Chambers
AND PARTNERS

CHAMBERS GLOBAL PRACTICE GUIDES

Acquisition Finance 2023

Definitive global law guides offering comparative analysis from top-ranked lawyers

UK: Law & Practice
Matthew Tobin, Kathrine Meloni and Rhiannon Singleton
Slaughter and May

UK

Law and Practice

Contributed by:
Matthew Tobin, Kathrine Meloni and Rhiannon Singleton
Slaughter and May

Contents

1. Market p.3
1.1 Major Lender-Side Players p.3
1.2 Corporates and LBOs p.3
1.3 Geopolitical and Global Health Considerations p.4

2. Documentation p.4
2.1 Governing Law p.4
2.2 Use of Loan Market Agreements (LMAs) or Other Standard Loans p.4
2.3 Language p.5
2.4 Opinions p.5

3. Structures p.5
3.1 Senior Loans p.5
3.2 Mezzanine/Payment-in-Kind (PIK) Loans p.7
3.3 Bridge Loans p.7
3.4 Bonds/High-Yield Bonds p.8
3.5 Private Placements/Loan Notes p.8
3.6 Asset-Based Financing p.8

4. Intercreditor Agreements p.9
4.1 Typical Elements p.9
4.2 Bank/Bond Deals p.10
4.3 Role of Hedge Counterparties p.11

5. Security p.11
5.1 Types of Security Commonly Used p.11
5.2 Form Requirements p.14
5.3 Registration Process p.15
5.4 Restrictions on Upstream Security p.15
5.5 Financial Assistance p.15
5.6 Other Restrictions p.15
5.7 General Principles of Enforcement p.16

6. Guarantees p.16
6.1 Types of Guarantees p.16
6.2 Restrictions p.16
6.3 Requirement for Guarantee Fees p.17

7. Lender Liability p.17
7.1 Equitable Subordination Rules p.17
7.2 Claw-Back Risk p.17

8. Tax Issues p.18
8.1 Stamp Taxes p.18
8.2 Withholding Tax/Qualifying Lender Concepts p.18
8.3 Thin-Capitalisation Rules p.19

9. Takeover Finance p.19
9.1 Regulated Targets p.19
9.2 Listed Targets p.20

10. Jurisdiction-Specific Features p.22
10.1 Other Acquisition Finance Issues p.22

Slaughter and May is a leading international law firm recognised throughout the business community for its commercial awareness and commitment to clients. The firm advises on the full range of commercial, financing and other matters. Its financing lawyers are highly regarded for their excellence, broad experience and versatility and have a strong reputation for providing the highest quality of service on the most difficult, demanding and innovative deals, acting for leading UK and international corporates, financial institutions, sovereigns and other organisations. Slaughter and May's acquisition finance practice covers financing for public takeovers, private acquisitions and asset purchases; this work is frequently complex and highly structured, involving sophisticated intercreditor and security-sharing arrangements. The firm's clients in this area include corporate buyers, venture capital and private equity funds, other types of equity investors and arrangers and providers of loan finance and capital markets instruments.

Authors

Matthew Tobin is a partner at Slaughter and May, and head of its financing practice. He advises on a wide range of banking and financing work, including acquisition and bid financing, capital markets and securitisation transactions. Matthew also leads the firm's Sustainable Finance practice, which has advised on several green and sustainability-linked bonds issued by banks and multinationals and on green and sustainability-linked loans. He is regularly invited to speak at conferences and client events and contributes to various banking publications.

Rhiannon Singleton is a senior professional support lawyer at Slaughter and May, focusing on legal, market and documentation issues relating to general banking, acquisition and leveraged finance matters.

Kathrine Meloni is a special adviser and head of treasury insight at Slaughter and May. Her practice focuses primarily on technical issues affecting banking transactions, including legal and regulatory developments and market documentation. She has a particular focus on investment-grade lending, advising the Association of Corporate Treasurers on documentation discussions with the Loan Market Association. Kathrine has published numerous articles on banking and related legal topics and is the author of the "ACT Borrower's Guide to LMA Loan Documentation for Investment Grade Borrowers".

Slaughter and May

1 Bunhill Row
London
EC1Y 8YY
UK

Tel: +44 207 600 1200
Email: webmaster@slaughterandmay.com
Web: www.slaughterandmay.com

SLAUGHTER AND MAY

1. Market

1.1 Major Lender-Side Players

While banks remain a significant source of funding for primary loans, particularly for corporate purchasers, private credit funds have become increasingly prominent, especially when bank lending is constrained. The nature of the acquisition, size of the facility and the identity of the purchaser (especially its credit rating and industry sector) will impact the debt structure, in terms of lender and product choice, with jumbo cross-border deals more typically featuring banks (both local and international). For bank lending transactions, the facilities will mostly be arranged and underwritten by the lead relationship banks, with the debt syndicated more broadly post-closing; for leveraged loan transactions, syndication will generally involve institutional investors.

Recent years have seen a sharp rise in direct lending products, especially for companies in the cross-over/leveraged bracket. Many credit funds have significant amounts of capital to deploy, allowing larger facilities to be offered, creating more scope for these funds to compete directly with the banks. As bank lending capacity was reduced, 2022 saw a sharp increase in the use of direct lending facilities provided by private credit funds, either on a standalone or consortium basis (see **1.2 Corporates and LBOs**), and this looks set to continue throughout 2023.

Other alternatives to bank finance, such as US and European private placements and *schuldschein* (the German private placement market) have become increasingly popular sources of funding for midmarket and smaller acquisitions. Unitranche facilities, for example, allow institutional investors to lend directly to purchasers and can offer a simpler alternative to the traditional senior mezzanine loan structure by combining senior and junior debt into a single tranche with a blended interest rate. Unitranche facilities are increasingly being used outside the sponsor-led market, as corporate purchasers seek to take advantage of the flexibility the structure can offer.

1.2 Corporates and LBOs

The year 2022 was a challenging one for acquisition finance. The end of 2021 had seen an increase in M&A activity and this had been expected to continue into 2022. However, unfortunately the events of the first quarter of 2022 – specifically, Russia's invasion of Ukraine – cast a significant economic shadow. The availability of traditional bank loans fell sharply, with lenders focusing on syndication and refinancing interim debt to clear their loan books, after several cas-

es of hung positions earlier in the year. Arranging bank finance for larger deals was particularly challenging and, while private funds stepped in for much of 2022, there was still a slowdown in transactions; overall 2022 saw fewer higher value deals over GBP1 billion than in 2021. In the sub-investment grade market, leveraged lending levels plummeted, with the leveraged loan and high yield bond markets all but shut during the second half of the year. Rising base rates and macroeconomic pressures triggered a corresponding increase in loan pricing, resulting in a drop in private equity-backed transactions, as returns were affected by the higher cost of capital.

