International Journal of Economics, Commerce and Management
United Kingdom ISSN 2348 0386 Vol. VIII, Issue 6, June 2020

http://ijecm.co.uk/

INTERNATIONAL PRACTICE, CREATION AND FEATURES OF A SYNDICATED LOAN

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A syndicated loan: unites interregional banks!

Abstract

The article, studying international practice, explores the concept and legal basis of a syndicated loan agreement, the general structure of legal relations, legal relations between lenders and borrowers, mutual decision-making between lenders, the rights and obligations of an agent bank, the regulation of interest on loans and others payments (fees), as well as the general terms of the syndicated loan agreement. This article is devoted to the disclosure of the issue of syndicated lending, namely, the concept, value and application of this banking product in practice are presented, the positive aspects of the syndicated loan are analyzed and identified, the problems are also investigated, and further prospects for the development of this sphere are considered. The problems of the syndicated loan market are identified. The directions of solving the problems of the syndication market are proposed.

Keywords: Syndicated loan, syndicate, agreement, borrower, creditors, agent-bank, global market, credit activity

INTRODUCTION

A syndicated loan is one of the widespread and effective methods of raising capital from the global financial market. In international banking practice, a syndicated loan is a loan issued by two or more lenders (banks, investment organizations, financial institutions and corporations) under the terms of a single document.

The peculiar features of a syndicated loan are the provision of a large amount of funds to a borrower through several sources, diversification of credit risks, and the participation of several lenders in the lending process.

The value of a syndicated loan increased many times by the middle of the 19th century, when large-scale financing of infrastructure and production was required. Large loans were provided for the construction of railways, port facilities, communications, which was associated with the expansion of domestic markets and international trade[1].

According to available statistics, today, on an international scale, syndicated loans are one of the widespread sources for attracting financial resources in the energy sector, telecommunications, oil and gas industry, construction, healthcare, transport infrastructure and the financial sector, as well as for financing them.

In international practice, the process of a syndicated loan organizing is carried out in 3 (three) stages (*refer fig 1*).

1. The syndication process implementation: development of a borrower financing structure, analysis of its activities; acceptance of a mandate letter for financing a borrower on the basis of a syndicated loan.

The mandate letter shall determine the legal relationship between the arranger of the syndicated loan to start the syndication process, the borrower and other participants providing a pledge or guarantee as loan security (by the state or companies with high rating indicators).

The mandate letter shall govern the appointment of the arranger and its functions, inviting participants to the syndication process, privacy rules, conflict of interest and other similar issues.

2. Syndication: after adoption of the mandate letter, the managing bank shall select the banks participating in the syndicated loan, and coordinate the loan allocation processes with them, prepare and approve the information memorandum, ensure the signing of the loan agreement by the borrower and participating banks. This stage shall finish with the signing of a syndicated loan agreement between syndicate participants.

3. After signing the syndicated loan agreement, the "life" of the syndicated loan shall start, that is, the implementation process for financing it.

[1] Fedyakina L.N. International Finance. M .: Peter, 2005, p. 19.

Figure 1 Stages of a syndicated loan

Stage I. Development of the initial stage of a syndicated loan and its financing scheme	***Deadline:*** 7 to 12 days ***Main objective:*** - development of a financing structure; - preparation of financing conditions; - coordination of financing conditions with the borrower.	***Completion of the initial stage*** Coordination of financing conditions with the borrower. Acceptance of the mandate letter.

Stage II. The most important stage in developing a syndicated loan financing scheme	***Deadline:*** 45 to 55 days ***Main objective:*** - analysis of the borrower's activities; - preparation of an information memorandum; - obtaining consent of the credit committee; - selection of banks participating in a syndicated loan; - coordination of the terms of financing with the borrower; - approval of participating banks; - approval of the information memorandum; - preparation of loan documents; - coordination of loan documents with the borrower; - creation of an accurate list of participants; - coordination of loan documents with participating banks; - preparation of loan documents for signing; - signing of loan documents.	***Completion of the second stage*** Creating an accurate list of participants. Signing of loan documents.

Stage III. The last stage in developing a syndicated loan financing scheme	***Deadline:*** up to 5 days ***Main objective:*** - starting the implementation of the loan agreement terms and conditions; - withdrawal of the Loan amount (financing process); - credit management and monitoring; - utilization by participating banks of their share or refusal of it (secondary market).	***Completion of the third stage*** Start fulfillment of terms and conditions of syndicated lending stages. Development and implementation of the latest syndicated loan financing scheme.

