

Finance Update

July 2009

OLSWANG



General Finance News

Association of Corporate Treasurers (ACT)

The ACT have published **their response** to the Turner Review, which was published in March. The Turner Review looked at the regulatory changes which are needed to stabilise the financial system and to guard against further crises in the future. The ACT response supports the proposals to increase the capital required to back proprietary trading by banks but does not agree with a separation of this activity from the other business of the bank. However, it does agree that there need to be controls placed on the quality of assets traded and an upper limit on the size of the banks' trading books. The ACT does not support the compulsory breaking up of large banks but would welcome other methods of limiting the size of banks in the future.

Bank of England

On 26 June the Bank of England published its half-yearly **Financial Stability Report**. This report looks at the causes of global financial instability at the end of 2008 and the start of 2009, assesses the current state of the financial system including potential vulnerabilities and considers what policy changes might be required in order to increase the stability of the financial system in the future. Some of the suggestions for future regulation include stronger market discipline, more public disclosures, self-insurance of banks. The report also considers how the larger banks should be managed and limited in size.

Banking Act 2009

A draft of the **Banking Act 2009 (Restriction of Partial Property Transfers) (Amendment) Order 2009** was published on 16 June. This makes a number of amendments, in light of comments made in relation to the current Safeguards Order including expressly stating that the benefit of a security may not be transferred without the liability it secures. Once the order has been approved it will be made by HM Treasury.

Basel Committee on Banking Supervision (BCBS)

The BCBS has published **principles for sound stress testing practices and supervision**. A stress test is a method of testing a bank's financial position in relation to a severe scenario and enables supervisors to identify a bank's vulnerabilities and to evaluate their capital adequacy. These principles aim to rectify the problems of current stress testing policies highlighted over the course of the last few years.

British Bankers Association (BBA)

General Finance

The BBA has announced its decision to increase the number of financial institutions that set LIBOR, by allowing banks not based in London to contribute to the rate-setting process as long as they are engaged in trade with institutions based in London.

Building Societies

The FSA has published the [building society statistics for 2008](#). The statistics are mostly compiled from the societies' regular financial monitoring returns and look at key aspects of societies' businesses, including operating ratios, lending levels, profits and capital.

Building societies do not have ordinary shareholders, unlike banks. Since ordinary shares comprise tier one capital for capital adequacy purposes building societies were limited as to how they could build their tier one capital reserves. The FSA has now agreed that profit-participating deferred shares (which are similar to ordinary shares) issued by building societies can be classified as tier one capital. See the FSA statement [here](#).

Companies Act 2006

A variety of legislation has been published in relation to the Companies Act 2006, including the following:

- the [Companies Act 2006 \(Consequential Amendments\) \(Uncertificated Securities\) Order 2009](#) was published on 22 June and comes into force on 1 October 2009. This updates the references to the Companies Act 1985 to the Companies Act 2006 in the Uncertificated Securities Regulations 2001;
- the [Companies Act 2006 \(Consequential Amendments\) \(Taxes and National Insurance\) Order 2009](#) was published on 22 June and comes into force on 1 October 2009. This amends tax and national insurance legislation to refer to the Companies Act 2006;
- the [Companies Act 2006 \(Consequential Amendments, Transitional Provisions and Savings\) Order 2009](#) was published on 26 June and comes into force on 1 October 2009. This makes amendments to UK legislation to take account of the provisions of the Companies Act 2006 which come into force on 1 October 2009;
- the [Companies Act 2006 \(Accounts, Reports and Audit\) Regulations 2009](#) came into force on 27 June 2009. This requires that where a corporate governance statement is a separate statement and not part of the directors' report it must be filed with the registrar of companies; and
- the draft [Companies \(Share Capital and Acquisition of a Company by its own Shares\) Regulations 2009](#) were published on 2 July. These regulations propose changes to the Companies Act 2006, including (a) reducing the subscription rights issue period from 21 to 14 days and (b) introducing a requirement for creditors to show that their claim is at risk and that a company has not taken adequate protection, when they object to a reduction of capital.

