

Workouts Principles - Memorandum of Understanding CSAF members

The **Council on Smallholder Agricultural Finance (CSAF)** is the leading global network of lending practitioners promoting an inclusive financial market for producer organizations and small- and medium-enterprises (SMEs) in the agriculture sector. Since 2013, CSAF's 16 members and affiliates have provided \$5B in lending to agricultural SMEs providing market access for 3.4M smallholder farmers across 65 countries in Africa, Asia, and Latin America. Loan sizes typically range from \$100,000 – \$3 million. CSAF has three workstreams focused on:

- Market Growth to meet the growing demand for financing among inclusive agricultural SMEs
- Responsible Lending Practices to ensure that market growth contributes to positive impact on agricultural businesses and the long-term sustainability of the sector
- Social & Environmental Impact that contributes positively to farmer and worker livelihoods as well as to agricultural and agro-forestry landscapes and ecosystems

CSAF members and affiliates include: AgDevCo, Alterfin, Common Fund for Commodities, Cordaid Investment Management, Global Partnerships, Grameen Credit Agricole Foundation, Incofin Investment Management, MCE Social Capital, Oikocredit, Rabo Rural Fund, responsAbility Investments AG, Root Capital, Shared Interest Society, SIDI, SME Impact Fund, and Triodos Investment Management.

1. Introduction

Increased co-lending by CSAF members has generated positive collaboration between lenders, resulting in additional funds for the borrowers, additional technical assistance, and a reduced burden in terms of reporting and coordination. In some instances, however, there has been a lack of coordination with sub-optimal outcomes for lenders and borrowers alike. The need for clearer principles and protocols for loan restructuring and workouts is magnified in the current environment given the uncertainties related to the COVID disruptions.

Although members are cautiously optimistic about the future, taking a proactive approach to potential repayment challenges will increase the capacity of borrowers in continuing as a going concern by streamlining negotiation processes and opening up new sources of financing. This will also result in minimizing potential financial losses for all, in addition to strengthening CSAF members' relationships with one another.

Additionally, members recognize that while the spirit of the CSAF responsible lending principles creates an expectation that members communicate openly during a loan workout, the lack of clear guidelines means that members can interpret the principles subjectively.

To reduce confusion going forward, CSAF members decided in November 2020 to develop more explicit expectations for loan workouts. Workshops on Loan Workouts were held in March 2021 to help CSAF members focus on the general principles and practices, drawing from experiences in adjacent sectors such as corporate lending and microfinance.

Following these Workshops, CSAF established a Workouts Working Group ("WWG") to develop basic principles, outlined in this MOU, that members can follow during loan restructurings and workouts. These principles are in line with the [CSAF Responsible Lending Principles](#), especially "trusted information sharing and collaboration", "working together", and "fair treatment". They are based on i) a review of documents produced by the CSAF members, [ii\) a process mapping exercise](#), and iii) nine sessions with the WWG consisting of four CSAF members, and on iv) inputs provided by six other CSAF members in one-on-one calls. **This MOU provides indicative guidelines** on best practices that can be applied in most workouts cases; however, it is recognized that specific circumstances vary and these guidelines are not intended to be legally binding or applied rigidly. For clients that may be acting in bad faith, these principles may not be as applicable. Ultimately, the legally binding agreements between lenders and borrowers take precedence.

The MoU text below has also been drafted using content of other similar documents regarding [coordination among microfinance investment funds in response to COVID-19](#), and [key principles to protect microfinance and their clients in the COVID-19 crisis](#).

