The Legal 500 Country Comparative Guides

United Kingdom: Lending and Secured Finance

This country-specific Q&A provides an overview of lending and secured finance laws and regulations applicable in United Kingdom.

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Disclaimer: The summary below is a high level summary of certain aspects of secured lending under the laws of England and Wales as at 10 April 2020. It does not purport to deal with every aspect or every exception that may apply in a given situation. It should not be relied upon as legal advice and specific legal advice should be sought. The summary is focused on lending to companies. Different regimes may apply to other forms of entities and individuals and specialist regimes apply for certain types of industries, which is beyond the scope of this high level summary. All references in the below summary to legislation is to that legislation as amended, supplemented and restated prior to the date hereof.
1. **Do foreign lenders require a licence/regulatory approval to lend into your jurisdiction or take the benefit of security over assets located in your jurisdiction?**

Lending to companies is not a regulated activity in the United Kingdom.

Generally, lenders do not require to be licensed or have a regulatory approval to benefit from guarantees and security over assets located in the United Kingdom. Certain exceptions apply in the case of regulated mortgages.

2. **Are there any laws or regulations limiting the amount of interest that can be charged by lenders?**

There are no usury laws in England and Wales. However, an English court may not enforce provisions requiring additional amounts to be paid, for example default interest, if it holds such additional amount to be a penalty. Default interest under English law facility agreements in practice is typically limited to one per cent. per annum.

3. **Are there any laws or regulations relating to the disbursement of foreign currency loan proceeds into, or the repayment of principal, interest or fees in foreign currency from, your jurisdiction?**

There are no exchange controls in the United Kingdom.

4. **Can security be taken over the following types of asset: i. real property (land), plant and machinery; ii. equipment; iii. inventory; iv. receivables; and v. shares in companies incorporated in your jurisdiction?**

Yes, security can be taken over the types of assets listed above.

If so, what is the procedure – and can such security be created under a foreign law governed document?

**Forms of security**

Different forms of security are available in England and Wales: mortgages, charges, assignments, pledges and liens. The choice of method will depend on the nature of the asset and the commercial requirements of the parties.

Mortgage: A mortgage can be legal or equitable. A legal mortgage, with the exception of a legal mortgage over land (see below), involves a transfer of legal and beneficial ownership of the asset subject to a right of redemption under which the creditor must re-transfer title to the debtor when the debt is discharged. Contrary to other jurisdictions where mortgages are reserved for security over immovable property, in England and Wales, a mortgage can also be
A charge creates a proprietary security interest in favour of the secured parties in respect of identifiable assets, without transfer of ownership or possession. The charge can be fixed or floating.

A fixed charge requires sufficient control by the secured parties over the debtor’s ability to deal with the asset, including the consent of the secured parties in respect of any disposal of the asset.

Where creditors do not have sufficient control over the assets charged, a charge may be characterised as a floating charge. Floating charges are suitable where security is to be taken over a fluctuating pool of assets such as inventory, stock and cash in bank accounts.

Floating charges allow the debtor to have control over the assets and to deal with the assets as part of its business including by selling the assets and substituting them by new assets of a similar type. For example, debtors may continue to withdraw cash from secured bank accounts to make payments and receive new payments from customers into the secured accounts.

Typically, security documents will provide that on a certain trigger event (e.g. event of default), either automatically or upon notice by the relevant secured creditors, the floating charge is converted into a fixed charge with control passing from the debtor to the secured party. This is often referred to as the crystallisation of the floating charge.

The distinction between fixed and floating charges is not only a matter of control. Floating charge holders rank lower in the payment waterfall in case of insolvent liquidation. Floating charge holders rank after fixed charge holders, preferential creditors (that is, employee salary claims and from 1 December 2020, claims from UK tax authorities in respect of certain tax claims) and liquidation expenses.

Crystallisation of a floating charge may however not change the ranking of the floating charge which may continue to be treated as a floating charge in case of insolvent liquidation especially if crystallisation happens just before entry into liquidation.

The Insolvency Act 1986 grants a statutory power to holders of a qualifying floating charge to have an administrator appointed (see question 22) without needing a court order. A qualifying floating charge is a floating charge over all or substantially all of the debtor’s property and which by its terms states that it intends to take effect as a qualifying floating charge for purposes of the relevant provisions of the Insolvency Act 1986. On leverage finance transactions, where agreed security principles often limit considerably the types of assets over which security will be taken, security taken in the form of a floating charge may not be a qualifying floating charge, irrespective of a stated intention in the security
document. An administrator can still be appointed in that case but via the court procedure which adds time and cost (see question 22).

