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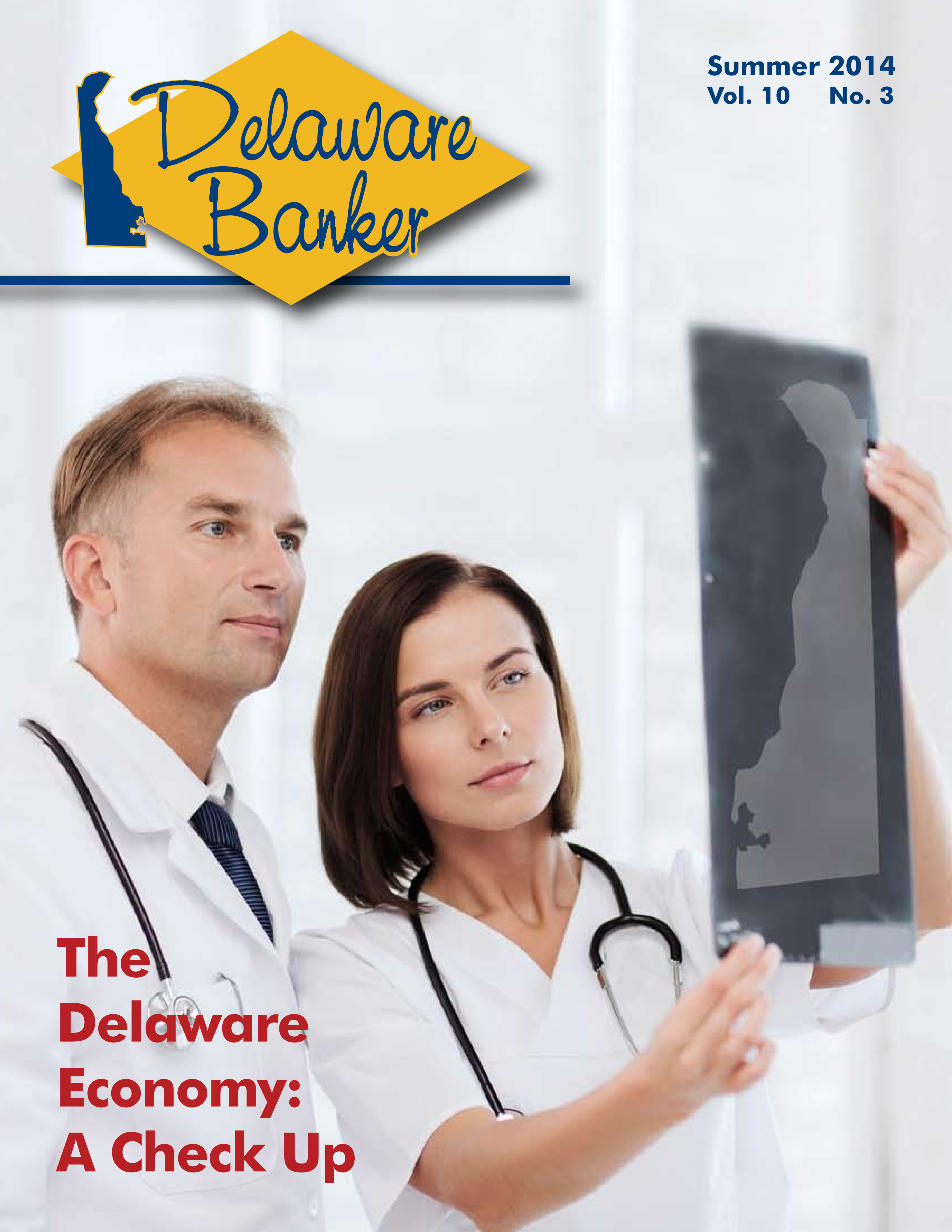

The Delaware Economy: A Check Up

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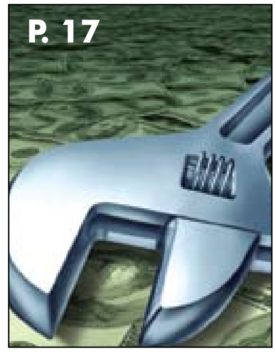

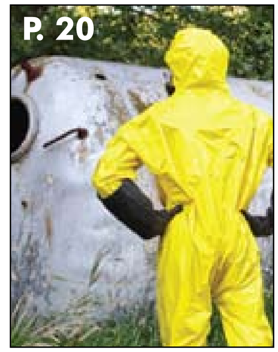

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SUBMISSIONS
Delaware Banker welcomes news items from members of the Delaware Bankers Association. The Editors reserve the right to refuse any advertising or editorial copy deemed unsuitable for publication. The Editors reserve the right to set the publication date in accordance with the Association's needs. Direct submissions to Greg Koseluk at greg.koseluk@debankers.com

SUBSCRIPTIONS
Delaware Banker is available free of charge to all officers, executives, management, and key personnel of DBA members. Paid subscriptions to Delaware Banker are available to all others at a rate of $20 per year. To be placed on the subscriber list, please email Greg Koseluk at greg.koseluk@debankers.com.

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View from the Chair

by
Rodger Levenson
Executive Vice President
WSFS Bank

Chairman
Delaware Bankers Association

"We are competitors, but we all work together for the common good through the DBA."

It is an honor to have been selected to Chair the Delaware Bankers Association as it embarks on its 120th year. I'd like to thank Past- Chairman Dave Gillan for his guidance and the entire DBA Board and membership for all the best wishes received over the last month. We have an extraordinary Board this year and I look forward to working with them. They are: David E. Gillan, Chairman of the Board and CEO, County Bank (Our Past Chairman); Lynda Messick, President & CEO, Community Bank Delaware (Our Chairman-Elect); Cynthia D.M. Brown, President, Commonwealth Trust Company; Mark A. Graham, EVP, Wealth Advisory Services, Wilmington Trust; Rob Habgood, Consumer Lending Executive, Bank Of America; Nicholas M. Marsini, Jr., Regional President, PNC Delaware; ; Donna G. Mitchell, President & CEO, Deutsche Bank Trust Company Delaware; James Roszkowski, President, Discover Bank; P. Randolph Taylor, President, Fulton Bank, N.A., Delaware National Division, and, William S. Wallace, Chief Operations Officer, Chase Consumer & Community Banking.

Mr. Gillan has advised that the year goes by fast, so I plan on jumping in immediately and enjoying the ride. My strategy for the upcoming year is to engage as many of you as I possibly can. To me, the word Association means collegiality and communication. We are competitors, but we all work together for the common good through the DBA. I encourage you to contact me at rlevenson@wsfsbank.com with suggestions or issues pertinent to our industry.

We have already scheduled some important events through next May. Plans are up and running for our widely popular Trust Conference , September 30-October 1st, at the Hotel duPont. Later in the Fall we will be partnering with the Maryland Bankers Association for a Director's College led by the FDIC. November brings our Annual Compliance School, followed by a new Bank Secrecy Act Seminar in early December. In March 2015, we will once again offer BSA for Trust professionals.

March 4,5,6, 2015 we take our Annual Washington Visit. If you have never attended this event, you should take a closer look. Meetings with our Congressional delegation on Capitol Hill are interspersed with briefings by the American Bankers Association, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, and the Consumer Financial Protection Bureau. Although the meetings are important, the opportunity to interact with your peers on the trip is equally beneficial. We end March with our Legislative Reception in Dover. This is our opportunity to communicate face-to-face with our State legislators. This valuable session helps make our voice heard in the General Assembly. We close our year with our Annual Meeting and Dinner, May 14, 2015. Again, this is one of the premier social events for banking in Delaware with special State and National guests and always features a popular guest speaker.

The Association is not just about events, it is about educational offerings, communication opportunities in our Digest and Banker Magazine, image building, financial literacy programs, committee participation, and last but certainly not least legislative involvement. We welcome your thoughts and suggestions....if you are not already, I encourage you to become associated with your Association.

President's Report

by
David G. Bakerian
President, CEO & Treasurer
Delaware Bankers Association

"2014 has been busy with social, educational and political events coordinated by the DBA"

The DBA has been pretty busy since our last report in the Spring edition of Delaware Banker. The Annual Meeting held in May, once again exceeded expectations with motivational author Alison Levine delivering an energetic presentation focused on the art of high impact leadership. Alison concluded her evening with us by signing hundreds of copies of her book *On The Edge*.

June, as it always is, had the DBA immersed in legislative activities in the General Assembly. Tom Collins, our EVP for Government Relations spearheaded our successful efforts in Dover. Tom was challenged with a variety of bills touching on lender liability for environmental hazards, elder fraud protection, trust administration, debt collection practices, and veteran's rights. In coordination with our government Affairs Committee, Tom lead the charge to support, defeat , or amend pending legislation. Kudos to Tom and the Committee for ensuring a successful session. In August, the DBA will publish its Legislative Bulletin, which summarizes all business and banking related bills that we monitored.

July marked our attendance at the American Bankers Association Summer Meeting where State Association Executives, bankers from across the nation and ABA staff met to discuss national legislative issues. The primary focus of the meeting is to hone the legislative priorities for bankers for the next Congress. Listed below are some of the important topics that have made it to the priority list:

- Preserving Mortgage Options-Qualified Mortgage Loans (QM's).
- Reforming Fannie Mae and Freddie Mac - Constructive Management of the GSE conservatorships and supporting a strong Federal Home Loan Bank System.
- Reasonable and Prudent Capital Standards.
- Ending the Credit Union Free Ride.
- Fair Tax and Regulatory Treatment for the Farm Credit System.
- Reducing Excessive Burden on Community Banks.
- Reforming the Dodd-Frank Act.
- Responding to Cyber Threats and Data Breaches.

