ALERT MEMORANDUM

New York Law Covenants in English Law Leveraged Facility Agreement

January 21, 2026

I. Executive Summary

In our last article on *Cross-Border Acquisition Financing – Navigating "SunGard" Conditionality and Certain Funds Requirements*, we examined the key similarities and distinctions between US "SunGard" conditionality practices and European "Certain Funds" requirements for acquisition financings, providing practical guidance for structuring competitive bids and managing closing processes in cross-border transactions.

It is common in English law governed leveraged facility agreements, in particular those in private equity backed financing structures, to have New York law interpreted incurrence covenants. This hybrid approach has become market practice largely due to the influence of private equity sponsors who prefer the flexibility and familiarity of US-style incurrence covenants. This hybrid approach has become the standard for Term Loan B facilities in the broadly syndicated market and is becoming increasingly common on direct lending deals. However, this creates potential interpretative challenges and compliance risks that require careful consideration. This article examines how certain covenants might potentially be interpreted differently under English law and New York law, which will have implications on English or non-American borrowers and their subsidiaries. Similar considerations apply when UK or EU companies issue high yield bonds governed by New York law.

II. Potential differences in English and New York law and practices

Courts may interpret the same term differently under New York law versus English law. Set out below a few examples:

- **Good faith**: Traditionally, English courts are generally reluctant to "read in" general duties of good faith, unless statutorily required or in specific context such as certain "relational" contracts involving long term relationship, substantial commitment and performance based on mutual

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trust and confidence with expectation of loyalty (which in practice, would only apply to a very small portion of commercial contracts as discussed in *Bates vs Post Office*[1]). New York law, however, imposes an implied covenant of good faith and fair dealing in every contract, including facility agreements, though such implied covenant cannot run against express terms of the contracts. This implied covenant could allow a New York court to find a breach based on bad faith conduct even if not expressly prohibited by a facility agreement where an English court would not (e.g. an English court might be more likely to enforce a "bad bargain" based on the contract alone than a New York court). This also has implications on bid documentation subject to SunGard or Certain Fund requirements, as there is a requirement to negotiate long form documentation in good faith in the US.

— **Ordinary course of business/trading**: Covenants in facility agreements often include permissions where certain actions are taken in the "ordinary course of business" or "ordinary course of trading". When interpreting the meaning of what constitutes ordinary course of business or trading, both English and New York courts focus on the facts, whilst New York courts may give stronger consideration to industry custom beyond the specific entity or business in particular during bankruptcy proceedings. Courts in both jurisdictions also consider whether the action would have been ordinary at the time the agreement was entered into versus at the time of the action, as well as whether the size or scale of the transaction is consistent with past practice. The typical view under English law is that "ordinary course of trading" is narrower in meaning, focusing on day-to-day revenue generating operations, while "ordinary course of business" may be broader and include ancillary functions. As such, borrowers in the UK would usually prefer "ordinary course of business" in covenant permissions. In New York, "ordinary course of trading" is not a standard, defined legal term so does not typically carry distinct meaning as compared to "ordinary course of business", and in any case both phrases are highly context specific and can vary across businesses.

— **Material adverse effect (MAE)**: The phrase "material adverse effect" is usually used as a materiality qualifier to covenants, and can also be a standalone event of default in some English law or European facility agreements. The general view is that both English law and New York law set a high bar for what constitutes MAE. The key difference may be less about the height of the bar and more about the methodology—English courts often focus on contractual construction whilst US courts may consider broader commercial context and circumstances.

— "**all or substantially all**": Facility agreements often have provisions that are triggered upon the disposition, transfer or release of "all or substantially all" assets or business. There is no bright line test under either English law or New York law for what threshold constitutes "substantially all" in the context of leveraged finance. English courts will seek to assess the natural and ordinary meaning of the relevant provision, the overall purpose of the provision and the agreement, the facts and circumstances at the time the agreement was entered into and commercial common sense, identifying objective instead of subjective intentions of the parties. Courts applying New York law consider multiple factors, both quantitative and qualitative. In some cases, a transfer of assets may be so quantitatively insignificant that an inquiry into the qualitative nature of the transfer is unwarranted. In other cases, a transfer that may seem moderate when judged quantitatively may still affect all or substantially all of a

[1] [2019] EWHC 606 (QB) at para 725.

corporation's assets because of its qualitative impact on the corporation. Furthermore, there are only a handful of cases under US law that provide guidance as to quantitative measures, and practitioners are cautioned against assuming any plain meaning to the phrase.