Looking to 2023, while investment grade credits are likely to be able to continue to access debt finance (albeit with higher pricing), for those lower down the credit spectrum, the current climate may present a greater opportunity for alternative sources of acquisition financing, with direct lending products expected to continue to feature prominently. Sponsor-led transactions may also look to other structures, such as consortium or co-investor bids, or higher equity cheques, to mitigate the challenging debt environment.

Other areas of note in 2022 include the continued growth of ESG-linked lending products. It is now common for environmental, social and governance (ESG) objectives to feature in facility agreements, particularly in the context of working capital facilities, but also increasingly in event-driven financings and leveraged loans. Where ESG features are included, they are typically structured as a sustainability-linked loan (SLL), whereby pricing is adjusted based on the achievement of specified sustainability performance targets. The growth in this product has been driven by both banks and sponsors, as a result of increased focus on ESG considerations in internal investment strategies, together with wider reputational implications.

1.3 Geopolitical and Global Health Considerations

See **1.2 Corporates and LBOs**.

2. Documentation

2.1 Governing Law

See **2.2 Use of Loan Market Agreements (LMAs) or Other Standard Loans**.

2.2 Use of Loan Market Agreements (LMAs) or Other Standard Loans

The recommended forms of facility agreement published by the Loan Market Association are generally the starting point for English law loan financings. As part of the transition away from LIBOR to risk-free-rates (RFRs), the Loan Market Association has updated its suite of documentation to include RFR-based agreements, which are the most widely used within the market.

Corporate acquisition facilities may be based on the terms of the corporate's working capital facilities, adapted to include:

- the required acquisition mechanics; and
- any additional protections sought by the lenders to address the group's increased leverage.

Private equity sponsors typically have their own preferred forms of facility agreement. The prevalence of term loan B-style facilities in the leveraged market has resulted in lending terms moving further from Loan Market Association norms.

The terms of investment grade bonds are reasonably standardised. High-yield bond terms are

not published by any trade association or body, but market practice has established a framework that is widely used. The European high-yield market is predominantly a New York law market, so bond terms tend broadly to follow the US style. The covenant exceptions and permissions are usually negotiated in some detail.

2.3 Language

There is no legal requirement that an English law governed loan agreement should be written in English, but it is uncommon for an agreement governed by English law to be drafted in a different language.

2.4 Opinions

Legal opinions are typically provided by the legal advisers to the agent and the arrangers for the transaction, and will be a condition precedent to completion. The lenders will generally require that the opinion covers three key areas:

- the capacity and authority of the entities entering into the finance documentation;
- the validity and enforceability of the finance documentation; and
- the effectiveness of any security to be granted as part of the transaction.

3. Structures

3.1 Senior Loans

Structures

The type and complexity of the financing arrangements depend on the purchaser, the target and its business sector. As mentioned above, corporate acquisitions are typically debt-financed using either:

- pre-existing loan facilities, which are capable of being drawn to fund the acquisition, or which can be amended to include an additional acquisition tranche; or
- newly arranged acquisition facilities.

Leveraged acquisitions will typically involve more complex financing structures, comprising different layers of debt. The financing will usually be secured, with the relationship between the creditors regulated by an intercreditor agreement.

Larger transactions are often funded using a combination of loan and bond finance. The acquisition is financed initially with an underwritten bridge loan (to provide certainty of funding, see **9.2 Listed Targets**), which is subsequently replaced with permanent long-term loan finance or, more commonly, refinanced with the proceeds of a capital markets issue (see also **3.3 Bridge Loans** and **3.4 Bonds/High-Yield Bonds**).

Senior Loans

Senior loans often comprise term loan tranches, coupled with a revolving credit (and ancillary) facilities. These facilities will usually be secured and the senior loans will rank in priority to other debt, both contractually pursuant to an intercreditor agreement and/or structurally; for example, junior debt may be lent at holding company level, making it structurally subordinated to the senior loans.

How senior loan facilities are structured in the European leveraged market has evolved significantly. Historically, senior loans comprised a six-year amortising term loan A, a seven-year term loan B and an eight-year term loan C, alongside working capital facilities. Since the 2008 financial crisis, amortising term debt has become less prominent and many senior acquisition facilities comprise a single tranche term loan B (TLB).

TLBs, which originated in the USA, have emerged to become a prominent feature of the European landscape. US-style TLBs are institutionally-led non-amortising term loan facilities. Their defining feature is that they are "covenant-lite"– this means the comprehensive suite of maintenance covenants commonly seen in traditional senior loan facilities (of the kind reflected in the Loan Market Association's leveraged finance documentation) is replaced with a set of incurrence-style covenants, more akin to those seen in a high-yield bond indenture.

The incurrence covenant model does not:

- prevent the borrowing group from taking specific actions on an ongoing basis subject to negotiated exceptions; or
- require the borrowing group to maintain any financial ratios or demonstrate periodic compliance.

Instead, the borrowing group is permitted to incur further debt, pay dividends, make payments on subordinated debt and grant security subject to financial parameters that are only tested as and when the action in question is taken. These financial parameters (or "incurrence tests") can comprise the same types of financial covenant ratio (for example, leverage) used in a traditional bank loan, but are used in a very different way and generally coupled with a number of other exceptions and baskets. In addition, the covenants may only apply to a restricted number of key companies in the group, rather than the whole group, known as "restricted subsidiaries" (see **5.1 Types of Security Commonly Used**).

The covenant-lite model is therefore much less restrictive from the point of view of the borrowing group. It is designed to allow the group to evolve subject to maintaining its overall leverage and debt service profile. Rather than shaping the group's movements, the covenants act as a brake if the company decides to take any restricted action that increases the investors' credit risk beyond the agreed limits.

Other advantages of covenant-lite loans for borrowers and sponsors include:

- greater flexibility to run the business without the continuing need for lender consents (and related fees);
- the benefits of a high-yield bond without the public reporting requirements; and
- for issuers who access both the loan and the bond market, the convenience of consistent terms across their debt package.

Rather than being written in the US style, European covenant-lite typically uses the broad framework of a Loan Market Association loan agreement as its starting point (although there are a range of approaches). The Loan Market Association financial covenants are removed and the negative covenant package is either adapted to incorporate incurrence-style permissions or replaced entirely with a schedule of high-yield bond style covenants. In most cases, the facility documentation is governed by English law. Where high yield-style covenants are adopted, for consistency, the covenant schedule is usually governed by New York law.

European covenant-lite is similar, but not identical in all respects to the New York law product. There also remains some variation in the terms that are achieved deal-to-deal. Further, in a European context, the term "TLB" does not always necessarily denote a covenant-lite loan in the sense described above. The market also encompasses a variety of leveraged term loans with more flexible terms than those which have

traditionally been applied to European leveraged loans. A European TLB may be covenant-lite, but the term TLB may also be used to encompass a "covenant-loose" loan – one containing limited maintenance covenants accompanied by some of the other features more usually associated with a covenant-lite loan (for example, the ability for the group to incur further debt).