Pledge: A pledge involves the transfer of possession to the secured party with respect to the secured asset. The transfer of possession can involve the transfer of possession of the actual asset (e.g. in the case of bearer securities) or be constructive (e.g. in the case of assets located in a warehouse to which the keys are transferred to the secured party). For this reason, pledges are not often used in the context of leveraged finance transactions where often businesses need to continue to operate and use their assets subject to the security without unnecessary administrative burden to seek consents from creditors but pledges are used in the context of other secured finance transactions, for example on certain structured or commodity finance deals.

As a matter of English law, it is not typically enough for notice of security to be placed on an asset to construe possession. For example, it may be insufficient to place a notice on an oil barrel to notify third parties of security given to named parties. The barrel may need to be placed in a locked room to construe possession. Assets that can be secured by way of pledge are therefore limited to assets that can be delivered and the transfer of possession must be practicable and commercially acceptable. Hence, while technically possible to use a pledge to give security over many assets, this is not typically the preferred method and a charge will in many circumstances be preferable.

For the above reasons, many security documents described in other jurisdictions as a form of pledge would as a matter of English law be characterised instead as a charge. This is relevant when determining whether overseas law security documents entered into by UK registered companies need to be registered as a charge at Companies House (see question 8).

Assignment: Assignments can be legal or equitable. A legal assignment involves the transfer of the legal right to the chose in action and express notice is required to be given to the debtor of the receivable or claim.

Liens: a lien can arise by law or be created by agreement. It gives the creditor the right to retain possession of an asset until the relevant obligation has been discharged. However, it does not typically grant the secured parties a power to sell the asset and be discharged from the proceeds. Hence, this is not typically used as a form of security in secured lending transactions.

Immovable property (land, buildings and any structures or machinery fixed on the land)

The most common forms to take security over immovable property are by way of mortgage / fixed charge. As an exception to the requirements for the creation of a legal mortgage, the Law of Property Act 1925 provides that a legal mortgage over land is created by a charge entered into by deed expressed to be by way of legal mortgage rather than requiring the
mortgagor to transfer the legal title to the land (as applies in the case of a legal mortgage over other assets).

Movable assets

The most common forms to take security over movable assets are by way of mortgage, fixed or floating charges and pledge.

Choses in action (receivables and rights)

The most common forms to take security over choses in action are by way of assignment or charge.

Governing law

It is possible for parties to select the laws of an overseas jurisdiction to govern security granted by a UK registered company over assets located overseas or in England and Wales subject to certain exceptions. However, the relevant security will need to be perfected in accordance with English law to be effective vis-à-vis relevant third parties and the security documents may need to meet certain substance requirements, for example, to qualify as fixed charges in the payment waterfall on insolvent liquidation.

5. Can a company that is incorporated in your jurisdiction grant security over its future assets or for future obligations?

Securing future assets

It is possible under the laws of England and Wales to take security over future assets of a debtor. However, not all forms of security can be used. A legal mortgage or legal assignment cannot be used to take security over a future asset as it involves the transfer of the debtor’s legal title to the asset. However, a charge or other equitable security interest can be created with the obligation to convert the security into a legal mortgage or legal assignment when the debtor acquires legal title. Both fixed and floating charges can be used to take security over future assets. A pledge cannot be used to create security over a future asset as it involves the delivery of the asset into the possession of the secured parties or their representative.

Securing future obligations

In a leverage finance context, where capital structures often are designed to permit significant amounts of additional senior secured and junior secured debt as well as refinancing debt, under existing or new documents, in the form of loans and bonds, the question whether guarantees and security can be given at the outset for all debt permitted to
be guaranteed and secured from time to time is very pertinent. The ability to do so will save time and legal fees. However, the provisions describing the obligations guaranteed and secured will need to be carefully drafted and may not in all situations, no matter how well the relevant provisions are drafted, avoid the need for supplemental security or confirmations.

