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LMA response to the Insolvency Service consultation on possible changes to corporate insolvency law

The LMA has consulted widely with its members, which include both banks and non-banks operating in the corporate, leveraged and project finance markets, on the Insolvency Service consultation - Encouraging Company Rescue. Input has been received from senior members of banks' and financial institutions' restructuring and credit teams, as well as those responsible for corporate relationships.

The UK insolvency regime is widely recognised as being fair and balanced. Nevertheless we welcome any efforts on the part of the Insolvency Service to further improve the UK regime.

However, we have a number of concerns about the new proposals in their current form; especially in terms of the lack of detail around certain key issues.

The proposed disregard of standard negative pledge language and the ability of new security to rank ahead of any existing security in the proposals erode the established hierarchy of priority in the UK. This would create uncertainty at a time when banks are looking to strengthen their credit standards and is likely to be controversial with lenders.

In particular, uncertainty around the definition of 'adequate protection' for existing creditors would cause uncertainty amongst potential and existing lenders and would be likely to precipitate a negative outcome in lending behaviours, both in terms of availability and cost of finance.

There is a strong feeling among our commercial bank members that the proposals could impact on their decision to lend at inception, due to increased perceived risk and potentially higher 'loss given default'. The potential erosion of any security granted may make access to finance harder to achieve, particularly for weaker companies. Even assuming that debt can be raised, the perceived higher risk would be likely to result in an increase in pricing to compensate.

On the subject of super-senior lending, it is important to note that under current arrangements banks already step up with new money when the proposition looks economically viable and assists in protecting outstanding debt. This happens in most successful restructurings so as to reduce damaging public awareness of problems and consequent further erosion of value in the business.

Notwithstanding these concerns, we recognise that freeing up assets and attracting rescue finance are important issues, and would welcome more detail on the conditions which would apply to the proposed override of the negative pledge and the granting of new security so that the position of existing creditors may be more fully considered.

We see limited benefit in extending a moratorium to medium/large companies for a period of 28 days or even, under court sanction, to three months, as a means of encouraging use of the CVA procedure, unless CVAs can provide a more efficient 'cramdown' process than current methods of scheme of arrangement or pre-pack insolvency.

Medium/large corporate restructurings are often undertaken by schemes of arrangement or pre-packs which facilitate an effective means of 'cramming down' dissenting, often 'out-of-the money' stakeholders and provide a faster, cheaper and less value-destroying restructuring of a business, retaining and preserving asset value, protecting jobs and positioning the business for recovery.

Further, due to the complexity of their financial structures, multi-jurisdictional nature of their business and divergence of interests, negotiations for the larger and more complex transactions are often only starting after 3 months. Moratoria are therefore less of an issue than obtaining agreement among conflicting stakeholders, particularly when there are secured creditors whose rights under a CVA cannot be altered without their agreement.

Certainly, if moratoria are to be included, a degree of flexibility would be more appropriate than a 'one size fits all' approach and it would also be worth considering Schemes of Arrangement in any reforms, as moratoria would then also apply to such schemes, increasing their effectiveness.

Notwithstanding the recent IMO Car Wash decision, we would suggest law reform should look at the status of 'out-of-the-money' creditors and their voting rights or disenfranchisement in an effort to expedite restructurings. Additionally, any proposals would require a proper framework for evaluating businesses and a mechanism to ensure that material contracts remain in place.

Clare Dawson, Managing Director, LMA, commented, "Changes cannot be made to the existing insolvency regime without further consultation and thought, particularly if trying to bring larger corporates within the scope of the amendments. The greater complexity of their financial structures and the multi-jurisdictional nature of their operations need to be considered and require an integrated approach with other countries' insolvency legislation regimes."

"The improvement of the insolvency regimes in our members' markets is an area on which we will continue to consult with our members."

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For further information, please contact:

Loan Market Association

Clare Dawson, Managing Director	020 7006 6007 clare.dawson@lma.eu.com
Nick Voisey, Director	020 7006 5364 nicholas.voisey@lma.eu.com

Penrose Financial

Andrew Nicolls/John Sarsfield	020 7786 4881/ 66 andrewn/johns@penrose.co.uk
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Loan Market Association

The Loan Market Association was founded in December 1996 by seven leading international banks in London. Its aim was to encourage liquidity and efficiency in both the primary and secondary loan markets by promoting market depth and transparency, as well as by developing standard forms of documentation and codes of market practice. Banks, law firms and other market practitioners/participants are welcome to apply to join the LMA.

The Association was established in anticipation of changing market conditions and of a perceived willingness on the part of the banking community to bring greater clarity, efficiency and liquidity to the relatively under-developed secondary market.

The initiative was clearly well timed, as there was sustained growth in secondary loan activity in the Euromarkets over the following ten years. Unsurprisingly, this trend reversed in 2008, when volumes for the year went down to EUR 80 billion from EUR 173 billion in 2007.

The LMA has gained recognition in the market and has expanded its activities to include all aspects of the primary and secondary syndicated loan markets. It sees its overall mission as acting as the authoritative voice of the syndicated loan market in Europe vis à vis banks, borrowers, regulators and other affected parties.

For more information, please visit www.lma.eu.com.