The concept of "springing" financial covenants is also relevant to the new generation of European revolving credit facilities (RCFs) offered to leveraged borrowers. If the borrower's only term debt takes the form of high yield notes or covenant-lite TLB (and therefore does not include maintenance covenants), it is generally the case that the revolving credit facility lenders will be offered a loose maintenance covenant (usually a leverage covenant) that is tested on a springing basis if the revolving credit facility is drawn by more than a certain amount on any quarter date.

TLBs are now the dominant senior lending structure for leveraged lending.

3.2 Mezzanine/Payment-in-Kind (PIK) Loans

As mentioned in **3.1 Senior Loans**, leveraged acquisitions tend to involve more complicated secured debt structures. The debt finance will typically take the form of senior loans, and may also involve junior – mezzanine/payment-in-kind (PIK) – loans, although these structures are not so commonly used since the 2008 financial crisis. Second lien facilities tend to emerge when the debt markets are more liquid. These are facilities that rank pari passu with the senior debt in terms of payments, but have a second ranking claim to the senior security package on enforcement.

Subordinated debt can also be accessed via unitranche facilities. Unitranche facilities blend senior and junior debt into a single facility. The facility comprises a single term loan with a blended interest rate, often coupled with a super-senior ranking RCF. The term loan will be made by private credit funds, while the RCF is generally made by banks (as non-bank lenders may not be able to provide working capital facilities). The participants in the term loan will agree the ranking of their respective claims and yields between themselves in a separate agreement. As the term loan is priced on a blended basis, interest will usually be higher than traditional bank funding.

3.3 Bridge Loans

Bridge loan facilities are intended to be short-term and are therefore structured to encourage swift refinancing. In practice, bridge facilities tend to be refinanced before they are drawn.

A bridge will generally be available for drawdown for the shortest period sufficient to permit the completion of the acquisition. The period will depend on the nature of the acquisition and, in particular, the length of time needed to obtain any consents or anti-trust clearances that are required. The maximum tenor of an English law bridge facility is generally 24 months, typically comprising an initial term of 12 months, subject to one or two extension options. Extension options (if applicable) are normally exercisable at the option of the borrower (so do not require lender consent), although they are likely to be subject to the borrower's compliance with the representations and undertakings in the loan agreement, the absence of any event of default and the payment of an extension fee.

Bridge loans are popular for larger transactions, which need to access the debt capital markets as well as the loan markets. A bridge provides

certainty of funding for the purposes of the acquisition, while allowing more time for any long-term capital markets issuance to be put in place. They are commonly used in public takeovers, where timetable pressures, together with the requirement that details of the initial debt funding the acquisition be disclosed publicly, can make the use of a bridge a practical option (see **9.2 Listed Targets**).

It is also common to see "interim" facilities negotiated, alongside pre-agreed commitment papers for the take-out financing. Interim facilities typically comprise short form loan facilities with minimal covenants which are designed to be replaced or refinanced with term loan debt and/or a full form bridge loan facility that will be refinanced in the capital markets. The use of interim facilities tends to increase in busy periods, particularly for private equity-backed acquisitions, as bidders seek to put financing terms in place as quickly as possible on certain funds terms.

3.4 Bonds/High-Yield Bonds

Bonds may be used to finance acquisitions. Bond finance is generally employed in conjunction with an initial bridge loan, which is refinanced out of the proceeds of the bond issue on or after completion of the acquisition. This is because it can be difficult from a timetabling perspective (although not impossible) to issue a bond to fund an acquisition upfront, which is why a bridge facility is used as a backstop. See **3.3 Bridge Loans**.

Acquisition financings under commitment papers, often with an interim facility agreement and a pre-completion capital markets issuance into escrow (ie, such that the bridge facility is not actually drawn) are also possible, although historically unusual and still less commonly seen than in some other jurisdictions (such as the USA).

3.5 Private Placements/Loan Notes

Some issuers may use privately placed notes (for example, a US private placement or *schuldschein*) to fund or part-fund acquisitions. As with bonds, these products may be used in conjunction with a bridge facility and other forms of debt.

In certain leveraged financing structures, loan notes form part of the equity investment from the sponsors or are used to finance deferred consideration payable to the vendors. The Loan Market Association's leveraged documentation contemplates that both investor and/or vendor loan notes may be issued as part of the financing for the acquisition, and that they will be subordinated to the senior liabilities and any high-yield bonds. Investor loan notes may be issued as an alternative to (or in conjunction with) the sponsor's subscription for shares in the holdco company. Vendor loan notes can be used where, for example, the acquisition is subject to an earn-out, allowing the vendors to receive additional consideration at a later date if specified performance objectives are met by the target company (particularly as part of a management buyout).

3.6 Asset-Based Financing

Asset-based financing is a form of senior secured lending, whereby funds are advanced based on the value of certain of the borrower's assets, and can be useful for acquisition financings. While it is a specialised area of lending and will not be suitable for all transactions, in an acquisition context, the target's assets may be used as the borrowing base for the facility, leveraging the performance of the asset class (instead of EBITDA) to determine the availability of the loan and monitor its performance.

While the structure will depend on the nature of the assets involved, asset-based lending can offer an alternative to cash-flow funding, as the interest charged will often be lower (as the facility will be closely linked with the valuation of the secured assets), and there may be fewer and more flexible covenants than a typical secured term loan. The facility will be secured against the relevant asset class and can be provided on its own or part of a wider debt package.

4. Intercreditor Agreements

4.1 Typical Elements

The relative priorities of the different classes of creditor can be established by the use of either:

- structural subordination, which involves the structurally subordinated creditors lending at a higher level in the group structure than the senior creditors; or
- contractual subordination, where the creditors document the agreed ranking among themselves in an intercreditor agreement.

The parties to the intercreditor agreement generally include each class of finance provider – for example, senior lenders, hedge counterparties, high-yield bondholders and any providers of intra-group debt or intra-group loans which downstream any equity contributions into the borrowing group. In larger transactions, the recommended forms of intercreditor agreement published by the Loan Market Association are often used as a starting point. However, the Loan Market Association templates generally require significant alteration to fit the applicable capital structure, which may be more or less complex than the assumed transactions contemplated by the Loan Market Association templates.

To protect the agreed subordination, each creditor group is subject to restrictions on the extent to which they can amend or waive the terms of their debt. To preserve the seniority of the senior creditors' claim, each class of creditor (other than the senior creditors) is generally restricted in relation to:

- the principal, interest, fees and other payments they are permitted to receive; and
- the steps they can take to enforce their debt.

Payment of Principal, Interest and Fees

Typically, both scheduled payments of principal and voluntary and mandatory prepayments of principal for the senior debt (whether that comprises loans, bonds or both) are permitted in accordance with the terms of the relevant senior debt. Payments of interest and fees on the senior debt are also unrestricted.