Security: It is possible under English law to take security for future or amended obligations. However, a court may narrowly interpret provisions granting security for obligations that may be materially amended or increased in the future. To determine whether obligations incurred or amended in the future are secured by an existing security document, it is important to be able to determine whether the relevant debtor providing the security intended those future or amended obligations to be secured when it entered into the relevant security document. This will be a matter of fact. It is generally helpful to the analysis if the relevant future obligations are described specifically rather than only in a generic savings clause. This could be for example by specifically contemplating an increase in the commitments under specified baskets or ratios in the facility agreement. Often debtors would enter into security confirmations at the time when future obligations are entered into or significant amendments to the credit documents are made. However, where it cannot be determined with sufficient certainty that the specific future or amended obligations were intended by the debtor to be covered by the security document, it is customary and prudent for secured creditors to request supplemental security to be entered into by the debtor.

Guarantees: An English court may narrowly interpret a provision allowing the obligations guaranteed to be increased or materially amended, without the consent of the guarantor. Again, it is important to be able to determine whether the guarantor intended for the relevant future obligations or amended obligations to be guaranteed when the guarantee was provided. Hence, where material changes are made to the guaranteed obligations, it is customary to obtain guarantee confirmations even where the guarantee contains generic savings language.

6. **Can a single security agreement be used to take security over all of a company’s assets or are separate agreements required in relation to each type of asset?**

A single security document, a debenture, can be used to take security over most types of assets without the need to enter into separate security documents per asset class. Often a debenture would describe the relevant classes of assets over which security is given and the method by which security over that class of asset is taken.

7. **Are there any notarisation or legalisation requirements in your jurisdiction? If so, what is the process for execution?**

There are no notarisation or legalisation requirements for UK registered companies or limited liability companies to enter into security documents.

However, certain legal requirements apply for the execution of the security documents as a
While these do not require to be executed in front of a notary or other official, certain formalities need to be observed including who can sign and how to execute the documents.

8. **Are there any security registration requirements in your jurisdiction?**

The requirements for perfection of security in England and Wales, i.e. the procedural requirements imposed by law aiming to protect a secured party’s priority and determine its ranking vis-à-vis other creditors, depend on the method of security and nature and jurisdiction of the person providing the security.

Registration is one form of perfection. The main types of security to be perfected by way of registration in England and Wales are:

- Charges
- Mortgages over land
- Security over certain forms of assets subject to specialist asset registers: certain intellectual property, aircraft and ships

**Charges**

Charges created on or after 6 April 2013 by UK registered companies must be registered at Companies House within 21 days after their creation subject to certain exclusions. Some headroom exists for the start of the 21-day period for charges created outside the United Kingdom.

The Companies Act 2006 provides that for purposes of the registration the concept of charge includes a mortgage. Pledges do not require to be registered as perfection is by the taking of possession of the asset.

Failure to register a charge within the 21-day period renders the charge void against any liquidator, administrator or other creditor of the debtor.

This applies whether the charges are created under the laws England and Wales or under the laws of an overseas jurisdiction. It is therefore important to consider the legal nature of any overseas law security document entered into by a UK registered company. For example, a security document labelled as a pledge agreement under overseas law may be a charge for registration purposes and it may be prudent to register the same at Companies House as a charge where in doubt.

Charges created on or after 1 October 2011 by overseas companies no longer require registration at Companies House. Prior to 1 October 2011, a different regime applied requiring charges created by certain overseas companies to be registered.
The Financial Collateral Arrangement Regulations exempt certain security over financial collateral from the registration requirements under the Companies Act 2006.

Land and other assets subject to specialist asset registers

Security over certain assets (land, intellectual property, aircraft and ships) may also require registration in a specialist asset register.

Other forms of perfection

Other forms of perfection consist of the taking of possession (in case of a pledge), transfer of legal title with obligation to re-transfer title on discharge in full of the secured obligations (in case of a legal mortgage with re-transfer of title) or the giving of notice of security (in case of an assignment).

9. Are there any material costs that lenders should be aware of when structuring deals (for example, stamp duty on security, notarial fees, registration costs or any other charges or duties), either at the outset or upon enforcement?

There are no material costs in England and Wales in relation to the taking or perfecting of security. Registration of security at Companies House, the Land Registry and other specialist asset registers only trigger nominal fees. Stamp duty is payable on the transfer of shares and some other securities and on certain real estate transactions. However, for a variety of reasons, including potential lender liability, secured parties seldom wish to be the legal owner of those assets which means stamp duty is mainly a consideration upon enforcement of security over those assets (see question 17).

