European Commercial Real Estate Lending Principles

Commercial Real Estate Finance Council Europe®

Commercial Real Estate Finance Council
EUROPE®

Contents

2 Introduction

2.1 Lender Committee

The Commercial Real Estate Finance Council Europe ("CREFC Europe") formed a Lender Committee ("Committee") to further underpin the strategic broadening of its remit. The Committee seeks to offer an opportunity for the providers of finance active in the European Commercial Real Estate market to interact and address issues particular to their business. This Committee is composed of commercial banks, pension funds, insurance companies, finance companies, funds and other private investors. It will examine best practices, effects of regulatory reform and, where possible, standardisation to the sector amongst other initiatives. The Committee's focus is broad in scope but incorporates considerations of:

- The senior balance sheet lending arena;
- The corporate and capital markets arena (such as unsecured debt, convertible bonds, derivatives, debentures and Eurobonds, CMBS, covered bonds / Pfandbrief);
- Subordinated debt (stretched senior, junior, mezzanine and preferred equity); and
- Growing involvement of alternative lender types (institutional, insurance, fund based capital providers).

2.2 Best Practices

The crisis of the last few years has meant that lending practices have been rigorously tested and significant insight as to their robustness gained. Meanwhile, there has been a profound reduction in the number of property lending personnel and the supply of debt remains constrained. Europe is seeing a fragmentation of lender type - not just balance sheet using banks and capital market issuers but the appearance of a more mature subordinated debt market and growing interest from new entrants such as the insurance sector. The Committee therefore recognises that there are good reasons to focus on Best Practices:

- *Human Capital*: Banking market consistently suffers from lack of experienced property bankers mainly due to the negative impact of the property cycle in recruitment / training.
- *Implementing Recent Lessons Learned*: Perfect opportunity to bring together knowledge recently gained from managing the fall out of the credit crisis.
- *Market Harmonisation Fostering Liquidity*: Seek to ensure that CREFC Europe supports the aim to deliver a high quality approach to lending that is harmonised across differing capital sources.

The Committee has identified six overarching lending “pillars”:

- Transaction Structuring;
- Documentation;
- Due Diligence;
- Intercreditor arrangements;
- Tax
- Hedging

The Committee had already determined to create a set of European principles holistically valid for lending. This paper covers Structuring / Documentation. A tax bulletin entitled “European Commercial Real Estate Lending Tax Guide” was issued in March 2012. Related papers on Due Diligence and Intercreditor arrangements will follow. Specific French and German variations will also be produced to demonstrate CREFC Europe’s commitment to representing the wider European market. This work will finally dovetail into the “Market Principles for Issuing European CMBS 2.0” process also being undertaken by CREFC Europe. In effect, CREFC Europe is focusing on ensuring loans are well structured, executed and managed and that those loans that are then ultimately (partially) securitised/syndicated are also subject to well structured, executed and managed securitisations/syndications.

CREFC Europe is part of the working group assisting the Loan Market Association (“LMA”) in developing an “LMA Standard” real estate finance facility agreement which should be completed in early 2012. The Bank of England has further sought best practice views from CREFC Europe.

2.3 Approach

The following recommendations assume a *professional* degree of existing knowledge and experience. They do not seek to incorporate the obvious basics of property lending but rather focus on areas of importance and controversy and where specific lessons have been learnt. A single advance term secured investment loan with multiple properties has been considered as the base transaction. It is intended that this paper will be updated on an annual basis by the Committee.