In leveraged financing structures, hedge counterparties usually have a senior or super-senior ranking claim to the same security package as the providers of the senior debt (whether that comprises loans, bonds or both). Scheduled payments due to any hedge counterparty under the terms of the hedging agreements are therefore permitted, although the circumstances in which the hedging transactions may be closed out will be subject to controls.

Typically, junior lenders are entitled to payments of cash pay interest, fees and indemnity payments in accordance with the terms of their debt, but their rights to receive payments of principal are heavily restricted. For example, in a senior/mezzanine loan structure, the mezzanine lenders are entitled to receive their share of any voluntary or mandatory prepayments only once the seniors are paid. Other prepayments of principal

may be allowed only where the prepayment is the result of:

- the operation of the illegality clause; or
- a tax or increased costs claim under the mezzanine loan agreement.

In any event, any payments to the mezzanine lenders will be subject to a payment stop following a senior default (which will occur automatically following a senior payment default, and on notice from the senior lenders following other defaults that are specified as stop events). Sometimes exceptions are negotiated – for example, to enable the mezzanine lenders to bring a claim for restructuring costs in a default scenario – but these are often very limited. The circumstances and duration of a payment stop are usually negotiated.

Payments to intra-group lenders are generally permitted (as they do not involve cash leaving the group) but are subject to an automatic stop on the occurrence of a default/event of default under the terms of the external creditors' debt documents.

Payments in respect of equity/quasi-equity financing involving cash leakage from the borrowing group are typically subject to strict conditions. These conditions are usually documented separately to the intercreditor agreement, which will refer back to the restricted payment covenants in the relevant loan and/or bond documentation.

Sharing Arrangements

If any of the creditors receive a payment (or the benefit of a payment) to which they are not contractually entitled in accordance with the intercreditor agreement, a turnover trust or claw-back mechanism generally ensures that the prior ranking creditor (or security trustee on their behalf) is able to recover the relevant amount from the junior creditor.

4.2 Bank/Bond Deals

As the prevalence of bank/bond deals increased, intercreditor terms (or the range of possibilities) became more standardised, leading the Loan Market Association to publish forms of intercreditor agreement for bank/bond structures comprising agreements contemplating transactions involving senior secured notes, high yield notes, and super senior facilities.

Where the secured debt package comprises a super-senior RCF and senior secured notes, the relationship between the bank debt and notes is typically as follows.

- Scheduled payments of principal and interest are permitted at all times to the RCF lenders and senior secured noteholders (referred to collectively as the "primary creditors"), save for an optional – and reciprocal – payment stop on enforcement. Junior liabilities, comprising intra-group obligations and vendor and equity liabilities, are contractually subordinated and payments are permitted only in accordance with their terms, as discussed above in relation to senior/mezzanine intercreditor structures.
- The RCF lenders (and associated hedge counterparties) rank first in the payment waterfall for the purposes of the proceeds of enforcement of the security package.
- There is no enforcement standstill applicable to the unsecured junior liabilities, save that proceeds of enforcement must be turned over.
- Voting instructions are generally passed on a majority super senior RCF and majority senior secured noteholder basis, save on enforce-

ment where the super-senior RCF lenders' instructions will take priority in limited circumstances (for example, where there is a failure to progress within a specified period).

- If high-yield notes are issued in conjunction with the senior secured notes and super-senior RCF, the intercreditor terms will operate slightly differently (it is assumed that the high-yield notes will be both structurally and contractually subordinated), as follows.
- Payments to the RCF lenders and senior secured noteholders typically operate as described above. In regard to the high-yield noteholders, permitted payments are generally subject to similar restrictions as mezzanine lenders, with similar payment stop mechanics. The high-yield noteholders are also subject to an enforcement standstill.
- All parties will typically be secured, although the high-yield noteholders' security is often less extensive, with two layers of security included:
  (a) security granted in favour of the "priority creditors" (ie, the RCF lenders, senior secured noteholders and related hedging counterparties); and
  (b) security granted in favour of all parties by the parent over its shares in the borrower and its rights in relation to intra-group debt (the "common transaction security"), in relation to which the high-yield noteholders will rank behind the other parties.
- Before enforcement, voting is typically carried out on a majority super-senior RCF lender and majority senior secured noteholder basis (as above) with the majority high-yield noteholders taking control of voting only after discharge of the RCF and senior secured notes. On enforcement, the RCF lenders and senior secured noteholders control the process, with the high-yield noteholders granted limited instruction rights on enforcement of the common transaction security.

4.3 Role of Hedge Counterparties

Leveraged transactions may require the borrower to enter into hedging arrangements to mitigate against interest rate and, for some transactions, exchange rate fluctuations. The hedge counterparties will be party to the intercreditor agreement, and rank pari passu with the senior facilities and share in the security package.

Scheduled payments under the hedging will usually be permitted until the seniors enforce or an insolvency event occurs. Generally, close-out (enforcement) will only be permitted for payment default (subject to illegality or tax events) or upon senior enforcement (and the senior lenders can force the hedging lenders to close-out if they are enforcing).

5. Security

5.1 Types of Security Commonly Used

Investment grade acquisition financings may be guaranteed or provided on an unsecured basis.

Financings for sub-investment grade/cross-over and leveraged credits usually involve the provision of both guarantees and security to the senior lenders and, if applicable, on a second-ranking basis to the junior (mezzanine) lenders.

The implementation of the security package is usually phased as follows:

- before the closing date, the lenders take security over the shares in the acquisition vehicle and its rights under the acquisition agreements; and

- after the closing date, the acquisition vehicle grants security over the shares of the target.

The remainder of the transaction security (which comprises both share security and asset security provided by the target and members of its group) is put into place within an agreed period from the date of closing, in accordance with a set of "agreed security principles" (that is, principles outlining the security sought and the considerations to be taken into account in determining whether security should be provided).

Guarantees are provided on a similar basis and are normally required from all "material companies". Material companies may be named companies in the target group. However, they are more commonly defined as all companies that represent a minimum percentage of the group's total assets or earnings before interest, taxes, depreciation and amortisation (EBITDA).

The agreed security principles normally provide that security will be granted over all shares and all assets of each company in the acquired group (or each material company) subject to agreed exceptions, for example where:

- there are legal impediments to granting security; or
- to grant security would involve disproportionate costs or present significant practical challenges.

If the group involves English companies only, it is legally straightforward to take all-asset security. The main legal impediments can be dealt with as a practical matter in most transactions.

Any exclusions are likely to be made only on the basis of a cost/benefit analysis and on a negotiated basis. For example, dormant subsidiaries or group companies with no material assets may be excluded. Similarly, if third-party consents are required for the provision of security (such as from landlords in relation to leased real estate or counterparties in relation to book debts and receivables), a commercial decision will be taken as to whether the value of the relevant security asset warrants those consents being pursued.