At the first stage of preparing a syndicated agreement, the basic conditions for financing projects shall be developed in a coordinated manner. This process is often carried out during the selection of creditors by the managing bank on the basis of a tender, according to the best financing conditions presented by them. In the developed Western market, after signing an agreement on the arrangement of financing that defines the main parameters of the agreements concluded (after acceptance of the mandate letter), very rarely changes shall be made to the conditions for raising funds to the borrower.

Stages of Syndicated Loan Agreements Creation in International Practice

The first syndicated loan agreement, based on English law, was developed in 1968, jointly by the law firms Hugh Pigott and Korkak Chance. At that time the Standard Bank acted as the borrower, and the Mitsui Trust acted as the agent bank. The volume of this first contract did not exceed 20 pages[2].

In the next few years, the number of contract forms was increased markedly. In 1979, the first attempt was made to standardize syndicated loan agreements. Martin Hughes Law firm has developed a universal syndicated loan agreement for Citibank. This agreement was widely used in the development of a unified policy of credit agreements in the international market[3].

In 1995 in New York, the American Association of Syndicated Loans (Loan Syndications and Trading Association, LSTA) was formed in a non-state form. Its main objectives were to protect market interests and increase investor confidence. According to the first Executive Director of the Allison Teylor Association, the idea of creating an LSTA was put forward by traders operating in the secondary syndicated loan market. The mission and scope of LSTA have been gradually expanded; it became the leader of the entire loan market and at the same time turned into an organization that defines the standards of the first syndicated loan agreements[4].

In the ten years since the establishment of LSTA, the number of syndicated loans in the United States has tripled, and the number of agreements in the secondary market - five times. During the same period, LSTA developed more than 50 standards, documents for consultation and market recommendations. Currently, LSTA has over 450 members, including commercial

[2] Ivanov O.M, History of Syndicated Credit Regulation. Bulletin of the University named after O.E. Kutafuna (MSLU), 2018. No. 10.
[3] Hughes M. Legal Principles in Banking and Structured Finance. Sec. ed. Tottel, 2006. P. 9.
[4] The Handbook of Loan Syndications and trading, ed. A. Taylor, A. Sansone. McGraw-Hill, 2007. Kindle edition. Line 1116.

and investment banks, investment funds, asset management (hedging) funds, troubled asset funds, insurance companies, law firms, audit organizations and other participants[5].

At such stages of development, on the initiative of leading international banks, the Loan Market Association (LMA) was formed, located in London. The main objective of the LMA was to develop a secondary syndicated loan market in Europe, and it brought standardized documents in line with English law.

For more than 20 years, LMA has developed many standards, guidelines and recommendations. They were classified by the characteristics of the syndicated loan market (primary and secondary) and by type of loan. In 1997, LMA developed Secondary Trading Documents recommended forms of documents for secondary market. After another two years, six contracts were prepared that were recommended for the primary market. They differed in the number of currencies used in the lending process (single or multicurrency), as well as in the types of loans (term loan or revolving credit line).

Later, LMA developed loan agreements for specialized loans: for the acquisition of real estate and pre-export financing. Taking into account the wishes of the participants, LMA also worked on the preparation of national documents that are consistent with the practice of drawing up international agreements. In 2002, standard syndicated loan agreements (investment grade) were developed, brought into line with French law, in 2007 - brought into line with German law and in 2013 - with Spanish legislation. Currently, the total number of LMA members exceeds 500, most of them are banks and international law firms.

In the history of interregional credit associations, the following associations were established: in 1998 - in Asia - the Asia Pacific Loan Market Association (APLMA)[6], and in 2001 - the Japan Syndication and Loan-trading Association[7].

Associations operate with constant cooperation, coordinating their initiatives. The common membership base helps in this activity. In 2005, LSTA and LMA jointly developed a common Users Guide for Distressed Trading Documents, as well as a single Glossary of Terms. The similarity of documents, the use of terms with the same meaning in their development shall eliminate the contradictions and disagreements encountered in international markets.