3 Best Practice Recommendations

3.1 General

Issue:	Recommendations:
Ensure related due diligence process is focused not just on property but also corporate aspects.	CREFC Europe is currently undertaking a comprehensive Due Diligence Best Practices exercise with draft papers envisaged in H2 2012. This paper simply highlights certain matters. Due Diligence typically includes: • Valuation; • Certificate of Title work covering title, planning and lease structure; and • Review of corporate documentation (e.g. Certificate of Incorporation, Memorandum and Articles of Association, recent financial accounts). • In addition Lenders should consider ensuring appropriate conditions precedent due diligence has been undertaken with regards to: **<u>PROPERTY LEVEL</u>** • Full lease review and tick back to source documentation; • Mechanical and Engineering soundness; • Tenant improvements ("TIs") / capital expenditure assessment; • Environmental contamination; • Energy efficiency; and • Insurance **<u>CORPORATE LEVEL</u>** • Accounting/legal due diligence of Borrower where it is "old" or where historical (contingent) liabilities are suspected of having existed. • Tax report that specifically covers the tax implications of purchasing, owning and selling property and the likely cash outflows resulting (please see the Ernst & Young/CREFC Europe "European Commercial Real Estate Lending Tax Guide" on this matter). The desirability of a formal tax report is clear but its absolute need will depend on the transaction complexity and leverage. Results of due diligence ultimately should feed into cash waterfalls. Ideally such due diligence should be undertaken by independent third parties or, if necessary, Borrower advisers under strong duty of care language and appropriate liability exposure. All due diligence must be addressed to enable reliance with appropriate disclosure language in all relevant circumstances.

Cross Border transactions create unforeseen enforcement issues.	The wide range of tax efficient structures often means that UK property may well be owned or managed by vehicles outside of the UK. The Channel Islands is a favoured location, for example. Recent experience has clearly indicated that the normal UK enforcement processes can be adversely impacted by other jurisdictions being involved. For example: • It may be impossible to appoint, or there may be additional costs in appointing, an administrator. • The local law may provide for a sale on enforcement but no ability to take control with a view to holding until better conditions prevail. • Local laws may be new and untested – a lack of clarity as to what they mean. The Lender's lawyers should provide clear written advice on the potential enforcement impact of any cross border structure with suggested mitigation strategies.

3.2 (Condition of) Utilisation

Issue:	Recommendations:
There may be material payments that need to be undertaken to protect the value of the underlying collateral (e.g. insurance premium or head leasehold payments).	Incorporation of the concept of "Property Protection Loans" as such advances are pre-agreed by the Borrower and allow the Lenders to unilaterally advance sums to cover these items if required to protect their position.
Risk that transaction fundamentals change between commitment and drawdown – biggest risk being interest rate movement. Interest Coverage Ratio ("ICR") analysis often considers stressed property cash flows using a static interest rate.	In many situations general best practices suggest incorporating draw stop conditions based on ICR, Loan to Value ("LTV") and Loan to Cost ("LTC") set at the initial underwriting position, not default levels. LTC is also often included to avoid the risk that valuation results lead to a materially higher LTC than LTV. Potentially consider stating a maximum acceptable interest strike rate.

3.3 Repayment / Prepayment / Cancellation

Issue:	Recommendations:
Intra Interest payment Date ("IPD") repayment.	Either (i) repayment on an Interest Payment Date or (ii) the margin is made whole to the next IPD. Minimum of 10 business days' notice for repayment.
Repayment priority.	Recommend pro-forma documents include requirements for senior debt to be fully repaid in priority to any subordinate debt. Often the precise deal mechanics will adjust this presumption.
Clarity on events that require mandatory prepayment.	Recommended to include disposals, lease premiums on surrender, insurance proceeds, compulsory purchase and illegality proceeds.