It goes without saying that the upcoming Congressional Session will be both interesting and critical to our industry. We plan to engage our Congressional team early and often this year regarding issues that are pertinent to our Nation and our State. If you have items that are not on the above priority list please feel free to contact the DBA staff with your suggestions. We are here for you!

Aside from the State and Federal legislative efforts, the DBA is gearing up to fine tune our mission to serve you better. Over the next few months you will be receiving surveys and information forms to help us update our database. We want to ensure the right information goes to the right person. Turnovers, retirements and promotions often delay us in getting that information to you on a timely basis. We would appreciate your response to our request for updated data on key personnel. On a related note, we are examining our Committee Structure and will be soliciting your input regarding what Committees are pertinent or outdated. In the meantime if you have any suggestions for Committee topics please feel free to send them along. The DBA is here to help make your job easier and we welcome your participation!

Sincerely,

David

What's New at the DBA

New Members
Associate Members

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First Republic Trust Company of Delaware LLC is a part of First Republic Bank. Using an open-architecture approach, we provide full trust administration services and serve as trustee of trusts designed to accomplish specific tax, financial, and estate planning goals using Delaware law.

DBA Annual Meeting

Rodger Levenson, Executive Vice President, WSFS Bank, was elected and installed as the Chairman of the Delaware Bankers Association (DBA) on May 8th at the DBA's 119th Annual Meeting in Wilmington.

David E. Gillan (r.) congratulates in-coming DBA Chairman Rodger Levenson

The DBA also elected and installed Lynda Messick, President & CEO, Community Bank Delaware, to the position of Chairman-Elect. Other Members of the DBA Board Of Directors are: Cynthia D.M. Brown, President, Commonwealth Trust Company; David E. Gillan, Chairman of the Board and CEO, County Bank (Past Chairman); Mark A. Graham, EVP, Wealth Advisory Services, Wilmington Trust; Rob Habgood, Consumer Lending Executive, Bank Of America; Nicholas M. Marsini, Jr., Regional President, PNC Delaware; Donna G. Mitchell, President & CEO, Deutsche Bank Trust Company Delaware; James Roszkowski, President, Discover Bank; P. Randolph Taylor, President, Fulton Bank, N.A., Delaware National Division, and, William S. Wallace, Chief Operations Officer Chase Consumer & Community Banking. Alison Levine, Explorer, Entrepeneur, and Author of *On the Edge: The Art of High Impact Leadership* was the evening's guest speaker.

Keys to Financial Success Scholarship Award

The DBA also announced the winners of the 2014 Keys to Financial Success Scholarship Award at the 119 Annual Meeting. The winners were Timothy Steindl and Dara Reilly, both seniors at Caesar Rodney High School. Both students participated in the Keys to Financial Success course. Each winner receives a $2,500 scholarship. Keys to Financial Success is a full-semester elective taught in 28 high schools throughout Delaware to over 4,200 students. The course was developed in partnership with

Charles Plosser, President and CEO of the Federal Reserve Bank of Philadelphia, and Rodger Levenson, DBA Chairman, and Executive Vice President, WSFS Bank congratulate the recipients of the 2014 Keys to Financial Success Scholarship. (l. to r.) Charles Plosser, Dara Reilly, Timothy Steindl, Rodger Levenson.

the University of Delaware's Center for Economic Education and Entrepreneurship (CEEE), Delaware Bankers Association, Federal Reserve Bank of Philadelphia, and Consumer Credit Counseling Service of Maryland and Delaware. Keys to Financial Success introduces students to the fundamentals of sound money management skills and basic financial planning concepts including Goals and Decision Making, Career Research, Money Management, Consumer Skills, and Risk Protection.

2014 Teach Children to Save Day Poster Contest Winner

Namo Yang, 4th grader at Robert S. Gallaher Elementary School was awarded first place in the 2014 Teach Children to Save Day poster contest in a ceremony at the school on Wednesday. Namo received $100, an autographed copy of *The Great Investo and the Secret Saver*, and an award certificate. Her winning entry, shown below was selected by the Teach Children to Save Day committee from over 400 entries submitted statewide. Second and third place winners were also awarded and each received $50. Namo's entry showed the steps in saving toward a goal, in her case a puppy. The poster was based on personal experience. When asked if she would spend or save the money, Namo replied: "I'm going to save it...to buy a dog!"

Cover Story

The Delaware Economy

A Regional Perspective on the Great Recession and Recovery

by Ardy L. Wurtzel
Research Associate, Corporate Affairs Department
Federal Reserve Bank of Philadelphia

The economic recovery experienced since the Great Recession has been relatively modest and slow, and it has varied in its strength and pace across the states. In particular, the recovery experienced so far in Delaware has lagged the nation's recovery in some sectors while outperforming the U.S. in others. Similar to all 50 states, Delaware's best measure of economic activity is the total dollar value of real gross state product, in which it ranks 31st among all 50 states, according to 2013 year-end data.[1] Due to Delaware's relatively weak housing market performance and the structural changes that have occurred in its labor market, the state has not weathered the Great Recession's storm and subsequent recovery very well, when compared with the nation.

In terms of real gross domestic product (GDP) per capita, the Great Recession's impact was greater on the U.S. compared with Delaware, yet the nation experienced a stronger recovery compared with the state. From 2007 to 2009, annual real GDP per capita for the nation decreased by 4.8%, compared with Delaware's lower decline of 4.1%. Over the course of the recovery from 2009 to 2013, annual real GDP per capita for the U.S. had a much stronger rebound of 6.0% when compared with Delaware, which actually contracted another 0.3% since the recovery began. On net, the nation's real GDP per capita is approximately 1% above its prerecession level, whereas Delaware's real GDP per capita remains below its prerecession level by 4.4% as of 2013. On a more encouraging note, Delaware's real GDP per capita growth has recently returned to positive territory, with 2013 growth at the highest it has been since 2009.[2]

Subdued confidence and multiple sources of uncertainty (such as new Dodd-Frank Wall Street Reform and Consumer Protection Act banking regulations, the Affordable Care Act's influence on consumer and business health-care costs, and global financial tensions) during the recovery have affected businesses, consumers, and the government, and this may continue to affect their future spending and investment decisions, putting further strain on economic recovery. The financial crisis that accompanied the Great Recession resulted from the collapse of a housing market price bubble, making the housing market recovery one of the determinants for the overall economic recovery. Moreover, stronger job growth is critical to the overall recovery because earned wage income is a key driver of consumer spending.

U.S. and Delaware Job Markets

In terms of the labor market, the economic recovery in Delaware has been wide-ranging compared with the national recovery. Delaware's unemployment rate is currently lower than the nation's rate, yet Delaware's job growth fared slightly worse than the nation's. As of May 2014, unemployment rates for the U.S. and Delaware remain above their prerecession levels; nonfarm payroll job losses in Delaware have yet to fully recover, whereas the nation's job growth surpassed its prerecession level.

Historically, Delaware's unemployment rate has been less than the nation's, and that trend has continued over this last recession. The nation's unemployment rate peaked at 10% following the recession while Delaware's peak was lower at 8.7%. During the recovery, the U.S. unemployment rate experienced a larger decrease of 3.7 percentage points (to 6.3% in May 2014) compared with Delaware's decrease of 2.5 percentage points (to 5.9% in May 2014).[3] Between January 2008 and February 2010, Delaware's nonfarm payrolls declined by 7.9% (29,500 jobs), which is more than the national decline of 6.3% (8.7 million jobs). Since February 2010, Delaware has added 24,700 jobs but remains 1.3 percent below its prerecession peak, whereas the U.S. has surpassed its prerecession peak by 1.0 percent.[4]

Delaware's Job Sector Gains/Losses

Delaware's job market performance has varied by sector. As of May 2014, seven of the state's 10 sectors remained below their peaks from January 2008 while the remaining three sectors surpassed their prerecession levels. The three best-performing sectors, as measured by the net percent of jobs gained from the beginning of the recession through the recovery, are ranked from highest to lowest in percentage growth in Table 1.

TABLE 1: DELAWARE'S BEST-PERFORMING SECTORS[5]
January 2008 to May 2014

EMPLOYMENT INDUSTRY SECTOR		NET JOB CHANGE
(1)	Education & Health	+14.8% (+9,100)
(2)	Leisure & Hospitality	+12.4% (+5,100)
(3)	Government	+2.4% (+1,500)

The education and health sector jobs did not decrease over the course of the recession. In fact, this sector experienced the largest percent increase in jobs and makes up the second largest share (16.2%) of Delaware's entire labor market; thus, the sector's 14.8% increase amounts to 9,100 newly added jobs.

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Delaware Economy

(continued from p. 11)

Delaware's second best-performing sector was leisure and hospitality, which had a net increase of 12.4% (5,100 jobs) throughout the recession and recovery, and makes up the fifth largest share (10.6%) of the job market. As of May 2014, the three industry sectors in Table 1 constituted 41.6% of all Delaware jobs, adding 15,700 total jobs between January 2008 and May 2014.

The Great Recession began with a housing market collapse resulting from an excessive buildup in housing inventory and overvalued home prices. The construction employment sector was directly affected by this collapse, as seen by the national and state job losses. From Delaware's job market peak in January 2008 to its trough in February 2010, the largest job decrease (in percentages) for the U.S. and Delaware occurred in the construction sector; the U.S. experienced a 26.1% decline in construction jobs (1.95 million jobs) while Delaware experienced a decline of 22.7% (6,100 jobs) in its combined mining and construction sector.[6] Delaware's overall worst-performing sectors over the course of the Great Recession through the recovery are shown in Table 2.

