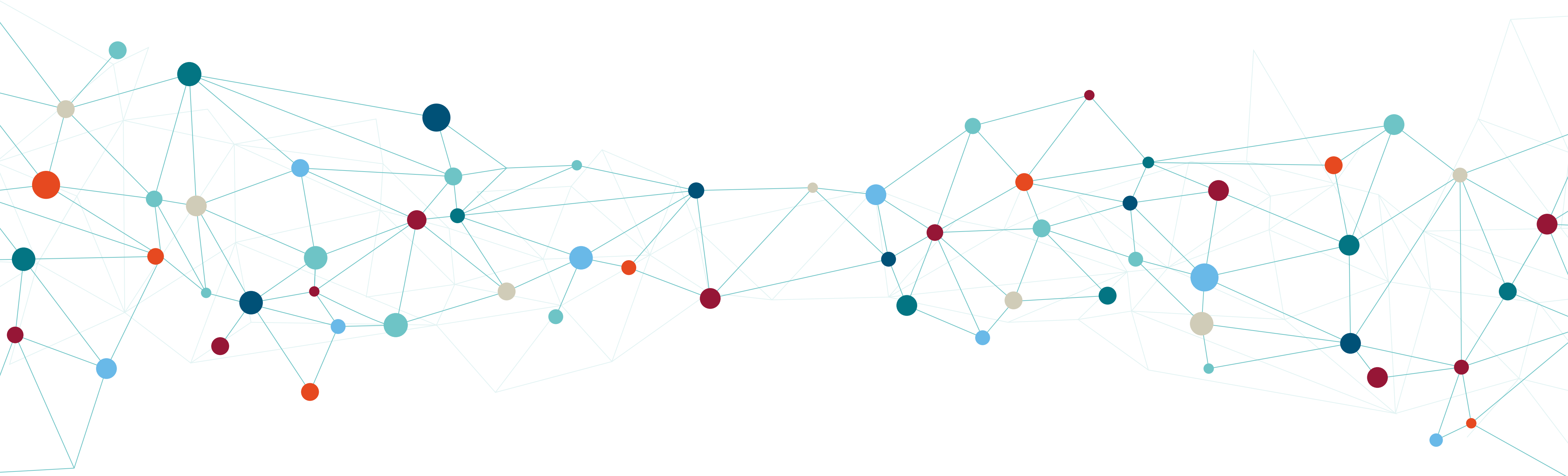
Priorities for International Banks | 2021/2

Contents

Introduction 1
Financial services regulation and Brexit 2
LIBOR 3
Clean energy 7
Data, privacy and cyber security 9
Disputes 11
Restructuring and insolvency 12
Sustainable/green finance 14
Business immigration 17
Real estate 19
Technology, e-commerce and outsourcing 22



Introduction

Many banks will have been glad to see the back of a financial year like no other in modern times and to start looking ahead into 2021/2 to identify the key areas of risk, opportunity and focus required. The arrival of various vaccines appears to provide light at the end of the tunnel and a route out of the pandemic, although the outlook still remains uncertain as second and third waves hit many countries and new variants threaten to disrupt the recovery.

This report provides short insights on the hot topics for the forthcoming 12 months, in each case from experts in the relevant practice supporting our international banks group at TLT. Our experts take you through the latest developments and what international banks can do to mitigate risks and take advantage of the potential opportunities.

Given the vast amount of airtime over the last few years, now that we have finally left the EU, regulatory experts Noline Matemera and Angela Hayes focus on the implications for international banks of the UK's departure from the EU as well as the fallout from the pandemic and the steps banks may consider taking at this stage.

Following the FCA's announcement of the cessation of LIBOR on 5 March, we provide an overview of developments on what remains a huge challenge for all financial institutions around the globe and one which will have to be dealt with, at least in part, this calendar year.

With the US back in the Paris Accord and the UK due to host the UN Climate Change Conference in November, climate change has become fixed at the top of the agenda both in terms of opportunity to fund clean energy projects and green investment becoming the global financial services industry's fastest-growing sector.

Just as we were becoming used to GDPR, data privacy expert Gareth Oldale highlights a recent decision which will require international banks to look again at the way they share data across borders and the steps which may need to be taken.

All this on top of the immediate issues created by the pandemic both in terms of the impact on borrower covenants and asset values and the longer terms effects on sectors such as IT and real estate.

These are just some of the highlights but the Priorities Report offers an invaluable single point of reference for our international banking clients by setting out legal and regulatory developments across ten key areas in the coming year, being:

- Financial services regulation and Brexit
- LIBOR
- Clean energy
- Data, privacy and cyber security
- Disputes
- Restructuring and insolvency
- Sustainable/green finance
- Business immigration
- Real estate
- Technology, e-commerce and outsourcing

We hope you find this report not only helpful in planning for the year ahead but also a clear demonstration of the breadth and depth of expertise at TLT and our ability to provide expert advice on all the issues and opportunities facing international banks as we emerge from the Covid-19 pandemic.

If you have any questions about the report or would like help dealing with or preparing for the issues we identify, please do get in touch.

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Financial services regulation and Brexit

What's changing?

Brexit

Now that the transition period has ended, international firms can no longer use the passporting regime to establish a branch or provide services on a cross border basis to the UK. To prepare for this, the FCA established the temporary permissions regime (**TPR**). This regime allows for European Economic Area (**EEA**) firms that had a passport to provide services in the UK (either on a freedom of establishment or services basis) to continue to do so for a limited period.

In February 2021, the FCA published a paper setting out its general approach to international firms seeking to provide financial services that require authorisation in the UK. Whilst the consultation paper concerns EEA firms that have applied for the TPR, it also covers international firms from non-EEA areas that had applied or intended to apply for authorisation in the UK, or were already authorised in the UK.

The FCA will generally expect international firms to meet (and continue to meet) a set of minimum standards, which are referred to as threshold conditions. One of those conditions will be the FCA's ability to effectively supervise firms, so international banks should review whether their governance structure and systems and controls are adequate for their UK activities. Part of this review should include their ability to access relevant information to provide to the FCA, if requested. The approach document also makes it clear that the FCA will assess an international firm's risks of harm. The FCA will be focused on reducing the risk of retail client asset and wholesale harm. International banks should work to understand the FCA's focus on each of these areas and put adequate risk mitigation plans in place.

Impact of Covid-19 on regulated firms

The ongoing impact of the Covid-19 pandemic has created continued uncertainty in financial services – for consumers as well as firms. The FCA expects that operational resilience will continue to be a particularly important focus for wholesale financial markets while the pandemic lasts. It has specified that firms should emphasise evaluating current arrangements while also managing any risks to employees and customers within business continuity plans.

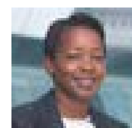
There will also be heightened scrutiny on information security. Cyber criminals have exploited the pandemic to take advantage of operational disruptions and vulnerable consumers. The FCA requires international firms to prioritise reinforcing information security, which will help manage and reduce major incidents, such as process outages, and cyber threats. This is also reflected in financial systems and controls, with the FCA insistent that international firms should not change their risk appetite due to the operational challenges of the current climate. Instead, the FCA expects international firms to re-prioritise or delay certain requirements, such as customer due diligence.

What should international banks do to prepare?

The FCA expects firms wishing to do business in the UK on more than a short-term basis to apply for full authorisation. Therefore, it is fundamental that all international banks understand the UK's authorisation requirements to provide financial services, and that they develop an authorisation plan to guide them through this journey.

