

**Date:** [Insert Date]

**To:** Chief Executive Officers and Boards of Directors of All Supervised Financial Institutions

**Subject:** Interagency Supervisory Guidance on Leveraged Lending Activities

### **1. Purpose**

The purpose of this letter is to provide updated guidance to financial institutions regarding expectations for sound risk management practices in leveraged lending activities. This guidance replaces previous communications and addresses the cumulative risks associated with the leveraged loan market.

### **2. Scope**

This guidance applies to all supervised financial institutions engaged in leveraged lending activities, including the underwriting, syndication, and holding of leveraged loans.

### **3. Definition of Leveraged Lending**

Institutions are expected to maintain a clear and consistent internal definition of leveraged lending. Common characteristics include:

- Loans used for buyouts, acquisitions, or capital distributions.
- Debt-to-EBITDA ratios exceeding industry standards (e.g., total debt to EBITDA exceeding 4x or 6x).
- High debt service coverage ratios or lack of traditional maintenance covenants.

### **4. Risk Management Expectations**

Supervisors expect institutions to demonstrate:

- **Underwriting Standards:** Realistic repayment assessments and the ability for the borrower to amortize a significant portion of senior debt or total debt over a reasonable period.
- **Pipeline Management:** Robust monitoring of market conditions and the ability to manage "hung" positions in the event of market disruptions.
- **Risk Rating:** Accurate internal credit risk ratings that reflect the high-leverage profile and potential for volatility.
- **Stress Testing:** Regular portfolio stress testing to evaluate the impact of economic downturns on borrower default rates and recovery values.

### **5. Documentation and Reporting**

Institutions must maintain comprehensive documentation of their leveraged lending risk appetite, limit structures, and exception reporting. Management should provide regular reports to the Board of Directors regarding concentrations and policy compliance.

### **6. Supervisory Review**

Examiners will review leveraged lending activities as part of the safety and soundness

examination process. Institutions failing to demonstrate adequate risk management may be subject to supervisory action or increased capital requirements.

Sincerely,

[Authorized Signature]

[Title of Regulatory Official]

[Name of Agency]