TABLE 2: DELAWARE'S WORST-PERFORMING SECTORS [7] January 2008 to May 2014	
EMPLOYMENT INDUSTRY SECTOR	NET JOB CHANGE
(1) Information Services	-24.3% (-1,700)
(2) Mining & Construction	-22.7% (-6,100)
(3) Manufacturing	-20.7% (-6,700)
(4) Transportation/Trade/Utilities	-5.6% (-4,600)
(5) Other Services	-4.5% (-900)
(6) Financial Services	-0.7% (-300)
(7) Business & Professional Services	-0.5% (-300)

The information services sector experienced the largest percentage decline in jobs, yet it accounts for the smallest share (1.2%) of all Delaware jobs. Consequently, the 24.3% decrease in information sector jobs amounted to the loss of only 1,700 jobs. Delaware's information sector (similar to the nation's) has been in a structural decline since 2001, reflecting job cuts in the publishing industries subsector (as a result of the dramatic decline in printed media consumption over the past decade) along with job losses in the telecommunications industries.[8] This structural decline indicates that information sector job losses are not fully attributed to the recession.

Based on the total number of jobs, the manufacturing sector was hit hardest, with 6,700 jobs lost. Undoubtedly, the recent closure of two major automobile plants, Chrysler and GM, contributed to this loss of manufacturing jobs in Delaware. Collectively, the seven sectors listed in Table 2 show a loss of 20,600 jobs and these sectors comprise 58.5% of all Delaware jobs.[9]

Housing Market

When compared with the nation, Delaware's housing market experienced a larger downturn during the recession and has been slower to recover. National home prices remain less depressed than Delaware home prices when compared with their prerecession levels. Housing starts in Delaware experienced a smaller percentage decline during the economic downturn when compared with the nation, and Delaware experienced a smaller percent increase in housing starts through the recovery when compared with the nation, as shown in Table 3.

TABLE 3: AVERAGE ANNUAL RATE OF HOUSING STARTS: U.S. & DE (1990 to 1Q2014)[16]		
	U.S.	DE
1990–2001 Average Annual Rate of Housing Starts (000s)	1,408	5.3
2002–2006 Average Annual Rate of Housing Starts (000s)	1,879	7.5
2007–1Q 2014 Average Annual Rate of Housing Starts (000s)	819	3.8
Percent Change (from 1990–2001 avg. to 2002–2006 avg.)	+33.5%	+42.5%
Percent Change (from 2002–2006 avg. to 2007–2013 avg.)	-56.4%	-50.2%

According to the Federal Housing Finance Agency's (FHFA) Purchase-Only Home Price Index,[10,11] between the housing price peak in 1Q 2007 and the trough in 2Q 2011, national home prices declined 20%. Since then, as of 1Q 2014, national home prices regained much of their loss while remaining 7.9% below their prerecession peak. Compared with the nation, Delaware's home prices experienced a larger percent decline of 22.9% from its price peak in 4Q 2006 to its trough in 3Q 2011 and had a smaller amount of that loss regained over the recovery, leaving Delaware home prices 18.3% below their prerecession peak.[12]

Delaware home prices took a much harder hit than the nation's home prices because Delaware's housing inventory buildup was much larger than the nation's. The average pace of U.S. housing starts increased by 33.5%, from the 1990–2001 average of 1.41 million starts to the 2002–2006 average of 1.88 million starts. Since then, the national average annual rate of housing starts from 2007 to 1Q 2014 decreased to 819,020 starts (56.4%).[13] Much of the housing buildup across the nation from 2002 to 2006 was speculative and was not met with equal increases in housing demand. Population growth and household formation, both key drivers of housing demand, decelerated over the same time frame.[14]

Delaware's buildup in housing inventory was significantly larger than the nation's; Delaware's average home starts from 1990–2001 to 2002–2006 increased by 42.5%. Since then, the average annual rate of starts decreased by 50.2% (from 2007 to 1Q 2014). Similar to the nation's, Delaware's acceleration in home starts wasn't met with adequate increases in Delaware's resident population, which increased 21.9% (1990–2006), about half of the acceleration in housing starts.[15]

Conclusion

Navigating the future of the current economic recovery is difficult because uncertainty in the recovery's strength and pace affects the economic decisions we face today. Compared with the national recovery, Delaware's recovery has shown a slightly weaker performance in its labor market conditions with a lower unemployment rate, yet it has experienced slower job growth. When it comes to the housing market, the nation has performed better than Delaware has; Delaware's housing buildup has left it unable to match the price growth advances seen at the national level throughout the recovery. Overall, Delaware's economic performance throughout the Great Recession and the subsequent recovery is, on balance, slightly behind that of the nation.

Ardy L. Wurtzel is a research associate in the Corporate Affairs Department with the Federal Reserve Bank of Philadelphia. She delivers economic outlook presentations to the District Bank's business & banking community, manages economic data sets and conducts research on current economic trends.

The views expressed here are those of Ardy L. Wurtzel and not necessarily those of the Federal Reserve Bank of Philadelphia or the Federal Reserve System.

Notes

1- The Bureau of Economic Analysis (BEA), Real GDP by State Release, last annual data point is for 2013, available at http://www.bea.gov/newsreleases/regional/gdp_state/2014/pdf/gsp0614.pdf.

2- BEA, source for the U.S. and Delaware demographic data: U.S. Census Bureau. Calculations to obtain the real GDP per capita data and the related percent changes were conducted by the author.

3- U.S. Bureau of Labor Statistics (BLS), Regional & State Employment and Unemployment, May 2014 release.

4- BLS, Regional & State Employment and Unemployment, May 2014 release. All calculations conducted by the author.

5- BLS, Regional & State Employment and Unemployment, May 2014 release. All calculations conducted by the author.

6- BLS; the BLS only publishes payroll sector data for the combined Mining & Construction payroll industry sector, as opposed to separating mining from construction jobs. All calculations conducted by the author.

7- BLS, Regional & State Employment and Unemployment, May 2014 release. All calculations conducted by the author.

8- According to the North American Industry Classification System (NAICS), the information sector includes the following subsectors: publishing industries (newspaper, periodical, book, directory, and software publishers); motion picture and sound recording industries (video and sound recording industries); broadcasting, excluding the Internet (radio and television broadcasting, cable and other subscription programming); telecommunications (wired telecommunication carriers, wireless telecommunication carriers, satellite telecommunications, and other telecommunications); data processing, hosting, and related services; and Other Information Services (news syndicates, libraries and archives, internet publishing, and broadcasting and web search portal services); http://www.census.gov/cgi-bin/sssd/naics/naicsrch?chart_code=51&search=2012.

9- BLS, Regional & State Employment and Unemployment, May 2014 release. All calculations conducted by the author.

10- FHFA's House Price Index (HPI) is a broad measure of the movement of single-family house prices. The HPI is a weighted repeat-sales index, meaning that it measures average price changes in repeat sales or refinancings on the same properties. This information is obtained by reviewing repeat mortgage transactions on single-family properties whose mortgages have been purchased or securitized by Fannie Mae or Freddie Mac since January 1975. See http://www.fhfa.gov/Default.aspx?Page=81.

11- The FHFA HPI only includes mortgages under Fannie Mae and Freddie Mac's conforming loan limits and, therefore, excludes jumbo home loans/mortgages. (Home loans above this "conforming loan limit" are known as jumbo loans.)

12- FHFA Purchase-Only House Price Index, seasonally adjusted and indexed 1Q 1991 = 100, as of 1Q 2014. This index includes only purchase price data; it does not include refinancings. All calculations conducted by the author.