Contractual Relations Structure in a Syndicated Loan Agreement

The main place in drawing up a syndicated loan agreement is a direct syndicated loan agreement; this shall determine the necessary conditions and legal basis of the agreement, the

[5] URL: www.lsta.org.
[6] URL: www.aplma.com.
[7] URL: www.jsla.org.

rights and obligations of the parties involved. The standard form of documents reduces the cost of transactions and prevents a misunderstanding of the terms of the contract.

Among the most difficult issues in the regulation of syndicated loans, special attention is paid to the following aspects: the legal basis of the syndicated loan agreement, the general structure of legal relations, the independence of legal relations between lenders and the borrower, the inter-loan agreement and the principles of collective decision-making between lenders, the rights and powers of the syndicate agent, accrual of interest on loans and bank payments (fees), as well as the procedure for its payment, classification of events of default of the borrower to fulfill obligations, the basis for early repayment of the loan, guarantee and security, obligations of the parties, conditions for granting a loan and refusing it (secondary market).

Unlike traditional bilateral loan agreements aimed at establishing of the credit relations between the lender and the borrower, the syndicated loan agreement is characterized by the participation of the several persons whose functions are clearly defined. From this point of view, the legal structure of the syndicated loan agreement should be separately analyzed.

The variety of legal relations regulated under the syndicated loan agreement means that there are a lot of parties involved in it. These parties are usually:

1) borrower;

2) guarantors;

3) lenders (banks, investment organizations, financial institutions and corporations);

4) facility agent (and the managing bank).

Legal relations regulated by a syndicated loan agreement are divided into at least three groups. ***The first group*** is legal credit relations between the borrower and the syndicate lenders. ***The second*** is the relationship between the lenders participating in the syndicate associated with determining the procedure for exercising the rights of lenders according to the borrower’s requirements, with the distribution between lenders of funds received from the borrower (accrued interest on the loan and the principal amount of the loan), with collective decisions, as well as other aspects of mutual cooperation. ***The third*** is agent relations that perform technical and administrative tasks between syndicate members and a special person appointed by them (agent bank)[8].

Lenders are independent in fulfilling obligations to provide loan amounts and are not responsible for the actions of other lenders involved in the syndicate. This is one of the basic rules that apply to all relationship structures within the framework of a syndicated loan.

[8] Mikhailov A.E Improving the pre-mandate stage in the organization of syndicated lending // Finance and Credit. 2013. Oct. No. 38 (566). B. 16–26.

Typically, lenders participating in a syndicate participate in granting a loan on general terms, but their participation in equal shares is not mandatory. In order to ensure effective participation of all syndicate participants, methods such as assuming bank obligations at various levels and distributing their role in participation are widespread in practice. In this regard, the share of each syndicate lender in the total loan amount should be established in the syndicated loan agreement.

As a rule, decisions on critical issues are taken by a majority vote. To take appropriate decisions of the syndicate, the consent of creditors must be obtained, providing at least 2/3 of the total amount of the syndicated loan (66.6 percent of the allocated loan amount).

The participation of several banks as a lender leads to difficulties for the borrower to enter into a dialogue separately with each bank. Also, lenders experience inconvenience in directly contacting the borrower.

In this regard, one of the mandatory features of syndicated lending is the need to appoint a single representative to protect the legal interests of all lenders and ensure relations between them ("bank-agent" under a syndicated loan agreement, as a technical intermediary between lenders and the borrower, usually the managing bank organizing syndicated loan, also serves as an agency).

The agent bank shall carry out its activities within the framework of the authority given to it by credit documents. Agency relations under a syndicated loan agreement shall be carried out mainly by the managing bank creating the syndicate.

It should be noted that large banks with many years of experience and business authority usually act as the managing bank of the syndicated loan - an agent.

As a rule, the managing bank is considered responsible for the process of preparing for the conclusion of a syndicated loan agreement. It is negotiating with the borrower regarding the terms of the contract. The function of the managing bank as an agent is advisory, and it does not take responsibility for the allocation of a loan under a syndicated loan agreement. Along with this, the managing bank can optionally participate in the syndicate and as a lender[9].

One of the main objectives of the agent bank is to study problems in the syndicate and manage some issues. It is the agent bank that accepts the amounts of the syndicated loan and transfers them to the borrower, and also distributes the funds received from the borrower between the creditors - participants of the syndicate.