10. Can a company guarantee or secure the obligations of another group company; are there limitations in this regard?

A company can provide guarantees or security for the obligations of a parent or other group company subject to certain legal limitations (see questions 11 and 12 below).

11. Are there any issues that lenders should be aware of when requesting guarantees (for example, financial assistance or lack of corporate benefit)?

Financial assistance

Financial assistance restrictions apply (see question 12 below).
Corporate benefit

Corporate benefit considerations apply. Under the Companies Act 2006, directors have a fiduciary duty to act in a manner which, in their good faith judgment, is most likely to promote the success of the company for the benefit of the company’s members as a whole. Directors could be held personally liable for transactions entered into in breach of this duty. Further, transactions entered into under value may be vulnerable to claw-back or restoration of the company’s position in case of administration or liquidation (see question 24 below).

Board resolutions typically describe the corporate benefit considerations to enter into the transactions and shareholders’ resolutions can be entered into to approve the relevant transactions where additional comfort is desirable.

In practice, corporate benefit is not narrowly interpreted and does not impose significant restrictions on a company’s ability to provide guarantees and security in the context of secured lending transactions to an associated group of companies.

Potential lender liability

Lenders should carefully consider potential lender liability issues when taking or enforcing security over certain types of assets. Relevant potential liabilities include pension and environmental liability.

Where a UK registered company has a defined benefit pension scheme, care should be taken when structuring share security. Secured creditors who are entitled to exercise or control the exercise of voting rights may be held liable by the UK pension regulator to provide financial support in case of a scheme deficit as a connected or associated person with the employer. Hence, the form of the share security will be relevant as well as any rights of the secured creditors on certain trigger events.

Are there any restrictions against providing guarantees and/or security to support borrowings incurred for the purposes of acquiring directly or indirectly: (i) shares of the company; (ii) shares of any company which directly or indirectly owns shares in the company; or (iii) shares in a related company?

Under the Companies Act 2006, it is unlawful for a public company to provide financial assistance for the acquisition of shares in itself or a holding company. This includes guarantees or security for debt used to make an acquisition of, or subscription for, shares in itself or in a direct or indirect holding company (irrespective of whether the holding company itself is a public or private company). The restriction on financial assistance no longer applies to private companies. However, private companies cannot give financial assistance for the acquisition of shares in a public parent company. Certain exceptions are available.
12. Can lenders in a syndicate appoint a trustee or agent to (i) hold security on the syndicate’s behalf, (ii) enforce the syndicate’s rights under the loan documentation and (iii) apply any enforcement proceeds to the claims of all lenders in the syndicate?

Lenders or other secured creditors (e.g. noteholders) can appoint a security agent or trustee to hold security on their behalf. The appointment is typically documented in the facility agreement or, where the capital structure is composed of different secured debt instruments, in the intercreditor agreement. The security agent or trustee will typically act in accordance with the instructions of the contractually required majority of secured creditors at a time when the security has become enforceable and apply proceeds of enforcement of the security paid to it, subject to any legal limitations, in accordance with the waterfall provided in the facility agreement or intercreditor agreement.

13. If your jurisdiction does not recognise the role of an agent or trustee, are there any other ways to achieve the same effect and avoid individual lenders having to enforce their security separately?

Not applicable.

14. Does withholding tax arise on (i) payments of interest to domestic or foreign lenders, or (ii) the proceeds of enforcing security or claiming under a guarantee?

The UK imposes withholding tax on payments of UK source interest on loans which are or may be outstanding for a year or more. In theory, this applies to both foreign and domestic lenders, but in practice wide exemptions apply in the case of corporate domestic lenders. The application of UK withholding tax to guarantee payments is an unresolved technical question. In our opinion, the better view in this context is that UK withholding tax only applies to guarantee payments which are in respect of UK source interest, and in that case, it applies regardless of whether the relevant guarantor is in the UK.

15. If payments of interest to foreign lenders are generally subject to withholding tax, what is the standard rate and what is the minimum rate possible under double taxation treaties?

The standard rate of withholding is currently 20% though many of the UK’s double taxation treaties reduce the rate to zero. Foreign lenders should note that reduced treaty rates do not apply automatically but require the approval of HM Revenue and Customs, the UK tax authorities, (“HMRC”) on application by the lender on prescribed forms. Regular lenders to the UK should consider applying for a “Treaty Passport” from HMRC, which effectively moves the administrative burden to the borrower. Lenders should also be aware that the UK has recently adjusted many of its double tax treaties to restrict benefits where the principal purpose of an arrangement is to obtain treaty benefits; we are yet to see how HMRC will apply this test.
16. Are there any other tax issues that foreign lenders should be aware of when lending into your jurisdiction?

