





1 Introduction

The provision of a term sheet to prospective participants in a syndicated loan transaction is a well-established and key component of the primary syndication phase of any deal. Together with financial and other due diligence, the term sheet should assist the analyst in forming a robust view of the investment proposal and should act as a key enabler in the commitment process. With other factors often dictating swift turnaround times for the agreement of full documentation, the timely provision of term sheets and sufficiency of their content are obviously of particular importance.

As part of a co-ordinated outreach exercise on behalf of their members, the LMA and the ELFA have sought to identify issues faced by the investor community with regard to term sheet sufficiency. The publication of this guidance paper is a result of that collaborative work, with invaluable input from respective LMA and ELFA working groups and specialist review providers (Covenant Review, Reorg and Xtract Research).

Feedback from working group discussions highlighted the following areas of concern.

- Term sheets vary significantly in content and sufficiency, varying from as few as 15 pages to more than 40 pages in length.
- Crucially, material terms that investors rely on in order to make their investment decision are often deficient in detail, or omitted completely and subsequently included without preview at the full documentation stage.
- The general format of term sheets appears to follow individual precedent rather than any accepted standard or template.¹
- The consensus was that, as a whole, current practice negatively impacts the investor's ability to appropriately analyse risk at a key stage of the investment decision process.

Following further investigative work with working groups and specialist review providers, the LMA and ELFA released an investor survey in Q2 2020 to assist in prioritising term sheet content where more fulsome disclosure is viewed as a prerequisite to an informed investment decision.

The checklist below is the result of these efforts, and sets out terms in groupings that reflect the results of the investor survey and subsequent additional consultation with the working groups.

Improvements in this area are crucial to the proper functioning of the syndication process and loan market as a whole.

¹ Given this, it was agreed across working groups that the results of the survey should be used to form the basis of this best practice document, rather than to attempt to translate these into a form of term sheet template at this stage.

2 Drafting for completeness – provisions

Set out below are a list of those provisions identified by investors as being of material importance to their investment decision. These reflect the determinations of the working groups, a wider group of investors consulted during the process, and the investor survey on term sheet completeness referenced in the introduction. It is important to note that this is not intended to be an exhaustive list of all terms that should be presented in the term sheet, but rather the most material terms that investors require fulsome disclosure on at the term sheet stage of a deal. Term sheets should contain, at a minimum, a fulsome description of all of the terms set out below.

2.1. EBITDA

- Fully drafted definitions of all iterations of Consolidation EBITDA and Consolidated Net Income
- Detail of any add-backs, run-rate adjustments, or similar, in full, with cap levels (and whether the adjustments presented in syndication are part of this cap) and levels requiring diligence
- Presentation of pro forma opening level of “covenant” EBITDA, including the full calculation
- Presentation of add-backs/run-rate adjustments included in the Base Case Model and/or the quality of earnings run-rate Consolidated EBITDA analysis in the buy-side financial due diligence report
- Whether EBITDA can be adjusted for IFRS 16, and whether this is consistent with treatment of consolidated indebtedness

2.2. Restricted Payments

- Definition of “retained cash”
- Amount of annual sponsor fee
- Specify whether debt capacity can be used for Restricted Payments, or vice versa
- Specify which baskets are blocked by events of default

2.2.1. Permitted Payments

- Definition of “Restricted Payment” plus material exclusions, including if restricts second lien prepayments

2.2.2. Restricted Payments “builder basket”, “Available Amount” or “Acceptable Funding Sources”

- The component elements from which it is “built”
- Conditions for use; any relevant “start date” from which it begins to build
- 100% reduction or floor components
- Present calculation of any accumulated existing capacity (if back-dated)
- Specify baskets that reduce availability under the builder basket

2.2.3. Permitted Investments

- Full capacity and explicit clarification of presence of J Crew loophole

2.3. Incremental Facility

- Specify cap amount and all components; dry powder additions
- Purpose
- Bullet / amortisation conditions
- Intercreditor accession obligations
- Specify covenant condition (no more onerous terms)