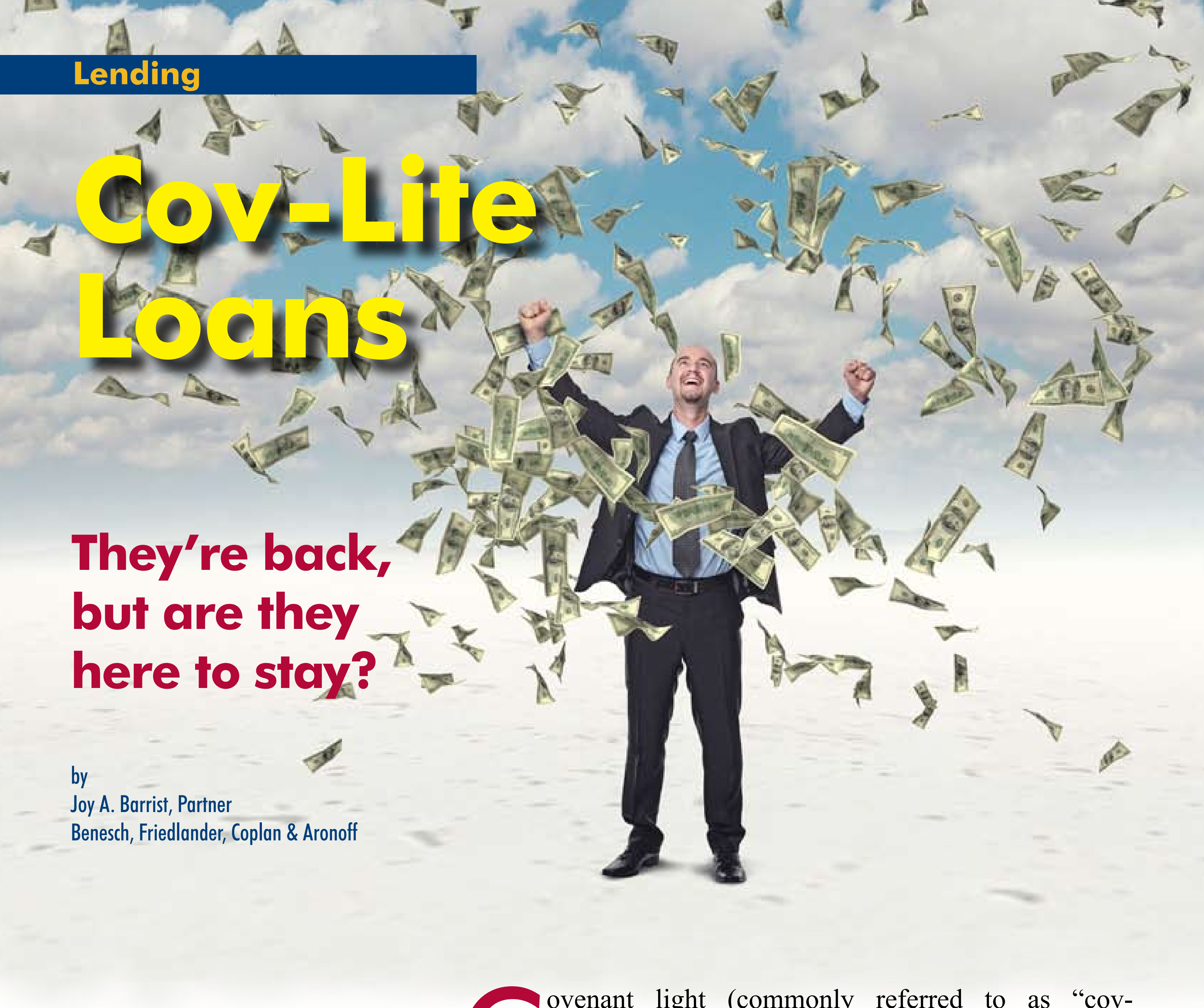
13- Bank of Tokyo-Mitsubishi UFJ. All calculations conducted by the author.

14- U.S. Census Bureau (data are seasonally adjusted at annual rates–SAAR). All calculations conducted by the author.

15- U.S. Census Bureau (data are seasonally adjusted at annual rates–SAAR). All calculations conducted by the author.

16- Bank of Tokyo-Mitsubishi UFJ (seasonally adjusted at annual rates–SAAR). All calculations conducted by the author.

Cov-Lite Loans



They're back, but are they here to stay?

by
Joy A. Barrist, Partner
Benesch, Friedlander, Coplan & Aronoff

Covenant light (commonly referred to as "cov-lite") loans are loans that do not contain financial maintenance covenants. The issuance of a cov-lite loan means that debt is being issued to borrowers with less restrictions on collateral, payments and level of income.

We started seeing a substantial increase in cov-lite loans around 2006, with the increasing strength of private equity firms and the decreasing opportunities for traditional corporate loans made by banks. The strength of the private equity firms performing highly leveraged buyouts drove a so called "race to the bottom" with groups of banks competing with each other to offer continuing less invasive terms to borrowers in relation to leveraged buy-outs. The financial crisis of 2007-08 led to a stall of the use of cov-lite loans. Recently, however, cov-lite loans are regaining popularity, especially in the syndicated markets. The use of cov-lite loans is now also making its way down into the middle markets (EBITDA less than $50 million) resulting from aggressive structures due to a lack of deal flow and persistent fundraising for middle market credit, especially in the form of junior capital. Cov-lite loan volume reached $118.5 billion through the middle of May, 2014, which accounted for about 63% of institutional leveraged loan volume.

Perhaps one of the reasons the use of cov-lite loans is on the rise is the data from the 2007-08 default cycle showing that first lien cov-lite loans defaulted at a lower rate than the overall market, and, when they defaulted, provided better recoveries, according to a special report published by DDJ Capital Management, citing data from Moody's Investors Service and S&P Leveraged Commentary & Data.

Regardless of this data, there is still debate as to whether the performance of cov-lite loans during the 2007-08 default cycle is repeatable. Unlike prior to the financial crisis, most of the 2013 cov-lite loans back refinancing and/or repricing of existing loans, not M&A and leveraged buy-out deals. According to the Financial Times, almost two-thirds of the leveraged loans now sold into the US markets contain fewer covenants than traditional deals, greatly exceeding the 29% proportion reached at the height of the leveraged buy-out boom in 2007. Regardless of the data, market participants chasing yield don't seem to care much, despite signs that the quality of today's cov-lite loan has deteriorated significantly from the last cycle.

So, what exactly makes a loan a cov-lite loan? While there are varying definitions throughout the industry, characteristically, cov-lite loans remove the requirement to report and maintain loan to value, debt to equity, EBITDA and other similar ratios. Cov-lite loans lack financial maintenance tests, which require the maintenance, at all times, of certain financial ratios. Cov-lite does not mean that a loan is not subject to any covenants. Often, such loans are not void of incurrance financial tests, which require that a borrower not take certain actions that push a financial covenant ratio beyond a specific limit.

More aggressively negotiated cov-lite loans may also remove "material adverse change" defaults, requirements to deliver annual accounts to the lender, restrictions on negative pledges and requirements for lender approval to changes in borrower's ownership. Many cov-lite loans apply springing financial maintenance covenants, in which such covenants become applicable when a revolving loan is drawn upon or when draws exceed a threshold amount.

One view is that cov-lite loans are riskier because they remove the early warning signs that lenders would otherwise receive through traditional covenants. During the credit crunch, cov-lite loans arguably hampered the ability of lenders to step in and both seek to rectify positions that were going bad and to limit exposure once matters had already gone bad.

The other side of this argument is that cov-lite loans simply reflect changes in bargaining power between borrowers and lenders, following from the increased sophistication in the loan markets where risk is quickly dispersed through syndication or credit derivatives. Additionally, there are many arguments that cov-lite loans provide companies with greater flexibility to manage their finances and can help them avoid going into bankruptcy. Examples of this flexibility include: (i) equity cure provisions in which the borrower's sponsors and shareholders are permitted to contribute equity to the borrower to cure a default without a requirement to prepay the loan; (ii) the borrower's ability to issue additional debt, if after giving pro-forma effect to the issuance, the borrower will comply with a maximum leverage ratio or a minimum interest coverage ratio; (iii) the borrower's ability to make unlimited acquisitions (instead of fixed annual or deal term limits) if the borrower will be in compliance with certain maintenance covenants on a pro-forma basis; and (iv) permitted repayment of subordinated, unsecured and/or second-lien debt so long as the borrower in compliance with an incurrence covenant.

It's not surprising that these looser covenant requirements (or lack thereof) have drawn the attention of the bank regulators, who are urging banks that arrange such deals to be more cautious. Even though most of these cov-lite loans don't stay on banks' balance sheets for very long, there is a danger that they could get stuck with a faulty loan if the market goes into another downward spiral before the loans are sold to investors. Currently, the leverage lending guidelines are fairly flexible and appear to be having minimal effect on the cov-lite market.

Some proponents of cov-lite loans question the importance to lenders of having financial maintenance covenants. Is it better to hold a good cov-lite loan than hold a bad credit with various financial maintenance covenants? Should credit ratings be more valuable than the proportion of cov-lite loans in a portfolio? Is a well-manage company with steady cash flow better than a poorly-managed company with uncertain cash flows under strict financial maintenance covenants? While, ideally,

(continued on p. 16)

Lending

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lenders are seeking out good-credit loans with traditional financial covenants, the answer surely lays somewhere in the middle. One important note is that a cov-lite loan does not, solely by its classification as such, mean a bad credit. Companies obtaining cov-lite loans are often among the strongest companies in the loan market.

Cov-lite loans do increase lender risk to a certain degree, but there is no indication that they are going anywhere as long as the credit market remains a highly competitive marketplace with investors, traditional and nontraditional, continuing to invest in the same. According to Forbes, many veteran loan managers once fixated on preserving covenant culture have surrendered to the new environment as the need to put money to work outweighs hunger for tighter loan structures.

"We just have to stick to our basics and do our credit work," one portfolio manager commented. "The market is what it is and we have to go with what's out there."

While all loans should be thoroughly reviewed and underwritten, in some cases thought should be given to the idea that a lack of maintenance covenants may not, in and of itself, be prohibitive to making a loan to an attractive, stable, profitable borrower.

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Ms. Barrist also represents investors and developers in real estate sales and acquisitions, and landlords and tenants in the negotiation, drafting and termination of leases for office and retail properties. She also has extensive experience in the rendering of legal opinions in finance and other commercial transactions. In particular, Ms. Barrist has represented regional and national banks and hedge funds in financing residential and commercial real estate projects throughout the United States, Mexico and the Caribbean.

Fixer Upper

Using an NJSA to Fix a Broken Directed Trust

by Todd A. Flubacher, Esq.
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Over the last decade, directed trusts have become commonplace in Delaware. More and more, settlors and beneficiaries are using trusts to implement complex investment, tax and wealth transfer objectives that come in conflict with the limitations of traditional fiduciary duties and pose potential risks on fiduciaries. Settlors often accomplish these objectives by employing directed trusts that bifurcate responsibilities (such as investments) from the rest of the traditional trust administration functions, assigning them to a separate adviser who will direct the trustee to carry out those specific objectives.

