KEY POINTS

- This article follows on from an article written by Jonathan Porteous and Matthew Padian,[1] now that there have been a number of new Restructuring Plans under the Corporate Insolvency and Governance Act 2020 (CIGA).
- There is also a new crown preference for HMRC introduced by the Finance Act 2020 (Crown Preference).
- The Loan Market Association has not considered it necessary to amend their suite of finance documents for CIGA or the Crown Preference.
- Both documentation and structural changes are becoming prevalent in secured lending and special situations documentation to mitigate the impacts of both CIGA and the Crown Preference.

Feature

Author Georgia M Quenby

The impact of the Corporate Insolvency and Governance Act 2020 and the Finance Act 2020 on drafting Loan Documentation and Practice: update

In this article, Georgia Quenby considers the documentary and structural changes that are becoming prevalent in secured lending and special situations documentation to mitigate the impacts of both the Corporate Insolvency and Governance Act 2020 and the Crown Preference.

CIGA MORATORIUM

The LMA community have determined that they are happy to rely on the following existing Events of Default in relation to CIGA moratoria:

> "A moratorium is declared in respect of any indebtedness of any member of the Group.
>
> Any corporate action, legal proceedings or other procedure or step is taken in relation to:
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> - the suspension of payments, a moratorium of any indebtedness, winding-up, dissolution, administration or reorganisation (by way of voluntary arrangement, scheme of arrangement or otherwise) of any member of the Group other than a solvent liquidation or reorganisation of any member of the Group which is not an Obligor."

Historically in most finance transactions a moratorium is most likely to arise on commencement of administration.[2] And where the security agent is the holder of a qualifying floating charge (QFC Holder) then the security agent can appoint the administrators or intervene if the company seeks to appoint administrators.[3] However, CIGA introduced a new free-standing moratorium which the company can commence without any input from the QFC Holder. The new moratorium does not need to be in respect of indebtedness, indeed given the carve-out of financing arrangements from the pre-moratorium debts without a payment holiday and that the moratorium does require payment of amounts which fall due, it is quite possible on a technical reading that a judge may find a moratorium not to be a moratorium of, at least, "financial" indebtedness.

The monitor under the moratorium can use floating charge assets of the company to fund the moratorium as an administrator can[4] and of course the security agent is stayed from taking enforcement action and the lenders are disincentivised from acceleration in reliance on the commencement of the moratorium because of the consequential loss of post-moratorium super-priority.

CREATION OF POTENTIAL FOR CHARACTERISATION CHALLENGES

The new moratorium therefore has three impacts which we are seeing in documentation and transaction structures within non-investment grade, asset-based lending and special situations financings:

- first, it creates, in the monitor, a person motivated to challenge the characterisation of charges between fixed and floating;
- second, it drives transaction structures away from charges with the attendant recharacterisation risk and towards receivables assignments, conditional sale arrangements, pledges and chattel mortgages; and
- third, it removes the historical general drive to pre-moratorium communication and collaboration created by the powers of the QFC Holder.

The new Crown Preference has also created, in HMRC, another person motivated to challenge the characterisation of charges between fixed and floating because the Crown Preference allows certain tax liabilities such as VAT to rank ahead of floating charge recoveries, but not fixed charge recoveries.

Rather than relying on the LMA moratorium-related Events of Default for the reasons described above, these impacts are being addressed in documentation in a variety of ways.

STRUCTURING RECEIVABLES FINANCINGS

From a transaction structure point of view if the underlying collateral is receivables, then

a receivables purchase (by way of assignment) rather than a fixed charge with payment into a controlled account mitigates recharacterisation risk. *Spectrum Plus*[5] gave us a stringent set of legal and operational hurdles to satisfy to be confident that a purported fixed charge will not be recharacterised as a floating charge. However, most financings done in reliance on receivables of a trading business (as opposed to a securitisation transaction utilising an SPV structure) are done in conjunction with charges on the other assets of the business such as inventory, equipment and intellectual property, at least one of which is likely to be a qualifying floating charge.

Again, pre-CIGA, the security agent would rarely expect the characterisation of a charge to be challenged, in part because the security agent is usually the party appointing the administrators. However, the funders are generally excluded from the appointment of a monitor and the monitor is motivated to make such a challenge, and on insolvency, HMRC is also motivated to make such a challenge. Therefore, funders are now mitigating the risk of challenge to the *Spectrum Plus* controls by switching to receivables purchases for the receivables component of a multi-asset financing.

CONSULTATION IN RELATION TO RESTRUCTURING PLANS AND MORATORIA

To address the exclusion point, we are seeing (and using) contractual commitments to consult and provide additional information prior to appointment of a monitor or commencement of a Restructuring Plan. The related additional provisions are:

A new repeating representation which will act as a drawstop if it cannot be made:

> "It has not taken any action nor (to the best of its knowledge and belief) have any steps been taken or legal proceedings been started or threatened against it for its winding-up, dissolution, re-organisation, arrangement or reconstruction, for the enforcement of any Security Interest over its assets, for the obtaining of a moratorium or the appointment of a liquidator, supervisor, receiver, examiner, administrator, administrative receiver, compulsory manager, trustee, monitor or other similar officer of it or in respect of any of its assets within the 12 months preceding the date on which this representation is made or repeated."

