula.

Networking with Private Equity Sponsors: Building Relationships That Generate Deal Flow

Sponsor relationships are important for origination and advisory roles, but they are not optional in the same way for every leveraged-finance career. Technical, portfolio, risk, legal and operational roles may create value through different constituencies and responsibilities.

Sponsor relationships rest on a foundation that looks simple and is actually quite demanding: the sponsor has to trust that when they work with you, you will be thoughtful, careful, reliable, honest, and genuinely invested in solving their problems rather than running up fees. That trust is built over time, through repeated interactions and the shared experience of working through complex transactions.

Synthetic teaching scenario: during a stressed market, an advisory team explains execution risks clearly, delivers the agreed work and gives candid advice within its mandate. The transaction may support future trust, but no long-term relationship or repeat mandate is assumed.

The time required to build a professional relationship varies. Describe the work actually authorised and performed, and do not give informal legal advice in place of retained counsel.

A successful transaction can lead to repeat work, but mandate outcomes also depend on price, capability, conflicts, competition and client choice. No single relationship should be presented as the guaranteed base of a

business.

What builds sponsor relationships that actually generate deal flow? First, be genuinely useful before asking for anything in return. Early in a career that might mean doing analysis the sponsor needs, helping them think through structures, being available when they have questions; later it might mean acting as a sounding board on strategy, helping them read different market conditions, or putting your network to work on their problems. The principle is constant: your value to them should never rest primarily on your ability to earn fees, but on your ability to help them do their job better.

Maintain important relationships at a cadence that fits the client's needs, firm policy and legitimate business purpose. Quarterly contact is an example, not a universal rule, and hospitality must follow conflicts, gifts and entertainment policies.

Third, be willing to play a supporting role as often as a leading one. Some of the most valuable sponsor relationships are ones where you are not the primary arranger but an important advisor on a specific aspect of the transaction, or not on the deal at all but available to think through problems as they arise. Being the person they call for perspective or advice can be as valuable as being the main financial advisor, and sometimes more so.

Professional relationships may include appropriate social interaction, but dinners, drinks, sport and golf are not requirements. Apply gifts, entertainment, anti-bribery, expenses, conflicts and equal-access policies, and respect personal, religious, health and caregiving boundaries.

Composite illustration: a sponsor considering another acquisition may benefit from separating strategic milestones from the amount of debt available. Any advice should be based on the actual portfolio, integration risk and downside—not a rule that a third platform can carry more leverage.

A useful conversation can strengthen a relationship, but one comment should not be credited with changing strategy or producing later mandates without clear evidence.

Track relationships only in approved systems and for legitimate business purposes. Apply data minimisation, access controls, retention rules and applicable privacy law; do not maintain informal personal dossiers on executives.

Early-career professionals can support sponsor work through authorised assignments, supervised meetings and approved industry activity. Do not volunteer services, contact clients independently or imply advisory authority outside your role.

Sponsor relationships are a large part of what sustains a career at a senior level. A move into advisory becomes possible because sponsors know who you are and trust you enough to work with you in a different capacity. Invitations to speak at sponsor conferences and events come out of relationships built over years. Opportunities to shape market developments or industry practice often arrive through sponsors who want to collaborate on something.

Building Relationships with Lawyers and Advisors: The Trusted Advisor Ecosystem

If sponsor relationships are the customer relationships of leveraged finance, relationships with lawyers and advisors are something different and equally important: peer relationships within the system that makes deals happen. A surprising amount of a career's trajectory is shaped by the quality of the relationships built with genuinely good lawyers and advisors.

Strong relationships with qualified lawyers and advisers can improve execution and learning. Their value depends on competence, independence, conflicts and the engagement; no single peer relationship is universally more valuable than all others.

Synthetic teaching scenario: repeated authorised work with capable counsel builds mutual respect even when clients' positions differ. The relationship remains subject to engagement scope, conflicts, privilege and confidentiality and does not imply a fixed number of matters or referrals.

Informal professional exchanges do not replace retained legal advice. Questions should be handled under appropriate engagement, privilege, conflicts and confidentiality arrangements, and career-transition referrals should not be assumed.