House of Lords Economic Committee

The House of Lords Economic Committee published its **report on banking supervision and regulation** on 2 June. The report looks at the supervisory and regulatory framework in the UK when the financial crisis began and recommends various changes. The recommendations in the report include an increase in regulatory minimum capital requirements for assets on banks' trading books and greater regulation of UK branches of multi-national banks.

HM Treasury

HM Treasury issued **an order** revoking the Landsbanki freezing orders it issued last year. This order was effective from 15 June.

Loan Market Association (LMA)

The LMA has updated its primary documents to address the difficulties that lenders and borrowers may have encountered in the syndicated loan market over the course of the last few years. These changes focus on four main areas:

- lender default;
- the effects of an Agent becoming subject to distress;
- protection for issuing banks; and
- the mechanics of dealing with market disruption in the interbank funding market.

These changes aim to mitigate the effect on syndicate members and lenders of a finance party failure. The cost of funds clause, market disruption clause and the definition of LIBOR/EURIBOR have been amended and changes have also been made to update the taxation provisions.

The LMA has posted new guidelines for dealing with requests for amendments and waivers to loan agreements. The document was drafted in consultation with a number of banks and financial institutions and seeks to provide best practice guidance for all market participants.

Interest Rates

On 9 July, the Bank of England announced that interest rates would again be held at 0.5% and that it would continue with the £125bn programme of asset purchases financed by the issuance of central bank reserves.

General Finance

World Markets

In May the UK Consumer Prices Index (CPI) fell to 2% (from 2.3% in April). This is higher than predicted, but this may be due to the rise in petrol prices and the increase in alcohol and tobacco duties as a result of the budget. The Bank of England is forecasting the CPI will fall over the coming months, but this may be limited by increases in oil and commodity prices which will exert an upward pressure on inflation.

According to the Office for National Statistics, the UK economy shrank by 4.9% in the year to the first quarter of 2009. This was the largest fall since records began and according to historic statistics was the largest fall since 1931. The Organisation for Economic Co-operation and Development has forecast that the recession in the UK will end this year, but 2010 will be a period of stagnation with zero growth.

The European Central Bank has downgraded its forecast, stating the economy across the euro-zone is likely to fall by 4.6% this year and a further 0.3% next year. It has also begun a process of quantitative easing, although this is on a much smaller scale than the process being undertaken by the Bank of England (just 0.6% of GDP, compared with 9% in the UK).

In the US, unemployment rates hit a 26 year high in June of 9.5%, this is higher than predicted by most economists and although the increase in the rate of unemployment has slowed a figure of 10% is expected within the next few months.

Stock markets have leapt in the last three months as optimism of an economic recovery increases. Sterling has risen 10% during the same period. In London, the FTSE 100 index has increased by 9% in the past quarter, however markets are still vulnerable to shocks and have tended to react in a volatile manner to the announcement of global economic data.

Real Estate Finance

Real Estate Finance News

Royal Institute of Chartered Surveyors (RICS)

The RICS Valuation Professional Group has published **advice on valuing property in a rapidly changing market**. It is aimed primarily at commercial property and is designed to encourage dialogue between the valuer and the lender and relates to the advice which can be given during loan security valuation reviews.

Real Estate Finance Market

According to Cushman & Wakefield, commercial property deals worth £1.43bn were completed in London in the second quarter of 2009, an increase of 110% on the first quarter figures. Figures from the Investment Management Association also showed that property funds obtained net investment inflow during May, the first inflows seen since April 2008. Colliers CRE has estimated that retail rents will fall by a fifth between the start of June 2009 and the end 2010 and some landlords are offering substantial rent-free periods to try to get tenants into occupation. However, in contrast, according to IPD, farmland reported rental growths of between 20% and 30% during 2008.