With regard to Covid-19, international wholesale financial markets, in particular, should ensure they focus on having an astute business continuity plan and overall resilience. Taking necessary measures will prevent them being deemed not fit for regulatory purpose in managing the issues caused by Covid-19. There should also be a wider consideration on ensuring financial systems and controls are not neglected to help prevent financial criminals from taking advantage of the pandemic.

Key contacts



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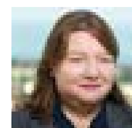

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LIBOR

What's changing and what should international banks do to prepare?

LIBOR cessation – the endgame

The cessation of the London Interbank Offered Rate (LIBOR) is, finally, in its last phases.

On 5 March 2021, the Financial Conduct Authority (FCA) announced that all LIBOR settings for all five currencies and tenors would either cease to be provided or would no longer be representative:

- immediately after 31 December 2021 in the case of all Sterling, Euro, Swiss Franc and Japanese Yen settings and the 1 week and 2 month US Dollar settings; and
- immediately after 30 June 2023 in the case of all remaining US Dollar settings.

The FCA has said that, based on undertakings received from the panel banks, it does not expect that any LIBOR settings will become unrepresentative before the relevant dates set out above. Representative LIBOR rates will not, however, be available beyond the dates set out above.

The announcement brings into sharp relief that this really is then the endgame for LIBOR.

Timetable for transition

To assist banks in meeting the 31 December 2021 deadline, the UK's Sterling Risk-Free Rate working group has set out a series of milestones for transition including: (i) ceasing to issue Sterling LIBOR contracts by 31 March 2021 and (ii) to actively progress and complete the transfer of contracts currently using Sterling LIBOR to an alternative rate by 30 September 2021.

What has taken the market by surprise is that USD LIBOR for the most common tenors (1/3/6/12 months) will continue to be published until 30 June 2023. It means that only existing USD LIBOR loans and products maturing after that date will need to be transitioned to an alternative rate nearer the time. However, the New York Fed has warned that continued publication will be for the limited purpose of assisting with run-off legacy contracts only; issuance of new USD linked contracts should cease by 30 June 2021 and certainly before the end of 2021.

The delay to cessation of the publication of USD LIBOR does create some interesting issues for transition in relation to multi-currency facilities as well as difficulties for central banks and regulators in some jurisdictions which peg their IBORs to USD and the timing of any transition.

"The announcement brings into sharp relief that this really is then the endgame for LIBOR."

Where should banks be by now?

Banks should have:

- identified all legacy contracts maturing after 31 December 2021 (or 30 June 2023 in the case of USD LIBOR) as well as the critical provisions which will impact on transition including fallbacks and amendment provisions;
- established a governance framework for the project and a plan for transition in line with the FCA's milestones;
- identified the appropriate alternative rate (whether an RFR, a fixed rate or central bank rate) which will replace LIBOR;
- established systems and processes to deliver loans and contracts based on the replacement rate; and
- commenced training staff and communicating with clients about the transition and its implications.

Banks can expect the FCA to monitor progress in these last few months before cessation.

Tough legacy contracts

The phrase tough legacy contracts does not have a fixed definition as yet but in essence it means financing arrangements which, for various reasons, are exceedingly complex or difficult to transition.

In the UK, the Financial Services Bill (which is yet to become law and maybe subject to further modification) will allow the FCA to declare a benchmark as being unrepresentative and prohibit its further use, whilst permitting certain categories of "tough legacy" contracts to be exempt from the prohibition. Acting through the rate administrator, the FCA may preserve certain LIBOR currencies and tenors whilst directing changes to the calculation methods. The continued publication of LIBOR under this different methodology is referred to as "synthetic LIBOR" and the FCA has now stated its intention to consult on using its powers to require IBA to continue the publication on a "synthetic" basis of the 1/3/6 Month GBP and JPY LIBOR, and will consider doing so in the future for the common tenors of USD LIBOR. This is not a means of extending the use of LIBOR – it is likely to apply to a restricted cohort of existing legacy contracts (yet to be defined). New use of synthetic LIBOR by UK regulated firms in regulated financial instruments would be prohibited under the Bill and firms should not treat the prospect of tough legacy contracts as an excuse to limit active transition efforts.

Conflict of laws

The solutions to tough legacy contracts likely to be adopted by regulators in the key jurisdictions is currently not consistent which could give rise to some complicated issues of conflict of laws and the potential for forum shopping. Under the amended EU BMR, the European Commission can replace any reference to LIBOR with a reference to a suitable replacement rate. The New York Fed has proposed a similar approach and the concept of a safe harbour protecting parties from liabilities arising from the automatic transition to the recommended benchmark (a concept which the UK is also considering adopting). Whilst the EU has confirmed that its fix will only apply to EU law contracts, both the UK and US solutions are stated to have extra territorial effect.

> "Lenders will need to achieve a balance between maintaining the status quo and revenue with the regulators warnings to ensure that customers are treated fairly."

Credit Adjustment Spread

As the switch from LIBOR to RFRs is not like for like (since LIBOR builds in credit risk and term liquidity premium which an RFR does not), a credit adjustment spread may be applied to the replacement rate to minimise the economic impact of transitioning away from LIBOR. Lenders will need to achieve a balance between maintaining the status quo and revenue with the need (as regulators have expressly warned) to ensure that customers are treated fairly. There are inherent challenges in the timing of the application of the CAS (and how that timing fits with the current differential between LIBOR and the RFR) and the methodology for its calculation.

Hedging products

ISDA has developed the IBOR Fallbacks Supplement and Protocol which came into effect on 25 January 2021. In essence, protocol and supplement have the effect of automatically transferring derivative contracts from LIBOR to RFRs when LIBOR ceases to be published upon the occurrence of cessation events. As well as the potential for hedging contracts to become mis-aligned with amended loan terms during transition, there may also be risks associated with fixing the credit adjustment spread (see above) well in advance of cessation (which for USD is 30 June 2023).

Conduct and litigation risk

The transition from LIBOR is complex and could expose banks to both conduct risk as well as wider litigation risk for instance from mis-selling claims concerning the RFRs or the imposition of the CAS (or its methodology or calculation). Added to that is the tension created for international banks operating in the UK (and those with responsibility for UK operations and transition), where the regulator is most active on transition for obvious reasons, and the head office in the home jurisdiction where the regulator is likely to be less advanced on transition. It will be important to ensure that UK branches and subsidiaries meet FCA deadlines and obtain all necessary support to do so.

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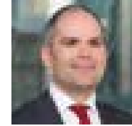