— **Best endeavours and reasonable endeavours**: Under English law these phrases, which are often found in undertakings in facility agreements, carry distinct meanings. "Best endeavours" requires a party to take all steps a reasonable, determined person would take, which may require some financial and/or commercial sacrifice but not unlimited expense; "reasonable endeavours" is less onerous. A third category, "all reasonable endeavours", sits between "best" and "reasonable" endeavours. Under New York law these terms are considered less hardwired—there is a tendency to interpret both similarly in many contexts.

III. Tailor-making required for English obligors

When undertakings and events of default are to be interpreted in accordance with New York law, consider if any tweaks will be required for English or non-American borrowers or guarantors, for example:

— **Insolvency-related representations, undertakings and events of default**: Instead of referring to the US Bankruptcy Code (in Chapter 11), it would be best to tailor to relevant English law insolvency concepts to make sure appropriate insolvency or insolvency proceedings are captured, for example moratoria, administration, the appointment of administrative receivers, schemes of arrangement (other than solvent ones), company voluntary arrangements (CVAs) and restructuring plans under Part 26A of the Companies Act 2006. The representation on "centre of main interests" (COMI) is often added to inform where an English or European court can open insolvency proceedings in respect of an entity, which is particularly important post-Brexit for determining which insolvency regime applies.

— **Applicable laws**: Beware that despite covenants or undertakings being interpreted under New York law, an English obligor is subject to laws and regulations applicable to it in the UK, for example, tax rules imposed by HMRC, sanctions (which may diverge from EU sanctions post-Brexit), anti-bribery and anti-money laundering regimes imposed by the Office of Financial Sanctions Implementation and His Majesty's Treasury, and the UK's financial services regulatory regime (FCA/PRA requirements) which may impose obligations on UK borrowers that wouldn't apply to US borrowers.

— **Pensions**: Instead of the Employee Retirement Income Security Act (ERISA), we look at employer liability under the Pensions Act in the UK, and in particular if there is a defined benefit scheme in place and whether there is any deficit in the relevant scheme. Key considerations include contribution notices and financial support directions, which are enforcement mechanisms by the Pensions Regulator that can be triggered by corporate transactions, as well as the Pensions Regulator's expanded moral hazard powers under the Pensions Act.

— **Guarantee limitations, security and perfection**: The practices in providing guarantee and security by UK obligors can be different from US practices. English law requires consideration of various limitations including corporate benefit (the requirement that guarantees provide tangible benefit to the guarantor, not just the group), financial assistance rules (which continue to apply to public companies), fraudulent/wrongful trading risks and the potential need for "limitation language" to prevent guarantees being void or unenforceable. On security formalities, as an example, it is not customary for UK obligors to register security over intellectual property or deliver endorsed insurance certificates. Instead,

there is a requirement to file security with Companies House within 21 days of creation of the security, even if the security agreement is New York law governed—a formality not to be missed as a failure to make a filing could make the security void against a liquidator or administrator and when the charge become void as a result of the failure to register the security, the money secured under the charge becomes immediately due and payable under statute (as well as any default which may occur as a result of the failure to register the charge under the facilities agreement itself). Note also that English law has different hardening periods for security granted in the run-up to insolvency compared to US law.

IV. Practical Recommendations/ Conclusion

As cross-border private equity activity between the US and UK/European markets continues to grow, and the practice of having New York law interpreted covenants in UK/European leveraged facility agreements becomes the norm, it is increasingly important for parties to understand the implications by:

— conducting a thorough review of covenant packages to identify terms that may be interpreted differently under the two legal systems;

— considering including express definitions or interpretative provisions for key terms where divergent interpretation is likely;

— maintaining clear documentation of commercial intentions to assist with interpretation disputes; and

— distinguishing clearly between the governing law of the agreement and the law governing interpretation of specific covenants, as this can be a source of confusion.

The above discussion provides a general summary for consideration and is not intended to be legal advice. The Cleary team includes experienced leveraged finance lawyers in both the US and the UK and we would be delighted to speak further if you need advice in relation to matters discussed in this article.

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