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The Cashless Roll: A Primer

LAUREN HANRAHAN AND TODD KORETZKY

This article provides an overview of the "cashless roll" mechanism, including explanations of when, why, and how it has been employed in recent U.S. syndicated credit facilities.

Recent refinancings of syndicated credit facilities, as well as repricings and amend-and-extend amendments, have often been accomplished utilizing, in part, a "cashless roll" mechanism. Although not a new feature of the syndicated loan market, it is being used with increasing frequency and transparency, and the technology for applying "cashless rolls" is evolving as borrowers, lenders and arrangers recognize the complexities involved. This article provides an overview of the "cashless roll" mechanism, including explanations of when, why, and how it has been employed in recent U.S. syndicated credit facilities.

WHAT IS A CASHLESS ROLL?

A "cashless rollover" or "cashless roll" is a deemed exchange of existing term loans for new or amended term loans from the same lender to the same borrower. As the name suggests, the exchange is accomplished on an in-kind, or cashless, basis. In effect, a lender "rolls over" its principal amount from one credit facility to a replacement, or amended, facility by applying the new principal amount in satisfaction of an equal amount of existing principal,

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rather than receiving a cash payment in respect of its existing term loan and shortly (or immediately) thereafter using the same cash to purchase the borrower's new term loans. Thus, the cashless exchange of principal eliminates the need to "round trip" cash from the borrower to the lender and back to the borrower again.

WHEN IS IT USED?

The "cashless roll" is deployed in situations where existing term loans would otherwise be repaid to existing lenders in cash at par with proceeds of new or amended term loans (e.g., a refinancing, or a repricing or amend-and-extend amendment that is structured as a new tranche of lower-priced and/or extended term loans that repay the existing term loans).

WHY IS IT USED?

The "cashless roll" mechanism was initially developed to accommodate certain institutional investors that preferred this funding mechanism to loan repayment for convenience and other reasons. For several years, the "cashless roll" was used sparingly. "Cashless rolls" are now frequently offered to all existing lenders in credit facilities being refinanced, repriced, or extended.

WHO IS INVOLVED?

The "cashless roll" requires an agreement between the borrower and the "rolling" lender. However, the administrative agent for both the existing and new or amended facilities must also be willing to handle its implementation.

When arranging the new or amended facility, the arranger, in consultation with the borrower, will determine whether a sufficient need (or desire) exists to warrant offering the "cashless roll" option to any or all existing lenders for purposes of facilitating syndication of the new or amended facility. In making this determination, arrangers consider various factors including expectations regarding the syndication of the new facility, investor demand and the administrative burdens involved.

In refinancing transactions, there should be no need for consent or

participation by any other lenders in connection with a "cashless roll" by a "rolling" lender. From a non-"rolling" lender's perspective, all existing term loans, including its own, are simply repaid by the borrower (presumably but not necessarily in cash) and the existing credit facility is terminated. In the amendment context, aside from lender approval of the amendment transaction generally, non-"rolling" lenders do not vote on any other lender's election and utilization of the "rollover" option.

HOW IS IT IMPLEMENTED?

The "cashless roll" mechanism varies from deal to deal. It may be accomplished by the express terms of an amendment (often with each lender presented with the option to select, on its signature page, a "cashless rollover" for all or a portion of its existing term loans) or by a separate letter agreement, executed concurrently with the proposed refinancing or amendment, between the existing lender and the borrower and acknowledged by the administrative agent(s). In each case, the borrower offers to exchange an aggregate principal amount of existing term loans outstanding immediately prior to the closing of the transaction, for the allocation of new or amended term loans in the initial syndication of the new or amended credit facility. Any interest and non-principal amounts owing by the borrower to the "rolling" existing lender in respect of the existing term loans (including any call premium payable on the existing term loans) and any consent fees or upfront fees (including amounts that might otherwise be treated as original issue discount) in respect of the new term loans are typically paid in cash by the borrower. As a result, although intended to reduce the number of cash payments at closing (i.e., by "rolling" certain principal amounts forward on a cashless basis), the flow of funds in a transaction involving a "cashless roll" option can actually become quite complex.

WHAT ARE THE KEY TERMS?

The documentation for "cashless rolls" continues to develop. "Cashless roll" letter agreements and amendment provisions typically contemplate that, in order to memorialize the deemed exchange, the administrative agent(s) will mark the register(s) to reflect both the cancellation of the exchanged

amount of existing term loans and the inclusion of each "rolling" lender as a party to the new or amended credit agreement immediately following the occurrence of the closing date. For this reason, the administrative agent(s) for both the existing and the new or amended credit facilities are required to accept and acknowledge such letter agreement or amendment provision. In the case of refinancings that are "fronted" by a lead arranger, all new, non-"rolling" term lenders in primary syndication will generally become lenders shortly after the closing date via an assignment of their allocated term loans from the arranger that fronted the new or amended term loans on the closing date. Possibly for this reason, "cashless roll" letter agreements or amendment provisions often also state that the "cashless roll" satisfies the requirements of an assignment agreement under the terms of the new or amended credit agreement, although a "cashless roll" is not technically an assignment.

