

7 April 2021

## European Leveraged Finance Association and Loan Market Association to create best practice guidance on incorporating ESG provisions into leveraged loan agreements

**London, 7 April 2021:** The European Leveraged Finance Association (ELFA) and Loan Market Association (LMA) are working together to produce best practice guidance for market participants to consider when structuring terms that incorporate ESG factors into documentary provisions in leveraged loans, including ESG-linked margin ratchets.

The ELFA and LMA are partnering on the best practice guidance to ensure loan market participants in Europe incorporate ESG provisions in an effective and appropriate way as this practice gains pace. The organisations are working closely with participants across the leveraged loan industry, using the Sustainability Linked Loan Principles\* as an underlying framework. The resulting guidance will set out the factors that borrowers should consider when integrating ESG factors into leveraged loan agreements.

Traditionally, margin ratchets have been linked to leverage to incentivise healthy de-leveraging for issuers, but the European loan market has recently seen ESG-linked margin ratchets appear. These are drafted to reward borrowers where pre-defined targets are met by decreasing margins and hold borrowers to account where there is a failure to meet targets by increasing margins.

Initial work has highlighted several areas that will be addressed in the guidance:

- ESG targets should be relevant to the company – for example, carbon emitters should include a measurable target for emissions reduction in their ESG ratchets.
- Key performance indicators (KPIs) should be meaningful and ambitious, and not something that can be achieved on day one of syndication.
- Structuring of ESG KPIs should be carefully planned well ahead of deal launch and, in any event, ESG KPIs should be agreed before the relevant provisions are drafted.
- ESG provisions should not be used as a lever for economics and loosened if a deal is syndicating well, which would go against the spirit of the provisions and invite scrutiny over greenwashing.

**Sabrina Fox, Chief Executive Officer, European Leveraged Finance Association, commented:**

“The ELFA has been working on several initiatives to support the growth of ESG within the European leveraged finance market to provide resources that will allow borrowers to increase the ESG data and disclosure that is provided to investors. Many opportunities are unlocked with this data, including the potential for contractual provisions that incentivise borrowers to improve their sustainability profile, and hold borrowers to account should targets not be met. However, such provisions must be drafted in a manner that genuinely stands to bolster a borrower’s sustainability profile with meaningful, ambitious targets that are appropriately tailored to the business and disclosed to investors at the term sheet stage. The guidance we are developing with the LMA is critical to helping our market avoid the risk of greenwashing and aims to support strong implementation of ESG principles documentation with a solid basis in the company’s overall business.”

**Gemma Lawrence-Pardew, Director – Legal, Loan Market Association, added:**

“The depth and breadth of the leveraged finance market means that it is uniquely positioned to aid the ESG journey for a large proportion of the corporate sector, from listed companies to medium sized enterprises. We and the ELFA believe it is imperative for all market participants to get the approach to ESG right in the leveraged finance market, and to do so from the start, in order to build a more sustainable future.”

The ELFA and LMA are urging market participants to share their views so that these can be reflected in the initial recommendations on the guidance.

**Ends**

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**Notes to Editors**

\*Sustainability Linked Loan Principles:

[https://www.lma.eu.com/application/files/5115/8866/8901/Sustainability\\_Linked\\_Loan\\_Principles\\_V032.pdf](https://www.lma.eu.com/application/files/5115/8866/8901/Sustainability_Linked_Loan_Principles_V032.pdf)

The ELFA and LMA Insights report on ESG-linked margin ratchets can be found [here](#).

**About the ELFA**

The ELFA is a trade association comprised of European leveraged finance investors from over 45 institutional fixed income managers, including investment advisors, insurance companies, and pension funds. The ELFA seeks to support the growth and resilience of the leveraged finance market while acting as the voice of its investor community by promoting transparency and facilitating engagement among European leveraged finance market participants. For more information, please visit the ELFA website: [www.elfainvestors.com](http://www.elfainvestors.com).

**About the LMA**

The LMA's key objective is improving liquidity, efficiency and transparency in the primary and secondary syndicated loan markets in Europe, the Middle East and Africa (EMEA). By establishing sound, widely accepted market practice, the LMA seeks to promote the syndicated loan as one of the key debt products available to borrowers across the region. The LMA's membership currently stands at 730 organisations covering 65 countries, comprising commercial and investment banks, institutional investors, law firms, borrowers, service providers, rating agencies, and regulatory and governmental bodies.