According to Nationwide, house prices rose by 0.9% (the second month in a row in which house prices have risen). However, house prices are 9.3% lower than this time last year. Standard & Poor's have stated that they expect house prices in the UK to stabilise during the final quarter of 2009 and the latest survey from the National Association of Estate Agents reported that the number of potential buyers registering with estate agencies has risen to its highest level since September 2007. The Council of Mortgage Lenders is also predicting a rise in mortgage lending in the near future and it has revised its forecast of the number of homes likely to be repossessed this year, to 65,000 from its previous forecast of 75,000.

Structured Finance

Structured Finance News

Alternative Investment Management Association (AIMA)

AIMA has published the first global **Guide to Sound Practices for Funds of Hedge Fund Managers**. It focuses on areas including risk management, due diligence, disclosure to investors, valuation, management of conflicts of interest and other operational issues.

International Organisation of Securities Commissions (IOSCO)

IOSCO has published its final report on hedge funds entitled **Hedge Funds Oversight: Final Report**. This report sets out six key principles for hedge fund regulation:

- mandatory registration for hedge funds and their managers/advisors;
- those people subject to registration to be subject to on-going regulatory requirements and disclosures;
- brokers and banks providing funding to hedge funds to be subject to supervision and regulation of risk management systems;
- managers/advisors and prime brokers to provide information to regulators for systematic risk purposes;
- regulators to encourage and develop good industry practices; and
- regulators to share information and co-operate to provide a global overview of the industry.

Islamic Finance

In the Financial Services Authority's business plan for 2009/2010 one of the key objectives was to promote an efficient, orderly and fair market in the UK and under this objective the FSA restated its commitment to the development of Islamic finance. During 2009/2010 the FSA has stated it will monitor development in the Islamic finance sector, work to ensure a suitable regulatory framework is in place in relation to Islamic finance and assist other organisations, such as IOSCO, in relation to their work in this sector.

Restructuring and Insolvency

Restructuring and Insolvency News

HM Treasury

HM Treasury has published a consultation paper entitled '**Developing Effective Resolution Arrangements for Investment Banks**'. This paper focuses on the issues which were highlighted by the failure of Lehman Brothers at the end of 2008 and proposes suggestions for what could be done to make the insolvency process for investment banks more effective in the future, looking at the assets of the investment bank, their customers and how to deal with open and unreconciled trading positions. The consultation period ended on 10 July 2009.

Insolvency Service

On 15 June the Insolvency Service launched a **consultation in relation to proposals to further encourage company rescue**. These proposals include:

- extending to medium and large companies the option of a moratorium against creditor action, in order to enable them to agree with their creditors a method of rescuing the company by way of a company voluntary arrangement;
- introducing a new court sanctioned moratorium for all companies; and
- allowing firms in difficulties to access further funding by allowing them to provide greater security against repayment of monies lent post-administration or company voluntary arrangement.

The consultation period ends on 7 September 2009.

Pension Protection Fund (PPF)

The PPF has published **guidance for insolvency practitioners** as to how they should interact with the PPF in a situation where an employer of an occupational pension scheme suffers an insolvency event.

Restructuring and Insolvency Market

The draft **Legislative Reform (Insolvency) (Miscellaneous Provisions) Order 2009** has been published. This order is due to come into force on 6 April 2010 and will make numerous changes to the Insolvency Act 1986 to reduce costs and administrative burdens by introducing more flexible procedures and increasing the dividends available to creditors. These changes include:

- allowing creditors to take part in insolvency meetings by telephone, video conferencing or other means;
- use of websites to send documents during insolvency proceedings; and

Restructuring and Insolvency

- allowing communication to creditors and shareholders by email.

According to figures published in the Financial Times, the bankruptcy and distressed deals in the first half of the year reached \$160.6bn worldwide, the second highest figure on record.