Aside from the funding mechanics of "cashless rolls," "rolling" lenders are not entitled to any additional substantive rights or benefits under the credit facilities as compared to other lenders under either the existing or new or amended credit facilities. Moreover, although "rolling" lenders are entitled to any call protection otherwise applicable to their term loans that are "rolled over" (and effectively prepaid), they typically waive their rights to the reimbursement of LIBOR "breakage" costs associated with the early retirement of such term loans.

Other transaction documents may be affected by the "cashless roll" mechanism as well. The payoff letter for the facility being refinanced may need to be modified to contemplate a portion of the outstanding loans being repaid on a cashless basis and not by wire transfer. Similarly, any co-arranger fronting letter may be modified to contemplate a smaller fronted amount than if the entire new term loan were disbursed by the fronting bank in cash. Credit agreements themselves may begin to include provisions intended to facilitate lenders becoming party pursuant to the "cashless roll" mechanism in addition to the traditional means of signing the credit agreement at closing or purchasing loans pursuant to an assignment agreement.

POINTS OF CONSIDERATION

The following highlights certain elements of a "cashless roll" transaction that warrant particular attention:

- *Exchanged Amount*. The exchanged amount, in the easiest formulation, consists of the "rolling" existing lender exchanging all of its existing term loans for the same amount of the new or amended term loans. However, if syndication of the new or amended term loans results in a significant oversubscription, the arranger of the new transaction may wish to reduce the allocation of the "rolling" lender in the new deal (as compared to its holdings in the existing deal), in which case the exchanged amount will be less than the full amount of the "rolling" lender's existing term loans and the "rolling" lender will also receive a cash repayment of its existing term loans in an amount equal to the amount by which its existing term loans exceed its exchanged amount. Similarly, the "rolling" existing lender may elect not to "cashlessly roll" all of its existing term loans or the new term loan facility might be smaller than the existing term loan facility, which scenarios also necessitate a partial cash repayment of such lender's existing term loans in an amount equal to the excess above the exchanged amount. On the other hand, the "rolling" existing lender may wish to increase its allocation, in which case such lender will fund such new loans in cash, in addition to exchanging all of its existing term loans.
- *Identity of the Existing and New Lenders in a Common Family*. The arranger of the new transaction (and the "rolling" existing lender) must also track the identity of each "rolling" lender in any group of affiliated lenders (i.e., funds and sub-funds of the same institution) that desires to "roll over" its loans. To the extent of any downsizing or upsizing of the existing lender's allocation in the new or amended transaction and any cash payment of fees, interest, premium and/or other amounts, the arranger must track, and pay, each entity separately on the transaction's flow of funds memorandum.
- *Rights During Interim Period*. Although the "cashless roll" is designed to occur concurrently with closing, the "rolling" lender does not sign the new or amended credit agreement, and thus may not be considered a lender of record under the new or amended facility immediately upon its effectiveness. Instead, the "rolling" lender becomes party to the new or amended facility pursuant to the deemed exchange of its "rolled" term loans and the registration of that exchange by the administrative agent promptly following the effectiveness of the new or amended credit facil-

ity. During this interim period, which should be only a moment in time, the initial term loan lender (i.e., the fronting bank) may be treated as the lender of record of the "rolled" term loans and may vote such "rolled" amounts in an amendment to approve the amended credit agreement into which the loans are "rolled-over." All other rights and benefits attaching to the "rolled" loans (such as the right to receive accrued interest) should transfer to the "rolling" lender immediately upon the consummation of the deemed exchange contemplated by the "cashless roll."

- *Tax Effects*. From a tax perspective, the "cashless roll" is generally treated as a funding mechanism, rather than a separate taxable transaction. In the event that there is a significant amount (more than 10% of the aggregate principal amount) of new lender money involved in the amendment or refinancing, the purchase price paid by the new lenders will set the "issue price" for tax purposes for all lenders (including the "rolling" existing lenders).

CONCLUSION

Suffice to say, "cashless rolls" seem to be here to stay – what was once a one-off accommodation designed for certain institutional investors has now become a mainstream feature of U.S. syndicated term loan refinancings. In order to avoid any unintended consequences, understanding the mechanics of the "cashless roll," the related legal documentation and its implications is important for borrowers, lenders, arrangers, and agent banks alike.