If the transaction is to be secured, the extent of the security is both a matter for negotiation and (to a certain extent) driven by the nature of the financing. In broad terms, where the debt is financed, or is to be refinanced shortly after closing, in the high-yield market the security package will be structured differently and may be less extensive than if the transaction is financed entirely in the covenanted loan market. Where the security is ultimately intended to benefit high-yield bondholders, the issuer group will generally be divided into (i) restricted subsidiaries and (ii) unrestricted subsidiaries.

Unrestricted subsidiaries are excluded from most of the contractual restrictions in the bond indenture and do not provide guarantees or security. The concept of a "restricted subsidiary" is broader in application than the concept of material companies referred to above (which is more common in the loan market as a means of defining guarantee/security coverage). This approach to the provision of security and guarantees (the designation of restricted and unrestricted subsidiaries to determine the scope of the security package) is also often used in the TLB market.

Types of Security

The choice of security interest depends on the nature of the asset and its importance in the context of the security package. Secured acquisi-

tion finance typically involves a combination of mortgages and charges.

Mortgages involve the transfer of title to the asset to the mortgagee by way of security, with a right to the transfer back of the mortgaged property when the secured obligation is satisfied. A mortgage can be legal or equitable (depending on whether legal or equitable title has been transferred). The form of transfer will depend on the nature of the asset in question. Mortgages over claims or receivables, for example, involve the assignment of rights by way of security; if the assignment complies with the requirements of Section 136 of the Law of Property Act 1925 it will be a legal mortgage, and if it does not then it will be an equitable mortgage.

Lenders do not generally require the more complex steps required to transfer legal title to an asset by way of legal mortgage to be taken in respect of all security assets at the outset of the transaction. In general, only the following are the subject of legal mortgages:

- freehold property;
- significant items of tangible movable property; and
- aircraft and ships.

In relation to other types of asset, equitable security is created and the secured creditors rely on contractual further assurance clauses and a security power of attorney to enable the transfer of legal title on the security becoming enforceable.

A charge involves an agreement by the chargor that certain of its property be charged as security for an obligation. It is a security interest which entails no transfer of title or possession to the chargee. In practice, there is little to distinguish a charge from an equitable mortgage, as the enforcement rights of a mortgage (such as the power to take possession, to sell the secured assets, and/or appoint a receiver) are routinely included in documents creating charges. More significant is which of the following forms the charge should take:

- A fixed charge – this attaches to a specific asset and restricts the chargor from dealing with (for example, disposing of) that asset.
- A floating charge – this attaches to a class of assets and the chargor is permitted to deal with those assets in the ordinary course of business without the consent of the chargee pending an event which causes the charge to "crystallise"; most floating charges encompass all of the chargor's assets, whether they are:
  (a) existing or future; or
  (b) tangible or intangible.

The main consequence of the characterisation of a charge as fixed or floating relates to the ranking of payments on insolvency. For example, the expenses of both liquidations and administrations are paid out of floating charge assets. These expenses can be very considerable and may exhaust all the floating charge assets. A floating charge also ranks behind certain claims of certain preferential creditors (broadly, certain rights of employees and certain amounts owing to Her Majesty's Revenue and Customs, HMRC) and, in respect of charges created on or after 15 September 2003, the "prescribed part", a ring-fenced fund, capped currently at GBP800,000 (where the floating charge was created on or after 6 April 2020, and is capped at GBP600,000 for charges created before that date), is also paid out of floating charge assets to unsecured creditors in priority to the floating chargee.

The other key difference between fixed and floating charges is that the holder of a floating charge which constitutes a "qualifying floating charge" relating to the whole or substantially the whole of a company's property enjoys privileged appointment rights in an administration. See **5.7 General Principles of Enforcement**.

When characterising a charge as fixed or floating, the courts will consider the substance of the relationship between the parties. The label attached by the parties themselves is largely irrelevant and, if inconsistent with the rights and obligations that the parties have granted to one another, the security will be re-characterised.

5.2 Form Requirements

English law security for acquisition financing typically takes the form of a debenture, which purports to take fixed security over as many of the chargor's assets as possible, together with a floating charge to sweep up other assets of the chargor. The following is a broad indication of the forms of security which can be taken over various types of asset pursuant to a debenture.

Shares

Security over registered shares usually takes the form of an equitable mortgage or fixed charge. A legal mortgage of shares requires the transfer of legal ownership which can have adverse tax and accounting consequences for the lenders. To facilitate enforcement, the certificates for the shares are usually deposited with the chargee together with signed but undated forms of transfer. If necessary, the target's articles of association (articles) are amended to ensure there are no restrictions on transfer in the event of enforcement.

Inventory

Security over a company's circulating assets is (by definition) encompassed within the floating charge.

Bank Accounts and Receivables

The appropriate method of taking security over claims and receivables such as book debts, bank accounts and cash depends on whether it is practical to create fixed security. If the intention is to create a fixed charge, the security document must contain adequate restrictions on the chargor's ability to deal with both the asset and its proceeds, and those restrictions must be complied with in practice. This generally means that the proceeds of charged receivables must be paid into a blocked account. This may be achievable in relation to certain specific sums (for example, the proceeds of certain disposals and other amounts that are required to be applied to prepay the loans). However, companies will need to have access to at least some of their bank accounts, so fixed security will not be achievable in all cases.

Intellectual Property Rights

These rights are more commonly the subject of a charge. A legal mortgage or assignment of the rights to intellectual property by way of security necessitates an exclusive licence back to the assignor to enable it to continue to use the rights, including a provision for re-assignment on discharge of the security.

Real Property

Legal mortgages can be taken over freehold property, depending on its value. Title is transferred to the mortgagee in writing alongside the title deeds if a legal mortgage is to be created. An equitable mortgagee will also generally request delivery of the title deeds.

Movable Assets
Significant items of tangible movable property can be the subject of a legal mortgage, but are more commonly the subject of equitable security for the reasons given above.

Registration Requirements
Security created by a company incorporated in England and Wales must be registered to protect the secured creditors. See further **5.6 Other Restrictions.**

5.3 Registration Process
Security interests created by English companies must be registered at Companies House within 21 days of creation, regardless of whether they are granted:

- over assets located in the UK or in a foreign jurisdiction; or
- under an English law or foreign law security document.

If this is not done, the security will be void as against a liquidator, administrator or creditor of the company and the secured liabilities will become immediately repayable.

The process for registration is specified by the Companies Act 2006: for charges created by a company registered in England and Wales, a "statement of particulars" (the prescribed forms to be completed are available from Companies House), together with a certified copy of the security instrument must be registered at Companies House. If the security is not created or evidenced by an instrument, a separate form must be completed. Forms can be filed in hard copy or electronically, and a filing fee is payable.

5.4 Restrictions on Upstream Security
See **5.5 Financial Assistance**.

5.5 Financial Assistance
The Companies Act 2006 restricts the provision of financial assistance for the purpose of:

- the acquisition of the shares of the target; and
- the reduction or discharge of a liability incurred for the purpose of the acquisition of the shares of the target.