Lenders should be aware that the UK imposes stamp duty on the transfer of shares and some other securities and on certain real estate transactions. It would be very unusual for the transfer of an interest in a typical secured finance loan to be subject to stamp duty, so this is most likely to be encountered on sales in connection with the enforcement of security.

17. Are there any tax incentives available for foreign lenders lending into your jurisdiction?

No.

18. Is there a history in your jurisdiction of financing structures being challenged by tax authorities, and if so, can you give examples.

No, not for typical third party lending transactions.

19. Do the courts in your jurisdiction generally give effect to the choice of other laws (in particular, English law) to govern the terms of any agreement entered into by a company incorporated in your jurisdiction?

English courts typically recognise and uphold the choice of law selected by the parties to govern their contractual obligations except where to do so would be inconsistent with Regulation (EC) No 593/2008 on the Law Applicable to Contractual Obligations (Rome I)(the “Rome I Regulation”). This applies irrespective of whether the governing law is the law of an EU member state.

Brexit

Under the Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and European Atomic Energy Community (the “UK Withdrawal Agreement”), the Rome I Regulation continues to apply in England and Wales to contracts entered into before the end of the transition period, currently until 31 December 2020.

The Rome I Regulation will continue in force in the EU member states following the transition period (subject to any amendments that may be made) and will therefore continue to recognise the choice of English law to govern contractual obligations in the EU member states.

New legislation has been introduced in the United Kingdom for the period after the transition period. The Law Applicable to Contractual Obligations and Non-Contractual Obligations
(Amendment etc.) (EU Exit) Regulations 2019 will incorporate the provisions of the Rome I Regulation, subject to certain amendments, into English law. The new legislation will come into effect after the end of the transition period.

20. **Do the courts in your jurisdiction generally enforce the judgments of courts in other jurisdictions and is your country a member of The Convention on the Recognition and Enforcement of Foreign Arbitral Awards?**

Recognition and enforcement of foreign judgments is governed by a number of different instruments and common law. Under certain regimes, registration of the judgment is required before the judgment can be enforced. Under other regimes, this is not required. Generally, an English court will recognise and enforce a foreign judgment subject to registration (where required) and certain exceptions, for example if contrary to public policy.

The Brussels (Recast) Regulation (Regulation (EU) 1215/2012) (the “Brussels Recast Regulation”) applies to the recognition and enforcement of judgments obtained in an EU member state in proceedings commenced on or after 10 January 2015.

Prior to the withdrawal of the United Kingdom from the European Union, the 2007 Lugano Convention (the “Lugano Convention”) applied to the recognition and enforcement of judgments obtained in Iceland, Norway and Switzerland. The Lugano Convention is modeled on the EU regime which preceded the Brussels Recast Regulation.

A large number of bilateral agreements are in place with other countries.

For countries with whom no multi-lateral or bilateral agreement is in place, recognition and enforcement of judgements is based on common law.

No reciprocal agreement is in place between the United States and the United Kingdom for the recognition and enforcement of judgments. A US judgment can however be enforced in England and Wales at common law by bringing new proceedings for the payment of a debt where the US judgment is treated as a contractual debt. An English court may decide not to enforce a US judgment at common law if the debt is not final and conclusive, the English court is not satisfied that the US court had jurisdiction, if the judgment was obtained by fraud, if contrary to public policy or in certain cases where no due process was observed.

The United Kingdom is a member of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards.
Brexit

Under the UK Withdrawal Agreement, the provisions regarding jurisdiction under the Brussels Recast Regulation continue to apply to legal proceedings commenced before the end of the transition period and to proceedings or actions commenced after the transition period but which are related to proceedings commenced before the end of the transition period. The provisions relating to recognition and enforcement of judgments under the Brussels Recast Regulation continue to apply to judgments issued in proceedings commenced before the end of the transition period but somewhat illogically not to judgments issued in related proceedings commenced after the transition period. The transition period runs until 31 December 2020.