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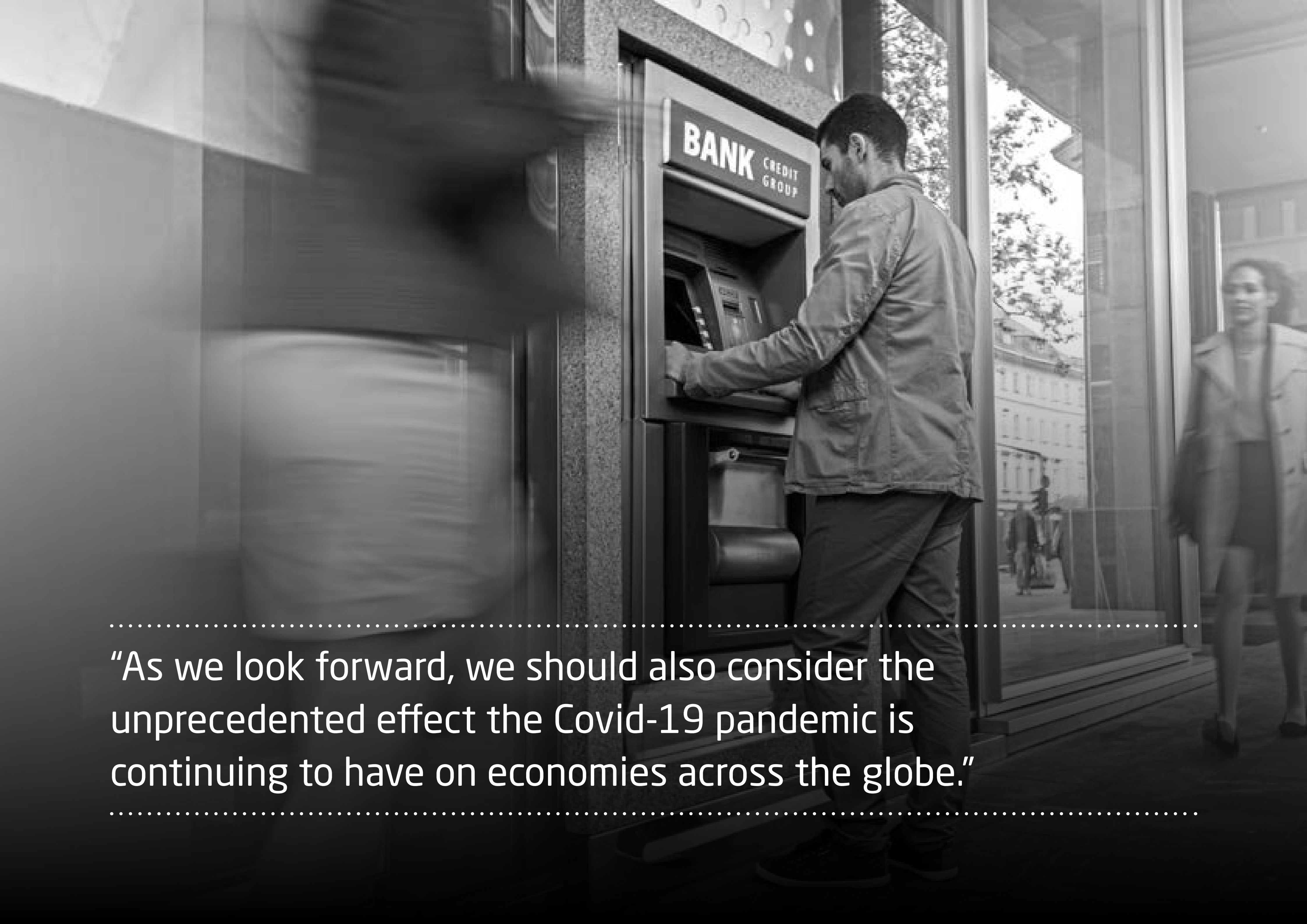

"As we look forward, we should also consider the unprecedented effect the Covid-19 pandemic is continuing to have on economies across the globe."

Clean energy

What's changing?

At the end of 2020, the Committee on Climate Change published the Sixth Carbon Budget. This sets out the rate of emission cuts that the UK needs to pursue in the 2030s to stay on course for net zero. In this Budget, the Committee highlighted that annual low carbon investment in the UK will need to reach £50bn to put the UK on track for net zero, and that the vast majority of that investment is going to come from the private sector. The budget, alongside the Energy White Paper and the Ten Point Plan, sets the stage for the clean energy sector to take the lead in the UK's journey to net zero.

It is clear that there is a significant opportunity for funders to take advantage of sector growth. Doing so will enable them to diversify lending portfolios into developing technologies such as energy storage, green hydrogen and electric vehicle charging infrastructure (EVCI) as these assets become more mainstream.

The market has already seen a number of debt funded energy storage projects but late 2020 saw some developments, including a project finance funding model which uses a multi-tranche debt structure that matches the tiered risk profile of the revenue model. Given the critical role energy storage will play in balancing the increase in clean energy generation on the grid, it is key that funding channels for this technology are unlocked.

As the UK moves towards its vehicle electrification target of 2030, there has been a sharp rise in electric vehicle sales. Along with it comes an increase in electric vehicle charging infrastructure, particularly across the public, retail and leisure sectors, as well as the development of new concepts such as electric forecourts. The initial debt funding of these schemes has very much been on a scheme-by-scheme basis due to their complex nature, but there is a significant opportunity for funders to take advantage of this growing area. As revenue streams become more sustainable due to usage increase and a rise in partnership arrangements, the opportunities are expected to grow.

Achieving net zero has put a spotlight on the role of clean energy generation. Driven in part by the challenges of modelling projects in a subsidy-free era, there is a growing trend to develop large-scale multi-technology projects that combine solar (or onshore wind) with energy storage (and EVCI) and private wire or corporate PPAs as a futureproofing mechanism. These schemes will play an important role in achieving net zero and offer large-energy users decarbonised power. Funders are aware that for solar and onshore wind "plus storage" is the future of the market, and it is likely that the coming months will see the first subsidy-free solar plus storage debt solutions.

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There also continues be a fertile ground for debt solutions for more established technologies such as hydro and biomass. In addition, the development of nascent technologies including green hydrogen, floating wind and pumped storage are also driving the sector. While investment in these areas is mainly an equity play at present, we are likely to see more funding models being developed as more schemes come to market and revenue streams are proven.

What should international banks do to prepare?

We are already seeing significant interest in the UK clean energy market from international banks. Given that an increased focus on ESG-linked funding is likely to make renewable generation projects even more attractive, we'd expect this growing interest to continue over the coming months. If you would like to discuss your upcoming project requirements, then contact our team of experts.

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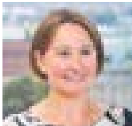

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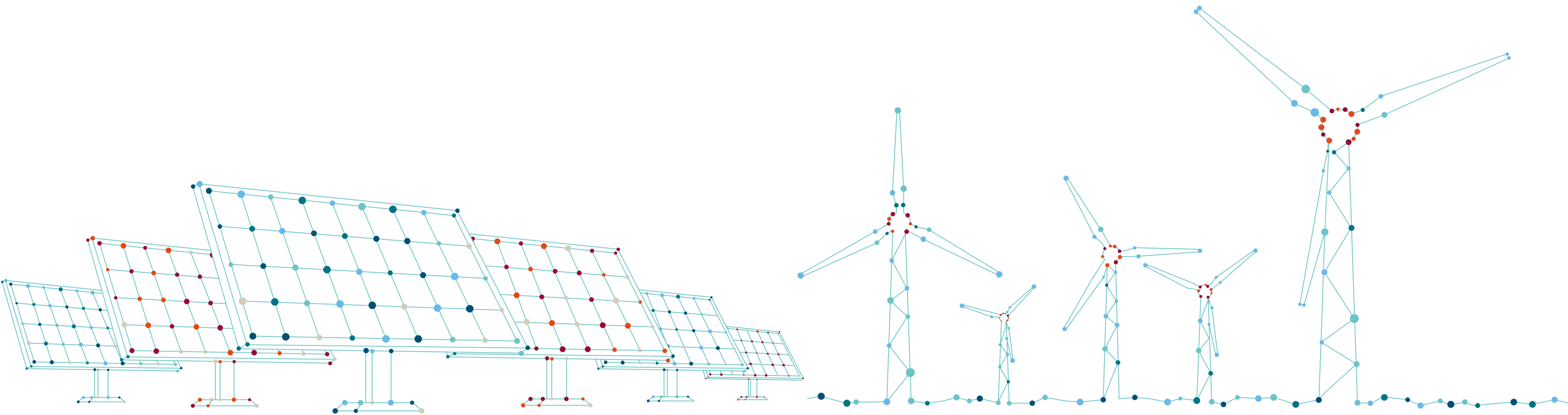


Data, privacy and cyber security

What's changing?