[9] Sorokina I.O. Features of the contract support for syndicated lending transactions // Bank lending. 2011. No. 2. [Electronic resource]. URL: http://base.consultant.ru/cons/cgi/online.cgi?req=doc;base=BI; n = 163251.

The agent bank also performs the function of transmitting information, in particular, it is a representative of the syndicate for taking information from the borrower, it also sends the lenders financial and other information on the loan agreement received from the borrower.

The Concept of a Syndicated Loan Agreement and its Legal Basis

A syndicated loan agreement is considered a single multilateral agreement between all participants, and also defines the main aspects of the loan process for the implementation of a syndicated loan in the secondary market. The possibility in syndicated loan agreements of selling their share to third parties in the secondary market is important for lenders. So, the following cases lead to the need for syndicate lenders to participate in the secondary market:

- in the event of a shortage of funds in the bank in order to urgently sell part of the loan;
- for the sale of part of the loan in violation of the requirements governing the activities of the bank, and requirements for the required reserve;
- attract even more efficient assets to the bank.

In the scientific literature, the legal basis structure of a syndicated loan agreement remains as a controversial issue. Many scholars call such contracts as mixed contracts. Some researchers believe that a syndicated loan agreement consists of a loan agreement and a syndicate (and agency) agreement. And others came to the conclusion that the agreement combines the elements of a loan agreement and an agreement on joint activities.

In general, a syndicated loan agreement is a type of loan agreement and is based on the same principles as a regular loan agreement. Only here the sources of funds and the mechanism for their provision are changing, and the procedure for mutual relations between the parties is becoming more complicated.

This feature arises from the above analysis of the contractual relationship system in a syndicated loan agreement. This agreement is not only an agreement determining credit relations, security (guarantee or pledge) of an agreement between a borrower and and managing bank (agent) and lenders. Along with this, it is also an agreement defining the unification of the rights and obligations of numerous parties in one document.

Such agreements must indicate the amount of the loan provided by the syndicate's lenders, the rights and obligations of the syndicate participants, as well as the form of participation of the lenders and the bank managing the syndicate.

General Terms of the Syndicated Loan Agreement

The terms of a syndicated loan agreement can be divided into three main groups: provisions governing relations between the borrower and the lenders; provisions governing key issues between syndicate members; provisions governing relations between the managing bank (and the agent) and other syndicate participants.

The main terms and conditions of any loan agreement are: loan amount, its purpose, loan term, interest rate and interest-free payments paid by the borrower, terms and methods of loan repayment.

The interest rate under a syndicated loan agreement conventionally consists of three elements. These include: the base average rate of raising funds from the interbank market (***LIBOR / EURIBOR***); the cost of bank services - arranger of the syndicate (***margin***); other mandatory costs of the borrower (***mandatory cost)***.

According to the agreement, the borrower, along with interest, pays other one-time payments (for example, for committing to issue a loan - ***commitment fee***, remuneration for arranging loans - ***arrangement fee***, payment to agency - ***agent fee***, remuneration for security management - ***security agent fee***, etc.)

Thus, the total cost of a syndicated loan includes four elements: interest and interest-free payments, payments of expenses incurred under the contract, payments for additional services under the contract.

A number of provisions of the syndicated loan agreement are based on mechanisms developed on the basis of international experience. This provides sufficient protection for the rights and interests of the parties to the contract.

A general analysis of the principles of a syndicated loan agreement shows that the participation of banks in the international financial market, as well as the intermediary relations between banks and the borrower, are clearly defined.

The standard, as an addition to the syndicated LMA agreement, is based on the distribution of the risks associated with the creditworthiness of the recipient between the creditors (participating banks). And this gives the parties the opportunity to take a more optimal approach when agreeing on the rules of the loan agreement and in this way reduces the cost of financing a syndicated loan agreement.

Based on international experience, the development of syndicated loan documents enhances banks' trust in each other, allows small banks to enter the international financial market, and creates the basis for the development of the secondary market. It also gives participating banks the opportunity to reduce the risks associated with lending, prevent a shortage of funds, comply with regulatory requirements of regulatory authorities and participate in new agreements. In turn, this leads to increased competition in the market and lower interest rates on loans. Syndicated loans contribute to the growth of the real sector in the country's economy, and also have a positive impact on innovative development.

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