Many governing instruments use different approaches with varying degrees of effectiveness to implement the directed trustee concept. A Delaware directed trustee that exercises its trustee power in accordance with a direction from an investment adviser as provided for in a properly drafted governing instrument should not be liable for any loss resulting directly or indirectly from taking such action, except in the case of the directed trustee's own wilful misconduct pursuant to 12 Del. C. § 3313. This limitation of liability applicable to a directed trustee under 12 Del. C. § 3313 is referred to in this article as the "Statutory Defense". However, not all directed trustee provisions are created equal. It is critical that a governing instrument describe, in clear and complete terms, the specific trustee powers that are exercised only at direction, with the balance of the trustee powers exercised solely by the trustee in its own discretion, so that there can be no doubt whether the directed trustee or the investment adviser is responsible for a particular matter. A provision in a governing instrument that falls short of this standard may create ambiguities that pose risks to the fiduciary that were not likely intended by the settlor nor the trustee. The focus of this article is how to identify problematic directed trust provisions, and how to use an NJSA to fix them by interpreting ambiguous or vague provisions that may cause risk.

How To Effectively Bifurcate Investment Responsibility

In order for a directed trustee to be able to rely upon the Statutory Defense, it is critical that the trust's governing instrument properly and unambiguously state which trustee powers, duties, and responsibilities are exercisable by the directed trustee only upon the written direction of the investment adviser and which are not. We begin with the principle that a trustee has all of the powers conferred upon it by a governing instrument as well as those conferred by applicable law, and that those are all of the powers exercisable by the trustee. See Restatement (Second) of Trusts, Section 186. Almost every governing instrument includes a somewhat lengthy list of powers granted to the trustee, including investment powers. In addition, Subsection 3324(a) of Title 12 of the Delaware Code provides that a trustee may exercise any powers conferred under the governing instrument and, except as limited by the governing instrument, under Chapter 33 of Title 12 of the Delaware Code, including 12 Del. C. § 3325. Section 3325 provides a discrete list of trustee powers conferred upon Delaware trustees. Thus, the complete list of investment powers possessed by a trustee is readily identifiable in the governing instrument and Section 3325 of Title 12 of the Delaware Code.

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The investment adviser provisions in some governing instruments do not cross-reference the actual trustee powers, rather they give a generic description of investment powers. For example, some investment adviser provisions merely state that the trustee shall act upon direction of an investment adviser with respect to the "investment and management of the trust assets," or perhaps it includes some form of short, generic description of investment activities, like "retention, purchase, sale, lending and voting" of trust assets. Some investment adviser provisions merely refer to the definition of "investment decisions" under Section 3313(d), which means "with respect to any investment, the retention, purchase, sale, exchange, tender or other transaction affecting the ownership thereof or rights therein and with respect to non-publicly traded investments, the valuation thereof". The problem with these provisions is that during the real-world administration of a trust, when the trustee receives a direction letter to execute complicated, nuanced transactions, it often becomes ambiguous whether such directions are clearly within the scope of trustee powers exercised only upon the direction of an investment adviser. When it comes time for the directed trustee to enter into a transaction involving complicated contractual arrangements like a stock purchase agreement, security agreement, a special purpose entity, loan, guarantee, documents that include representations and warranties or grant proxies or powers of attorney, or to manage investment paying real estate taxes or life insurance premiums, there are ambiguities relating to the scope of the direction provision in the governing instrument that immediately become apparent. Can the trustee safely rely on the direction letter and be protected by the Statutory Defense if it is not clear whether the trust powers that it exercises in order to carry out certain investment activities fall within the scope of the investment adviser provision?

Ambiguities Create Fiduciary Risk

The powers that a directed trustee can exercise exclusively at direction should be described in the governing instrument by express cross-reference to the investment powers granted under the governing instrument and under Section 3325. The risk associated with an improperly drafted governing instrument is that if the investment adviser provision in the governing instrument does not specifically reference all such powers, there could be an argument that the trustee independently possesses any powers that are not specifically referenced, and that those powers could (or should) be exercised by the directed trustee without direction from the adviser. Furthermore, if a governing instrument uses a generic description of investment activities, there could be an argument that certain actions taken by the trustee fall outside of the direction language because there is ambiguity as to whether a specific trustee power or investment transaction is covered by that language. In other words, if a governing instrument was drafted in an arguably ambiguous manner, the beneficiaries could make an argument that investment losses or poor investment decisions are the result of actions taken by the trustee that were not within the scope of an ambiguous directed trustee provision, or that the trustee possessed independent powers that could have been exercised to mitigate such losses. If such arguments prevail, the directed trustee might not be entitled to the Statutory defense.

Another issue arises when a document provides that the investment adviser may direct the trustee with respect to the exercise of certain powers, but does not clearly state that the trustee shall exercise those powers "only" upon direction. Without providing that the trustee only has the ability to exercise those powers as and when directed, it could be argued that not only may the investment adviser direct the trustee to exercise the powers, but the trustee also has the power to exercise those powers independently.

Others issues relate to the due diligence and reporting that might be performed by a directed trustee. Subsection 3313(e)(3) of Title 12 creates a default rule that, absent clear and convincing evidence or a contrary provision in a governing instrument, any action of the directed trustee with respect to "matters within the scope of the investment adviser's authority" are presumed to be administrative actions of the directed trustee solely to allow the directed trustee to perform its duties and shall not be deemed to constitute an undertaking by the directed trustee to monitor the investment adviser or otherwise participate in actions within the scope of the investment adviser's authority. However, if the language of the governing instrument creates an ambiguity as to whether certain powers are within the scope of the investment adviser's authority, the directed trustee may not be entitled to the protection under Subsection 3313(e)(3).

A directed trustee may, and often does, consult with or request information from an investment adviser. Without the protection afforded by Subsection 3313(e), a directed trustee could theoretically expose itself to a risk of liability based on the directed trustee's course of conduct. For example, it may be possible that consultation with an investment adviser or requests for information could, in certain circumstances, expose the directed trustee to an argument that the directed trustee, by requesting or receiving such documentation on a frequent basis, has undertaken the duty of monitoring whether such asset remains a proper investment for the trust. Additionally, the investment adviser could theoretically argue that notwithstanding the terms of the governing instrument, the directed trustee's conduct led the investment adviser to believe that the directed trustee was independently monitoring such assets and the investment adviser relied on such monitoring and assumed the directed trustee would provide advice as and when it was necessary to act with respect to such asset. This risk could be compounded if there is an argument that certain investment activities do not fall within the directed trustee provision, or that the trustee possesses independent investment powers that could be exercised without direction.

Clearly, none of these risks and potential arguments were intended or even anticipated by a settlor who included an investment adviser provision in the governing instrument with the intent to separate investment responsibility from other trustee functions and allocate that responsibility to an investment adviser. However, issues could potentially stem from the potential ambiguity in the governing instrument.

Ambiguities Can Be Fixed With An NJSA

In 2013, Delaware enacted a Non-Judicial Settlement Agreement ("NJSA") statute as new Section 3338 of Title 12 of the Delaware Code. Subsection 3338(b) provides that "interested persons" may enter into a binding NJSA with respect to any matter involving a trust. Subsection 3338(c) provides that a nonjudicial settlement agreement is valid only to the extent that it does not violate a material purpose of the trust and includes terms and conditions that could be properly approved by the Court of Chancery. The term "material purpose" is not defined in new Section 3338. Subsection 3338(d) provides a list of six matters that may be resolved by an NJSA, including: "(1) interpreting or construing the terms of a trust" and "(6) determining the liability of a trustee for an action relating to the trust". Although there is some question as to whether an NJSA can be used to modify irrevocable trusts under Delaware law to add new investment adviser provisions or modify an investment adviser provision, an NJSA under Section 3338 clearly can be used to interpret or construe an existing investment adviser provision to eliminate any ambiguities. Consequently, an NJSA can be used to resolve the types of ambiguities described in this article and minimize or even eliminate the related risks.

For example, if an investment adviser provision includes only a vague, generic description of investment activities that are to be exercised at the direction of an investment adviser, an NJSA could interpret and construe that provision to clarify that all investment powers are to be exercised only upon direction (by specific reference to each of them) and to limit trustee duties and liability in connection with such matters under the authority of the investment adviser. Also, an investment adviser provision that cross-references the investment powers in the governing instrument but fails to cross-reference the investment powers granted to the trustee under Section 3325 of Title 12 of the Delaware Code could be construed to include the investment powers found in Section 3325. An investment adviser provision that does not clearly provide that the trustee shall exercise certain powers only upon the direction, could clarify that the trustee shall not exercise those powers except upon written direction. An NJSA can also reinforce the willful misconduct standard of liability and clarify that the directed trustee shall have no duty to monitor the investment adviser or notify beneficiaries if the trustee does not agree with the investment adviser's decisions. An NJSA can also make it clear that the trustee shall value assets subject to the direction of an investment adviser shall only as directed.

Generally, existing governing instruments that include directed trustee provisions clearly manifest the settlor's intent that the investment responsibility should rest exclusively with the investment adviser and not the trustee. The inclusion of such a provision demonstrates it was the intent of the settlor and the trustee at the time they entered into the trust agreement that the trustee should not take part in investment decisions and should have limited liability and charge lower compensation for the reduced role. In other words, fully bifurcating the investment function is clearly consistent with the settlor's intent, and is indeed a material purpose of the trust. Nevertheless, there may be potential risks associated with some directed trusts to the extent that an ambiguous investment adviser provision provides a beneficiary with an argument, after investment losses occur, that the trustee could have taken some action, or that actions taken by the trustee were not within the scope of powers exercisable only at the direction of the investment adviser. For such trusts, an NJSA can be used to minimize or even eliminate that risk and effectuate the settlor's intent.