2. Challenges and Principles

2.1. Collaboration when two or more lenders provide a loan to the same client

Key Challenge	Principle
<p>Collaboration between lenders from the outset is a key success factor that facilitates the workouts organization required in case of issues with repayment. This begins with communication when a new CSAF lender considers financing a business already receiving financing from another CSAF lender and continues through the life cycle of the loan and subsequent loan renewals. It is sometimes a challenge to coordinate the renewal of the loan when the lending decisions of some of the lenders change - as they may decide not to renew a loan, or not the same amount - while the agricultural business has some specific expectations and needs (particularly related to timing given harvest cycles) in terms of working capital.</p>	<p>Whenever possible, lenders should communicate and collaborate as soon as they contemplate lending to the same client. It is the responsibility of the new lender to consult existing lenders prior to entering into a relationship with a borrower. Lenders should obtain permission from the borrower in accordance with the terms of bilateral agreements before sharing any information that is not in the public domain.</p> <p>Points of coordination include: existing lenders sharing appropriate information with a new lender; loan monitoring; early warning signs; technical assistance;¹ and contingency planning. In addition, lenders should coordinate with the agricultural business to inform the other lenders in a timely manner in case of default or material concerns about financial performance of their common client.</p> <p>Appropriate coordination of the lenders for loan renewal leads to better results. When a lender experiences material delays in financing a common borrower or decides not to renew financing a borrower, it should share this decision with the other lenders as soon as possible as any delays or reductions in financing the borrower’s agricultural season may jeopardize the investment of all the lenders. In cases where several lenders have a significant exposure to the same borrower, which often builds up over several years of progressively larger lending, lenders are encouraged (1) to adopt a sensible lending approach, so as not to overburden the balance sheet with liabilities, and (2) to sign an inter-creditor agreement (including some clauses to protect the confidentiality of the client).</p>

¹ When the agricultural business of the customer is a going concern, the technical assistance is most useful for business strengthening (not yet for turn-around). In this case it is advised that the client pays a portion of the technical assistance. Having an early technical assistance relationship with a customer improves the results of a subsequent technical assistance intervention regarding turn around.

2.2. Organization of the credit group when initiating a loan workout

Key Challenge	Principle
<p>In order to facilitate the monitoring of an agricultural business that has had a default or where one of the lenders has a material concern, the constitution of a lenders group is essential and information sharing is vital to manage the crisis. The agricultural business should communicate transparently with all its lenders, in accordance with the principle of fair treatment of each lender. This in turn applies to the lenders themselves, who are also responsible for the smooth running of the lenders group. Though lenders need additional information beyond regular reporting requirements at this time, their intention is not to overburden the agricultural business and its staff.</p>	<p>We recognize that the interests of all stakeholders are better served in the long run and across multiple workout situations by coordinating efforts. In a loan workout situation, we agree on designating a leader among the lenders in each lenders group (often the creditor with the largest exposure to the debtor, or with particular expertise in managing informal workout negotiations), to facilitate coordination within the group and with the client. A steering committee can also be used to represent interests of the smaller lenders. We agree that the lender’s group needs to be careful to establish a balanced and fair relationship with the client to avoid imposing any unilateral decisions. Dialogue and transparent communication remain key.</p> <p>We agree that the additional information requested from the client in this time of crisis shall be harmonized between lenders, with appropriate permission from the borrower, not to be unreasonably withheld. The debtor should provide all lenders with equal access to relevant information simultaneously. This information may include business continuity plans, stress tests, liquidity plans, country updates, and increased frequency of reporting.</p>

2.3. Coordination of Technical Assistance (TA)

Key challenge	Principle
<p>Not all clients have the same capacity to work on projections or liquidity analysis. This is especially true for smaller clients. Some clients have already started</p>	<p>We acknowledge that managing financial stress may be beyond the professional ability of the debtor’s management. We should therefore consider identifying and paying for technical assistance for necessary special analysts, to facilitate</p>