2.4. Fees

- Margin (matrix likely to be blank); margin holiday period length; margin ratchet – number of steps down that apply under the margin ratchet to Facility B
- Ticking fee and whether it crystallises if debt is not drawn
- Terms of any junior debt (e.g. pre-placed second lien or PIKs)

2.5. Permitted Disposals/ Asset Sales

- Definition of “Asset Sale” and any non-standard exceptions; payment waterfall
- Details on de-minimis and other material carve-outs
- Step-down ratios applicable to use of asset sale proceeds

2.6. Transaction Security

- Whether the Agreed Security Principles exclude material subsidiaries
- Where transaction security excludes material subsidiaries or certain jurisdictions, specify the % of EBITDA / Total Assets of the Group and which specific entities are not included
- Guarantor Cover Test: level, % of what (EBITDA/Total Assets, etc) and calculation to show expected closing level
- “Excluded Jurisdictions”
- Specific effective guarantor coverage in light of the Agreed Security Principles
- Precise details of entities providing post-closing security

2.7. Permitted Company Debt

- Specify whether or not (and if there is, the amount) of any sub-limit on the amount of debt that may be incurred by companies in the credit group that are not themselves borrowers/guarantors
- Specify obligor to non-obligor transfers sub-limit

2.8. Ratios

- Specify definitions of each
- Define all ratio components, e.g. does the numerator of “Senior Secured Net Leverage Ratio” include only debt secured equally on the credit agreement transaction security or does it also capture effective senior/structurally senior debt
- Specify pro forma exclusions under Ratio definitions
- Specify pro forma opening levels of all ratios to be used in the credit agreement, calculated as per SFA definitions; set out what headroom to base case EBITDA was/will be used for the determination of the financial covenant level
- Provide calculation of all opening ratios so investors can see how they were arrived at

2.9. Events of Default

- Specify cross default / acceleration thresholds

2.10. Debt Incurrence

- Specify ranking of second lien debt – e.g., is it pari passu in right of payment and subordinated in right of security or subordinated in right of payment and security?
- Indicate presence of inside maturity basket, no worse test
- Specify conditions of permitted refinancing indebtedness

2.11. Details on Baskets:

- Should include de minimus thresholds, caps, conditions to use

2.12. Amendments and Waivers

- Unanimous consent matters
- Structural adjustment matters and required consents
- Super majority lender threshold and matters
- Treatment of non-consenting lenders

2.13. Change of Control

- Fully drafted definition and whether the deal is portable

2.14. Transfers

- Presence of any deemed consent period
- Details and definition of distress debt fund/loan to own restrictions
- Conditions relating to permitted sub-participations
- Requirement to notify to sponsor
- Any caps on white lists, on a per annum basis and over the life of the facilities
- Information on agent and transfer fees
- Minimum transfers
- Minimum holds

2.15. MFN rate, length, calculation, and exclusions/carveouts

2.16. Maturity condition and all exclusions/carveouts

2.17. Ring-fencing

- Presence of any Unrestricted Subsidiaries / other excluded subsidiaries on closing
- Permitted Investments capacity that can be used for designating Unrestricted Subsidiaries or transferring assets / property to Unrestricted Subsidiaries
- Conditions for future Unrestricted Subsidiary / excluded subsidiary designation

2.18. Fully drafted definition of Indebtedness

2.19. Debt purchase

- Specify conditions related to permitted debt purchase transactions

2.20. Treatment of IFRS 16/Operating Leases

- Treatment for covenant calculations under EBITDA and with respect to the balance sheet
- Whether the calculation mechanics can be changed, and under what circumstances

2.21. Reports

- Date when the first reports are due and when first compliance certificate is due
- Timing of monthly / quarterly / annual accounts, management presentation, budget

3 Conclusion

It is hoped that more a fulsome disclosure of key provisions in the initial term sheet will aid investor's ability to analyse key risks, and commit to new deals in the market, aiding liquidity generally.