3.4 Hedging

Issue:	Recommendations:
Hedge Counterparty – Following the Lehman Brothers Chapter 11 experience there is greater awareness of counterparty credit positions and changes to that counterparty.	• Compromise of a counterparty being either an original Lender, an approved acceding Lender or a rated counterparty. • Clear implications on failure to perform should be set out. • Rating language may well be at least needed for any capital markets issuance. • No changes permitted to counterparty without Lender and counterparty consent. • Lenders to have ability to require closing out of hedging on insolvency of counterparty.
Ensure up front and ongoing agreement of hedging strategy.	Written strategy pre-agreed by all Lenders probably including parameter ceilings e.g. maximum strike rate. No changes without all Lenders consent.
Appropriate ranking and security.	Pari passu beneficiary of security; carve outs for any margin call agreements (that are to be used first).
Termination rights – no market standard.	The only market consensus is that there is no market consensus regarding counterparty termination rights. Bank hedge desks have increasingly had greater input in the loan negotiation process with a strong focus on when they have the unilateral right to close out hedging positions as opposed to explicit acceleration rights. Historically such termination rights might have occurred on loan acceleration. Now this varies from institution to institution with termination due to insolvency, default, tax event, tax event on merger and force majeure being hotly discussed. Furthermore, counterparty voting rights are also being raised, usually in the post termination period. It must be emphasised that these issues are being repeatedly discussed on a deal by deal basis and CREFC Europe intends to focus on this issue in 2012 within the Loan Hedging Working Group.
Hedging levels – automatic mechanisms to cater for over/under hedging.	No more than 105% and presumption of 90% of loan amount hedged at any time but greater permitted if occurs through a non-credit related product e.g. a cap.

3.5 Fees, Costs & Expenses

Issue:	Recommendations:
Up Front Fee – ensure actually paid irrespective of whether loan drawn.	"Payable" at signing and "paid" no later than earlier of first drawdown or expiry of commitment period. Ensure consideration as to who is responsible for paying when the Borrower is a Special Purpose Vehicle ("SPV") – often the main client entity will guarantee such obligations. Current accounting practices require clarity on the reason for the payment. As a general rule 'structuring' or 'arrangement' fees can be recognised at loan commencement. "Participation" fees often are required to be amortised over the loan life.
Agency costs tend to increase post default.	Agency Fee needs to flex to take account of work involved post default.
Prepayment Fees sometimes unfair when either the Borrower addresses a loan deterioration or where issues occur beyond its control.	Prepayment Fees not payable on cure of (potential) default, increased costs occurring due to illegality or on receipt of insurance proceeds. Prepayment fees should however be distinguished with break costs.
Prepayment Fees structured to reflect capital at work.	The current market standard is typically fixed basis point penalties for the first few years. A number of Lenders (especially the non-bank lenders) are starting to advocate margin make whole provisions for a certain number of years. Such a choice is at the discretion of Lenders.
Default margins apply purely on a payment default. In a low interest rate environment many problematic situations can arise without actual payment default occurring.	Historically default margins have only applied on payment default. The introduction of Basel II and inevitably Basel III has demonstrated banks' capital costs rise significantly post any default. Arguably should a default margin apply on any default it could be represented as a genuine pre-estimate of the additional costs of the default which should generally mitigate the risk that it is identified as a penalty and therefore unenforceable. Whilst this approach is being adopted by a growing number of Lenders it is by no means a market standard. An alternative structure which only captures declining deal performance is an LTV/ICR margin grid where a default triggers the highest margin. Finally some law firms are now recommending charging default interest for failure to satisfy a condition subsequent or failure to provide information on time.

