

Finance Update
March 2010

OLSWANG



General Finance

General Finance News

Association of Corporate Treasurers (ACT)

The ACT's guide to the Loan Market Association (LMA) facilities agreement for investment grade borrowers has been updated and reissued on the ACT website. This guide looks at the new provisions which have been inserted into LMA standard documentation to deal with defaulting lenders and market disruption and considers the circumstances when borrowers should negotiate changes to these provisions.

Budget

On 24 March, the Chancellor of the Exchequer presented the 2010 Budget. The Budget contained a number of measures, including, among other things:

- a new stamp duty holiday was introduced for properties of up to £250,000 for first time buyers, from midnight on 24 March, to be funded through an increase in stamp duty from 4% to 5% on properties worth £1 million or more from April next year;
- the annual ISA limit will rise from £7,200 to £10,200, of which half can be saved in cash, from next month;
- the Government will set UK Finance for Growth to help expand the financial sector and the FSA is to speed up the licensing process for new banks;
- the main rate of capital gains tax will not increase and entrepreneurs' relief for capital gains tax will be increased to £2 million;
- the Government will set up a new green investment bank, which will control £2 billion of equity, to fund a low-carbon economy; and
- confirmation of the 0.5 per cent increase in National Insurance for people earning over £20,000, which will come into effect from April next year.

For more information see the Olswang Budget Blog [here](#).

Department of Business, Innovation and Skills (BIS)

BIS have launched a consultation (see [here](#)) on proposals to revise the current scheme for the registration of company charges under the Companies Act 2006. The consultation also considers the registration of charges created by LLPs. The consultation period opened on 12 March and ends on 18 June. The proposals put forward by the consultation include, among other things:

- any charge created by a UK company should be registered unless specifically excluded as current statutory lists do not accord with commercial practice;
- the requirement to register existing charges on property acquired should be abolished;

- a change to the required particulars so that, among other things, for floating charges it should be noted on the register whether there is an automatic crystallisation clause and/or a negative pledge;
- Companies House should issue a certificate for each charge registered, that is conclusive evidence of the identity of the chargor, the date of registration, confirmation that the charge was registered within 21 days of its creation and the class(es) of property charged; and
- the introduction of a requirement that only the company which created the charge may register it.

Execution of documents

On 16 February, the Law Society published a practice note entitled '**Execution of documents by virtual means**'. This practice note advises on good practice following the decision in *R (on the application of Mercury Tax Group and another) v HMRC [2008] EWHC 2721* (see the **January 2009 Finance Update**), which cast into doubt the effectiveness of virtual signings in certain circumstances. By way of reminder, a joint working party of The Law Society Company Law Committee and The City of London Law Society Company Law and Financial Law Committees also published guidance last year on the execution of documents at virtual signings or completions (see the **June 2009 Finance Update**).

Executive remuneration

The Association of British Insurers (ABI) has published its annual update of its guidelines on executive remuneration policies in the form of a **position paper and revised guidelines**. This paper is intended to give guidance on how shareholders expect the guidelines to be implemented and includes some of the following recommendations:

- keeping shareholders involved in the remuneration process;
- bonus payments where a company has under performed should be avoided as it can be seen as rewarding failure;
- performance targets should include conditions linked to the performance of the company and should be considered in comparison with the performance of competitor companies; and
- performance based bonuses should focus on longer-term shareholder value and use longer performance periods.

Financial Services Authority (FSA)

The FSA has published two consultation papers entitled '**Strengthening capital standards 3**' and '**Capital planning buffers**'. Strengthening capital standards sets out proposals for implementing the amendments to the Capital Requirements Directive and also looks at changes which could be made to address some of the issues highlighted by the recent financial crisis. The second consultation aims to clarify the FSA's approach to capital planning buffers (CPB). CPB is the amount of capital that a firm should hold so it is able to absorb losses and meet higher requirements in the adverse circumstances, for example during an economic downturn.

HM Treasury

HM Treasury has published a consultation paper entitled '**Establishing resolution arrangements for investment banks**'. This paper sets out detailed proposals for the effective management and resolution arrangements for failed investment banks, including:

- a new insolvency regime with special administration objectives;
- ensuring creditors are sufficiently protected;
- reconciling and returning client money and assets; and
- mitigating the impact of the failure on market counterparties.

