Covid-19: Liquidity support scheme for large businesses

This note reflects the position as at 5pm on 23 March 2020. *This note will be updated from time to time, including following release of any further information on the CCFF. The summary provided in this note is for general information purposes and does not constitute legal advice. The situation is fast-moving and additional details or changes may be announced so it is particularly important to seek specific advice on the circumstances applicable to your business.*

The Government, through HM Treasury, and the Bank of England (the Bank) have announced a number of schemes and measures to support business during the "Covid-19 shock". This note considers the Covid Corporate Financing Facility (CCFF), intended to assist companies with liquidity and working capital issues. The CCFF was described in a Market Notice issued on 18 March 2020[1] and further information was released on 23 March 2020[2].

This note is designed both for those familiar with the money markets and those that may be looking at this kind of lending for the first time. We have provided both an overview and a more detailed explanation of some of the key points to assist a wide range of companies. We have also included a glossary to explain some of the terms used for those who are less familiar with this area.

INTRODUCTION

In headline terms, the CCFF will involve funding through the purchase by a Government company (the Fund) of commercial paper (CP) issued by the relevant business.

CP is explained in more detail below. In broad terms, CP is simply a debt instrument, similar to bonds or loan notes in that it represents a promise by the issuer to repay an amount in the future. CP is usually issued on standard market form documents and has a maturity date of less than 12 months with fairly simple terms and limited default provisions.

While many of those looking at the CCFF may have issued CP before, it is open to businesses that have not done so and may not have participated in the money markets before. Although companies with a credit rating may be able to access the CCFF more quickly, it is not be necessary to have an existing credit rating. The minimum issue size under the CCFF is £1 million.

Further information will continue to become available now that the CCFF is formally available. What is known so far is summarised below. This note covers the main issues around the CCFF, including:

- an overview of CP generally
- eligibility for the CCFF
- the terms of CP eligible under the CCFF
- documentation needed to be able to issue CP
- steps that a business should be taking to be in a position to use the CCFF

[1] https://www.bankofengland.co.uk/markets/market-notices/2020/ccff-market-notice-march-2020

[2] https://www.bankofengland.co.uk/news/2020/march/the-covid-corporate-financing-facility

COMMERCIAL PAPER

CP is a form of debt instrument, with the same essential characteristics as a bond or loan note, with maturity of less than a year. As with other types of debt instruments such as medium-term notes (MTNs), CP is typically issued pursuant to a programme. CP is usually cleared through the main international clearing systems (Euroclear and Clearstream) – and CP under the CCFF needs to be issued this way – but is not usually listed on a stock exchange.

One or more "dealers" (generally investment banks) are involved in setting up and running the programme. Dealers act as the "interface" between the issuer and the CP purchaser. Where CP is purchased by the Fund under the CCFF immediately upon its issue in the primary market, the purchase must be carried out through dealers. They are also involved in documenting a CP programme.

Companies wanting to use the CCFF who do not already have a CP programme in place will want to speak to one or more of their relationship banks quickly to check that they would be able to help.

ELIGIBILITY FOR THE CCFF

The minimum size of an individual issue of CP eligible for purchase by the Fund is £1 million nominal. To be able to use the CCFF, a business:

- does not need to have issued CP previously, but will need to establish a CP programme if it does not already have one
- must make a material contribution to the UK economy
- can be a non-financial company or a non-bank financial company if they materially contribute to corporate financing in the UK (banks and other regulated financial institutions are not eligible)
- must have been in sound financial health prior to the Covid-19 shock
- must use a UK-incorporated issuer (which can be a finance subsidiary, in which case a guarantee will be needed from the "primary entity" in the group) but can be foreign-owned with a "genuine business" in the UK

Looking at some questions businesses are likely to have about eligibility:

- when assessing "material contribution to economic activity in the UK", relevant factors will include
    - employment in the UK
    - whether the business headquarters are in the UK
    - the extent of UK revenues, customer base and operating sites

GLOSSARY

clearing systems: regulated electronic systems to facilitate sale and purchase ("settlement") of debt instruments in the primary and secondary markets. The clearing systems evidence holdings of CP, rather than physical pieces of paper