3.6 Accounts

Issue:	Recommendations:
Rent Account: Practical balance on flow of everyday funds.	• Agent sole signing rights to Rent Account, complete lockbox account. • However it should be queried whether tenants pay directly into that account or not. • The credit crisis is a recent reminder that property costs usually have to be paid irrespective of whether Lenders assumed they did not. • It is generally more practical to get a managing agent to owe a duty of care, collect monies, retain appropriate (and capped) irrecoverable/agreed property costs and then transfer net amount to the Rent Account. Hedging counterparty transfers any payments direct to Rent Account. • Agent then deals with head lease payments, debt service requirements, capex / TI and tax retentions and any surplus goes into General Account where Borrower has signing rights. • Consider whether corporate SPV costs (pre-agreed and capped) come out before or after Rent Account. • Typical to leave Borrower to deal with VAT flows.
Capital Expenditure ("Capex") / Tenant Improvements ("TI") Account	• Given increased focus on Capex a separate identified account is usually justified. • Based on initial and annually updated professional advice (see Business Plan point above). • Funded day one with pre-determined "Catch Up" Capex. Periodic transfers occur in an agreed way to cover identified future Capex obligations and TIs likely to arise. • Only Agent has signing rights and releases as and when required. • Ensure Borrower cannot commit to Capex / TIs above an agreed amount without Lender consent.
Tax Account	• Based on initial and annually updated tax advice. • If interest on shareholder debt used as a tax shield then robust accountant opinion on tax deductibility should be obtained. • Pre funded with identified Stamp Duty Land Tax / VAT liabilities. • Periodic transfers from Rent Account on pre-agreed accruals basis to cover corporation tax liabilities. • Only Agent has signing rights and releases as and when required.
General Account	• Lenders can lockbox the account on default.
Rating	• Whilst arguably not market standard CREFC Europe believes recent history recommends a minimum rating requirement for account providers certainly for accounts where large capital sums flow through.

3.7 Tax / Increased Costs / Other Indemnities

Issue:	Recommendations:
Lenders' own tax position – new entrant funds, insurers, etc that are not classically banks could create risk they are subject to withholding tax from day one.	Initial Lenders to confirm that they are not subject to withholding tax then Borrower takes subsequent change of law risk for such Lenders; subsequent Lenders treated in a similar way.

3.8 Guarantees & Guarantors

Issue:	Recommendations:
Use of Guarantees prevalent and shown to have inherent weakness, especially Fund Guarantees.	Acceptances of guarantees are always a subjective decision by Lenders. Common mistakes in their use include failing to take account of Guarantor jurisdiction and consequent enforceability rights, requirement to prove loss, contingent commitments, other guarantees, differentiating between net assets and actual liquidity, whether capital is invested or merely committed and by whom and ensuring guarantees are called long before either liquidity is utilised or unused commitments are drawn or expire unused. Serious consideration of the wording and nature of guarantee tests/covenants is advisable.
First demand guarantee or not?	First demand is strongly encouraged.

3.9 Representations

Issue:	Recommendations:	Notes:
A lack of market standard approach exists and a number of “bear traps” for the Lender exist.	The LMA process intends to produce a pro forma clause. CREFC Europe feels such a list should at least focus on for each obligor: • Status - status of the obligor and its power to own its assets and carry on its business; • Binding obligations - obligations expressed to be assumed by the obligor are legal, valid, binding and enforceable; • Non conflict with other obligations - the entry into and performance by the obligor of the transactions contemplated by the documents will not conflict with laws or regulations, constitutional documents or other agreements binding upon it; • Power and authority - the obligor has the power to enter into and perform the relevant transactions and no limit on its powers will be exceeded by the transactions; • Validity and admissibility in evidence - all necessary authorisations required to enable the obligor to enter into and perform its obligations and to make the relevant documents to which it is party admissible, and all authorisations necessary for the conduct of its business, have been obtained or effected and are in full force and effect;	All such representations should be deemed repeated on each utilisation request, the first day of each interest period and when a new entity becomes an obligor. “To the best of knowledge” caveat should be resisted. Accuracy of representations is ultimately a risk, not fault, allocation exercise. For example, it may not be the fault of the Borrower that information provided by or on behalf of itself and upon which the Lender has based its decision to lend is inaccurate, but the Borrower, not the Lender, should bear the risk. The fact that a representation is incorrect or misleading is typically only an event of default insofar as it is incorrect or misleading in a "material" respect. Adding materiality language to the representation may amount to "doubling up" on materiality.