Administration – Pre-Packs

In the matter of Re Kayley Vending Limited [2009] EWHC 904 (Ch) an application for an administration order was made to the court in circumstances where following the appointment of an administrator it was intended that a pre-pack sale would immediately take place.

Following the implementation of the new SIP 16, the court gave some guidance as to how the court would approach administration applications that would be followed by a pre-pack sale. The court held that the applicant must provide enough information for the court to decide whether the order would be in the best interests of the creditors as a whole and that the application should contain information similar to that required under SIP 16.

In this case the administration order was made on the basis that the creditors were likely to obtain a better return from a pre-pack sale. It was also ordered that the costs of the administrator before their appointment, whilst negotiating the pre-pack sale, would rank as an expense of the administration as the balance of the benefit arising from those costs was in favour of the creditors.

Insolvency – Removal of Administrator

In the case of *Clydesdale Financial Services Ltd & Ors v Smalles* Ch D 18/6/2009 a joint administrator was closely involved in the negotiations and drafting of an eventual contract for a pre-pack sale. When the terms of the contract were questioned and an independent review was required, the court was able under Paragraph 88 of Schedule B1 of the Insolvency Act 1986 to order the removal of the previous administrator so that a new independent administrator could be appointed to carry out the review.

Receivership – Priority of Creditors

In the matter of Golden Key Ltd (In Receivership) [2009] EWCA Civ 636 the decision made by the High Court was appealed (see the [March 2009 Finance Update](#)).

In this case it was held that unless it was indicated to the contrary the court should assume that the commercial documents intended to give a commercial result. Therefore, the commercial paper which had become due and payable before the mandatory acceleration event should be paid out on a pay-as-you-go basis, thereby upholding the decision made at first instance.

The information in this update is intended as a general overview only of the subjects covered. Detailed specialist advice should always be taken before taking or refraining from taking any action. For more guidance on the changes and their application, please get in touch with your usual Olswang contact.

About Olswang

Olswang is a leading business law firm with a distinctive approach. Our pioneering and problem-solving ethos has established a commanding reputation in the technology, media and real estate sectors, as well as a wide range of other industries.

Founded in 1981, our Firm has grown to a team of over 650, including more than 100 partners, across four European offices. In addition, Olswang has a long-established best friends' network of leading independent law firms throughout the world.

Our Firm continues to be acknowledged as a leading practice in many of our core areas: Olswang was voted TMT Team of the Year 2009 for the second year running at the annual Legal Business Awards; Olswang's Corporate Group won M&A Law Firm of the Year at the M&A Awards 2008 in conjunction with M&A Magazine, and was named Corporate Team of the Year – Mid markets at The Lawyer Awards 2008.

Resourceful drive and a climate of shared knowledge and empowerment are the hallmarks of our meritocratic, unstuffy culture. For the last five years Olswang has been ranked in The Sunday Times 100 Best Companies to Work For and our strong management team is dedicated to the personal and professional development of our people.

We are committed to encouraging every member of staff to engage in lasting and meaningful pro bono and volunteering activities, both legal and non legal. The time invested by our people through the Firm's HELP Programme to assist those in need is a positive contribution to the community which is reflected in the values and culture of Olswang.

We recruit personalities with a genuine fascination and notable reputation in the sectors they focus on, which is reflected in the quality of our advice. We also understand the importance of achieving our clients' goals and ensure that our advice is, above all else, practical.

From world-class businesses to entrepreneurial startups, the rich diversity of our client base ensures a broader perspective and, as a result, deeper commercial insight. Transactional work is the most obvious feature of the role we perform. However, ongoing non-transactional support is an integral part of our business, and we focus on creating long-term relationships with our clients. We employ a range of proactive initiatives such as client care programmes, secondments, client training and feedback sessions to ensure our client relationships are strong.

At Olswang the passion of our lawyers, the confidence of our approach and the commercial edge to our advice provide a unique and compelling service.

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