

DRAFTING FOR EXTENSION OPTIONS

THE LMA EXTENDS A HAND

Extension options, which give the borrower the option to request an extension to the maturity of a facility, have been a common feature of investment grade working capital facilities for many years. Increasingly onerous capital requirements for banks, amongst other things, have made access to committed funding for more than five or so years for the average borrower almost impossible. The extension option offers borrowers the possibility to extend the maturity of their facilities for a year or two on the same terms, thereby delaying the need for a formal “amend and extend” or full refinancing, without lenders having to make any upfront commitment (and incur the increased capital costs that go along with that). In short, everyone is a winner.

While used extensively in the market, there has, until recently, been no template drafting available for extension options. That has now changed with the LMA having published a form of extension option drafting.

The LMA drafting is neither conceptually difficult nor particularly controversial. It adopts a structure which will be familiar to most market participants and broadly reflects market practice, although it is acknowledged that the negotiated terms of individual extension options can vary. In this short briefing, we provide an overview of the LMA’s new drafting and consider a few key points for borrowers to keep in mind when looking to incorporate an extension option based on the new LMA form.

Overview of the LMA’s extension option drafting

The LMA’s extension option drafting is presented as a slot-in rider, intended to be used in conjunction with the LMA’s investment grade recommended forms.

The rider reflects the commonly agreed “+1+1” structure, whereby the borrower is able to request a one-year extension to the initial tenor of a facility on two separate occasions. The first request must be made within a specified period before the first anniversary of the agreement, and the second request must be made within a specified period before the second anniversary of the agreement.

The LMA drafting includes a form of extension request and makes the delivery of such extension request conditional on the absence of any Default/Event of Default and the material accuracy of the repeating representations. There is an option to make the extension itself subject to the same conditions, as well as subject to any outstanding fees having been paid.

Importantly, the extension option is uncommitted - the lenders are free to accept or reject a request from the borrower to extend the facility in question. If a lender rejects the request (or if a lender simply fails to respond to the request), then the termination date applicable to its whole commitment in the relevant facility will remain unchanged. There is no option for a lender to choose to extend only part of its commitment.

Key points for borrowers

The new LMA drafting is refreshingly simple and there is little of particular concern from the borrower’s point of view. There are, however, a handful of improvements which borrowers may wish to consider negotiating if offered an extension option mechanic on LMA terms.

- *Automatic nature of extension* - The LMA drafting contemplates that once the extension request has been delivered and provided that the specified conditions are met (for which, see the discussion above), the commitments of lenders who accept the request will automatically be extended on the extension date regardless of the number of lenders who accept and the proportion of the total commitments that they represent. There is no option for the borrower to withdraw the extension request if the extension is not accepted by all lenders, a right which the borrower may want to incorporate. Alternatively, and to the same effect, the borrower may wish to build an additional step into the extension process whereby it is required to formally accept the extension once notified of the level of acceptances, before the extension can take effect.
- *Removal or replacement of a non-consenting lender* - The LMA drafting does not give the borrower the option to remove and/or replace a lender who does not accept an extension request. This can be useful to the borrower in the event that less than unanimous acceptance is achieved. Where it is agreed that the borrower is to have the flexibility to manage the lending syndicate in this way, the details will need to be agreed, for example whether the borrower has the right to require the non-consenting lender to transfer its position to a third party of the borrower’s choosing, or whether the existing lenders in the syndicate are to have a right of first refusal on a pro rata basis.
- *Flexibility of the extension* - The LMA drafting permits the borrower to request a one-year extension before

the first anniversary of the agreement and either a one-year extension (in the case of already extended commitments) or two-year extension (in the case of non-extended commitments) before the second anniversary of the agreement. Borrowers may want to think about whether there should be additional flexibility to request either a one- or two-year extension before the second anniversary of the agreement in respect of non-extended commitments.

- *Extension fees* - The LMA drafting contains a placeholder for extension fee arrangements, in recognition of the fact that there are different approaches adopted in practice. There are broadly two options available to borrowers - either to agree a fixed fee upfront or to leave the fee to be agreed at the time the extension option is exercised. This is a commercial point; both options are seen in practice. Bearing in mind that the option is non-binding on the lenders (meaning that in situations where there is concern about the success of the extension, any specified fees might fall to be negotiated in any event) there is possibly little to choose between them.

The extension option drafting is a welcome addition to the LMA's documentation library. Helpfully, the drafting has been kept simple and reflects the framework which is widely used in the market, but acknowledging that the terms of extension options can vary in practice and that the LMA drafting may need to be amended on a case-by-case basis. For further background on extension options, readers are referred to our [ACT Borrower's Guide to the LMA's Investment Grade Agreements](#).

For further information, please speak to your usual Slaughter and May contact or one of the lawyers listed below.

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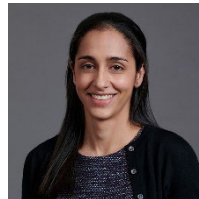
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