Arguably the most significant development during 2020 affecting the laws around data protection was the judgment by the Court of Justice of the European Union (CJEU) concerning the validity of the EU-US Privacy Shield arrangement. This previously allowed EU organisations to export data to the US, provided they self-certified their adherence to certain data protection principles.

The CJEU has now determined that mass surveillance laws in the US allow too much access to personal data, and that the complaints mechanism in place offered insufficient redress for those whose privacy rights are infringed. As a result, the CJEU found the Privacy Shield did not provide a level of protection equivalent to that required by the General Data Protection Regulation (GDPR). This was an unexpected shock for businesses, as in 2019 the CJEU's Advocate General (AG) had expressed the opinion that there was no need to review the Privacy Shield arrangement.

The CJEU's decision originated from the so-called "Schrems II" case. This was based on a complaint from Austrian privacy activist Max Schrems, who in 2015 had similarly brought down the Privacy Shield's predecessor, the Safe Harbor arrangement. As a result of this more recent judgment, EU and UK-based banks operating under the requirements of GDPR can no longer use the Privacy Shield when transporting data to the US.

Changes to the SCCs

The standard contractual clauses (SCCs), which were the primary focus of Schrems II, remain valid – albeit with some significant caveats. The SCCs exist to provide sufficient safeguards for data to be transferred internationally, meaning they can therefore theoretically be used to export data from the UK and the EU to other jurisdictions, including the US. However, the obligations in the SCCs can be overridden by the laws of other jurisdictions, exposing individuals to the risk that recipients of their data might be obliged by government agencies in third countries to share it.

Any transferor of data wishing to use the SCCs must therefore carry out an assessment of the data protection laws of any third countries to ensure they are adequate, before relying on the SCCs. The onus is now on data controllers in the UK and the EU to ensure that SCCs can provide an equivalent level of protection to the GDPR. If not, transferors should use additional safeguards, such as strong encryption.

SCCs are also widely acknowledged as being out of date. The European Commission (EC) has published new draft SCCs to replace the current versions, which the EC consulted on at the end of 2020. The consultation has closed and the final version of the new SCCs is awaited. The UK also intends to publish its own version of the SCCs. While a lack of clarity will continue in the continued absence of the finalised versions, the draft SCCs suggest that a year's grace period will be conceded to those companies transferring data before compliance with the new SCCs becomes obligatory.

The impact of Brexit

Following the end of the Brexit transition period on 31 December 2020, the UK has become a "third country" for the purposes of transfers of personal data from the European Economic Area (EEA). EU authorities have agreed to continue to recognise the UK's level of data protection as adequate for six months (during which time the UK has committed not to move away from the provisions of the GDPR) pending a formal finding of "adequacy". The EC published draft adequacy decisions in February 2021. If approved, these would allow data flows from the EEA to the UK to continue uninhibited for at least four years, with the potential to renew if the UK's legal framework continues to provide adequate protection for personal data.

The UK has also said it will continue to regard all EEA countries as 'adequate' for a period of four years. This means data flows from the UK to EEA countries will be able to continue over the medium term until the UK issues its own "adequacy" findings in relation to the EEA countries.

What should international banks do to prepare?

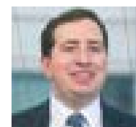
Data-mapping is key: banks need to carry out detailed data mapping activities, including to ensure they fully understand what data they are transferring to different destinations and where they rely on Privacy Shield and the SCCs. Where SCCs are used, banks will need to conduct a contract remediation exercise to repaper existing contracts to incorporate the new version of the SCCs. Whilst the grace period granted is helpful in this regard, this could be a significant exercise and we recommend that banks start their data mapping as soon as possible to ensure they have sufficient time to complete this repapering exercise.

Be prepared to appoint EU representatives: UK-based banks that serve customers in EU countries but have no branches or other companies there may now be required to appoint a European representative to continue providing services in those countries. In addition, UK banks that own separate entities that operate in the EU and have come under the supervisory authority of the UK Information Commissioner's Office (ICO) may need to appoint an EU-based supervisory authority. This is because the UK is no longer part of the EU-wide 'one-stop shop' supervisory mechanism following Brexit.

Focus on security for home-workers: during 2020, banks and other companies across the world were faced with the need for unprecedented numbers of employees to work remotely. This has led to a range of data-privacy challenges, from the risks associated with employees leaving laptops open (enabling others sharing their working space to view sensitive data) to the heightened potential for hacking or data theft as a result of new remote working and conferencing technologies. We strongly advise all companies, including banks, to ensure that all software patches are up to date, workers are protected by virtual private networks (VPNs), all policies are regularly revisited and refreshed and employees receive adequate and regular training on privacy issues.

Ensure employee monitoring is proportionate: another effect of the shift to remote working has been a rise in the number of employers using electronic monitoring to keep tabs on work rates. This gives rise to significant GDPR and ethical question marks relating to the impact on employee privacy. Employee monitoring requires robust justification to demonstrate that it is proportionate, and employers should consider less intrusive ways of tracking activity levels. In any event, covert monitoring (i.e. without informing employees that monitoring is taking place) is highly unlikely to meet GDPR requirements. Employers should always carry out a thorough data protection impact assessment (DPIA) to assess the risks and ensure their approach is both proportionate and justified.

Key contacts



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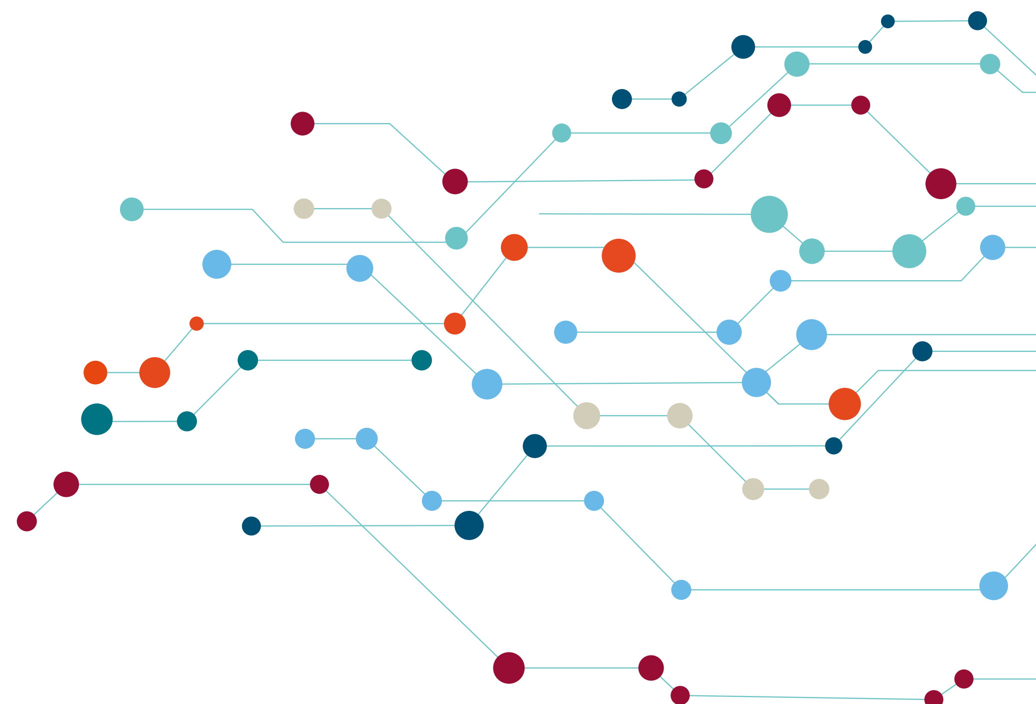


Disputes

What's changing?