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Tank Trap?

Lender Liability Reform and Expanded Scope of Underground Storage Tank Liability for Owners and Operators

by Robert W. Whetzel and
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In the 2013 legislative session, Delaware adopted environmental lien legislation authorizing the Delaware Department of Natural Resources and Environmental Control ("DNREC") to impose environmental liens on real property to recover its cleanup costs. Left unresolved in 2013, but addressed in the recently concluded legislative session, is the broader topic of lender liability for environmental conditions at sites that have been impacted by hazardous or regulated substances.

Environmental Lender Liability - The Basics

Environmental liability statutes, like the federal Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA") and the Delaware Hazardous Substance Cleanup Act ("HSCA"), generally impose liability on "owners" and "operators" of sites that are impacted by a release of hazardous or regulated substances.

Liability is strict, joint and several, and retroactive – meaning that liability is imposed without regard to fault or culpability, and that any one responsible party can be held liable for the entire cost of addressing the environmental condition of an impacted site. Defenses are few and difficult to establish, with the result that a liable party may be forced into funding the cleanup of a site that it had little, if any, responsibility for creating.

Consider, against this background, the activities that lenders typically engage in when conducting due diligence or underwriting, or when facing a non-performing loan requiring workout and potential foreclosure. Consider also the broad provisions in loan agreements allowing the lender to take action to protect its interests, provisions that may strike environmental regulators as including actions taken by facility owners and operators. These uncertainties led to the oft-cited *Fleet Factors* case in the federal Eleventh Circuit Court of Appeals (*United States v. Fleet Factors Corp.*, 901 F.2d 1550 (11th Cir. 1990)), which stated that even the "capability to control" activities at a facility could give rise to "operator" liability under CERCLA.

The *Fleet Factors* decision led to much consternation in the lending community and ultimately to a number of regulatory and legislative reforms. The reforms culminated in the 1996 enactment of amendments to CERCLA to provide greater clarity and certainty to lenders and fiduciaries. At the state level, notwithstanding the similarities between the federal CERCLA and state HSCA standards of liability, comparable amendments were not enacted – until now.

Delaware's Environmental Lender Liability Reform

In the 2013 Delaware legislative session, the Delaware General Assembly enacted environmental lien legislation to bring Delaware in line with a vast majority of its sister states and the United States with respect to environmental liens, and to provide a tool to protect the State's treasury by recovering money expended by the State on contaminated sites.

During discussions of the environmental lien bill, it was noted that Delaware had not adopted the federal lender liability provisions contained in CERCLA, and the administration committed to address that issue in the 2014 legislative session. The General Assembly has now done so, in the form of three bills (Senate Bill No. 198, House Bill No. 367, and House Bill No. 368) that adopt CERCLA-like lender liability provisions in HSCA, and also in the State's statutes regulating aboveground and underground storage tanks. Senate Bill No. 198, amending HSCA, is instructive of the lender liability provisions provided in the bills.

The HSCA amendments adopt definitions for a "fiduciary" and "lender." A "fiduciary" is defined broadly to include trustees, executors, guardians, and personal representatives. Specifically excluded from the definition of "fiduciary," however, are (i) "A person that is acting as a fiduciary with respect to a trust or other fiduciary estate that was organized for the primary purpose of, or is engaged in, actively carrying on a trade or business for profit, unless the trust or other fiduciary estate was created as part of, or to facilitate, one or more estate plans or because of the incapacity of a natural person" and (ii) "A person that acquires ownership or control of a facility with the objective purpose of avoiding liability of the person or of any other person."

"Lender" is defined to mean:

a. An insured depository institution (as defined in the Federal Deposit Insurance Act at 12 U.S.C. § 1813(c)(2)) or an insured credit union (as defined in the Federal Credit Union Act at 12 U.S.C. § 1752(7)) authorized by law to do business in Delaware;

b. A bank or association chartered under the Farm Credit Act of 1971 (12 U.S.C. § 2001 et seq., as amended) authorized by law to do business in Delaware;

c. A leasing or trust company that is an affiliate of an insured depository institution authorized to do business in Delaware;

d. Any person (including a successor or assignee of any such person) that makes a bona fide extension of credit to or takes or acquires a security interest from a nonaffiliated person;

e. Any legally recognized person authorized to buy or sell loans or interests in loans in a bona fide manner in Delaware;

f. A person that insures or guarantees against a default in the repayment of an extension of credit, or acts as a surety with respect to an extension of credit, to a nonaffiliated person; and

g. A person that provides title insurance and that acquires a facility as a result of assignment or conveyance in the course of underwriting claims and claims settlement.

With these definitions in place, HSCA's standard of liability was amended to specify that a person who acquires, for subsequent disposition, title to or possession of a property to protect a security interest and "does not participate in management of the property" is not liable under HSCA so long as there is no other basis for liability independent from the exemption. Similarly, fiduciaries who have legal title to or manage any property for purposes of administering an estate or trust are exempt.

In general terms, so long as a lender does not "participate in management," the statutory safe harbors will be protective. The term is defined to mean "actually participating in the management or operational affairs of a facility and does not include merely having the capacity to influence, or the unexercised right to control, facility operations." A person that is a lender or fiduciary that holds indicia of ownership primarily to protect a security interest in a property is considered to participate in management only if, while the borrower is still in possession of the property encumbered by the security interest, the person:

- Exercises decision-making control over the environmental compliance related to the facility, such that the person has undertaken responsibility for the hazardous substance handling or disposal practices related to the facility; or
- Exercises control at a level comparable to that of a manager of the facility, such that the person has assumed or manifested responsibility: (i) for the overall management of the facility encompassing day-to-day decision making with respect to environmental compliance; or (ii) overall or substantially all of the operational functions, as distinguished from financial or administrative functions, of the facility other than the function of environmental compliance.

The term "participate in management" does not include performing an act or failing to act prior to the time at which a security interest is created in a property; and, provided the actions do not rise to the level of participating in management above, does not include:

A. Holding a security interest or abandoning or releasing a security interest;

B. Including in the terms of an extension of credit, or in a contract or security agreement relating to the extension, a covenant, warranty, or other term or condition that relates to environmental compliance;

C. Monitoring or enforcing the terms and conditions of the extension of credit or security interest;

D. Monitoring or undertaking one or more inspections of the facility;

E. Requiring a remedy or other lawful means of addressing the release or threatened release of a hazardous substance in connection with the facility prior to, during, or on the expiration of the term of the extension of credit;

F. Providing financial or other advice or counseling in an effort to mitigate, prevent, or cure default or diminution in the value of the facility;

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G. Restructuring, renegotiating, or otherwise agreeing to alter the terms and conditions of the extension of credit or security interest, exercising forbearance;

H. Exercising other remedies that may be available under applicable law for the breach of a term or condition of the extension of credit or security agreement; or

I. Conducting a remedy under this chapter or otherwise under the direction of DNREC.

A person who is a lender that does not otherwise participate in the management of a facility may, after foreclosure, sell, re-lease (in the case of a lease finance transaction), or liquidate the property, maintain business activities, wind up operations, undertake a remedy under HSCA with respect to the facility, or take any other measure to preserve, protect, or prepare the facility prior to sale or disposition. However, such person must seek to sell, re-lease, or otherwise divest the facility at the earliest practicable, commercially reasonable time, on commercially reasonable terms, taking into account market conditions and legal and regulatory requirements.

The HSCA amendments further delineate potential fiduciary liability and provide that the liability of a fiduciary for the release or threatened release of a hazardous substance at, from, or in connection with a facility held in a fiduciary capacity will not exceed the assets held in the fiduciary capacity; provided, however, that the person is not liable under HSCA independently of the person's ownership of a facility as a fiduciary or actions taken in a fiduciary capacity.

The General Assembly enacted similar lender liability reforms in the statutory provision regulating underground storage tanks (USTs). Additionally, in the case of USTs, in the case of foreclosure, a person is not considered an owner if it provides the required in-service or out-of-service notification to the DNREC, and empties all known and registered USTs on foreclosed real property. This provision now imposes affirmative obligations on a foreclosing lender in order to maintain the statutory exemptions from liability.

Underground Storage Tank Liability - A New Era for Owners and Operators

Although not specifically related to lender liability issues, the General Assembly has significantly expanded the scope of liability for owners and operators of USTs, and in some instances this expansion could also impact the interests of a lender.

Historically, the Delaware Underground Storage Act ("DUSTA") was more limited in its scope of liability than HSCA. Under the recently passed legislation, however, DUSTA will impose liability on owners and operators of UST facilities on a retroactive, joint and several basis – subject to several defenses that are intended to alleviate some of the more onerous aspects of this liability scheme.

Significantly, under the amended DUSTA, responsible parties who own, owned, operate, or operated a facility or an underground storage tank located at a facility on or after January 1, 2016, are liable for remediation and corrective action for all released regulated substances on or under the facility, or on or under other real property but that originated or emanated from the facility, regardless of whether any responsible party proximately caused any release, and regardless of when and how the regulated substances were released. The ownership or operational association with the facility establishes the nexus for liability under this section to attach to these responsible parties. These new liability provisions are to become effective in January 2016 and apply to ownership or operation of tanks after that date.

The defenses to liability for a potentially responsible party under the new statutory scheme are limited. First, a potentially responsible party will not be liable for regulated substances if it can establish that the release was caused solely by an act of God, an act of war, or, in certain instances, the act or omission of certain third-parties. The third-party defense applies to an act or omission of a third party other than:

(1) an employee or agent of the responsible party; or

(2) any person whose act or omission occurs in connection with a contractual relationship, existing directly or indirectly, with the responsible party, but not including a contractual relationship in connection with the sale or transfer of the facility by or from the responsible party to a third party.