HM Treasury has published a consultation paper entitled '**Implementing amendments to the Capital Requirements Directive**'. The consultation seeks views on how the Government proposes to implement the Directive using an effective, proportionate and risk-based approach and the consultation period ends on 30 March 2010.

HM Treasury has published a discussion paper entitled '**Discussion paper on non-bank lending**'. This paper looks at the barriers to the use of non-bank lending to large and mid-sized companies and considers whether there are more effective methods whereby non-bank investors can invest in corporate debt.

International Monetary Fund (IMF)

The IMF has published a working paper entitled '**Lessons and Policy Implications from the Global Financial Crisis**'. This paper analyses the current financial crisis and considers the deficiencies it has highlighted in financial regulation, particularly in the treatment of systemically important financial institutions, the assessments of system risks and vulnerabilities and the resolution arrangements for financial institutions.

Interest Rates

On 4 March, the Bank of England announced that interest rates would again be held at 0.5% and that it would continue with the £200 billion programme of asset purchases (both of these proposals were agreed unanimously by the Monetary Policy Committee).

On 4 March the European Central Bank held interest rates at 1% across the euro zone and on 16 March, the US Federal Reserve held interest rates between 0% and 0.25%.

World markets

In the UK, recent economic data suggests improvements in the economy although recovery seems to be fairly slow and patchy. In January the Association of British Insurers reported that consumer confidence in the economy fell during the final quarter of 2009, with nearly a third expecting the economy to worsen during 2010. Worries over job security have also increased, with 31% of those surveyed concerned about their job security, compared with a figure of 22% three months previously. Sterling also fell during the end of February and the start of March amid fears of a hung parliament which may prevent swift and decisive action being taken over Britain's public finances.

UK manufacturing output grew by a better-than-expected 0.9% during December and the British Retail Consortium reported that total sales in January were up by 1.2% from a year earlier, while like-for-like sales were down by 0.7%. However, the goods deficit with the rest of the world unexpectedly widened to £7.3 billion in December from £6.8 billion in November, mainly due to a big jump in imports from non-EU countries.

The Greek debt problem has highlighted the weakness of the eurozone and economic growth in Europe has also slowed, with 0.4% growth being reported in the third quarter of 2009 and just 0.1% growth during the fourth quarter. The US is also struggling, with bank lending falling at the fastest rate in history, at an annual rate of 16% since the credit crisis began in 2007 and there are worries that deflation may become an increasingly important issue in the US during the course of 2010. However, US unemployment figures released at the start of March remained stable at 9.7% indicating that US unemployment may now be close to its peak.

General Finance

General Finance Cases

Acceleration of payment under bonds

In the case of *Bank of New York Mellon v GV Films Ltd [2009] EWHC 3315 (Comm)* it was held that the bank was entitled to summary judgment in respect of sums due under various bonds where it had given valid notice of events of default and accelerated payment.

Facts: G made two bond issues (under English law and jurisdiction) and B was the trustee of each issue. About a year after issuing the bonds G started proceedings in India to sanction a scheme of arrangement proposing a 'de-merger' of its business. This would have involved part of its assets and liabilities being transferred to two new companies. Neither B nor the bondholders were notified of these proceedings. The bondholders intervened in the proceedings to oppose the de-merger. The scheme of arrangement was refused and G appealed, the appeal has not yet been heard.

A few months later B notified G by letter of the events of default in the case of both sets of bonds. The alleged events of default all concerned the proposed scheme of arrangement and required G to rectify the events of default, as far as they were able to be rectified. By further letters B gave notice accelerating repayment of the bonds. The events of default on which B relied were G's failure to pay B's legal costs on demand, the bringing of proceedings in India for sanction of the proposed scheme of arrangement and G's failure to give relevant information to B.

Decision: (1) Under the trust deeds G had an obligation to pay B's legal costs on demand and failure to do so was a breach giving rise to an event of default. G's argument that the legal costs must be reasonable was rejected. A trustee must be able to take legal advice in the confidence that any costs will be reimbursed without agonising over whether the costs involved would be considered reasonable. (2) It was held that the proceedings to sanction the scheme of arrangement without the permission of B or the bondholders constituted an event of default. (3) G had failed in its obligation to provide information to B which also constituted an event of default, however it did belatedly send this information to B and arguably had remedied this event of default. However, due to the other two events of default B was granted summary judgment.