	• Registration requirements - except for specified registration requirements, it is not necessary to register any of the relevant documents in any public place or elsewhere; • Governing law and enforcement - the choice of [English] law as the governing law and any judgment obtained in England in relation to the documents will be recognised and enforced; • Deduction of tax - no day one requirement to deduct for on account of tax from any payment under the relevant documents and there is no requirement to deduct tax from rental income; • No filing or stamp taxes - it is not necessary under the relevant laws to file, record or enroll or pay any stamp, registration or similar tax in relation to any of the relevant documents and any required disclosures in relation to stamp duty land tax have been made; • VAT - the obligor is not a member of a value added tax group [other than a group made up solely of obligors]; • No default - no default is continuing or might reasonably be expected to result from the transactions and no other event or circumstance which constitutes a default or termination event under an agreement is reasonably likely to have a material adverse effect; • Information - all information (including general information, information in relation to the property due diligence reports and information in relation to the valuation) is true and accurate and does not omit relevant information; • Financial statements - its financial statements have been prepared in accordance with GAAP including, if applicable, IFRS and there has been no material adverse change since the day one financial statements; • Pari passu ranking - the obligor's payment	

	obligations under the relevant documents rank at least pari passu with unsecured and unsubordinated creditors; • No proceedings pending or threatened - no litigation, arbitration or administrative proceedings have been started or threatened against the obligor; • Title to property - the relevant obligor holds legal and beneficial, and good and marketable, title to the relevant property free from security interests and except as disclosed in the property due diligence reports there are no issues in relation to the properties; • no other business - no obligor has traded or carried on any other business, it has no subsidiaries and it has no employees or obligations in respect of a pension scheme; • Centre of main interests and establishment - the obligor's centre of main interests and establishment is in [England and Wales]/[its jurisdiction of incorporation]; • Ranking of security - the security conferred by the security documents is first priority security of the type described; • Ownership - the obligor is owned by the person or persons identified as part of the credit process.	

3.10 Information Undertakings

Issue:	Recommendations:
Financial Statements	Whilst filing dates and requirements to produce consolidated accounts may influence deal specifics. Timely production of statutory and interim management accounts under recognised accounting standards is vital.
Compliance Certificate regularly provided and undertaken on an appropriate basis.	Provided in advance of IPD assessing position at that IPD and signed by 2 directors.
Lack of consistent property reporting.	Property monitoring reports provided on each IPD should seek to cover information on: • Existing occupational tenants showing rent, service charges, VAT, key lease terms (annual rent, lease term/breaks, rent review provisions, unusual lease provisions); • Management accounts / cash-flows; • Arrears information; • Rent reviews, lease expiries, surrenders and (prospective) new lettings; • Material correspondence regarding insurance; and • Up-to-date capital expenditures and repair/maintenance plans.
Business Plans	Provision of annual business plan for approval; especially to cover irrecoverable operational expenses which is a general waterfall deduction.

3.11 Warning Milestones / Financial Covenants

Issue:	Recommendations:
Hard as it is to believe – some deals have no consequence to covenant breach.	Ensure purpose to covenant structure.
Too often deals have a simple covenant breach point that moves the transaction from "performing" immediately to "default".	• Cash sweep triggers that occur on ICR/LTV ratios designed to reflect that the deal has moved beyond only a moderate deterioration point • Sweeps create cash liquidity that can be used on appropriate asset management strategies and amortisation • On some deals consider other ratio triggers that allow Lender greater rights e.g. right to have greater sign off on asset management strategies or requirement to replace property/asset manager

