

Fund Finance Friday



LSTA Publishes New Forms of Term SOFR Amendments

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The LIBOR transition process continues to roll along. New transactions are (mostly) being closed without using LIBOR any more, and many legacy transactions are naturally transitioning when refinanced or renewed this year. However, a significant portion of the legacy loan market remains that will require active transition at or before LIBOR cessation on June 30, 2023. In order to help members think through the process, the LSTA has produced and distributed a series of **amendment forms** (LSTA membership required to access forms) that may be used by market participants as part of the LIBOR transition.

There are three basic ways to transition from a legacy LIBOR loan to a benchmark replacement rate. The first can be called a “Consensual Amendment.” This is a standard, old-fashioned type of amendment – the parties to a transaction get together and all (typically this would require 100% lender vote) agree to modify an agreement to replace LIBOR with a replacement rate. The second is by operationalizing the ARRC-style “Amendment Approach.” This would allow certain parties (typically the agent and the borrower) to select a new rate and, pursuant to an amendment, incorporate the new rate and mechanics necessary to implement it with a consent threshold that is typically lower than a Consensual Amendment (e.g., as long as 50% of the lenders do not object after a certain period of time). The third is by using the “Hardwired Approach.” This method provides for a transition to a pre-agreed rate on a certain date, as long as such rate is available and administratively feasible.

However, it is important to remember that, even under the ARRC Amendment Approach or Hardwired Approach, the fallback provisions are only part of what is necessary in order to fully transition loan documentation into alternative rates. While standard fallback language may tell you what rate to transition to, and when, it almost never provides the actual mechanics to transition. For example, fallback language may instruct the parties that, upon LIBOR cessation, the interest rate under a loan will change to Term SOFR plus an ARRC-recommended spread. However, as an additional step, the loan agreement will need to be modified to insert the definitions and mechanics of the Adjusted Term SOFR rate (e.g., inserting definition of “Adjusted Term SOFR,” deleting LIBOR references, modifying how “Interest Period” is used, changing the eurocurrency liabilities language, adding U.S. Government Securities Business Day definition, etc.). These technical, administrative or operational changes are referred to, in standard ARRC and LSTA drafting, as “Benchmark Replacement Conforming Changes” and often may be implemented on a unilateral basis by agents.

There are two basic ways to accomplish the mechanical portion of LIBOR transition developing in the market, with variations on the spectrum in between. One is a “standard” amendment. This is what it sounds like – it’s a normal-looking amendment that we are all used to. Think of this as “delete Section 2.05(a) and insert the following Section 2.05(a) in lieu thereof.” It is bespoke for a loan agreement, and describes (with specificity) which changes are necessary to implement a transition. It requires careful tailoring and drafting unique to each loan agreement.

Another option is a bit of a novelty that, as far as we know, was developed just for purposes of LIBOR transition. This we’ve nicknamed a “golden amendment.” A golden amendment is designed to be a blunt tool that could modify documents en masse. Think of this as “if you have anything in your agreement that is a LIBOR definition or provisions that relate to LIBOR, they are deemed modified to refer to Adjusted Term SOFR instead.” In order to be useful as a tool, it needs to be very generic and capture, to the extent possible, any variations or provisions that might be seen in the market for syndicated credit agreements.

There are pros and cons of using either approach (standard or golden amendments), or gradations in between, and some lenders are using each in different circumstances. Cadwalader is happy to talk through the options and considerations with any market participants (mandatory business development pitch quota satisfied!).

Below we will explain how the forms the LSTA has provided may be used in certain circumstances.

Term SOFR/Daily Simple SOFR Consensual Amendment: This is a form that would allow parties to implement a conformed, blacklined credit agreement (which would be attached as an exhibit) to transition the benchmark rate. This is a standard amendment, *i.e.*, it does not utilize fallback provisions. Many agents will have their own form of amendment that can be used for this purpose; the LSTA provided this form as an example. It will require a detailed modification exercise to have a correct conformed credit agreement, and is particularly helpful if other changes are being made at the same time.

Benchmark Replacement Amendment: This form is to be used in connection with ARRC-style Amendment Approach fallbacks. The faceplate of this amendment selects the replacement rate and replacement date, subject to necessary consents. An exhibit would be attached to include the “operative terms” that implement the details of the transition.

Benchmark Replacement Conforming Changes: This is the cover amendment used to implement Benchmark Replacement Conforming Changes. The Benchmark Replacement Conforming Changes are typically implemented unilaterally by the agent, and therefore neither the borrower nor any lenders are signing. An exhibit would also be attached to this form to include the “operative terms” that implement the details of the transition.

Operative Terms/Exhibit A: This is where the magic really happens. These are the operative terms for a “golden amendment” modification of a syndicated loan agreement. This exhibit can be attached to either a Benchmark Replacement Amendment or Benchmark Replacement Conforming Changes faceplate. These provisions, among other things:

- insert the applicable definitions for the new benchmark rate structure
- delete any unused LIBOR-related definitions
- set a date for LIBOR to be no longer available
- modify provisions in the documents to refer to Adjusted Term SOFR instead of LIBOR
- delete London Business Day and London interbank market references
- change notice periods to be a standard [three (3)] U.S. Government Securities Business Days
- update eurocurrency liabilities language

Note that this Operative Terms/Exhibit A makes it clear that you do not “break into” existing LIBOR tranches for purposes of transition, consistent with ARRC and LSTA drafting and most market participants’ expectations. That is if a 3-month LIBOR tranche was set on June 1, 2023, that loan would continue to bear interest at 3-month LIBOR until September 1, 2023 (even if LIBOR ceases on June 30, 2023).

The LSTA is preparing Daily Simple SOFR versions of these documents, where applicable, for later distribution.

Cadwalader was drafting counsel for the LSTA in the challenging and rewarding process of developing these documents, which worked their way through various working groups, the LSTA’s primary markets committee and, eventually, widespread distribution. We always remain happy to discuss these, or any matters, with our clients and friends.