The lesson is to invest deliberately in relationships with highly competent professionals from other disciplines. The best investment bankers keep excellent relationships with a small number of really good lawyers, with quality financial advisors, sometimes with senior bankers at competing firms whom they respect, and with accounting firms, academic experts and regulatory advisors. These are not transactional relationships; they rest on genuine respect and repeated positive interactions over years.

Preparation, reasoned positions and professional conduct help build respect across disciplines. Present any account of a lawyer's feedback as a confirmed quotation or a clearly labelled composite, and do not disparage junior bankers as a group.

Second, professional courtesy and respect — obvious, perhaps, but not always practiced. Meet deadlines, and be honest when you cannot. Respect their time. Engage properly with their feedback, and acknowledge a good point even when it is inconvenient for your side. Remember that they have other clients and other priorities, and that you are not the only matter on their desk. Professional courtesy compounds.

Ask advisers for perspective within the scope of the relationship and respect when a question requires a formal engagement, conflicts check or fee. Do not disguise substantive professional advice as an informal favour.

Introductions and referrals must serve a legitimate purpose and comply with conflicts, anti-bribery, procurement, independence and disclosure rules. Do not imply an exchange of favours or an expected return.

A strong adviser network can provide challenge, feedback and introductions, but information and referrals must remain within engagement, conflict, confidentiality, privilege and consent boundaries. It is not a personal asset free of those constraints.

Lawyers, accountants and other advisers may make introductions where professional rules, conflicts and client consent permit. Referrals are one possible source of work, not a guaranteed determinant of career trajectory.

The Path from Analyst to MD: What Differentiates People at Each Level

Promotion timelines and titles vary by firm. Four years as an analyst is neither inherently long nor equivalent to six years of full-time effort; chronic excess hours should not be converted into a badge of competence.

The analyst-to-associate transition often adds judgment, ownership and coaching responsibility. Junior staff should solve issues within authority and escalate material uncertainty, errors, conflicts or control concerns promptly.

The transition from associate to manager is bigger. You are now responsible for relationships; for understanding what clients want, not just what they ask for; for the quality of the work done by the team under you; and for business development — it is no longer enough to deliver what is asked, you need to identify new opportunities and bring them to the firm. You are expected to hold a view on market developments and to be starting to specialize, with areas where your expertise is distinctive. The associates who make this step are typically the ones who have shown they can manage relationships, manage teams and develop business.

At some firms, external relationships and judgment become more important at senior levels; at others, titles and responsibilities differ. Avoid presenting 'senior manager' as a universal stage or claiming sponsors will ask for

someone by name.

Director or MD selection varies by institution and may consider leadership, risk management, conduct, commercial contribution, investment results, client service and technical judgment. Network and public visibility are not universal primary criteria.

Technical competence remains important, but the required depth varies by role. Senior leaders also need judgment, controls, conduct, team development and stakeholder management; 'thought leadership' is not a universal promotion requirement.

Career transitions do not occur on a fixed seven-year schedule. Advancement should be described through demonstrated responsibilities and outcomes, not a chronology of sponsor relationships, publications and conferences that may not apply to the author or firm.

At a director-equivalent level, responsibilities may include strategic client or investment decisions, risk ownership and team leadership. Titles and the route to those responsibilities vary by institution.

A move into advisory can occur at many stages and changes the mix of client, commercial and technical responsibilities. Evaluate the actual role rather than comparing it with a single conventional promotion path.

Competency needs change with role and institution. Continue technical development while adding leadership, risk, commercial or investment responsibilities as required; avoid a rigid early-, mid- and late-career formula.

Maintain the capabilities required for the role and build complementary strengths. Neither directors nor managers necessarily plateau because they lack external visibility, thought leadership or sponsor relationships; promotion criteria are institution-specific.

Mentorship: Finding Mentors, Being a Mentor, the Distinction Between Sponsor and Mentor

A first real mentor in leveraged finance is often a group head of the kind described earlier — someone who invests deliberately in development. Such a mentor does not just assign work and expect you to figure it out. They spend time teaching you how to think about deals, give feedback on your writing and your analysis, challenge you when you are wrong, put opportunities in front of you, and hold you to the standard of what they believe you can become.

There are usually other informal mentors over the years — people from whom much is learned through observation and relationship, but who are not deliberately investing in your development in the same way. Sponsors take an interest in a career; peers become the people with whom the really important conversations happen. But a true mentor, someone deliberately investing in your development, holding you accountable and opening doors, is rarer than the other kinds of relationship.