Ensure Interest Cover acts as an early warning trigger rather than reflecting disaster has already struck. Also recognition than SPV financing means one should be looking at corporate level NOI not pure Net Rent.	Comparison of Finance Costs against Net Operating Income ("NOI") **NET OPERATING INCOME** • Not Net Rent. • Unless property has extremely short leases then one should undertake an annual projected income calculation; if short leases do exist where assuming all leases that can break do is often unrealistic, then a 3-month look back annualised figure is perhaps more appropriate (unless also a seasonal cash flow (e.g. hotels) when a one year look back may be considered). • Net Rent is effectively calculated by taking a forward 12-month projection of Gross Rent and then: - Break clauses assumed to occur; - Only considering contracted rent; - Recognising only contracted rent reviews increases; - Ignoring all rental flows where tenant already one+ months in arrears or where insolvent • And then deducting irrecoverable property costs (including related VAT) such as: - Ground rents; - (Empty) rates ignoring any short term empty business rates mitigation scheme; - Service charges; - Insurance premium; - Repair and value maintaining Capex; and - Agreed and capped property and asset management fees. • NOI = Net Rent less any approved and capped SPV running costs. • Interest on cash balances and ancillary income to be ignored unless very compelling rationale. • Tenant incentives and Capex are arguably items of a capital nature and "below the line". **FINANCE COSTS** • Interest and fees. • Finance costs always forward looking projection. • Take account of hedging; for swaps use the swap rate; for caps use the cap itself or the LIBOR rate for the remaining loan period (especially relevant in an upward sloping LIBOR curve environment) or, at a minimum the 12 month LIBOR rate.

Loan to Value – consistent and independent basis.	**LOAN** • Use the standing loan amount unless there is a reason to use the facility amount (e.g. when structure allows for provision of guarantees under facility terms). • Measures of mark to market are not at all market standard. Some situations (e.g. significant loan/hedge term imbalance) may warrant some considerations. **VALUE** • RICS Red Book Market Value. • No artificial constructs (e.g. internal leases) to be considered. • Adoption of strict German Mortgage Bank rules in Valuer independence • Lender right to call valuation at least annually and when believes default outstanding or where a default might arise as a consequence of such a further valuation. • Copies of all valuations received by Borrower to be provided to Lenders although to be ignored for covenant testing purposes.
Covenants should apply at all times not just on discrete dates.	Only formally tested quarterly but ongoing duty of directors to ensure complied with at all times.
Who undertakes the covenant calculations?	The Borrower should prepare the calculations and provide them to the Agent with supporting documentation. The Agent's calculation should prevail on any disagreement.
Curing of covenant breaches should be permanent. Where temporary curing this should be severely restricted in terms of time or extent to avoid prolonged artificial maintenance of a transaction.	Make a clear distinction between "permanent" cures and "subsidy" cures. Permanent cures such as capital repayment or cash collateral (when finance costs related to that cash sum are ignored) should be unlimited. Subsidy cures such as cash injection for interest test shortfall should be limited to no more than a maximum of two consecutive IPDs and/or not more than two in any twelve month period and/or four to six times in total.

3.12 General Undertakings

Issue:	Recommendations:	Notes:
Negative Pledge carve outs can create issues.	Lenders should adopt an approach that there should be no other liabilities incurred apart from pre-identified specific exemptions.	"Basket" exceptions and wide exceptions language (e.g. "ordinary course of business") should be avoided.
Merger / Acquisitions	Not allowed without Lender consent.	
VAT	Bar on VAT group unless solely with other obligors as membership of a VAT group gives rise to liabilities for VAT obligations of other group members.	

3.13 Property Covenants

Issue:	Recommendations:
Insurance – more care needed in clause formulation.	• Legal advisers have already tightened insurance provisions. The German Pfandbrief led banks remain extremely focused here recommending a number of aspects be considered as almost mandatory. The Lenders should ideally be co-insured with appropriate non-vitiation, subrogation waiver and loss payee clauses. At the very least the Lenders interest should be noted. A Borrower may seek a carve out that permits proceeds below a certain de minimis threshold to be paid to the Borrower for minor insured events/claims. • In addition an inconsistent approach exists in relation to the use of rating level requirements for insurance counterparties, notwithstanding its use is arguably sensible. • Pfandbrief rules also require insurance to be asset specific (i.e. not a block policy) and the borrower/owner must insure (i.e. insurance via a superior interest holder does not work).
Lenders still require input on leasing matters without this being too intrusive.	Each transaction is far too specific to provide generalised comments. The trust placed in the asset manager, the scale of assets, lease diversity and asset quality are all deciding factors. That said, some consent control over material new leases and cumulative surrenders is still advisable (by % GOI or ICR for example).