<p>asking for help in obtaining tools to monitor the COVID crisis and anticipate its future consequences (or other shocks / crises that may arise in the future). Technical assistance programmes could be proposed to clients depending on their needs and capacities.</p> <p>Technical assistance tends to be most relevant for a larger group of lenders with mature partners (and large joint exposure) because providing technical assistance to clients with small loans is often too expensive relative to the lender exposure. It is often useful to plan for technical assistance to continue for a longer time period beyond initial assessment.</p>	<p>turnaround planning, and to review restructuring decisions proposed by management.</p> <p>We agree to coordinate technical assistance and training efforts and resources among CSAF Lenders, in order to avoid duplication, improve efficiency of TA delivery, and amplify knowledge-sharing amongst stakeholders. The coordination of the technical assistance should be managed by one lender, ideally the leader of the group of lenders (assuming the lead lender has the capacity to do so), with input from the other lenders. The technical assistance agenda must also work on identifying potential funding for such new programmes.</p> <p>In situations where lenders have access to funds for technical assistance, the cost of the technical assistance should be covered by lenders pro-rata unless it is otherwise agreed. In some instances, and for some specific types of technical assistance, it can be covered to a larger extent by an equity investor (over a lender).</p>
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3. Restructuring Protocols

3.1. Shared goal of a long-term, going-concern solution

When a borrower is in financial trouble, all relevant creditors should be prepared to collaborate and give sufficient time to the debtor to produce a turnaround plan. We aim at making our best effort to preserve and maximize the long-term, going-concern value of the debtor’s agricultural business for the benefit of all involved parties, including farmer suppliers and employees.

3.2. Timely and effective creditor coordination

If the agricultural business is deemed to be viable, we will favour prompt solutions (as possible and feasible) through timely lenders group coordination and handshake agreements. This will help agricultural businesses create a feasible plan that rolls over, reschedules, restructures, or

refinances the debt before it is in danger of default. The handshake agreement will include, among other things, mutual expectations regarding the confidentiality of the information shared between the parties and undertaking from each participating lender not to take unilateral enforcement actions. We will cooperate to design formal agreements at a later stage if required due to the severity of the restructuring required.

3.3. Reasonable period of standstill and moratorium

During this period of coordination to establish the terms of restructuring, all lenders pledge to refrain from enforcing claims unilaterally to reduce exposure as lenders acknowledge that their positions are better served by a going concern of the borrower. During this period, lenders should communicate to borrowers that they are expected not to take any action that might affect the relative position of the creditors. Lenders should refrain from initiating any action with the borrower to improve their seniority relative to other lenders. We are willing to cooperate in giving a reasonable period of relief and timely moratorium to a viable debtor (an agricultural business that is solvent and acting in good faith). We will exercise restraint during that time from enforcing our claims against, or reducing our exposure to, the debtor agricultural business. If and when required due to the severity of the crisis, a more formal agreement may be signed. We agree to make our best effort to provide specific, time-bound, and limited covenant breach waivers to give the institution needed breathing room. We will be transparent with other lenders on our existing covenants and related waivers with the agricultural business, with appropriate permission from the borrower, not to be unreasonably withheld, and agree to harmonize them as much as possible.

3.4. Legal and regulatory regime applicable to the debtor client

If and when required due to the severity of the crisis, we will engage reliable local counsel to ensure that formal agreements are enforceable and adapted to the legal and regulatory requirements in the country where the borrower is domiciled. Whenever possible, proposals to solve financial difficulties should reflect the applicable law and relative positions of all creditors.

3.5. Transparency and Conflicts of Interest disclosed

The restructuring process should be transparent to all stakeholders. Communication between the lenders and with the borrower should be coordinated by the Lenders Group and not unilaterally. Local banks might not follow the same principles or might not be willing to compromise seniority for the sake of a long-term, going-concern solution. Interaction with non-CSAF lenders, their inclusion in the Group, and ultimately their inclusion in the restructuring process should be managed on a case-by-case basis. Each creditor should disclose at the outset to the other lenders the extent and nature of their relationship to the debtor.