A new undertaking specific to the new moratorium and restructuring plan:

> "Moratorium and Restructuring Plan
> (a) Without prejudice to [the insolvency/insolvency proceedings events of default], in respect of a moratorium under Part 1A of the Insolvency Act 1986 (a Relevant Moratorium) and/or an arrangement or reconstruction under Part 26A of the Companies Act 2006 (a Restructuring Plan):
> (i) no Obligor shall take any corporate action, legal proceedings or other procedure or step:
> (A) to obtain a Relevant Moratorium and/or appoint a monitor in respect of such Relevant Moratorium and/or propose a Restructuring Plan without giving the Agent at least 20 Business Days' notice;
> (B) to extend or seek to extend any such Relevant Moratorium; and/or
> (C) to obtain permission of the court or otherwise howsoever to dispose of any of its property which is subject to a Security Interest under the Security Documents as if it were not subject to such Security Interest; and
> (ii) any Obligor which is considering obtaining a Relevant Moratorium and/or proposing a Restructuring Plan shall:
> (A) consult with the Agent as to the identity of the proposed monitor of a Relevant Moratorium and only appoint a monitor who is a partner in an accounting firm of international repute;
> (B) provide the Agent with copies of any draft proposed Restructuring Plan not less than 20 Business Days prior to formally proposing such Restructuring Plan; and
> (C) mpromptly on request, provide such further information regarding any such Relevant Moratorium and/or Restructuring Plan as the Agent may from time to time request.
> (b) If and to the extent that the Agent (acting on the instructions of the Lenders) consents in writing to:
> (i) an Obligor obtaining a Relevant Moratorium;
> (ii) an Obligor proposing a Restructuring Plan; and/or
> (iii) an Obligor disposing of an asset which is subject to a fixed charge or equivalent Security Interest under the Security Documents as if it were not subject to such Security Interest,
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> and approves the terms on which the Obligor intends to operate during such Relevant Moratorium and, if applicable, Restructuring Plan, no Event of Default shall be deemed to have occurred under [the insolvency/insolvency proceedings events of default] and the applicable Event of Default shall be deemed waived for all purposes under the Facility Agreement, provided that such waiver shall be limited solely to the specifics of the Relevant Moratorium, Restructuring Plan or disposal as consented to by the Agent and shall not extend or otherwise be deemed to be a waiver of any other Default or Event of Default which may arise as a result of such Relevant Moratorium, Restructuring Plan or disposal."

And in relation to the LMA Events of Default quoted above, the following amendments:

> "A moratorium is declared in respect of any indebtedness of any Obligor *or a moratorium is obtained or ordered in respect of any Obligor*

Biog box
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pursuant to the provisions of Part A1 of the Insolvency Act 1986. If a moratorium occurs, the ending of the moratorium will not remedy the Event of Default caused by the occurrence of such moratorium."

Any corporate action, legal proceedings or other procedure or step is taken in relation to:

"the suspension of payments, a moratorium of any indebtedness *or enforcement rights (including, but not limited to, a moratorium under Part A1 of the Insolvency Act 1986)*, winding-up, dissolution, administration or reorganisation (by way of voluntary arrangement, scheme of arrangement, arrangement or reconstruction under Part 26A of the Companies Act 2006 or otherwise) of any Obligor."

BORROWING BASE RESERVES

In relation to borrowing base reserves, the Crown Preference is being specifically addressed and potential for recharacterisation under CIGA is being addressed indirectly, often using the following additional language:

"Reserves to reflect the full amount of any liabilities or amounts which may (by virtue of any Security Interest granted to any person other than the Finance Parties, the provisions of the Insolvency Act 1986, the Enterprise Act 2002, *the Finance Act 2020, the Corporate Insolvency and Governance Act 2020* and any other statutory provision or otherwise) rank equally with or in priority to the Security Interests granted to the Secured Parties under the Finance Documents or to reflect any Security Interests intended to be created pursuant to the Finance Documents and which may be unavailable to the Secured Parties in the event of an insolvency."

USE OF ALTERNATIVE FORMS OF SECURITY INTERESTS

Finally, where the underlying collateral is tangible personal property which is not inventory that needs to be sold in the ordinary course of business (ie where a floating charge is the only viable form of security interest), there is renewed interest in the possibility of using old legal techniques such as pledges, chattel mortgages and contractual liens instead of a floating charge. These interests would sit alongside a qualifying floating charge, and while subject to the stay created by the new moratorium, if correctly utilised they ringfence the secured assets from either use by a monitor or priming by HMRC. The author has covered this in more detail in an article[6] first published in *Recovery Magazine* focused on company rescue and reconstruction in the UK. ■

1 The impact of the Corporate Insolvency and Governance Act 2020 on drafting loan documentation and practice', (2021) 4 JIBFL 273.
2 Paragraphs 41-43 of Sch B1 to the Insolvency Act 1986.
3 Paragraph 36 of Sch B1 to the Insolvency Act 1986.
4 Paragraph 70 of Sch B1 to the Insolvency Act 1986.
5 *National Westminster Bank plc v Spectrum Plus Ltd and others* [2005] UKHL 41.
6 Georgia Quenby, "Back to the Future – Old Legal Techniques for Modern Transactions" (Autumn 2021) *Recovery Magazine*.

Further Reading:

- The impact of the Corporate Insolvency and Governance Act 2020 on drafting loan documentation and practice (2021) 4 JIBFL 273.
- Rank inequality: the consequences of the creation of "super priority" debts under the Corporate Insolvency and Governance Act 2020 moratorium (2021) 2 JIBFL 97.
- LexisPSL: Restructuring & Insolvency: Practice Note: Restructuring plans toolkit – CRI and JIBFL articles.