Meaning of 'Subsidiary'

In the case of *Enviroco v Farstad Supply A/A [2009] EWCA Civ 1399* it was held that where a parent company provided shares in its subsidiary as security for a loan and the shares were registered in the name of the lender, the subsidiary would no longer be a subsidiary within the meaning of sections 736 and 736A of the Companies Act 1985.

Facts: 50% of the shares in E were originally held by ASCO plc, (the company which E argued was its holding company). ASCO controlled E through a shareholders' agreement and E was classed as a subsidiary by virtue of section 736(1)(c) Companies Act 1985 which requires the "holding company" to be a member of the "subsidiary" and to control a majority of the voting rights in it.

However, ASCO subsequently charged the shares it held in E to a bank by way of a legal mortgage, as a result of which the bank and not ASCO became the registered shareholder. The issue then arose as to whether E was still a subsidiary of ASCO.

Decision: The court's decision (overturning the more commercial approach of the court at first instance) upheld the strict language in the statute and held that E was no longer a subsidiary of ASCO.

Comment: The decision in this case could lead to a "de- grouping" of subsidiary companies where the holding company merely "controls", as opposed to "holds", a majority of the voting rights in the subsidiary and either, pledges its shares in the subsidiary by way of legal mortgage (rather than the more common equitable mortgage where the registered holder of the shares does not change) or otherwise transfers the shares in the subsidiary to a nominee so that it is no longer registered as a member. Although the decision related to the interpretation of provisions of the Companies Act 1985, it is relevant to the interpretation of the same definition in section 1159 Companies Act 2006 as the definitions are broadly the same.

Real Estate Finance

Real Estate Finance News

Mortgage market review

The FSA have published a consultation paper entitled '**Mortgage Market Review**'. This paper sets out the proposals aimed to help ensure that mortgage holders in arrears are treated fairly, including:

- mortgage lenders must consider all options for a borrower in default, repossession should always be a last resort;
- mortgage lenders must not add early repayment charges on arrears charges and related interest;
- payments by customers in financial difficulties must first be allocated to clearing the missed monthly payments, arrears charges can be cleared at a later date; and
- mortgage lenders should record all arrears telephone calls and keep records of these calls for three years.

Real Estate Finance Market

According to the CBRE monthly index, commercial property values rose 1.4% in February and according to figures from Moody's, US commercial property prices rose 4.1% during December 2009. Figures from the Investment Management Association also showed that property funds saw investment inflows of £460m during January, which were slightly lower than the figures for net investment in December 2009, but investment from institutions rose in January, from £63m in December to £88m during January. Rental growth also returned to the City of London and the West End during January by 0.2% and 0.3% respectively, according to the IPD UK Monthly Index.

According to the Land Registry's House Price Index, in January there was annual price change of 5.1%, the second month in a row in which this figure has been positive. However, according to the Nationwide House Price Index, UK house prices fell by 1% in February, this was the first fall recorded on this index in 10 months. Figures from the Bank of England showed that mortgage approvals fell for the second consecutive month in January to an eight month low and the number of loans remortgaged also fell to its lowest figure since January 1999.

Restructuring and Insolvency

Restructuring and insolvency news

Insolvency (Amendment) Rules 2010 (Amendment Rules)

The Amendment Rules amend the current provisions of the Insolvency Rules 1986. The key changes, due to be implemented on 6 April 2010, are as follows:

- to allow insolvency office-holders to pay costs and expenses incurred before appointment as an expense of the relevant insolvent estate. Therefore, the costs incurred in negotiating a pre-pack sale of the assets of an insolvent company will now be recoverable;
- to allow for the remuneration of insolvency practitioners on a fixed fee basis (as opposed to just on an asset value or time costs basis: a combination of all three will also be possible);
- to allow for electronic communication between an office-holder and the creditors of an insolvent company or individual;
- to streamline the disclaimer procedure, by removing the need to have the court endorse a notice of disclaimer for it to be valid. A disclaimer notice will now be valid as soon as the liquidator/trustee in bankruptcy signs it; and
- to bring insolvency court proceedings more into line with the Civil Procedure Rules.

