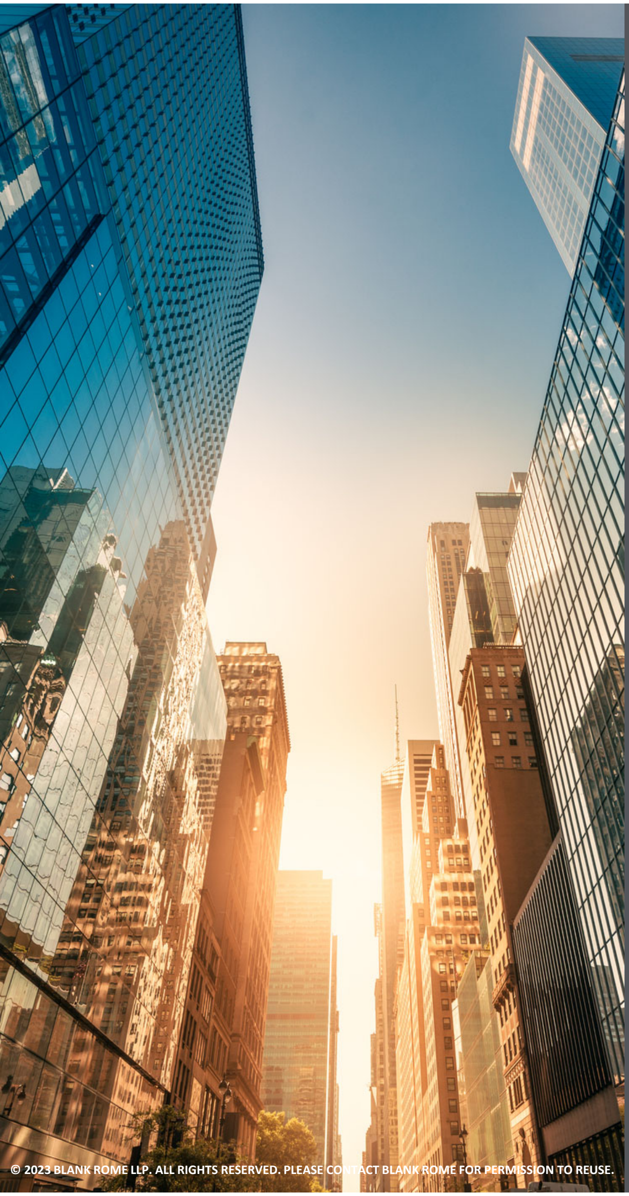


ACC

BLANKROME

NAVIGATING DISTRESSED LOANS:

STRATEGIC INSIGHT FOR BORROWERS AND LENDERS

October 28, 2025

INTRODUCTION

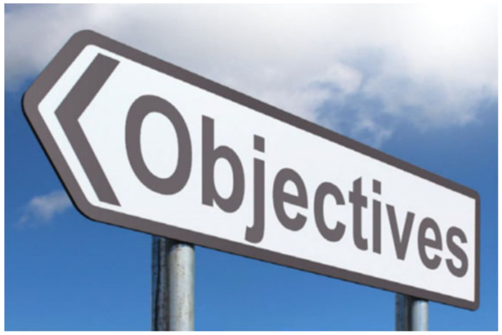
- Co-Chair of Blank Rome's Finance, Restructuring, and Bankruptcy Practice Group
- Blank Rome is an Am Law 100 firm with 16 offices and more than 750 attorneys and principals who provide a full range of legal and advocacy services to clients operating in the United States and around the world.
- Blank Rome's 90+ attorney Finance Practice represents clients through the U.S., predominantly serviced from Los Angeles, New York, Philadelphia, Chicago, Boston, Dallas, Houston, Washington D.C. and Wilmington, DE.
- The Finance team is consistently ranked top-tier by Chambers USA an US News – Best Lawyers
- Blank Rome attorneys lead transactions across many industries, including: Automotive, Cannabis, Construction, Energy, Entertainment and media, Financial services, Healthcare, Information technology, Manufacturing, Real estate, Retail, Software, Telecommunications, Timber, and Waste treatment.
- Our attorneys have significant depth of talent in financial services legal matters and experience in representing senior and subordinate lenders, including mezzanine and second lien, ABL, cash flow and syndicated lenders, as well as factors.
- While we handle billion-dollar-plus deals, our primary focus lies in the middle and upper-middle market. This segment, which we consider the most vital part of the market, encompasses transactions typically ranging from $50 million to $500 million. Our expertise in this area is recognized by key clients, including all of the major banks.
- Advised on over 300 credit facilities last year with commitments in excess of $20 billion.