Senior professionals may mentor several people, but capacity, quality and fair access matter more than a target number.

Some lessons about mentorship in leveraged finance. First, good mentorship is not about solving problems for the person being mentored; it is about helping them develop the judgment to solve problems themselves. When a junior banker brings a covenant structure question, the better response is not simply the answer. Ask what they think, why they think it, what the implications of their approach would be, what the sponsor would likely care about, and help them work toward the right answer. That is how judgment gets built.

Second, good mentorship is candid. If someone you mentor is making a career decision that looks like a mistake, say so. If they are not developing the skills their level requires, say so. If they appear to be avoiding something they should be doing, say so — directly, not harshly. Sugar-coating feedback does not actually help anyone. What helps is telling someone what you actually think, then helping them work out what to do with that feedback.

Third, mentorship is about opening doors. As you become more senior and more visible, one of the things you can do for the people you mentor is provide visibility: suggest them for speaking opportunities, introduce them to sponsors, recommend them for advisory relationships, get them into rooms they would not otherwise reach. That access is genuinely valuable.

Mentorship requires time and boundaries. It should not displace required supervision, create unmanaged conflicts or be reduced to a universal annual-hour estimate.

Mentorship supports learning and reflection. Sponsorship is different: a senior person actively advocates for access, visibility or advancement and takes reputational responsibility for that advocacy. Neither relationship is financial capital in a literal sense.

Sponsorship often grows from trusted work and judgment, but professionals can appropriately ask what advancement requires, seek advocates and request consideration for opportunities. Advocacy should be fair, evidence-based and consistent with firm processes.

At different points in a career you need different things from your relationships with more senior people. Early on you need mentors, people deliberately investing in your development. By mid-career you still want mentors, but you also want sponsors — people willing to advocate for you and put their credibility on the line on your behalf. By late career you want both, and you have probably become both for other people.

A mentoring relationship can begin through a direct, bounded request, a formal programme or repeated work. No one should have to prove they are 'worth mentoring'; access should be fair, expectations explicit and boundaries respected.

Mentorship received is worth being grateful for. It can genuinely shape development in ways that free agency would not have, and it is worth paying forward with the people you mentor in turn.

Internal versus External Brand: Managing Both Simultaneously

One of the awkward features of building a personal brand in leveraged finance is that you are really building and managing two brands at once: an internal brand, your reputation within your firm, and an external brand, your reputation in the market more broadly. They are not the same thing.

Early-career professionals usually need to prioritise their core responsibilities and internal trust, but appropriate external activity can also support learning. Follow employer approval and do not assume the same sequence fits every role.

External visibility can create benefits and conflicts at any institution. Review employment terms, intellectual property, client confidentiality, regulatory status and communications policy before publishing or speaking.

Some firms actively benefit from individual bankers having external visibility: speaking at conferences supports the firm's brand, publishing articles positions the firm as a thought leader, and relationships with sponsors ultimately become firm business. In that kind of environment it is possible to build an external brand without undermining the internal one.

A 'views are my own' disclaimer does not override employer policy, regulatory supervision, recordkeeping, confidentiality, intellectual property or market-abuse law. Obtain required pre-clearance, use approved channels and never publish confidential or inside information.

If an employer restricts external activity, first understand the legal, regulatory and business reasons and discuss approved alternatives. Whether to change roles is a separate career decision, not the automatic consequence of a visibility policy.

On a move to advisory the balance shifts: the external brand matters more than the internal one to the new firm, because part of what is being hired is the external relationships and reputation. It still pays to be a good colleague, to contribute to the firm's reputation and to maintain the internal relationships.

The best position is the one where the internal and external brands are aligned and mutually reinforcing: known inside the firm as excellent at the craft, known outside the firm as excellent at the craft, recognized both through the firm and on your own name. That is the position to aim for.

External visibility cannot replace competent, ethical work. Internal disagreement does not automatically expose or end an external reputation, however; assess the evidence and address performance through fair processes.

Technical Credibility: Knowing Your Craft Deeply

Something underrated in most discussions of personal branding in finance deserves space here: actual technical competence. It is unglamorous and generates no LinkedIn engagement, but it is the foundation on which the rest stands.