In our Priorities for International Banks 2020 report, we discussed the end of LIBOR and the contentious issues that could arise from transitioning to a new reference rate, particularly around so called "tough legacy contracts". This will come into sharper focus as we approach the new financial year, especially following the FCA's announcement on 5 March 2021 confirming that all LIBOR settings will either cease to be provided by any administrator or no longer representative immediately either after 31 December 2021 for Sterling, Euro, Swiss Franc, Japanese Yen and 1 week and 2 month US Dollar settings or immediately after 30 June 2023 for all other US Dollar settings. Our previous advice on minimising the scope for potential disputes remains appropriate, including providing clear and transparent communications and explanations of the transition to customers; ensuring staff are appropriately trained; and keeping detailed records of engagements with customers, including minutes of meetings and notes of phone calls.

As we look forward, we should also consider the unprecedented effect the Covid-19 pandemic is continuing to have on economies across the globe. While there has been positive news at the start of this year with the arrival of vaccines, restrictions will continue to be in place in many countries during at least the first few months of the new financial year. Consequently, many forecasters are predicting a worsening economic climate through the first half of 2021, with a recovery not following until Q3 as the rollout of vaccines progresses.

The weak economic climate will inevitably mean banks face increasing non-performing loans (NPLs), which for some will exacerbate already prevalent NPL issues. This could lead to banks having their own issues, including meeting capital adequacy ratios set by their regulator. Banks may also find their options to resolve NPLs constrained because many governments have imposed temporary measures to try and help borrowers who are struggling because of the pandemic. For instance, borrowers may be given additional time to pay or lenders may have to wait longer to start court proceedings or initiate insolvency action.

What should international banks do to prepare?

Banks should take steps to identify and react early to any signs of distress. To do so, they should monitor compliance with loan covenants and potentially utilise contractual provisions that enable them to request copies of management accounts. These steps will highlight any difficulties in their financial performance.

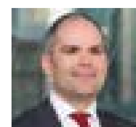
Reservation of rights letters can preserve potential remedies available to banks. They can be especially helpful where the bank is engaging and negotiating with the customer with a view to supporting them through what may be tough, but hopefully temporary, financial difficulties. Care should be taken to ensure that the terms of any forbearance is accurately recorded and agreed with the customer.

Banks should also take care to ensure that existing guarantees are not impacted by any amendments to facilities.

Most guarantees contain consent provisions confirming that any amendment to the obligations will not affect the validity of the guarantee. However, banks should review the terms of any guarantees to ensure they remain enforceable when re-negotiating with customers. In some circumstances it may be appropriate to seek express consent from the guarantor to the proposed amendments or ask that they re-state their guarantees as part of the re-structure. This is equally important when repapering loans as a result of the end of LIBOR.

Finally, we are seeing growing interest from clients in litigation funding with an ever-increasing number of providers and options available. That growth is likely to continue as banks look for alternative ways to manage their NPLs. From simply funding enforcement action to assigning a debt outright or providing up-front payments in return for a share of any recoveries, there are several innovative solutions available to assist with cash-flow and meeting capital adequacy.

Key contacts



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Restructuring and insolvency

What's changing?

There has been a growing focus over recent years on banks seeking to recover non-performing loans and that is showing every sign of continuing over the next 12 months. There is also an increasing appetite amongst lenders to identify the causes of business failure whilst also looking beyond the primary borrower(s) for repayment with a view to pursuing other obligors and identifying other avenues for recoveries.

In a related trend, regulators are putting banks under increased pressure to respond quickly to non-performing loans as they emerge and they are being encouraged to take active steps to pursue debtors. To assist with this, new opportunities are opening up to lenders, including minimising their risk by selling off entire debt portfolios or sharing in the risk/reward associated with pursuing recovery though the courts.

Beyond enforcement and recovery work are changes to insolvency legislation, the impact of the pandemic and Brexit, and opportunities for investors.

Changes to insolvency law

There have been significant changes in insolvency laws both here in the UK but around the world as well. Many countries have been mulling over proposed changes for some time, with the pandemic bringing the need for change into sharp focus. In the UK, for example, the government introduced the most significant changes in over two decades to the corporate insolvency regime, to give business distressed by the impact of the pandemic more time to seek advice and achieve a rescue with the introduction of the Corporate Insolvency and Governance Act 2020. Its reforms include a new Restructuring Plan process, known as the 'super scheme', which is seen as a move towards the US Chapter 11 insolvency framework. Across the EU, discussions are taking place to implement the Preventative Restructuring Framework Directive which is aimed at increasing the efficiency of insolvency processes across the EU whilst also enabling restructuring to be as straightforward as possible and available prior to a formal insolvency process.

Significant changes are not restricted to the UK: in India, a new pre-pack insolvency regime is being debated which would allow for increased investment in the distressed asset space with interest being sparked amongst international investors. Although cross border provisions are yet to be enacted under the Insolvency and Bankruptcy Code, there is a clear indication from cases such as that of Jet Airways that there is an understanding for the need and an appetite for cross-border collaboration between different insolvency professionals where, ultimately, the aim is a recovery back to creditors.

Pandemic fuels aggressive investment

There has clearly been considerable fall-out from Covid-19, resulting in a significant increase in business insolvencies and restructurings. Growth in the number of over-leveraged businesses has also stoked the interest of cash-rich international investors, particularly from the US and Canada, looking for value among distressed entities. Increasing numbers of well-financed businesses in the UK are also actively seeking acquisition targets among distressed competitors or companies with which they have a strategic fit and vice versa. For inbound investment, it remains to be seen what impact the new National Security and Investment Bill (which has reached final stages with Parliament now giving consideration to final amendments) will have in terms of restricting acquisitions in sectors or businesses which are of national strategic importance.

"...new opportunities are opening up to lenders..."

What should international banks be focused on over the next 12 months?

Monetising their non-performing loans: with the market for litigation funding continuing to open up with new entrants and products arriving to the market all the time, banks need to not only be alive to their existence but also have an informed understanding of how they can assist in turning their otherwise non-performing loans into recoveries. Greater knowledge at the outset increases the likelihood of recovery in the long term.

Keep up-to-date with change following Brexit: leaving the EU has brought with it significant changes to how the UK's insolvency processes will work for corporate groups with interests across Europe. Pre-Brexit, there was certainty afforded to recognition and enforcement processes with automatic access in most cases to an agreed process in corresponding EU countries. Now this door is closed, and with it come uncertainties about how cross-border insolvencies involving UK institutions will operate.

Stay focused on the LIBOR situation: in a development that is highly relevant to the restructuring marketplace, we can predict that transitioning Borrowers who are already in default may well be problematic without a longer term future relationship. Query though whether these Borrowers will fall within the "tough legacy" provisions which are coming into force and if so, in which jurisdiction?

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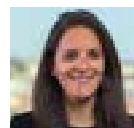

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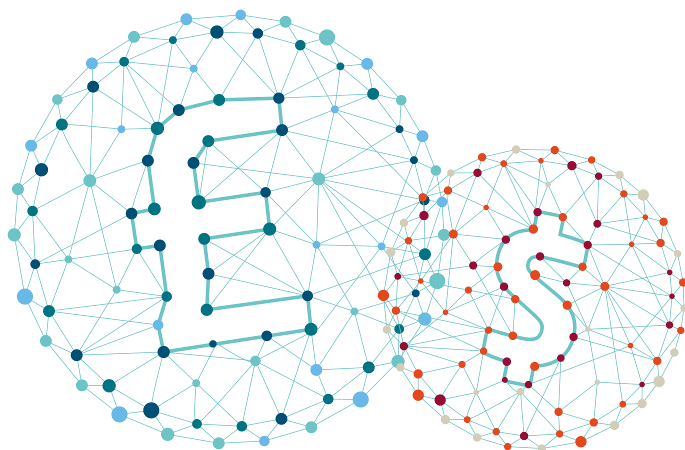

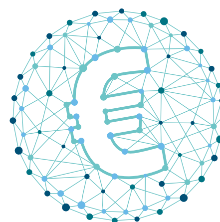

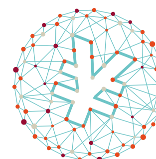

Sustainable/green finance

What's changing?