The UK government has indicated it wishes to enter into new arrangements with the European Union to govern civil justice matters, including the recognition and enforcement of judgments. In the absence of new arrangements, one route may be for the United Kingdom to become a party to the Lugano Convention. No transitional provisions exist for the continued application of the Lugano Convention during the transition period. The Lugano Convention currently applies between EU member states and Iceland, Norway and Switzerland. New draft legislation, the Private International Law (Implementation of Agreements) Bill, was submitted on 27 February 2020. This sets out the basis for application of the Hague Convention on Choice of Court Agreements 2005 (the “Hague Convention”) as part of English law with ability to implement other international agreements, including the Lugano Convention.

In the absence of new arrangements with EU member states and if the United Kingdom does not become party to the Lugano Convention nor the Hague Convention, judgments issued by European member states will still be able to be recognised and enforced by English courts based on common law principles, as applies for US judgments.

21. **What (briefly) is the insolvency process in your jurisdiction?**

Different insolvency and restructuring processes are available in England and Wales under both insolvency and general company law. The main processes are administration, company voluntary arrangement, scheme of arrangement and winding up/liquidation. Special regimes apply for certain industries.

Under English law, a company is considered to be insolvent when it is “unable to pay its debts”. The Insolvency Act 1986 defines when a company is unable to pay its debts including the situations of a cash-flow based insolvency and a balance sheet insolvency. Some processes are only available to insolvent companies, others are available to both insolvent and solvent companies.
Administration

Administration involves the appointment of a qualified insolvency practitioner, an administrator, to take control over the company with the aim to achieve one of the objectives set out in Schedule B1 of the Insolvency Act 1986. The first objective is to rescue the company on a going concern basis. If this cannot be achieved, the second objective is to achieve a better result for the creditors of the company as a whole than the result that would likely be achieved by putting the company into liquidation. If that cannot be achieved, the third objective is to realise the company’s property for distribution to the company’s secured and preferential creditors.

A moratorium applies during administration (see question 23).

A company enters administration either by court order, which can be at the request of certain persons including a creditor, the company, a director of the company and certain insolvency officials under other insolvency processes, or through an out of court procedure by filing a notice of intention to appoint an administrator. The latter can be filed by the company or a director of the company or the holder of a qualifying floating charge (see question 4). To enter administration the company must be insolvent or likely to become insolvent, unless the administrator is appointed by the holder of a qualifying floating charge.

Company voluntary arrangement

The process for a company voluntary arrangement (“CVA”) is set out in the Insolvency Act 1986. A CVA involves an arrangement between the company, its shareholders and certain or all of its unsecured creditors whereby typically a portion of the debt owing to the relevant creditors in written down, the period for payment of the debt is extended or some other compromise or arrangement is reached over the payment of the relevant debt.

A CVA is proposed by the company for approval by the relevant unsecured creditors and members. A CVA requires 75 per cent. of creditors in value responding to approve the arrangement but the resolution will be invalid if creditors representing more than 50 per cent. of creditors unconnected to the company voted against the proposal. The CVA binds all unsecured creditors that were entitled to vote on the arrangement. A CVA does not bind, and may not adversely affect, secured or preferential creditors, except with their consent. A CVA further requires a simple majority of members to approve the proposal.

A short moratorium can be obtained for small companies but this is not available for larger companies (see question 23).
Scheme of arrangement

A scheme of arrangement is a statutory procedure which involves a court sanctioned arrangement between a company and its creditors/ members or relevant class of creditors/ members. The procedure is set out in the Companies Act 2006. The purpose of a scheme is not prescribed by statute. In practice, it can be used to implement a wide range of transactions, for example a take private transaction of a listed company or to address financial or operational difficulties. A scheme requires 75 per cent. of creditors/ members or relevant class of creditors/ members in value present and voting in person or by proxy at a court-convened meeting to approve the scheme. The company must be a party to the scheme. Schemes bind all creditors/ members or class of creditors/ members convened to vote on the scheme.

Winding up / liquidation

Winding-up, also called liquidation, is a court-based procedure set out in the Insolvency Act 1986. It involves the appointment of a qualified insolvency practitioner, a liquidator, to realise the assets of a company and distribute the proceeds in the order prescribed by law. Most companies cease trading on entry into liquidation. The powers of the directors of the company cease when a liquidator is appointed unless specified consents are provided for certain of their powers to remain.