Among bankers, the ones with the most durable careers — not necessarily the fastest promoted, but the ones who sustain a trajectory without plateauing — are the ones with genuine technical depth. They understand the mathematics deeply and know the documentation intimately. They understand not just what the rules are but why they exist and what problems they are trying to solve. They can think through edge cases and implications, and they spot problems that are not obvious.

Technical credibility requires accurate leverage calculations, covenant analysis, liquidity assessment, debt-paydown mechanics and priority analysis. Mental arithmetic can be a useful reasonableness check, but it never replaces a sourced model, document review or independent validation.

This cannot be faked. Sponsors, lawyers and other bankers all know when you understand the mathematics and when you do not. Without genuine technical depth you can be charming, articulate and visible, and you will still eventually be exposed as not really knowing what you are talking about.

There are bankers who are more charismatic, more extroverted, better networkers — and who plateau nonetheless because they lack genuine technical depth. Clients eventually discover that, good as such a banker is at the relationship side, they are not actually the best source of technical advice, and that limits what they can do.

Conversely, there are bankers who are not particularly charismatic and not strong on external visibility, but who are extraordinarily technically sound. They sustain careers because they can always fall back on the fact that they know the subject matter deeply.

Build technical depth through study, supervised practice, document review and feedback. The CFA programme may be relevant for some roles, but check current requirements and role fit; it is not a general leveraged-finance prescription.

By mid-career the technical competence should be very solid. You should understand not just your own area but the adjacent ones, be reading widely, be tracking how markets are evolving, and be thinking about what is changing and what is staying the same.

By late career the technical knowledge should be deep enough for sophisticated conversations on very specific issues, and broad enough to take in the interconnections. You may specialize in certain kinds of transactions or certain kinds of markets, but you should understand the broader context around them.

What keeps technical depth alive over a long career is never getting comfortable. Assume there is something you do not know. When a new instrument emerges or a market develops in a new way, study it; when you encounter a deal structure you have not seen before, work it through properly. Read every day — analyst reports, ratings

agency comments, loan market developments, sponsor perspectives, academic research. That constant intake keeps you current and keeps the technical foundation strong.

Technical credibility is also the best protection against the uncertainty of a career in finance. Markets change, industries evolve, firms restructure, deal flow ebbs and flows. The one thing you control is the depth of your own technical competence, and that competence is portable: it moves with you between firms, between roles and between geographies. That is worth a great deal.

Social Media Presence Beyond LinkedIn: Twitter/X and Market Commentary

X, formerly Twitter, can support real-time professional discussion, but it can also create distraction, conduct and information risks. Its usefulness depends on audience, employer policy and how it is used.

Financial professionals use X and other platforms for public market commentary, but any post must be sourced, within competence and compliant with employer supervision, recordkeeping, confidentiality and market-conduct obligations.

Visibility may lead to media or speaking opportunities, but audience growth is not evidence of expertise and the causal link should not be claimed without data.

Open or use an account only through permitted channels. Post deliberately, distinguish fact from opinion, cite sources, preserve required records and avoid confidential, inside or client information; do not treat market commentary as casual conversation.

LinkedIn, X and other platforms differ in format and audience, but none owns 'real-time conversation' or serves one universal branding function. Choose channels based on purpose and policy.

A relevant following may create useful introductions, but follower count is not a quality measure. Evaluate the accuracy of the work and the relevance of the audience instead.

Credibility online depends on accuracy, context and conduct. Transparent promotion may be permissible when approved; misleading, undisclosed or unrecorded promotion is not.

Fast-moving platforms increase the risk of error, confidentiality breaches and unrecorded business communications. Use review, delay and approved channels proportionate to the risk.

Online discussion can support professional relationships, but it is not inherently more real than other communication. Treat it as one channel subject to the same standards of evidence, civility and compliance.

Becoming the Go-to Person: Building a Reputation in a Niche

Many professionals begin broadly and later deepen one or more areas. Generalists can also become highly differentiated through judgment, synthesis or cross-product experience; specialisation is an option, not a requirement at year five or six.

A niche may be geographic, product-based, sectoral or technical. Nordic LBO structures are one possible example; choose a niche that reflects genuine, current expertise.

Develop regional expertise through authorised transactions, public research, local counsel and relationships, with attention to language, law, regulation and market structure. Travel and networking alone do not establish expertise.