Disclosures in accordance with the Task Force on Climate-related Financial Disclosures (TCFDs) become gradually mandatory on a 'comply or explain' basis across the corporate financial landscape; 'green' products and services have entered the mainstream. Equally significant, the clients of banks and other institutions have come to expect full disclosure on sustainability performance, not only at a product level but also in terms of corporate behaviour.

When it comes to new product development and customer demand, green investment is widely regarded as the global financial services industry's fastest-growing sector. As significant change sweeps through the green finance marketplace, lenders across the world are understandably keen to be both involved and to be recognised as such. The potential opportunities are substantial, as the world's largest companies are increasingly eager to use corporate green finance solutions as part of their net zero strategies.

We look forward to the UN Climate Change Conference (COP26), to be held in November this year under the presidency of the United Kingdom, where green finance is one of the main areas of focus. We anticipate there will be much discussion around the economic opportunities provided by the transition to net zero and how to bridge the gap between the needs and the actual finance flows. Channelling the investment required to enable and accelerate this change will require collaboration from both public and private institutions. One option which has potential is for governments to encourage institutions to focus on sustainable opportunities by offering preferential capital weighting for sustainable investments in conjunction with penalties for failure to meet net zero targets.

What should international banks do to prepare?

Communicate with authenticity: there is a large-scale training and communication task to be undertaken, for lenders and borrowers alike, helping companies identify the best products and providers while enabling financial institutions to present their credentials in the most transparent and compelling way to build trust and awareness. Corporations and individual customers are increasingly aware of any disconnect between a lender's claims for the credentials of its products and its own sustainability record. Authenticity is therefore a fundamental requirement for all communications.

This was emphasised at a recent green finance conference by the Director of Strategy at the UK regulator, the Financial Conduct Authority (FCA). It included a call for institutions to engage with customers via three central means:

- **Transparency:** total clarity in the information given to customers, enabling them to understand the benefits and potential impacts of working with specific organisations and individual products.
- **Trust:** enabling customers to identify and understand the benefits provided by products, through green-labelling and other schemes.
- **Tools:** driving innovation and continuous improvement via effective collaboration between financial services organisations and data-technology providers.

Focus on innovation: currently, there is significant potential for banks and other institutions to gain first-mover advantage in the sustainable finance sector by developing and launching truly innovative and differentiated products that meet emerging customer needs. Growing consumer demand and capacity for growth mean that the opportunities to develop highly successful new offerings are very attractive.

"The potential opportunities are substantial."

Expect legislative change: following Brexit, the EU taxonomy (which defines the types of activities that are environmentally sustainable) will not apply in the UK and the UK government committed to at least match the ambition of the EU Taxonomy but we do not yet have any clarity in relation to the UK green taxonomy.

"Expect further innovation in the home finance market over the next few years as lenders look to develop their retail product sets beyond existing green mortgage offerings."

Track developments in the future of housing finance: one cause of concern for environmentally aware homeowners is that the expense of retrofitting their properties with sustainable solutions such as solar panels or ground heat pumps is unlikely to be recoverable when they come to sell. One solution would be a model of home finance where the finance attaches to the home rather than the borrower (similar to the property-linked 'PACE' (Property Assured Clean Energy) mortgage model used in the US. This would enable vendors and buyers to share the costs and benefits of such retrofitting activity. Expect further innovation in the home finance market over the next few years as lenders look to develop their retail product sets beyond existing green mortgage offerings.

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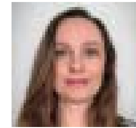

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"...annual low carbon investment in the UK will need to reach £50bn to put the UK on track for net zero."

Business immigration

What's changing?

EU Settlement Scheme

The EU Settlement Scheme is in place to ensure EU/EEA/Swiss nationals (hereafter "**EU nationals**") and certain non-EU national family members maintain their right to live in the UK post-Brexit. A successful application to the Scheme preserves residence and working rights in domestic UK law, which is necessary now that EU free movement has ended.

As a general rule, EU nationals who were resident in the UK by 11pm on 31 December 2020 are eligible to apply under the Scheme. They have until 30 June 2021 to make their Scheme applications. The application process should be straightforward for most applicants. It can be completed online and requires minimal supporting documentation. Applicants may be granted Settled Status (essentially permanent residence) if they have 5 years' continuous residence, or Pre-Settled Status (temporary residence) if they have lived in the UK for less than 5 years. It is possible to convert Pre-Settled Status into Settled Status at a later date, assuming they continue to meet the Scheme's rules.

Although an application does not necessarily require input from an employer, it makes sense for banks to publicise the Scheme to staff, so that individuals know that they need to apply before the June 2021 deadline. The UK Government has published an employer toolkit to assist with employee communications.

Skilled Worker Visa

Following the end of free movement, employers now need a Sponsor Licence to sponsor non-UK nationals who arrive in the UK from 1 January 2021. It is worth pointing out that sponsorship won't always be necessary, as there are some other visa permissions that also allow the right to work. For example, those who hold status under the Settlement Scheme won't require sponsorship.

Before December 2020, the most common work visa for non-EU nationals was known as a Tier 2 (General) visa. This has now been replaced by the Skilled Worker visa. Key changes include:

- The system applies to both EU and non-EU nationals who arrive in the UK from 1 January 2021 onwards unless they have status under the Settlement Scheme.
- Previously, only roles that would typically require a Degree or Masters qualification (RQF Level 6 roles) were eligible for sponsorship whereas the new Skilled Worker visa is available to individuals filling lower-skilled roles at RQF Level 3 (A-level).
- In line with the reduction in the skill level threshold, the baseline minimum salary requirements are also lower. An employer will generally need to pay a minimum salary of £25,600 or the "going rate" for the job (whichever is higher). Exceptions will apply for those with a PhD, roles considered to be in shortage and new entrants to the labour market. Sometimes the "going rate" can be significantly higher than the general minimum of £25,600.
- The Resident Labour Market Test has been abolished, meaning that mandatory 28-day advertising of vacancies to the UK workforce is no longer required.
- The system is more flexible than Tier 2 (General). Under the Skilled Worker rules, applicants can "trade" various characteristics in order to obtain the requisite number of points to successfully apply for a visa.

As well as Tier 2 (General) permissions, some banks may have held Tier 2 (Intra Company Transfer) licences for the purpose of intra-group assignments and secondments. The Intra Company Transfer rules will remain largely unchanged, but this route will likely become less relevant because the new Skilled Worker visa will largely apply. Banks with either a Tier 2 (General) or (ICT) licence would have had this automatically converted by the Home Office to accommodate the new system and terminology when the rules changed.

What should international banks do to prepare?

Banks should carry out audits of existing right to work documentation to identify current employees who should be making Settlement Scheme applications, if they haven't done so already. To conduct the audits, they could use self-service HR portals to ask all employees to confirm their nationality. Having all employees conduct this exercise helps to mitigate race/nationality discrimination risks from an employment law perspective. Although employers cannot force employees to make a Scheme application, it makes sense to encourage staff to do so to reduce the risk of business disruption.