3.6. Flexibility, responsiveness and priority status of additional debt funding

Additional debt funding will often be needed to ensure the continued access of agricultural businesses and their clients. Creditors shall be responsive and look for flexible solutions to help

agricultural businesses access short-term funding. When exploring a funding opportunity from a new creditor, the debtor agricultural business shall inform the existing lenders and request a non-objection from its lenders before it signs the new agreement. If a lenders group is formally constituted in a workouts situation and one or more lenders is willing to inject liquidity, it is reasonable in most cases for that additional capital to be senior in position relative to existing financing for the business.

3.7. Debtor client's responsibility for workout costs

In case of workout costs, the lenders acknowledge that the debtor's agricultural business is responsible for the costs of the voluntary workout when lenders are enforcing their claims. To the extent such costs are under the control of lenders, however, these costs should be both clearly defined and minimized. The cost should be covered based on each lender's respective exposure.

4. Rescheduling Approach

4.1. Rescheduling approaches for ordinary renewals or ordinary restructuring

The restructuring approaches concern mainly clients where neither fraud nor severe governance issues have been identified. In the case of stronger clients requesting additional liquidity who demonstrate low risk of solvency shortage, low-medium risk of liquidity shortage, and low operational stress with no existing payment defaults: these clients generally have the capacity to overcome crisis with no extensive restructuring required as some key lenders can offer the required funding. It is in the best interest of the client and lenders for lenders to renew loans of stronger clients. In line with the principle of collaboration, it is recommended that CSAF Lenders in consultation with the client continue to coordinate with other relevant lenders before providing fresh funding to share views and ensure alignment.

On the other hand, when weaker clients show substantial risk of solvency shortage and a high liquidity risk, going concern becomes at risk. The client may be unable to overcome the crisis and honor its debts or even ordinary expenses, and additional capital is required. Clients may request liquidity support directly, including rescheduling of payments, or CSAF Lenders may raise an alarm. Such scenarios surpass the scope of this MOU document and should be deferred to the Lenders' respective restructuring processes, recovery specialists, and legal teams.

In between these two scenarios are cases in which going concern clients are low- or medium-risk and need support from a wider group of lenders in either an informally coordinated manner or through formally coordinated and binding support, but not arising to the point of a formal Restructuring Agreement. Further guidance on best practices for these rescheduling approaches are provided in the following sections.

4.2. Handshake agreements for low/medium risk going concern clients

Some going concern clients may be expected to recover relatively quickly after a difficult financial year or harvest, and demonstrate low risk of solvency shortage and medium, temporary risk of liquidity shortage. In these cases, concerted action between CSAF Lenders is needed, focused on rapid assurance that moratorium on principal payments or coordinated rollover of principal instalments will be adequate to stabilize the funding base. Such clients may have requested liquidity support (rescheduling of payments or payment moratorium), or evidence of support is demonstrated at the initiative of the Lender's calling for concerted actions in anticipation of liquidity risk.

In such scenarios, the 1-2 CSAF Lenders with the largest outstanding exposure are likely to lead the lenders group to coordinate close cooperation of the client. It is presumed that the scenario can be resolved through a standard, non-legally binding handshake agreement (e.g. via email) between all CSAF Lenders who hold significant exposure to prolong, resolve, or terminate any previously standing informal agreements. The informal agreement between lenders should subsequently be reflected formally in bilateral agreements with clients. CSAF Lenders may agree on coordinated rescheduling timelines, the most common version of which is modifying principal maturities of previous bilateral agreements.² At the end of the handshake payment holiday period, the way forward (getting back to normality, extension of the payment holiday or restructuring project) should be agreed among the CSAF Lenders.

4.3. Legally binding agreements for low/medium risk going concern clients

In the case of going concern clients, when there is less certainty as to the client's ability to get back to the original repayment schedule, a more formal process is required to sustain the client involving support from a wider group. This may include international lenders, local lenders, shareholders and other stakeholders.