Specialisation can make someone more useful for a class of questions, but recognition is not automatic or necessarily durable for twenty years. Maintain competence and keep evidence current.

The lesson is that you become a go-to person by specializing deeply and building genuine expertise in a specific area. The area can be geographic (Nordic deals), a transaction type (continuation fund financings), a structural innovation (subscription lending) or a sponsor type (lower mid-market family offices). But it has to be something real, in which you actually develop the expertise.

Becoming the go-to person requires several things. First, actually develop the expertise: work on multiple transactions in the niche, read everything about it, build relationships within it — sponsors, lawyers, accountants, other specialists — and learn the nuances, the subtle differences between approaches, what works and what does not.

Make expertise discoverable through accurate, approved work and clear role descriptions. The aim is credible usefulness, not an unsupported claim to be the best.

Third, deliver. When people work with you because of the niche expertise, the reputation has to be justified: be right, provide value, and make sure they come away feeling they made the right decision in working with you.

The downside of being known for a niche is the risk of being pigeonholed — people may assume you only do Nordic deals when your competence runs wider. The upside is that you are the person people think of for that area, and that creates opportunity.

A professional may begin with deep expertise in one region and later broaden through authorised work, public research and collaboration with local specialists. There is no fixed timetable.

Career Transitions in LevFin: Bank to Sponsor, Sponsor to Advisor, and Other Moves

Leveraged finance is an industry where mid-career transitions are fairly common. Someone spends a decade on the banking side, then moves to a sponsor to understand the perspective from the other side. Someone spends time as a banker, then becomes a legal advisor. Someone works at a bank, then at a sponsor, then at an advisory firm. The pathways vary.

A transition from banking to advisory can occur at any stage. Readiness depends on skills, mandate, opportunity, conflicts and personal circumstances, not a suggested sixteen-year timetable or unverified sponsor offer.

A transition can change compensation, benefits, deferred awards, job security and responsibilities. Compare the actual terms and risks rather than assuming a smaller advisory firm is necessarily less certain.

Reasons for moving may include learning, role fit, client mix, autonomy, culture or personal priorities. Advisory is not inherently a late-career role and may still involve management, sales and demanding hours.

Every transition involves new incentives, relationships and expectations. Assess the role on its own responsibilities, constraints and opportunities rather than treating one career path as universal.

Such a transition, and watching others make career moves in leveraged finance, teaches a few things. First, the fundamentals of credibility transfer between roles: the skills and reputation built as a good banker do not disappear on the move to advisory. But you do need to re-establish yourself in the new context, prove that you understand the new role, and be humble about what you do not know.

Skills and relationships can transfer between roles, subject to confidentiality, non-solicitation, garden-leave, conflicts and data-protection obligations. A professional network is not an asset that can simply be taken from an employer.

Third, different roles attract different people. Some are energized by the urgency and client-service intensity of banking; some by the strategic and analytical side of sponsorship; some prefer the advisory role, working across

many different situations rather than being embedded in a single organization. Knowing what energizes you matters.

Hiring conditions can affect the ease of a move, but timing markets is uncertain. Evaluate demand, funding, role quality and downside scenarios rather than assuming growth makes a move easy.

Not every career involves many radical moves. Staying within leveraged finance, moving between roles but not constantly, is a perfectly viable path — though partly because developed expertise and visibility provide options. Someone earlier in their career may need to be more opportunistic, taking the better role or the better firm even when it is not an obvious choice.

Evaluate a transition by purpose, role, people, economics, legal constraints and downside. Reputation may help, but skills, evidence, opportunity and fit also determine whether a move is possible.

The Importance of Credentials: CFA, LPC, MBA, and Whether They Matter

Credentials invite some mildly contrarian thinking. They matter in leveraged finance, but probably not in the way a lot of people think they do.

Credentials can be useful when a role, regulator or employer values them, but requirements and relevance vary. Use current official sources rather than generalising from reputation.

An MBA may support recruiting, learning or a career transition, but outcomes depend on programme, location, cost, experience and target role. Employers may care about education at any stage; avoid claiming that nobody cares by mid-career.

The CFA charter currently requires completion of all three exam levels and required practical skills modules, qualifying work experience and CFA Institute membership. CFA Institute states that charterholder work experience must total at least 4,000 hours over a minimum of 36 months. Requirements can change, so link to the current official criteria rather than relying on a 300-hours-per-level or four-year estimate.