3.14 Disposals / Substitution

Issue:	Recommendations:
Portfolio transactions invariably contain property of mixed quality. Applying a dogmatic standard allocated release amount ("ALA") release pricing that applies at all times leads to cherry picking risk especially at a time when poorer properties are illiquid.	• If using ALAs then ensure based on qualitative assessments as much as value. • Consider ALA flexing on basis of updated values and quality review (probably on annual basis). • Any sweep covenants should also apply to disposal proceeds.
Ensure that no transaction manipulation permissible through use of disposals clause.	• Sales only on arms' length basis to third party. • Lender consent specifically required if the net disposal value is below the initial value.
Value destruction risk exists on sale of part of an asset (e.g. individual residential sales can lead to remaining "Swiss Cheese" residential block).	Majority or all Lender consent specifically required for part sales.
Danger of collateral deterioration and fundamental shift of deal type through poorly controlled substitution rights.	No pro forma substitution clause. To be considered on a deal by deal basis with caution and with Lender consent required – perhaps without having to act reasonably (i.e. absolute discretion).

3.15 Security

Issue:	Recommendations:
Recent history has shown that many creditors have been frustrated in their attempts to enforce and sell the Borrower SPV as opposed to the underlying asset. SPV sale might be desired for reasons of speed, efficiency, SDLT mitigation. A principal stumbling block is the existence of non-consenting other creditors.	Obtain appropriate security over other material liabilities (e.g. subordinate third party debt, shareholder loans) that allow the cancellation or movement of such liabilities to facilitate SPV level (as opposed to direct asset level) sale.
Only comprehensive belts and braces security package ensure creditors can maximise their enforcement options.	A strong security package will typically include, but will not be limited to: (i) A first legal mortgage over the underlying properties; (ii) First fixed and floating security over all assets of the obligors including: a. First ranking charge over rental income and all receipts; b. First charge over the bank accounts; c. First ranking assignment of insurances with the Lender as co-insured; d. First ranking assignment of hedging instruments; e. Assignment of the benefit of all relevant (and material) contracts in which the obligors have an interest; (iii) Charge over the shares in the obligors; (iv) First charge over all subordinated indebtedness. (v) Subordination deed and intercreditor agreement (as appropriate); (vi) Duty of care with each property manager and asset manager; and (vii) Cross-guarantees or such other structure or instrument to achieve full cross collateralisation of the obligors.
Looking beyond the SPV is sometimes desirable to strengthen security position.	Consider whether Holdco security or convertible rights on default might further enhance a specific transaction.
Recovery claims from Report Providers rarely considered upfront.	CREFC Europe believes that it may be appropriate to incorporate provisions for prepayments out of the proceeds of claims made against report providers (e.g. claims against solicitors who prepared the certificate of title).

3.16 Changes to the Lenders / Obligors / Other Parties

Issue:	Recommendations:
Allow easy asset management transfer on enforcement.	Lender right to terminate asset management agreements with no more than 3 months' notice on default / acceleration.
Change of Control ("CoC") is often structured to trigger mandatory prepayment which is an "after the fact" trigger.	Better to structure CoC as an event of default which is therefore requiring dialogue "before the fact".
CoC prevention.	CoC may be declined by banks for deal specific or KYC reasons. In addition another explicit valid reason is consequential increase to cluster risk (i.e. overall group exposure to a lender).
Due to KYC / money laundering great focus is	Lender consent required for CoC of the Borrower, Ultimate Shareholder, Asset Manager and, if relevant, Fund Manager.