KEVIN O'MALLEY
Blank Rome

BLANKROME

COURSE OBJECTIVES

- Understanding Early Warning Signs of a Distressed Loan
- Obligations of the Company / Borrower to its Lenders and other Creditors
- Officer and Director Considerations and Concerns
- Timeline / Process of Workout (Notices of Default, Forbearance Agreements, Restructurings) and Strategies of Lenders
- Understanding Roles of Advisors (Independent Directors, Chief Restructuring Officer, Investment Bankers)
- Understanding Bankruptcy and other Out of Court Restructurings
- What is Lender Liability?



BLANKROME

SOME QUICK FACTS ABOUT DISTRESSED LOANS

- Harlan Platt of Northeastern University conducted a study of companies experiencing various degrees of distress.
- It takes 6 to 10 months to turnaround a company where there are several unresolved issues which if left unchecked could lead to a crisis. This would be a loan with a criticized risk rating (or increased risk of default).
- It takes 27+ months to turnaround a company in crisis. This would be a loan with a nonaccrual risk rating (90 days past due, in default or unlikely to be repaid in full).
- 93% of companies with a criticized risk rating survived the turnaround process.
- 63% of companies that were rated nonaccrual or worse survived the turnaround process.
- 70% of the companies experiencing problems had no cashflow forecast.
- 72% could not deliver timely and accurate accounting and financial data.
- Poor management was the most prevalent cause of deterioration.

BLANKROME

EARLY RED FLAGS FROM A LENDER’S PERSPECTIVE

- Slowing A/R or A/P vs. historical vs. industry averages (shrinking liquidity)
- Stretching Payables
- Vendor Pressure and/or Loss of Key Customer or Supplier Relationship
- Financial / Insolvency issues of a material customer or supplier
- Delayed and/or Inaccurate Reporting
- Projection Variances
- Inability to provide a cash forecast
- Financial Covenant Defaults

BLANKROME

TIMELINE / PROCESS OF A WORKOUT OR DISTRESSED LOAN

- Do Borrowers have an obligation to report a default or potential default to their Lender? Review reporting and affirmative covenant provisions of your credit facility.
- Are all defaults the same?
- Is there an obligation to report an impending financial covenant default?
- Notices of Default / Reservation of Rights from Lender
  - Default Rate Interest
  - An Event of Default will permit the Lender to not lend (does the lender have cash dominion?)
  - The Lender may continue to lend but implement a cap or other reserves, or try to unilaterally impose additional restrictions or conditions.
  - Alternatively, if the default is not materaial, the notice may just be to paper the file.

BLANKROME

TIMELINE / PROCESS OF A WORKOUT OR DISTRESSED LOAN

- Lender may require additional reporting.
  - 13 Week Cash Flow
  - Variance Reports
- Commence discussions on a Default Waiver
  - Is the Company projected to be back in compliance in the next quarter?
  - Reset Financial Covenants, Impose new Financial Covenants and Waive Defaults or enter into a Forbearance Agreement
  - Amendment / Forbearance / Waiver Fees

BLANKROME

FORBEARANCE AGREEMENTS

- A Forbearance is not a waiver of the existing defaults.
  - The Lender agrees to forbear from exercising remedies for a specified period of time so long as the Borrower is in compliance with the forbearance agreement.
- The Lender may impose additional covenants
  - Liquidity or Availability.
  - Cash Receipts / Disbursements vs Projections
  - Lender may require the company to engage a Financial Advisor, CRO, Independent Directors or an Investment Banker to refinance the debt and/or sell the business. Generally the Lender will set milestones that must be complied with in order for the forbearance to remain in effect.
- Lender may require additional collateral or credit support
  - Additional debt or equity issuances if available
  - Personal Guarantees
  - Additional Collateral
- Lender may require sales of underperforming divisions or business lines; Cost cutting measures such as reducing workforce. Any dividends andother leakage of cash or assets from the Borrower will be restricted.