The following are prohibited from providing financial assistance:

- if the target is a public company formed and registered under the Companies Act 2006, the target and any of its subsidiaries (whether public or private); and
- if the target is a private company formed and registered under the Companies Act 2006, any subsidiaries of the target that are public companies.

A number of exceptions apply but they are often not relevant in the context of acquisition finance. In practice, if security and guarantees are required from the target group then, post-acquisition, the relevant public companies in the target group will be re-registered as private companies before the financial assistance is given.

5.6 Other Restrictions
Other than registration of the security at Companies House (see **5.3 Registration Process**), the main considerations in terms of the validity of security are the presence of corporate benefit and the claw-back rules under the insolvency regime, as well as the financial assistance rules.

Corporate benefit is analysed on a company-by-company basis. The perceived benefits are recorded in the security provider's board minutes. A transaction that might otherwise fall outside the scope of the directors' powers can be

ratified by a unanimous shareholder resolution. Secured creditors usually require such a resolution to be passed by each provider of upstream or cross-stream security as a condition precedent to funding.

5.7 General Principles of Enforcement

Generally speaking, lenders are able to enforce security themselves (or through a security trustee acting on their behalf) without applying to court. The triggers for enforcement will mainly be a matter of contract, and well-drafted security documentation will include detailed provisions relating to the timing and manner of enforcement. Such enforcement rights will usually be extremely broad and permit the lender to undertake a range of actions (such as a power of sale and a right to appoint a receiver). It is more common for lenders/security trustees to appoint a receiver (or, where appropriate, an administrator, discussed below) to enforce the security, rather than enforce it themselves.

If the security document does not include mechanics relating to the enforcement of security, rights are available as a matter of law under the Law of Property Act 1925 and the Insolvency Act 1986. It is common for the contractual rights of enforcement included in security documentation to expressly include (and enhance) all rights available as a matter of law.

If the security includes a floating charge over all or substantially all the security provider's assets (a "qualifying floating charge") the lender will also have important rights in relation to the commencement of administration proceedings under the Insolvency Act 1986 to enforce its security. A qualifying floating charge-holder may:

- appoint an administrator (either in court or out-of-court) at any time when the charge is enforceable; or
- substitute their own preferred candidate for an administrator proposed to be appointed by any other person.

Once a company enters into administration, it will benefit from a moratorium, preventing creditors from enforcing their claims. Administration proceedings allow an administrator to try and rescue a struggling company or achieve a better result for creditors than if the company were wound up (which often means selling the company and distributing the proceeds to those entitled, including the secured creditors). If neither of these objectives are achievable, the administrator will realise the assets to make a distribution to the secured creditors.

6. Guarantees

6.1 Types of Guarantees

See **5.1 Types of Security Commonly Used**.

6.2 Restrictions

When considering whether it is appropriate to enter into a guarantee, the directors of the company must consider whether it is in the best interests of the company to give the guarantee. For downstream guarantees, the directors may be able to conclude that borrowing funds under the facility agreement (particularly if it is a condition of the agreement that the parent provides a guarantee) will enable the subsidiary to carry on and enhance its business, thus increasing both its own value and the dividends the parent guarantor will receive.

Upstream guarantees can be more complicated. The analysis will always depend on the

facts of each transaction, but relevant factors may include the benefit the guarantor will derive from being a member of a group which will have access to increased liquidity or, if the guarantor is dependent on the borrower for liquidity support or other intra-group services, the benefit derived may be the continuation of those services as a result of the loan being made to the borrower.

Maintenance of capital rules must be complied with, and upstream guarantees may also need to consider financial assistance restrictions (see **5.5 Financial Assistance**). The lenders are likely to require a shareholder resolution to be passed to approve upstream guarantees.

6.3 Requirement for Guarantee Fees

There is no requirement for a guarantee fee to be charged. However, there may be circumstances in which it is appropriate for a fee to be paid, including to help with the corporate benefit analysis discussed above, particularly in relation to upstream or third-party guarantees.

7. Lender Liability

7.1 Equitable Subordination Rules

See **7.2 Claw-Back Risk**.

7.2 Claw-Back Risk

The "claw-back" rules relating to transactions at an undervalue, preferences and voidable floating charges under the Insolvency Act 1986 may all be relevant in relation to any security granted as part of the financing package for an acquisition.

A transaction entered into by a company incorporated in England and Wales, or any foreign company subject to English insolvency law proceedings, is at risk of being challenged by the insolvency officer if both of the following apply:

- it is given within a certain period of time prior to commencement of liquidation or administration; and
- it represents a preference, a transaction at an undervalue or is a voidable floating charge.

To be considered a preference, all of the following must apply:

- the transaction must have been entered into within the specified period;
- the company must have been influenced by a desire to produce a preferential effect; and
- the company must have been insolvent (as defined by statute) at the time of the transaction or become so as a result of entering into it.

A voidable transaction at an undervalue must have been entered into within the vulnerable period and the company must have been insolvent (as defined by statute) at the time of the transaction, or become so as a result of entering into it. In practice, this ground for challenge is of relatively limited concern in most secured loan transactions because of the good faith defence that is available. It is therefore a defence if both of the following can be shown:

- the transaction was entered into by the company in good faith and for the purpose of carrying on its business; and
- at the time of the transaction, there were reasonable grounds for believing that it would benefit the company.

A floating charge may be set aside except to the extent of the value given to the company at the same time as or after the creation of the

charge. If the parties are not connected, it is a defence if the company was solvent (within the statutory definition) when the charge was created and did not become insolvent as a result of the transaction.

The vulnerability periods are:

- six months for preferences (two years if the counterparty is a connected person);
- two years for transactions at an undervalue; and
- one year for a voidable floating charge claim (two years if the counterparty is a connected person).

8. Tax Issues

8.1 Stamp Taxes

The execution of a loan agreement will not, in itself, attract stamp taxes in England and Wales. In any event, the finance documentation for an acquisition will usually seek to protect the lenders against any stamp taxes that might arise; for example, the Loan Market Association's recommended forms of agreement, including its template for leveraged acquisition transactions, include an indemnity from the obligors for any stamp taxes, together with a representation that no filing obligations or stamp taxes apply.

Transfers of shares generally attract stamp duty, payable on the consideration for the transfer. If the loan agreement is secured and includes security over shares, however, stamp duty will not be chargeable as a transfer of shares by way of security is exempt from stamp duty as it is deemed (for the purpose of stamp taxes) that there is no consideration payable for the grant of security.