CP or **commercial paper:** a debt instrument where the holder lends money to the issuer and the issuer promises to pay it back on a maturity date no later than 364 days from the issue date

dealers: dealers are banks (generally investment banks) involved in setting up and running programmes. Dealers act as the "interface" between the issuer and the CP purchaser

eligible counterparties: financial institutions that are regulated and meet other criteria set by the Bank of England

Euroclear and **Clearstream:** these are the main clearing systems

finance subsidiary: a company set up by a company specifically to raise debt. Debt issued in this way is usually guaranteed and it is a requirement of the CCFF that the "primary entity" in a group gives a guarantee

Fund: Covid Corporate Financing Facility Limited, the company established by HM Treasury and the Bank of England to buy the CP

global notes: a single document representing a whole CP issue, irrespective of how many people are CP purchasers/holders

ICMA: International Capital Market Association, a debt capital markets trade body (of which CMS is a member)

Information memorandum: a document containing information on an issuer and its debt instruments, typically shorter than a full prospectus

issuer: the entity that will become the debtor under the CP

primary market: the market where CP is purchased directly from the issuer, usually through dealers

programme: a debt issuance platform set up by an issuer to issue CP up to a set value. Programmes allow issuers to issue debt instruments over a period of time in "series" or "tranches" rather than on a one-off basis

prospectus: a detailed disclosure document explaining the terms, risks and other features relevant to someone considering subscribing (signing up for) a debt instrument. Contents are governed by the EU Prospectus Regulation. A prospectus isn't needed for CP

secondary market: trading in debt instruments that have already been issued

- CP issued by regulated entities including banks, building societies and insurance companies is not eligible, or if issued by leveraged investment vehicles or by companies in “groups which are predominantly active in business subject to financial sector regulation”
- eligibility will be based on pre-Covid-19 shock credit rating. This means a short-term credit rating on 1 March 2020 of at least A-3/P-3/F-3/R3 from at least one of S&P, Moody’s, Fitch and DBRS Morningstar, the major rating agencies. If a company does not have a short-term rating:
    - if it has a long-term rating, the Bank is likely to “read across” that rating to the equivalent short-term rating. It has indicated that the equivalent long-term ratings would be BBB-/Baa3/BBB-
    - if it has no rating, the Bank will consider whether it is able to assess whether it is of equivalent financial strength. The Bank suggests that the companies contact one of the major rating agencies to seek an assessment of credit quality and say that they have been in touch with those rating agencies. It is uncertain how long such a process might take. Whereas a full ratings process might normally take months, we would expect this process to be carried out more quickly, subject to the number of applicants. On the Issuer Eligibility Form, the Bank of England asks issuers who do not have a rating whether they have started the process of getting one. If not, they ask for evidence of financial condition before 1 March 2020, suggesting that the Bank may be willing to carry out its own credit assessment independent of the rating agencies, perhaps where companies have particularly urgent liquidity needs

TERMS

Purchases can take place in the “primary market” by issuing directly to the Fund (technically via the dealers for the relevant CP programme, discussed further below) or in the “secondary market” from eligible counterparties who already hold CP. The CCFF will be available for at least 12 months.

To be purchased under the CCFF, CP needs to have a maturity of one week to 12 months, though for regulatory reasons discussed below, the maximum maturity will be 364 days. Drawings can be rolled while the CCFF is open, subject to eligibility. The CP must not have “non-standard” features. The Issuer Eligibility Form asks for confirmation that CP under the programme is “not complex”, including that the CP is not subordinated and does not contain features such as extendibility. As such, we think it unlikely that anything “structured”, including CP with security or involving intra-group arrangements and covenants other than in connection with a guarantee, will not be considered eligible.

Pricing is intended to achieve rough equivalency with market pricing pre-crisis. In technical terms, the Fund will purchase CP at a spread above a reference rate, based on the current sterling overnight index swap (OIS) curve. Spreads will be set with a view to achieving pricing close to the market spreads prevailing before the Covid-19 shock.

CONFIDENTIALITY AND UNDERTAKINGS

The names of issuers and details of CP purchased or eligible for purchase by the Fund will not be disclosed publicly.

Every Thursday at 3pm, the Bank will publish the aggregate amount of CP purchased under the CCFF up to Wednesday that week.