(3) This defense applies only when the responsible party asserting the defense has exercised due care with respect to the facility, the foreseeable acts or omissions of the third party, and the foreseeable consequences of those acts or omissions. However, notwithstanding the foregoing, where the relationship arises in connection with the sale or transfer of the facility by or from the responsible party to a third party, the defense applies if the responsible party asserting the defense has exercised due care with respect to the facility during the period of ownership or operation of the facility by the responsible party, and with regard to the foreseeable acts or omissions of the third party based on the responsible party's knowledge and information at the time of sale or transfer of the facility.

The third-party defense is complex (at best) and reflects a compromise among the differing interests that surfaced in the legislative process. The third-party defense will, in some cases, protect an owner/operator who did not cause a release, and who exercised due care with respect to the facility. The third-party defense will place a premium on good record-keeping and sound due diligence that documents the existing set of conditions at the time of facility transfer.

Second, a potentially responsible party will not be liable for regulated substances that were released before the time period when the party owned or operated the facility and/or underground storage tank, only if it had no knowledge or reason to know, at the commencement of its ownership or operation, of any prior release. To establish that it had no reason to know of any prior release, the potentially responsible party must demonstrate that on or before the date on which it acquired or began operations at the facility, all appropriate inquiries, as provided in DUTSA, were carried out into the previous ownership and operation of the facility in accordance with generally accepted good commercial and customary standards and practices. This exemption does not affect or diminish the liability of a responsible party who, by any act or omission, caused or contributed to the release of regulated substances.

The DUTSA amendments provide for an express right of contribution among responsible parties. In resolving contribution claims, the Delaware Superior Court may allocate costs among the responsible parties using such principles of fairness and justice as the Superior Court deems appropriate.

What's A Lender to Do?

In all likelihood, most lenders and institutional fiduciaries in Delaware have well-developed environmental due diligence procedures and guidance, tailored to the federal CERCLA lender liability provisions. Although the Delaware reforms to HSCA and the other state statutes are similar, a review of the applicable policies and guidance may be warranted to ensure consistency with the new state-specific provisions. In addition, the specific new defenses in the Delaware Underground Storage Tank Act warrant consideration to ensure that those provisions have been adequately addressed.

In the context of due diligence and loan underwriting, lenders should be mindful of existing environmental guidelines and policies, and ensure that borrowers and their due diligence environmental consultants perform in accordance with the statutory provisions. In many cases, once a loan is funded and a borrower is performing, the newly enacted legislation may have little actual impact on the lender's activities.

In the context of a non-performing loan, and especially in the case of workout or foreclosure actions, special attention is warranted since the lender's activities in those circumstances may resemble more closely the "participation in management" of an impacted site. Importantly, the new provision of DUSTA imposes certain affirmative, post-foreclosure obligations on a lender to maintain the exceptions from liability. In some cases, assessment of the loan and collateral value may warrant actions other than traditional foreclosure, and involvement of the responsible state agencies may be warranted to seek additional certainty.

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NJSA Statute

Another View

Utilizing Nonjudicial Settlement Agreements to Modify Trusts

by Michael M. Gordon, Esq. and
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Since the enactment of Delaware's nonjudicial settlement agreement statute, 12 Del. C. § 3338 (the "NJSA Statute") in 2013, trust practitioners and trust industry professionals have debated whether the NJSA statute may be used to modify trust provisions. For several reasons, we believe that it can.

The plain wording of the NJSA statute, modeled after Section 111 of the Uniform Trust Code (the "UTC"), is purposely broad and allows the interested persons to enter into a NJSA with respect to "any matter" involving a trust. The phrase "any matter" is inclusive rather than restrictive, suggesting that the presumption should be that any matter does fall within the proper subject matter of a NJSA rather than not. In fact, jurisdictions that have adopted similar statutes but did not want NJSAs to be used to modify trusts, such as Iowa and Michigan, have found it necessary to explicitly state this restriction in the statute to counteract the otherwise expansive language contained in Section 111 of the UTC.
Further, the non-exclusive list of matters under paragraph (d) of the NJSA Statute that can be resolved by a NJSA includes the ability to grant a trustee "any necessary or desirable power." Use of a nonjudicial settlement agreement in this manner would logically include necessary or desirable powers not already granted in the trust (otherwise the use of a NJSA to grant such powers would be unnecessary), and, as such, would effectuate a de facto trust modification.

Paragraph (c) of the NJSA Statute provides that a NJSA is valid "only to the extent it does not violate a material purpose of the trust and includes terms and conditions that could be properly approved by the Court of Chancery." The vast majority of trust modifications are purely administrative in nature and would not violate a material purpose of a trust. Furthermore, if the settlor of the trust is living at the time a NJSA is contemplated, then the issue of whether a material purpose of the trust is being violated is largely moot. The settlor can be asked to represent that any attendant changes to the trust effectuated by the NJSA do not violate a material purpose of the trust and are consistent with the settlor's intentions in creating the trust. Finally, the requirement imposed by paragraph (c) of the NJSA Statute that the NJSA is valid only to the extent it includes terms and conditions that could properly be approved by the Court of Chancery does not impose any impediment to using the NJSA Statute to modify trusts, as the Court of Chancery routinely enters orders modifying trusts.

Although it is true that, due to the short period of time since the NJSA Statute was enacted, no Delaware case has approved the use of a NJSA to modify a trust, the same may be said of other nonjudicial methods to modify a trust under Delaware law, such as decanting. In fact, one could easily surmise that the Court might look more favorably upon the use of a NJSA for such purposes due to the language of paragraph (a) of the NJSA Statute, which requires all "interested persons" to sign the NJSA effectively builds in the considerable protections set forth in Court's own Rule 101(a)(7) relating to consent petitions. In contrast, decanting and merger do not even require notice to beneficiaries who would otherwise need to sign off in connection with a consent petition. In short, when contemplating how the Court would look upon this issue, Trustees may want to consider that a NJSA is far more akin to a consent petition than decanting or merger.

A Trustee might find a NJSA preferable to decanting or merger due to the ability to incorporate consent and release language in a single, cohesive document. Further, although the Trustee must exercise some level of discretion to sign a NJSA, the Trustee's signature has no effect on the trust until all other parties have signed, in contrast to decanting or merger, where the Trustee's discretion is the sole determinative act under the applicable statute.

Trustees should consider NJSAs as a valuable tool that may be used to modify trusts, especially when the trust's grantor is living. Indeed, the protections that the NJSA Statute affords to trust beneficiaries may make this a more attractive approach than other nonjudicial options for modifying trusts.

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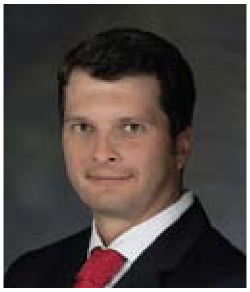

A Matter of Trust

by
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"As regulation evolves, and the often informal thinking of regulators evolves, there is sometimes pushback on certain common estate planning techniques. "

Regulatory Trends Affecting Trust Administration

Bankers are well aware that the regulatory environment has changed dramatically over the last five years. Much of this alphabet soup of regulation is designed to impact the risk appetite banks are willing to absorb. This article will examine the potential impact of one proposed new regulatory guideline as well as some trends that will influence how banks administer trusts.

Recently, the Office of the Comptroller of the Currency (OCC) has issued a Notice of Proposed Rulemaking (NPR) asking for public comment on proposed "Heightened Expectations Guidelines" to establish minimum standards for the design and implementation of risk governance frameworks by certain large banks and minimum standards for Boards of Directors. While the guidelines would generally apply to banks that exceed a $50 billion in asset threshold, the OCC reserves the right to apply the Heightened Expectations Guidelines to institutions that do not meet the threshold.

The Guidelines will apply to three specific risk management related roles; the bank's "front line" units, independent risk management and internal audit. The Guideline's detailed requirements regarding roles, responsibilities and reporting structures would represent a significantly increased level of regulatory intervention in bank management and internal processes. As the OCC moves away from recommendations in favor of Matters Requiring Attention (MRA's), it is expected that these Guidelines will become more stringently enforced.

The "Front Line" aspect of the Guidelines, encompassing sales, acceptance and trust administration will most likely be influenced by more controls and less risk taking. If approved as proposed, expect banks to struggle in implementing stronger Front Line controls as a great deal of trust administration involves highly skilled and experienced individuals making subjective decisions. Quality assurance is a large element of the Guidelines and some banks may have to change processes to align risk and strategy. The bottom line is that if implemented as proposed, banks will most likely take on less risk in acceptance and distribution decisions. Drafters should consider whether some trusts are better drafted as directed rather than discretionary to address the risk issues the banks will face when administering certain unique and hard to value assets

As regulation evolves, and the often informal thinking of regulators evolves, there is sometimes pushback on certain common estate planning techniques. Where a bank cannot control or diversify an asset, it cannot exercise certain duties fundamental to being the trustee. Again, consider whether certain assets within a trust would be easier to administer as directed trusts. Further, if this trend takes hold, it may be an opportunity to work with the beneficiaries to pro-actively modernize the trust.