When making EU hires between January and June 2021, banks must not ask individuals to prove that they hold status under the Settlement Scheme. Instead, they should carry out right to work checks, following the current Home Office guidelines. It is highly likely that new guidance on right to work checks will be issued from July 2021, but the Home Office has previously confirmed that retrospective checks on all EU staff won't be required. Care should be taken during recruitment processes when addressing right to work issues, which should generally be discussed as late in the process as reasonably possible.

In terms of recruitment strategies, the biggest change will be that much more stringent rules now apply to the recruitment of EU nationals who arrive in the UK from 1 January 2021 and who do not have status under the Settlement Scheme. Banks that do not already have a Sponsor Licence should actively consider whether a Licence may be required to maintain access to a wide talent pool of non-UK applicants as we move further into 2021.

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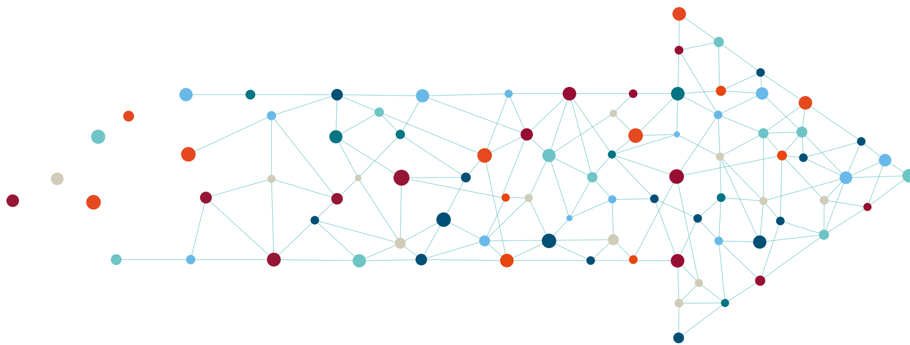

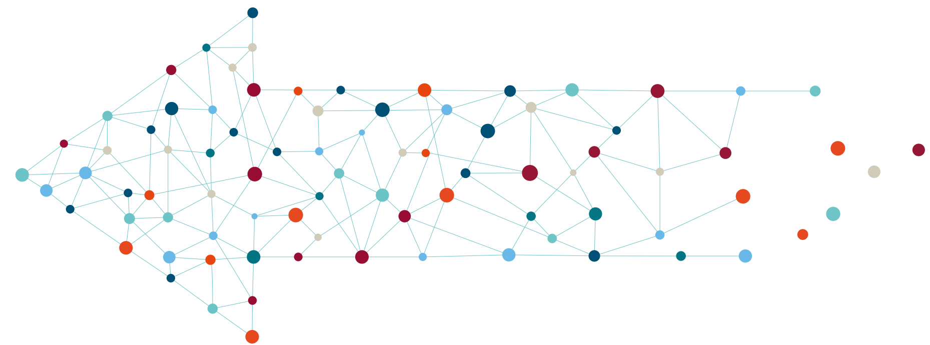

Real estate

What's changing?

It remains to be seen what the long-term impact of the Covid-19 pandemic will be on the real estate market. It seems likely that the way in which office space is occupied will change. More people are expected to work from home for at least part of the working week, reserving time in the office for team building/collaborative initiatives. In some cases, this could mean tenants look to rid themselves of space by taking advantage of break clauses, or by trying to sublet or surrender leases. In other instances, tenants may want to alter the configuration of their premises, and the extent of any permitted alterations will be governed by the terms of the lease. The market for short-term flexible space is likely to continue to grow, and it is possible that we will start to see more 'hybrid' leases in the market – a combination of traditional leases and service agreements.

A direct impact of Covid-19 is the current ban on landlords forfeiting a commercial lease for non-payment of rent, which has been extended in both England and Wales until 30 June 2021. A further extension in either or both jurisdictions cannot be ruled out. The UK government has launched a **call for evidence** on commercial rents and Covid-19 to "support the government's decision making on the best way to withdraw or replace these measures while preserving tenant businesses and the millions of jobs that they support".

In an attempt to support the market over the summer of 2020, the government introduced the new planning use class E (which combines commercial, business and hospitality type uses). This allows for flexible changes between these uses without the need for planning permission. The government has recently confirmed **a new permitted development right will be introduced** from class E to residential. The legislation introducing the new permitted development right came into force on 21 April 2021. However, the right is subject to a requirement to obtain prior approval and an application for prior approval cannot be made until 1 August 2021. The ability to switch freely between the very wide class E and residential may have an impact on investment value.

In addition to the fallout from Covid-19 and the changes in the occupation of office space, the government has announced that it will be launching a review of commercial landlord and tenant legislation in 2021. This will include a consideration of the procedure to exclude a tenant's security of tenure provisions of the Landlord and Tenant Act 1954, different models of rent payment, and a general review of the impact of Covid-19 on the commercial landlord and tenant market.

The recent theme of increasing regulation in the private rented sector looks set to continue into 2021 and beyond. The government is consulting on changes to the regulation of carbon monoxide alarms in rented accommodation in England. It is proposed that private landlords will have additional obligations to:

- Install a carbon monoxide alarm in any room used as living accommodation where a fixed combustion appliance that uses any fuel type is installed (excluding gas cookers). Currently, a carbon monoxide alarm only needs to be installed in rooms used as living accommodation that contain a solid fuel burning combustion appliance.
- Repair or replace alarms that are reported as faulty during the tenancy. Currently, landlords only need to ensure that the required alarms are present and in proper working order on the first day of every new tenancy.

Recent regulation of electrical standards in private rented accommodation will come into full force in 2021. The new rules have applied since 1 July 2020 to tenancy agreements signed on or after 1 June 2020. From 1 April 2021, the regulations will apply to agreements signed before 1 June 2020. They require landlords to:

- Ensure that a qualified person inspects every electrical installation at least every five years and issues a report.
- Supply a copy of the report to each existing tenant within 28 days of the inspection.
- Supply a copy of the last report to any new tenant before occupation, or any prospective tenant within 28 days of a request.

There have been sweeping changes to the rules around obtaining possession as part of the response to the Covid-19 pandemic. Eviction notices relating to property in England and Wales must currently give tenants an increased period of at least six months. The six-month notice period is reduced in certain serious cases, such as where the grounds of eviction relate to anti-social behaviour or domestic violence. In England, a shorter notice period is also permitted for fraud or where at least six

months' rent is unpaid at the date on which the notice seeking possession is served. The measures requiring these increased notice periods are currently due to expire on 31 May 2021 in England and 30 June 2021 in Wales.

The default position, if there is no further legislation, is that the notice period for 'no-fault' evictions will revert to two months from 1 June 2021 (in England) and 1 July 2021 (in Wales) and the notice periods for the fault based grounds will revert to what they were in each case before the pandemic. However, it is impossible to rule out further changes or a further extension of the current arrangements.

Additionally, the enforcement of residential evictions is still banned (subject to limited exceptions) until 31 May in England and 30 June 2021 in Wales.

Irrespective of these short-term pandemic-inspired measures, the government still intends permanently to ban 'no-fault' evictions of residential tenants in England. This could impact on the ability for landlords and their lenders to gain possession. In Wales, it is anticipated that the broad changes to the private rented sector set out in the Renting Homes (Wales) Act 2016 will finally be brought into force in 2021 and these include permanently increasing the notice period for a 'no-fault' eviction to six months. We have previously written about some of the changes envisaged by the Act **here**.

What should international banks do to prepare?

International banks should keep abreast of developments in both the commercial and residential sectors to ensure they can protect the value of their lending portfolio.