given to the legal owning entities. Surprisingly often a lack of focus occurs regarding the entities actually managing the investment (e.g. a GP of a fund) or the asset manager undertaking the core property work.	
The mechanisms for the replacement of Lenders has been found wanting. Examples of this are “Tranche warfare”, dissenting syndicates, “Loan to Own” strategies, non-bank Lenders with varying requirements, Borrowers restricting assignment to an extent that damages liquidity.	Overarching proposals: • No Borrower consent rights over Lender assignment of its position. Consultation rights may be a compromise so long as “consultation” is properly defined to ensure no more than non-binding dialogue. • Comprehensive drafting permitting syndication, securitisation and loan tranching to facilitate optimised balance sheet management and foster market liquidity. • Due consideration as to whether other Lenders get consent rights in certain circumstances e.g. sales to non-banks or vulture funds pre default or the sale of any subordinated debt by that creditor. • “Yank the Bank” and non performing Lender clauses are contentious but the LMA does have language to include if chosen. • Agent to keep a record of all ultimate Lenders available to all others and Lender disclosure mandatory. The LMA are not in agreement with this point although CREFC Europe continues to see this proposal as sensible. • General prohibition on Borrower or partners related to Ultimate Shareholder taking position in debt.

3.17 Agent / Arranger

Issue:	Recommendations:
Clarification of Agent role required. In most sectors, Agents are actively seeking to reduce their unilateral decision-making powers. Conversely, in Real Estate Finance, Agent roles are often either structured with strong decision-making powers or Agents interpret their role that way. Clarity should be sought.	• Start from presumption that the Agent has no discretionary decision making powers and is a pure processer. Decisions should be made on the instructions of the lending group. While most decisions should be able to be made by Majority Lenders, some particularly important decisions should be reserved to all Lenders (such as amendments to pricing, release of security/guarantees, etc). • If the Lenders determine to empower Agent with some decision making power there should be a specific agency document that clearly sets out what these are. • This does not detract from the need to allow Agents to act unilaterally when to not quickly act is damaging.
Agent/Arranger role in club deals.	• Generally one or more of the Lenders will carry out the co-ordination role and will receive an arrangement fee for doing so. • One of the Lenders (often through a related entity) will carry out the role of facility agent (and security trustee, if the two roles are separate) and will receive an agency fee for doing so. • The agency / security trustee roles are independent from lending roles and the agent may have separate requirements in respect of the loan and security documentation.
Substantial conflicts of interest have been seen to arise e.g. when Senior Agent is also in the subordinated debt or equity.	Agent should have explicit requirement to give due consideration to conflicts of interest.

3.18 Confidential Information

Issue:	Recommendations:
Onerous confidentiality restrictions impair liquidity of loan positions.	Recognition that certain parties e.g. in securitisations will not or cannot enter into confidentiality undertakings. In particular numerous lenders have found it challenging to share information with insolvency practitioners/receivers in the run up to an anticipated bankruptcy/enforcement or when potential buyers/asset managers are involved in strategies such as pre-pack administration. Lenders should however give due regard to any information process or recognise certain information is proprietary or price sensitive.
Avoid needing Borrower's consent to appointing third party advisers post default.	Ensure pre-agreed mechanism incorporated into documentation.

About CRE Finance Council Europe:

Commercial Real Estate Finance Council Europe (CREFC Europe), part of CRE Finance Council (CREFC) headquartered in the U.S., is the premier trade organisation for the global commercial real estate finance industry and has been active in Europe since August 2004. We are dedicated to promoting the strength, transparency and liquidity of commercial real estate finance worldwide. We have become an effective channel for the industry to influence the regulatory framework and play a vital role in setting industry standards and promote best practices. We also provide educational sessions led by leading industry experts and networking opportunities for all market participants within this key sector of the global economy.

CREFC Europe's focus has expanded far beyond its roots in CMBS to encourage participation and drive involvement from the wider CRE markets. Our Members come from areas across the commercial real estate finance spectrum and include participants from the lending, investing, servicing and professional services communities across Europe.

www.CREFC.org/eu