Two main procedures exist: a compulsory liquidation and a voluntary liquidation which can be either a members’ voluntary liquidation or a creditors’ voluntary liquidation.

A moratorium applies in case of compulsory liquidation (see question 23).

A compulsory liquidation is commenced by the submission of a winding-up petition to court. A petition can be made by among others a company’s creditor, the company itself or the directors of the company. The Insolvency Act 1986 sets out the grounds on which a court may order the winding-up of a company. Winding-up petitions are often presented by creditors on the grounds that the company is unable to pay its debts.

A voluntary liquidation is commenced by a special resolution of the members of the company resolving that the company should be wound up.

In a members’ voluntary liquidation, all creditors of the company are required to be paid in full with the balance of proceeds or assets returned to the members of the company and the directors (or, if more than two, a majority of the directors) must make a statutory declaration that, having made full inquiry into the affairs of the company, they are satisfied that the company will be able to pay its debts in full, including any official interest, within a period specified in the declaration, not to exceed 12 months from the start of the winding-up. If
subsequently all creditors cannot be repaid within the specified period, directors who have made a statutory declaration may be subject to a fine or imprisonment.

In a creditors’ voluntary liquidation, all creditors of the company may not be paid in full and no statutory declaration by the directors is required. Consequently, creditors are by law given more control over the process, including the right to nominate a liquidator, and more access to information than in case of a members’ voluntary liquidation where they are expected to recover in full.

22. **What impact does the insolvency process have on the ability of a lender to enforce its rights as a secured party over the security?**

The impact on the ability of a lender to enforce its security under English law depends on the nature of the insolvency process.

In the case of administration, an automatic moratorium is imposed for the duration of the administration process. A moratorium starts on the application to court for the appointment of an administrator or notice of intention to appoint an administrator. A moratorium freezes creditors’ rights. Creditors cannot take any legal action or enforce their security during the moratorium.

In the case of a company voluntary arrangement, a short moratorium can be obtained for small companies by the directors proposing a CVA, subject to certain exclusions. The moratorium freezes creditors’ rights. Creditors cannot take any legal action or enforce their security during the moratorium. No moratorium is available for larger companies and certain criteria apply for group parent companies. A contractual standstill may however be entered into.

In the case of a scheme of arrangement, no moratorium or other stay on creditors’ rights automatically applies by law nor is there a specific procedure as part of a scheme process to obtain a moratorium while the scheme process is conducted. A contractual standstill can be entered into or the scheme may be conducted in parallel to an administration giving the company the protection of the administration’s moratorium.

In the case of liquidation, an automatic moratorium is imposed only in the case of a compulsory liquidation process for the duration of the winding up. The moratorium starts when a winding-up order by the court is made or a provisional liquidator is appointed. An interim moratorium may be sought from courts with relevant jurisdiction to stay pending proceedings after a winding-up petition is filed but before the automatic moratorium commences. The moratorium freezes certain creditors’ rights. Creditors cannot take or continue any legal action or proceedings without court approval but secured creditors are permitted to claim in respect of assets secured in their favour. No automatic moratorium applies in case of members’ voluntary liquidation (solvent liquidation) nor in case of a
creditors’ voluntary liquidation. However, the liquidator, a creditor or shareholder may apply to the court to stay any proceedings.

23. **Please comment on transactions voidable upon insolvency.**

The Insolvency Act 1986 grants liquidators and administrators certain powers to look back at transactions entered into within certain periods prior to a company’s insolvency with a view to unwinding transactions or otherwise restoring the company’s position. The statutory periods vary depending on the nature of the transaction and whether the persons with whom transactions are entered into are connected with the company. The main transactions are transactions at undervalue, preferences and certain floating charges.

**Transactions at undervalue**

In the case of a transaction at undervalue, a liquidator or administrator may seek a court order to restore the company’s position to the position it would have been in had it not entered into the transaction.

A transaction at undervalue is a transaction entered into within a period of two years prior to the onset of insolvency, at a time when the company was insolvent or the company became insolvent by the transaction, and consisted of a gift or other transaction without consideration or for consideration that was significantly less than the consideration provided by the company. Certain exceptions apply where the company acted in good faith.

**Preferences**

In the case of preferences, a liquidator may seek a court order to restore the company’s position to the position it would have been in had it not granted the preference.