8.2 Withholding Tax/Qualifying Lender Concepts

It is standard for the borrower to be required to gross up interest payments for any tax payable and to indemnify the lenders in respect of certain other tax liabilities relating to the loan agreement. However, there are multiple exemptions from UK withholding tax. It is, therefore, standard practice for borrowers to agree to gross up (and therefore in practice include in syndicates) only lenders to whom one of these exemptions apply, defined as "qualifying lenders". The borrower's obligation to gross up lenders in respect of withholding tax liabilities is limited to lenders who are qualifying lenders on the date of the agreement. The result very broadly is that the gross up obligation is triggered only if, after the date of the agreement, there is a change in law that results in the relevant lender losing its qualifying lenders status.

The concept of a qualifying lender is reflected in the Loan Market Association's English law documentation for investment grade and leveraged transactions. The concept essentially captures lenders who (on the basis of the UK tax regime in existence at the date of the agreement) can be paid free of withholding tax – allowing the borrower to conduct due diligence on its syndicate at the outset of a transaction that only those lenders to whom withholding tax does not apply are participating in the loan. From a borrower's perspective, the risk of paying withholding tax in relation to the primary syndicate should generally only apply if there is a change in law. Lenders joining the syndicate after primary syndication are typically required to confirm their qualifying lender status.

8.3 Thin-Capitalisation Rules

A company may be thinly capitalised due to either:

- a special relationship between the borrower and the lender; or
- a guarantee given by a person connected with the borrower (such as a parent company) in respect of debt advanced by a third party.

Thin capitalisation can, therefore, impact the deductibility of interest for tax purposes on an acquisition finance transaction, although deals are typically structured to minimise any potential impact as far as possible.

The UK rules require each borrower to be considered according to its own financial circumstances for the purposes of determining the amount which it would have borrowed from an independent lender and whether it should be considered to be thinly capitalised. The assets and income of the borrower's direct and indirect subsidiaries can be taken into account to the same extent that an unconnected lender would recognise them, but the assets and income of other group companies are disregarded.

There is no "statutory safe harbour" under the UK regime by reference to which tax relief is assured. Historically, His Majesty's Revenue & Customs, HMRC (which deals with tax matters in the UK) would not generally regard a company as thinly capitalised where the level of debt to equity did not exceed a ratio of 1:1 and the ratio of income (EBIT) to interest was at least 3:1. However, current guidance moves away from this to apply the "arm's-length" standard on a case-by-case basis and assumes that borrowing will be on a sustainable basis, so that the business must be able to trade, invest and meet its other obligations as well as servicing the debt.

9. Takeover Finance

9.1 Regulated Targets

Regulated Industries

If competition issues arise, the Competition and Markets Authority or the European Commission may have jurisdiction over an acquisition or merger in any sector. Similarly, if the bidder is a listed company, the requirements of the UK Listing Rules (which, for example, require that shareholder consent is sought for transactions within certain parameters) may affect the transaction. If the target is a listed company, the requirements of the Takeover Code will also be relevant (see further **9.2 Listed Targets**). Where the acquisition falls within the scope of the National Security and Investment Act 2021, this will also affect the timetable for the transaction (see further **10.1 Other Acquisition Finance Issues**).

In addition, transactions in certain sectors may give rise to specific requirements. Regulated industries in the UK include the following sectors:

- utilities (such as water and power);
- financial services;
- insurance; and
- media and communications.

Effect on Transaction

The effect on the transaction will vary according to the sector. For example, the consent of the regulator may be required and/or sector-specific licence requirements may need to be complied with. Regulatory compliance by the target group and the maintenance of its required authorisations may need to be addressed in the terms of the debt financing documents (for example, in the representations, undertakings and events of default in the loan agreement).

9.2 Listed Targets

Specific Regulatory Rules

If the target is a listed company, the Takeover Code, which governs the conduct of takeovers and mergers of public companies in the UK, must be complied with. The Takeover Code is administered by the Takeover Panel, which has various statutory powers under Part 28 of the Companies Act to address non-compliance, including the power to impose financial penalties.

Methods of Acquisition

Takeovers of listed companies are structured either as contractual offers or schemes of arrangement.

A contractual offer involves an offer by a bidder to all shareholders, which may or may not be recommended by the board of directors to the shareholders. A contractual offer requires acceptances in excess of 50% of the issued share capital of the target to obtain sufficient control to complete the transaction. In practice, acceptance conditions are often set at a higher level.

A scheme of arrangement is typically used for recommended offers only under Section 896 of the Companies Act. A scheme of arrangement is initiated by the target company and must be approved by both the requisite percentage of shareholders and the court. A scheme requires the approval of 75% in value of the shareholders present and voting in person or by proxy at the court meeting to approve the scheme. If the scheme achieves 75% approval, the bidder will automatically acquire 100% of the shares. The majority of takeovers of listed companies in the UK are completed by way of scheme of arrangement.

Funding

The bidder must announce a bid only after ensuring that it can fulfil in full any cash consideration, having taken all reasonable measures to secure the implementation of any other type of consideration (General Principle 5, Takeover Code). The bidder should only announce a firm intention to make an offer if, after careful and responsible consideration, it has every reason to believe that it can and will continue to be able to implement the offer (Rule 2.7(a), Takeover Code).

The "cash confirmation" requirement states that if an offeror offers to pay the consideration wholly or partly in cash, its financial advisor must confirm that the bidder has sufficient cash resources available to it to meet this requirement. This confirmation must be incorporated into the offer documentation. Debt or equity financing arrangements intended to finance takeovers must therefore be provided on a "certain funds" basis, which normally means that a loan facility is required to satisfy these requirements, even if the intention is ultimately to finance the offer in the public markets.

Market practice, rather than the Takeover Code, dictates the conditions to which a certain funds facility may be subject. In summary:

- the facilities must be underwritten before the offer is announced; and
- most of the typical conditions precedent to the availability of funds must be satisfied when the agreement is signed.

Broadly speaking, to satisfy the certain funds requirement, any remaining conditions must (as applicable):

- be within the control of the offeror to satisfy (for example, the covenants restricting the

incurrence of indebtedness or the creation of security);
- depend on the offer proceeding (for example, receipt of the required level of acceptances or approval for the scheme); or
- relate to the solvency of the bidder.

The requirements of the Takeover Code with regard to confidentiality affect to whom information regarding a potential offer may be disclosed prior to the bid being announced. The Takeover Code also requires that all shareholders have access to equal information. These rules affect the manner in which debt can be arranged and syndicated both prior to and after the commencement of an offer period. However, they have been in place now for some time and the procedures to be put in place to facilitate compliance are well established.

The Takeover Code also contains a number of requirements with regard to the information that is to be made publicly available in relation to the financing of the bid:

- the financing documents must be made publicly available at the time the bid is announced and only very limited aspects are permitted to be redacted; and
- the offer document, when subsequently published, must include a description of how the offer is to be financed and the sources of the finance, together with details of any flex rights that remain exercisable and any fees and expenses incurred in relation to the financing.