Restructuring and Insolvency Market

The Ministry of Justice has published its quarterly statistics on insolvency proceedings issued in the High Court and county court for individuals and businesses for the final quarter of 2009. During this period the following numbers of petitions were issued:

- 2,670 company winding up petitions – a decrease of 21% on the same quarter of 2008 and a decrease of 14% on the previous quarter;
- 4,148 creditors' petitions – a decrease of 12% on the same quarter of 2008 and a 20% decrease on the previous quarter; and
- 13,678 debtors' petitions – a decrease of 11% on the same quarter of 2008 and a 16% decrease on the previous quarter.

Restructuring and insolvency cases

Administration - payment of rent

In the case of *Goldacre (Offices) Ltd v Nortel Networks UK Ltd (In Administration)* [2009] EWHC 3389 (Ch) the question of whether administrators could use their discretion to determine whether they should pay rent as an expense of the administration was considered.

Facts: N was the tenant of two long leases and G was the landlord. N went into administration and its administrators occupied small areas of both premises for the purposes of the administration. G sought confirmation from the court that having decided to use any part of the premises for the administration the administrators were liable to pay the rent in accordance with the terms of the leases as an expense of the administration. N claimed that rent was not an administration expense and that they only needed to pay a portion of the rent equivalent to the amount of the premises which they occupied.

Decision: It was held that the payment of rent was not discretionary and should be paid as an administration expense (in this case quarterly and in advance under the terms of the two leases) so long as the administrators retained or used any part of the demised premises for the purposes of the administration.

Comment: The decision is controversial and gives rise to numerous questions on the responsibilities of administrators of tenant companies, not least as to the status of rent for the period from the date of administration to the next quarter date. Olswang acted for the landlord in this case. For more information in relation to this see [here](#).

Client Money Rules

In the matter of Lehman Brothers International (Europe) (in administration) [2009] EWHC 3228 (Ch) considered issues relating to the identification and distribution of client money held by Lehman Brothers International (Europe) (LBIE) when it went into administration.

Facts: When LBIE was put into administration it had credit balances totalling US\$2.16bn in accounts which were used exclusively for segregating client money. LBIE had to comply with the Client Money Rules contained within the FSA Client Assets Sourcebook (CASS). When segregating client money LBIE followed the alternative approach set out in CASS 7. Under the alternative approach, a firm that receives client money pays the money into its own account and then at the end of each day carries out a reconciliation process to transfer or top up the sums of money held in its segregated client accounts. The operation of this rule should have allowed the clients of LBIE to receive their money back in full, free from creditors' claims on the insolvency of LBIE. One of the problems in this approach is that there is a mixing of client and firm money in house accounts between receipt and segregation.

Unfortunately, to compound this problem, LBIE did not fully segregate large amounts of money for a significant number of its clients, in particular money received from its own affiliates. LBIE had also

deposited US\$1bn of segregated client money with another LBIE affiliate (Lehman Brothers Bankhaus AG (AG)) which became subject to a moratorium by the German regulator.

Main issues: (1) The correct approach to interpret CASS7; (2) whether the statutory trust created by CASS7 came into effect on receipt or upon segregation of the client money; (3) did the client money pool include all identifiable client money held by LBIE, whether segregated or not, and if not segregated how could the client money be identified; (4) could the client money pool be topped up from non-pooled identifiable client money or from the firm's general funds; and (5) how should the amount due to each client be calculated i.e. on the basis of the amount which was segregated for each client or the amount which should have been segregated.

Decision: It was held that where client money was received from, or for the account of a client, the trust arose when the money was received by LBIE. It was also held that there was no requirement to top up the client money pool after the insolvency of LBIE had occurred as this would affect the principle of *pari passu* distribution of a company's assets on an insolvency to unsecured creditors. The amount of money due to the clients should be assessed by reference to the amount of client money which had actually been segregated, not the amount which should have been segregated. The date for calculating all the clients' shares in the money pool should be at the same date and following the decision in the case of *Re Global Trader Europe Ltd (No 1) [2009] EWHC 602 (Ch)*, this should be the date of the administration order.

An appeal in relation to this case was filed on 15 January 2010.

Centre of Main Interests (COMI)

The case of *Hellas Telecommunications (Luxembourg) II SCA [2009] EWHC 3199 (Ch)* concerned a Luxembourg-incorporated telecoms company which sought to shift its COMI from Luxembourg to England and effect a pre-packaged administration sale of its assets (principally the shares in its wholly owned subsidiary) to another company in the same group as Hellas.