In such scenarios, the 1-2 CSAF Lenders with the largest outstanding exposure are likely to lead the lenders group to coordinate close cooperation of the client. It is recommended that Lenders formalize a legally binding agreement drafted by an external legal counsel to prolong, resolve or terminate current handshake agreement. Lenders may choose to include a governance framework and consider a unified set of financial covenants. In such an agreement, Lenders may agree on coordinated rescheduling timelines regarding principal payments as well as actions to be taken in the case of payment defaults and breaches of covenants. It is anticipated that higher hedging costs may affect loan terms and conditions and may be taken into consideration. At the

² In more complex cases: a unified set of financial covenants may be considered by the CSAF Lenders. The covenants should include common terms across the CSAF Lenders during the defined period.

end of the handshake payment holiday period, the way forward (getting back to normality, extension of the payment holiday or restructuring project) should be agreed among the Lenders.

5. Standards

CSAF Lenders commit to the following principles in their approach to loan workouts and restructuring:

- **Going concern.** Voluntary debt restructuring, standstill and workouts are aimed at preserving and maximizing the long-term, going-concern value of the client for the benefit of all involved parties.
- **Tolerance.** CSAF Lenders accept that, from time to time and as long as these are exceptions rather than the rule, members in the group may not be able to follow on a collective action taken by the group, due to objective constraints of their funds/investors (i.e. liquidity). When an individual lender is not able to align with the rest of the Lender Group, that lender is responsible for communicating transparently and proactively so that the other lenders are aware and can make informed decisions about how to proceed.
- **Additional support.** CSAF Lenders acknowledge that providing extra support or fresh funding during stressed times can have big positive effects to the benefit of the client and all its stakeholders. This should be encouraged and supported. Loans provided during these times will be recognized as such and may be treated with some preference. To be determined on a case-by-case basis. Each lender pledges to contribute its fair share of support within its capabilities and mandates.
- **No general critical mass.** CSAF Lenders may not always hold a majority of debt in clients but they are very likely to represent a substantial part of foreign lenders. As the group shows cohesion, it is expected that the signal sent to other lenders, particularly international ones, will encourage them to joint efforts of pragmatic, agile and empathetic coordination of support to clients. Therefore, it is accepted that general critical mass of debt to clients on a case-by-case basis is not required under situations requiring intervention through ordinary renewals or handshake agreements.
- **Free lunch treatment.** Notwithstanding the above-mentioned principle of tolerance, CSAF Lenders who cannot participate in an informal handshake agreement are encouraged to offer alternatives to mitigate the effects of their inability to follow and avoid falling into legally binding agreements or formal restructuring. These alternatives may include for example proposals of haircuts or simple commitment to continue forbearing payment (as opposed to switching to rescheduling agreements).

- **Fair-burden:** CSAF Lenders pledge to apply the principle of fair-burden sharing among stakeholders.
- **Local lenders.** If local lenders (or any lenders) are not included in these agreements, borrowers should provide updates if any moratorium or rescheduling has taken place.
- **Breaches of covenant.** CSAF Lenders may opt to waive breaches of financial or technical covenants in some circumstances, even informally. In the event that lenders decide to send borrowers Reservation of Rights (RoR) letters in accordance with their fiduciary duty, lenders commit to inform peer lenders before or upon sending their RoR letter.
- **Non-Acceleration.** Without prejudice to CSAF Lenders' rights reservation and in the case of non-payment of principal or financial covenant breaches by a going-concern borrower, subject to the approval of the investment/credit committees of each lender, CSAF Lenders pledge to exercise restraint from accelerating their respective loan agreements until a "handshake agreement" is reached or formal restructuring is properly formalized.
- **Hedging arrangements.** For local currency loans with hedging arrangements, respective hedging strategies to be elaborated individually by each CSAF Lender. It may include hedge rollover, conversion into USD/EUR or a different option. The creditors shall together strive to minimize the impact for the borrowers of additional hedging costs related to debt work out. The creditors shall strive not to increase the borrower's exposure to foreign exchange risk, beyond what it is able to manage and to absorb.