BLANKROME

FINANCIAL ADVISORS, CHIEF RESTRUCTURING OFFICERS AND INVESTMENT BANKERS

- What right does the Lender have to impose engagement of ID's IB or CRO?
  - A Lender will often require the engagement of various Financial Advisors as a condition to the Forbearance Agreement.
- In most instances a lender will not direct the company who to engage, but will provide a list of 3-5 advisors who are acceptable. This is due to Lender Liability concerns.
- Independent Director – A lender may require one independent director who's affirmative vote must be obtained for certain transactions or they may require that the board consist of a majority of independent directors, or a committee of independent directors be appointed. The ID is someone who does not have a material relationship with the company and is neither part of its executive team nor involved in day to day operations.
- Investment Banker – a lender may require the company to engage an Investment Banker to refinance their debt or to find a buyer for the company (which may include a buyer in an Article 9 Sale conducted by the Lender)
- Chief Restructuring Officer – Appointed by the Board with decision making authority. A CRO will be involved in the day to day operations and may: layoff workers, negotiate leases and vendor / customer contracts, certify the projections to Lender, request borrowings, assist the investment banker in the refinancing or sale process; and generally take any action to streamline business processes, cut costs and implement measures to improve productivity and efficiency.   Note that CRO's have the same fiduciary duties as other officers so they will be more than likely working with and cooperating with the Lender.

BLANKROME

LENDERS' NON-BANKRUPTCY OPTIONS

Company Liquidation

Work cooperatively with the company for a company-side liquidation of assets and wind down of the company

Balance Sheet Restructuring

De-lever the balance sheet by converting debt into equity. Sometimes can do this without bankruptcy; other times through a plan.

Third Party Advisers

Engage a CRO, consultant, investment banker, appraiser, liquidator and/or other third-party adviser.

Forbearance

Amend, Extend and/or Waive and/or Seek Additional Credit Support

BLANKROME

LENDERS' NON-BANKRUPTCY OPTIONS

Receivership

Used most frequently in real estate and healthcare cases—can be an effective tool and less expensive than bankruptcy.

ABC

Assignment for the Benefit of a Creditor is a state law tool to appoint an assignee who will wind down and sell assets.

Note Sale

The note may be sold at par or at a discount.

Article 9 Sale / Foreclosure

Sell assets through Art. 9 sale. Art. 9 deals with personal property (inventory, equipment, etc.). Real estate & leases are addressed separately.

BLANKROME

Bankruptcy Options

- Bankruptcy may be beneficial for, among other things:
  - Unlocking value that cannot be unlocked outside of bankruptcy (leasehold interests, valuable contracts, etc.…)
  - Sale of assets under Section 363; Assets can be sold free and clear of all liens and other interests, including judgments, environmental liabilities, etc.…. (An Article 9 Sale does not give the Buyer a court order insulating them from such claims so some buyers may prefer a 363 sale).
  - The sheer size of liquidation requires a centralized forum
  - Automatic Stay – Any enforcement actions must cease (e.g., a lender exercising secured creditor rights, litigation stay, entry or enforcement of a judgment or tax lien)
- If bankruptcy is an option, it is far better to coordinate the filing with the Lender.
- Other Benefits – structured forum for negotiating, litigation and resolving disputes;
- Drawbacks – time consuming, expensive

BLANKROME

Financing in Bankruptcy

- DIP Financing
  - New financing provided to the Debtor (Borrower) after filing of the bankruptcy case. Can be provided by existing lenders or new lenders.
  - DIP Financing is provided "super-priority" status and takes priority over all other pre-bankruptcy debt, including secured debt. It can also secured by a priming lien, however a priming lien is only granted if the existing lender is either adequately protected or consents in writing.
  - The existing Lender will most likely want to provide the DIP Financing to protect their lien on the pre-petition debt and to maintain control over the case and budget.
  - Roll Up – All pre-petition debt is paid in full upon approval of the DIP Financing (essentially gives the prepetition debt super priority status)
  - Creeping Roll UP – pre-petition debt is paid off as collections on receivables and other revenue is received post bankruptcy filing.
- Use of Cash Collateral
  - Company can use cash proceeds of A/R and Inventory to finance operations and the bankruptcy case.

BLANKROME

D&O CONSIDERATIONS FOR DISTRESSED COMPANIES – WARN ACT

- Federal WARN Act
  - Enacted in 1988 requires, subject to certain limited exceptions, most "employers" to provide 60 days advance notice of any "plant closing" or "mass layoff" (or failing that, to pay its affected employees for up to 60 days of back pay and benefits)
  - Who Must Give Notice – all businesses employees 100 or more employees (excluding "part time" employees)
  - Triggers for Notice – Either a "plant closing or "Mass Layoff"
  - Plant Closing = permanent or temporary shut down of a site of employment resulting in "employment loss" during any 30 day period for 50 or more full time employees.