Facts: H made an administration application to the English courts on the grounds it was unable to pay its debts and that administration would produce a better result for creditors than a winding up. The main issues before the judge, were whether H fell into the definition of company for the purposes of the Insolvency Act 1986 (the court held that H was a separate legal entity, being a combination of joint stock company and limited partnership, and therefore fell within the definition) and whether H's COMI was in England, which would give the judge jurisdiction to make the administration order sought.

Decision: Under the EC Regulation on Insolvency Proceedings 2000, in the case of a company or legal person, there is a presumption (rebuttable by clear, objective and ascertainable facts) that a company's COMI shall be the place of the company's registered office. The judge therefore considered the following facts on which H relied in support of its contention that it had shifted its COMI from Luxembourg to England three months prior to the administration application:

- a new head office (and principal operating address) had been opened in London, where H's board meetings were held and from where correspondence was sent out;
- H's creditors were noticed of the change of address, and a press release stated that the company's activities were shifting to England;

- a new bank account was opened in London, with all payments made into and from that bank account (although a bank account in Luxembourg remained to deal with minor miscellaneous payments);
- H was registered at Companies House as a foreign company and as a UK establishment of an overseas company (although its registered office remained in Luxembourg); and
- all negotiations between the company and its creditors took place in London.

The judge stated that the purpose of COMI "*is to enable creditors in particular to know where the company is and where it may deal with the company*": on the basis of the evidence (the most important fact being that all negotiations with creditors were conducted in London), he was satisfied that H's COMI had been moved and he accordingly had jurisdiction to make the administration order.

Removal of Administrator

In the case of *Clydesdale Financial Services Ltd and Ors v Smailes* [2009] EWHC 1745 (Ch) it was held that failing to comply with professional guidelines, in this case Statement of Practice 16 (SIP 16), cannot be used as the basis for removing an administrator from office.

Facts: An insolvent firm of solicitors (X) went into administration following advice from S, an insolvency practitioner, who thought that an administration would achieve a better result for the creditors of X than if it were wound up. S became the administrator of X. Y valued X by way of a desktop review, X's files were not examined as part of the valuation and he was entirely reliant on the information provided to him by X. X negotiated a sale of its business. S did not inform the creditors, until a month after his appointment, of the sale. S stated that this letter was intended to comply with the requirements of SIP 16, however it did not contain all the information required by SIP 16 and was actually only sent out to one creditor. C went to court asking for the removal of S from his position as administrator of X on the basis that:

- the letter did not comply with SIP 16;
- that the sale was not likely to achieve the best price for the business of X; and
- the creditors were not consulted before the sale took place.

Decision: On the evidence the administrators had been too closely involved in the negotiations which led to the sale and that taken as a whole the evidence highlighted serious issues for investigation. Since the sale contract had been entered into the majority of X's creditors had supported the application for removal of S. The views of the creditors had to be considered and in the circumstances it was appropriate for the court to remove S from office. However, the court noted that despite the non-compliance with SIP 16 this on its own did not form grounds for the removal of S.

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.

Olswang is committed to being a responsible business and has developed Corporate Responsibility programmes that allow us to actively manage the social and economical impact of the Firm's activities. For example, through our Green initiative we recycle almost 90% of our waste and on the 1 May 2009 Olswang achieved CarbonNeutral® accreditation. As part of our Corporate Responsibility strategy we also encourage every member of staff to engage in lasting and meaningful pro bono and volunteering activities, both legal and non legal.

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.

OLSWANG

London
Olswang LLP
90 High Holborn
London WC1V 6XX
T +44 (0) 20 7067 3000
F +44 (0) 20 7067 3999

Thames Valley
Olswang LLP
Apex Plaza, Forbury Road
Reading RG1 1AX
T +44 (0) 20 7067 3000
F +44 (0) 20 7071 7499

Berlin
Olswang LLP
Potsdamer Platz 1
D-10785 Berlin
T +49 (0) 30 700171-100
F +49 (0) 30 700171-900

Brussels
Olswang LLP
Avenue Louise 326 bte 26
Louizalaan 326 bus 26
B-1050 Bruxelles/Brussel
T +32 2 647 4772
F +32 2 644 2165