Issuers need to sign an undertaking and confidentiality undertaking when applying to issue CP to the Fund under the CCFF. In this document, the company:

- gives confirmations that no insolvency events have occurred (or that they have occurred only as a result of Covid-19 and have been disclosed to the Bank)
- makes various representations and undertakings, including about the accuracy of financial statements and projections, its ability to enter into CCFF documentation and its ongoing eligibility for the CCFF
- agrees to give a guarantee from the “primary entity” in its group and, where that primary entity is incorporated outside England & Wales, a legal opinion

- undertakes to pay the Bank's costs and expenses (including legal expenses) in connection with the CCFF (though the size of such expenses and whether the Bank will enforce this provision remain unclear)
- agrees to notify the Bank if, subject to certain exceptions, it grants security for any debt, unless the CP purchased by the Fund benefits from the same security
- agrees to the operating procedures of the CCFF and to any unilateral changes to the procedures or documentation that the Bank may make
- agrees, along with the Bank, to keep information confidential, including the fact that the issuer is participating in the CCFF

DOCUMENTATION

The documentation for a CP programme tends to be in relatively standard form, usually closely following the standard market forms published by ICMA. CP documents are generally not heavily negotiated, compared to the documents for a loan facility or longer-term debt instruments. The programme documentation generally includes:

- a dealer agreement governing the relationship between the issuer and its dealer(s). The terms of each CP issuance are agreed at the time of the issue and there are no commitment fees. Dealers are typically compensated by a commission on each CP issue or a fee based on the amount of CP outstanding. Fees for a CP programme created for the CCFF may be lower than for a "normal" CP programme because issuers should not need the dealers to source investors given that the Fund will be the purchaser
- an information memorandum containing details about the programme and the issuer (assuming that one is needed under the CCFF – see below). We would expect an information memorandum to incorporate by reference (if not physically include) the most recent audited financial statements and any available interim statements. Information currently available does not suggest that a CP issuer will need to produce extra financial statements as a result of a having a CP programme under the CCFF
- a guarantee, if applicable (for instance, if a finance subsidiary is the issuer, as is common and as is anticipated by the CCFF). The Issuer Eligibility Form asks whether the CP benefits from a guarantee "or similar arrangements" that have been provided to other creditors of the issuer. The form of guarantee that will be expected in connection with the CCFF is available on the Bank of England's website[3]
- an issue and paying agency agreement governing the relationship between the issuer and the bank acting as agent to carry out certain mechanical tasks in connection with issuing the CP, holding the notes as depositary for the clearing systems and making payments on the CP (and the agent would usually be expected to be from the same bank group as the dealers, so the dealers would be expected to help with this)
- the legal documentation representing the CP itself, usually being one or more global notes. CP essentially represents a promise to repay the principal amount (the face value or "par") of the CP at maturity; there are generally no, or limited, events of default, negative pledge or other covenants (and we note that the information released by the Bank of England, including the Issuer Eligibility Form, requires there to be no complex features). The notes normally contain a tax gross-up clause. For those familiar with other kind of debt issues like MTN programmes, there is no trustee or noteholder meeting provisions
- a deed of covenant, under which holders of CP are given direct rights of enforcement against the CP issuer or guarantor if the CP issuer defaults on payment

[3] https://www.bankofengland.co.uk/-/media/boe/files/news/2020/march/ccff-proforma-guarantee.docx

- legal opinions as to capacity and enforceability addressed to the dealers. Dealers may be willing to waive this requirement. Where a guarantee is provided by a company other than the CP issuer and the guarantor is not incorporated in England & Wales, a legal opinion will be needed. The form of this is provided on the Bank of England website[4]

As expected, the Bank anticipates that CP programmes under the CCFF will closely follow the template suggested by ICMA that is familiar in the market. The ICMA templates were previously available only to members of ICMA, but they have made them available generally in light of the CCFF.[5]

The Issuer Eligibility Form asks for confirmation that the CP programme is "substantially in the form of the ICMA recommended template" and for details of any material deviations from them. Existing CP programmes that may be eligible under the CCFF would is likely already to be based on this template.