BLANKROME

D&O CONSIDERATIONS FOR DISTRESSED COMPANIES– WARN ACT

- Federal WARN Act
  - Mass Layoff = Reduction in workforce (other than a Plant Closing) result in employment loss for either:
    - At a single site of employment at least (A) 33% of the full time employees or (B) 50 full time employees; or
    - At least 500 full time employees
  - Who Must Receive Notice
    - 60 days advance notice must go to (i) the affected employees' union representative (or if none, to each affected employee), (ii) the state disclosed worker unit, and (iii) the chief elected official of the relevant local government.
  - Exceptions
    - Notice would Preclude Needed Capital or Business
    - Natural Disaster
    - Business Circumstances Not Reasonably Foreseeable

BLANKROME

D&O CONSIDERATIONS FOR DISTRESSED COMPANIES– WARN ACT

- Liabilities for Failure to Comply; Employers who fail to comply are liable to each aggrieved employee for:
  - Up to 60 days of back pay and up to 60 days of benefits
- Note that while there is no direct personal liability for directors and officers under the WARN Act, Directors and Officers can be sued for breaching their fiduciary duty to the Company by causing it to violate the act.
- <u>California WARN Act</u>
  - California Act applies to “covered establishments” that employ or have employed in the prior 12 months, 75 or more full and part time employees (note Federal Warn only applies if over 100 full time employees)
  - Applies to any Plant closure affecting any amount of employees or a Layoff of 50 or more employees w/in a 30 day period regardless of % of workforce.

BLANKROME

D&O CONSIDERATIONS FOR DISTRESSED COMPANIES - FIDUCIARY DUTIES

- Under Applicable State Law, officers, managers and directors have duties of loyalty and duties of care to their shareholders
- Solvent Companies – Officers and Directors owe fiduciary duties to the Company with the members or shareholder being the residual stakeholders.
- Zone of Insolvency- Officers and Directors continue to owe a fiduciary duty to the company but the residual stakeholders can be in state of flux.
- Insolvent Companies – Creditors of the Company become the residual stakeholders, Creditors are permitted to bring derivative suits on behalf of the company, but not direct causes of action.
  - If the Company is in the Zone of Insolvency or Insolvency, Officers and Directors should realize they are running the company for the benefit of their Lender and other creditors.

BLANKROME

Alternatives for Company In Zone of Insolvency

Out of Court Restructuring Alternatives

I. **Out of Court Financing and Restructuring**
   - Replacement RLOC
   - Term Debt
   - Minority Equity Financing

II. **Out of Court Turnaround Plan**
   - CRO Appointment

III. **Sale of Business as Going Concern**
   - If unsuccessful, can pivot to bankruptcy and will likely shorten process

IV. **Out of Court Liquidation**
   - Article 9 Sale

In Court Alternatives

I. **Chapter 11 Reorganization**
   - Overview of Costs of a Bankruptcy and Process

II. **Chapter 11 Sale**
   - Marketing of all or part as going concern
   - Orderly liquidation of assets not sold as going concern

III. **Chapter 7 Liquidation**

BLANKROME

LENDER LIABILITY – WHAT IS IT?

- Liability of alender for its actions or inactions or mistreatment of borrowers. The legal claims are generally claims arising from a breach of the covenant of good faith and fair dealing.
- CONTROL over the borrower is the most common issue.
  - High degree of control can give rise to fiduciary duties.
  - Lower degree of control may give rise to tortious interference claims.
- Most common lawsuits relate to causes of action:
  - directly by the borrower against the lender, *i.e.,* contract breaches, fraud, tortious interference, misrepresentation
  - that seek to impose afiduciary duty on the lender in favor of other stakeholders of the borrower (*e.g.*, other creditors).
- Often based on alleged promises or failure to act.
  - You "promised" to extend the maturity date.
  - You "promised" to amend the loan agreement.
  - You "promised" not to foreclose.
  - You didn't lend money to pay payroll or fund these inventory purchases.

BLANKROME

Lender Liability-What Is It?

- Avoid the following tempting terms:
  - Having officers, directors, employees or agents of the lender serve as directors, officers or managers of the borrower
  - Determining who serves as an officer or director of the borrower
  - Having lender employees on borrower's payroll
- Do not engage in day-to-day business decisions of the borrower.
  - Do not exercise influence over salaries of your borrower's employees
  - Do not instruct your borrower which vendors to pay.
  - Do not insist on hiring a particular person for any position.
  - Do not insist on particular directors being placed on the board.
  - Do not draft the borrower's legal or business documents, *e.g.*, leases, customer contracts, governing documents.
  - Resist the urge to substitute your business judgment for that of the borrower’s (courts defer to borrower’s business judgment, not your judgment).

BLANKROME