For solicitors in England and Wales, the Solicitors Qualifying Examination has replaced the LPC as the main route. The LPC route remains only for candidates who meet the SRA's transitional requirements, currently ending in 2032. Other jurisdictions and legal roles have different qualification rules; consult the relevant regulator.

Demonstrated competence matters, but credentials can be mandatory or materially relevant for some roles and jurisdictions. Avoid claiming that an uncredentialed candidate will almost always beat a credentialed one.

Consider an MBA or CFA programme only after checking current requirements, costs and relevance to the intended role. To qualify as a solicitor in England and Wales, follow the current SRA pathway: generally the SQE, with the LPC route limited to eligible transitional candidates. Obtain jurisdiction-specific guidance.

The CFA charter's relevance varies across investing, research, advisory and other roles. Check actual job criteria and current employer evidence rather than ranking its value by assertion.

Work-Life Balance in Leveraged Finance: The Honest Truth

Workload in leveraged finance can be intense, but hours vary significantly by role, firm, geography, seniority and deal cycle. This section should discuss risks and choices without presenting harmful practices as inevitable.

Working hours vary by role, firm, geography and market cycle. Chronic excessive hours create fatigue and control risk; staffing and working arrangements should comply with applicable law and firm policy rather than normalise a universal extreme-hours path.

Sustained overwork can impair health, relationships and decision quality. Firms and managers should plan staffing, monitor fatigue, enable leave and provide escalation routes rather than rewarding single points of failure.

Do not frame endurance as luck, suggest that a spouse must absorb the work, or imply that people without children are better suited to the industry. Caregiving and family status should not determine access or advancement.

Some leveraged-finance roles have periods of limited predictability, but firms and teams differ. Avoid declaring the entire industry incompatible with balance or claiming advisory is less extreme; assess actual practices and applicable working-time rules.

Professionals should not be penalised for lawful boundaries, health needs or caregiving responsibilities. Performance should be assessed on role requirements, quality and outcomes, and unsafe staffing or retaliation should be escalated through appropriate channels.

Do not prescribe ten to fifteen years of overwork as the route to later control. Build sustainable practices from the start, reassess workload and role fit, and seek support or change when demands are unsafe or incompatible with important obligations.

Career workload does not follow a universal brutal-then-selective arc. Responsibility may rise with seniority, and advisory work can be as time-intensive as banking. Use role-specific evidence.

People differ in their tolerance for intensity, and preferences can change. Organisations still have a duty to manage workload and conduct; individual enthusiasm does not make unsafe practices acceptable.

Work-life balance is possible to different degrees across roles and institutions; it is not categorically unavailable early or guaranteed later. Evaluate the actual job, negotiate where possible and do not equate lower intensity with lower professional worth or upside.

Managing Your Career Through Market Cycles: What to Do in a Downturn

A long career may span several downturns, but the relevant episodes depend on geography and product. Use dated sources for market history and avoid implying that every reader experienced the same cycle sequence.

Reputation, relationships and technical expertise can be valuable in a downturn, but no evidence establishes personal brand as the most valuable asset. Liquidity, role, firm stability, skills and conduct also matter.

During the 2008-2009 crisis, many credit markets and institutions were severely disrupted, but the timing and level of deal activity varied by segment and region. Any duration claim should use a defined market dataset.

In a downturn, provide sponsor or client support only within an authorised engagement and approved commercial terms. Uncompensated advice can create conflicts, liability, fairness and recordkeeping issues.

Relationships maintained through a downturn may support future work, but do not claim that business returned first to those advisers without evidence. Recovery timing and mandate awards depend on many factors.

In a downturn, avoid impulsive decisions but do not dismiss legitimate concern. Update liquidity and employment scenarios, maintain skills and relationships, and seek advice where needed; strong reputation does not guarantee outperformance or job security.

Second, stay visible. It is counterintuitive, but business does not all stop in a downturn. Some sponsors are refinancing, some are being restructured, some are doing smaller deals, some need advisory work. If you stay visible, keep your relationships warm and keep offering perspective, you are positioned to win the business when it comes.

Third, invest in relationships. In good times, when you are busy, relationships can feel like a luxury; in downturns, when you have more time, they are your most important asset. Reach out to people. Have conversations. Check in with sponsors. Talk to lawyers. Reinforce the relationships you have built.