From a legal and regulatory perspective, issuing CP:

- does not need a detailed prospectus, but may need a straightforward information memorandum. CP falls outside the scope of the Prospectus Regulation (which still applies in the UK during the EU withdrawal implementation period) because of its short maturity. This means that no prospectus is required under this legislation. By convention, a more straightforward information memorandum is prepared for a CP programme. Where CP is issued solely to the Fund, we queried whether the Bank might dispense with this requirement given that issuers will have gone through its own application and eligibility process. However, the request that documentation is "substantially in the form of the ICMA recommended template" suggests that issuers under the CCFF will be expected to produce one
- would generally not require an issuer to be authorised by the FCA. So long as certain requirements are met, which we would expect to be standard requirements and features of CP programmes under the CCFF, issue of CP would not generally breach deposit-taking or financial promotion rules
- would, as with most issues of debt instruments, often be undertaken by a PLC, rather than a (non-public) limited company. This is not an absolute rule and companies proposing to use the CCFF would need to consider and take advice on this point
- can generally avoid withholding tax if interest-bearing (which is generally not the case as CP is typically offered at a discount). This is because interest paid on debt with a maturity of less than a year would not generally be expected to be "yearly interest" for the rules on withholding tax

From a timing perspective, we would usually expect the process of setting up a programme to take around 4–6 weeks. However, assuming that one or more banks have agreed to act as dealers, with appropriate focus and subject to any initial bottle-necks if several issuers want to access the CCFF immediately now that it has launched, it would be possible in theory to agree the documentation and set up the programme within a few days. Once the programme has been established, individual issues of CP can be carried out very quickly – potentially within hours of a decision to issue.

The Bank has said that if they confirm eligibility before 4pm on a working day, companies will be able to sell CP to the Fund via a dealer the next working day. Purchase decisions will be made by the Bank every working day between 10am and 11am.

STEPS TO TAKE

Companies planning to access the CCFF should:

- consider the eligibility criteria and make contact with the Bank of England to discuss eligibility on: CCFFeligibleissuers@bankofengland.gsi.gov.uk
- speak to your bank(s) to ensure that they are able to help with the establishment of a CP programme and provision of dealers and a paying agent (including in what timeframe and for what fees). We would recommend you contact your existing relationship managers in the first instance. UK Finance have also released details of banks who have indicated that they will be able to act as dealers[6]

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[4] https://www.bankofengland.co.uk/-/media/boe/files/news/2020/march/ccff-proforma-legal-opinion-on-the-guarantee.docx

[5] https://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/covid-19-market-updates/ under the "Market Practice" tab

[6] https://www.ukfinance.org.uk/covid-19-corporate-financing-facilities

- familiarise yourself generally with details of the CCFF, including the information available on the Bank of England website, such as the main CCFF application form and the guidance that accompanies it, issuer eligibility form, issuer undertaking and confidentiality agreement, form of guarantee and form of legal opinion that may be required
- ensuring financial statements and other key information about the business are available, particularly if the company does not already have a short-term rating
- checking the terms of other documentation, particularly loan agreements, intercreditor and security arrangements and other financing documents, to ensure that the issue of CP, which is a form of debt, is permitted (and, if so, considering seeking appropriate amendments or waivers)
- consider any constitutional restrictions or requirements applicable to the relevant issuer/guarantor companies, including whether any amendments may be needed to the articles of the company and what board or other authorisations may be required

HOW CMS CAN HELP

We have extensive experience advising clients on previous government assistance programmes, interactions with the Bank and other regulators and on commercial paper programmes.

We anticipate that there will be considerable demand for funding from the CCFF now that it is “open for business”. The Bank is likely to operate a “queuing” system for applicants based upon priorities set by the Bank. They have said that they aim to confirm eligibility of CP programmes “as quickly as possible”.

Although it is important that participants register an interest with the Bank, it is vital that they consider carefully what information (such as financial data) they need for a successful application and begin preparing this now in order to minimise any delays in the process. CMS can help you consider what steps you can be taking now.

We can advise as you consider whether the scheme is right for your business and whether you would be eligible for it, on the work you can be doing in advance of a potential application to participate in the CCFF, with applications to the Bank, with the establishment of your CP programme and on any state aid implications of participation in the CCFF.

The situation continues to evolve and we will continue to provide updates on any further announcements and developments. Our *Law-Now* service at www.cms-lawnow.com provides up to date information and advice on the implications of the outbreak.

To discuss any of the issues in this note in more detail, or for further advice, please contact any of us.

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