A preference is a transaction entered into with a person who is one of the company’s creditors or a surety or guarantor in respect of any debt of the company, entered into within a period of six months prior to the onset of insolvency (in the case of transactions entered into with persons who are not connected with the company) or two years (if entered into with connected persons), at a time when the company is insolvent or the company became insolvent by the transaction, with the desire and effect of putting that person in a better position in case of insolvent liquidation of the company.

**Voidable floating charges**

A floating charge created within a period of one year (in the case of a floating charge created in favour of persons unconnected to the company) or two years (in the case of connected persons) prior to the onset of insolvency to the extent no new money or value was provided at
the time or after the floating charge was created.

Onset of insolvency is defined in the Insolvency Act 1986 in function of the nature of the procedure.

In addition to the above transactions that may be set aside, certain other remedies are available under English law making directors personally liable to contribute to the insolvent estate in certain cases. For example, where value was lost by a company continuing to trade at a time when the directors knew or ought to have known that there was no reasonable prospect for the company not going into insolvent liquidation.

24. Is set off recognised on insolvency?

Insolvency set-off applies in the context of administration and liquidation. The rules are mandatory provisions of law. A liquidator or administrator has an obligation to take account of the sums owing to each party as part of any mutual dealings between a creditor and the company. Any mutual claims are set-off automatically. Certain exceptions apply.

Except for the above and relevant exceptions, contractual rules on set-off and netting apply and those may be varied in the context of certain consensual restructuring processes.

25. Can you comment generally on the success of foreign creditors in enforcing their security and successfully recovering their outstandings on insolvency?

There is no particular legal concern that foreign creditors generally are less likely compared to domestic creditors to be able to enforce their security, file claims and recover in insolvency.

26. Are there any impending reforms in your jurisdiction which will make lending into your jurisdiction easier or harder for foreign lenders?

The withdrawal by the United Kingdom from the European Union on 31 January 2020 is expected to give rise to certain legislative changes in England and Wales after the end of the transition period, currently until 31 December 2020. In particular, all European Union law which is directly applicable in the EU member states will cease to be directly applicable in England and Wales and further changes may be made to existing European Union Directives previously implemented in the United Kingdom and other European Union law transposed into English law. This affects certain contractual matters including choice of law and jurisdiction and recognition and enforcement of judgments and certain security related matters. In some areas, there is not yet full clarity on the proposed content of the new legislation or any new treaties between the United Kingdom and the European Union post the transition period. At a practical level, lenders seem comfortable to continue to enter into secured lending transactions governed by English law and with submission to the English courts (also where obligors are incorporated in an EU member state) notwithstanding some
remaining uncertainty.

As corporate lending is not a regulated activity in the United Kingdom, the UK’s withdrawal from the European Union is not expected to make it harder for foreign lenders to lend to corporate borrowers in the United Kingdom.

The order in which creditors are paid on insolvent liquidation of a company’s property is expected to change with effect from 1 December 2020. From this date, HM Revenue and Customs, the UK tax authorities, will no longer be an unsecured creditor and will rank instead as a preferential creditor in the payment waterfall with respect to certain tax payments the company collects / withholds and holds on behalf of other persons, for example, VAT and PAYE. They remain an unsecured creditor in respect of other taxes including corporate income tax. Preferential creditors on liquidation rank after the claims of fixed charge holders and expenses of the insolvency but ahead of floating charge holder claims and unsecured claims.

The UK government further announced on 28 March 2020 certain temporary changes to UK insolvency legislation in light of COVID-19 and an intention to bring forward the planned reforms to UK insolvency legislation previously announced in August 2018. The objective of the potential reform is to enhance the ability to rescue operationally sound UK companies on a going concern basis similar to Chapter 11 in the United States.

27. What proportion of the lending provided to companies consists of traditional bank debt versus alternative credit providers (including credit funds) and/or capital markets, and do you see any trends emerging in your jurisdiction?

The United Kingdom can be considered a mature debt market in which syndicated and direct lending as well as bonds are customarily used as part of capital structures for UK registered companies. The relative proportion of each product is largely market driven at any given point in time and may change over the course of any year in light of relative pricing and available liquidity. While no perfect data is available on the relative size of each product, in comparison to the United States, the portion of bank lending to all debt made available to companies in the United Kingdom is still considerably higher than in the United States. Direct lending has increased in importance in recent years with direct lenders playing in the mid market and large cap space able to provide very large ticket sizes to take all or specific tranches of the debt.

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