Certain issues have been trending for a while, but still occasionally find themselves in new documents. Having a bank responsible for making subjective decisions on issues such as morality or chemical dependency are difficult to administer. In areas where the grantor has concern over such issues it may be best to put the onus on the beneficiary. In addition, in situations where individual co-trustees have the ability to out vote a corporate trustee, the corporate trustee may wish to evaluate whether it should remain corporate trustee or resign

The above are but a few of the things that are beginning to influence how banks administer trusts. While it is not always possible to account for every nuance, many issues can be easily addressed in advance through building flexibility into documents, using directed structures where it makes sense and working closely with banks to understand what influences their decision making.

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September - October 2014

September 30th and October 1st –
2014 Delaware Trust Conference. Hotel du Pont, Wilmington.

The 2014 Delaware Trust Conference presents a novel approach to wealth planning. This, the ninth annual edition of this premiere trust event will feature detailed case studies to tell the story of the Delaware Trust advantage. Join dozens of expert panelists from the trust, legal, and accounting fields to learn the latest Delaware Exclusive information. Learn how to meet your clients' great expectations in both the best of times and the worst of times with unique Delaware trust strategies.

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November 18th, 19th, and 20th -
2014 Regulatory Compliance School.
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The Delaware Bankers Association and FIS Enterprise Governance, Risk & Compliance (EGRC) Solutions present the 2014 Regulatory Compliance School offering a comprehensive review of federal laws and regulations affecting the financial services industry. Keep current on the important changes in the Regs you deal with every day on the job, and earn CPE, CRCM, DE and PA CLE continuing education credit!

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December 9th -
Bank Secrecy Act Compliance & Anti-Money Laundering Seminar
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Fulfill your federal BSA training requirements and avoid regulatory pitfalls. Attend this one-day session presented by the DBA and FIS Enterprise Governance, Risk & Compliance (EGRC) Solutions.

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For more information, or to register, please visit the Web Seminar link at www.debankers.com. The DBA has introduced an improved web seminar catalog featuring an easy to view, searchable listing. There is no log-in required to view the catalog. The checkout function has also been improved and includes itemized receipts.

August - September 2014

August 5 - Fair Lending Update

August 6 - BSA/AML Compliance: Recent Developments & Common Errors

August 7 - Security: Some Assembly Required

August 8 - Advanced Call Report: Revisions & Update

August 11 - I Knew Something Was Wrong

August 12 - Advanced Call Report: RC-R, Risk-Based Capital

August 13 - 2014 Integrated Disclosures: New Loan Estimate

August 18 - Lending Basics for Support Personnel

August 20 - 2014 Integrated Disclosures: New Closing Disclosure

August 21 - All Things Credit

August 22 - Branch Strategy Workshop

August 25 - Analyzing Business Financial Statements

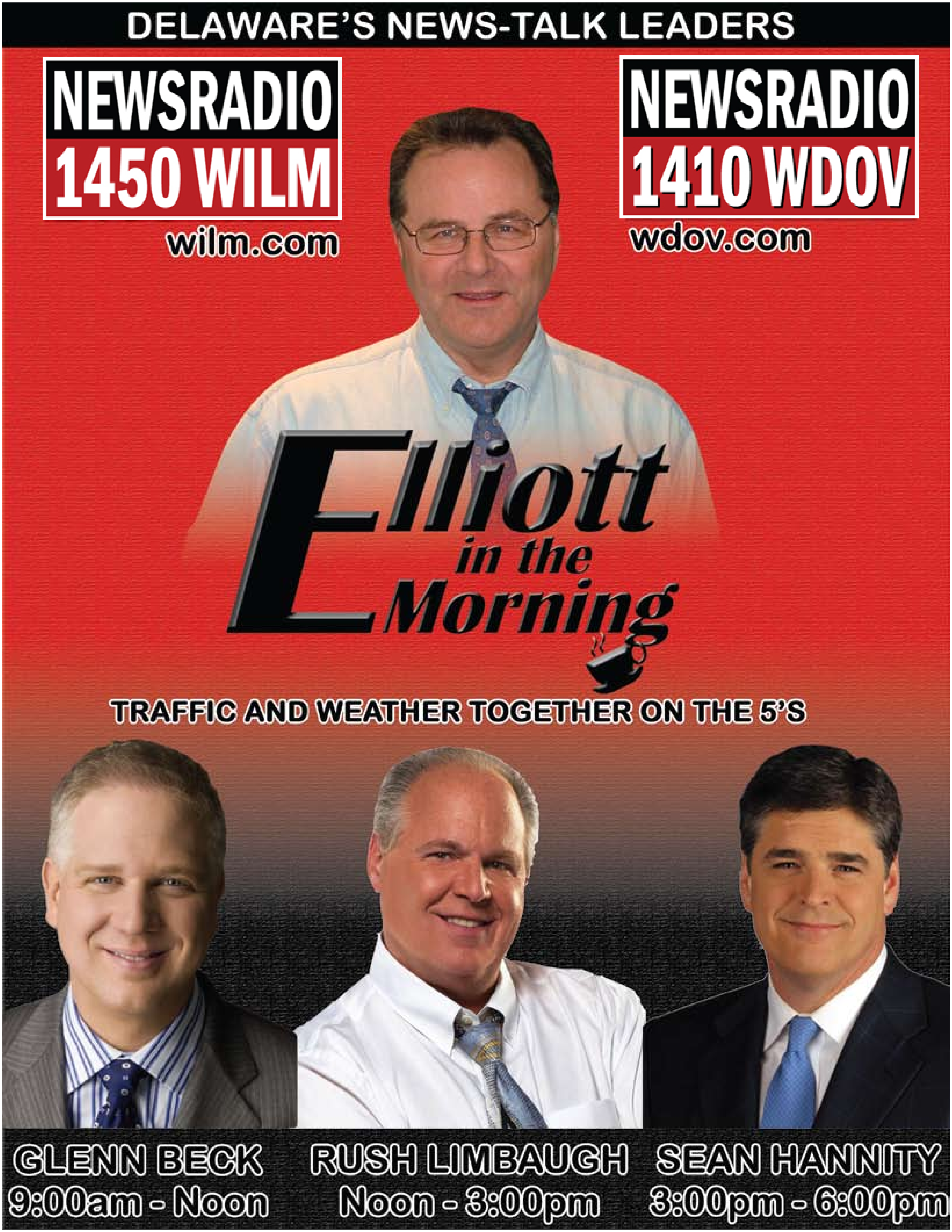
August 26 - Advanced Call Report: Regulatory Report Preparation of FR Y-9C

August 28 - Analyzing Business Cash Flow

September 3 - Walking Through the Maze of an ACH Audit & Risk Assessment

September 5 - Overdraft Priviledge Programs Update & Review 2014

September 9 - The Four C's of Exceptional Supervision



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GLENN BECK
9:00am - Noon
RUSH LIMBAUGH
Noon - 3:00pm
SEAN HANNITY
3:00pm - 6:00pm

Employment Law Update

by
Scott A. Holt, Esq.
Young Conaway Stargatt & Taylor, LLP

"Many financial sector employers require those who have significant client contact to sign non-solicitation agreements."

Protecting Your Most Valuable Asset

Significant time, money, and resources often goes into developing client relationships, so it is only natural that businesses take appropriate steps to protect these intangible assets. Many financial sector employers require those who have significant client contact to sign non-solicitation agreements.

However, executing and enforcing that agreement are two different matters. Customer non-solicitation agreements, like traditional non-competes, are considered restraints on trade, and most courts will enforce them only if they are "reasonable."

In considering reasonableness, Courts will traditionally assess three factors: 1) the employer's interest in protecting its business; 2) the employee's right to earn a living; and 3) the public's interest in competitive markets. Following is practical guidance to increase the likelihood that an agreement is enforced.

Be Clear About What You Are Trying to Protect

The most widely recognized protectable interest a business's goodwill with its customers. Most jurisdictions recognize that a company has an interest in protecting its client relationships against departing employees. This is particularly true where the employee had personal contact with clients.

Courts have also recognized that companies have a right to protect their confidential information by prohibiting former employees from soliciting clients. Courts may restrict a former employee from soliciting customers even if that employee had no direct contact, if the employee gained significant knowledge of those customers during his employment. But note that the information must be of such confidential nature that it would give the former employee an unfair competitive advantage. This rule excludes general knowledge or skills acquired during employment or information that is publicly available.

Set a Reasonable Time Period

Non-solicitation agreements must have a reasonable time limit. This is often interpreted to be the period needed for the company to rebuild its customer relationships. The determination is fact specific and case specific.

In some instances, a period of several months is reasonable. If the selling or servicing of the relationship is complex, a longer period may be justified.

Courts in Delaware generally presumed that restrictions of two years or less are reasonable. Longer periods may be necessary if the former employee had access to confidential information.

Avoid the "I Didn't Solicit Them; They Called Me" Defense

A common defense invoked by former employees is that they did not "solicit" the customer. Where the term "solicit" is not defined, courts typically defer to the dictionary definition, and will take into account public policy considerations.

Employers can avoid this uncertainty by specifying that a former employee may not accept business from the employer's customers. Many jurisdictions will enforce such language.

Consider a Liquidated Damages Provision

Finally, consider including a liquidated damages provision. It is usually easier to sue for money than obtain injunctive relief from a court, and the potential for a significant award may make the employee think twice about poaching clients.

In order for a liquidated damages provision to be enforceable, it must be a reasonable estimate of the loss likely to be suffered, yet relate to an injury incapable of accurate estimate. Estimates might include the payments made by the solicited customer to the former employer during a certain time frame.

Scott Holt is a partner at Young Conaway Stargatt & Taylor, LLP and member of the Firms' Unfair Competition and Trade Secret Counseling and Litigation practice groups.