Interest Rate Hedging Agreements Linked to Credit Agreements

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We often see banks requiring their borrowers to enter into interest rate hedge agreements in conjunction with their credit agreements. There are a number of reasons why borrowers should take care to ensure that they have the related ISDA Agreements and Schedules considered by experienced counsel. Here are just two of those reasons.

Linkage to the Credit Agreement

ISDA Agreements often include the termination of the Credit Agreement as either an Additional Termination Event or an Event of Default. The result of such an inclusion is that if the Credit Agreement is repaid early (whether upon a sale of the company or otherwise) then the borrower will be responsible for any out of the money payments that are owing at the time of the repayment. These out of the money payments could be significant and borrowers will need to become sufficiently versed in the nature of the ISDA Agreements and the related financial repercussions at the outset of the transaction to avoid surprises down the road.

Assignment by the Lender

For secured hedges, lenders will often include an Additional Termination Event should the lender assign its loan. That opens up the possibility that a lender would have the power to essentially unilaterally cause the termination of an ISDA Agreement by assigning its loan to a third party. If that termination occurs at a point when the borrower is in an out of the money position then it could be a very costly assignment to the borrower. One way to address this issue is to provide in the terms of the Credit Agreement a restriction on the lender's ability to assign its loan (or its portion thereof for syndicated deals) where the result of such an assignment would be to permit the lender to terminate the related ISDA Agreement.