The main objection to these requirements in practice is the requirement to disclose flex rights (both via the documents on display and in the offer document). Bidders often feel that such rights are commercially sensitive. The Takeover Panel has subsequently conceded that flex terms do not need to be disclosed at the time of announcement and can therefore be redacted from the documents on display. In effect, however, this only gives the bidder and its financiers a period of up to 28 days between announcement of the firm offer and publication of the offer document for the debt to be syndicated if they desire to avoid the requirement to disclose live flex terms in the offer document – in many cases, this can be too small a window. Using short term bridge facilities can provide a solution to this tight timetable, see **3.3 Bridge Facilities**.

2021 Changes to the Takeover Code

In July 2021, changes to the Takeover Code came into force, largely relating to the conditions to the proposed scheme of arrangement or takeover offer and the related timetable. The changes allow bidders greater flexibility, to accommodate protracted regulatory clearance periods and affect cash confirmations in that they have implications for the required duration of the certain funds period, which will need to be reflected in the acquisition financing arrangements.

Squeeze-Out Procedures

A scheme of arrangement, in effect, involves a squeeze-out, which takes place automatically following the requisite approvals being obtained.

In relation to contractual offers, a statutory squeeze-out applies, which entitles the bidder to buy out the minority if the bidder has acquired or is unconditionally contracted to acquire both (i) 90% of the shares to which the offer relates and (ii) 90% of the voting rights in the company to which the offer relates.

10. Jurisdiction-Specific Features

10.1 Other Acquisition Finance Issues

National Security and Investment Act 2021

The National Security and Investment Act 2021 (NSIA) came into force in January 2022and introduced a new regime which allows the government to intervene in business transactions in 17 specified sectors, including acquisitions and the grant of security, which might reasonably raise national security concerns. Acquisitions that fall within the scope of the legislation will require advance notification and clearance, which will need to be factored in to the acquisition timetable.

An investment, for the purposes of the NSIA, extends beyond a simple acquisition of shares or assets. In terms of its impact on financings, while the issue of most financing instruments such as loans and bonds should not give rise to notification requirements or call-in powers under the terms of the NSIA, the implications of the NSIA will need to be considered in relation to:

- the structure and terms of the financing of an acquisition with implications under the NSIA – if the acquisition is a notifiable acquisition (ie, the target undertakes activities in one of the 17 specified areas), clearance under the NSIA will most likely be a condition precedent to the acquisition itself; it will also likely be a condition precedent to the advance of funds under the associated loan agreement;
- security arrangements and documentation (whether or not entered into in the context of an acquisition); and
- any related legal opinions.

Pension Schemes Act 2021

Since the introduction of the Pensions Act 2004, there has been increased scrutiny by lenders of defined benefit (DB) pension scheme liabilities within borrower groups. Engagement with DB pension scheme trustees has been a routine part of preparations for acquisition financings. In some transactions, obtaining voluntary clearance from the UK Pensions Regulator is a condition precedent to funding. However, clearance is a time-consuming process and impacts on transaction timetables. It can also impact the terms of a financing.

The process of considering whether to seek clearance will involve a negotiation with the scheme trustees, who may impose conditions to mitigate the effect of the transaction on the pension scheme, such as rights to share in the security package and intercreditor controls. The Pension Schemes Act 2021 has further boosted the Pensions Regulator's powers in this regard and this has resulted in renewed focus on pension issues (where there is a DB scheme within the group) by lenders.

Economic Crime (Transparency and Enforcement) Act 2022

The Economic Crime (Transparency and Enforcement) Act 2022 (ECA) establishes a framework for a new Register of Overseas Entities (the "Overseas Register"). It came into effect on 1 August 2022. The ECA has implications for acquisition finance transactions where the security includes the grant of a mortgage/charge over real estate in the UK created by an overseas entity.

The Overseas Register seeks to improve transparency of ownership of property in the UK by requiring overseas entities which already own or subsequently acquire UK property to disclose details of their beneficial owners. Under the new regime, overseas entities which wish to acquire a "qualifying estate" in England and Wales (being a freehold estate, or leasehold estate granted

for a term of more than seven years) must apply to Companies House to be registered on the Overseas Register. As part of the registration process, overseas entities must provide verified information about their beneficial owners, as specified in the ECA. Failure to register in advance of acquiring a qualifying estate has, from September 2022, meant that an application to register title at the Land Registry in relation to the land in question will be rejected.

The ECA also has retrospective application, requiring overseas entities which acquired a qualifying estate on or after 1 January 1999 to apply to be included on the Overseas Register. These entities had a six-month transitional period from 1 August 2022 to register with Companies House. Finally, overseas entities which disposed of a qualifying estate between 28 February 2022 and the end of the transitional period are also required to provide details of their beneficial ownership as it was immediately prior to the disposition to Companies House.

After successfully registering with Companies House, the overseas entity will receive a unique Overseas Entity ID, which must be supplied to the Land Registry whenever the entity wishes to register title to, or any disposition of, a qualifying estate. There is an obligation to confirm/update the information at least annually.

Failure to register with Companies House has implications for the registration of certain dispositions at the Land Registry. Since 5 September 2022, overseas entities which acquired a qualifying estate after 1 August 2022 will be prevented from registering at the Land Registry – and thus from acquiring legal title – unless registered on the Overseas Register. They will also be prevented from registering certain dispositions, these being a transfer, grant of a lease for more than seven years and grant of a charge. In addition, since 1 February 2023 (the end of the transitional period), overseas entities which have failed to register existing interests will be restricted from registering dispositions at the Land Registry unless registered with an up-to-date registration on the Register at the time of disposition. Overseas entities which fail to comply with the updating duty, will also be treated as unregistered.

There are a number of exceptions to the Land Registry restrictions on dispositions. These include:

- dispositions made in pursuance of a statutory obligation or court order, or occurring by operation of law;
- dispositions made in pursuance of a contract made before the restriction is entered in the register;
- dispositions made in the exercise of a power of sale or leasing conferred on the proprietor of a registered charge or a receiver appointed by such a proprietor; and
- dispositions made by a specified insolvency practitioner in circumstances to be prescribed by future regulations.

What does this mean for loan transactions where the security includes the grant of security over qualifying real estate by an overseas entity? Lenders will be keen to ensure that the overseas entity has complied with its obligations to register, and its updating obligations, to avoid any potential complications upon registration of the security at the Land Registry and in the event of an enforcement scenario. Protection by way of condition precedent, requiring the overseas entity to demonstrate it has a valid entry on the Overseas Register, and representations/undertakings relating to its ongoing compliance may be requested.

CHAMBERS GLOBAL PRACTICE GUIDES

Chambers Global Practice Guides bring you up-to-date, expert legal commentary on the main practice areas from around the globe. Focusing on the practical legal issues affecting businesses, the guides enable readers to compare legislation and procedure and read trend forecasts from legal experts from across key jurisdictions.

To find out more information about how we select contributors, email Katie.Burrington@chambers.com