Fourth, keep your expertise current. Downturns tend to bring structural change, regulatory change and market evolution. Stay on top of it: read, think, develop perspectives. When the market recovers, you want to be someone whose expertise is current and relevant.

Assess a move during a downturn carefully. Some firms hire while others retrench, but the market does not make the timing inherently good; compare role quality, funding, compensation, contractual restrictions and downside.

Disciplined relationships, current expertise and useful work can improve resilience. Do not assume a recovery date or promise that these actions will position someone successfully when it comes.

The Importance of Cross-Border Experience in European LevFin

European and U.S. leveraged-finance markets differ in documentation, law, participants and practice, but each is internally diverse. Cross-border experience can be valuable; it is not one of the most valuable career assets by definition.

European leveraged finance spans multiple legal systems, currencies, insolvency regimes, tax rules, languages and market practices. Avoid assigning one leverage culture to Germany, France, the Nordics or Southern Europe without a current, defined dataset.

The economic logic of leverage travels across markets, but a covenant does not work identically in Germany, Sweden and France. Governing law, drafting, security, guarantees, enforcement, insolvency and local mandatory rules can change its operation; use local counsel and the actual documents.

Do not claim that Nordic sponsors delever earlier or manage leverage better than other markets without representative evidence. Compare transaction terms, borrower sectors, vintages and samples before drawing regional conclusions.

Exposure to multiple markets can broaden perspective, but deep expertise in one market is also valuable. Cross-border work does not automatically create better pattern recognition and must be paired with local expertise.

Cross-border experience is built partly systematically and partly opportunistically. Deliberately seek assignments in different European markets, build relationships with professionals in different markets, read about what is happening in each. Over time you become someone who understands European leveraged finance more broadly, not just one regional market.

Cross-border experience may help with multi-jurisdiction transactions and regional analysis. Credibility still depends on accurate, local-law-informed work rather than the breadth of a conference narrative.

Cross-border exposure can be useful but is not required for every European leveraged-finance role. Seek it where relevant and obtain local legal, tax, regulatory and language support.

What Experience Teaches: The Reflection Section

Sustained work across transactions and market cycles can broaden perspective, but experience should be evaluated by the quality and relevance of the work rather than an unsupported count of years, transactions or sponsors.

What a career of working in leveraged finance teaches about building a personal brand that matters comes down to the following.

First, technical excellence is not optional. Everything else rests on a foundation of genuine competence. You can be charismatic, well-networked and visible, but if you do not actually know your craft, people will work it out, and once they do, the brand is damaged. The investment in becoming excellent at what you do is the most important investment you can make.

Second, relationships matter. Opportunities and trust can grow through consistency, reliability, useful work and genuine engagement, alongside price, capability, conduct and competition. Social media can support relationships; it cannot replace them.

A durable reputation should reflect genuine interests, supportable expertise and honest communication. Authenticity does not excuse oversharing or bypass employer and regulatory approval.

Specialisation can support differentiation, but generalists can create substantial value through synthesis, breadth and judgment. Neither approach universally beats the other.

Consistency can build trust, but career outcomes do not belong only to people who publish or attend conferences for decades. Quality, conduct and results matter, and public visibility is optional for many roles.

Generosity can strengthen professional relationships, but time, knowledge and introductions should be shared within confidentiality, conflicts, procurement and workload boundaries. Reciprocity is possible, not guaranteed.

Seventh, a personal brand should be a reflection of your actual work and your actual expertise. It is not a marketing project separate from the job; it is a byproduct of the quality of the work, the relationships built, the perspectives developed, and the visibility that follows from being genuinely good.

Eighth, market timing matters. Some opportunities come from being in the right place at the right time, or from holding a particular expertise when the market needs it. You can influence this partly — by developing expertise in areas that are becoming important, by positioning yourself for market changes — but luck plays a role, and it is honest to acknowledge it.

A strong reputation can create options, but career transitions also depend on transferable skills, market demand, contractual restrictions, resources and opportunity. No move is made feasible by personal brand alone.

Interest in the work can sustain learning, but enthusiasm does not replace competence, ethics or sustainable working practices.

A professional reputation grows from competent, ethical work, reliable relationships and responsible communication. Public visibility is optional and must remain accurate, authorised and within legal and employer boundaries.