Where commercial tenants are looking to make changes to charged premises, lenders should consider any impacts on the value or marketability of those premises and take suitable professional advice. While no doubt under pressure to provide consent rapidly, it is important that it is properly considered.

Where borrowers are looking to forfeit leases once this is permitted, the full commercial implications should be considered. It is possible that a tenant paying no rent but incurring the business rates liability will be preferable to an empty unit with the borrower obliged to pay the rates.

In the residential market, lenders need to make themselves aware of the increasingly wide-ranging and prescriptive requirements for residential tenancies and ensure that their landlord borrowers have complied with them. In England, a failure to comply can prevent the service of a valid 'no-fault' eviction notice, making obtaining possession more difficult.

Lenders should also keep up to date on future developments around taking possession of residential property. Changes in this area are almost guaranteed as the private rented sector recovers from emergency Covid-19 pandemic measures. The English and Welsh regimes, which already have different emergency protection measures for tenants, will diverge significantly once the Renting Homes (Wales) Act 2016 comes into force. Lenders will need to keep up to date on the requirements that apply.

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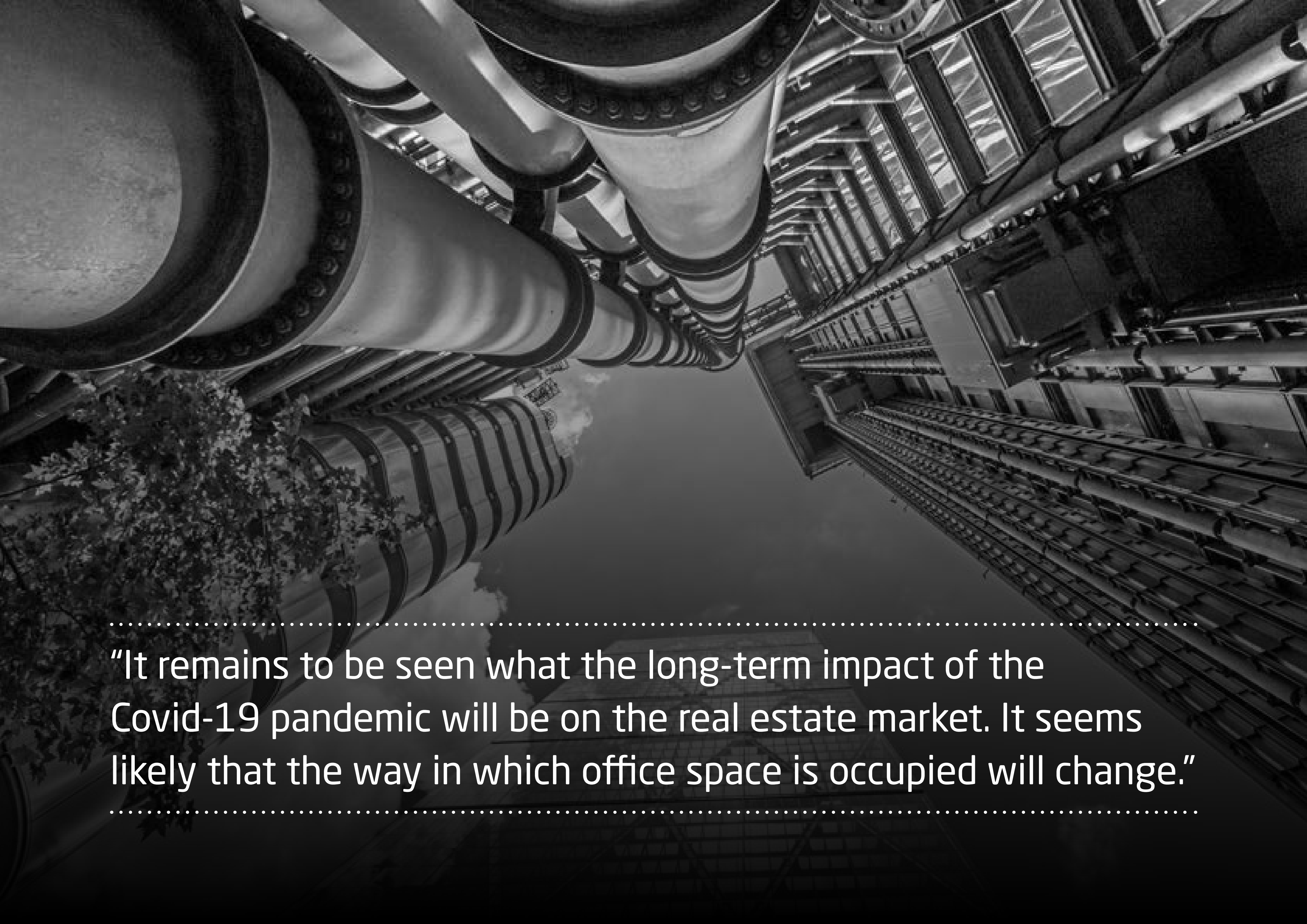

"It remains to be seen what the long-term impact of the Covid-19 pandemic will be on the real estate market. It seems likely that the way in which office space is occupied will change."

Technology, e-commerce and outsourcing

What's changing?

On 30 September 2019, the European Banking Authority (EBA) guidelines on outsourcing came into force. Although the Prudential Regulatory Authority (PRA) released its consultation paper on the Guidelines in December 2019, the submission deadline was extended due to Covid-19 and it closed in October. The PRA has yet to publish the findings and outcomes of the consultation process, which may be subject to further consideration regarding the impact of the UK's departure from the EU.

Whilst the Guidelines have been in force since 2019, the Covid-19 pandemic and the delay in the PRA providing additional practical guidance has paused or had an impact on many institutions' focus on resolving and addressing outstanding compliance issues. The December 2021 compliance deadline has not been extended and institutions will still be required to ensure they fully comply with the Guidelines by the final deadline.

As a reminder, the Guidelines are intended to be an update to the existing regulatory regime for banks when outsourcing functions, as set out in SYSC8 and MiFID II, as well as building on existing guidelines for outsourcing services to the cloud. The Guidelines have been produced following increasing interest from the European and UK regulators on how banks and other financial services firms use and rely on IT and digital services in an increasingly complex technology landscape.

The Guidelines set out the expectations on banks in several areas, which are:

- **The pre-outsourcing phase:** banks must have clear outsourcing policies to identify what is and isn't outsourcing, to establish critical and important outsourcing, and to carry out due diligence of suppliers.
- **The contractual phase:** banks must have written agreements with all suppliers that include specific contractual provisions and protections set out in the Guidelines.
- **The operational phase:** banks must monitor suppliers on an ongoing basis, keep a register of suppliers and report this to the PRA, and be able to exit the arrangement in an orderly way.

The Guidelines state a number of clear exceptions, but the PRA's view is that the majority of arrangements with third parties should be considered outsourcing by default. As such, the focus should be on what is critical and important, so that appropriate measures can be taken both contractually and operationally. Intra-group outsourcing is permitted but must be objectively justifiable. It should be subject to arm's length contractual conditions and a separate sub-set of requirements, particularly where the intra-group outsourcing is to countries outside of the EEA.

What should international banks do to prepare?

International banks should re-evaluate their outsourcing policy in the UK to ensure compliance, and update template contracts and documents accordingly. They also need to consider all UK operation's supplier arrangements (including intra-group arrangements) to establish whether they fall within the Guidelines and if contractual documents need to be updated.

Contracts for outsourced services must be updated now for new agreements. For arrangements that were already in place on or before 30 September 2019, firms should make required changes on renewal and at the latest by 31 December 2021.

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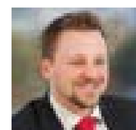

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